TalkTalk
For Everyone

EMBARGOED UNTIL 7.00 AM ON 10th MAY 2017

10 May 2017

TalkTalk Telecom Group PLC

Preliminary results for the year ended 31 March 2017 (FY17)

- Headline EBITDA (1) +17% to £304m
- Customer base returned to growth in Q4 (+22k) with positive net adds in Retail and Wholesale
- Q4 churn reduced to 1.40% (Q3: 1.64%)
- Over 1m customers now on new plans with 59% of on-net Retail base in-contract
- Strong growth in TalkTalk Business Ethernet base (+8k) fuelling Data revenue growth
- New operational structure and fewer, simpler priorities to drive growth
- Review of mobile strategy to create alternative less capital intensive offering
- Leverage reduced to 2.57x, new debt facilities secured, and dividend reset.

FY17 Financial Highlights

- Total revenue -3% to £1,783m (FY16: £1,835m); On-net -4% to £1,342m (FY16: £1,399m)
- Corporate revenues (ex-Carrier) + 4%; Data +31%, Legacy Voice -18%
- FY On-net base -49k, with growth in Q4 of 22k
- £34m of benefits delivered from MTTS; cumulative £87m delivered
- Statutory Profit Before Tax £70m (FY16: £14m); statutory EPS 6.1p (FY16: 0.2p)
- Final dividend 5.0p (FY16: 10.58p), total FY17 dividend 10.29p (FY16: 15.87p)

Looking forward

- New price plans and falling churn underpin confidence in driving customer base growth
- Retail base growth and continuing growth in TTB to drive return to growth in Group revenues
- FY18 headline EBITDA(1) expected to be £270m-£300m as a result of SAC investment to drive growth
- FY18 Dividend reset to 7.5p; growth expected to resume once business returns to earnings growth and leverage has reduced towards 2.0x

(1) Headline EBITDA is defined in Note 1, and reconciled to Statutory measures in Note 7.

Charles Dunstone, Executive Chairman of TalkTalk commented:

“I’m enjoying having a more ‘hands on role’ at TalkTalk and I’m very excited about the progress we have already made and the prospects for the business. The promotion of Tristia Harrison and Charles Bligh to their new positions has created a clear and simpler operating structure and I can already see the difference they are making. My focus for the company is growth, cash generation and profit – in that order. We will be smart about how we invest, focusing on our fixed network, avoiding other capital intensive distractions. In light of these new priorities, we have also decided to reset the dividend as we look to deliver growth and strong sustainable shareholder returns over the long term.”

Tristia Harrison, Chief Executive of TalkTalk commented:

“The last 12 months have seen the business lay down solid foundations from which to drive sustainable base and revenue growth in both our Retail and B2B businesses. This will allow us to build upon our core strength as a value for money fixed line connectivity provider as we focus on delivering growth, improving our customers’ experience, investing in and future-proofing our fixed network, and driving operational efficiencies across the business, whilst being more disciplined and smarter with our assets.”

Presentation and Q&A

9.00am – 10.30am: The Ned, 27 Poultry, London EC2R 8AJ

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SUMMARY FINANCIALS

Headline Profit & Loss[1]	2017	2016
Revenue (£m)	**1,783**	1,838
EBITDA (£m)	**304**	260
EBITDA margin (%)	**17.0**	14.1
Operating profit (£m)	**165**	131
Profit before taxation (£m)	**133**	107
Profit after taxation (£m)	**100**	79
Basic EPS (p)	**10.5**	8.4
Dividend per share (p)	**10.29**	15.87

Statutory Profit & Loss	2017	2016
Operating profit (£m)	**95**	38
Profit before taxation (£m)	**70**	14
Profit after taxation (£m)	**58**	2
Basic EPS (p)	**6.1**	0.2

Cash flow (£m)	2017	2016
Operating free cash flow[1]	**143**	104
Interest and taxation	**(33)**	(22)
Free cash flow[1]	**110**	82
Exceptional items	**(46)**	(88)
Acquisitions	**(18)**	(12)
Dividends	**(150)**	(135)
Sale of own shares	**1**	63
Net Debt	**782**	679
Net Debt/Headline EBITDA	**2.57x**	2.61x

Key Performance Indicators	2017	2016
On-net Broadband Net Adds ('000)	**(49)**	(181)
On-net Churn (%)	**1.45%**	1.60%
TV as % of Broadband base	**35%**	38%
Fibre as % of Broadband base	**25%**	19%
Mobile as % of Broadband base	**25%**	19%
EFM & Ethernet Net Adds ('000)	**7.7**	8.9

(1) Headline and non-statutory measures are defined in Note 1, and reconciled to Statutory measures in Note 7.

Q4 trading - Return to Retail net adds growth as planned

We saw continuing strong and greater than expected demand for our new Fixed Low Price Plans ("FLPP") in Q4, both from existing customers wishing to re-contract and from new customers, which took the total FLPP base to 993k and the proportion of in-contract customers at the year end to 59% (FY16: 53%). Combined with continuing improvements to customer service from operational initiatives, this momentum helped reduce churn during the quarter to 1.40% (Q3FY17: 1.64%), and drive net adds growth of 22k, with the Retail base returning to growth.

Demand for fibre remained strong, with nearly 30% of new customers choosing to take fibre and within that, more than twice as many customers as a year ago choosing the 76Mbps product. As a result, we added 73k new fibre customers during the quarter, taking the total base to 927k (25.5% of the on-net base). We also saw improving demand for TV which helped drive a turnaround in the momentum of the base with net adds of -14k (Q3FY16: -31k). Mobile net adds of 45k were in line with our plan. We delivered another strong quarter of Ethernet growth with 2.3k net adds, taking the year-end base of installed lines to over 26k.

Group headline revenues* (ex-Carrier) declined by 2.5% year on year, driven primarily by the impact of a lower average base, higher mix of Wholesale customers and ARPU dilution from re-contracting activity on On-net revenues (-3%). Corporate revenues (ex-Carrier), grew by 9.1% driven by Data revenues (+19.4%) and a significantly lower decline in Legacy Voice revenues (-3.3%; Q3FY16: -19.4%) from growing traction in our Next Generation voice product.

We made good progress in diversifying our sources of finance and extending the maturity of our facilities: we refinanced £400m of our short dated bank debt through the successful issue of a debut 5 year public bond, and post year end, refinanced our banking facilities for a further five years.

Looking forward

Our priorities in FY18 are to sustain the momentum built during Q4FY17 to deliver growth in the on-net base and on-net revenues; sustain strong growth in TalkTalk Business ("TTB"); continue our fixed network investment; focus on customer service improvements and operational efficiency; improve headline cash flow*; and reduce net debt.

We expect continuing lower costs per add and reducing churn to support more economically attractive gross additions during FY18, however incremental volume growth will require higher SAC & Marketing investment. As a result we expect to deliver headline EBITDA* of £270m-£300m, year on year growth in headline revenues, and improved headline cash flow allowing us to reduce net debt. Beyond FY18 we expect the growing on-net base, comprising higher quality lower churning customers, to support a return to headline EBITDA* growth.

We have reorganised the business under our new leadership team to focus on fewer, clearer priorities that are focused on investment in our core fixed network. As part of our review of how we allocate capital and our clear focus on investing in fixed connectivity we have reassessed our mobile strategy. While we remain committed to offering all our customers a compelling mobile proposition, we have decided not to pursue an inside-out mobile network strategy, and instead we will continue to work closely with Telefónica UK on the right platform and customer offering. We expect to have more information to update on this in due course.

Dividend

The Board is committed to returning the business to revenue and customer base growth, improving cash generation and reducing leverage, and in this context has declared a Final dividend for FY17 of 5.0p (FY16: 10.58p), taking the total dividend for the year to 10.29p (FY16: 15.87p). For FY18 the Board expect to declare an Interim cash dividend of 2.5p (FY17: 5.29p) and a Final cash dividend of 5.0p (FY17: 5.0p) taking the total cash dividend for the year to 7.5p (FY17: 10.29p). Looking beyond FY18, the Board expects to resume dividend growth once the business returns to earnings growth and has reduced leverage towards Net Debt/Headline EBITDA* of 2.0x.

**Headline measures are defined in Note 1 to the financial Statements and reconciled to statutory measures in Note 7.*

FY17 Business Review

Summary: 17% growth in headline EBITDA*; strong foundations in place for future growth

We made solid progress in establishing the operational foundations for future growth with clear improvements in customer experience metrics, tangible network enhancements, the relaunch of our brand and Retail propositions, and excellent growth in TTB. As a result we exited the year with stronger than expected re-contracting and gross additions activity driving growth in the broadband base, lower churn and a higher proportion of the base in contract.

Group headline* revenues fell by 3.0% with On-net revenues down 4.1%, Corporate +3.4% and Off-net (2.5% of total; FY16: 3.0%) declining by 20%. The decline in On-net revenues reflects the c.3% lower average base during the year (as a result of churn and lower connections activity), and on-net ARPU which was 1.3% lower year on year at £28.16, reflecting the higher proportion of Wholesale customers on the base (24%, FY16: 21%), and during H2, the dilutive impact of FLPP offset in part by increased fibre penetration and price increases.

Corporate revenue growth of 3.4% was driven by Data revenues (+31%) which benefited from c8k net adds to our Ethernet and EFM base. Growth in Data and Next Generation Voice (+20%) offset Legacy Voice (-17.9%), with Carrier revenues broadly flat year on year.

FY Headline EBITDA* of £304m (FY16: £260m) grew by 17% (statutory operating profit grew by 150% year on year as a result of the higher, cyber related exceptional costs in FY16), driven by a significant improvement in subscriber acquisition costs (SAC) and marketing, and £34m of savings from our transformation programme Making TalkTalk Simpler (MTTS). In SAC, we benefited from the extension of our agreement with a major distribution partner for a 5 year period, to provide the Group with a lower cost outsourced solution for the management of fixed line customer acquisitions. During the year this enabled us to accelerate gross additions, whilst deferring a proportion of the upfront SAC cost, which contributed £24m, net of expensed hardware costs of £17m. By delivering a growing and higher quality base, at a lower cost per add, we expect to see both revenues and gross profit expand in future years.

Net debt at 31 March 2017 was £782m (30 September 2016: £847m), with headline* leverage falling from 2.82x to 2.57x and committed headroom, reflecting the issuance of the Group's debut bond, at 31 March of £412m.

1. Over 1m customers now on Fixed Low Price Plans and 59% of on-net base in-contract

During FY17 we built upon the substantial operational and customer service improvements delivered by Making TalkTalk Simpler, and extensive customer research, to launch a comprehensive brand refresh and our simpler, fairer, Fixed Low Price Plans.

We launched FLPP at the beginning of October 2016, ahead of the wider industry's move to all-in pricing. Existing and new customers responded extremely well to the new plans through H2, with the 24 month plans introduced in Q4 showing particularly strong demand. As a result we now have over 1m customers on the new plans. Many more customers chose to take fibre than expected; and attachment rates for calling boosts and TV have also been stronger than we had expected reflecting both the attractiveness of our simple and clear pricing, and the much improved online experience that we have delivered through MTTS. The heightened churn that we experienced during the first quarter of the launch, from the re-pricing of legacy propositions, reduced sharply in the final quarter of the year to 1.40%.

**Headline measures are defined in Note 1 to the financial Statements and reconciled to statutory measures in Note 7.*

2. Delivered lasting operational and customer service benefits

We made significant progress during FY17 across all our customer experience improvement programmes, which have driven materially better outcomes for customers, and as a result, £34m of gross P&L savings. Key areas in which we made strong progress include:

- New technical support and repair processes introduced for front-line service representatives, built on technology deployed in FY16, reducing customer effort and increasing first-time fix rates, with fewer customers with a broadband issue calling back within 7 days.
- More than 600,000 customers enrolled on TalkSafe, TalkTalk's innovative, secure and low-effort new voice biometric verification system.
- Tailored Next Best Action technology deployed across online and phone channels, increasing Net Promoter Scores (NPS) and upsell.
- Introduced a redesigned simpler, more informative and transparent online bill.
- Re-platformed the highest traffic parts of our websites to optimise for mobile as well as desktop devices and improve performance.

With all the initiatives that comprised MTTS now fully embedded within the business, the programme is now substantially complete, with cumulative financial benefits of £87m delivered.

3. Ongoing network investment has improved customer experience

In addition to improving customer experience through MTTS, we continued to invest in our network across four major areas:

- Backhaul and core network enhancement to ensure the best outcome for customers at peak time. As a result we are ranked best with *samknows* for peak time throughput.
- We replaced our Dynamic Line Management (DLM) system for improving speed and line stability and rolled out a new secure Domain Name System (DNS) to improve resilience, security, and responsiveness.
- We completed software upgrades to the collector nodes and began our major access network upgrade to 10gb+ capacity, with over 100 exchanges fully migrated to date.
- We deployed more Netflix caches at the edge of our network to improve streaming experience by pushing content closer to the customer. For customers taking sports boosts, we engineered a substantial uplift in video quality, which combined with the DLM improvements has translated into an improved viewing experience.

We have made excellent progress with our Fibre-To-The-Premise (FTTP) trial in York. The initial roll out to over 14,000 homes, was completed in March 2017, with penetration of serviceable homes at c27% (c2,500 of whom are TalkTalk customers). Build costs were under our £500 per home target, with take-up and customer satisfaction also ahead of targets. Following the success of this first phase, work has now begun on the planning work to extend the network to a further 40,000 premises across the rest of York.

4. Improving customer satisfaction, churn and a return to base growth

The combined effect of MTTS, our network quality improvements and the launch of FLPP, helped deliver substantial improvements in customer satisfaction, churn and base growth during FY17.

Churn across the year fell to 1.45% (FY16: 1.60%) with year-on-year improvements in both H1 (1.40%; H1FY16: 1.48%) and H2 (1.51%; H2FY16: 1.72%), despite elevated levels of churn in Q3 from the planned tariff rationalisation and re-pricing of legacy propositions when we launched FLPP.

Customer satisfaction with our service agents and complaints to Ofcom which are drivers of churn, also improved during the year. Critically, these improvements, combined with falling costs per add as a result of more efficient distribution channels through our extended outsourcing arrangement with DCP, allowed us also to increase new acquisition activity in the final quarter of the year. The resulting gross additions exceeded our expectations and coupled with lower churn, enabled a return to Retail base growth. As a result we exited the year with 3.947m on-net customers (FY16: 3.996m). Within this, the Retail base declined by 178k during the year, while the Wholesale base continued to grow robustly (+129k).

5. Growth in triple and quad play penetration

In line with our strategy of growing fibre, triple and quad play penetration, we saw strong take-up of fibre (+223k) and mobile (+214k). There were 927k customers taking fibre at the year-end (25.5% of the on-net base), with H2 net adds nearly double the level in H1 as customers responded to our pricing initiatives and easier on-line upsell journeys.

In Mobile, we ended the year with 913k SIM and handset contracts, again with H2 net adds stronger than H1 as we introduced an upgraded SIM as part of our launch of FLPP**.**

While the TV base contracted during the year by 101k, we saw an inflection in the rate of decline during Q4 (-14k) as customers responded positively to the improving functionality and performance of our next generation YouView interface, and our multi-device TV App.

At the end of the year our on-net base comprised c42% dual-play customers (taking voice and broadband), c39% triple-play customers (taking voice, broadband and either TV or mobile), and c12% quad-play customers (taking all four products), with strong fibre penetration across all three.

6. Continuing strong growth at TTB: Corporate (+4.2%) and Data (+30.8%)

TTB delivered another year of strong performance in Corporate. Revenues (ex-Carrier) grew by 4.2%, with an acceleration in H2 to +6.1% from +2.3% in H1. Data revenues grew 30.8% year-on-year with the number of Ethernet and EFM lines up by 8k during the year. Legacy voice revenues declined (-17.9%) in line with the established trend but we saw strong take-up of our new next generation voice product, with revenue growth during the year of 20%. As planned, Carrier revenues were broadly flat year-on-year (+1.7%).

Following our acquisition of tIPicall in April 2015, our next generation voice portfolio continued to gain good momentum. 116 Partners have signed up to sell this new service and the total base of SIP channels on the platform, including acquired base, increased by 7,340 channels (+65%) during the year. The acquisition has continued our diversification into next generation telephony services, further demonstrated by our hosted telephony platform which saw the user base grow by 43%.

PRIORITIES FOR FY18

We have a clear and defined strategy of driving profitable growth by leveraging our extensive network assets, improving the customer experience, and driving operational efficiency. Under our new leadership team and operational structure we will now focus on delivering growth in the on-net base and on-net revenues, sustaining strong growth in TTB; continuing to improve and future-proof our network, driving a step change in customer experience, and realising further efficiencies.

1. Returning the Retail base to profitable growth

There is compelling evidence that our new propositions are delivering not only reduced churn but happier more satisfied customers; the vast majority of whom are signing up to 24 month contracts, wanting certainty in pricing and service: early life churn on the FLPP base is less than 1%; FLPP customers reported Net Promoter Score is significantly higher than for non-FLPP customers; and TalkTalk brand satisfaction has grown in each of the last four months.

This coupled with simpler, better value propositions for new customers, materially improving customer service, and reducing costs per add underpins our confidence in driving profitable subscriber growth in our retail base through gross adds activity.

As outlined above our TV business has seen significant improvements in service and customer satisfaction and our aggregator approach to free and pay TV across multiple devices is paying off - our investments in TV continue to lead to broadband churn reduction.

In mobile, while we remain committed to offering all our customers a compelling proposition, we have decided not to pursue an inside-out mobile network strategy, and instead we will continue to work closely with Telefónica UK on the right platform and customer offering. We expect to have more information to update on this in due course.

2. Sustaining momentum in TTB

Our market share of Ethernet circuits (c10%) offers significant further opportunities for growth, supported by the pricing optionality from favourable Ethernet and dark fibre regulation. We are seeing increasing demand in the future pipeline from small businesses looking to use our high speed Ethernet products as they transition to hosted voice products. We are also growing the pipeline with large corporates looking to take advantage of our new managed network connectivity products.

Having expanded our portfolio of data products to offer a complete portfolio of FTTC and Ethernet products, we expect to see strong demand from both our partners and direct customers. The number of partners wholesaling FTTC from us has grown in the last year and we expect continued growth in this area.

3. Delivering a step change in customer experience

Having delivered progressive improvements in customer experience from MTTS, our focus over the next twelve months and beyond will be on consolidating these achievements to drive a step change in three key areas: consistency of service across all channels, joining and repair processes, and in-home connectivity/experience. The investments we have already made in simplifying and upgrading our customer-facing systems and processes have begun to deliver measurable returns in the form of higher customer satisfaction, lower complaints volumes and improved churn. Our overall focus from here on will be to continue to put the customer at the heart of the service experience to make sure whichever channel they choose (online, social to call centre) we give a consistent experience and advice which increases loyalty to the brand. This also includes our B2B customers where we have good customer satisfaction with both direct and wholesale customers and we have plans to improve this to industry leading levels. These improvements will require modest incremental investment that will be covered within our overall commitment of capex/revenues of 6%-7%.

4. Network investment

Continuing investment in the network over the next two years (within our 6%-7% capex/revenue commitment) will deliver a fully upgraded access layer (switches and backhaul) with over 1,000 exchanges equipped with 10Gig backhaul circuits, to support growing FTTC penetration and data usage. We also plan to scale dark fibre deployment across the entire network, helped by a more favourable regulatory pricing environment. This will allow us to support the expected increase in capacity utilisation at reduced unit costs, and significantly mitigate future network operating costs that otherwise, would grow substantially as we expand our Ethernet, FTTC & FTTP base.

Following this network investment programme, we expect the entire data network to be at the latest switching and network technology. It will be simplified, more resilient, using the latest Tier 1 networking technologies (both software and hardware), and will future-proof the network for the expected needs of consumers and businesses.

5. Operational excellence

Delivering better quality at a reduced cost of operation is fundamental to our growth expectations. Our new operating structure will allow us to further simplify our service footprint and customer insight systems; reduce the costs of failure; and better leverage our procurement and cost assurance processes. Over the medium term, this will result in a fundamentally higher quality of operation, and reduce our cost / revenue ratio whilst also allowing us to reinvest efficiencies into further customer experience improvements.

Finance Review

The Group uses Headline measures that exclude items which are non-trading or non-recurring to monitor the performance of the Group. Headline measures are used to partly determine the variable element of remuneration of senior Management throughout the Group and are also in alignment with performance measures used by certain external stakeholders in the context of the telecoms sector. In particular, EBITDA and Free Cashflow are commonly used across the telecoms industry to aid stakeholders in making comparisons between the performance of the Group and its peers. Unless stated otherwise, the discussion of the Group's financial performance below, is on a Headline basis. Headline measures are defined in Note 1 and reconciled to statutory measures in Note 7.

£m	**2017**	**2016**
On-net	1,342	1,399
Corporate	397	384
Off-net	44	55
Headline Revenue	**1,783**	**1,838**
Headline Gross Margin	949	993
%	*53.2*	*54.0*
Operating expenses excluding amortisation and depreciation	(459)	(473)
SAC and Marketing	(186)	(260)
Headline EBITDA	**304**	**260**
%	*17.0*	*14.1*
Exceptional items	(57)	(83)
Statutory EBITDA	**247**	**177**
Depreciation and amortisation (1)	(131)	(121)
Non-operating amortisation	(10)	(10)
Share of results of joint ventures	(11)	(8)
Operating profit	**95**	**38**
Net finance costs (2)	(25)	(24)
Profit before taxation	**70**	**14**
Taxation	(12)	(12)
Profit after taxation	**58**	**2**

(1) Includes exceptional items of £3m (FY16: Nil)

(2) Includes and exceptional credit of £7m for interest receivable on settlement of a dispute

Overview

FY Headline revenue declined by 3% to £1,783m (FY16: £1,838m), however the Group delivered a 17% increase in Headline EBITDA to £304m (FY16: £260m) and with an increase in statutory profit before taxation of £70m (FY16: £14m). The Board has recommended a Final dividend of 5.0p taking the total dividend for the year to 10.29p (FY16: 15.87p). Net debt/Headline EBITDA fell from 2.82x in H1 to 2.57x (FY16: 2.61x) as some of the H1 Headline working capital outflow reversed in H2 and net debt fell from its usual seasonal peak of £847m at the half year, to £782m at year end. The Group's medium term leverage target remains 2.0x. Committed headroom at 31 March 2017 was £412m (FY16: £162m), reflecting the issuance of the Group's debut bond in Q4.

Headline Revenue

Headline group revenue of £1,783m was 3% lower year on year with On-net revenues 4% lower, Corporate revenues 3% higher and Off-net revenues (2% of total) 20% lower. The decline in On-net revenues reflects the c3% lower average base (as a result of churn and lower connections activity), and the dilutive impact of FLPP launched in October 2016, offset in part by the increased penetration of Fibre, and re-pricing of legacy propositions following the launch of FLPP. Corporate revenue growth was largely driven by Data revenues (+31%) which benefited from c8k new connections to our Ethernet and EFM base. The strong growth in Data revenues and 20% growth in Next Generation Voice from tIPcall offset the now established decline in Legacy Voice (-18%). As expected, Carrier revenues were broadly flat year on year (+2%).

On-net ARPU for the year of £28.16, was 1.3% lower year on year, reflecting the higher Wholesale mix of the on-net base (24%, FY16: 21%), with price increases in Q3 offsetting the mix effect and dilution from re-contracting on FLPP.

Headline Gross margin

Headline gross margin of 53.2% was 80bps lower year on year but saw a significant improvement in H2 rising to 54.5% from 52.0% in H1, driven by a reduction in carrier trading volumes, the impact of price increases at the beginning of the half, growth in data revenues and the settlement of supplier claims, which together offset the impact on margins of lower ARPU FLPP, a higher mix of Wholesale customers in the On-net base, and higher Fibre volumes.

Headline Operating costs, SAC and Marketing

Group operating costs declined by £14m year on year (and by £93m on a statutory basis, as a result of higher cyber related costs in FY16), with the benefits of MTTS, lower levels of bad debt provisioning linked to the benefit of FLPP on churn and property reorganisation offsetting investment in network and IT infrastructure. In total the MTTS programme delivered savings of £34m across the P&L in the year and since inception in 2013 has yielded cumulative savings of £87m.

MTTS reached substantial completion during FY17 and continued to deliver various improvements to the customer experience, namely repairing voice, broadband and diagnostics flows, simplicity of bill redesign, introduction of the Premium Address Source to improve leakage, and improvements in Homemove and Online. The delivery of the new agent desk top interface for Collections and Tech agents was rolled out in Q4 to improve handling times.

Operating costs saw further reductions from our revised property footprint with the adoption of revised ways of working enabling us to rationalise our London property footprint and the realisation of a £2m profit on the sale and leaseback of our data centre site in Milton Keynes.

Network operating costs grew modestly with investment in new backhaul investment, access network technology, IT systems, security and maintenance offsetting rate savings, and lower exchange costs.

SAC & Marketing costs fell by 28% year on year, with the growth in SAC within TTB up 10% as a result of higher Ethernet volumes being more than offset by lower retail connection volumes, and a year on year increase in the settlement of service related disputes. In SAC, we benefited from the extension of our agreement with a major distribution partner for a 5 year period, to provide the Group with a lower cost outsourced solution for the management of fixed line customer acquisitions. During the year this enabled us to accelerate gross additions, whilst deferring a proportion of the upfront SAC cost, which contributed £24m, net of expensed hardware costs of £17m. By delivering a growing and higher quality base, at a lower cost per add, we expect to see both revenues and gross profit expand in future years.

Headline EBITDA

Headline EBITDA grew by 17% to £304m (FY16: £260m). The margin for the year grew from 14.1% to 17.0%, with the H2 margin of 19.8% improving over H1 (14.4%) and FY16 H2 of 18.4%. In addition to the revenue, gross margin, opex and SAC movements identified above, Headline EBITDA was impacted by a number of additional items including rebates from suppliers (£13m offsetting £13m associated costs), incremental income regarding service level disputes (£10m) and a reassessment of management estimates related to the recoverability of certain trading receivables (£5m). Further details are contained in Note 3.

Exceptional items

The net exceptional charge in the year amounted to £57m (FY16: £83m) and includes one-off costs relating to the delivering of the MTTS programme, which has now been substantially completed. £31m of exceptional costs were incurred across the MTTS programme as a result of continued improvement to the customer experience, systems and processes and implementing changes to the Group's organisational structure, including costs associated with our move to a new single North West location in the Soapworks, Salford in June 17.

During the year ended 31 March 2017, the Group began to reorganise the business under the new leadership team focusing on fewer, clearer priorities and less capital intensive projects that are focused on investment in growing the Group's core fixed line connectivity business. As part of the review the Group reassessed its mobile go to market strategy and whilst remaining committed to offering mobile to its customers, has concluded not to pursue a femto enabled, inside out network strategy and instead to work closely with Telefonica UK on an alternative customer offering. This has given rise to exceptional costs of £49m (£9m cash) comprising impairment charges and onerous lease costs in relation to technology equipment that has no further economic benefit. Further costs may be incurred during FY18 as the Group works with its MNO partners on developing an alternative mobile distribution strategy.

In addition, £8m has been incurred relating to one-off costs in our technology estate, as we change our underlying network structure for efficiency and scalability over the next two years. These costs have been offset by an exceptional credit of £29m in relation to various prior year disputed network charges.

Cash exceptionals of £46m (FY16: £88m) include the costs incurred during FY17 in relation to the delivery of MTTS and transforming our network together with the timing impact of prior year provisions and working capital movements, most notably the timing of cyber-attack related technology cash costs of £12m. Looking forward to FY18, the Group expects cash exceptional costs to fall to c£10m-£20m as it reaches settlement of the disputed network balances taken to exceptional income in the current year and delivers on its plans to transform its technology estate, pursue alternative mobile offerings for all its customers, complete its property relocations and incurs further reorganisation costs following the transition to a new management structure.

Depreciation and amortisation

Depreciation and amortisation expense increased from £131m to £141m and included exceptional costs amounting to £3m in relation to network transformation. Non-operating amortisation was flat year on year at £10m.

Share of results of joint ventures

Share of costs of joint ventures increased to £11m (FY16: £8m) mainly due to the Group's investment in Youview.

Net finance costs

Headline net finance costs for the year were £32m (FY16: £24m) comprising of a blended interest rate of 3.6% (FY16: 3.1%) and including £2m of amortisation of bank fees (FY16: £1m). On a cash basis, interest was £35m, including £8m of fees related to the execution of the Group's debut bond issue in January 2017, debtor securitisation and new bank facilities arranged during the year. In addition, following an Ofcom determination, the Group recognised an exceptional credit of £7m in relation to interest on a BT dispute settled in FY14 for the overcharging of certain wholesale Ethernet services. The average cash finance cost in FY18 is expected to be c4.4%.

Taxation

The headline tax charge for the year was £33m implying an effective headline tax rate of 25% (FY16: 26%) against a statutory rate of 20%, mainly driven by the impact of a reduction in the statutory tax rate on our deferred tax assets. The statutory tax charge of £12m, is net of the release of a provision following the settlement of a legacy demerger issue with HMRC during H2. There were no cash tax payments in the year and in H1, the Group recovered from HMRC £2m in relation to the accounting period ended 31 March 2015. We exited the year with recognised carried forward tax losses of £339m (FY16: £299m) and continue to apply a 10 year time horizon from a recognition perspective.

Profit before taxation

Headline PBT, before exceptional items, was £133m up 24% year on year, with statutory PBT of £70m up £56m on FY16.

Earnings per share

	2017	**2016**
Headline earnings (£m)	**100**	**79**
Basic EPS	10.5p	8.4p
Diluted EPS	10.4p	8.3p
Statutory earnings (£m)	**58**	**2**
Basic EPS	6.1p	0.2p
Diluted EPS	6.0p	0.2p

EPS on a headline basis is provided alongside our statutory measures to allow easier comparison year on year, due to the impact of non-operating amortisation and exceptional items. A full reconciliation to Statutory results can be found in note 6 to the financial statements.

Basic headline EPS was 10.5p (FY16: 8.4p) and on a statutory basis it was 6.1p (FY16: 0.2p). Fully diluted headline EPS was 10.4p (FY16: 8.3p) and on a statutory basis it was 6.0p (FY16: 0.2p).

Net debt and cashflow

	2017	2016
Headline EBITDA	304	260
Working capital	(28)	10
Capital expenditure	(133)	(166)
Operating free cash flow	**143**	**104**
Interest and taxation	(33)	(22)
Free cash flow	**110**	**82**
Exceptional items	(46)	(88)
Acquisitions	(18)	(12)
Dividends	(150)	(135)
Share of own shares	1	63
Net cashflow	**(103)**	**(90)**
Opening net debt	(679)	(589)
Closing net debt	**(782)**	**(679)**

Net debt decreased from £847m in H1 to £782m at the year end (FY16: £679m), with headline leverage falling from 2.82x to 2.57x (FY16: 2.61x). Committed headroom at 31 March 2017 was £412m (FY16: £162m), reflecting the issuance of the Group's debut bond in Q4.

Net cash-flow for the year represented an outflow of £103m, with the inflow from £304m Headline EBITDA offset by a combination of the dividend (£150m), capital expenditure (£133m), interest costs (£35m), exceptional items (£46m) and working capital (£28m).

Capital expenditure for the year was £133m, representing c7.5% (FY16: 9%) of revenues and includes income from the sale and leaseback of the Milton Keynes facility of £15m. This expenditure represents continued investment and enhancement of our network capability, additional costs in relation to our MTTS programme, spend on our online systems to support the launch of our new propositions, and investment in our TV platform. We expect capital expenditure in FY18 to be within our capex/revenue target of 6%-7%.

During the first half of the year the Group invested £59m in working capital to finance a combination of stock delivered towards the end of the last financial year, supplier payments related to the extended distribution arrangement and the prepayment of marketing costs ahead of the launch of FLPP in the Autumn. Approximately £30m of this working capital investment reversed in the second half, with the impact of lower stock balances being broadly offset by a reduction in trade payables. Debtors increased during the period by £28m, reflecting a combination of amounts due in respect of supplier claims and a higher level of prepayments in respect of financing, fees network and IT costs and property related expenses linked to our move to the Soapworks.

Acquisitions expenditure in the year of £18m (FY16: £12m) represents £10m (FY16: £8m) in respect of the YouView joint venture and £8m in respect of contingent consideration for prior period acquisitions of tiPicall, the Virgin Media off-net broadband base and the Tesco broadband base.

Dividends

Dividends of £150m paid in the year (FY16: £135m) comprised the final dividend for FY16 10.58p and the interim dividend for FY17 of 5.29p.

The Board is committed to returning the business to revenue and customer base growth, improving cash generation and reducing leverage, and in this context has declared a Final dividend for FY17 of 5.0p (FY16: 10.58p), taking the total dividend for the year to 10.29p (FY16: 15.87p). For FY18 the Board expect to declare an Interim cash dividend of 2.5p (FY17: 5.29p) and a Final cash dividend of 5.0p (FY17: 5.0p) taking the total cash dividend for the year to 7.5p (FY17: 10.29p). Looking beyond FY18, the Board expects to resume dividend growth once the business returns to earnings growth and has reduced leverage towards the Group's Net Debt/Headline EBITDA target of 2.0x.

The Final dividend for FY17 will be paid on 4th August 2017, subject to approval at the AGM on 19th July 2017 for shareholders on the register 7th July 2017 (ex-dividend 6th July 2017).

Funding and capital structure

The group is financed through a combination of bank facilities, US Private Placement notes, Senior notes, debtor securitisation, retained profits and equity.

The Group continues to review its funding and capital structure with the objectives of diversifying sources and managing both the average tenor and interest cost. During the year the Group made significant progress on these objectives with the introduction of a £75m debtor securitisation facility in September 2016 and in January 2017, following the publication of credit ratings from both Fitch (BB-stable outlook) and Standard & Poor's (BB- positive outlook), the successful launch of our debut public bond offering. On 15 January 2017, the Group raised £400m of Senior notes at a coupon rate of 5.375%, enabling it to retire £150m of shorter dated bank facilities. The Senior notes have been listed on the Channel Island exchange.

At 31 March 2017, the Group had total facilities, including the Senior notes and US Private Placement notes, of £1,244m (FY16: £944m), further detail of which is given in the notes. At 31 March 2017 £832m (FY16: £689m) had been drawn under these facilities, leaving £412m (FY16: £255m) of undrawn facilities.

Subsequent to the year end, the group has completed the refinancing of its banking facilities for a further 5 years and as such, at 9 May 2017, the Group's debt facilities consisted on the £400m Senior notes, $185m US Private Placement notes, £75m debtor securitisation facility and £640m committed bank facility. The average term of our debt at 31 March 2017 was 3 years 11 months which has increased to 4 years 10 months from 8 May 2017.

The Group was in compliance with the terms of all its facilities, including the financial covenants, at 31 March 2017 and throughout the year and expects to remain in compliance with the terms going forward.

Going concern

The Directors have acknowledged the guidance 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting', published by the FRC in September 2014.

Our business activities, together with the factors likely to affect our future development, performance and position are set out in the Business Review. Our financial position, cash and borrowing facilities are described within this Finance review.

The breadth of our base, our value for money proposition, continuing improvements in operating efficiency and the largest unbundled network in the UK means that the Directors are confident in our ability to continue to compete effectively in the UK telecoms sector.

We have £1,244m (FY16: £944m) of committed credit facilities and as at 31 March 2017 the headroom on these facilities was £412m (FY16: £255m). Our forecasts and projections, taking into account reasonably possible changes in trading performance, indicate that there is sufficient cash and covenant headroom on our facilities and that this, together with our market positioning, means that we are well placed to manage our business risks successfully and have adequate resources to continue in operational existence for the foreseeable future. The Directors have therefore adopted the going concern basis of accounting preparing the financial statements.

Consolidated income statement

For the year ended 31 March 2017

		2017			2016		
	Notes	**Headline – before non-operating amortisation [1] and exceptional items [2] £m**	**Non-operating Amortisation [1] and exceptional items [2] £m**	**Statutory – after non-operating amortisation [1] and exceptional items [2] £m**	Headline – before non-operating amortisation [1] and exceptional items [2] £m	Non-operating amortisation [1] and exceptional items [2] £m	Statutory – after non-operating amortisation [1] and exceptional items [2] £m
Revenue	2	**1,783**	**–**	**1,783**	1,838	(3)	1,835
Cost of sales		**(834)**	**21**	**(813)**	(845)	–	(845)
Gross profit		**949**	**21**	**970**	993	(3)	990
Operating expenses excluding amortisation and depreciation		**(645)**	**(78)**	**(723)**	(733)	(80)	(813)
EBITDA	7	**304**	**(57)**	**247**	260	(83)	177
Depreciation	3	**(69)**	**(3)**	**(72)**	(72)	–	(72)
Amortisation	3	**(59)**	**(10)**	**(69)**	(49)	(10)	(59)
Share of results of joint ventures		**(11)**	**–**	**(11)**	(8)	–	(8)
Operating profit	3, 7	**165**	**(70)**	**95**	131	(93)	38
Net finance costs	4	**(32)**	**7**	**(25)**	(24)	–	(24)
Profit before taxation	7	**133**	**(63)**	**70**	107	(93)	14
Taxation	5,7	**(33)**	**21**	**(12)**	(28)	16	(12)
Profit for the year attributable to the owners of the Company	7	**100**	**(42)**	**58**	79	(77)	2
Earnings per share							
Basic (p)	8			**6.1**			0.2
Diluted (p)	8			**6.0**			0.2

	Notes	2017	2016
Statutory operating profit		**95**	38
Adjusted for:			
Non-operating amortisation	7	**10**	10
Exceptional items	7	**60**	83
Headline operating profit		**165**	131

Consolidated statement of comprehensive income

For the year ended 31 March 2017

	Notes	**2017 £m**	2016 £m
Profit for the year attributable to the owners of the Company		**58**	2
Other comprehensive (expense)/income			
Items that may be reclassified to profit or loss:			
(Losses)/gains on a hedge of a financial instrument		**(5)**	2
Currency translation differences		**–**	1
Total other comprehensive (expense)/income		**(5)**	3
Total comprehensive income attributable to the owners of the Company		**53**	5

[1] Non-operating amortisation represents amortisation of acquisition intangibles.

[2] See note 7 for a reconciliation of exceptional items.

Consolidated balance sheet

As at 31 March 2017

	Notes	2017 £m	2016 £m
Non-current assets			
Goodwill		**495**	495
Other intangible assets		**243**	227
Property, plant and equipment		**235**	302
Investment in joint ventures		**8**	9
Trade and other receivables		**6**	3
Derivative financial instruments		**31**	18
Deferred tax assets	5	**108**	115
		1,126	1,169
Current assets			
Inventories		**18**	57
Trade and other receivables		**369**	294
Current income tax receivable		**–**	3
Cash and cash equivalents		**50**	10
		437	364
Total assets		**1,563**	1,533
Current liabilities			
Trade and other payables		**(511)**	(563)
Current income tax payable		**(5)**	–
Borrowings		**–**	(25)
Provisions		**(22)**	(18)
		(538)	(606)
Non-current liabilities			
Borrowings		**(871)**	(684)
Derivative financial instruments		**–**	(1)
Provisions		**(14)**	(11)
		(885)	(696)
Total liabilities		**(1,423)**	(1,302)
Net assets		**140**	231
Equity			
Share capital		**1**	1
Share premium		**684**	684
Translation reserve		**(64)**	(64)
Demerger reserve		**(513)**	(513)
Retained earnings and other reserves		**32**	123
Total equity		**140**	231

Consolidated cash flow statement

For the year ended 31 March 2017

	Notes	2017 £m	2016[(1)] £m
Operating activities			
Operating profit	3	**95**	38
Share-based payments		**5**	5
Depreciation of property, plant and equipment	3	**72**	72
Amortisation of other operating intangible fixed assets	3	**59**	49
Non-operating amortisation	7	**10**	10
Share of losses of joint ventures		**11**	8
Impairment of inventory	7	**18**	–
Impairment of property, plant and equipment	7	**22**	–
Profit on disposal of property, plant and equipment	3	**(2)**	–
Operating cash flows before movements in working capital		**290**	182
(Increase)/decrease in trade and other receivables		**(63)**	15
Decrease/(increase) in inventory		**21**	(26)
(Decrease)/increase in trade and other payables		**(26)**	17
Increase/(decrease) in provisions		**8**	(6)
Cash generated from operations		**230**	182
Income taxes received		**2**	–
Net cash flows generated from operating activities		**232**	182
Investing activities			
Acquisition of subsidiaries and joint ventures, net of cash acquired		**(10)**	(14)
Disposal of subsidiaries and customer bases		**–**	2
Investment in intangible assets		**(82)**	(106)
Investment in property, plant and equipment		**(71)**	(72)
Disposal of property, plant and equipment		**20**	12
Cash flows used in investing activities		**(143)**	(178)
Financing activities			
Settlement of Group ESOT shares		**1**	2
Net sale of own shares		**–**	61
Payment of contingent consideration		**(8)**	–
Drawdown of borrowings	10	**143**	90
Interest paid		**(35)**	(22)
Dividends paid	6	**(150)**	(135)
Cash flows used in financing activities		**(49)**	(4)
Net increase in cash and cash equivalents		**40**	–
Cash and cash equivalents at the start of the year		**10**	10
Cash and cash equivalents at the end of the year		**50**	10

Consolidated statement of changes in equity

For the year ended 31 March 2017

	Note	Share capital £m	Share premium £m	Translation reserve £m	Demerger reserve £m	Retained earnings and other reserves £m	Total equity £m
At 1 April 2015		1	684	(65)	(513)	190	297
Profit for the year		–	–	–	–	2	2
Other comprehensive income							
Items that may be reclassified to profit or loss:							
Gain on hedge of a financial instrument		–	–	–	–	2	2
Currency translation differences		–	–	1	–	–	1
Total other comprehensive income		–	–	1	–	2	3
Total comprehensive income		–	–	1	–	4	5
Transactions with the owners of the Company							
Share-based payments reserve credit		–	–	–	–	5	5
Share-based payments reserve debit		–	–	–	–	(1)	(1)
Sale of own shares		–	–	–	–	61	61
Settlement of Group ESOT		–	–	–	–	2	2
Equity dividends	6	–	–	–	–	(135)	(135)
Taxation of items recognised directly in reserves		–	–	–	–	(3)	(3)
Total transactions with the owners of the Company		–	–	–	–	(71)	(71)
At 31 March 2016		1	684	(64)	(513)	123	231
Profit for the year		**–**	**–**	**–**	**–**	**58**	**58**
Other comprehensive income							
Items that may be reclassified to profit or loss:							
Loss on hedge of a financial instrument		**–**	**–**	**–**	**–**	**(5)**	**(5)**
Total other comprehensive expense		**–**	**–**	**–**	**–**	**(5)**	**(5)**
Total comprehensive income		**–**	**–**	**–**	**–**	**53**	**53**
Transactions with the owners of the Company							
Share-based payments reserve credit		**–**	**–**	**–**	**–**	**5**	**5**
Share-based payments reserve debit		**–**	**–**	**–**	**–**	**(2)**	**(2)**
Sale of own shares		**–**	**–**	**–**	**–**	**–**	**–**
Settlement of Group ESOT		**–**	**–**	**–**	**–**	**3**	**3**
Equity dividends	6	**–**	**–**	**–**	**–**	**(150)**	**(150)**
Total transactions with the owners of the Company		**–**	**–**	**–**	**–**	**(144)**	**(144)**
At 31 March 2017		**1**	**684**	**(64)**	**(513)**	**32**	**140**

Notes to the consolidated financial statements

1. Basis of preparation

The financial information is derived from the Group's consolidated financial statements for the year ended 31 March 2017, which have been prepared on the going concern basis in accordance with International Financial Reporting Standards (IFRS) as adopted for use in the European Union, IFRS Interpretations Committee and those parts of the Companies Act 2006 ('the Act') applicable to companies reporting under IFRS. There are no new or revised standards and interpretations that have had a material impact on the Group during the year. The financial statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments and investments. The financial statements are presented in Sterling, rounded to the nearest million, because that is the currency of the principal economic environment in which the Group operates.

The consolidated financial statements were approved by the Directors on 10 May 2017.

The financial information does not constitute statutory accounts within the meaning section 435 of the Companies Act 2006 or contain sufficient information to comply with the disclosure requirements of IFRS.

The Company's auditors, Deloitte LLP, have given an unqualified report on the consolidated financial statements for the year ended 31 March 2017, which did not include reference to any matters to which the auditors drew attention without qualifying their report and did not contain any statement under section 498 of the Companies Act 2006. Subject to approval by the Company's shareholders, the consolidated financial statements will be filed with the Registrar of Companies following the Company's Annual General Meeting on 19 July 2017.

Alternative Performance Measures

In response to the Guidelines on Alternative Performance Measures (APMs) issued by the European Securities and Markets Authority (ESMA), additional information on the APMs used by the Group is provided below. The following APMs are used by the Group.

- Headline Revenue;
- Headline EBITDA;
- Headline Operating profit;
- Headline profit before taxation;
- Headline profit after taxation;
- Headline basic EPS;
- Headline free cashflow;

Where relevant, a reconciliation between statutory reported measures and Headline measures is shown in note 7.

EBITDA is defined as Earnings before interest, tax, depreciation and amortisation. Free cashflow is defined as operating cash flows after movements in working capital, net capital expenditure and interest and taxation excluding cash exceptional items (note 7).

Headline measures exclude items which are non-trading or non-recurring. These items are not included in the performance measures the Board uses to monitor the performance of the Group.

Headline measures are used to partly determine the variable element of remuneration of senior Management throughout the Group and are also in alignment with performance measures used by certain external stakeholders in the context of the telecoms sector.

In particular, Headline EBITDA and Free Cashflow are commonly used across the telecoms industry to aid stakeholders in making comparisons between the performance of the Group and its peers.

Headline EBITDA and Free Cashflow are not defined terms under IFRS and may not be comparable with similarly titled profit measures reported by other companies. They are not intended to be a substitute for, or superior to, GAAP measures. All APMs relate to the current year results and comparative periods where provided.

2. Segmental reporting

Accounting policy

IFRS 8 'Operating Segments' requires the segmental information presented in the financial statements to be that used by the chief operating decision maker (CODM) to evaluate the performance of the business and decide how to allocate resources. The Group has identified the Board as its CODM. The Board considers the results of the business as a whole when assessing the performance of the business and making decisions about the allocation of resources. Accordingly the Group has one operating segment with all trading operations based in the United Kingdom.

	2017 £m	2016 £m
Headline revenue	**1,783**	1,838
Headline EBITDA	**304**	260
Depreciation	**(69)**	(72)
Amortisation of operating intangibles	**(59)**	(49)
Share of results of joint ventures	**(11)**	(8)
Headline operating profit (note 7)	**165**	131
Non-operating amortisation	**(10)**	(10)
Exceptional items – revenue	**–**	(3)
Exceptional items – cost of sales	**21**	–
Exceptional items – operating expenses excluding amortisation and depreciation	**(78)**	(80)
Exceptional items – depreciation	**(3)**	–
Statutory operating profit (note 7)	**95**	38

The Group's revenue is split by On-net, Off-net and Corporate products as this information is provided to the Group's CODM. On-net and Off-net comprise Consumer and Business customers that receive similar services.

	2017 £m	2016 £m
On-net	**1,342**	1,399
Corporate	**397**	384
Off-net	**44**	55
Headline revenue	**1,783**	1,838

The Group has no material overseas operations; as a result, a split of revenue and total assets by geographical location has not been disclosed.

Corporate revenue is further analysed as:

	2017 £m	2016 £m
Carrier	**121**	119
Data	**157**	120
Voice	**119**	145
	397	384

3. Operating profit

Operating profit is stated after charging/(crediting):

	2017 £m	2016 £m
Depreciation of property, plant and equipment	**69**	72
Amortisation of other operating intangible fixed assets	**59**	49
Amortisation of acquisition intangibles	**10**	10
Profit on disposal of property, plant and equipment	**(2)**	–
Impairment loss recognised on trade receivables	**60**	71
Employee costs	**136**	139
Cost of inventories recognised in expenses	**55**	72
Rentals under operating leases	**105**	100
Supplier rebates (1)	**(13)**	(13)
Service level related disputes (2) (3)	**(27)**	(17)
Auditor's remuneration	**1**	1
Exceptional items (note 7)	**86**	83
Exceptional items – disputed network charges in relation to prior years (note 7) (3)	**(29)**	–
Exceptional items – depreciation (note 7)	**3**	–

(1) Included in operating profit are associated increased costs of £13m relating to these supplier rebates.
(2) Included in operating profit are associated increased costs relating to these service level related disputes.
(3) Included in 2017 exceptional items are £12m of service level related disputes relating to 2016.

4. Net finance costs

Net finance costs are analysed as follows:

	2017 £m	2016 £m
Interest on bank loans and overdrafts	**27**	21
Facility fees and similar charges	**5**	3
Exceptional – finance income (note 7)	**(7)**	–
	25	24

In FY17, the Group recognised interest of £7m (2016: £nil) on a BT dispute settled in FY14 for the overcharging of certain wholesale Ethernet services (note 7). In 2016 the impact of finance income was not material.

In FY17, the Group issued £400m Senior Notes due 2022 (the bond). Arrangement fees of £5m were paid and are being amortised over the life of the notes. Upon receipt of the bond proceeds the Group repaid £50m of the term loan and the 2016 £100m RCF in full, accelerating the amortisation of the fees relating to this facility. The remaining fees in relation to the 2014 RCF, term loan and US Private Placement continue to be amortised over the expected life of the loans and are included within facility fees and similar charges above. The average interest rate in the year was 3.60% (2016: 3.10%).

5. Taxation

Accounting policy

Current tax, including UK corporation tax and overseas tax, is provided at amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is provided on temporary differences between the carrying amount of an asset or liability in the balance sheet and its tax base.

Deferred tax liabilities represent tax payable in future periods in respect of taxable temporary differences. Deferred tax assets represent tax recoverable in future periods in respect of deductible temporary differences, and the carry-forward of unused tax losses and credits. Deferred tax is determined using the tax rates that have been enacted or substantively enacted at the balance sheet date and are expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

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. Current and deferred tax is recognised in the income statement except where it relates to an item recognised directly in reserves, in which case it is recognised directly in reserves.

Deferred tax assets and liabilities are offset where there is a legal right to do so in the relevant jurisdictions.

Tax – income statement

The tax charge/(credit) comprises:

	2017 £m	2016 £m
Current tax:		
UK corporation tax	**5**	–
Adjustments in respect of prior years:		
UK corporation tax	**–**	(1)
Total current tax charge/(credit)	**5**	(1)
Deferred tax:		
Origination and reversal of timing differences	**9**	7
Effect of change in tax rate	**7**	6
Adjustments in respect of prior years – deferred tax credit	**(1)**	(3)
Adjustments in respect of prior years – exceptional (credit)/charge	**(8)**	3
Total deferred tax charge/(credit)	**7**	13
Total tax charge	**12**	12

The tax charge on Headline earnings for the year ended 31 March 2017 was £33m (2016: £28m), representing an effective tax rate on pre-tax profits of 25% (2016: 26%). The tax charge on Statutory earnings for the year ended 31 March 2017 was £12m (2016: £12m). The reconciliation between the Headline and Statutory tax charge is shown in note 6.

The principal differences between the tax charge and the amount calculated by applying the standard rate of UK corporation tax of 20% (2016: 20%) to the profit before taxation are as follows:

	2017 £m	2016 £m
Profit before taxation	**70**	14
Tax at 20% (2016: 20%)	**14**	3
Items attracting no tax relief or liability	**–**	1
Effect of change in tax rate	**7**	6
Adjustments in respect of prior years	**(1)**	(3)
Adjustments in respect of prior years – exceptional (credit)/charge	**(8)**	3
Movement in recognised tax losses during the year	**–**	3
Movement in unrecognised tax losses during the year	**–**	(1)
Total tax charge through income statement	**12**	12

Tax – retained earnings and other reserves

Tax on items recognised directly in retained earnings and other reserves is as follows:

	2017 £m	2016 £m
Total tax charge through income statement	**12**	12
Deferred tax charge recognised directly in retained earnings and other reserves	**–**	3
Total tax charge through retained earnings and other reserves	**12**	15

The deferred tax charge recognised directly in retained earnings and other reserves for the years ended 31 March 2017 and 31 March 2016 relates to share-based payments.

Tax – balance sheet

The deferred tax assets recognised by the Group and movements thereon during the year are as follows:

	Share-based payments £m	Timing differences on capitalised costs £m	Tax losses £m	Other timing differences £m	Total £m
At 1 April 2016	**3**	**53**	**56**	**3**	**115**
(Charge)/credit to the income statement	**–**	**(11)**	**4**	**–**	**(7)**
At 31 March 2017	**3**	**42**	**60**	**3**	**108**

	Share-based payments £m	Timing differences on capitalised costs £m	Tax losses £m	Other timing differences £m	Total £m
At 1 April 2015	6	54	69	1	130
(Charge)/credit to the income statement	–	(1)	(13)	2	(12)
Charge to reserves	(3)	–	–	–	(3)
At 31 March 2016	3	53	56	3	115

No deferred tax assets and liabilities have been offset in either year, except where there is a legal right to do so in the relevant jurisdictions.

On 6 September 2016, a reduction in the UK statutory rate of taxation was substantively enacted, bringing the tax rate down from 19% to 17% from 1 April 2020, replacing the 18% announced previously. Accordingly, the tax assets and liabilities recognised at 31 March 2017 take account of these changes.

At 31 March 2017, the Group had unused tax losses of £606m (2016: £650m) available for offset against future taxable profits. A deferred tax asset of £60m (2016: £56m) has been recognised in respect of £339m (2016: £299m) of such losses, based on expectations of recovery in the foreseeable future.

No deferred tax asset has been recognised in respect of the remaining £267m (2016: £351m) as there is insufficient evidence that there will be suitable taxable profits against which these losses can be recovered. All losses may be carried forward indefinitely.

6. Dividends

Accounting policy

Dividend income is recognised when payment has been received. Final dividend distributions are recognised as a liability in the financial statements in the year in which they are approved by the relevant shareholders. Interim dividends are recognised in the year in which they are paid.

The following dividends were paid by the Group to its shareholders:

	2017 £m	2016 £m
Ordinary dividends		
Final dividend for the year ended 31 March 2015 of 9.20p per ordinary share	**–**	85
Interim dividend for the year ended 31 March 2016 of 5.29p per ordinary share	**–**	50
Final dividend for the year ended 31 March 2016 of 10.58p per ordinary share	**100**	–
Interim dividend for the year ended 31 March 2017 of 5.29p per ordinary share	**50**	–
Total ordinary dividends(1)	**150**	135

(1) Deducted from Company reserves.

The proposed final dividend for the year ended 31 March 2017 of 5.0p (2016: 10.58p) per ordinary share on approximately 950 million (2016: 946 million) ordinary shares (approximately £48m) was approved by the Board on 10 May 2017 and will be recommended to shareholders at the AGM on 19 July 2017. The dividend has not been included as a liability as at 31 March 2017. The payment of this dividend will not have any tax consequences for the Group.

The Group ESOT has waived its rights to receive dividends in the current and prior year and this is reflected in the analysis above.

7. Reconciliation of Headline information to statutory information

Headline information is provided because the Directors consider that it provides assistance in understanding the Group's underlying performance.

Accounting policy

Headline results are stated before the amortisation of acquisition intangibles and exceptional items. Exceptional items are those that are considered to be one-off or non-recurring in nature and so material that the Directors believe that they require separate disclosure to avoid distortion of the presentation of underlying performance and should be separately presented on the face of the income statement.

Critical judgements in applying the Group's accounting policy

The classification of items as exceptional is subjective in nature and therefore judgement is required to determine whether the item is in line with the accounting policy criteria outlined above. Determining whether an item is exceptional is a matter of qualitative assessment, making it distinct from the Group's other critical accounting judgements where the basis for judgement is estimation.

Year ended 31 March 2017	Revenue £m	EBITDA £m	Operating profit £m	Profit before taxation £m	Taxation £m	Profit for the year £m
Headline results	**1,783**	**304**	**165**	**133**	**(33)**	**100**
Exceptional items – Operating efficiencies – MTTS (a)	**–**	**(24)**	**(24)**	**(24)**	**5**	**(19)**
Exceptional items – Operating efficiencies – property (b)	**–**	**(8)**	**(8)**	**(8)**	**2**	**(6)**
Exceptional items – Network transformation (c)	**–**	**(8)**	**(11)**	**(11)**	**2**	**(9)**
Exceptional items – Mobile proposition (d)	**–**	**(49)**	**(49)**	**(49)**	**10**	**(39)**
Exceptional items – Acquisitions and disposals (e)	**–**	**1**	**1**	**1**	**–**	**1**
Exceptional items – Disputed network charges (f)	**–**	**29**	**29**	**29**	**(6)**	**23**
Exceptional items – Operating expenses – cyber attack (g)	**–**	**2**	**2**	**2**	**(1)**	**1**
Exceptional items – Finance income (h)	**–**	**–**	**–**	**7**	**(1)**	**6**
Exceptional items – Taxation (i)	**–**	**–**	**–**	**–**	**8**	**8**
Amortisation of acquisition intangibles (j)	**–**	**–**	**(10)**	**(10)**	**2**	**(8)**
Statutory results	**1,783**	**247**	**95**	**70**	**(12)**	**58**

Year ended 31 March 2016	Revenue £m	EBITDA £m	Operating profit £m	Profit before taxation £m	Taxation £m	Profit for the year £m
Headline results	1,838	260	131	107	(28)	79
Exceptional items – Revenue – cyber attack (g)	(3)	(3)	(3)	(3)	1	(2)
Exceptional items – Operating expenses – cyber attack (g)	–	(39)	(39)	(39)	8	(31)
Exceptional items – Operating efficiencies – MTTS (a)	–	(31)	(31)	(31)	6	(25)
Exceptional items – Operating efficiencies - property (b)	–	(10)	(10)	(10)	2	(8)
Exceptional items – Acquisitions and disposal (e)	–	–	–	–	–	–
Exceptional items – Taxation (i)	–	–	–	–	(3)	(3)
Amortisation of acquisition intangibles (j)	–	–	(10)	(10)	2	(8)
Statutory results	1,835	177	38	14	(12)	2

During the year ended 31 March 2017, Cash exceptional items amounted to £46m (2016: £88m).

a) Operating efficiencies – Making TalkTalk Simpler (MTTS)

During the year ended 31 March 2017, the Group concluded its wide ranging transformation programme that is delivering material improvements to our customers' experience, driving operating cost savings, and reducing SAC through lower churn and costs per add (CPA).

The costs incurred in the year include work on improving Consumer and TalkTalk Business systems and processes which focus on customer experience and the review of the organisational structure of the business.

These programmes have resulted in £24m (2016: £31m) of costs including project management, redundancy, consultancy, migration and call centre costs.

A total taxation credit of £5m has been recognised on these costs in the year ended 31 March 2017 (2016: £6m).

b) Operating efficiencies – property rationalisation

During the prior year the Group reviewed the sites from which it operates, and announced its intention to exit its Warrington and Irlam sites to relocate to one site at the Soapworks in Salford.

These programmes have resulted in £8m (2016: £10m) of costs including redundancy, property, consultancy and dual running costs.

A total taxation credit of £2m has been recognised on these costs in the year ended 31 March 2017 (2016: £2m).

c) Network transformation

During the year ended 31 March 2017, the Group embarked on a significant transformation programme which will fundamentally restructure the Group's network, IT infrastructure and technology organisation. The change the Group is undertaking will ensure it is fit for the future and underpins the wider Group strategy in providing a great service to our customers as a value provider in the industry. This is a discrete project expected to run until FY20.

This programme has resulted in £11m (2016: £nil) of costs including project management, consultancy, dual running costs, decommissioning costs and accelerated depreciation costs.

A total taxation credit of £2m has been recognised on these costs in the year ended 31 March 2017 (2016: £nil).

d) Mobile proposition

During the year ended 31 March 2017, the Group began to reorganise the business under the new leadership team focussing on fewer, clearer priorities that are focused on investment in the Group's core fixed network. As part of the review the Group reassessed its mobile strategy and how we allocate capital. The Group has therefore decided not to pursue an inside-out mobile network strategy and instead to work with our partners on an alternative distribution strategy.

As a result, the Group has assessed that items within inventory and property, plant and equipment have no further economic benefit to the Group leading to impairment charges and onerous lease costs of £49m (2016: £nil). Additional reorganisation costs may be incurred in FY18 as the Group works with its MNO partners on developing an alternative mobile distribution strategy.

A total taxation credit of £10m has been recognised on these costs in the year ended 31 March 2017 (2016: £nil).

e) Acquisitions and disposal

During the year ended 31 March 2017, final migrations of prior year customer base acquisitions were completed, following completion any amounts provided for but not utilised were released resulting in a credit of £1m (2016: £nil).

The tax impact in either year is immaterial.

f) Disputed network charges

During the year ended 31 March 2017, the Group has recognised a £29m credit (2016: £nil) following the resolution of disputes relating to prior periods.

A total taxation charge of £6m has been recognised on these credits in the year ended 31 March 2017 (2016: £nil).

g) Cyber attack

During the year ended 31 March 2017, the Group received insurance proceeds of £3m (2016: £nil) in relation to specific cyber related costs incurred in the prior year offset by £1m of costs incurred in the current year, including an ICO fine of £0.4m.

A total taxation charge of £1m has been recognised on these items in the year ended 31 March 2017 (2016 £nil).

In the prior year, there was a significant and sustained cyber attack on the TalkTalk website. Following this attack the Group issued an increased number of credits to retain its customers. The costs of these credits are recognised against revenue and amounted to £3m. The Group also incurred costs of £39m. These costs included restoring our online capability with enhanced security features, associated IT, incident response and consultancy costs and providing free upgrades to our customers.

A total taxation charge of £nil has been recognised on these items in the year ended 31 March 2017 (2016: credit of £8m).

h) Finance income

During the year ended 31 March 2017, the Group recognised interest of £7m (2016: £nil) on a BT dispute settled in FY14 for the overcharging of certain wholesale Ethernet services.

A total taxation charge of £1m has been recognised on these items in the year ended 31 March 2017 (2016: £nil).

i) Taxation items

During the year ended 31 March 2017, the Group resolved a longstanding enquiry with HMRC in relation to the tax treatment of £85m of losses in respect of TalkTalk Brands Limited. This has resulted in a tax credit of £8m (2016: £nil).

In the prior year, the Group recognised a tax charge of £3m which relates to the impact of the statutory corporation tax rate change from 20% to 19% and then to 18% on prior year exceptional tax assets.

j) Amortisation of acquisition intangibles

An amortisation charge in respect of acquisition intangibles of £10m was incurred in the year ended 31 March 2017 (2016: £10m).

A total taxation credit of £2m has been recognised in relation to the charge in the year ended 31 March 2017 (2016: £2m).

8. Earnings per ordinary share

Earnings per ordinary share are shown on a Headline and statutory basis to assist in the understanding of the performance of the Group.

	2017 £m	2016 £m
Headline earnings (note 7)	**100**	79
Statutory earnings	**58**	2
Weighted average number of shares (millions):		
Shares in issue	**955**	955
Less weighted average holdings by Group ESOT	**(7)**	(19)
For basic EPS	**948**	936
Dilutive effect of share options	**11**	11
For diluted EPS	**959**	947

	2017 Pence	2016 Pence
Basic earnings per ordinary share		
Headline	**10.5**	8.4
Statutory	**6.1**	0.2

	2017 Pence	2016 Pence
Diluted earnings per ordinary share		
Headline	**10.4**	8.3
Statutory	**6.0**	0.2

There are no share options considered anti-dilutive in the year ended 31 March 2017 (2016: nil).

9. Cash and cash equivalents and borrowings

(a) Cash and cash equivalents are as follows:

	2017 £m	2016 £m
Cash at bank and in hand	**50**	10

The effective interest rate on bank deposits and money market funds was 0.1% (2016: 0.3%).

(b) Borrowings comprise:

	Maturity	2017 £m	2016 £m
Current (£100m term loan)	2017	**–**	25

	Maturity	2017 £m	2016 £m
Non-current			
$185m US Private Placement (USPP) Notes	2021, 2024, 2026	**148**	129
£560m revolving credit facility	2019	**165**	430
£50m bilateral agreements	2019	**50**	50
£100m term loan	2019	**50**	75
£100m revolving credit facility	2017	**–**	–
£75m receivables purchase agreement facility	2018	**58**	–
£400m Senior Notes due 2022	2022	**400**	–
Non-current borrowings before derivatives		**871**	684
Total borrowings before derivatives		**871**	709
Derivatives		**(39)**	(20)
Borrowings after derivatives		**832**	689

	Maturity	2017 £m	2016 £m
Undrawn available committed facilities	2018, 2019	**412**	255

The book value and fair value of the Group's borrowings, are as follows:

	2017 £m	2016 £m
Less than 1 year	**–**	25
1 to 2 years	**58**	25
2 to 3 years	**265**	–
3 to 4 years	**–**	530
4 to 5 years	**482**	–
Greater than 5 years	**27**	109
Borrowings after derivatives	**832**	689

Borrowing facilities

The Group's committed facilities total £1,244m (2016: £944m). The Group's uncommitted facilities total £116m (2016: £81m) giving headroom on committed facilities and uncommitted facilities of £412m (2016: £255m) and £116m (2016: £81m) respectively.

The financial covenants included in each bank facility and the USPP Notes restrict the ratio of net debt to EBITDA and require minimum levels of interest cover. The amounts used in the covenant calculations are subject to adjustments as defined under the terms of the arrangement. The Group was in compliance with its covenants throughout the current and prior periods.

Details of the Group's borrowing facilities of the Group as at 31 March 2017 are set out below:

£400m Senior Notes due 2022

On 15 January 2017 TalkTalk Telecom Group PLC issued £400m Senior Notes due 2022. The Senior Notes include incurrence-based covenants customary for this type of debt, including limitations on TalkTalk's ability to incur additional debt and make restricted payments, subject to certain exceptions. The Group is permitted to incur additional debt subject to compliance with a net debt to EBITDA ratio of 4.0x and to pay dividends when net debt to EBITDA is below 3.0x (2.75x from January 2019). Regardless of the Company's net debt to EBITDA ratio, dividends are also permitted to be paid out of a basket based on 50% of cumulative consolidated net income from 1 October 2016. The Senior Notes also contain a separate exception for the payment of the final dividend for FY17 up to £105m. The interest rate payable on the notes is 5.375% payable semi-annually. The bond proceeds were used to repay the drawings of the £100m 2016 revolving credit facility in full, and partially repay the drawings under the 2014 revolving credit facility and term loan.

$185m USPP Notes

In July 2014, the Group issued $185m of USPP Notes maturing in three tranches ($139m in 2021, $25m in 2024 and $21m in 2026). The interest rate payable on the Notes is at a margin over US treasury rate for the appropriate period. The USPP proceeds were swapped to Sterling to give £109m (£82m in 2021, £15m in 2024 and £12m in 2026) and the net debt includes retranslation of the USPP funds at the rates achieved where hedged by cross-currency swaps. The fair value of the cross currency rate swap at 31 March 2017 was £39m (2016: £20m).

£560m revolving credit facility (RCF) and £50m bilateral agreement

The Group has a £560m RCF, which matures in July 2019. The interest rate payable in respect of drawings under this facility is at a margin over LIBOR and for the appropriate period. The actual margin applicable to any drawing depends on the ratio of net debt to EBITDA calculated in respect of the most recent accounting period. In addition to the RCF, the Group also has a £50m bilateral agreement on the same terms, signed in July 2014, which matures in July 2019.

£100m term loan

Following repayment of £50m from the bond proceeds, the Group has a committed term loan of £50m (March 2016: £100m), with a final maturity date of July 2019. The interest rate payable in respect of drawings under this facility is at a margin over LIBOR for the appropriate period. The actual margin applicable to any drawing depends on the ratio of net debt to EBITDA calculated in respect of the most recent accounting period.

Receivables purchase agreement

In September 2016, the Group signed a £75m receivables purchase agreement which matures in September 2018 and is included within committed facilities. The Group has the ability on a rolling basis to sell its receivables to a third party vehicle in exchange for a discounted consideration. The Group is deemed to control the third party vehicle and therefore continues to consolidate the relevant receivables on the grounds that substantially not all the risks and rewards of ownership have been transferred under the programme.

Uncommitted money market facilities and bank overdrafts

These facilities are used to assist in short term cash management and bear interest at a margin over the Bank of England base rate.

New £640m revolving credit* facility *(RCF)

On 8 May 2017, the Group refinanced the 2014 RCF, the 2014 bilateral agreement and the £100m term loan. The new £640m 2017 RCF is a five year committed facility which contains financial covenants that restrict the ratio of net debt to EBITDA and requires minimum levels of interest cover. The interest rate payable on this facility is at a margin over LIBOR for the appropriate period. The actual margin applicable to any drawing depends on the ratio of net debt to EBITDA calculated in respect of the most recent accounting period.

10. Analysis of changes in net debt

	Opening £m	Net cash flow £m	Non-cash movements £m	Closing £m
2017				
Cash and cash equivalents	**10**	**40**	**–**	**50**
Borrowings	**(709)**	**(143)**	**(19)**	**(871)**
Derivatives	**20**	**–**	**19**	**39**
	(689)	**(143)**	**–**	**(832)**
Total net debt	**(679)**	**(103)**	**–**	**(782)**

	Opening £m	Net cash flow £m	Non-cash movements £m	Closing £m
2016				
Cash and cash equivalents	10	–	–	10
Borrowings	(615)	(90)	(4)	(709)
Derivatives	16	–	4	20
	(599)	(90)	–	(689)
Total net debt	(589)	(90)	–	(679)