# FINANCIAL RESULTS

17 November 2016

## ROYAL MAIL PLC
## RESULTS FOR THE HALF YEAR ENDED 25 SEPTEMBER 2016

Royal Mail plc (RMG.L) today announced its results for the half year ended 25 September 2016.

**Moya Greene, Chief Executive Officer, commenting on the results, said:**

"Our performance was broadly in line with our expectations. Group revenue increased by one per cent on an underlying basis, driven by a good performance from GLS, our continental European parcels business. We delivered UK parcel volume and revenue growth including new contract wins. Addressed letter volume decline was within our forecast range. The recent acquisition of ASM in Spain and GSO in California supports GLS' strategy of targeted and focused geographic expansion.

"We have increased our cost avoidance target from £500 million to £600 million of annualised costs cumulative over the three financial years ending 2017-18. We are targeting to reduce underlying UKPIL operating costs before transformation by up to one per cent in 2016-17, depending on the absorbable rate of change within our organisation. We are past the peak of investment. Net cash investment is expected to be no more than £500 million per annum, compared with an average of £615 million over the past three years.

"As always, our performance for the full year will be dependent on the important Christmas period. Extensive planning, which began in the spring, will help us to manage our busiest time. This includes the recruitment of over 19,000 temporary staff and opening nine temporary parcel sort centres."

**Group financial highlights**

| Adjusted[1] results (£m) | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 | Underlying change[2] |
|---|---|---|---|
| Revenue | **4,583** | 4,395 | 1% |
| Operating profit before transformation costs | **320** | 342 | (5%) |
| Operating profit after transformation costs | **262** | 248 | |
| *Margin* | ***5.7%*** | *5.6%* | *40bps* |
| Profit before tax | **252** | 240 | |
| Earnings per share | **19.2p** | 18.1p | |
| **Reported[3] results (£m)** | | | |
| Operating profit before transformation costs | **206** | 208 | |
| Operating profit after transformation costs | **148** | 114 | |
| Profit before tax (continuing operations) | **110** | 116 | |
| Earnings per share (continuing operations) | **8.6p** | 8.8p | |
| In-year trading cash flow | **116** | 1 | 115 |
| Net debt[4] | **(452)** | (369) | |
| Interim dividend per share | **7.4p** | 7.0p | 0.4p |

**Business performance**

| | Revenue | | | Adjusted operating profit before transformation costs | |
|---|---|---|---|---|---|
| (£m) | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 | Underlying change[2] | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 |
| UKPIL[5] | **3,641** | 3,654 | (1%) | **247** | 290 |
| GLS | **942** | 741 | 9% | **73** | 52 |
| Group | **4,583** | 4,395 | 1% | **320** | 342 |

**Group financial performance**

- Revenue was up one per cent on an underlying basis, with good growth in GLS offsetting the decline in UKPIL revenue.
- Adjusted operating profit before transformation costs was £320 million.
- Adjusted operating profit margin after transformation costs increased by 40 basis points.
- In-year trading cash flow increased to £116 million, reflecting more efficient investment spend.
- In line with our stated interim dividend policy, the Board has declared a dividend of 7.4 pence per share for the half year ended 25 September 2016.

**Business performance**

- UKPIL revenue declined one per cent on an underlying basis. Parcel volumes were up two per cent, driven by growth in Royal Mail account and import parcels. Parcel revenue increased by three per cent.
- Addressed letter volumes declined by four per cent on an underlying basis within our forecast range of a 4-6 per cent decline per annum. Total letter revenue declined by three per cent. Marketing mail revenue was down eight per cent. Uncertainty leading up to and after the EU Referendum led to a reduction in overall UK marketing activity.
- On an underlying basis, total adjusted UKPIL operating costs before transformation costs were flat.
- UKPIL collections, processing and delivery productivity increased by 2.2 per cent, within our target range of a 2.0-3.0 per cent improvement per annum.
- GLS continued to perform well over the period, taking into account the impact of public holidays across Europe. Volumes were up 10 per cent on an underlying basis, benefiting from strong growth in export volumes. Revenue increased by nine per cent, with growth in almost all markets. Operating profit was up 25 per cent on an underlying basis.
- GLS recently acquired ASM in Spain and Golden State Overnight in California, supporting its strategy of targeted and focused geographic expansion.

**Outlook summary**

- The key drivers for the UK letters and parcels markets remain unchanged. Letter volumes, particularly advertising letter volumes, are linked to movements in GDP and we are monitoring developments in the UK economy closely.
- We are now targeting to avoid around £225 million of UKPIL operating costs in 2016-17 and around £600 million of annualised operating costs cumulative over the three financial years ending 2017-18.
- We are now targeting to reduce underlying UKPIL operating costs before transformation costs by up to one per cent in 2016-17. The outcome of our cost performance will be dependent on the absorbable rate of change within our organisation.
- Transformation costs are now expected to be between £130-160 million for 2016-17.
- GLS will remain a focus for investment to help drive growth.
- We are reprofiling our investment spend, which will be lower overall and weighted to growth. We now expect net cash investment to be no more than £500 million per annum going forward, compared with an average over the last three financial years of £615 million.
- We remain very focused on improving our products and services, controlling costs, improving the efficiency of our spending and investing in new areas to support growth. The outcome for the full year will be dependent on the important Christmas period.

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[1] Adjusted results are a non-IFRS measure and exclude specific items and the pension charge to cash difference adjustment. The commentary in this review, unless specified otherwise, focuses on the operating results on an adjusted basis. This is consistent with the way that financial performance is measured by Management and reported to the Board and assists in providing a meaningful analysis of the results of the Group. A reconciliation between adjusted and reported numbers is included on page 14.

[2] All movements are on an underlying basis unless otherwise stated. Underlying change is calculated after adjusting for working days in UKPIL, movements in foreign exchange and ASM in GLS and other one-off items that distort the Group's underlying performance. For volumes, underlying movements are adjusted for working days and exclude the impact of political parties' election mailings in UKPIL and ASM in GLS.

[3] Reported – prepared in accordance with International Financial Reporting Standards (IFRS).

[4] Net debt is calculated by netting the value of financial liabilities (excluding derivatives) against cash and other liquid assets.

[5] Following the Group's acquisition of the remaining 49 per cent shareholding in Romec Limited (Romec) at the beginning of 2016-17, Romec has been consolidated into the UKPIL segment (previously the Group's 51 per cent shareholding was reported within the 'Other' segment). The 2015-16 UKPIL results have been re-presented to reflect this change.

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**Results presentation:**
A results presentation for analysts and institutional investors will be held in London at 9:30am on 17 November 2016 and a simultaneous webcast will be available at www.royalmailgroup.com/results.

A trading update covering the nine months ending 25 December 2016 is expected to be issued on 19 January 2017.

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# CHIEF EXECUTIVE OFFICER'S REVIEW

**Our performance**

Performance in the first half was broadly in line with our expectations. We delivered a resilient performance against a backdrop of low inflation and highly competitive markets. Initiatives put in place over recent years have helped us to maintain our leading position in UK letters and parcels.

Group revenue increased by one per cent[1]. GLS performed well, with revenue up nine per cent[1]. This more than offset a one per cent decline[1] in UKPIL revenue.

Adjusted Group operating profit before transformation costs was £320 million. Adjusted Group operating profit margin after transformation costs increased by 40 basis points[1] to 5.7 per cent. This reflected lower transformation costs of £58 million.

In-year trading cash flow increased to £116 million, largely due to more efficient investment spend.

**Competitive marketplaces**

The UK parcels market is one of the most developed in Europe and remains highly competitive. Annual addressable market volume growth will continue to be impacted by the expansion of Amazon Logistics. E-retail continues to fuel growth in cross-border parcel volumes, while consumers expect a seamless international delivery and returns service. International cross-border services increasingly reflect UK market dynamics.

We continue to forecast a 4-6 per cent decline per annum in addressed letter volumes (excluding the impact of political parties' election mailings) in the medium-term. Movements in Gross Domestic Product (GDP) are drivers for letter volumes. We are closely monitoring the economic environment in the UK.

**Winning in parcels**

UKPIL parcel revenue increased by three per cent[1]. Parcel volumes were up two per cent[1], driven by continued growth in Royal Mail account parcels and lower average unit revenue (AUR) import products. We are seeing an improving trend in export due to movements in foreign exchange and increasing cross border e-commerce.

Improving the customer experience remains a key strategic focus. Over the past three years, we have stepped up the rate of technological change. Through our new and significantly enhanced IT parcel systems we have the ability to offer any account customer a tracked service. In part due to these IT developments, we have won further volumes from major retailers and have seen five per cent[1] growth in account volumes, excluding Amazon. Royal Mail Tracked 24®/48® volumes have grown by 38 per cent; returns volumes are up 19 per cent.

Royal Mail delivers more parcels each year in the UK than all of our competitors combined. We recently commenced the phased roll-out of delivery confirmation on all barcoded standard parcels to account customers. This is supported by our new Postal Digital Assistants (PDA) and the national roll-out of doorstep scanning. Around 50 per cent of all our UKPIL parcels carry a barcode, with work continuing to increase this. Around a third of UKPIL parcels are already being tracked in some way.

We continue to improve customer convenience and flexibility to support consumers, SMEs and marketplace sellers. Customers can now drop-off pre-paid items for delivery at our 1,200 Royal Mail Enquiry Offices, including more than 200 which are now open on Sundays.

Christmas is our most important time of year. We are recruiting over 19,000 temporary staff. We are opening nine temporary parcel sort centres to manage increased traffic over our busiest period, including a new parcel sortation hub at Atherstone, Warwickshire. We will be extending opening hours at our Enquiry Offices and going out later for deliveries.

GLS delivered another good performance with revenue up nine per cent[1]. Revenue growth was achieved in almost all of its markets. Volumes grew by 10 per cent[1], with strong growth in international volumes.

In June 2016, we announced the acquisition of the Spanish express parcels delivery company, ASM[2]. Operating mainly in the business-to-consumer (B2C) segment, it accounts for around 10 per cent of Spain's domestic parcels market. ASM has strengthened GLS' network and services within Spain, particularly in the express segment. The acquisition supports GLS' strategy of targeted and focused geographic expansion.

GLS continues to develop its B2C delivery capability. Launched in Germany in April 2016, GLS *Sameday* offers same day evening deliveries in 11 cities, providing an attractive offering for online shoppers. GLS also recently expanded GLS-ONE in Germany, a portal to facilitate the sending and receiving of parcels. Consumers can create their own label to send parcels and choose to have the parcel delivered to a specific address, parcel box or GLS Parcelshop.

**Defending letters**

Addressed letter volume decline was four per cent[1] (excluding the impact of political parties' election mailings). Total letter revenue (including marketing mail) was down three per cent[1]. Within this, marketing mail[3] revenue was down eight per cent.

Marketing mail is particularly sensitive to changes in economic activity. Uncertainty leading up to and after the EU Referendum led to a reduction in UK marketing activity. We are rolling out new collaborative projects with the advertising industry. We are promoting the use of letters for both wholesale and retail customers with a range of sales activities. For example, we have launched the next phase of our Mailmen campaign with a new line-up of industry chiefs. Five new Mailmen have joined the campaign, including Maurice Saatchi, co-founder of M&C Saatchi.

The Strategic Mailing Partnership™ (SMP), a joint initiative with the mailing house industry, promotes mail by sharing ideas for development and working to resolve critical industry issues. It aims to improve overall efficiency and operational processes and to grow mail volumes. Examples of this include joint industry activities to maximise the benefits of Mailmark®, our letter barcode technology and online-reporting tool, as well as working together with mail producers to introduce innovations such as the digital stamp.

Royal Mail is co-ordinating an industry-wide response to tackle fraudulent mail at its source. A substantial package of measures complements our joint initiative with the National Trading Standards Scams Team. It includes an industry-wide code of practice, developed by Royal Mail and supported by firms including Whistl and UK Mail. We have written to all of the UK access operators and asked them to sign up to the code.

We continue to win back and retain key contracts. In October 2016, Royal Mail won a three-year contract to handle the postal services for 27 of the 33 London Boroughs' postal services. We also announced that we had been awarded a three year framework to provide Scottish Public Bodies with postal services. The framework means that Royal Mail becomes the supplier for Scottish Government, local authority and public body postal services.

On 25 May 2016, Ofcom published its proposals in respect of its Review of the Regulation of Royal Mail. We continue to participate in the consultation process and expect a final decision by March 2017.

**Growing in new areas**

GLS is well positioned to grow in new markets. It has a replicable and scalable business model founded on the development of strong regional businesses. Through increasing its footprint and focusing on growth opportunities in the deferred parcels space, with selective growth in the B2C parcels market, GLS is well positioned to support Royal Mail Group's overall strategy.

On 4 October 2016, we announced that GLS had acquired Golden State Overnight[4] (GSO), a leading provider of regional next day parcel delivery services, principally in California[5]. The area in which GSO operates has a GDP roughly equivalent to the UK[6]. It is an attractive regional market representing the world's fifth largest economy[7], and provides GLS with an opportunity to grow GSO within its existing footprint.

We are expanding our relationships with retailers and network partners to stimulate cross-border volumes between the UK and Asia. We are working with China Post to provide Chinese and UK customers with faster delivery and tracking services.

**Strategic focus on costs and investment**

We continue to adopt a strategic approach to costs. UKPIL operating costs before transformation costs were flat in the first half[1], in part reflecting the strong performance in the comparative period. Productivity improvement of 2.2[8] per cent was within our target range of 2.0-3.0 per cent, reflecting a 1.1 per cent reduction in core network hours, coupled with increased workload. Our cost avoidance programme is on track. We are now targeting to avoid around £600 million of annualised costs cumulative over the three financial years to 2017-18 (previously £500 million).

We continue to pursue opportunities across our cost base to deliver efficiency improvements. In logistics, we are optimising the efficiency of our network, where possible reducing the number of miles as well as driver hours. We have largely completed our major IT transformation programme and expect to benefit from efficiencies going forward. We continue to extend Collections on Delivery. Over 40,000 postboxes have already been covered by the programme, which moves low-volume postboxes to collection while our postmen and women are on their delivery rounds. We are optimising management structures within operations. We are also seeking to simplify and streamline processes in other areas, including central functions, property and Parcelforce Worldwide.

After several years of high levels of spending to catch up with historic underinvestment, we believe we are now past the peak of investment in the business. We have conducted a review of our spending plans and future investments. As a result of this review, we now expect net cash investment to be no more than £500 million per annum going forward, compared with an average of £615 million over the past three financial years.

**Technology and innovation**

Mailmark® has delivered a number of benefits to Royal Mail and its business customers, notably improving order handling procedures for customers and more accurate billing. Around 70 per cent of machine-readable mail (around 45 per cent of total addressed letter volumes) currently bears a Mailmark®. We are on track to reach 90 per cent of suitable letters by March 2017. This is supported by a more resilient IT backbone as a result of our major IT transformation programme.

We are continuing to make it easier for customers to access our international services. We are building on our shipping solutions, using the cross-border capabilities of Intersoft. With Intersoft, we have developed our export solutions and now have the capability to offer tracked cross-border outbound and returns services to our larger customers.

**Our workforce**

We are well advanced with the triennial review of the Royal Mail Pension Plan (RMPP, the Plan), which remains open to future accrual by around 90,000 members. We wrote to these colleagues in the summer, indicating that it was unlikely that Royal Mail could afford to keep the Plan open in its current form beyond the committed period to March 2018. We are in active discussions with the Trustee about the 2015 valuation, and with the unions about the nature of our future pension arrangements. We are targeting to have this resolved around the end of this financial year. This is further discussed in the Financial Review.

We exceeded our 93.0 per cent First Class mail target, with 93.4 per cent of this mail delivered the next working day. We have also exceeded our regulatory Quality of Service target of 98.5 per cent for Second Class mail for the first half of 2016-17. 98.9 per cent of Second Class mail was delivered within three working days.

In October 2016, all eligible full-time employees received 81 SIP 2016 Free Shares. Since our flotation on the London Stock Exchange in October 2013, in total, each eligible full-time employee has received 913 shares in our Company, for free. This means that eligible full-time employees with 913 Free Shares will receive an interim dividend payment of over £67 on 11 January 2017; a total of around £500 (before tax) since privatisation.

Our people put the customer at the heart of everything they do. In the first half, our mean business customer satisfaction score[9] was 78, an improvement on the full year 2015-16. We continue to improve our Net Promoter Score, which measures the loyalty of our business customers, scoring 36 in the period. We were disappointed that we have seen an overall increase in complaints. We take complaints very seriously and continue to highlight business standards and key procedures to tackle denial of receipt through the use of 'With your Neighbour' cards and the importance of correct doorstep scanning.

**Outlook**

The key drivers for the UK letters and parcels markets remain unchanged. Letter volumes, particularly advertising letter volumes, are linked to movements in GDP. We are monitoring developments in the UK economy closely as we have already seen some impact of the softer economic conditions on our marketing mail revenue. Growth in e-commerce is the key driver for B2C parcel volumes but the parcels market remains highly competitive, particularly in the international space.

We are expanding our multi-year, strategic approach to costs so we are now targeting to avoid around £225 million of UKPIL operating costs in 2016-17 and around £600 million of annualised operating costs cumulative over the three financial years to 2017-18. For 2016-17, we are now targeting to reduce underlying UKPIL operating costs before transformation costs by up to one per cent. The outcome of our cost performance will be dependent on the absorbable rate of change within our organisation. Due to a change in the mix of projects, we now expect transformation costs to be between £130-160 million for 2016-17.

GLS continues to perform well and will remain a focus for investment to help drive growth.

Over the last five years, we have made significant investments in projects to support growth and to replace and replenish our assets. Now that some of the larger projects - rebuilding our legacy IT systems and resizing the core network - are largely complete, we are reprofiling our investment spend, which will be lower overall and weighted to growth. We now expect that our total net cash investment will be no more than £500 million per annum going forward, compared with an average over the last three financial years of £615 million.

We are harvesting the benefits of the technology rebuild. We remain very focused on improving our products and services, controlling costs, improving the efficiency of our spending and investing in new areas to support growth.

As in previous years, the outcome for the full year will be dependent on our performance over the important Christmas period.

**Thank you**

We are honoured and delighted that Their Royal Highnesses The Prince of Wales and The Duchess of Cornwall joined us at a reception to celebrate 500 years of the postal service. It was a privilege to introduce the Royal couple to so many inspirational people from across our business, from long-serving colleagues with more than half a century of loyal service to charity champions. Above all, it is our people I would like to thank for making our 500 years celebrations something to remember.

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[1] All movements are on an underlying basis unless otherwise stated. Underlying change is calculated after adjusting for working days in UKPIL, movements in foreign exchange and ASM in GLS and other one-off items that distort the Group's underlying performance. For volumes, underlying movements are adjusted for working days and exclude the impact of political parties' election mailings in UKPIL and ASM in GLS.

[2] Agencia Servicios Mensajería S.A.U.

[3] Includes data, redirections, Address Management Unit and addressed and unaddressed advertising mail.

[4] Golden State Overnight Delivery Service Inc.

[5] GSO also operates in Arizona, Nevada and New Mexico.

[6] World Development Factors, World Bank and US Bureau of Economic Analysis.

[7] World Development Factors, World Bank and US Bureau of Economic Analysis. United States, China, Japan and Germany generated higher GDP than the combined GDP of California, Arizona, Nevada and New Mexico in 2015.

[8] Collections, processing and delivery in core network.

[9] Royal Mail Business Customer Satisfaction survey, conducted by Ipsos MORI.

# UK PARCELS, INTERNATIONAL & LETTERS (UKPIL)

The adjusted results presented below are non-IFRS measures, which exclude specific items and reflect the pension charge to cash difference adjustment, which Management believes is more a meaningful basis upon which to analyse the business performance and is consistent with the way financial performance is reported to the Board.

| Summary trading results (£m) | **Adjusted[1] 26 weeks ended 25 September 2016** | Adjusted[1,2] 26 weeks ended 27 September 2015 | Underlying change[3] |
|---|---|---|---|
| Letters & other mail | **1,562** | 1,584 | (2%) |
| Marketing mail | **547** | 591 | (8%) |
| Total letters | **2,109** | 2,175 | (3%) |
| Parcels | **1,532** | 1,479 | 3% |
| Revenue[4] | **3,641** | 3,654 | (1%) |
| Operating costs before transformation costs | **(3,394)** | (3,364) | Flat |
| Operating profit before transformation costs | **247** | 290 | (11%) |
| *Margin* | ***6.8%*** | *7.9%* | *(70bps)* |
| Transformation costs | **(58)** | (94) | |
| Operating profit after transformation costs | **189** | 196 | |
| *Margin* | ***5.2%*** | *5.4%* | *20bps* |
| | | | |
| **Volumes (m)** | | | |
| **Letters** | | | |
| Addressed letters | **5,937** | 6,195 | (4%) |
| Unaddressed letters | **1,404** | 1,347 | 4% |
| | | | |
| **Parcels** | | | |
| Core network | **487** | 473 | 2% |
| Parcelforce Worldwide | **46** | 45 | 2% |
| **Total** | **533** | 518 | 2% |

The following commentary refers to movements on an underlying basis. In UKPIL, underlying movements are calculated after adjusting for working days, changes in employment legislation and acquisitions as set out at the end of the Financial Review.

### Revenue and volumes

UKPIL revenue was down one per cent, with parcel revenue up three per cent and total letter revenue down three per cent. Weaker Sterling had a positive impact of £12 million on UKPIL revenue.

Total parcel volumes increased by two per cent. Parcel volume growth was driven by Royal Mail account parcels and import parcels, which more than offset the decline in higher AUR export parcels. In account parcels, we more than replaced lost Amazon traffic such that account parcel volumes, excluding Amazon, grew by five per cent. In the consumer channel, we are seeing improved volume and revenue trends. The rate of increase in lower AUR import parcel volumes, largely from China, has slowed indicating an impact from weaker Sterling. We have focused on improving AURs in this channel by improving service levels offered, including a tracked product. The decline in export parcel volumes has moderated, but export parcels is an increasingly competitive market. As expected, the rate of volume growth in Parcelforce Worldwide has slowed to two per cent, reflecting the highly competitive express parcels market.

Addressed letter volumes declined by four per cent (excluding the impact of political parties' election mailings) as the positive one-off impacts seen in the first quarter of the year diminished. Total letter revenue (including marketing mail) decreased by three per cent, reflecting the impact of low inflation, customers continuing to switch to lower cost products and the decline in marketing mail.

Marketing mail revenue, which includes our data businesses, declined by eight per cent. We saw a slowdown in activity over the period reflecting a continued softening in economic conditions. Low AUR unaddressed letter volumes were up four per cent, due to EU Referendum mailings and a weak prior period.

**Operating costs**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 | Underlying change[3] |
|---|---|---|---|
| People costs | **(2,351)** | (2,340) | (1%) |
| Non-people costs | **(1,043)** | (1,024) | 2% |
| Distribution & conveyance costs | **(370)** | (361) | 2% |
| Infrastructure costs | **(360)** | (345) | 4% |
| Other operating costs | **(313)** | (318) | (2%) |
| **Total operating costs before transformation costs** | **(3,394)** | (3,364) | Flat |

As a result of the acquisition of the minority shareholding in Romec on 31 March 2016, the costs of Romec, previously reported in the 'Other' segment, have been incorporated into UKPIL people and non-people costs for 2016-17, replacing the facilities management charge previously included within infrastructure costs (H1 2015-16 £68 million). UKPIL operating costs for 2015-16 have been re-presented to reflect this change.

Total adjusted operating costs before transformation costs were flat on an underlying basis. This partly reflects a strong performance in the first half of 2015-16, which benefited from the acceleration of our efficiency programme. Given the phasing of cost reductions in the prior year, we are targeting a better performance in the second half. Our cost avoidance programme in UKPIL is on track, with £87 million costs avoided in the first half, comprising people costs of £60 million and non-people costs of £27 million. In the first half, we have delivered benefits across a number of initiatives including optimisation of our management structures within operations, better vehicle utilisation and lower property costs.

As previously disclosed, as a result of the new single-tier state pension scheme introduced in April 2016, the Group saw an increase in its employer National Insurance contributions for employees participating in the RMPP of £33 million in the first half. This has been excluded from underlying movements. We now expect the increase in National Insurance contributions to be around £65 million in 2016-17.

People costs declined by one per cent, largely driven by a 2.2 per cent improvement in collections, processing and delivery productivity in the core network. This more than offset pay increases, largely the 1.6 per cent frontline pay award. The improvement in productivity was achieved through a 1.1 per cent reduction in core network hours, coupled with the absorption of a higher workload, driven by an increase in tracked products. We continue to target annual productivity improvements of 2.0-3.0 per cent per annum.

Non-people costs increased by two per cent. Distribution and conveyance costs increased by two per cent, driven by a £15 million increase in terminal dues resulting from weaker Sterling. Total diesel and jet fuel costs of £74 million were £8 million lower than the prior year due to lower pricing and improved fleet management. We expect diesel and jet fuel costs to be around £155 million in 2016-17.

Infrastructure costs were up four per cent due to the phasing of annual property maintenance and a £7 million increase in depreciation driven by IT investments. The prior year benefited from certain one-off savings related to property. Within infrastructure costs, the cost avoidance programme has delivered benefits in property through the integration of Romec and lower discretionary spend across the entire estate.

Other operating costs were down two per cent with the increased cost of marketing in our new business areas being mitigated by activity within the cost avoidance programme, including improved utilisation of low value assets and lower discretionary spend.

On a reported basis, UKPIL operating costs before transformation costs increased by £10 million to £3,508 million.

**Transformation costs**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 |
|---|---|---|
| Voluntary redundancy | **(26)** | (63) |
| Project costs | **(32)** | (30) |
| Business transformation payments | **-** | (1) |
| **Total** | **(58)** | (94) |

Transformation costs were £36 million lower due to higher levels of activity in the prior period as a result of the acceleration of our efficiency programme. There was a net increase of around 330 employees in UKPIL in the first half. However, there was a reduction of around 1,360 FTEs[5] to 147,804 FTEs during the first half, reflecting a change in the mix of full-time and part-time employees and a reduction in variable hours. Project costs were £32 million, largely relating to projects supporting the cost avoidance programme.

**Operating profit after transformation costs**

Adjusted operating profit after transformation costs was £189 million, giving a margin of 5.2 per cent, up 20 basis points on an underlying basis due to lower transformation costs.

Reported operating profit after transformation costs was £75 million, giving a margin of 2.1 per cent, reflecting the IAS 19 pension charge to cash difference adjustment.

# GENERAL LOGISTICS SYSTEMS (GLS)

| Summary trading results (continuing operations) (€m) | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 | Underlying change[3] |
|---|---|---|---|
| Revenue | **1,155** | 1,029 | 9% |
| Operating costs | **(1,066)** | (957) | 8% |
| Operating profit | **89** | 72 | 25% |
| *Margin* | ***7.7%*** | *7.0%* | *90bps* |
| | | | |
| **(£m)** | | | |
| Revenue | **942** | 741 | |
| Operating costs | **(869)** | (689) | |
| Operating profit | **73** | 52 | |
| | | | |
| **Volumes (m)** | **233** | 204 | 10% |

GLS' performance for the first half of 2016-17 includes three and a half months' contribution from ASM, which was acquired in June 2016. Underlying movements in GLS' results exclude the impact from ASM. The following commentary refers to movements on an underlying basis.

**Revenue and volumes**

GLS continued to perform well. Performance in the period benefited from the timing of Easter and other public holidays across Europe, which are estimated to have accounted for around two percentage points of the volume and one percentage point of the revenue movements. Volumes were up 10 per cent, with continued strong growth in international volumes. Revenue increased by nine per cent, as pricing was impacted by lower average parcel weights. Revenue growth was achieved in almost all markets and from a broad customer base, with the largest customer accounting for around two per cent of total GLS revenue. The three major markets, Germany, Italy and France, accounted for 66 per cent of total GLS revenue.

| Operating costs (€m) | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 | Underlying change[3] |
|---|---|---|---|
| People costs | **(256)** | (233) | 8% |
| Non-people costs | **(810)** | (724) | 8% |
| Distribution & conveyance costs | **(705)** | (628) | 9% |
| Infrastructure costs | **(71)** | (69) | (3%) |
| Other operating costs | **(34)** | (27) | 21% |
| **Total operating costs** | **(1,066)** | (957) | 8% |

Total operating costs were up eight per cent.

People costs increased by eight per cent as a result of increased semi-variable costs linked to volume, pay inflation and a one-off provision release of €3 million in the prior period. Distribution and conveyance costs were up nine per cent, driven by higher volumes. Infrastructure costs decreased by three per cent, in part due to a one-off provision release of €2 million for IT related costs. Other operating costs increased by 21 per cent, including the impact of €2 million transaction and initial integration costs in respect of ASM.

**Operating profit**

Operating profit was €89 million, giving a profit margin of 7.7 per cent, an improvement of 90 basis points over the prior year. This performance was largely due to improved profitability in Germany and Italy. Reported profit in Sterling terms, compared with the prior year, benefited from a £7 million impact from exchange rate movements.

**Germany**

Revenue in GLS Germany grew by five per cent, driven by international volumes.

**Italy**
GLS Italy continues to perform strongly. Revenue growth of 15 per cent was due to strong B2C volume growth, driven by Amazon and other customers. Given the strong performance over the last two years, it will be challenging to maintain this rate of growth going forward.

**France**
GLS France delivered an improved rate of revenue growth of eight per cent, largely from international customers. Operating losses reduced by €3 million to €5 million.

**Other developed European markets (including Austria, Belgium, Denmark, Ireland, Netherlands, Portugal and Spain)**
Revenue growth was achieved in the majority of other developed European markets with strong growth in Denmark. In June 2016, we announced the acquisition of ASM for a total consideration (including debt taken on) of €71 million. ASM generated around €78 million of revenue in the year ended 31 December 2015. Given the potential synergies, the transaction is expected to be economic profit accretive for GLS in 2018-19.

**Other developing/emerging European markets (including Croatia, Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia)**
We saw revenue growth in all developing/emerging European markets, with particularly strong growth in Romania. This has been largely driven by the growing parcels markets in these countries.

**USA**
On 4 October 2016, we announced the acquisition of GSO, a regional next day parcel delivery company operating primarily in California, for a total consideration of $90 million. GSO will be operated as a standalone business but will be incorporated into the results of GLS. For the year to 31 March 2016, GSO generated revenue of $114 million. The transaction is expected to be economic profit accretive for GLS in 2019-20.

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[1] Adjusted results are a non-IFRS measure and exclude specific items and the pension charge to cash difference adjustment. The commentary in this review, unless specified otherwise, focuses on the operating results on an adjusted basis. This is consistent with the way that financial performance is measured by Management and reported to the Board and assists in providing a meaningful analysis of the results of the Group. A reconciliation between adjusted and reported numbers is included on page 14.

[2] Following the Group's acquisition of the remaining 49 per cent shareholding in Romec Limited (Romec) at the beginning of 2016-17, Romec has been consolidated into the UKPIL segment (previously the Group's 51 per cent shareholding was reported within the 'Other' segment). The 2015-16 UKPIL results have been re-presented to reflect this change.

[3] All movements are on an underlying basis unless otherwise stated. Underlying change is calculated after adjusting for working days in UKPIL, movements in foreign exchange and ASM in GLS and other one-off items that distort the Group's underlying performance. For volumes, underlying movements are adjusted for working days and exclude the impact of political parties' election mailings in UKPIL and ASM in GLS.

[4] Stamped, metered and other prepaid revenue channels are subject to statistical sampling surveys to derive the revenue relating to parcels, marketing mail and letters. These surveys are subject to continuous refinement, which may over time reallocate revenue between the products above, and which may occasionally lead to a consequent change to this estimate.

[5] Full time equivalent (FTE) numbers relate to the total number of paid hours (including part-time, full-time and agency hours) divided by the standard full-time working hours in the same period.

# FINANCIAL REVIEW

**Reported results**

Group revenue increased to £4,583 million (H1 2015-16 £4,395 million). Operating costs before transformation costs increased to £4,377 million (H1 2015-16 £4,187 million). Group operating profit before transformation costs reduced to £206 million (H1 2015-16 £208 million) and operating profit after transformation costs increased to £148 million (H1 2015-16 £114 million). Operating specific items increased to £90 million (H1 2015-16 £74 million). As a result, Group operating profit was £58 million (H1 2015-16 £40 million). Profit before tax from continuing operations reduced to £110 million (H1 2015-16 £116 million). Earnings per share from continuing operations reduced from 8.8 pence to 8.6 pence.

**2015-16 Results re-presentation for the consolidation of Romec Limited (Romec)**

As a result of the acquisition of the minority shareholding in Romec on 31 March 2016, the revenue and costs of Romec previously reported in the 'Other' segment, have been consolidated into UKPIL people and non-people costs for 2016-17, replacing the facilities management charge of £68 million for the first half of 2015-16 previously included within infrastructure costs. At Group level, there is a re-presentation of this £68 million charge between infrastructure and other costs. Both the Group and UKPIL reported and adjusted results for 2015-16 have been re-presented to reflect this change as shown below:

| **Group**<br>**(£m)** | **Adjusted 26 weeks ended 27 September 2015** | **Romec Adjustment** | **Re-presented 26 weeks ended 27 September 2015** |
|---|---|---|---|
| **Revenue** | 4,395 | - | 4,395 |
| **Operating costs** | (4,053) | - | (4,053) |
| People costs | (2,508) | - | (2,508) |
| Non-people costs | (1,545) | - | (1,545) |
| Distribution & conveyance costs | (813) | - | (813) |
| Infrastructure costs | (463) | 68 | (395) |
| Other operating costs | (269) | (68) | (337) |
| **Operating profit before transformation costs** | 342 | - | 342 |

| **UKPIL**<br>**(£m)** | **Adjusted 26 weeks ended 27 September 2015** | **Romec Adjustment** | **Re-presented 26 weeks ended 27 September 2015** |
|---|---|---|---|
| **Revenue** | 3,651 | 3 | 3,654 |
| **Operating costs** | (3,367) | 3 | (3,364) |
| People costs | (2,301) | (39) | (2,340) |
| Non-people costs | (1,066) | 42 | (1,024) |
| Distribution & conveyance costs | (361) | - | (361) |
| Infrastructure costs | (413) | 68 | (345) |
| Other operating costs | (292) | (26) | (318) |
| **Operating profit before transformation costs** | 284 | 6 | 290 |

| **Other**<br>**(£m)** | **Adjusted 26 weeks ended 27 September 2015** | **Romec Adjustment** | **Re-presented 26 weeks ended 27 September 2015** |
|---|---|---|---|
| **Revenue** | 3 | (3) | - |
| **Operating costs** | 3 | (3) | - |
| People costs | (39) | 39 | - |
| Non-people costs | 42 | (42) | - |
| Distribution & conveyance costs | - | - | - |
| Infrastructure costs | - | - | - |
| Other operating costs | 42 | (42) | - |
| **Operating profit before transformation costs** | 6 | (6) | - |

## Presentation of results

The remaining commentary in this Financial Review, unless otherwise indicated, focuses on the adjusted results. The adjusted results are non-IFRS measures, which exclude specific items and reflect the pension charge to cash difference adjustment which Management believes is a more meaningful basis upon which to analyse the business performance (in particular given the volatile nature of the IAS 19 charge) and is consistent with the way financial performance is reported to the Board. Movements in revenue, costs, profits and margins are on an underlying basis. This is consistent with the way that financial performance is measured by Management and reported to the Board. Again, this assists in providing a meaningful analysis of the trading results of the Group. The analysis of underlying movements in adjusted results is set out at the end of the Financial Review.

The adjustments to reported results are set out below. Reported results are set out in the financial statements at the end of this document. Following the publication of an amendment to IAS 1, the Group no longer shows non-IFRS adjustments on the face of its income statement.

| (£m) | **26 weeks ended 25 September 2016** Reported[1] | **Specific items and pension adjustment** | **Adjusted[2]** | 26 weeks ended 27 September 2015 Reported[1,3] | Specific items and pension adjustment | Adjusted[2,3] |
|---|---|---|---|---|---|---|
| **Revenue** | **4,583** | - | **4,583** | 4,395 | - | 4,395 |
| **Operating costs** | **(4,377)** | (114) | **(4,263)** | (4,187) | (134) | (4,053) |
| People costs | (2,674) | (114) | (2,560) | (2,642) | (134) | (2,508) |
| Non-people costs | (1,703) | - | (1,703) | (1,545) | - | (1,545) |
| Distribution & conveyance costs | (945) | - | (945) | (813) | - | (813) |
| Infrastructure costs | (417) | - | (417) | (395) | - | (395) |
| Other operating costs | (341) | - | (341) | (337) | - | (337) |
| **Operating profit before transformation costs** | **206** | (114) | **320** | 208 | (134) | 342 |
| Transformation costs | **(58)** | - | **(58)** | (94) | - | (94) |
| **Operating profit after transformation costs** | **148** | (114) | **262** | 114 | (134) | 248 |
| Operating specific items: | | | | | | |
| Employee Free Shares charge | **(79)** | (79) | **-** | (76) | (76) | - |
| Legacy (costs)/credit | **(11)** | (11) | **-** | 2 | 2 | - |
| **Operating profit** | **58** | (204) | **262** | 40 | (208) | 248 |
| Non-operating specific items: | | | | | | |
| Profit on disposal of property, plant and equipment | **4** | 4 | **-** | 27 | 27 | - |
| Loss on disposal of business | **(2)** | (2) | **-** | - | - | - |
| **Earnings before interest and tax** | **60** | (202) | **262** | 67 | (181) | 248 |
| Finance costs | **(11)** | - | **(11)** | (9) | - | (9) |
| Finance income | **1** | - | **1** | 1 | - | 1 |
| Net pension interest (non-operating specific item) | **60** | 60 | **-** | 57 | 57 | - |
| **Profit before tax** | **110** | (142) | **252** | 116 | (124) | 240 |
| Tax (charge)/credit | **(23)** | 36 | **(59)** | (26) | 31 | (57) |
| **Profit for the period from continuing operations** | **87** | (106) | **193** | 90 | (93) | 183 |
| **Discontinued operations** | | | | | | |
| Profit from disposal of discontinued operations (non-operating specific item) | **-** | - | **-** | 31 | 31 | - |
| Tax on profit from disposal of discontinued operations | **-** | - | **-** | (5) | (5) | - |
| **Profit for the period** | **87** | (106) | **193** | 116 | (67) | 183 |
| **Profit for the period attributable to:** | | | | | | |
| Equity holders of the parent Company | **86** | (106) | **192** | 114 | (67) | 181 |
| Non-controlling interests | **1** | - | **1** | 2 | - | 2 |
| **Earnings per share** | | | | | | |
| Basic – continuing operations | **8.6p** | (10.6)p | **19.2p** | 8.8p | (9.3)p | 18.1p |
| Diluted – continuing operations | **8.6p** | (10.5)p | **19.1p** | 8.7p | (9.3)p | 18.0p |
| Basic – total Group | **8.6p** | (10.6)p | **19.2p** | 11.4p | (6.7)p | 18.1p |
| Diluted – total Group | **8.6p** | (10.5)p | **19.1p** | 11.3p | (6.7)p | 18.0p |

[1] Reported - prepared in accordance with International Financial Reporting Standards (IFRS).

[2] Adjusted results are a non-IFRS measure and exclude specific items and the pension charge to cash difference adjustment.

[3] Re-presented to reflect the Group's acquisition of the remaining 49 per cent shareholding in Romec Limited (Romec) at the beginning of 2016-17, and to consolidate the results of Romec into the UKPIL segment (previously the Group's 51 per cent shareholding was reported within the 'Other' segment). The 2015-16 UKPIL results have been re-presented to reflect this change.

**Group revenue**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 | Underlying change |
|---|---|---|---|
| UKPIL | **3,641** | 3,654 | (1%) |
| GLS | **942** | 741 | 9% |
| **Total revenue** | **4,583** | 4,395 | 1% |

Parcel revenue accounted for 54 per cent of Group revenue (H1 2015-16 51 per cent). The main factors impacting revenue in the year are described in the sections entitled 'UK Parcels, International & Letters (UKPIL)' and 'General Logistics Systems (GLS)'.

**Group operating costs**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 | Underlying change |
|---|---|---|---|
| People costs | **(2,560)** | (2,508) | Flat |
| Non-people costs | **(1,703)** | (1,545) | 4% |
| Distribution & conveyance costs | **(945)** | (813) | 6% |
| Infrastructure costs | **(417)** | (395) | 3% |
| Other operating costs | **(341)** | (337) | Flat |
| **Total operating costs** | **(4,263)** | (4,053) | 1% |

Group operating costs increased by one per cent, due to increases in GLS. The main factors impacting operating costs in the year are described in the sections entitled 'UK Parcels, International & Letters (UKPIL)' and 'General Logistics Systems (GLS)'.

**Group operating profit after transformation costs**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 |
|---|---|---|
| UKPIL | **189** | 196 |
| GLS | **73** | 52 |
| **Group operating profit after transformation costs** | **262** | 248 |
| *Margin* | ***5.7%*** | *5.6%* |

Lower transformation costs in UKPIL led to operating profit margin after transformation costs increasing by 40 basis points on an underlying basis to 5.7 per cent.

**Specific items and pension non-cash adjustment**

Operating specific items in the period related mainly to the Employee Free Shares charge of £79 million (H1 2015-16 £76 million). The pension charge to cash difference adjustment was £114 million (H1 2015-16 £134 million). The difference between the pension charge and cash cost represents the difference between the income statement pension charge rate of 28.8 per cent and the actual cash payments into the RMPP at 17.1 per cent. The pension charge to cash difference adjustment is expected to be around £230 million for the full year.

The Employee Free Shares charge has increased to reflect the Free Shares awarded in October 2015 under SIP 2015, but has been partially offset by lower charges from SIP 2013 and SIP 2014 due to employees leaving the Group. The Employee Free Shares charge is expected to be around £110 million for the full year. The charge will be lower in the second half as a result of SIP 2013 maturing in October 2016.

The increase in legacy costs is driven by a reduction in the discount rate used to calculate the industrial diseases provision. Other specific items relate to the integration of Romec staff.

Non-operating specific items include a profit on disposal of property, plant and equipment of £4 million (H1 2015-16 £27 million) mainly arising from the sale of the Maidstone Delivery Office. The loss on disposal of business relates to the sale of NDC 2000 Limited (NDC) and reflects the transfer of cash and other assets to the purchasers. The net pension interest credit was £60 million (H1 2015-16 £57 million), higher than the prior period due to the increase in the accounting surplus at 27 March 2016. The pension interest credit for the full year is expected to be around £120 million.

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 |
|---|---|---|
| **Pension charge to cash difference adjustment (within People costs)** | **(114)** | (134) |
| **Operating specific items** | | |
| Employee Free Shares charge | **(79)** | (76) |
| Legacy (costs)/credit | **(11)** | 2 |
| Potential industrial diseases claims | (9) | 3 |
| French Competition Authority investigation costs | - | (2) |
| Other | (2) | 1 |
| **Total operating specific items and pensions adjustment** | **(204)** | (208) |
| **Non-operating specific items** | | |
| Profit on disposal of property, plant and equipment | **4** | 27 |
| Loss on disposal of business | **(2)** | - |
| Net pension interest | **60** | 57 |
| Profit on disposal of discontinued operations | **-** | 31 |
| **Total non-operating specific items** | **62** | 115 |
| **Total specific items and pensions adjustment before tax** | **(142)** | (93) |
| **Total tax credit on specific items and pensions adjustment** | **36** | 26 |

## Net finance costs

Net finance costs were £10 million compared with £8 million in the prior period. Interest on the €500 million bond was £5.5 million, £1.3 million higher than the prior period as a result of weaker Sterling.

| **Facility** | **Rate** | **Facility (£m)** | **Drawn (£m)** | **Facility end date** |
|---|---|---|---|---|
| €500 million bond | 2.5% | 431 | 431 | 2024 |
| Loans in GLS (Spain) | 1.9% | 7 | 7 | 2019 |
| Revolving credit facility | LIBOR+0.55% | 1,050 | 100 | 2020-21 |
| **Total** | | **1,488** | **538** | |

The blended interest rate on gross debt including finance leases for 2016-17 is expected to be approximately three per cent. The retranslation impact of the €500 million bond is accounted for within reserves.

## Taxation

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 |
|---|---|---|
| UK tax charge | **(38)** | (41) |
| Foreign tax charge | **(21)** | (16) |
| **Total tax charge** | **(59)** | (57) |
| *Effective tax rate* | ***23%*** | *24%* |

The Group effective tax rate on adjusted profit before tax was 23 per cent. The UK adjusted effective tax rate of 21 per cent is broadly in line with the UK statutory tax rate. GLS' effective tax rate of 29 per cent has reduced due to lower French losses for which no deferred tax is recognised.

## Earnings per share (EPS)

Basic adjusted EPS for continuing operations was 19.2 pence compared with 18.1 pence in the prior period, reflecting the decrease in transformation costs.

**In-year trading cash flow**

| (£m) | **Adjusted 26 weeks ended 25 September 2016** | Adjusted 26 weeks ended 27 September 2015 |
|---|---|---|
| EBITDA before transformation costs | **352** | 343 |
| Pension charge to cash difference adjustment | **114** | 134 |
| Adjusted EBITDA before transformation costs | **466** | 477 |
| Trading working capital movements | **(127)** | (159) |
| Share-based awards (SAYE and LTIP) charge adjustment | **6** | 2 |
| Total investment | **(201)** | (299) |
| Income tax paid | **(16)** | (9) |
| Net finance costs paid | **(12)** | (11) |
| **In-year trading cash inflow** | **116** | 1 |

In-year trading cash flow was an inflow of £116 million, £115 million higher than the prior period, mainly driven by more efficient investment and lower trading working capital absorption. Adjusted EBITDA before transformation costs was £11 million lower, principally due to higher National Insurance costs. Trading working capital movements were an outflow of £127 million, £32 million lower than the prior year largely due to an improved settlement profile in our international business.

In the UK we continue to be able to offset the majority of taxable profits with capital allowances and brought forward losses. This is expected to normalise in 2018-19. Research and development credits could extend this timeframe.

**Investment**

| (£m) | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 |
|---|---|---|
| Growth capital expenditure | **(80)** | (74) |
| Replacement capital expenditure | **(61)** | (89) |
| Transformation operating expenditure | | |
| Voluntary redundancy | **(28)** | (105) |
| Project costs | **(32)** | (30) |
| Business transformation payments | **-** | (1) |
| **Total investment** | **(201)** | (299) |
| Proceeds from disposal of property (excluding London property portfolio), plant and equipment | **7** | 34 |
| **Net investment** | **(194)** | (265) |

Total gross investment decreased from £299 million to £201 million, mainly due to lower spend in relation to voluntary redundancy payments. Growth capital expenditure increased by £6 million as a result of continued investment in parcels initiatives. Replacement capital expenditure reduced by £28 million, due to the timing of ongoing property maintenance and lower spending on certain property and technology projects.

**Net debt**

Net debt is calculated by netting the value of financial liabilities (excluding derivatives) against cash and other liquid assets. Net debt was £452 million at 25 September 2016, £228 million higher than at 27 March 2016, driven by the 2015-16 final dividend of £149 million, acquisitions of £71 million and a £27 million impact from movements in foreign exchange rates on our Euro denominated net debt.

A calculation of net debt is shown below.

| (£m) | **25 September 2016** | 27 March 2016 |
|---|---|---|
| Loans/bonds | (538) | (392) |
| Finance leases | (182) | (220) |
| Cash and cash equivalents | 248 | 368 |
| Pension escrow (RMSEPP) | 20 | 20 |
| **Net debt** | **(452)** | (224) |

A reconciliation of net debt is shown below.

| (£m) | | **26 weeks ended 25 September 2016** | | 26 weeks ended 27 September 2015 |
|---|---|---|---|---|
| Net debt brought forward at 27 March 2016 and 29 March 2015 | | **(224)** | | (275) |
| **In-year trading cash inflow** | **116** | | 1 | |
| Other working capital movements | (16) | | (10) | |
| Cash cost of operating specific items | (47) | | (2) | |
| Proceeds from disposal of property (excluding London property portfolio), plant and equipment | 7 | | 34 | |
| Cash impact of disposal of discontinued operations and subsidiary | (3) | | 41 | |
| Acquisition of business interests | (71) | | (7) | |
| Cash flows relating to London property portfolio | (17) | | (8) | |
| **Free cash flow** | | **(31)** | | 49 |
| Dividends paid to equity holders of the parent Company | | **(149)** | | (143) |
| Dividends paid to non-controlling interests | | **(8)** | | (2) |
| Purchase of own shares | | **(6)** | | - |
| Loans in GLS (Spain) | | **(7)** | | - |
| Foreign currency exchange impact on cash and cash equivalents | | **15** | | (1) |
| Foreign currency exchange impact on €500 million bond and finance lease creditors | | **(42)** | | 3 |
| **Net debt carried forward** | | **(452)** | | (369) |

Free cash flow is based on reported net cash flow before financing activities, adjusted to include finance costs paid and to exclude net cash generated from the purchase/sale of financial asset investments.

Other working capital movements include movements in GLS client cash held and in deferred revenue from stamps purchased in prior periods. GLS client cash held at 25 September 2016 was £19 million.

The cash cost of operating specific items largely related to the French Competition Authority fine of €55 million that was paid in April 2016. Property disposal proceeds of £7 million relate to the sale of two Delivery Offices.

Acquisition of business interests cash flows of £71 million relate to amounts paid in respect of investments made in the half year, mainly eCourier, the remaining 49 per cent of Romec and acquisitions in GLS, including ASM and deferred consideration paid in relation to acquisitions made in prior periods.

A reconciliation of cash flows relating to acquisitions is shown below.

| (£m) | **26 weeks ended 25 September 2016** |
|---|---|
| eCourier | (9) |
| ASM | (49) |
| **Total consideration (see Note 6)** | **(58)** |
| Add back net cash acquired on acquisition of business | 3 |
| **Acquisition of business interests, net of cash acquired (see statutory cash flow statement)** | **(55)** |
| Deferred consideration paid in respect of prior years' acquisitions | (3) |
| | (58) |
| Acquisition of remaining 49% holding in Romec | (13) |
| **Acquisition of business interests** | **(71)** |

Cash flows relating to the London property portfolio of £17 million largely relate to remediation work, reprovisioning costs and professional fees in relation to the Nine Elms and Mount Pleasant sites.

**Pensions**

The Company's overall IAS 19 pension position at 25 September 2016 was a surplus of £4,282 million, compared with a surplus of £3,430 million at 27 March 2016. The IAS 19 accounting position and key assumptions for the valuation are provided in Note 3 to the consolidated financial statements.

The accounting liabilities have increased over the period due to the fall in corporate bond yields. This has been offset by the increase in the RMPP assets, largely due to the hedging strategy adopted by the Plan.

**Royal Mail Pension Plan (RMPP)**

The triennial valuation of RMPP at 31 March 2015 is still in progress. However, based on a set of assumptions which we believe are likely to form the basis for the March 2015 valuation, the RMPP actuarial surplus at 30 September 2016 was estimated to be £1,575 million, comprising of assets of £9,583 million and liabilities of £8,008 million (31 March 2016 £1,765 million).

Based on this set of assumptions, the cost of the benefits being accrued each year, based on market conditions at the end of September 2016, would currently be around £1.4 billion. This is significantly greater than the total annual contributions of around £500 million that the Company and employees make. Accordingly, we expect that the actuarial funding surplus will be exhausted during 2018. After this time, the annual cost would be more than double the current contributions, which, as we pointed out to Plan members in a letter we sent in June 2016, is unaffordable for the Company.

As part of the March 2012 actuarial valuation, the Company agreed to pay additional contributions of up to £50 million each year from April 2016 onwards if the Trustee considers these necessary to maintain the Plan's projected funding position at March 2019, on the March 2012 valuation basis. The Trustee has carried out its assessment of liabilities at March 2016 on that basis and has confirmed that no payment is due for 2016-17.

**Royal Mail Senior Executives Pension Plan (RMSEPP)**

The RMSEPP triennial valuation at 31 March 2015 has been completed, based on the assumptions agreed as part of the Funding Agreement made between the Company and the Trustee in 2013. On this basis, the actuarial surplus was £16 million at 31 March 2015 comprising assets of £410 million and liabilities of £394 million.

The RMSEPP closed in December 2012 to future accrual. Therefore the Company makes no regular future service contributions. As agreed in the February 2013 Funding Agreement with the Trustee, the Company makes deficit correction payments of £10 million per annum (H1 2016-17 £5 million) until at least the date on which the March 2018 valuation is completed (no later than 30 September 2018).

**Dividends**

The final dividend of 15.1 pence per share in respect of the 2015-16 financial year was paid on 29 July 2016, following shareholder approval.

The Board has declared an interim dividend of 7.4 pence per ordinary share, payable on 11 January 2017 to shareholders on the register at the close of business on 9 December 2016.

As previously stated, given the seasonality of the Group's business, the Board would expect to pay an interim dividend each year equal to approximately one-third of the prior year's total dividend and to set the final dividend for each year in light of the full year performance of the Group.

## Underlying change

Movements in revenue, costs, profits and margins are shown on an underlying basis. Underlying movements take into account differences in working days in UKPIL (H1 2016-17 152.8; H1 2015-16 152.0) and movements in foreign exchange in GLS (H1 2016-17 £/€ 1.23; H1 2015-16 £/€ 1.39). In addition, adjustments are made for non-recurring or distorting items, which by their nature may be unpredictable, such as acquisitions. For volumes, underlying movements are adjusted for working days in UKPIL, ASM in GLS and exclude political parties' election mailings in letters volumes. For the nine months ending 25 December 2016, the number of working days in UKPIL is 230.3 (9M 2015-16 227.5). For 2016-17, the estimated impact of working days in UKPIL will be around £65 million (2016-17 305.6 days; 2015-16 303.0 days)

| (£m) | Adjusted 26 weeks ended 25 September 2016 | Re-presented Adjusted 26 weeks ended 27 September 2015 | Working days (UKPIL) | Wage legislation (UKPIL) | Foreign exchange (GLS) | Acquisitions (UKPIL & GLS) | Underlying 26 weeks ended 27 September 2015 | Underlying change |
|---|---|---|---|---|---|---|---|---|
| **Revenue** | | | | | | | | |
| UKPIL | 3,641 | 3,654 | 19 | - | - | 4 | 3,677 | (1%) |
| GLS | 942 | 741 | - | - | 99 | 22 | 862 | 9% |
| **Group** | 4,583 | 4,395 | 19 | - | 99 | 26 | 4,539 | 1% |
| | | | | | | | | |
| **Group Costs** | | | | | | | | |
| People | (2,560) | (2,508) | - | (33) | (22) | (6) | (2,569) | Flat |
| Distribution & conveyance costs | (945) | (813) | - | - | (60) | (16) | (889) | 6% |
| Infrastructure costs | (417) | (395) | - | - | (7) | (3) | (405) | 3% |
| Other operating costs | (341) | (337) | - | - | (3) | (1) | (341) | Flat |
| Non-people costs | (1,703) | (1,545) | - | - | (70) | (20) | (1,635) | 4% |
| Operating costs before transformation costs | (4,263) | (4,053) | | (33) | (92) | (26) | (4,204) | 1% |
| **UKPIL** | | | | | | | | |
| People | (2,351) | (2,340) | - | (33) | - | (3) | (2,376) | (1%) |
| Distribution & conveyance costs | (370) | (361) | - | - | - | (1) | (362) | 2% |
| Infrastructure costs | (360) | (345) | - | - | - | - | (345) | 4% |
| Other operating costs | (313) | (318) | - | - | - | - | (318) | (2%) |
| Non-people costs | (1,043) | (1,024) | - | - | - | (1) | (1,025) | 2% |
| Operating costs before transformation costs | (3,394) | (3,364) | - | (33) | - | (4) | (3,401) | Flat |
| **GLS** | | | | | | | | |
| Operating costs | (869) | (689) | - | - | (92) | (22) | (803) | 8% |
| | | | | | | | | |
| **Profit, margins and EPS** | | | | | | | | |
| **Group** | | | | | | | | |
| Operating profit before transformation costs | 320 | 342 | 19 | (33) | 7 | - | 335 | (5%) |
| *Margin* | *7.0%* | *7.8%* | | | | | *7.4%* | *(40bps)* |
| Transformation costs | (58) | (94) | - | - | - | - | (94) | |
| Operating profit after transformation costs | 262 | 248 | 19 | (33) | 7 | - | 241 | 9% |
| *Margin* | *5.7%* | *5.6%* | | | | | *5.3%* | *40bps* |
| Profit before tax | 252 | 240 | | | | | 233 | - |
| Tax | (59) | (57) | | | | | (57) | - |
| Profit for the period | 193 | 183 | | | | | 176 | - |
| Profit attributable to equity holders of the parent Company | 192 | 181 | | | | | 174 | - |
| Group earnings per share (pence) | 19.2 | 18.1 | | | | | | |
| **UKPIL** | | | | | | | | |
| Operating profit before transformation costs | 247 | 290 | 19 | (33) | - | - | 276 | (11%) |
| *Margin* | *6.8%* | *7.9%* | - | - | - | - | *7.5%* | *(70bps)* |
| Transformation costs | (58) | (94) | - | - | - | - | (94) | |
| Operating profit after transformation costs | 189 | 196 | 19 | (33) | - | - | 182 | 3% |
| *Margin* | *5.2%* | *5.4%* | | | | | *5.0%* | *20bps* |
| **GLS** | | | | | | | | |
| Operating profit before transformation costs | 73 | 52 | - | - | 7 | - | 59 | 25% |
| *Margin* | *7.7%* | *70%* | | | | | *6.8%* | *90bps* |

# PRINCIPAL RISKS

The Board considers that the principal risks faced by the Group for the remaining six months of the financial year are substantially unchanged from those described at pages 32-35 of the Royal Mail plc Annual Report and Financial Statements 2015-16, except where noted below. In summary, our principal risks are:

- We may not be able to adequately respond to evolving customer behaviours or market changes.
- Flat or declining economic conditions could adversely impact letter and parcels revenues. Uncertainty leading up to and after the EU Referendum led to a reduction in UK marketing activity. We continue to monitor this as well as the wider economic impact following the Referendum vote.
- Our ability to manage the transition to new arrangements in respect of the Royal Mail Pension Plan.
- Material disagreements or disputes could lead to widespread industrial action.
- We might not achieve the effective control of costs and the efficiency benefits required to deliver our strategy.
- We may fail to attract and retain senior management and key personnel.
- We may be adversely impacted by Ofcom's fundamental review of postal services regulation.
- Changes to laws and regulations relating to employment, or their interpretation, could adversely affect the Group's labour costs.
- Cyber attacks could threaten the confidentiality, integrity and availability of data in our systems, and the reputation of the business.

One risk has been added to the list of principal risks:

- Our success in growing in new areas of business is dependent on such factors as our continued ability to identify new profitable and sustainable areas of business, implementing appropriate investments, and having in place suitable structures to support the continued transformation of the business.

The following risks are no longer considered to be material and have been removed from the list of principal risks:

- Failure to successfully transform our IT estate. We are close to successfully completing the transformation.
- Changes to VAT position. The circumstances giving rise to this risk have changed, reducing the risk to the business.

# CONDENSED CONSOLIDATED INCOME STATEMENT

| | Notes | **Reported[1] 26 weeks ended 25 September 2016 £m** | Reported[1,2] 26 weeks ended 27 September 2015 £m |
|---|---|---|---|
| **Continuing operations** | | | |
| **Revenue** | 2 | **4,583** | 4,395 |
| Operating costs[3] | | **(4,377)** | (4,187) |
| People costs | | (2,674) | (2,642) |
| Distribution & conveyance costs | | (945) | (813) |
| Infrastructure costs | | (417) | (395) |
| Other operating costs | | (341) | (337) |
| **Operating profit before transformation costs** | | **206** | 208 |
| Transformation costs | | **(58)** | (94) |
| **Operating profit after transformation costs** | | **148** | 114 |
| Operating specific items: | | | |
| Employee Free Shares charge | | **(79)** | (76) |
| Legacy/other (costs)/credit | | **(11)** | 2 |
| **Operating profit** | | **58** | 40 |
| Non-operating specific items: | | | |
| Profit on disposal of property, plant and equipment | | **4** | 27 |
| Loss on disposal of business | | **(2)** | - |
| **Earnings before interest and tax** | | **60** | 67 |
| Finance costs | | **(11)** | (9) |
| Finance income | | **1** | 1 |
| Net pension interest (non-operating specific item) | 3 | **60** | 57 |
| **Profit before tax** | | **110** | 116 |
| Tax charge | | **(23)** | (26) |
| **Profit for the period from continuing operations** | | **87** | 90 |
| **Discontinued operations** | | | |
| Profit from disposal of discontinued operations (non-operating specific item) | | **-** | 31 |
| Tax on profit from disposal of discontinued operations | | **-** | (5) |
| **Profit for the period** | | **87** | 116 |
| | | | |
| **Profit for the period attributable to:** | | | |
| Equity holders of the parent Company | | **86** | 114 |
| Non-controlling interests | | **1** | 2 |
| | | | |
| **Earnings per share** | 4 | | |
| Basic – continuing operations | | **8.6p** | 8.8p |
| Diluted – continuing operations | | **8.6p** | 8.7p |
| Basic – total Group | | **8.6p** | 11.4p |
| Diluted – total Group | | **8.6p** | 11.3p |

[1] Reported - prepared in accordance with International Financial Reporting Standards (IFRS).
[2] The sub-analysis of operating costs has been re-presented as detailed in Note 2. Total operating costs remain unchanged.
[3] Operating costs are stated before transformation costs, Employee Free Shares charge and Legacy/other (costs)/credit.

# CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | Notes | **Reported 26 weeks ended 25 September 2016 £m** | Reported 26 weeks ended 27 September 2015 £m |
|---|---|---|---|
| **Profit for the period** | | **87** | 116 |
| Other comprehensive income/(expense) for the period from continuing operations: | | | |
| **Items that will not be subsequently reclassified to profit or loss:** | | | |
| Amounts relating to pensions accounting | | **727** | (164) |
| IFRIC 14 adjustment relating to defined benefit surplus | 3 | 120 | (85) |
| Remeasurement gains/(losses) of the defined benefit surplus | 3 | 787 | (157) |
| Tax on above items | | (180) | 78 |
| **Items that may be subsequently reclassified to profit or loss** | | | |
| Foreign exchange translation differences | | **17** | (1) |
| Exchange differences on translation of foreign operations (GLS) | | 58 | (4) |
| Net (loss)/gain on hedge of a net investment (€500 million bond – 2.375% Senior Fixed Rate Notes due July 2024) | | (39) | 3 |
| Net loss on hedge of a net investment (Euro denominated finance lease payables) | | (3) | - |
| Tax on above items | | 1 | - |
| Designated cash flow hedges | | **23** | (3) |
| Gains/(losses) on cash flow hedges deferred into equity | | 17 | (18) |
| Losses on cash flow hedges released from equity to income | | 11 | 15 |
| Tax on above items | | (5) | - |
| Total other comprehensive income/(expense) for the period from continuing operations | | **767** | (168) |
| Total other comprehensive income for the period from discontinued operations | | **-** | - |
| **Total comprehensive income/(expense) for the period** | | **854** | (52) |
| **Total comprehensive income/(expense) for the period attributable to:** | | | |
| Equity holders of the parent Company | | **853** | (54) |
| Non-controlling interests | | **1** | 2 |

# CONDENSED CONSOLIDATED BALANCE SHEET

| | Notes | **Reported At 25 September 2016 £m** | Reported At 27 March 2016 £m |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | | **2,008** | 2,002 |
| Goodwill | | **262** | 206 |
| Intangible assets | | **515** | 451 |
| Investments in associates and joint venture | | **8** | 9 |
| Financial assets | | | |
| Pension escrow investments | | **20** | 20 |
| Derivatives | | **6** | 2 |
| Retirement benefit surplus – net of IFRIC 14 adjustment | 3 | **4,282** | 3,430 |
| Other receivables | | **13** | 12 |
| Deferred tax assets | | **15** | 9 |
| | | **7,129** | 6,141 |
| **Assets held for sale** | | **45** | 39 |
| **Current assets** | | | |
| Inventories | | **25** | 21 |
| Trade and other receivables | | **960** | 1,020 |
| Income tax receivable | | **16** | 6 |
| Financial assets | | | |
| Derivatives | | **7** | 5 |
| Cash and cash equivalents | | **248** | 368 |
| | | **1,256** | 1,420 |
| **Total assets** | | **8,430** | 7,600 |
| **Current liabilities** | | | |
| Trade and other payables | | **(1,529)** | (1,700) |
| Financial liabilities | | | |
| Interest-bearing loans and borrowings | | **(102)** | - |
| Obligations under finance leases | | **(64)** | (84) |
| Derivatives | | **(19)** | (33) |
| Income tax payable | | **(34)** | (23) |
| Provisions | | **(100)** | (151) |
| | | **(1,848)** | (1,991) |
| **Non-current liabilities** | | | |
| Financial liabilities | | | |
| Interest-bearing loans and borrowings | | **(436)** | (392) |
| Obligations under finance leases | | **(118)** | (136) |
| Derivatives | | **(2)** | (8) |
| Provisions | | **(103)** | (96) |
| Other payables | | **(49)** | (41) |
| Deferred tax liabilities | | **(660)** | (469) |
| | | **(1,368)** | (1,142) |
| **Total liabilities** | | **(3,216)** | (3,133) |
| **Net assets** | | **5,214** | 4,467 |
| **Equity** | | | |
| Share capital | | **10** | 10 |
| Retained earnings | | **5,160** | 4,451 |
| Other reserves | | **37** | (3) |
| Equity attributable to parent Company | | **5,207** | 4,458 |
| Non-controlling interests | | **7** | 9 |
| **Total equity** | | **5,214** | 4,467 |

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | Share capital £m | Retained earnings £m | Foreign currency translation reserve £m | Hedging reserve £m | Equity holders of the parent £m | Non-controlling interests £m | Total equity £m |
|---|---|---|---|---|---|---|---|
| Reported at 29 March 2015 | 10 | 3,993 | 14 | (30) | 3,987 | 9 | 3,996 |
| Profit for the period | - | 114 | - | - | 114 | 2 | 116 |
| Other comprehensive expense for the period | - | (164) | (1) | (3) | (168) | - | (168) |
| Total comprehensive income/(expense) for the period | - | (50) | (1) | (3) | (54) | 2 | (52) |
| Dividend paid to equity holders of the parent Company | - | (143) | - | - | (143) | - | (143) |
| Dividend paid to non-controlling interests | - | - | - | - | - | (2) | (2) |
| Share-based payments | | | | | | | |
| Employee Free Shares issue[1] | - | 73 | - | - | 73 | - | 73 |
| Save As You Earn (SAYE) scheme | - | 1 | - | - | 1 | - | 1 |
| Long-Term Incentive Plan (LTIP)[2] | - | 1 | - | - | 1 | - | 1 |
| Reported at 27 September 2015 | 10 | 3,875 | 13 | (33) | 3,865 | 9 | 3,874 |
| Profit for the period | - | 127 | - | - | 127 | 5 | 132 |
| Other comprehensive income for the period | - | 419 | 9 | 8 | 436 | - | 436 |
| Total comprehensive income for the period | - | 546 | 9 | 8 | 563 | 5 | 568 |
| Release of Post Office Limited separation provision | - | 5 | - | - | 5 | - | 5 |
| Dividend paid to equity holders of the parent Company | - | (70) | - | - | (70) | - | (70) |
| Dividend paid to non-controlling interests | - | - | - | - | - | (5) | (5) |
| Share-based payments | | | | | | | |
| Employee Free Shares issue[1] | - | 79 | - | - | 79 | - | 79 |
| Save As You Earn (SAYE) scheme | - | 2 | - | - | 2 | - | 2 |
| Long-Term Incentive Plan (LTIP)[2] | - | 14 | - | - | 14 | - | 14 |
| **Reported at 27 March 2016** | 10 | 4,451 | 22 | (25) | 4,458 | 9 | 4,467 |
| **Profit for the period** | **-** | **86** | **-** | **-** | **86** | **1** | **87** |
| **Other comprehensive income for the period** | **-** | **727** | **17** | **23** | **767** | **-** | **767** |
| **Total comprehensive income for the period** | **-** | **813** | **17** | **23** | **853** | **1** | **854** |
| **Dividend paid to equity holders of the parent Company** | **-** | **(149)** | **-** | **-** | **(149)** | **-** | **(149)** |
| **Dividend paid to non-controlling interests** | **-** | **-** | **-** | **-** | **-** | **(8)** | **(8)** |
| **Acquisition of non-controlling interests** | **-** | **(13)** | **-** | **-** | **(13)** | **-** | **(13)** |
| **Recognition of put options for non-controlling interests** | **-** | **(14)** | **-** | **-** | **(14)** | **-** | **(14)** |
| **Disposal of subsidiary** | **-** | **-** | **-** | **-** | **-** | **(1)** | **(1)** |
| **Acquisition of subsidiary** | **-** | **-** | **-** | **-** | **-** | **6** | **6** |
| **Share-based payments** | | | | | | | |
| **Employee Free Shares issue[1]** | **-** | **76** | **-** | **-** | **76** | **-** | **76** |
| **Save As You Earn (SAYE) scheme** | **-** | **1** | **-** | **-** | **1** | **-** | **1** |
| **Long-Term Incentive Plan (LTIP)[2]** | **-** | **5** | **-** | **-** | **5** | **-** | **5** |
| **Purchase of own shares[3]** | **-** | **(10)** | **-** | **-** | **(10)** | **-** | **(10)** |
| **Reported at 25 September 2016** | **10** | **5,160** | **39** | **(2)** | **5,207** | **7** | **5,214** |

[1] Excludes £3 million (at 27 September 2015 £3 million, at 27 March 2016 £6 million) National Insurance, charged to the income statement, included in provisions on the balance sheet.

[2] Excludes £1 million (at 27 September 2015 £nil, at 27 March 2016 £1 million) National Insurance, charged to the income statement, included in provisions on the balance sheet.

[3] Includes £6 million in respect of LTIP and Employee Free Shares schemes and £4 million associated HMRC payments.

# CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

| | Reported 26 weeks ended 25 September 2016 £m | Reported 26 weeks ended 27 September 2015 £m |
|---|---|---|
| **Cash flow from operating activities** | | |
| **Profit before tax** | **110** | 116 |
| Adjustment for: | | |
| Net pension interest | **(60)** | (57) |
| Net finance costs | **10** | 8 |
| Profit on disposal of property, plant and equipment | **(4)** | (27) |
| Loss on disposal of business | **2** | - |
| Legacy/other costs/(credit) | **11** | (2) |
| Employee Free Shares charge | **79** | 76 |
| Transformation costs | **58** | 94 |
| **Operating profit before transformation costs** | **206** | 208 |
| Adjustment for: | | |
| Depreciation and amortisation | **145** | 135 |
| Share of post-tax loss from associates and joint venture | **1** | - |
| **EBITDA before transformation costs** | **352** | 343 |
| Working capital movements | **(143)** | (169) |
| (Increase)/decrease in inventories | (3) | 1 |
| Decrease in receivables | 106 | 73 |
| Decrease in payables | (231) | (259) |
| Net decrease in derivative assets | 2 | - |
| (Decrease)/increase in provisions (non-specific items) | (17) | 16 |
| Pension charge to cash difference adjustment | **114** | 134 |
| Share-based awards (SAYE and LTIP) charge adjustment | **6** | 2 |
| Cash cost of transformation operating expenditure[1] | **(60)** | (136) |
| Cash cost of operating specific items | **(47)** | (2) |
| **Cash inflow from operations** | **222** | 172 |
| Income tax paid | **(16)** | (9) |
| **Net cash inflow from operating activities** | **206** | 163 |
| **Cash flow from investing activities** | | |
| Finance income received | **2** | 2 |
| Proceeds from disposal of property (excluding London property portfolio), plant and equipment (non-operating specific item) | **7** | 34 |
| London property portfolio costs (non-operating specific item) | **(17)** | (8) |
| Proceeds from disposal of discontinued operations (non-operating specific item) | **-** | 41 |
| Disposal of business (non-operating specific item) | **(3)** | - |
| Purchase of property, plant and equipment[1] | **(62)** | (79) |
| Acquisition of business interests, net of cash acquired | **(55)** | (4) |
| Acquisition of non-controlling interests | **(13)** | - |
| Purchase of intangible assets (software)[1] | **(79)** | (84) |
| Payment of deferred consideration in respect of prior years' acquisitions | **(3)** | (3) |
| Net sale of financial asset investments (current) | **-** | 56 |
| **Net cash outflow from investing activities** | **(223)** | (45) |
| **Net cash (outflow)/inflow before financing activities** | **(17)** | 118 |
| **Cash flow from financing activities** | | |
| Finance costs paid | **(14)** | (13) |
| Purchase of own shares | **(6)** | - |
| Payment of capital element of obligations under finance lease contracts | **(46)** | (56) |
| Cash received on sale and leasebacks | **5** | 9 |
| New loans | **100** | - |
| Dividends paid to equity holders of the parent Company | **(149)** | (143) |
| Dividend paid to non-controlling interests | **(8)** | (2) |
| **Net cash outflow from financing activities** | **(118)** | (205) |
| **Net decrease in cash and cash equivalents** | **(135)** | (87) |
| Effect of foreign currency exchange rates on cash and cash equivalents | **15** | (1) |
| Cash and cash equivalents at the beginning of the period | **368** | 287 |
| **Cash and cash equivalents at the end of the period** | **248** | 199 |

[1] Items comprise total investment within In-year trading cash flow measure (see Financial Review).

# NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

**1. Basis of preparation**

The comparative figures for the year ended 27 March 2016 are not the Company's statutory accounts for that financial year. Those accounts have been reported on by the Company's auditor and delivered to the registrar of companies. The report of the auditor was (i) unqualified; (ii) did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying their report; and (iii) did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

This condensed set of unaudited financial statements has been prepared in accordance with IAS 34 'Interim Financial Reporting' as adopted by the European Union (EU).

The annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. As required by the Disclosure Guidance and Transparency Rules of the Financial Conduct Authority, this condensed set of financial statements has been prepared applying the accounting policies and presentation that were applied in the preparation of the Group's published consolidated financial statements for the year ended 27 March 2016, except for the changes detailed below.

**Significant accounting policies**

*Accounting standards adopted in 2016-17*

IFRS 11 (Amended) 'Accounting for Acquisitions of Interests in Joint Operations'

IAS 16 (Amended) and IAS 38 (Amended) 'Clarification of acceptable methods of depreciation and amortisation'

IAS 27 (Amended) 'Equity Method in Separate Financial Statements'

IAS 1 (Amended) 'Disclosure Initiative'

Annual Improvements 2012-2014

The adoption of these standards will not have a material impact on the financial performance or position of the Group.

The Directors do not expect that the adoption of any other new or amended standards issued during the reporting period that are not yet effective, will have a material impact on the financial performance or position of the Group in future periods.

**Reported performance**

The condensed consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU and as issued by the International Accounting Standards Board (IASB) (i.e. on a 'reported' basis). In previous reporting periods, adjustments have been made to 'reported' results to provide an 'adjusted' measure of performance in the income statement and selected Notes. Following the recent amendment to IAS 1 'Presentation of Financial Statements', these adjustments are now included in the Group's Financial Review (see page 13), with the exception of; the Segment information in Note 2, which still includes an 'adjusted' measure, as this is how performance is reported to the Chief Operating Decision Maker (CODM); and the earnings per share information in Note 4 as Management consider this a key measure that needs to be part of the notes to the financial statements.

**Additional non-GAAP line items**

In the reporting of financial information, the Group discloses certain line items in the financial statements (detailed below) that are not required under IFRS, the Generally Accepted Accounting Principles (GAAP) under which the Group reports. Management believe that these additional line items assist with the understanding of the performance of the business and they also provide a foundation for further adjustments to the 'reported' numbers as outlined in the Financial Review.

*Reported operating profit before transformation costs*

This is the operating profit not adjusted for the pension charge to cash difference adjustment (see Financial Review on page 15 for definition) and before transformation costs. This is a key performance indicator in the Corporate Balanced Scorecard which is used to determine employee incentives.

## 1. Basis of preparation (continued)

*Transformation costs*

These costs relate to the ongoing transformation of the business, and include voluntary redundancy, project costs and other transformation-related payments.

*Reported operating profit after transformation costs*

This is the operating profit not adjusted for the pension charge to cash difference adjustment and after transformation costs.

*Operating specific items*

These are recurring or non-recurring items of income or expense of a particular size and/or nature relating to the operations of the business that in Management's opinion require separate identification.

These include items that have resulted from events that are non-recurring in nature, even though related income/expense can be recognised in subsequent periods. These items currently include the charge for Employee Free Shares, legacy costs (for example, movements in the industrial diseases provision) and impairments.

*Non-operating specific items*

These are recurring or non-recurring items of income/expense of a particular size and/or nature which do not form part of the Group's trading activity and in Management's opinion require separate identification. These items include profit or loss on disposal of property, plant and equipment and businesses, the IAS 19 non-cash pension interest credit, and profit on disposal of discontinued operations.

*Earnings before interest, tax, depreciation and amortisation (EBITDA) before transformation costs*

This line item in the Condensed consolidated statement of cash flows is based on the 'Reported operating profit before transformation costs' (see above for definition) adjusted for non-cash items i.e. depreciation and amortisation and share of post-tax profit from the Group's associate and joint venture companies.

*Adjusted earnings per share*

Basic earnings per share, excluding operating and non-operating specific items and the pension charge to cash difference adjustment.

### Significant accounting judgements, estimates and assumptions

The preparation of the condensed consolidated financial statements requires Management to make various judgements, estimates and assumptions when determining the carrying value of certain assets and liabilities. The significant judgements and estimates applied by the Group in these condensed consolidated financial statements are consistent with those applied in the Annual Report and Financial Statements 2015-16.

### Going concern

The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for at least the next 12 months. Accordingly, they continue to adopt the going concern basis in preparing the financial statements for the 26 weeks ended 25 September 2016.

## 2. Segment information

The Group's operating segments are based on geographic business units whose primary services and products relate to the delivery of parcels and letters. These segments are evaluated regularly by the Chief Executive's Committee and the Royal Mail plc Board – the Chief Operating Decision Maker (CODM) as defined by IFRS 8 'Operating Segments' – in deciding how to allocate resources and assess performance.

In the period, following the acquisition of the minority shareholding (49 per cent) on 31 March 2016, Romec Limited, previously reported in the 'Other' segment, has been incorporated into the UKPIL segment, to better reflect how the segment's resources are managed and reported to the CODM. The 2015-16 comparative information has been restated accordingly. There has also been a re-presentation of £68 million costs between infrastructure costs and other operating costs in the Group income statement. Of the residual businesses previously included in the 'Other' segment, the Group disposed of its 51 per cent shareholding in NDC 2000 Limited on 24 April 2016 and the results of the Quadrant Catering Limited associate company do not materially impact Group results.

## 2. Segment information (continued)

The key measure of segment performance is operating profit before transformation costs (used internally for the Corporate Balanced Scorecard). This measure of performance is disclosed on an 'adjusted' basis i.e. excluding specific items and the pension charge to cash difference adjustment (see Note 1), which is consistent with how financial performance is measured internally and reported to the CODM.

Segment revenues have been attributed to the respective countries based on the primary location of the service performed. Trading between UKPIL and GLS is not material.

### Seasonality

Mail volumes are subject to seasonal variation. The Group's busiest period is from September to December, when there is an increase in marketing mail volumes as businesses seek to maximise sales in the period leading up to Christmas, an increase in parcel volumes as a result of online Christmas shopping and an increase in addressed letter volumes as a result of the delivery of Christmas cards. During this period the Group would expect to record higher revenue as greater volumes of letters and parcels are delivered through its networks. It also incurs higher costs as the Group, particularly in UKPIL, hires large numbers of temporary workers to assist in handling the increased workload. Other seasonal factors that can affect the Group's results of operations include the Easter period, the number of bank holidays in a reporting period and weather conditions. Within the year, mail volumes typically decline in the summer months due to the holiday period, and then increase during autumn through the peak period at Christmas.

| **26 weeks ended 25 September 2016** | **UK operations** | **Other European operations** | **Group** | | **Group** |
|---|---|---|---|---|---|
| | | **Adjusted** | | **Specific items[1] and pension adjustment** | **Reported** |
| **Continuing operations** | **UKPIL £m** | **GLS £m** | **Total £m** | **£m** | **Total £m** |
| Revenue | **3,641** | **942** | **4,583** | **-** | **4,583** |
| People costs | **(2,351)** | **(209)** | **(2,560)** | **(114)** | **(2,674)** |
| Non-people costs | **(1,043)** | **(660)** | **(1,703)** | **-** | **(1,703)** |
| **Operating profit before transformation costs** | **247** | **73** | **320** | **(114)** | **206** |
| Transformation costs | **(58)** | **-** | **(58)** | **-** | **(58)** |
| **Operating profit after transformation costs** | **189** | **73** | **262** | **(114)** | **148** |
| Operating specific items | | | | | |
| Employee Free Shares charge | **-** | **-** | **-** | **(79)** | **(79)** |
| Legacy/other costs | **-** | **-** | **-** | **(11)** | **(11)** |
| **Operating profit** | **189** | **73** | **262** | **(204)** | **58** |
| Non-operating specific items | | | | | |
| Profit on disposal of property, plant and equipment | **-** | **-** | **-** | **4** | **4** |
| Loss on disposal of business | **-** | **-** | **-** | **(2)** | **(2)** |
| **Earnings before interest and tax** | **189** | **73** | **262** | **(202)** | **60** |
| Net finance costs | **(9)** | **(1)** | **(10)** | **-** | **(10)** |
| Net pension interest (non-operating specific item) | **-** | **-** | **-** | **60** | **60** |
| **Profit before tax** | **180** | **72** | **252** | **(142)** | **110** |

[1] Specific items all relate to UKPIL.

## 2. Segment information (continued)

| 26 weeks ended 27 September 2015 | UK operations | Other European operations | Group | | Group |
|---|---|---|---|---|---|
| | | Adjusted | | Specific items[2] and pension adjustment | Reported |
| Continuing operations | UKPIL £m | GLS £m | Total £m | £m | Total £m |
| Revenue | 3,654 | 741 | 4,395 | - | 4,395 |
| People costs | (2,340) | (168) | (2,508) | (134) | (2,642) |
| Non-people costs | (1,024) | (521) | (1,545) | - | (1,545) |
| Operating profit before transformation costs | 290 | 52 | 342 | (134) | 208 |
| Transformation costs | (94) | - | (94) | - | (94) |
| Operating profit after transformation costs | 196 | 52 | 248 | (134) | 114 |
| Operating specific items | | | | | |
| Employee Free Shares charge | - | - | - | (76) | (76) |
| Legacy credit | - | - | - | 2 | 2 |
| Operating profit | 196 | 52 | 248 | (208) | 40 |
| Profit on disposal of property, plant and equipment (non-operating specific item) | - | - | - | 27 | 27 |
| Earnings before interest and tax | 196 | 52 | 248 | (181) | 67 |
| Net finance costs | (8) | - | (8) | - | (8) |
| Net pension interest (non-operating specific item) | - | - | - | 57 | 57 |
| Profit before tax | 188 | 52 | 240 | (124) | 116 |

[2] Specific items comprise £122 million charge in UKPIL and £2 million charge in GLS.

## 3. Retirement benefit plans

### Summary pension information

| | **26 weeks ended 25 September 2016 £m** | 26 weeks ended 27 September 2015 £m |
|---|---|---|
| **Ongoing UK pension service costs** | | |
| UK defined benefit plan (including administration costs)[1] | **(291)** | (320) |
| UK defined contribution plan | **(24)** | (22) |
| UK defined benefit and defined contribution Pension Salary Exchange (PSE)[2] | **(76)** | (23) |
| **Total UK ongoing pension service costs** | **(391)** | (365) |
| GLS defined contribution type plan costs | **(3)** | (2) |
| **Total Group ongoing pension service costs** | **(394)** | (367) |
| **Cash flows relating to ongoing pension service costs** | | |
| UK defined benefit plan employer contributions[3] | **(172)** | (181) |
| Defined contribution plan employer contributions | **(27)** | (24) |
| UK defined benefit and defined contribution plan employer PSE contributions | **(76)** | (23) |
| **Total Group cash flows relating to ongoing pension service costs** | **(275)** | (228) |
| **RMSEPP deficit correction payments** | **(5)** | (5) |
| **Pension charge to cash difference adjustment** | **(114)** | (134) |

[1] These pension service costs are charged to the income statement. They represent the cost (as a percentage of pensionable payroll – 28.8 per cent (2015-16 29.8 per cent)) of the increase in the defined benefit obligation due to members earning one more years' worth of pension benefits. They are calculated in accordance with IAS 19 and are based on market yields (high quality corporate bonds and inflation) at the beginning of the reporting year. Pensions administration costs for the RMPP of £3 million (H1 2015-16 £3 million) continue to be included within the Group's ongoing UK pension service costs.

[2] At the beginning of August 2015, PSE was introduced under which eligible employees who are enrolled into PSE opt out of making employee contributions to their pension and the Group makes additional contributions in return for a reduction in basic pay. As a result there is a decrease in wages and salaries and a corresponding increase in pension costs of £76 million (H1 2015-16 £23 million) for the 26 weeks ended 25 September 2016.

[3] The employer contribution cash flow rate (17.1 per cent in both the current and prior period) forms part of the payroll expense and is paid into the Royal Mail Pension Plan (RMPP). The contribution rate is set following each actuarial funding valuation, usually every three years. These actuarial valuations are required to be carried out on assumptions determined by the Trustee and agreed by Royal Mail.

## 3. Retirement benefit plans (continued)

### Long-term assumptions

The main assumptions used to calculate the accounting position of the pension plans are shown below.

| | At 25 September 2016 % | At 27 March 2016 % |
|---|---|---|
| Retail Price Index (RPI) | **3.0** | 3.0 |
| Consumer Price Index (CPI) | **2.0** | 2.0 |
| Discount rate | | |
| - nominal | **2.3** | 3.5 |
| - real (nominal less RPI)[4] | **(0.7)** | 0.5 |

[4] The real discount rate used reflects the long average duration of the RMPP of around 30 years.

### Accounting and actuarial surplus position (RMPP and RMSEPP)

The combined plans' assets and liabilities are shown below.

| | Accounting (IAS 19) | | Actuarial/cash funding | |
|---|---|---|---|---|
| | **At 25 September 2016 £m** | At 27 March 2016 £m | **At 30 September 2016 £m** | At 31 March 2016 £m |
| Fair value of plans' assets[5] | **9,992** | 7,374 | **10,033** | 7,442 |
| Present value of plans' liabilities | **(5,701)** | (3,815) | **(8,469)** | (5,665) |
| **Surplus in plans (pre IFRIC 14 adjustment)** | **4,291** | 3,559 | **1,564** | 1,777 |
| IFRIC 14 adjustment | **(9)** | (129) | **n/a** | n/a |
| **Surplus in plans** | **4,282** | 3,430 | **1,564** | 1,777 |

[5] Difference between accounting and actuarial/cash funding asset fair values arises from the different period end dates used for the valuation of the assets under both methods.

There is no element of the present value of the plans' liabilities above that arises from plans that are wholly unfunded. The actuarial liabilities are calculated specifically for these financial statements and as such are required within a relatively short timeframe, which can lead to differences in the approximations and assumptions used compared with the plan actuary's funding updates.

In the current period, the surplus in RMPP is assumed to be recoverable as a reduction to future employer contributions. Therefore, no IFRIC 14 adjustment is required. The Directors do not believe that the current excess of pension plan assets over the liabilities on an accounting basis will result in an excess of pension assets on a funding basis. However, the Directors are required to account for the pension plan based on their legal right to benefit from a surplus, using long-term actuarial assumptions current at the reporting date, as required by IFRS.

As RMSEPP is closed to future accrual, the surplus is assumed to be available as a refund as per IFRIC 14 and, as such, is shown net of taxation withheld.

### Sensitivity analysis for RMPP liabilities

The RMPP liabilities are sensitive to changes in key assumptions. The potential impact of the largest sensitivities on the RMPP liabilities is as follows:

| **Key assumption change** | **Potential increase in liabilities £m** |
|---|---|
| Additional one year of life expectancy | **190** |
| Increase in inflation rate (both RPI and CPI simultaneously) of 0.1% p.a. | **150** |
| Decrease in discount rate of 0.1% p.a. | **150** |
| Increase in CPI assumption (assuming RPI remains constant) of 0.1% p.a. | **30** |

This sensitivity analysis has been determined based on a method that assesses the impact on the defined benefit obligation, resulting from reasonable changes in key assumptions occurring at the end of the reporting period. Changes inverse to those in the table (e.g. an increase in discount rate) would have the opposite effect on liabilities.

### 3. Retirement benefit plans (continued)

Changes in the value of the defined benefit pension liabilities, fair value of the plans' assets and the net defined benefit surplus are analysed as follows:

| | Defined benefit asset | | Defined benefit liability | | Net defined benefit surplus | |
|---|---|---|---|---|---|---|
| | **At 25 September 2016 £m** | At 27 March 2016 £m | **At 25 September 2016 £m** | At 27 March 2016 £m | **At 25 September 2016 £m** | At 27 March 2016 £m |
| **Retirement benefit surplus (pre IFRIC 14 adjustment) at 28 March 2016 and 30 March 2015** | **7,374** | 6,619 | **(3,815)** | (3,237) | **3,559** | 3,382 |
| **Amounts included in the income statement** | | | | | | |
| Ongoing UK defined benefit pension plan and administration costs (included in people costs) | **(3)** | (6) | **(349)** | (694) | **(352)** | (700) |
| Pension interest income/(cost)[6] | **132** | 240 | **(72)** | (127) | **60** | 113 |
| Total included in profit before tax | **129** | 234 | **(421)** | (821) | **(292)** | (587) |
| **Amounts included in other comprehensive income – remeasurement gains/(losses)** | | | | | | |
| Actuarial gain/(loss) arising from: | | | | | | |
| Financial assumptions | **-** | - | **(1,558)** | 102 | **(1,558)** | 102 |
| Experience adjustment | **-** | - | **72** | 186 | **72** | 186 |
| Return on plans' assets (excluding interest income) | **2,273** | 32 | **-** | - | **2,273** | 32 |
| Total remeasurement gains/(losses) of the defined benefit plans | **2,273** | 32 | **(1,486)** | 288 | **787** | 320 |
| **Other** | | | | | | |
| Employer contributions | **245** | 488 | **-** | - | **245** | 488 |
| Employee contributions | **3** | 48 | **(3)** | (48) | **-** | - |
| Benefits paid | **(27)** | (47) | **27** | 47 | **-** | - |
| Curtailment costs | **-** | - | **(2)** | (45) | **(2)** | (45) |
| Movement in pension-related accruals | **(5)** | - | **(1)** | 1 | **(6)** | 1 |
| Total other movements | **216** | 489 | **21** | (45) | **237** | 444 |
| **Retirement benefit surplus (pre IFRIC 14 adjustment) at 25 September 2016 and 27 March 2016** | **9,992** | 7,374 | **(5,701)** | (3,815) | **4,291** | 3,559 |

[6] Pension interest income results from applying the plans' discount rate at 27 March 2016 to the plans' assets at that date. Similarly, the pension interest cost results from applying the plans' discount rate at 27 March 2016 to the plans' liabilities at that date.

## 4. Earnings per share

| | 26 weeks ended 25 September 2016 | | 26 weeks ended 27 September 2015 | |
|---|---|---|---|---|
| | **Reported** | **Adjusted** | Reported | Adjusted |
| Attributable to equity holders of the parent Company | | | | |
| Profit from continuing operations (£ million) | **86** | **192** | 88 | 181 |
| Weighted average number of shares issued (million) | **1,000** | **1,000** | 1,000 | 1,000 |
| Basic earnings per share (pence) | **8.6** | **19.2** | 8.8 | 18.1 |
| Diluted earnings per share (pence) | **8.6** | **19.1** | 8.7 | 18.0 |

The diluted earnings per share for the 26 weeks ended 25 September 2016 is based on a weighted average number of shares of 1,005,528,552 (H1 2015-16 1,004,627,886) to take account of the issue of potential ordinary shares resulting from the Long-Term Incentive Plan (LTIP) for certain senior management and the Save As You Earn (SAYE) scheme. Shares held in an Employee Benefit Trust for the settlement of options and awards to current and former employees are treated as treasury shares for accounting purposes. The Company, however, does not hold any shares in treasury.

## 5. Dividends

| | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 | **26 weeks ended 25 September 2016** | 26 weeks ended 27 September 2015 |
|---|---|---|---|---|
| **Dividends on Ordinary Shares** | **Pence per share** | Pence per share | **£m** | £m |
| Final dividends paid | **15.1** | 14.3 | **149** | 143 |
| **Total dividends paid** | **15.1** | 14.3 | **149** | 143 |

The final dividend of 15.1p was paid on 29 July 2016 to shareholders whose names appeared on the register of members on 1 July 2016.

## 6. Acquisition of businesses

Acquisitions made in the period for a total consideration of £58 million (H1 2015-16 £nil million) in respect of ASM and Revisecatch Limited (trading as eCourier) are not considered to be individually material and therefore the following disclosures are made on an aggregated basis. The following tables set out the provisional fair value of the identifiable assets and liabilities recognised as at the date of acquisition.

| | **26 weeks ended 25 September 2016 £m** |
|---|---|
| Tangible assets acquired | **4** |
| Intangible assets recognised on acquisition | **31** |
| Trade and other receivables | **23** |
| Cash and cash equivalents | **3** |
| Goodwill recognised on acquisition | **36** |
| **Total assets acquired** | **97** |
| Trade and other payables | **(26)** |
| Loans | **(7)** |
| Non-controlling interests | **(6)** |
| **Net assets acquired** | **58** |
| Cash paid during the period | **58** |
| Deferred consideration | **-** |
| **Total consideration** | **58** |

The fair value of trade debtors is equal to the gross contractual amounts receivable. An initial review of trade debtors has not indicated any recoverability issues.

The intangible assets recognised relate to customer lists, software and brands. The goodwill of £36 million (H1 2015-16 £nil million) arising on these acquisitions is indicative of the acquired business knowledge of products and markets, and synergies that are expected through the integration of services.

Revenue generated from these entities since the date of acquisition is £26 million and the combined profit is £nil million. If these combinations had taken place at the beginning of the financial year revenue generated would have been £48 million and the combined profit would have been £1 million.

### 6. Acquisition of businesses (continued)

There are no material non-controlling interests in relation to these acquisitions.

### 7. Contingent liabilities

On 28 July 2015, the Group received a Statement of Objections setting out Ofcom's provisional, preliminary findings in relation to its investigation into the terms on which the Group proposed to offer access to letter delivery services, alleging a potential distortion of competition. The investigation was launched in February 2014 following a complaint brought by TNT Post UK (now Whistl) about certain proposed changes to Royal Mail's Access contracts.

The Group has publically stated that it is considering Ofcom's provisional findings, and that it will robustly defend against Ofcom's allegations.

The Group is still not in a position to accurately predict when it will receive Ofcom's final decision nor has it received any detail as yet from Ofcom as to the quantum of any potential penalty (which will only be received if Ofcom intends to make an infringement finding). The Group continues to maintain that it has not infringed competition law and its representations to Ofcom have been on that basis.

### 8. Events after the reporting period

**Acquisition of Golden State Overnight Delivery Service Inc. (GSO)**

Subsequent to the reporting period end, on 4 October 2016 it was announced that General Logistics Systems (GLS), a subsidiary of Royal Mail plc had acquired 100 per cent of the shares of GSO, a leading provider of regional next day delivery services, principally in California, for a cash consideration of $90 million (approximately £70 million).

The financial statements of Royal Mail plc for the 52 week period to 26 March 2017 will include disclosure, in accordance with IFRS 3, of the consideration paid, the fair value of the net assets acquired and goodwill recognised, based on the initial accounting for the business combination being complete at that date. No fair value disclosure has been made in these financial statements as the acquisition balance sheet is still being compiled under the terms of the purchase agreement.

**Interim dividend**

The Board has declared an interim dividend of 7.4 pence per ordinary share (H1 2015-16 7.0 pence per share). The dividend amounts to £74 million (H1 2015-16 £70 million) and will be paid on 11 January 2017 to shareholders on the register at the close of business on 9 December 2016. The ex-dividend date is 8 December 2016.

# RESPONSIBILITY STATEMENT OF THE DIRECTORS IN RESPECT OF THE HALF YEAR FINANCIAL REPORT

We confirm that to the best of our knowledge:

- the condensed set of financial statements has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU; and
- the interim Financial Report includes a fair review of the information required by:

    (a) DTR 4.2.7R of the Disclosure Guidance and Transparency Rules, being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements; and a description of the principal risks and uncertainties for the remaining six months of the year; and

    (b) DTR 4.2.8R of the Disclosure Guidance and Transparency Rules, being related party transactions that have taken place in the first six months of the current financial year and that have materially affected the financial position or performance of the Company during that period; and any changes in the related party transactions described in the last annual report that could do so.

By order of the Board

| | |
|---|---|
| **Moya Greene** | **Matthew Lester** |
| Chief Executive Officer | Chief Finance Officer |
| 16 November 2016 | 16 November 2016 |

# INDEPENDENT REVIEW REPORT TO ROYAL MAIL PLC

**Introduction**

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the 26 weeks ended 25 September 2016 which comprises the Condensed consolidated income statement, the Condensed consolidated statement of comprehensive income, the Condensed consolidated statement of cash flows, the Condensed consolidated balance sheet, the Condensed consolidated statement of changes in equity, and the related explanatory notes. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with the terms of our engagement to assist the Company in meeting the requirements of the Disclosure and Transparency Rules ("the DTR") of the UK's Financial Conduct Authority ("the UK FCA"). Our review has been undertaken so that we might state to the Company those matters we are required to state to it in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our review work, for this report, or for the conclusions we have reached.

**Directors' responsibilities**

The half-yearly financial report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the half-yearly financial report in accordance with the DTR of the UK FCA.

As disclosed in Note 1, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the EU. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU.

**Our responsibility**

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

**Scope of review**

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity issued by the Auditing Practices Board for use in the UK. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

**Conclusion**

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the 26 weeks ended 25 September 2016 is not prepared, in all material respects, in accordance with IAS 34 as adopted by the EU and the DTR of the UK FCA.

**Richard Pinckard**
**for and on behalf of KPMG LLP**
*Chartered Accountants*
15 Canada Square
London
E14 5GL

16 November 2016

## FORWARD-LOOKING STATEMENTS

This document contains certain forward-looking statements concerning the Group's business, financial condition, results of operations and certain of the Group's plans, objectives, assumptions, projections, expectations or beliefs with respect to these items. Forward-looking statements are sometimes, but not always, identified by their use of a date in the future or such words as 'anticipates', 'aims', 'due', 'could', 'may', 'will', 'should', 'expects', 'believes', 'intends', 'plans', 'potential', 'targets', 'goal' or 'estimates'.

Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the Group's actual financial condition, performance and results to differ materially from the plans, goals, objectives and expectations set out in the forward-looking statements included in this document. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements.

By their nature, forward-looking statements relate to events and depend on circumstances that will occur in the future and are inherently unpredictable. Such forward-looking statements should, therefore, be considered in light of various important factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements. These factors include, among other things: changes in the economies and markets in which the Group operates; changes in the regulatory regime within which the Group operates; changes in interest and exchange rates; the impact of competitive products and pricing; the occurrence of major operational problems; the loss of major customers; undertakings and guarantees relating to pension funds; contingent liabilities; the impact of legal or other proceedings against, or which otherwise affect, the Group; and risks associated with the Group's overseas operations.

All written or verbal forward-looking statements, made in this document or made subsequently, which are attributable to the Group or any persons acting on their behalf are expressly qualified in their entirety by the factors referred to above. No assurance can be given that the forward-looking statements in this document will be realised; actual events or results may differ materially as a result of risks and uncertainties facing the Group. Subject to compliance with applicable law and regulation, the Group does not intend to update the forward-looking statements in this document to reflect events or circumstances after the date of this document, and does not undertake any obligation to do so.