

Directors' report

REPORT ON THE AFFAIRS OF THE GROUP

The Directors present their Annual Report on the affairs of the Group together with the financial statements and auditor's report for the year ended 31 December 2017. The Corporate Governance statement set out on pages 49 to 57 forms part of this report.

An indication of likely future developments in the business of the Company and details of research and development activities are included in the Strategic Report. The Group's policies relating to equality, diversity and employee consultation can be found in the 'Sustainable and responsible business' section of the Strategic Report on pages 35 to 37.

Details of the proposed dividend are set out on page 28.

The Greenhouse gas emissions statement can be found on page 38.

Capital structure

Details of the issued share capital, together with details of the movements in the Company's issued share capital during the year, are shown in note 25. The Company has one class of ordinary shares which carries no right to fixed income. Each share carries the right to one vote at general meetings of the Company.

There are no specific restrictions on the size of a holding nor on the transfer of shares, which are both governed by the general provisions of the Articles of Association and prevailing legislation. The Directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or on voting rights.

Details of employee share schemes are set out in note 32.

No person has any special rights of control over the Company's share capital and all issued shares are fully paid.

With regard to the appointment and replacement of Directors, the Company is governed by its Articles of Association, the UK Corporate Governance Code, the Companies Act and related legislation. The Articles themselves may be amended by Special Resolution of the shareholders. The powers of Directors are described in the Main Board terms of reference, copies of which are available on request, and the Corporate Governance statement on page 56.

Treasury

The Group's policy enables it to use financial instruments to hedge foreign currency exposures. The main trading currency of the Group is the Pound Sterling. The Group's use of financial instruments and the related risks are discussed further in notes 19, 20 and 23.

At the 2017 AGM held on 16 May 2017, the Company's shareholders granted the Company authority to make one or more market purchases (within the meaning of section 693(4) of the Companies Act 2006) of ordinary shares of 10 pence each in the capital of the Company.

The Company did not purchase any shares for cancellation or to be held as treasury in 2016 or 2017.

Directors and their interests

The Directors who served during the year, and subsequent to the year-end, unless otherwise stated, were as follows:

Robin Williams – Chairman

Doug Edwards – Chief Executive Officer

Lily Liu – Chief Financial Officer and Company Secretary (appointed on 2 May 2017)

Ted Wiggans – Chief Operations Officer

Margaret Rice-Jones – Senior Independent Director

Chris Morgan – Non-Executive Director

Andrew Herbert – Non-Executive Director

Alex Bevis – Chief Financial Officer and Company Secretary (resigned on 29 March 2017)

Brief biographical descriptions of the Directors are set out on pages 40 and 41. Full details of their interests in shares of the Company and its subsidiary undertakings are included in the Directors' Remuneration report on pages 58 to 79.

Directors' report continued

REPORT ON THE AFFAIRS OF THE GROUP CONTINUED

Shareholdings in the Company

The interests of the Directors in the shares of the Company and its subsidiaries (all of which are beneficial) as at 31 December 2017 are as follows:

	Number of ordinary shares of 10p each 31 December 2017	Number of ordinary shares of 10p each 31 December 2016
Doug Edwards	33,885	32,913
Lily Liu	14,000	–
Ted Wiggans	71,239	71,239
Robin Williams	10,000	4,000
Margaret Rice-Jones	5,700	5,700
Chris Morgan	–	–
Andrew Herbert	–	–

There have been no changes in the Directors' interests in shares of the Company between 31 December 2017 and 21 March 2018. Directors' interests in options over shares in the Company are shown in the Directors' Remuneration report.

Directors' liabilities

The Company has granted an indemnity to all of its Directors against liability in respect of any potential proceedings that may be brought by third parties, subject to the conditions set out in the Companies Act 2006. Such qualifying third party indemnity provision remains in force as at the date of approving the Directors' report.

Share capital

As at 31 December 2017 the Company had been notified in accordance with Chapter 5 of the Financial Conduct Authority's (FCA's) Disclosure and Transparency Rules of the following material interests in its share capital:

	Number of ordinary shares held	Percentage of issued share capital
AXA Framlington Investment Managers	11,139,285	14.22%
T Rowe Price Global Investments	7,324,672	9.35%
Legal & General Investment Management	7,115,856	9.08%
M&G Investment Management	6,755,669	8.62%
Oppenheimer Funds	4,000,000	5.11%
Aberdeen Standard Investments	3,887,118	4.96%
Baillie Gifford	3,740,692	4.78%
Schroder Investment Management	3,607,743	4.61%
Generation Investment Management	3,586,998	4.58%
Majedie Asset Management	1,712,431	2.19%

During the period 31 December 2017 to 21 March 2018, the Company received the following notifications pursuant to chapter five of the FCA's Disclosure and Transparency Rules:

On 7 March 2018 and 20 March 2018, the Company received notifications from Legal & General Assurance (Pensions Management) Limited (part of Legal & General Investment Management), advising that their interests in the total voting rights of the Company were 3,116,780 ordinary shares, being 3.98% of the issued share capital at 7 March 2018, and 3,303,412 ordinary shares, being 4.22% of the issued share capital at 20 March 2018. The overall Legal & General Investment Management interests in the total voting rights of the Company were 9.06% and 9.31% respectively of the issued share capital at the dates of notification.

Annual General Meeting

The notice convening the Annual General Meeting is set out on pages 135 to 138. Resolutions 1 to 11 set out in the notice of the meeting deal with the ordinary business to be transacted at the meeting. The special business to be transacted at the meeting is set out in Resolutions 12 to 14.

Re-election of Directors

Resolutions 5 to 10

The Company's Articles of Association require the Directors to retire by rotation at least once every three years, with the number to retire by rotation at each Annual General Meeting being the number nearest to but not exceeding one third of the Board. However, the UK Corporate Governance Code provides that all Directors of FTSE 350 companies should be subject to re-election by their shareholders every year. In accordance with this provision of the UK Corporate Governance Code and in keeping with the Board's aim of following best corporate governance practice, the Board has decided that, as at recent Annual General Meetings of the Company, all Directors should retire at each Annual General Meeting and offer themselves for re-election.

Directors' Remuneration report

Resolution 11

This Resolution seeks shareholder approval for the Directors' Remuneration report, which includes the remuneration policy. The Directors' Remuneration report can be found on pages 58 to 79 (inclusive) of the Annual Report and Financial Statements.

In accordance with regulations which came into force on 1 October 2013, Resolution 11 offers shareholders an advisory vote on the implementation of the Company's existing remuneration policy.

Authority to purchase own shares

Resolution 12

It is proposed by Resolution 12, by Special Resolution, to authorise the Company generally and unconditionally to purchase its own shares at a price of not less than the par value of the shares and not more than the higher of:

- (i) 5% above the average of the middle market quotations of the shares as derived from the London Stock Exchange Daily Official List for the five dealing days immediately preceding the day on which the purchase is made; and
- (ii) the amount stipulated by article 5(1) of the Buy-back and Stabilisation Regulation 2003 (in each case exclusive of any expenses payable by the Company).

The authority will be for a maximum of 14.9% of the Company's issued share capital and will expire at the earlier of the next Annual General Meeting of the Company or within 15 months from the date of the passing of this resolution. The Directors currently have no intention to exercise the authority and will only purchase shares if it is in the best interests of shareholders as a whole.

The total number of options to subscribe for ordinary shares outstanding at 21 March 2018 (including options awarded under LTIP which may be satisfied by subscription of new shares) was 2,946,231. This represents 4% of the issued ordinary share capital at that date. If Xaar plc was to buy back the maximum number of ordinary shares permitted pursuant to the passing of this resolution, then the total number of options to subscribe for ordinary shares outstanding at 31 December 2017 would represent 4% of the reduced issued ordinary share capital.

Power to issue securities

Resolution 13

Under the Companies Act 2006 the Directors of the Company may only allot shares (whether for cash or otherwise) with the authority of shareholders given at a general meeting of the Company. In accordance with institutional guidelines, under Resolution 13, to be proposed as an Ordinary Resolution, authority is sought to allot shares:

- (i) in relation to a pre-emptive rights issue only, up to an aggregate nominal amount of £5,221,953.00, which represented two thirds of the Company's ordinary share capital as at 21 March 2018; and
- (ii) in any other case, up to an aggregate nominal amount of £2,610,976.60, which represented one third of the Company's ordinary share capital as at 21 March 2018.

The Directors do not currently have an intention to exercise the authority.

Directors' report continued

REPORT ON THE AFFAIRS OF THE GROUP CONTINUED

Resolution 14

This resolution, to be proposed as a Special Resolution, will give the Directors power to allot shares:

- (i) up to an aggregate nominal amount of £5,221,953.00 (representing approximately 66% of the Company's issued share capital) on an offer to existing shareholders on a pre-emptive basis (subject to any adjustments, such as for fractional entitlements and overseas shareholders, as the Directors see fit); and
- (ii) for cash up to a maximum aggregate nominal value of £783,292.90, representing 10% of the ordinary share capital of the Company as at 21 March 2018, otherwise than in connection with an offer to existing shareholders.

In previous years, the Directors have sought, and been granted, power to allot equity securities for cash free from pre-emption rights (otherwise than in connection with a rights issue or similar pre-emptive issue) up to a maximum nominal amount representing approximately 5% of the Company's issued ordinary share capital. Such power has given the Directors the ability to allot equity securities for cash non pre-emptively in any circumstances. The limitation of the disapplication power to a maximum of 5% of the Company's issued ordinary share capital accorded with best practice as set out in The Pre-Emption Group's Statement of Principles on the Disapplication of Pre-Emption Rights (July 2008).

In March 2015, The Pre-Emption Group published a revision of its Statement of Principles. In addition to restating the existing 5% disapplication limit, the 2015 Statement of Principles introduced greater flexibility for companies to undertake non pre-emptive issues for cash in connection with acquisitions and specified capital investments. This relaxation is intended to allow companies the opportunity to finance expansion opportunities as and when they arise.

Accordingly, the 2015 Statement of Principles provides that a company may now seek power to issue on a non-pre-emptive basis for cash equity securities representing (i) no more than 5% of the Company's issued ordinary share capital in any one year; and (ii) no more than an additional 5% of the Company's issued ordinary share capital provided that such additional power is only used in connection with an acquisition or specified capital investment.

Accordingly, in line with the 2015 Statement of Principles (which have been endorsed by The Investment Association), the Directors are seeking power to allot equity securities for cash (otherwise than in connection with a rights issue or similar pre-emptive issue) up to a maximum nominal amount of £783,292.90, representing approximately 10% of the Company's issued ordinary share capital as at 21 March 2018 (being the latest practicable date prior to publication of this document). Whilst the Directors may use up to one half of this amount to issue equity securities for cash non pre-emptively in any circumstances, they confirm that they would only use the other half in connection with an acquisition or a specified capital investment which is announced contemporaneously with the issue, or which has taken place in the preceding six-month period and is disclosed in the announcement of the issue.

The Directors also confirm their intention to adhere to the provisions of the 2015 Statement of Principles regarding cumulative use of authorities within a rolling three year period. Those Principles provide that equity securities should not be allotted for cash on a non-pre-emptive basis (other than pursuant to a rights issue or pre-emptive offer) in excess of an amount equal to 7.5% of the total issued ordinary share capital of the Company in any rolling three year period, without prior consultation with the Company's shareholders. This limit excludes any equity securities issued pursuant to a specific disapplication of pre-emption rights and any equity securities issued pursuant to a general disapplication of pre-emption rights in connection with an acquisition or specified capital investment.

The Directors do not currently have an intention to exercise any power given to them by shareholders to allot shares for cash on a non-pre-emptive basis.

The authorities contained in Resolutions 13 and 14 will expire no later than 15 months after the passing of those resolutions.

Additional information for shareholders

The following provides the additional information required for shareholders as a result of the implementation of the Takeovers Directive into UK law.

The structure of the Company's issued share capital is shown in note 25.

Details of ordinary shares held in trust owned by the Company can be found in note 27.

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities and/or voting rights.

The Directors are authorised to issue and allot shares and to undertake purchases of the Company's shares. Appropriate resolutions to renew these authorities are proposed to be passed at the AGM as detailed above and notice of which is on pages 135 to 138.

Ordinary shares

On a show of hands at a general meeting of the Company every holder of ordinary shares present in person and entitled to vote shall have one vote for every ordinary share held and, on a poll, every member present in person or by proxy and entitled to vote shall have one vote for every ordinary share held. The notice of the AGM on pages 135 to 138 specifies deadlines for exercising voting rights either by proxy notice or present in person or by proxy in relation to resolutions to be passed at the AGM. All proxy votes are counted and the numbers for, against or withheld in relation to each resolution are made available at the AGM and are published on the Company's website after the meeting. No person holds securities carrying special rights with regard to control of the Company.

Restrictions

There are no restrictions on the transfer of ordinary shares in the Company other than:

- Certain restrictions may from time to time be imposed by laws and regulations (for example, insider trading laws and market requirements relating to close periods)
- Pursuant to the Listing Rules of the FCA whereby all employees of the Company require the approval of the Company to deal in the Company's securities.

The Company's Articles of Association may only be amended by a Special Resolution at a general meeting of the shareholders. Directors are reappointed by Ordinary Resolution at a general meeting of the shareholders.

Appointment of Directors

The Board can appoint a Director but anyone so appointed must be elected by an Ordinary Resolution at the next general meeting. All Directors are required to submit themselves for reappointment every year at the AGM.

Significant interests

Directors' interests in the share capital of the Company are shown in the table on page 44. Major interests (i.e. those greater than 3%) of which the Company has been notified are shown on page 44.

Company share schemes

The Xaar plc ESOP Trust holds 1.7% of the issued share capital of the Company in trust for the benefit of employees of the Group and their dependants. The voting rights in relation to these shares are exercised by the Trustees.

Change of control

The Company is not party to any agreements which take effect, alter or terminate upon a change of control of the Company following a takeover bid. There are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment (whether through resignation, purported redundancy or otherwise) that occurs because of a takeover bid. Depending on the achievement of performance conditions, share-based payment arrangements may vest on change of control but this is subject to the approval and exercise of the discretion of the Remuneration Committee.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 16 to 21 and 34. Notes 19, 20 and 23 include a description of the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future, based on the Group's forecasts and projections for the next 12 months, taking account of reasonably possible changes in trading performance. For this reason, we continue to adopt the going concern basis in preparing the financial statements.

Directors' report continued

REPORT ON THE AFFAIRS OF THE GROUP CONTINUED

Viability statement

The long term viability of the Company is assessed by the Directors as part of the risk management process and regular strategic reviews. As well as continually monitoring and managing risk the Directors lead a comprehensive review of the principal risks to the Company at least annually. This review, which also involves key individuals from all areas of the business, was last performed in January 2018. The Company's strategy is regularly discussed by the Board and is biannually subject to a full review.

The Directors' assessment of the Company's viability has been made with reference to the strategic planning documented on pages 16 to 21 and 34. The Company's strategic plans are based on the four strategic pillars which underpin the Company's vision for 2020. Strategic plans for the whole Company and each of the pillars are updated taking into consideration assumptions concerning existing and future products and technology, customer engagements, business relationships, partnership opportunities and the commercial, technological and macro-economic risks. The strategic plan for the Company is approved by the Executive Committee which tracks both current and forecast performance against this plan.

The Company is aware that it operates in an uncertain environment and faces risks both internally and externally that could potentially impact on the Company's ability to achieve its strategy. The principal risks and uncertainties faced by the Company are included on pages 29 to 33. As part of the process of reviewing these risks, and other potential risks, the Board assigns responsibility for these to members of the Executive Committee. It is the responsibility of the Executive Committee members to manage the risk and the mitigating actions. This process is supplemented with strong internal controls and processes. This combination ensures that the Company manages the risks it faces appropriately and that these are considered in all of the financial models.

Taking account of the Company's current financial position, operating performance, and the principal risks and uncertainties, the Directors have assessed the prospects of the Company, and confirm that they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due for the next four years, to December 2021.

Auditor

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to reappoint them will be proposed at the forthcoming AGM.

Directors' statement as to disclosure of information to auditor

The Directors who were members of the Board at the time of approving the Directors' report are listed on page 43.

Having made enquiries of fellow Directors, each of these Directors confirm that:

- To the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the Group's auditor is unaware
- Each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Group's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Approval

The Directors' report was approved by the Board on 21 March 2018 and is signed on its behalf by:



Lily Liu
Chief Financial Officer and
Company Secretary