

# Shaping the future



**MEARS**

**Mears is a market leader in providing housing management and maintenance services to the affordable housing sector and a major presence in the homecare and support market.**



## Housing



## Care

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## Financial highlights

- Interim results are in line with management expectations.
- Group revenues were £435.3m (2017: £470.8m), with Housing revenues stabilising, as expected.
- Operating margins increased to 4.7% (2017: 4.1%), driven by the improving profitability of the Care division.
- Profit before tax and before the amortisation of acquisition intangibles and exceptional costs increased to £19.0m (2017: £18.3m).
- The review of central support structures has identified and secured annualised savings of circa £5.0m in line with previous guidance. The cost of implementing the changes, amounting to £4.0m, has been classified as exceptional.
- Cash generated from continuing operations as a proportion of EBITDA, excluding the impact of Housing development projects, was 84% (2017: 72%) for the rolling twelve-month period to 30 June 2018.
- Strong current bid pipeline of over £2.8 billion for 2018 is significantly higher than normal levels and includes two opportunities that are very large in scale. The Group has made encouraging progress with tenders in the period and the Board remains cautiously optimistic of a successful outcome.
- The Board has declared an interim dividend of 3.55p per share (2017: 3.45p), an increase of 3%.
- The Board remains confident of delivering its expectations for the full financial year and in the Group's long-term prospects.



*Pick up where you left off, any time*

▶ Read this report at any time on our website, [www.mearsgroup.co.uk](http://www.mearsgroup.co.uk)

### Group revenue

£435.3m -8%

2018	£435.3m
2017	£470.8m
2016	£466.2m

### Group operating profit\*

£20.5m +5%

2018	£20.5m
2017	£19.4m
2016	£19.4m

### Dividends per share

3.55p +3%

2018	3.55p
2017	3.45p
2016	3.30p

### Normalised diluted earnings per share\*

15.04p +8%

2018	15.04p
2017	13.98p
2016	13.55p

\* On continuing activities stated before the amortisation of acquisition intangibles and exceptional costs. The normalised EPS measure is further adjusted to reflect a full tax charge.

## Mears at a glance

**We focus on long-term outcomes and positive social, economic and environmental impact, across our two divisions.**

# Housing

## Revenue

£374.9m -6.8%

2018	£374.9m
2017	£402.1m
2016	£389.6m

## Operating profit\*

£19.0m -8.8%

2018	£19.0m
2017	£20.8m
2016	£18.9m

## Operating margin\*

5.1%

2018	5.1%
2017	5.2%
2016	4.8%

\* Before amortisation of acquisition intangibles and long-term incentive plans.

**We carry out 6,000 repairs a day in Homes across the UK.**

### The Housing division made satisfactory progress in 2018

Our broader service offering, incorporating our new homes capability alongside housing management and maintenance, supports our involvement in new emerging placemaking partnerships, where our involvement extends beyond traditional outsourcing and is focused on creating more sustainable communities.

Our clients are increasingly looking for partners who can operate strategically as well as operationally across a range of housing services. Mears has extended its core reactive and planned maintenance offering to include housing management to support clients in delivering more integrated solutions, aligned to their strategic challenges.

This strategic evolution has given the Group access to opportunities that previously would have been out of reach.

#### Our services

- Repairs and maintenance
- Planned and cyclical maintenance
- Estate management
- Asset management
- Income management
- Emergency accommodation
- New housing development

#### Our customers

- Local Authorities
- Registered Social Landlords
- Private landlords
- Tenants and service users
- Community groups
- Pension funds



## Our key strengths

### Differentiated service delivery

In order for customers to recommend us, we must deliver excellent service. We randomly conduct over 80,000 Housing customer surveys each year.

### Strategic relationships

We listen carefully to the needs of our clients and their tenants. As our clients' needs have changed, we have developed a broader service offering which has increased the depth of our client partnerships.

### Strong financial management

We operate in a high volume, low value and low margin environment where we have delivered consistent financial results over an extended period of time. This is achieved through works management systems, conservative accounting policies and a culture of giving attention to detail.

### Social value

We lead the way with social value in the markets where we operate, delivering meaningful outcomes through positive community engagement projects and effective measurement.

## Care

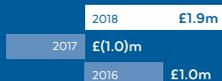
Revenue

£60.3m -12.2%



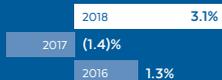
Operating profit/loss\*

£1.9m +290%



Operating margin\*

3.1%



\* Before amortisation of acquisition intangibles and long-term incentive plans.

## We provide personal care to over 15,000 elderly and disabled people.

### The Care division made good progress in the period

We are continuing to see the emergence of new commissioning models that are long-term partnering orientated. We are focused on improving quality and cost over time and combining services into an integrated approach to achieve better outcomes for users at less overall cost to the public purse.

The Group is increasingly directing its Care bidding activity towards those clients where there are likely to be opportunities to provide a complete Housing service.

We deliver broad solutions to the independent living challenges faced by so many elderly people, as well as younger people with physical or mental disabilities.

At the heart of what we do is the provision of quality care to those that depend on us.

### Our services

- Independent living services
- Aids and adaptation
- Complex care
- Assistive technology
- Live-in care
- Extra care

### Our customers

- Local Authorities
- Community groups
- Charities
- NHS



## Business review



**“Mears is evolving its service, especially in areas of Housing Management and Development, to align fully with customer demand and to provide additional growth opportunities.”**

**David Miles**  
Chief Executive Officer

### Summary

- Mears has continued to be highly selective towards the opportunities that it chooses to tender. Increasingly, the Group's drive is towards developing opportunities within housing management and housing development, or securing 'placemaking' opportunities.
- The housing market has changed positively in recent years and Mears has evolved well to ensure that its service offering fully addresses the challenges of its clients.
- As expected, the Care division has delivered a significantly improved first half performance with margins improving from those delivered in the second half of 2017. Management remains highly selective in bidding for any new work and regularly revisits its existing activities, striving to deliver good quality care at a sustainable margin.
- Mears continues to evolve its strategic direction towards providing a broader Housing offering. The divisions are operating very well and our excellent service delivery is putting Mears in a good position to secure new business opportunities.

### Introduction

Mears has delivered a solid performance in the first half of 2018 with results in line with management expectations.

Group revenues for the half year reduced to £435.3m (2017:£470.8m). This represents a positive improvement when compared with the second half of 2017 and reflects the expected stabilisation in Housing revenues. Profit before tax and before the amortisation of acquisition intangibles and exceptional costs grew to £19.0m (2017: £18.3m) with operating margins increasing to 4.7% (2017: 4.1%), driven by the improving profitability of the Care division. Normalised diluted earnings per share, based upon earnings before the amortisation of acquisition intangibles and non-recurring costs, and adjusted for a full tax charge, increased by 8% to 15.04p (2017: 13.98p).

As reported previously, the Group has carried out a review of its central support structures to ensure that they are efficient and deliver value. This is particularly relevant given the changing sales mix across our broad service offering that brings a differing support requirement. The review has identified and secured annualised savings of circa £5.0m in line with previous guidance. The cost of implementing the changes, amounting to £4.0m, has been classified as exceptional costs and has been added back within the normalised results. In addition to the central review, a review of local operations is progressing with a view to identifying further efficiency improvements and cost savings around the Group.

Cash generated from continuing operations as a proportion of EBITDA, excluding the impact of Housing development projects, was 84% (2017:72%) for the rolling twelve-month period to 30 June 2018. While satisfactory, management remains focused on improving the level of conversion. Importantly, average daily net debt, excluding the property acquisition facility, was £102.1m (2017: £85m), slightly better than our expectations. Further detail in respect of the Group's working capital management is set out later in this statement.

The Board remains confident about the Group's prospects and regularly reviews the Group's dividend policy to maximise returns to shareholders whilst maintaining a prudent capital structure and retaining the ability to invest for growth. The Board is declaring an increased interim dividend of 3.55p per share (2017: 3.45p), an increase of 3%, payable on 8 November 2018 to shareholders on the Register on 19 October 2018.

## Operations

### Housing

	2017 H1	2017 H2	2018 H1
Revenue £m	402.1	364.0	<b>374.9</b>
Operating profit £m*	20.8	18.7	<b>19.0</b>
Operating profit %*	5.2%	5.1%	<b>5.1%</b>

\* Before long-term incentive plan

The Housing division delivered a satisfactory first half performance. As expected, revenues show a reduction when compared with the comparative period in 2017; however, when looking on a sequential basis, revenues in the first half were maintained at a similar level to the second half of 2017, demonstrating that Housing activity has stabilised since the well documented events which triggered the sudden change in customer spending priorities last year. While operating margins were broadly consistent with the prior year, driving greater operating efficiency remains a key area of focus for the business.

The housing market has changed positively in recent years and Mears has evolved well to ensure that its service offering fully addresses the challenges facing its clients. Mears has widened its focus over and above simply scheduling and delivering responsive and planned maintenance in housing and it has successfully developed its capabilities to provide a broad spectrum of housing services. Similarly, the Group has been successful in developing its capabilities of building new homes. Whilst the Group does not see itself as a property developer, more and more opportunities require a broad service offering and it is a key strength to deliver a set of key core services within a single business capability. Local Authorities and Housing Associations remain the key stakeholders, but Mears service offering crosses the boundaries of social, affordable, community, key worker, shared-ownership and private rented housing. Importantly, Mears is a Registered Provider in its own right and this positions us well as the market continues to develop.

Housing revenues have been categorised as maintenance, management and development. Whilst Housing is operated and managed as a single division, and will continue to be reported as such, this level of disclosure reflects the fact that these revenue streams carry differing growth expectations, working capital requirements and risk profiles. Moreover, opportunities are increasingly being secured that require a full asset management service that do not slot easily into a single category. Given the level of shared overheads and support costs, it would not be meaningful to disclose any split of operating profit.

	2017 H1	2017 H2	2018 H1
Revenue			
Housing maintenance	325.2	281.7	<b>292.9</b>
Housing management	66.1	67.1	<b>67.9</b>
Housing development	10.8	15.2	<b>14.1</b>
Total	402.1	364.0	<b>374.9</b>

Mears has continued to be highly selective towards the opportunities that it chooses to tender. Increasingly, the Group's drive is towards developing opportunities within housing management and housing development, or securing 'placemaking' opportunities that combine traditional maintenance contracting with a full suite of housing management and asset management services. Whilst the traditional stand-alone maintenance market still provides potential for growth, the Group has reduced its dependency upon client discretionary spend. Mears previously made a decision to stop bidding for one-off refurbishment projects as this was an area which had become increasingly price competitive. This decision has been further vindicated given the latest Registered Provider accounts which report spending on major capital repairs reducing by 14% over a twelve-month period as funding is redirected to increasing the housing stock. Whereas two years ago, Mears estimated that around 15% of its traditional maintenance revenues were discretionary, this is now only around 5%, which is positive and gives a higher degree of revenue certainty.



## Business review continued

### Operations continued

#### Housing continued

Mears anticipates its Housing division will deliver annual revenue growth of 5% over the medium term, being a blend of differing growth expectations across each area of activity as detailed below:

Indicative medium-term annual revenue growth

Housing maintenance	1%
Housing management	10%
Housing development	25%
Weighted average	5%

In Housing maintenance, growth is expected to be low. Most work in this area is secured through a formal public procurement process. Positively, over the next 18 months, there are no existing contracts up for renewal; therefore, any new orders secured are accretive to the current revenue run-rate. The Group has a number of existing contracts up for rebid in 2020 which inevitably represents some risk over the medium term but with it comes opportunity. It is worth emphasising also that the Group's housing management activities incorporate an element of maintenance; therefore, whilst the maintenance growth in isolation is low, this reflects a change in allocation more than simply a change in activity.

In housing management, the business expects to continue to deliver double-digit growth for the medium term. The majority of growth within our current budget is secured through a negotiated rather than competitive route. Notwithstanding that, as previously highlighted, there are currently two very significant competitive bids, working with Central Government departments, which provide scope for the Group to outperform its current expectations if we are successful.

**“We have developed a broader service offering to meet our clients’ needs.”**

Housing development is the smallest but fastest-growing revenue stream in the Group, driven by the significant shortage of affordable housing, whilst leveraging the Group's reputation and extensive customer relationships. This element of work follows either a contracting model or a joint venture model. The latter model brings with it some requirement for the Group to provide an element of funding, which is a substantial constraint on growth in this area.

#### Care

	2017 H1	2017 H2	2018 H1
Revenue £m	68.7	65.3	<b>60.3</b>
Operating profit £m*	(1.0)	1.5	<b>1.9</b>
Operating profit %*	(1.4)	2.3	<b>3.1</b>

\* Before long-term incentive plan

As expected, the Care division has delivered a significantly improved first half performance with margins improving from those delivered in the second half of 2017.

Management remains highly selective in bidding for any new work and regularly revisits its existing activities, striving to deliver good quality care at a sustainable margin rather than placing emphasis upon top-line growth. The Group is increasingly directing its Care bidding activity towards those clients where there are likely to be opportunities to provide a complete housing service and, consequently, there is less focus on those opportunities which provide a single care service in isolation. This trend is evidenced by the significant extra care housing scheme secured in the first half year which encompasses all the Group's services, as set out below.

The Care division has secured satisfactory charge rate increases of 3.0%, which broadly matched the increasing cost base driven by an increase in the National Living Wage and increase in the pension auto-enrolment contribution rate. The main challenge in Care remains the sourcing and retention of sufficient care workers of good quality and this is an area that continues to receive significant attention.

*We need to communicate more clearly the fundamental role played by Care within our Housing business*

## Business development

Mears continues to evolve its strategic direction towards providing a broader Housing offering. The divisions are operating very well and our excellent service delivery is putting Mears in a good position to secure new business opportunities. This strategic evolution has given the Group access to opportunities that previously would have been out of reach and, given the nature of the type of work, the contracts we secure are increasingly larger and of a longer duration, with multiple revenue streams.

The pipeline of traditional opportunities continues to flow through at a consistent level, with around £1 billion expected to be tendered this year. The Group is well placed on a number of these and expects to deliver a bid conversion rate, by value, in line with historical norms of one in three. Encouragingly, in the year to date, the Group has delivered a conversion in excess of this, securing new revenues of £70m, including:

- A contract to deliver repairs and maintenance services to Riverside Housing Association for an initial period of five years, valued at £62m. There is an option to extend the contract for a further five years, taking the total opportunity to £125m. The contract covers over 11,500 homes across the Midlands, East Anglia and the South of England. The service requires Mears to work alongside Riverside's own in-house maintenance provider and commenced in July 2018.
- A contract as a single supplier, under a pilot arrangement, to carry out data migration activities which include digitisation and transformation of Local Authorities' Local Land Charge Registers on behalf of Her Majesty's Land Registry. This contract is valued at £1.3m for the initial nine-month period with potential for further works upon completion of a successful pilot. This is an important additional service for the Group, which is already the UK's largest specialist provider of land referencing services.

In addition, Mears has been appointed preferred bidder for a significant opportunity for the provision of housing with care services. The award of this contract will be subject to completion of due diligence and, at present, the Group is not in a position to name the client. Subject to the final award, Mears will create four extra care housing schemes via a design, build, finance and operate (DBFO) model. The value of the works are estimated to be £110m comprising around £50m relating to the design and build component, which is anticipated to be delivered in 2019–2020, around £50m for housing management and maintenance over a 50-year period and £10m for care provision over an initial ten-year period. This is particularly pleasing given that, whilst the majority of these revenues will be delivered through our Housing division, the bidding opportunity was commissioned by social services and it was our

care expertise and awareness in dealing with elderly and vulnerable tenants that was fundamental in being appointed preferred bidder. We continue to see a good pipeline of similar opportunities developing with Local Authorities to procure new care accommodation for Supported Living and Extra Care services which, in the majority of instances, involves a combination of funding, build, property management and care provision.

The Group has been successful in being appointed to the Crown Commercial Service (CCS) approved supplier list for the provision of management services. Mears would typically not announce such arrangements, and no value has been placed against this within the Group's order book, however, this appointment is significant. The arrangement is for an initial period of two years, with the option for this to be extended by up to a further three years, and allows Government departments, such as the Ministry of Defence, to award work at short notice without going through a lengthy procurement process, so making Mears eligible for such contracts.

In addition to the pipeline of traditional maintenance opportunities, the Group anticipates bidding a further £1.8 billion of placemaking opportunities during the next twelve months. As stated previously, this pipeline includes two opportunities that are very significant in scale. The Group has made encouraging progress in the period and the Board remains cautiously optimistic of a successful outcome.

The increasingly innovative nature of our housing management solutions means that work can often be secured without the requirement for an extended, competitive and expensive tender process. These opportunities are not valued in the Group's pipeline or in the bid conversion metrics but are becoming increasingly material to the Group. New orders secured in the first half year through this negotiated route include:

- A partnership with the London Borough of Waltham Forest (LBWF) to arrange the purchase and refurbishment of 365 homes currently under private ownership. The key aim is to provide LBWF with an alternative, affordable housing supply to reduce the significant bed and breakfast accommodation costs currently being incurred. Mears has engaged funding partners to finance the purchase of properties on behalf of the client, while it will carry out refurbishment works and act as managing agent for the portfolio. The contract will be operated by LBWF and Mears for 40 years and the arrangement is valued at circa £75m. The operation will mobilise in August 2018 and the purchase and refurbishment phase will continue over a period of 24 months.

## Business review continued

## Business development continued

→ Mears has entered into a partnership with CBRE Global Investors and 'Step Forward', a property company established by former service personnel who are seeking to provide affordable homes for ex-service personnel and enable Local Authorities to meet their duty under the Armed Forces Covenant. The proposal is that, under a nomination agreement, a Local Authority agrees that for each s106 affordable housing unit, priority will be given to former and current service people. CBRE has created an investment fund of around £250m and anticipates acquiring 2,000 properties over the next two years to place into this arrangement. Mears, through its Registered Provider, manages the housing, assuming responsibility for rent collection, occupancy and asset management over a 22-year period, whilst ensuring that the conditions of the s106 planning consent are met. Based on property numbers of 2,000, this would equate to revenues in excess of £100m over the contract term.

→ Mears has entered into a joint venture with Sovereign Housing Association to build 65 units of mixed tenure in Wantage, Oxfordshire. The works are expected to commence on site in Spring 2019 and are due to complete at the end of 2020. Under the terms of the joint venture, Sovereign has acquired the land and, through a development agreement, Mears is responsible for service delivery.

The Group is pleased with the progress made in securing new work orders. A number of these contracts have a long mobilisation phase, with revenues building up over an extended period, and, as such, have little impact upon 2018 in terms of revenue or profit. These contracts underpin our long-term growth prospects.

## Working capital

	Rolling twelve months to June 2018 £m	Rolling twelve months to June 2017 £m
Operating profit before amortisation of acquisition intangibles	<b>36.2</b>	41.9
Depreciation and amortisation	<b>8.8</b>	7.6
EBITDA (reported)	<b>45.0</b>	49.5
EBITDA (excluding profit from development projects)	<b>43.4</b>	49.5
Cash inflow from operating activities	<b>27.4</b>	34.9
Working capital outflow relating to housing development	<b>8.9</b>	0.6
Cash inflow from operating activities, excluding housing development	<b>36.3</b>	35.5
EBITDA to cash conversion	<b>84%</b>	72%
Average daily net debt (operating)	<b>102.1</b>	85.0
Average daily net debt (property acquisition facility)	<b>12.3</b>	—
Total average daily net debt	<b>114.4</b>	85.0
Net debt (operating) at 30 June	<b>44.5</b>	19.6
Net debt (property acquisition facility) at 30 June	<b>30.0</b>	—
Total net debt at 30 June	<b>74.5</b>	19.6

Mears has a strong track record over many years of converting its profits to cash. Similarly, over that time the Group has maintained a disciplined approach to debt, seeking to keep gearing at conservative levels whilst also looking to minimise capital expenditure. The Group's core principles in this regard have not changed.

The business has experienced a period of significant evolution. Accordingly, Mears has endeavoured to participate in a number of emerging opportunities and, as a result, has at times needed to show a higher appetite for debt funding, particularly in the short term.



*Our strategic priorities  
are the building blocks  
of our business*

Previously, the Group has highlighted an innovative homelessness solution where the Group acquires units from the private sector and makes them available to our Housing clients at an affordable rent. This replaces their expensive and lower quality temporary housing solutions. The Group has completed two material contracts in this area with the London Borough of Bromley and LBWF respectively, in each case introducing a long-term funding partner into the arrangement. Mears' role is to source, negotiate and buy each property on behalf of the client. All acquired properties are refurbished to the Decency Standard and Mears manages the ongoing tenancy and property maintenance. In late 2017, the Group announced that it had secured a £30m property acquisition facility to provide short-term bridging finance where properties become available at short notice and the necessary timetable for the transaction cannot be matched by the funding partner. An excellent example of this is LBWF, where the contract terms were agreed in January 2018 but legal completion will not take place until August 2018. The availability of this bridging funding has allowed over 50 units to be purchased to date. Whilst the primary driver for having the property acquisition facility is to enable new opportunities, it also provides some additional margin opportunity for the Group. The balance drawn at 30 June 2018 was £30m (2017: £nil). The properties owned by the Group at 30 June 2018 had a value of £30.9m (2017: £nil) and are disclosed separately on the face of the balance sheet as 'Assets classified as held for sale'. It is anticipated that the majority of these assets will be sold and the associated funding repaid over the next six weeks.

The Board is mindful that mixed views have been expressed from investors and other stakeholders in respect of the property acquisition facility. The facility has been helpful in gaining early traction on a number of client opportunities and has allowed Mears to drive opportunities harder rather than simply waiting for work to emerge. Mears is not a speculative purchaser of properties – the units that are being acquired have a clear exit route with a predetermined exit value. The risk to Mears is low but the Board is mindful of the temporary impact that this facility has on the Group's overall gearing.

As the business has continued to evolve, it is finding alternative funding solutions that may reduce the Group's requirement to use its own balance sheet. The Group will continue to look to identify funding partners that have a range of quantum and risk profiles which can provide solutions for the different opportunities that the Group is developing.

The Mears business has changed to reflect the requirements of its clients. The significant shortage of suitable housing has become our clients' key challenge and the Mears solution has moved away from providing traditional maintenance as a singular component towards providing a full asset management service. An important part of this broader offering is an ability for Mears to build new homes as part of its homelessness solution for clients. Mears has developed this in-house capability in a controlled manner over the last five years. Mears' preferred route is to engage with clients on a contracting basis which removes any requirement for the Group to provide funding. However, a number of the placemaking opportunities require Mears to take the lead, and those opportunities typically require the Group to share the funding with its Registered Provider partner. As at 30 June 2018, the working capital invested in housing development amounted to £13.7m (2017: £4.8m) which is in line with the capital planned to be allocated to this new area several years ago. The peak cash commitment is expected to reduce from this level before the year end. In order to better understand the underlying cash performance of the business, the outflow of £8.9m (2017: £0.6m) absorbed in Housing development is excluded from the headline cash conversion metric.

Average daily net debt (operating) increased to £102.1m (2017: £85.0m), which was slightly better than expected at the half-year stage. In addition to the additional £8.9m working capital absorbed within housing development activities and set out above, the Group has incurred cash outflows of £9.3m relating to the discontinued UAE activities and £11.2m in respect of deferred consideration relating to previous acquisitions. All deferred consideration is now settled. Over the medium term, management anticipate seeing average net debt reduce from the current level and return to a more conservative multiple of one to two x to EBITDA.

## Business review continued

### New accounting standards

There have been two significant mandatory accounting changes which apply from 1 January 2018 – the adoption of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments'. In addition, the impact of IFRS 16 'Leases', which is effective on 1 January 2019, is also being determined by the Group.

#### IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 changes the timing of recognising revenue and costs in respect of certain long-term contracts. In the case of the large majority of our contracts, the accounting methodology will be unchanged. Mears has typically looked to recognise revenue and cost at the individual works order level, whether that be a singular maintenance order or care visit. This has ensured that the valuation of working capital balances is straightforward and contains fewer areas of significant judgement.

However, there are a small number of arrangements where the Group has accounted for multiple service contracts by treating them as a single supply of a service. This occurs where local contract mechanics were not easily aligned with the commercial framework of the contract. The new accounting standard requires Mears to allocate the total transaction price to each distinct performance obligation. In addition, a number of contracts include variable consideration, where revenue and profit are linked to the achievement of performance targets and milestones. The new standard requires more detailed analysis in determining the appropriate timing of recognising this revenue.

IFRS 15 has been applied using the modified retrospective approach on transition which results in an adjustment to the opening balance of equity at 1 January 2018 and no restatement of the prior period. The impact of this change in 2018 will see a reduction in the opening balance of equity of £23.9m. The change to IFRS 15 has no impact on the lifetime profitability of the contracts and there are no cash flow impacts, although the change will drive better alignment between the timing of profit recognition and its associated cash flow. Moving forward, it is expected to have a positive impact in respect of operating profit from 2018 through to 2027, as performance obligations are satisfied. The impact of this standard has been to increase the operating result for the first half of 2018 by £0.65m.

#### IFRS 9 'Financial Instruments'

In respect of IFRS 9, Mears does not hold complex financial instruments and the impact of this standard on its hedging instruments is not material. However, included within financial assets are trade and other receivables. From 1 January 2018, Mears is required to recognise a loss allowance for expected credit losses on these financial assets. The new standard states that if the credit risk on a financial instrument has significantly increased since initial recognition, the loss allowance must be measured using the lifetime expected credit loss.

Given the significant majority of our invoicing is to public sector clients, assessed to have a very low credit risk, expected credit losses to this customer type are deemed to be negligible. However, Mears provides regulated services to private individuals in both its Housing and Care businesses and, as such, services cannot immediately be withdrawn when the Group becomes aware of an increased credit risk. Mears has both a moral and legal obligation to continue to provide services whilst alternative arrangements are being made for these service users.

The difference between the previous carrying amount and the carrying amount at the beginning of the reporting period under IFRS 9 is recognised as an adjustment to the opening balance of equity. The impact of this change at 1 January 2018 is a reduction in the opening balance of equity of £1.7m.

#### IFRS 16 'Leases'

The Group has reviewed the impact of IFRS 16 'Leases', which becomes mandatory for accounting periods starting on 1 January 2019. The new standard aligns the treatment of operating leases and finance leases and will require Mears to recognise leases on the balance sheet which will reflect the right to use an asset for a period of time, together with its associated lease liability. Mears currently has operating leases in respect of 3,200 vehicles (with an average lease term of 4.5 years) and 5,000 properties (with an average lease term of 2.5 years) that are within scope of IFRS 16: therefore this is a significant change. The Board estimates that the balance sheet impact will increase assets and liabilities in the range of £90.0m to £120.0m, which is in line with previous indications. However, this estimate is sensitive to the timing of lease renewals and the continued organic growth within the housing management business. In terms of the income statement, EBITDA will increase by around £32.0 to £42.0m but it is expected to have a neutral impact at a PBT level given that the reduction in administrative expenses is expected to broadly match the increase in amortisation and financing costs.

IFRS 16 will affect a large number of commonly used financial ratios and performance metrics including gearing, interest cover, EBITDA, EBIT, operating profit and ROCE. The Group's banking covenants will not be affected by this accounting change as these are 'frozen' and are based on accounting standards at the time the facility agreements came into force. The Group's bank facility runs to 2022 which provides ample time for the banking community to properly digest the impact of IFRS 16 on its performance metrics.

### Corporate governance and risk management

The Board sets itself high standards of corporate governance. Our Corporate Governance Report, issued within our Annual Report, details how the Group approaches governance and the areas of focus for the Board in 2018 and into the future.

In recent years, the Board has evolved steadily, matching its skills and expertise to the strategic development of the Group and its key operating markets along with the requirement for good corporate governance. As a result of this, three new Non-Executive Directors Roy Irwin, Jason Burt and Elizabeth Corrado, have been appointed since June 2017, bringing valuable relevant sector experience and knowledge to the Board. As announced previously on 6 July 2018, as part of this ongoing Board evolution, Mears' Chairman, Bob Holt, has indicated that he does not wish to stand for re-election at the 2019 Annual General Meeting. The Board expects to have identified a new Chairman by the end of October and it will keep shareholders updated as the process progresses.

During the period, the Board was delighted to announce the appointment of Amanda Hillerby as an Employee Director following her election at the AGM. Amanda has worked for the Group since 2011, commencing her career on the Group's graduate management programme, during which she worked across all areas of the business including Care, Housing and central support. Amanda is currently delivering a national role of Quality Manager within the Care division. Mears is one of the first listed companies to take this bold step and the Board firmly believes that better employee representation can improve the quality of decision making. The benefits of listening to employees and engaging them in both consultation and decision making are already widely recognised. This appointment will assist the Board in receiving full, open and honest representations from its workforce on how strategic initiatives are implemented, and will provide the workforce.

### Social value

Mears' commitment to the communities where it works was again reflected by our branches supporting 315 different projects and generating a social value of £11.5m in the first half of 2018. Mears is now supporting 780 apprentices across the Group, creating opportunities for skills development across an increasingly wide range of disciplines.

The Group is working hard to encourage more women to consider housing as a career and to become future leaders in the business. Given this objective, it was pleasing to see Mears recognised with two awards at the National Diversity in Housing Awards. One award was for gender equality and one for having the best diversity scheme.

### Outlook

I commend our employees for their continued commitment and energy and the enormous part they have played in making Mears the business that it is. We have delivered solid performance in the first half of 2018 and our financial and market position remains strong, as we seek to build on existing strengths and take advantage of new opportunities.

The Group is very well positioned to continue to provide innovative solutions to address the increasingly complex challenges we face. We will continue to play a leading role in shaping both our core markets, underpinned by our dedication to providing our clients with a first-class service.

The Board remains confident of delivering its expectations for the full year.

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# Half-year condensed consolidated income statement

For the six months ended 30 June 2018

	Note	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000	Year ended 31 December 2017 £'000
<b>Sales revenue</b>	3	<b>435,257</b>	470,782	900,184
Cost of sales		<b>(333,924)</b>	(356,085)	(676,482)
<b>Gross profit</b>		<b>101,333</b>	114,697	223,702
Other administration expenses		<b>(80,866)</b>	(95,269)	(184,551)
<b>Operating result before amortisation of acquisition intangibles and exceptional costs</b>		<b>20,467</b>	19,428	39,151
Exceptional costs		<b>(3,975)</b>	—	—
Amortisation of acquisition intangibles		<b>(2,159)</b>	(5,550)	(10,638)
<b>Total administration expenses</b>		<b>(87,000)</b>	(100,819)	(195,189)
<b>Operating profit</b>	3	<b>14,333</b>	13,878	28,513
Net finance charge	5	<b>(1,478)</b>	(1,148)	(2,029)
Profit for the period before tax, amortisation of acquisition intangibles and exceptional costs		<b>18,989</b>	18,280	37,122
<b>Profit for the period before tax</b>		<b>12,855</b>	12,730	26,484
Tax expense	6	<b>(2,044)</b>	(1,991)	(4,315)
<b>Profit for the period from continuing operations</b>		<b>10,811</b>	10,739	22,169
<b>Discontinued operations</b>				
Exceptional loss from discontinued operations		—	—	(16,500)
Tax income from discontinued operations		—	—	3,176
<b>Loss for the period after tax from discontinued operations</b>		—	—	(13,324)
<b>Profit for the period from continuing and discontinued operations</b>		<b>10,811</b>	10,739	8,845
<b>Attributable to:</b>				
Equity holders of the Company		<b>10,864</b>	10,173	7,582
Non-controlling interests		<b>(53)</b>	566	1,263
Profit for the period		<b>10,811</b>	10,739	8,845
<b>Earnings per share</b>				
Basic	8	<b>10.49p</b>	9.90p	7.35p
Diluted	8	<b>10.44p</b>	9.86p	7.29p

# Half-year condensed consolidated statement of comprehensive income

For the six months ended 30 June 2018

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000	Year ended 31 December 2017 £'000
<b>Net result for the period</b>	<b>10,811</b>	10,739	8,845
Other comprehensive income for the period			
Which will be subsequently reclassified to the income statement:			
Cash flow hedges:			
– gains/(losses) arising in the period	<b>3</b>	124	(54)
– reclassification to the income statement	<b>244</b>	310	645
Decrease in deferred tax asset in respect of cash flow hedges	<b>(35)</b>	(97)	(143)
Which will not be subsequently reclassified to the income statement:			
Actuarial gain on defined benefit pension scheme	—	—	13,879
Decrease in deferred tax asset in respect of defined benefit pension schemes	—	—	(2,637)
Other comprehensive income for the period	<b>212</b>	337	11,690
Total comprehensive income for the period	<b>11,023</b>	11,076	20,535
<b>Attributable to:</b>			
Equity holders of the Parent	<b>11,076</b>	10,510	19,272
Non-controlling interests	<b>(53)</b>	566	1,263
Total comprehensive income for the period	<b>11,023</b>	11,076	20,535

# Half-year condensed consolidated balance sheet

As at 30 June 2018

	As at 30 June 2018 £'000	As at 30 June 2017 £'000	As at 31 December 2017 £'000
Note			
<b>Assets</b>			
<b>Non-current</b>			
Goodwill	193,642	193,712	193,642
Intangible assets	15,102	21,280	17,266
Property, plant and equipment	24,405	20,993	22,037
Pensions and other employee benefits	27,308	15,992	27,308
Deferred tax asset	8,188	5,704	4,314
	<b>268,645</b>	257,681	264,567
<b>Current</b>			
Assets classified as held for sale	30,886	—	13,941
Inventories	26,810	10,552	18,705
Trade and other receivables	132,300	167,525	153,912
Current tax assets	—	—	111
Cash at bank and in hand	75,495	75,367	24,770
	<b>265,491</b>	253,444	211,439
<b>Total assets</b>	<b>534,136</b>	511,125	476,006
<b>Equity</b>			
<b>Equity attributable to the shareholders of Mears Group PLC</b>			
Called up share capital	10 1,036	1,030	1,036
Share premium account	60,339	58,504	60,204
Share-based payment reserve	1,844	2,375	1,469
Hedging reserve	(114)	(437)	(326)
Merger reserve	46,214	46,214	46,214
Retained earnings	77,260	94,077	100,897
<b>Total equity attributable to the shareholders of Mears Group PLC</b>	<b>186,579</b>	201,763	209,494
Non-controlling interest	(529)	(76)	96
<b>Total equity</b>	<b>186,050</b>	201,687	209,590
<b>Liabilities</b>			
<b>Non-current</b>			
Long-term borrowing and overdrafts	70,000	95,000	50,559
Pensions and other employee benefits	4,966	7,498	4,966
Deferred tax liabilities	6,688	6,259	7,098
Financing liabilities	22	149	79
Other liabilities	5,036	5,078	5,036
	<b>86,712</b>	113,984	67,738
<b>Current</b>			
Borrowings related to assets classified as held for sale	30,000	—	13,941
Short-term borrowings and overdrafts	50,000	—	—
Trade and other payables	171,305	182,449	184,484
Financing liabilities	126	481	253
Current tax liabilities	1,083	3,873	—
Dividend payable	8,860	8,651	—
	<b>261,374</b>	195,454	198,678
<b>Total liabilities</b>	<b>348,086</b>	309,438	266,416
<b>Total equity and liabilities</b>	<b>534,136</b>	511,125	476,006

# Half-year condensed consolidated cash flow statement

For the six months ended 30 June 2018

	Six months ended 30 June 2018 £'000	Last twelve months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000	Year ended 31 December 2017 £'000
<b>Operating activities</b>				
Profit for the period before tax	12,855	26,609	12,730	26,484
Adjustments	8,329	18,632	10,846	21,148
Change in inventories and operating receivables	(17,490)	(16,454)	(8,617)	(7,580)
Change in operating payables	(344)	(1,433)	(10,292)	(11,381)
Cash inflow from continuing operating activities before taxes paid	3,350	27,354	4,667	28,671
Net cash outflow from operating activities of discontinued operations	(950)	(9,259)	(1,045)	(9,354)
Taxes received/(paid)	846	(2,307)	(622)	(3,776)
Net cash inflow from operating activities	3,246	15,788	3,000	15,541
<b>Investing activities</b>				
Additions to property, plant and equipment	(5,069)	(8,444)	(2,197)	(5,572)
Additions to other intangible assets	(1,308)	(3,419)	(1,551)	(3,661)
Proceeds from disposals of property, plant and equipment	1	205	—	204
Acquisition of property for resale	(16,944)	(30,886)	—	(13,941)
Acquisition of subsidiary undertaking, net of cash	(11,163)	(11,163)	(5,000)	(5,000)
Sale of subsidiary undertaking	—	1,582	—	1,582
Net cash disposed of with subsidiary	(26)	(1,260)	—	(1,234)
Loans made to other Group entities (non-controlled)	(1,006)	(1,243)	(252)	(232)
Receipts from other Group entities (non-controlled)	—	257	—	—
Interest received	17	355	14	351
Net cash outflow from investing activities	(35,498)	(54,016)	(8,986)	(27,503)
<b>Financing activities</b>				
Proceeds from share issue	135	1,841	188	1,894
Receipts from borrowings related to assets classified as held for sale	16,059	30,000	—	13,941
Finance lease payments	(435)	(2,098)	(291)	(1,954)
Interest paid	(1,673)	(3,093)	(1,170)	(2,591)
Dividends paid – Mears Group PLC shareholders	—	(12,219)	—	(12,218)
Dividends paid – non-controlling interests	(550)	(1,075)	—	(525)
Net cash inflow/(outflow) from financing activities	13,536	13,356	(1,273)	(1,453)
Cash and cash equivalents at beginning of period	(25,789)	(19,633)	(12,374)	(12,374)
Net decrease in cash and cash equivalents	(18,716)	(24,872)	(7,259)	(13,415)
<b>Cash and cash equivalents at end of period</b>	<b>(44,505)</b>	<b>(44,505)</b>	<b>(19,633)</b>	<b>(25,789)</b>
<b>Cash and cash equivalents is comprised as follows:</b>				
– cash at bank and in hand	75,495	75,495	75,367	24,770
– borrowings and overdrafts	(120,000)	(120,000)	(95,000)	(50,559)
<b>Cash and cash equivalents</b>	<b>(44,505)</b>	<b>(44,505)</b>	<b>(19,633)</b>	<b>(25,789)</b>

# Half-year condensed consolidated statement of changes in equity

For the six months ended 30 June 2018

	Attributable to equity shareholders of the Company							Non-controlling interests £'000	Total equity £'000
	Called up share capital £'000	Share premium account £'000	Share-based payment reserve £'000	Hedging reserve £'000	Merger reserve £'000	Retained earnings £'000			
At 1 January 2017	1,026	58,320	1,975	(774)	46,214	92,555	(642)	198,674	
Net result for the period	—	—	—	—	—	10,173	566	10,739	
Other comprehensive income	—	—	—	337	—	—	—	337	
Total comprehensive income for the period	—	—	—	337	—	10,173	566	11,076	
Issue of shares	4	184	—	—	—	—	—	188	
Share option charges	—	—	400	—	—	—	—	400	
Dividends	—	—	—	—	—	(8,651)	—	(8,651)	
At 30 June 2017	1,030	58,504	2,375	(437)	46,214	94,077	(76)	201,687	
At 1 January 2018	1,036	60,204	1,469	(326)	46,214	100,897	96	209,590	
Impact of change in accounting policies*	—	—	—	—	—	(25,641)	—	(25,641)	
Adjusted balance at 1 January 2018	1,036	60,204	1,469	(326)	46,214	75,256	96	183,949	
Net result for the period	—	—	—	—	—	10,864	(53)	10,811	
Other comprehensive income	—	—	—	212	—	—	—	212	
<b>Total comprehensive income for the period</b>	—	—	—	212	—	10,864	(53)	11,023	
Issue of shares	—	135	—	—	—	—	—	135	
Share option charges	—	—	375	—	—	—	—	375	
Changes in non-controlling interests	—	—	—	—	—	—	(22)	(22)	
Dividends	—	—	—	—	—	(8,860)	(550)	(9,410)	
<b>At 30 June 2018</b>	<b>1,036</b>	<b>60,339</b>	<b>1,844</b>	<b>(114)</b>	<b>46,214</b>	<b>77,260</b>	<b>(529)</b>	<b>186,050</b>	

\* The Group has applied IFRS 15 using the modified retrospective approach on transition and IFRS 9 in accordance with IFRS 9 paragraph 7.2.15. Under these methods, the comparative information is not restated (see note 4).

# Notes to the half-year condensed consolidated statements

For the six months ended 30 June 2018

## 1. Corporate information

Mears Group PLC is a public limited company incorporated in England and Wales whose shares are publicly traded. The half-year condensed consolidated financial statements of the Company and its subsidiaries for the six months ended 30 June 2018 were authorised for issue in accordance with a resolution of the Directors on 13 August 2018.

## 2. Basis of preparation and accounting principles

### (a) Basis of preparation

The half-year condensed consolidated financial statements for the six months ended 30 June 2018 have been prepared in accordance with the Disclosure and Transparency Rules (DTR) of the Financial Conduct Authority and with IAS 34 'Interim Financial Reporting'. The half-year condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements and should be read in conjunction with the Group's annual financial statements as at 31 December 2017, which have been prepared in accordance with IFRS as adopted by the European Union.

This half-year condensed consolidated financial information does not comprise statutory accounts within the meaning of Section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2017 were approved by the Board of Directors on 19 March 2018. Those accounts, which contained an unqualified audit report under Section 495 of the Companies Act 2006 and which did not make any statements under Section 498 of the Companies Act 2006, have been delivered to the Registrar of Companies in accordance with Section 441 of the Companies Act 2006.

The half-year condensed consolidated financial statements for the six months ended 30 June 2018 have not been audited or reviewed by an auditor pursuant to the Auditing Practices Board guidance on the Review of Interim Financial Information.

There have been no significant changes to estimates of amounts reported in prior financial years.

After reviewing the Group's performance against budget for the current financial year, and longer-term plans, the Directors consider that at the date of approving this half-year statement, it is appropriate to adopt the going concern basis in its preparation.

### (b) Significant accounting policies

The accounting policies adopted in the preparation of the half-year condensed consolidated financial statements are consistent with those followed in the preparation of the Group's annual financial statements for the year ended 31 December 2017, except for the application of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments'.

#### **IFRS 15 'Revenue from Contracts with Customers'**

IFRS 15 replaces the previous measurement standard IAS 18 'Revenue' and IAS 11 'Construction Contracts'. IFRS 15 has been applied using the modified retrospective approach on transition which results in an adjustment to the opening balance of equity at 1 January 2018 and no restatement of the prior period. The scope of the transitional adjustment is all contracts with customers which span the 1 January 2018 transition date. For the comparative period, the financial statements are reported under the aforementioned accounting standards, IAS 18 and IAS 11.

IFRS 15 provides a single, principles-based five-step model to be applied to all sales contracts as outlined below. It is based on the transfer of control of goods and services to customers and replaces the separate models for goods, services and construction assets. The below sets out the principal types of contract and how the revenue is recognised in accordance with IFRS 15.

The Group's contract portfolio has been assessed by operating segment. The contracts with customers in Housing have a wide variation of and goods and services being provided to customers with differing performance obligations and levels of complexity. Within Housing, IFRS 15 does not apply to lease contracts within the scope of IAS 17 'Leases'. In Care, there is a single performance obligation within all contracts and the segment follows a single revenue recognition methodology.

## 2. Basis of preparation and accounting principles continued

### (b) Significant accounting policies continued

#### *IFRS 15 continued*

#### **Revenue – Housing**

##### *Schedule of rates (SOR) contracts*

Each works order is completed at a point in time, when the job is operationally complete, which is the point at which the customer benefits from work done. Each job is priced using a fixed pricing schedule, which allows each job to be identified and valued. This pricing schedule is referred to as the SOR which determines the transaction price.

Each work order represents a performance obligation which is assessed individually to determine the point at which the value of the good or service has been transferred to the customer, at which time the value of that work order is recognised in revenue. For part completed works, the direct cost incurred that are explicitly chargeable to the customer under the contract are capitalised and released as performance obligations are satisfied.

##### *Lump sum contracts*

Lump sum contracts may involve delivering a range of goods and services; however, there is a single fixed lump sum payment per period which represents the transaction price.

The obligation within a lump sum contract is deemed to be being available to deliver the goods and services in the scope of the contract, not the actual performance of the individual works orders themselves. Therefore revenue will be recognised on a straight-line basis as performance obligations are being met over time.

##### *Contracting*

For contracting projects, the contract states the scope and specification of the construction works to be carried out, for a fixed price. Mears is continuously satisfying this single performance obligation as cost is incurred, determining progress against the performance obligation on an input basis. The customer simultaneously receives the benefits of all direct costs incurred on site and therefore revenue is recognised over time. An assessment is made of construction costs incurred to date and the costs required to complete the project. If a project is not deemed to be profitable, the expected full loss is recognised immediately.

##### *Variable consideration*

The Group's Housing revenue includes elements of variable consideration. Where there is uncertainty in the measurement of variable consideration, at both the start of the contract and subsequently, management will consider the facts and circumstances of the contract in determining either the most likely amount of variable consideration when the outcome is binary, or the expected value based on a range of possible considerations. Included within this assessment will be the extent to which there is a high probability that a significant reversal in variable consideration revenues will not occur once the uncertainty is subsequently resolved.

##### *Rental income*

Where the Group is acting as principal, lessor operating lease revenue is recognised in Revenue on a straight-line basis over the tenancy in accordance with IAS 17 'Leases', which will be replaced by IFRS 16 'Leases' from 1 January 2019.

Where the Group is providing a management service, Mears recognises revenue as an agent (the net management fee) on a straight-line basis where significant initial costs are required to make good the housing to perform housing management activities, the costs directly attributable to the initial upgrade will be recognised as costs incurred to fulfil a contract and held within current assets, to the extent that it is determined that costs are recoverable.

## **2. Basis of preparation and accounting principles continued**

### **(b) Significant accounting policies continued**

#### ***IFRS 15 continued***

##### **Revenue – Care**

The stand-alone selling prices for providing care are overtly stated in the contract, and the method of application of the rate of charge is on a unit of time basis, usually expressed as a rate per visit. Revenue will be recognised in respect of this single performance obligation by reference to the chargeable rate and time for completed care visits in the period.

From time to time, care contracts with customers include a fixed fee per period for performing a consistent scope of care. For these contract types, the revenue recognition is consistent with lump sum contracts above.

There is a shift towards rewarding providers of care on the basis of achievement of specific outputs achieved and moving away from the traditional input-based per hour measurement. Care outputs are either achieved or not achieved and are determined by service user. Revenue will be recognised when the specific performance obligation has been satisfied.

##### ***Significant judgements in the application of this standard***

Previously IAS 18 'Revenue' and IAS 11 'Construction Contracts' allowed contracts with a variety of services to be combined in certain circumstances in determining the percentage of completion of those multi-service contracts. Disaggregating these contracts to determine the satisfaction of performance obligations, as detailed above, significantly changes the timing of revenue recognition. £19.1m of the reduction in the opening balance of equity at 1 January 2018 relates to the disaggregation of contracts previously combined. The total transaction price of these contracts does not change under IFRS 15.

The Group's assessment of variable consideration revenue recognition under IFRS 15 is detailed above. The judgement applied under IFRS 15 more closely aligns timing of revenue recognition with cash inflows where the contractual mechanism contains uncertainty. Previously, the Group utilised expected value calculations in determining the variable consideration revenue to be recognised. £4.8m of the reduction in the opening balance of equity at 1 January 2018 relates to the Group's application of IFRS 15 in relation to variable consideration. The total amount of variable consideration will not change under IFRS 15.

##### ***IFRS 9 'Financial Instruments'***

From 1 January 2018, the assets generated from goods or services 'transferred to customers are now presented as either receivables or contract assets, in accordance with IFRS 15. The assessment of impairment of receivables or contract assets from 1 January 2018 is in accordance with IFRS 9.

All of Mears' cash flows from customers are solely payments of principal and interest, and do not contain a significant financing component. Financial assets generated from all of the Group's revenue streams are therefore initially measured at their transaction price (as defined in IFRS 15) and are subsequently remeasured at amortised cost.

Under IFRS 9, Mears will now recognise a loss allowance for expected credit losses (ECL) on financial assets subsequently measured at amortised cost, using the 'simplified approach'.

## 2. Basis of preparation and accounting principles continued

### (b) Significant accounting policies continued

#### IFRS 9 'Financial Instruments' continued

The Group has concluded that transactions with public bodies (including but not limited to: Local Authorities, Housing Associations and NHS entities) contain only a negligible credit risk and the ECL is deemed to be immaterial. The Group has identified two further customer types which have different credit risk profiles:

Care – private pay service users; barriers to making payment can include physical or mental ailments or disabilities together with a high mortality risk.

Housing – tenants; are typically dependent upon their welfare benefits and they may default on their obligations under their tenancy agreement to pay rent when it falls due.

Mears will utilise the practical expedients within IFRS 9 which allows the use of a provision matrix:

The measurement of ECL will be presented as impairment losses within current assets. This results in an increased gross loss adjustment to trade and other receivables of £2.1m. The total of £1.7m, which is after recognising a deferred tax asset of £0.4m, will be deducted from the opening balance of equity as at 1 January 2018.

## 3. Segment reporting

Segment information is presented in respect of the Group's business segments. Segments are determined by reference to the internal reports reviewed by the chief operating decision maker.

The Group operated two business segments during the period:

- Housing – services within this segment comprise a full housing maintenance and management service predominately to Local Authorities and other Registered Social Landlords; and
- Care – services within this segment comprise personal care services for people in their own homes.

All of the Group's activities are carried out within the UK and the Group's principal reporting to its chief operating decision maker is not segmented by geography.

The principal measures utilised by the chief operating decision maker to review the performance of the operating segments are that of revenue growth and operating margins in both core divisions of Housing and Care. The operating result utilised within the key performance measures is stated before amortisation of acquisition intangibles, exceptional costs and costs relating to long-term incentive plans.

	Six months ended 30 June 2018		Six months ended 30 June 2017	
	Revenue £'000	Operating result £'000	Revenue £'000	Operating result £'000
Housing	374,920	18,983	402,052	20,813
Care	60,337	1,859	68,730	(985)
	<b>435,257</b>	<b>20,842</b>	470,782	19,828
Long-term incentive plans		<b>(375)</b>		(400)
Operating result before intangible amortisation and exceptional costs		<b>20,467</b>		19,428
Exceptional costs		<b>(3,975)</b>		—
Amortisation of acquisition intangibles		<b>(2,159)</b>		(5,550)
Operating profit		<b>14,333</b>		13,878
Net finance costs		<b>(1,478)</b>		(1,148)
Tax expense		<b>(2,044)</b>		(1,991)
Profit for the period		<b>10,811</b>		10,739

## Notes to the half-year condensed consolidated statements continued

For the six months ended 30 June 2018

## 4. Changes in accounting policies

As detailed in note 2, there have been two significant mandatory accounting changes which apply from 1 January 2018: the adoption of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments'. The impact to retained earnings as a result of these changes is detailed below:

	Retained earnings £'000
Retained earnings as previously stated at 31 December 2017	100,897
Impact of restatement on trade and other receivables (IFRS 15)	(29,537)
Impact of restatement on deferred tax asset (IFRS 15)	5,612
Impact of restatement on trade and other receivables (IFRS 9)	(2,119)
Impact of restatement on deferred tax asset (IFRS 9)	403
Retained earnings as restated at 31 December 2017	75,256

The effect of the application of IFRS 15 and IFRS 9 on the six months ended 30 June 2018 is detailed below:

	As would have been reported under old accounting standards £'000	Impact of IFRS 15 £'000	Impact of IFRS 9 £'000	As reported under new accounting standards £'000
<b>Income statement for the six months ended 30 June 2018</b>				
Sales revenue	434,607	650	—	435,257
Tax expense	63	(2,107)	—	(2,044)
<b>Balance sheet as at 30 June 2018</b>				
Deferred tax asset	4,279	3,506	403	8,188
Trade and other receivables	163,306	(28,887)	(2,119)	132,300
Retained earnings	104,207	(25,381)	(1,716)	77,110

The change to IFRS 15 has no impact on the lifetime profitability of the contracts and there are no cash flow impacts. The impact of this standard has been to increase the operating result for the first half of 2018 by £0.7m. Moving forward, it is expected to have a positive impact in respect of operating profit as performance obligations are met.

The change to IFRS 9 had no impact on the operating result for the first half of 2018. Moving forward, this new standard is likely to result in an earlier recognition of credit loss, resulting in an impairment in trade receivables and contract assets. Based upon the current activities of the Group, it is unlikely that this impairment would be material in any single year.

## 5. Net finance charge

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
Interest charge on overdrafts and short-term loans	(1,393)	(957)
Interest charge on interest rate swap (effective hedges)	(244)	(310)
Interest charge on defined benefit obligation	(100)	(105)
<b>Finance costs</b>	<b>(1,737)</b>	<b>(1,372)</b>
Interest income resulting from short-term bank deposits	9	14
Interest income resulting from defined benefit obligation	250	210
<b>Net finance charge</b>	<b>(1,478)</b>	<b>(1,148)</b>

## 6. Tax expense

The tax charge for the six months ended 30 June 2018 has been based on the estimated tax rate for the full year.

Tax recognised in the income statement:

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
United Kingdom corporation tax and total current tax recognised in the income statement	348	2,949
Adjustment in respect of previous periods	—	—
Total current tax recognised in the income statement	348	2,949
Total deferred tax recognised in the income statement	1,696	(958)
Total tax expense recognised in the income statement	2,044	1,991

## 7. Dividends

The interim dividend of 3.55p (2017: 3.45p) per share is not recognised as a liability at 30 June 2018 and will be payable on 8 November 2018 to shareholders on the Register of Members at the close of business on 19 October 2018.

The dividend disclosed within the half-year condensed consolidated statement of changes in equity represents the final dividend of 8.55p (2017: 8.40p) per share proposed in the 31 December 2017 financial statements and approved at the Group's Annual General Meeting on 7 June 2018 (not recognised as a liability at 31 December 2017).

## Notes to the half-year condensed consolidated statements continued

For the six months ended 30 June 2018

## 8. Earnings per share

	Basic		Diluted	
	Six months ended 30 June 2018 p	Six months ended 30 June 2017 p	Six months ended 30 June 2018 p	Six months ended 30 June 2017 p
Earnings per share	<b>10.49</b>	9.90	<b>10.44</b>	9.86
Effect of amortisation of acquisition intangibles	<b>2.08</b>	5.40	<b>2.08</b>	5.38
Effect of exceptional costs (including tax impact)	<b>3.17</b>	—	<b>3.15</b>	—
Effect of full tax adjustment	<b>(0.64)</b>	(1.26)	<b>(0.63)</b>	(1.26)
Normalised earnings per share	<b>15.10</b>	14.04	<b>15.04</b>	13.98

A normalised earnings per share (EPS) is disclosed in order to show performance undistorted by amortisation of intangibles and adjusted to reflect a full tax charge. The Directors believe that this normalised measure better allows the assessment of operational performance, the analysis of trends over time, the comparison of different businesses and the projection of future performance. The profit attributable to shareholders before and after adjustments for both basic and diluted EPS is:

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
Profit attributable to shareholders:	<b>10,864</b>	10,173
– amortisation of acquisition intangibles	<b>2,159</b>	5,550
– exceptional costs (including tax impact)	<b>3,278</b>	—
– full tax adjustment	<b>(659)</b>	(1,299)
Normalised earnings	<b>15,642</b>	14,424

The calculation of EPS is based on a weighted average of ordinary shares in issue during the year. The diluted EPS is based on a weighted average of ordinary shares calculated in accordance with IAS 33 'Earnings Per Share', which assumes that all dilutive options will be exercised. The additional normalised basic and diluted EPS use the same weighted average number of shares as the basic and diluted EPS.

	Six months ended 30 June 2018 Millions	Six months ended 30 June 2017 Millions
Weighted average number of shares in issue:	<b>103.60</b>	102.80
– dilutive effect of share options	<b>0.40</b>	0.40
Weighted average number of shares for calculating diluted earnings per share	<b>104.00</b>	103.20

## 9. Fair value measurement of financial instruments

IAS 34 requires that interim financial statements include certain of the disclosures about fair value of financial instruments set out in IFRS 13 and IFRS 7. These disclosures include the classification of fair values within a three-level hierarchy. The three levels are defined, based on the observability of significant inputs to the measurement, as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3: unobservable inputs for the asset or liability.

The following table shows the levels within the hierarchy of financial assets and liabilities measured at fair value on a recurring basis at 30 June 2018, 31 December 2017 and 30 June 2017:

	As at 30 June 2018 £'000	As at 30 June 2017 £'000	As at 31 December 2017 £'000
<b>Financial assets</b>			
<b>Loans and receivables</b>			
Trade receivables	42,651	54,243	51,602
Amounts recoverable on contracts	73,661	97,650	88,948
Cash at bank and in hand	75,495	75,367	24,770
	<b>191,807</b>	227,260	165,320
<b>Financial liabilities</b>			
<b>Fair value (Level 2)</b>			
Interest rate swaps – effective	(148)	(630)	(332)
<b>Fair value (Level 3)</b>			
Contingent consideration in respect of acquisitions	—	(11,457)	(11,163)
<b>Amortised cost</b>			
Borrowings related to assets held for sale	(30,000)	—	(13,941)
Bank borrowings and overdrafts	(120,000)	(95,000)	(50,559)
Trade payables	(109,847)	(110,865)	(103,432)
Other creditors	(5,737)	(5,564)	(9,965)
	<b>(265,732)</b>	(223,516)	(189,352)
	<b>(73,925)</b>	3,744	(24,072)

The fair values of interest rate swaps and forward commodity contracts have been calculated by a third party expert discounting estimated future cash flows on the basis of market expectations of future interest rates (Level 2).

The fair values of deferred and contingent consideration have been calculated by the Directors by reference to expected future income and expenditure in respect of the acquired businesses.

There were no transfers between Level 1 and Level 2 during the six-month period to 30 June 2018 or the year to 31 December 2017.

## Notes to the half-year condensed consolidated statements continued

For the six months ended 30 June 2018

## 9. Fair value measurement of financial instruments continued

The reconciliation of the carrying values of financial instruments classified within Level 3 is as follows:

	As at 30 June 2018 £'000	As at 30 June 2017 £'000	As at 31 December 2017 £'000
Balance, beginning of period	11,163	16,457	16,457
Paid in respect of acquisitions	(11,163)	(5,000)	(5,000)
Released on reassessment	—	—	(294)
Balance, end of period	—	11,457	11,163

Contingent consideration represents an estimate of future consideration likely to be payable in respect of acquisitions. Contingent consideration is discounted for the likelihood of payment and for the time value of money. Contingent consideration becomes payable based upon the profitability of acquired businesses.

The carrying value of the following financial assets and liabilities is considered a reasonable approximation of fair value:

- trade and other receivables;
- cash and cash equivalents; and
- trade and other payables.

## 10. Share capital

	As at 30 June 2018 £'000	As at 30 June 2017 £'000	As at 31 December 2017 £'000
Allotted, called up and fully paid			
At 1 January 103,567,091 (2017: 102,559,799) ordinary shares of 1p each	1,036	1,026	1,026
Issue of 54,485 (2017: 431,768) ordinary shares of 1p each on exercise of share options	—	4	10
<b>At 30 June 103,621,576 (2017: 102,991,567) ordinary shares of 1p each</b>	<b>1,036</b>	<b>1,030</b>	<b>1,036</b>

54,485 (2017: 431,768) ordinary 1p shares were issued in respect of share options exercised. The difference between the nominal value and the total consideration of £0.1m has been credited to the share premium account.

## 11. Notes to the half-year condensed consolidated cash flow statement

The following non-operating cash flow adjustments have been made to the pre-tax result for the period:

	Six months ended 30 June 2018 £'000	Last twelve months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
Depreciation	2,832	6,267	2,670
Loss on disposal of property, plant and equipment	23	47	—
Profit on disposal of subsidiary	—	(961)	—
Intangible amortisation	3,472	9,717	6,523
Share-based payment charges	375	801	400
IAS 19 pension movement	—	31	—
Net finance charge	1,627	2,730	1,253
Total	8,329	18,632	10,846

## 12. Half-year condensed consolidated financial statements

Further copies of the Interim Report are available from the registered office of Mears Group PLC at 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH or [www.mearsgroup.co.uk](http://www.mearsgroup.co.uk).

## 13. Principal risks and uncertainties

The nature of the principal risks and uncertainties faced by the Group has not changed significantly from those set out on pages 25 and 26 of the 2017 Annual Report and Accounts and is not expected to change over the next six months. The four principal risks identified are: reputation, people, health and safety, and IT and data.

## 14. Forward-looking statements

This report contains certain forward-looking statements with respect to the financial condition, results of operations and businesses of Mears Group PLC. These statements involve risk and uncertainty because they relate to events and depend upon circumstances that will occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements.

The Directors confirm, to the best of their knowledge, that this condensed set of financial statements has been prepared in accordance with IAS 34 as adopted by the European Union and that the interim report includes a fair review of the information required by Rules 4.2.4, 4.2.7 and 4.2.8 of the Disclosure and Transparency Rules of the UK Financial Conduct Authority.

The names and functions of the Directors of Mears Group PLC are as listed in the Group's Annual Report for 2017 with the exception of Peter Dicks, who did not stand for re-election at the Annual General Meeting on 7 June 2018 and Amanda Hillerby, who was appointed at the same meeting.

By order of the Board

### **D J Miles**

**Chief Executive Officer**

[david.miles@mearsgroup.co.uk](mailto:david.miles@mearsgroup.co.uk)

14 August 2018

### **A C M Smith**

**Finance Director**

[andrew.smith@mearsgroup.co.uk](mailto:andrew.smith@mearsgroup.co.uk)

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### Internet

The Group operates a website which can be found at [www.mearsgroup.co.uk](http://www.mearsgroup.co.uk). This site is regularly updated to provide information about the Group. In particular all of the Group's press releases and announcements can be found on the site.

### Registrar

Any enquiries concerning your shareholding should be addressed to the Company's registrar. The registrar should be notified promptly of any change in a shareholder's address or other details.

### Investor relations

Requests for further copies of the Annual Report and Accounts, or other investor relations enquiries, should be addressed to the registered office.

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