KCOM Preliminary results 2018

5 June 2018

Key points

Overall

- EBITDA ahead of expectations despite lower revenue
- Remain confident in medium-term prospects; with proposed final dividend of 4.00p, consistent with stated commitment
- Existing dividend commitment extended to FY19

Hull & East Yorkshire

- Good progress, revenue growth up 2% overall, alongside benefit of £4.4m multi-year hereditament rates rebate
- Fibre to be available to 100% of addressable market by March 2019
- More customers taking broadband over full-fibre now than over copper

Enterprise

- Margin and profit improvement, despite 3% revenue decline
- Strengthened management team driving momentum from cloud-based wins and renewals

National Network Services

- Revenue decline as a result of reducing legacy activity, as expected
- HSCN compliance level 2 achieved; pipeline of opportunities developing

Creating shareholder value

Income and capital growth

Enterprise	Hull & East Yorkshire	National Network Services
Provision of cloud-enabled solutions for UK enterprises	Communications services for the region's consumers and businesses	Connectivity-based services for organisations nationwide
Investment light/ customer funded	**Investment focus**	**Targeted investment**
Growth opportunity	**Income**	**Manage for value**
	c.140,000 homes c.7,000 small & medium businesses	

Financial performance

Summary financial results

	FY18 £m	FY17 £m	% Change
Revenue	**301.9**	**331.3**	**(9%)**
EBITDA*	**68.3**	**67.6**	**1%**
EBITDA %	*23%*	*20%*	
Profit before taxation	**34.0**	**30.5**	**11%**
Adjusted basic EPS (pence)**	5.26	6.10	
Exceptional items	0.7	(7.9)	
Cash capex	(43.9)	(47.2)	
Net debt	(62.6)	(42.4)	
Final dividend per share (pence)	4.00p	4.00p	

* Amounts are before exceptional items

** Adjusted basic EPS is basic EPS adjusted for post tax impact of exceptional items

- Profit ahead of expectations
- Revenue reduction principally driven by anticipated decline in National Network Services
- EBITDA benefitted from £4.4m multi-year network rates rebate (Hull & East Yorkshire)
- Exceptional credit due to regulatory settlement and a reduction in the level of restructuring costs
- Net debt and capex positions reflect continued investment in fibre deployment
- Confirmed final dividend of 4.00p per share (full year 6.00p per share)

Segmental performance

	HEY		Enterprise		NNS		Central		Group	
	FY18 £m	**FY17 £m**	**FY18 £m**	**FY17 £m**	**FY18 £m**	**FY17 £m**	**FY18 £m**	**FY17 £m**	**FY18 £m**	**FY17 £m**
Revenue	**104.2**	**102.3**	**88.3**	**91.0**	**113.2**	**141.8**	**(3.8)**	**(3.7)**	**301.9**	**331.3**
Gross margin	**85.4**	**78.5**	**29.9**	**25.6**	**32.0**	**41.0**	**-**	**-**	**147.2**	**145.1**
%	*82%*	*77%*	*34%*	*28%*	*28%*	*29%*	*0%*	*0%*	*49%*	*44%*
Indirect costs	(19.7)	(18.1)	(24.7)	(21.1)	(23.0)	(25.0)	(11.5)	(13.2)	(79.0)	(77.5)
Contribution / EBITDA	**65.7**	**60.4**	**5.1**	**4.5**	**9.0**	**16.0**	**(11.5)**	**(13.2)**	**68.3**	**67.6**
%	*63%*	*59%*	*6%*	*5%*	*8%*	*11%*			*23%*	*20%*

Indirect costs reflects savings as a result of tighter cost control (some of which have been reinvested) and the inclusion of a bonus provision

Central costs have declined year on year as a result of tighter cost control and lower headcount across the Group

Hull & East Yorkshire

	FY18 £m	FY17 £m	% Change
Revenue			
Consumer	58.5	56.1	4%
Business	30.5	29.6	3%
Wholesale	10.8	11.0	(2%)
Core channels	**99.8**	**96.7**	**3%**
Media	1.9	2.4	(21%)
Contact Centres	2.5	3.2	(22%)
Total revenue	**104.2**	**102.3**	**2%**
Gross margin	**85.4**	**78.5**	**9%**
Gross margin %	*82%*	*77%*	
Contribution	**65.7**	**60.4**	**9%**
Contribution %	*63%*	*59%*	

- Strong financial performance, 3% revenue growth in core channels
- Continued successful fibre deployment
  - Consumer revenue increased by 4% driving 4% ARPU uplift (to £35.17 per user per month)
  - 3% Business growth
- Wholesale broadly flat, stabilising decline from prior years
- Contact Centres closed in March 2018, as previously disclosed
- FY18 margin and contribution benefitted from network rates rebate of £4.4m relating to prior years (FY17: £1.0m supplier credit)

Enterprise

	FY18 £m	FY17 £m	% Change
Revenue			
Projects	35.5	48.3	(27%)
Managed Service	39.8	30.5	30%
Network	13.0	12.2	7%
Total revenue	**88.3**	**91.0**	**(3%)**
Gross margin	**29.9**	**25.6**	**17%**
Gross margin %	*34%*	*28%*	
Contribution	**5.1**	**4.5**	**13%**
Contribution %	*6%*	*5%*	

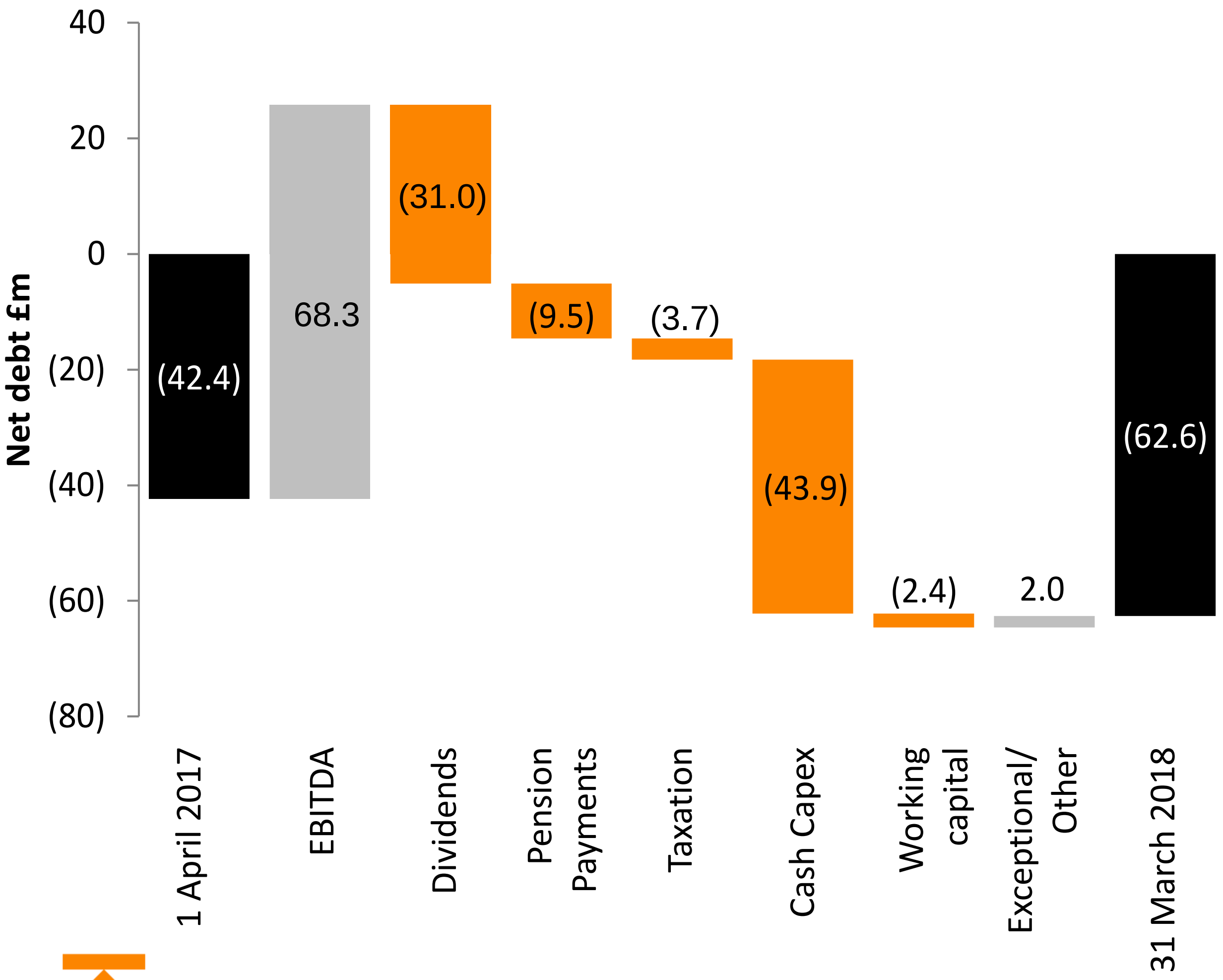
- Revenue declined by 3%
  - Project revenue impacted by the UK General Election and Brexit
- Prior year project activity successfully translated into annuity revenue through growth in Managed Service and Network
  - Revenue from our top five customers has grown by 5%
- Losses on complex software contracts of £5.3m (FY17: £3.7m)
  - Two complex software contracts now mutually exited
  - Customer relationship maintained, with new business
- Despite this, margin % and contribution have improved

National Network Services

	FY18 £m	FY17 £m	% Change
Revenue			
SMB	51.9	52.6	(1%)
Partners	33.9	41.8	(19%)
Large Corporate	27.4	47.4	(42%)
Total revenue	**113.2**	**141.8**	**(20%)**
Gross margin	**32.0**	**41.0**	**(22%)**
Gross margin %	*28%*	*29%*	
Contribution	**9.0**	**16.0**	**(44%)**
Contribution %	*8%*	*11%*	

- Revenue decline as anticipated, gross margin % maintained
- SMB revenue broadly flat. Focus on providing value with larger customers
  - Growth in managed WAN connectivity services to multi-site organisations
- Partners revenue has declined due to anticipated customer churn alongside the industry wide change in mix of services in intelligent numbering (e.g. movement to 03 numbers)
- Large Corporate revenue decreased as expected due to decision to cease support for certain services
- There will be a further small decline in legacy services in FY19

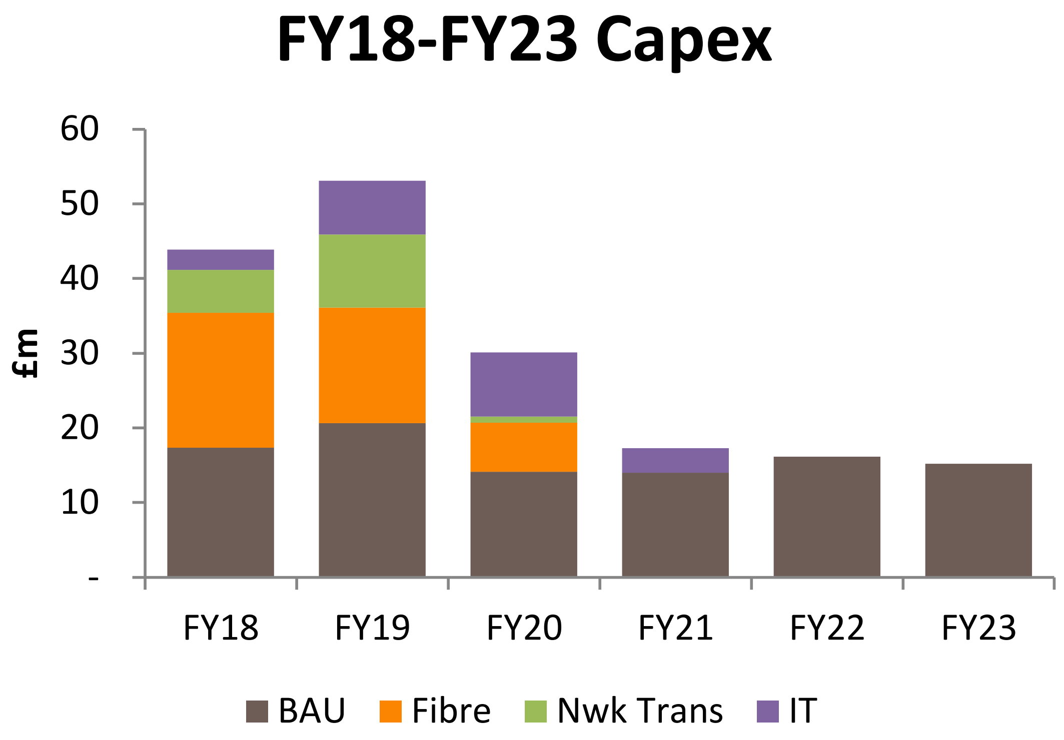
Net debt and cash flow



- Net debt of £62.6m drives net debt: EBITDA of 0.9x
- Increase due to continued investment in transformation capex (fibre deployment in Hull & East Yorkshire)
- Small working capital outflow across the year (reversing half year position)
- Underlying receipts and payments continue to be well controlled:
  - DSO 30 days – broadly in line with last year (27 days)
  - DPO consistent with the prior year

Capital investment

- Capex will peak next year. In FY19 our investment will be focused on:
    - Completing our fibre deployment in Hull & East Yorkshire
    - Accelerating our systems investment in order to update our IT estate and reduce underlying costs
    - Transforming our network which reduces our cost base
- We expect capex to reduce in FY20 and decline further to an underlying level of less than £20.0m from FY21 onwards



Actual/Forecast capex by spend area

IFRS 15 – revenue recognition

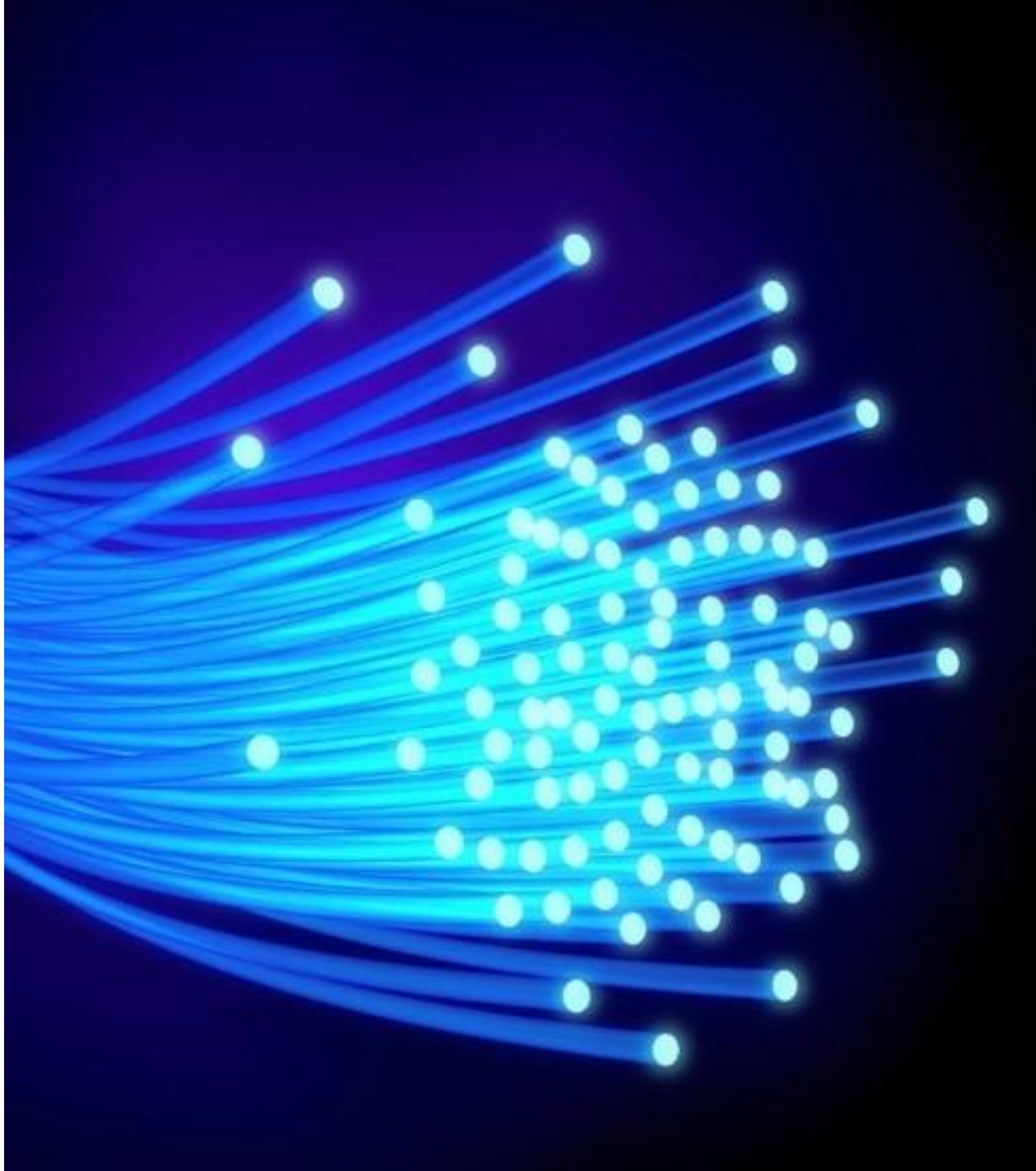
- IFRS 15 is the new standard impacting revenue which is applicable from 1 April 2018
  - This is timing only and cash flow neutral
  - First reporting interim results to 30 September 2018
  - Adopting on a modified retrospective basis, cumulative reserves adjustment of (£0.5m) to £0.5m
- **The principal areas of impact are:**
  - Routers in HEY segments (revenue now recognised up front) **EBITDA c£2m lower, PBT neutral**
  - Revenue in Enterprise – “agent” v “principal” **Revenue c£3m lower, EBITDA and PBT neutral**
- Other areas **of lesser impact include the** treatment of licences, connections and commissions

Business update

Hull & East Yorkshire

Fibre deployment progress

- Fibre availability
  - 27,000 premises passed during FY18, making fibre available to 164,000 premises
- Customer connections
  - 24,000 premises connected in the year (net)
  - Total active fibre customers now 67,000, including over 3,500 businesses
  - 64% of our broadband customers in our fibre-enabled areas are taking a fibre service
- Investment
  - Total investment of c£80m to make fibre available to our addressable market by March 2019
  - A further c£5m in FY20 to continue to connect customers, as previously communicated

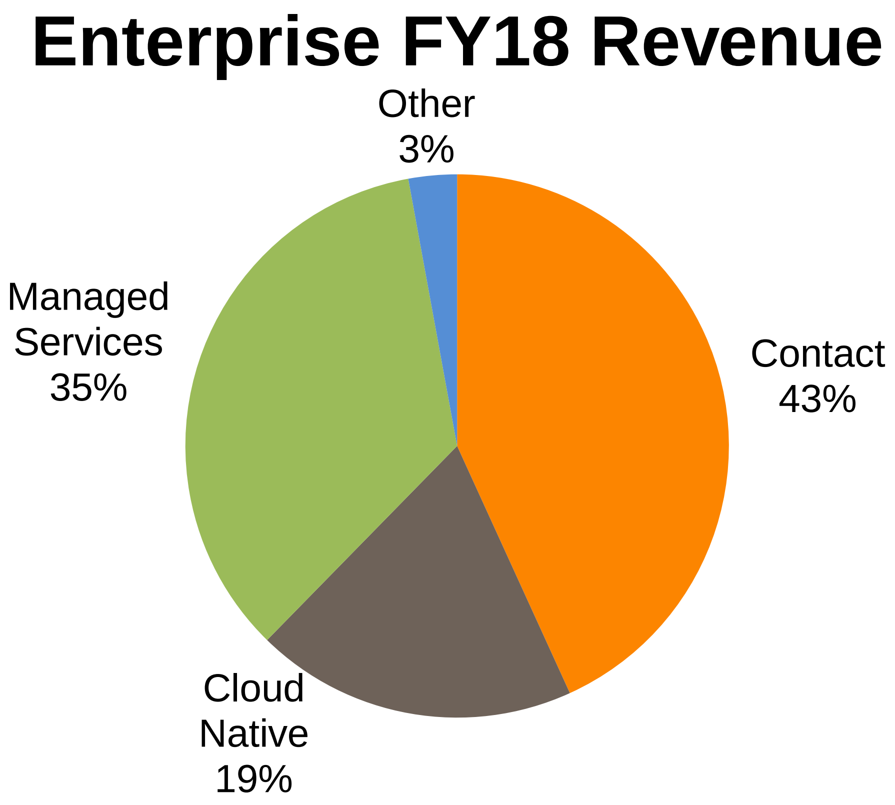


Hull & East Yorkshire – priorities

- Driving growth across all three core channels: consumer, business and wholesale through launch and evolution of proposition set
  - New consumer packages launched giving customers ability to design their service based on speed and data requirements; early indication of ARPU growth
- Continued execution of plan to reach remaining 25% of addressable market by March 2019
  - Deployment progressing as expected
  - Participation in new DCMS voucher scheme for businesses
- Services roadmap, including over-the-top applications, is developing

Enterprise - priorities

- Offers opportunity for long-term growth
- Focus on core capabilities around cloud, contact and collaboration services
- Continue to build relationships with key customers including HMRC and NFUM
- Revenue growth from top five customers
- Tightened cost control
- Contracts with new customers such as Jaguar Land Rover, InterDigital, SES Water and ITSO
- Joined Google Cloud Partner programme, adding to relationships with Amazon Web Services and Microsoft Azure

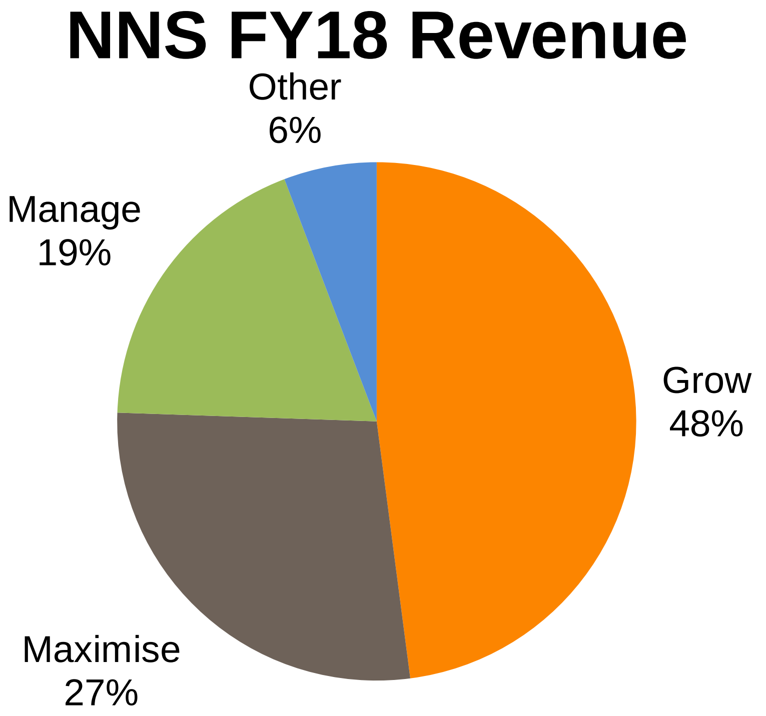


*Based on management judgement

National Network Services

- Continued targeting of Wide Area Networks, particularly within the retail and charitable sectors
  - Building on reputation with customers including Dominos, One Stop, Furniture Village, Wren Kitchens, RSPB, RNLI and Terrence Higgins Trust
- Leverage Health and Social Care Network opportunity
  - Level 2 compliance already achieved
  - Number of opportunities in progress
  - Focus on up and cross-selling WAN capabilities
- Further refinement of call management offering
- Legacy activities will continue to decline albeit at a lower rate

HEALTH & SOCIAL CARE NETWORK COMPLIANT



*Based on management judgement

Investment in core assets and capabilities

Transforming to simplify, create greater granularity of performance and reduce operating costs

Network Managed Service

- BT managed service arrangement exited at 1 April 2018; relationship remains strong
- Benefit from scale operations within Hull & East Yorkshire
- Significant capital and opex savings; insource completed on time and to budget

Customer Service Operations Centre operational

- Opened February 2018, with initial phase covering Enterprise and Hull & East Yorkshire technical support
- Single ownership and accountability for level 1 and 2 technical support, in one common operations centre
- Single service desk and service Interface for any incident, with resolver groups available for deeper technical issues

2018/19 Focus

Work continues to provide greater clarity of segment economies and value to reduce costs

- Continued transformation of the network, including decommissioning of System X and migration to IP-based voice service to reduce both operating cost and risk
- Accelerated investment in simplifying and upgrading IT systems
- Work to strengthen project management completes in Q1
- Continued development of customer technical services capability

Outlook

- Remain confident about medium-term prospects
- Investment will underpin long-term sustainable value, greater understanding of segmental performance and simplified operating model
- Extension of existing 6.00p dividend commitment for an additional year