K3 Business Technology Group plc

Unaudited Half Yearly Report for the six months to 31 December 2015

World Class Software. World Class Service.

K3 Business Technology Group plc

K3 is the UK's leading supplier of integrated business systems encompassing mission critical business software*, Customer Relationship Management (CRM) software, Business Intelligence and e-commerce, hosting and managed services to the retail, manufacturing and distribution sectors. Focussed on these markets, we support more than 3,000 customers in over 30 countries.

*Enterprise Resource Planning (ERP)

AIM: KBT
k3btg.com

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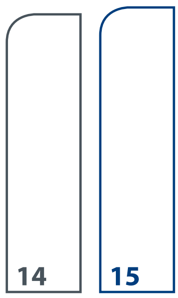
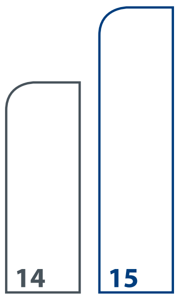


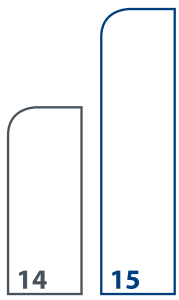
Revenue
£42.29m

2014: £41.67m



Adjusted
Profit Before Tax*1
£4.72m

2014: £3.56m



Adjusted
Earnings Per Share*2
12.0p

2014: 8.4p

Operational Key Points

- Continued encouraging progress as business transitions to increase own IP content – strong growth in chosen focus areas of own IP, channel sales and hosting
- Major new orders remained buoyant at £11.3m (2014: £12.3m)
- Channel partner sales – a key to accelerating growth – progressing very well, with first major contracts with Global Systems Integrators ("GSIs")
- Major endorsement from Microsoft – membership of elite Microsoft Dynamics 'Inner Circle' – supports channel partner sales strategy and relationships with GSIs
- Hosting and managed services activities growing well and bolstered by the acquisition of Starcom in April 2015
- Board remains confident regarding future prospects

*1 Calculated before amortisation of acquired intangibles of £1.60m (2014: £1.61m) and exceptional reorganisation costs of £0.85m (2014: £0.16m).

*2 Calculated before amortisation of acquired intangibles (net of tax) of £1.28m (2014: £1.29m) and exceptional reorganisation costs (net of tax) of £0.68m (2014: £0.13m).

Chairman's Statement

K3's half year trading results are in line with management expectations, and show a significant improvement in profitability... This reflects a strong performance from our retail activities and cloud hosting as well as the benefits of reorganisation changes.

Overview

K3's half year trading results are in line with management expectations, and show a significant improvement in profitability with adjusted profit before tax*[1] up 33% to £4.72m (2014: £3.56m) (36% with constant currency). This reflects a strong performance from our retail activities and cloud hosting as well as the benefits of reorganisation changes, which helped lift the Group's gross margin percentage to 55.6% from 50.7% in the same period last year. As expected, Group revenues at £42.29m (2014: £41.67m) were affected by the shift towards cloud-based consumption licensing and the weaker Euro.

We continue to be very encouraged by the progress we are making in driving sales in areas we have chosen to focus on, which are our own IP software products, channel sales and hosting. We are particularly pleased with the major orders for our fashion retail product on Microsoft Dynamics AX. As a result of this strong sales performance, our own IP product software licence revenue of £4.89m accounted for 25% (2014: 23%) of all product software licence revenue sold in the period. Total revenues derived from our own IP amounted to £9.56m which represents approximately 23% of the Group's total sales and importantly, the gross margin percentage on this income also improved to 65.5% from 63.9%.

A key part of our growth plans for K3 is to drive sales of our own IP software products through channel partners as well as through our own direct sales teams. We are making excellent progress here and, as we previously reported, in September 2015, we received our first order through a Global Systems Integrator ("GSI") for our "ax|is fashion" product. The order was our largest so far through our channel partner network and our first in Germany, Europe's largest market for fashion. Over the period, we signed three major contracts through GSIs and new channel partners, and continue to remain very confident of the significant opportunity that the channel represents. Microsoft's endorsement of K3 in July 2015 as member of its elite Microsoft Dynamics 'Inner Circle' supports the growing channel partner interest in our solutions and we are also engaging with Microsoft on potential opportunities.

Major new orders in the period remained encouraging, totalling £11.3m against a strong prior period (2014: £12.3m) and we have closed the half year with a pipeline of potential new deals valued at £56.5m (2014: £56.7m). This pipeline includes the remaining part of an initial order with a global fashion retailer which has the potential to grow significantly.

The business continues to deliver high levels of recurring revenues, which made up 47% of the Group's total revenues in the first half. At £19.72m (2014: £19.84m), they are mainly derived from annual software licence renewals, support contracts and hosting. I am also pleased to highlight the increase in gross margin percentage on this income which has risen to 70.0% from 63.9% in the comparative period.

We also focused on driving the growth of our cloud hosting and managed services activities. These operations are growing well and annualised subscription income is now at £8.2m, of which over £6.4m is from our cloud hosting operations. Our cloud hosting business has since won its largest ever order, and has a number of other contracts for implementation in the coming months.

Looking forward, we remain confident about the potential to exploit our own IP and expect to see continuing progress in our growth strategy. We also expect cloud-based consumption licensing to be an increasing feature of the Group's revenue mix, together with rising channel partner sales and hosting. As we seek to further develop the business, we also intend to consider acquisitions which enhance our existing product offering.

*See note 8 on page 20 for further details

Financial Results

	Revenue (£m)		Gross Margin (£m)		Gross Margin (%)	
	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m	Six months to 31 December 2015 %	Six months to 31 December 2014 %
Software licences	**6.88**	7.63	**4.54**	4.78	**66.0%**	62.6%
Services	**13.19**	11.93	**4.55**	3.18	**34.5%**	26.5%
Recurring*	**19.72**	19.84	**13.81**	12.68	**70.0%**	63.9%
Hardware and other	**2.50**	2.27	**0.62**	0.49	**24.8%**	21.6%
Total	**42.29**	41.67	**23.52**	21.11	**55.6%**	50.7%

	Six months to 31 December 2015	Six months to 31 December 2014	% change
Adjusted profit from operations*2 (£m)	**5.11**	4.11	+24%
Recurring revenue* as % of total revenues	**46.6%**	47.6%	-2%
Customer adds	**111**	81	+37%

**Recurring revenue: software maintenance renewals, support contracts, and hosting and managed services.*

K3 Intellectual Property

We highlight the revenue generated by K3's own IP below, which is included in the revenues above.

	Revenue	
	Six months to 31 December 2015 £m	Six months to 31 December 2014[iii] £m
K3 Product Licence[i]	**4.89**	4.54
K3 Product Related[ii]	**4.67**	4.53
Total K3 Product	**9.56**	9.07
Gross margin (£m)	**6.26**	5.80
Gross margin (%)	**65.5%**	63.9%

i) K3 Product Licence includes initial and annual software licences.
ii) K3 Product Related represents the additional identifiable revenues which flow directly from our K3 Product sales.
iii) Adjusted to reflect reclassification of £0.35m from product licence to product related.

"A key part of our growth plans for K3 is to drive sales of our own IP software products, through channel partners as well as through our own direct sales teams"

*See note 8 on page 20 for further details

For the six months to 31 December 2015, total revenues rose by 1% to £42.29m (2014: £41.67m) affected by consumption licencing and a weakening Euro. Recurring revenues, from software maintenance renewals, support contracts, hosting and managed services, accounted for 47% of the Group's income and totalled £19.72m (2014: £19.84m). Services revenue was up 11% to £13.19m (2014: £11.93m) and reflected strong activity levels following the excellent close to the last financial year. Software licence sales at £6.88m (2014: £7.63m) represented a good performance against a record result in the prior year and as expected, the current year has seen an increase in consumption-based licencing.

Results show a significant year-on-year improvement in gross margin which increased by 11% to £23.52m (2014: £21.11m) with the gross percentage margin rising to 56% (2014: 51%). This improvement reflects the benefits of the initiatives we implemented to reduce resourcing costs for implementations through in-house training and near-shore resourcing. The gross margin on recurring income also benefitted from the higher margin on our hosting and managed services businesses and a reduced impact of Microsoft embed partner margin. Overhead costs[*2] increased to £18.4m (2014: £17.0m) and includes an additional £1.0m of personnel cost, £0.2m of additional premises costs and £0.1m of additional development cost amortisation.

Adjusted profit from operations[*3] increased by 24% to £5.11m (2014: £4.11m). Key drivers in this improvement were the reorganisations and management changes we announced in September 2015 at a cost of £0.85m (2014: £0.16m). These costs are reported as exceptional in these results and have contributed to a step change in the performance of our retail operation. The charge for amortisation of acquired intangibles was £1.60m, in line with the prior year.

Net finance expenses decreased to £0.39m (2014: £0.55m) as a result of reduced debt and the impact of currency.

Adjusted profit before tax[*3] rose by 33% to £4.72m (2014: £3.56m) and adjusted earnings per share[*4] increased by 43% to 12.0p (2014: 8.4p).

Reported profit before tax increased by 27% to £2.28m (2014: £1.79m) with basic earnings per share rising by 51% to 5.9p (2014: 3.9p). There was a net tax charge for the period of £0.41m (2014: £0.57m) after the benefit of a £0.14m deferred tax credit (2014: £0.12m).

Cash flow and banking

Net debt at 31 December 2015 decreased by 13% to £10.45m (2014: £12.07m). Cash flow from operations was up 16% at £4.97m (2014: £4.30m) reflecting the higher profit in the period and management of working capital. In what is traditionally our stronger half year for cash generation due to SYSPRO annual licence billings, the adjusted cash flow generated from operations[*5] increased to 114% (2014: 109%) of adjusted operating profit[*3]. Net cash absorbed by financing in the period was £1.36m (2014: £3.06m net generated from refinancing).

The expenditure on capitalised development increased to £2.17m (2014: £1.75m) as we continued to execute our strategy of building our own product IP. Expenditure on fixed assets was £0.57m (2014: £0.33m) and deferred consideration on acquisitions cost a further £0.03m (2014: £nil).

Dividend

In line with the Group's dividend policy, no interim dividend will be declared but the Directors intend to propose a progressive final dividend.

Board Change

In December 2015, we were delighted to welcome Jonathan Manley to the Board as a Non-executive Director. He has over 35 years' experience in IT, both in the UK and US including at Harrods Ltd, where he is currently leading an IT change program, John Lewis and Estee Lauder. He replaces Peter Cookson who retired from the Board with our grateful thanks for all his hard work and contribution to K3.

Outlook

We are starting to see the benefits of our focus on own IP come through in increased Group profitability, channel partner sales and hosting, and remain very excited about ongoing opportunities.

As part of our growth strategy we will continue to invest significantly in developing our product offerings and also intend to consider acquisitions which complement our existing activities. As we have previously noted, cloud-based subscription models are becoming increasingly important to us as customers move towards consumption-based licensing. While this shift away from traditional on-premise models means that income from contracts is recognised over longer periods rather than upfront, the lifetime value has the potential to be significantly higher. The estimate of this lifetime value will be a key metric for monitoring the development of the business going forward.

The pipelines across both our retail and manufacturing and distribution activities remain very healthy and we are confident that K3 will continue to make good progress with its growth plans.

Lars-Olof Norell
Chairman
21 March 2016

*See note 8 on page 20 for further details

Operational Review

Our new elevated status as a member of the Microsoft Dynamics Inner Circle will greatly assist our strategy to drive global sales

Results Overview By Industry Sector

The operational results for the Group are summarised by industry sector as follows:

	Revenue		Adjusted profit	
	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m
Retail*6	**19.72**	19.63	**2.51**	1.06
Manufacturing & Distribution*7	**22.57**	22.04	**2.99**	3.40
Head Office	**–**	–	**(0.39)**	(0.35)
Total	**42.29**	41.67	**5.11**	4.11

"We are starting to see the benefits of our focus on own IP come through in increased Group profitability, channel partner sales and hosting."

*See note 8 on page 20 for further details

Retail Activities

Results Overview

	Revenue (£m) Six months to 31 December 2015 £m	Revenue (£m) Six months to 31 December 2014 £m	Gross Margin (£m) Six months to 31 December 2015 £m	Gross Margin (£m) Six months to 31 December 2014 £m	Gross Margin (%) Six months to 31 December 2015 %	Gross Margin (%) Six months to 31 December 2014 %
Software licences	**4.50**	4.08	**3.13**	2.87	**69.6%**	70.3%
Services	**7.68**	7.63	**2.34**	1.57	**30.5%**	20.6%
Recurring*	**6.20**	6.78	**4.39**	3.84	**70.8%**	56.6%
Hardware and other	**1.34**	1.14	**0.40**	0.28	**29.9%**	24.6%
Total	**19.72**	19.63	**10.26**	8.56	**52.0%**	43.6%

	Six months to 31 December 2015	Six months to 31 December 2014	% change
Adjusted profit from operations*6 (£m)	**2.51**	1.06	+137%
Recurring revenue* as % of total revenues	**31.4%**	34.5%	-9%
Customer adds	**51**	33	+55%

**Recurring revenue: from software maintenance renewals, support contracts, and hosting and managed services.*

Intellectual Property

	Revenue Six months to 31 December 2015 £m	Revenue Six months to 31 December 2014[iii] £m
K3 Product Licence[i]	**3.13**	2.62
K3 Product Related[ii]	**4.49**	4.32
Total K3 Product	**7.62**	6.94
Gross margin (£m)	**4.47**	3.84
Gross margin (%)	**58.7%**	55.4%

i) K3 Product Licence includes initial and annual software licences.
ii) K3 Product Related represents the additional identifiable revenues which flow directly from our K3 Product sales.
iii) Adjusted to reflect reclassification of £0.35m from product licence to product related.

"We were... delighted to sign our first contract for "ax|is" through a Global Systems Integrator ("GSI")."

*See note 8 on page 20 for further details

Retail Performance

Our retail operations performed strongly overall, with adjusted profit from operations[*6] more than doubling to £2.51m (2014: £1.06m) on revenues of £19.72m (2014: £19.63m). Encouragingly, revenue attributable to our own IP has risen by 10% to £7.62m from £6.94m in 2014.

The significant improvement in profitability was driven by both higher software licence sales and the initiatives we put in place to reduce the cost of software implementations. While trading conditions in the Dutch fashion and retail market and the weaker Euro hampered results, the cost base reductions we made in Holland at the beginning of the period helped to offset this effect.

Software sales at £4.50m were up 10% year on year with the 70% gross margin on these sales reflecting the own IP content of the deals. Services revenues at £7.68m were in line with the prior year with gross margin significantly increased to 30.5% (2014: 20.6%) as implementation costs reduced. While recurring revenues decreased to £6.2m (2014: £6.78m) because of the lower number of multi-year enhancement deals, the gross margin percentage increased significantly to 70.8% from 56.6%. This reflected the increase in own IP in the revenue mix, a reduced impact from the low margin Microsoft Embed (OEM) programme and higher margin on support renewals.

Major new orders in the period totalled £6.6m (2014: £6.8m).

We continued to drive sales across all our retail solutions, however a key focus remains on our own IP and, in particular, delivering the full potential of our "ax|is" product, which we consider is significant. An important element of our growth strategy is to expand sales through channel partners as well as through our own direct sales teams. We were therefore delighted to sign our first contract for "ax|is" through a Global Systems Integrator ("GSI") in the period. The deal secured with TriStyle, a leading European mail order fashion retailer, via a GSI in Germany was the largest order secured to date through our channel partner network. It was also K3's first win in Germany, the largest market for fashion in Europe. We subsequently signed two further major channel partner contracts for "ax|is fashion" in the period. This included a second win in Germany with one of Germany's largest online fashion retailers, KLiNGEL. We are also now well advanced with initial work on a contract for a large global fashion retailer which has potential to deliver significant annual revenue in future years.

In the second quarter, we signed a major deal with a new customer, to provide our Microsoft Dynamics NAV retail software suite on a hosted consumption basis. The contract is notable because it was our first major cloud-based subscription model win. As we have previously indicated, we expect to see an increasing shift in the way we sell our solutions, away from traditional 'on-premise' sales to the 'consumption' model as customers move towards adopting cloud hosted systems. This move towards more consumption based delivery is underscored by Microsoft's move to launch its new version of AX for a six month period via the cloud on its Azure platform.

Our business with IKEA was also strong in the period, with a good mix of licence, support and services from Inter IKEA and the concept franchisees following the extension of our strategic partnership in 2014 through to 2020, which included a multi-year enhancement licence commitment. At the lower end of the Retail market we were also encouraged by the excellent performance of our Retail Essential Solutions, which focuses on "events and venues" and is a flourishing section of the UK retail market, as well as our Unisoft Dutch business which focuses on smaller retailers in Benelux.

Reflecting the importance of our IP and channel partner strategy, during the period, we established a core IP team. This team is solely focused on developing our innovative core solutions for sale through our channel partner network. We see the expansion of this activity as a key part of our strategy to improve profitability and replace lower margin services income. As indicated in our last annual report, we took steps to tackle performance issues in our services centric Dutch fashion and retail business and rationalised our retail management structure at a cost of £0.66m.

Retail Prospects

We remain very positive about the global sales potential of our "ax|is" offering and our new elevated status as a member of the Microsoft Dynamics Inner Circle will greatly assist our strategy to drive global sales, both directly and indirectly through an international network of channel partners.

Our pipeline as we entered the second half of the financial year stands at a healthy £26.3m (2014: £28.7m) and with potential deals across both "ax|is fashion" and our more established solutions, we believe that our retail operations will continue to make encouraging progress.

*See note 8 on page 20 for further details

Manufacturing and Distribution Activities

Results Overview

	Revenue (£m)		Gross Margin (£m)		Gross Margin (%)	
	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m	Six months to 31 December 2015 %	Six months to 31 December 2014 %
Software licences	**2.39**	3.54	**1.41**	1.91	**59.0%**	54.0%
Services	**5.50**	4.30	**2.21**	1.59	**40.2%**	37.0%
Recurring*	**13.52**	13.06	**9.42**	8.84	**69.7%**	67.7%
Hardware and other	**1.16**	1.14	**0.22**	0.21	**19.0%**	18.4%
Total	**22.57**	22.04	**13.26**	12.55	**58.8%**	56.9%

	Six months to 31 December 2015	Six months to 31 December 2014	% change
Adjusted profit from operations*7 (£m)	**2.99**	3.40	-12%
Recurring revenue* as % of total revenues	**59.9%**	59.3%	+1%
Customer adds	**60**	48	+25%

**Recurring revenue from software maintenance renewals, support contracts, and hosting and managed services.*

Intellectual Property

	Revenue	
	Six months to 31 December 2015 £m	Six months to 31 December 2014 £m
K3 Product Licence[i]	**1.76**	1.92
K3 Product Related[ii]	**0.18**	0.21
Total K3 Product	**1.94**	2.13
Gross margin (£m)	**1.80**	1.96
Gross margin (%)	**92.8%**	92.0%

i) K3 Product Licence includes initial and annual software licences.
ii) K3 Product Related represents the additional identifiable revenues which flow directly from our K3 Product sales.

“The outlook for our manufacturing and distribution activities is encouraging, supported by a very robust recurring income”

*See note 8 on page 20 for further details

Manufacturing and Distribution Performance

Our manufacturing and distribution activities performed robustly in the period, with revenues up by 2.4% to £22.57m. While adjusted profit from operations at £2.99m[*7] (2014: £3.40m) was impacted by order delays in some units, gross margins improved to 58.8% (2014: 56.9%). This reflected growth in hosting and efficiency improvements in the delivery of services.

Nearly 60% of this segment's revenue comprises recurring income which provides significant cash flow for the investment activities for the whole Group. (It also accounts for approximately 69% of the Group's total recurring income.) Recurring income increased by 4% to £13.52m in the period, with SYSPRO maintenance and support renewals continuing to account for the major part. SYSPRO renewal rates remained high at 98% (2014: 98%) and, as annual renewals are billed in October, revenues and cash flows from this segment are significantly weighted to the first half of the financial year.

Overheads increased by £1.03m following the investment in resources noted at the prior year end and the addition of Starcom.

Our SYSPRO business performed in line with expectations as we updated our core own IP products (Dataswitch Connectivity, Equator Payroll and Orchard Warehouse Management) and achieved initial sales through our channel partners. We expect to see continuing progress in these areas in the second half. Our hosting and managed services businesses continued to grow well, benefiting from the merger with Starcom, acquired in April 2015. The combined business has enabled us to provide hosting to different service level requirements and also to merge a number of on-premise support businesses under common management. The hosting operations now trade solely under the Starcom name.

New orders were encouraging at £4.7m (2014: £5.5m) although a number of larger software deals, which include own IP related revenues, moved into the second half.

SYSPRO™ Simplifying your Success

Services revenues rose 28% to £5.5m (2014: £4.3m) reflecting delivery of contracts signed in the prior year in SYSPRO, our NAV and AX manufacturing business, and in our hosting operation where Starcom has a small level of chargeable services. The NAV and AX business closed the half year with a strong pipeline, which we are now starting to see converting into orders since the period end. The Sage business delivered lower levels of services revenues reflecting the relatively low numbers of deal closures in the first four months of the period with margins also reduced as a result. In recent months though, we have seen an increase in the Sage prospects pipeline which provides encouragement for the second half year.

Our hosting and managed services operation is performing well with the addition of Starcom boosting our delivery capabilities. Now part of a merged hosting operation, we estimate that it added approximately £1.5m to sales and £0.2m to adjusted operating profit[*8] in the period. Hosting and managed services contributed £3.79m of recurring revenues in the period (2014: £2.73m) and the closing contracted run rate of subscription income has increased by 29% to £8.22m (2014: £6.36m). This run rate now includes the major hosting contract referred to in our retail activities, running for an initial period of five years. The range of cloud hosting activities that we offer across a variety of products and price points is proving attractive to customers and we remain very optimistic about continuing growth prospects for our hosting and managed services business.

Manufacturing and Distribution Prospects

The outlook for our manufacturing and distribution activities is encouraging, supported by a very robust recurring income and a pipeline of prospects worth £30.2m at the period end (2014: £28.0m). In addition, we are continuing to focus strongly on the growth potential of our cloud hosting business.

*See note 8 on page 20 for further details

Central Costs

Head Office

Head office costs for the period were £0.49m (2014: £0.35m) with the increase reflecting investment in legal staff and consultancy as the business has expanded. Costs are stated net of recovery of elements recharged to the operating units.

Outlook

We continue to be optimistic about the performance of the Group as we transition to an increased product focus. We are encouraged by the progress we have made in the current period and will continue to seek ways to accelerate this process.

David Bolton
Chief Executive Officer

Consolidated Income Statement

for the six months ended 31 December 2015

	Notes	Unaudited Six months to 31 December 2015 £'000	Unaudited Six months to 31 December 2014 £'000	Audited Year to 30 June 2015 £'000
Revenue		**42,291**	41,669	83,427
Profit from operations before amortisation of acquired intangibles and exceptional reorganisation costs		**5,107**	4,108	8,151
Amortisation of acquired intangibles		**(1,595)**	(1,606)	(2,800)
Acquisition costs		**–**	–	(138)
Exceptional reorganisation costs		**(847)**	(158)	(408)
Profit from operations		**2,665**	2,344	4,805
Finance income		**18**	7	6
Finance expense		**(405)**	(558)	(932)
Profit before taxation		**2,278**	1,793	3,879
Tax expense	2	**(406)**	(574)	(436)
Profit for the period		**1,872**	1,219	3,443

All of the profit for the period is attributable to equity holders of the parent.

	Notes			
Earnings Per Share	3			
Basic		**5.9p**	3.9p	10.9p
Diluted		**5.8p**	3.8p	10.7p

Consolidated Statement of Comprehensive Income

for the six months ended 31 December 2015

	Unaudited Six months to 31 December 2015 £'000	Unaudited Six months to 31 December 2014 £'000	Audited Year to 30 June 2015 £'000
Profit for the period	**1,872**	1,219	3,443
Other comprehensive income (expense)			
Exchange differences on translation of foreign operations	**703**	(421)	(2,226)
Other comprehensive income (expense), net of tax	**703**	(421)	(2,226)
Total comprehensive income for the period	**2,575**	798	1,217

All of the total comprehensive income for the period is attributable to equity holders of the parent. All of the other comprehensive income will be reclassified subsequently to profit or loss when specific conditions are met.

Consolidated Statement of Financial Position

as at 31 December 2015

	Notes	Unaudited As at 31 December 2015 £'000	Unaudited As at 31 December 2014 £'000	Audited As at 30 June 2015 £'000
ASSETS				
Non-current assets				
Property, plant and equipment		**2,414**	2,306	2,316
Goodwill		**43,808**	43,839	43,541
Other intangible assets		**20,483**	19,557	20,806
Deferred tax assets		**636**	418	736
Available-for-sale investments		**98**	98	98
Total non-current assets		**67,439**	66,218	67,497
Current assets				
Trade and other receivables		**32,522**	32,497	31,839
Cash and cash equivalents		**2,118**	1,366	1,895
Total current assets		**34,640**	33,863	33,734
Total assets		**102,079**	100,081	101,231
LIABILITIES				
Non-current liabilities				
Long-term borrowings	4	**9,131**	10,406	10,531
Other non-current liabilities	5	**494**	656	882
Deferred tax liabilities		**2,964**	3,056	3,437
Total non-current liabilities		**12,589**	14,118	14,850
Current liabilities				
Trade and other payables	6	**29,531**	28,875	29,405
Current tax liabilities		**354**	598	38
Short-term borrowings	4	**3,440**	3,034	3,443
Total current liabilities		**33,325**	32,507	32,886
Total liabilities		**45,914**	46,625	47,736
EQUITY				
Share capital		**7,965**	7,946	7,949
Share premium account		**9,524**	9,457	9,462
Other reserves		**10,448**	10,448	10,448
Translation reserve		**(1,294)**	(192)	(1,997)
Retained earnings		**29,522**	25,797	27,633
Total equity attributable to equity holders of the parent		**56,165**	53,546	53,495
Total equity and liabilities		**102,079**	100,081	101,231

Consolidated Statement of Cash Flows

for the six months ended 31 December 2015

	Notes	Unaudited Six months to 31 December 2015 £'000	Unaudited Six months to 31 December 2014 £'000	Audited Year to 30 June 2015 £'000
Cash flows from operating activities				
Profit for the period		**1,872**	1,219	3,443
Adjustments for:				
Share based payments charge		**4**	9	18
Depreciation of property, plant and equipment		**493**	451	916
Amortisation of intangible assets and development expenditure		**2,763**	2,670	4,690
Loss on sale of property, plant and equipment		**–**	–	2
Finance income		**(18)**	(7)	(6)
Finance expense		**405**	558	932
Tax expense		**406**	574	436
Increase in trade and other receivables		**(531)**	(4,030)	(3,031)
(Decrease) increase in trade and other payables		**(421)**	2,856	2,200
Cash generated from operations	7	**4,973**	4,300	9,600
Finance expense paid		**(392)**	(697)	(956)
Income taxes (paid) received		**(212)**	242	(264)
Net cash generated from operating activities		**4,369**	3,845	8,380
Cash flows from investing activities				
Acquisition of subsidiaries, net of cash acquired	7	**(25)**	(458)	(1,998)
Development expenditure capitalised		**(2,169)**	(1,748)	(3,806)
Purchase of other intangible assets		**–**	–	(78)
Purchase of property, plant and equipment		**(573)**	(326)	(680)
Finance income received		**–**	7	6
Net cash absorbed by investing activities		**(2,767)**	(2,525)	(6,556)
Cash flows from financing activities				
Net proceeds from issue of share capital		**78**	44	69
Proceeds from long-term borrowings		**–**	3,650	5,400
Payment of long-term borrowings		**(1,464)**	(625)	(1,875)
Payment of finance lease liabilities		**(4)**	(9)	(20)
Dividends paid		**–**	–	(397)
Net cash (absorbed by) generated from financing activities		**(1,390)**	3,060	3,177
Net change in cash and cash equivalents		**212**	4,380	5,001
Cash and cash equivalents at start of period		**1,895**	(2,997)	(2,997)
Exchange gains (losses) on cash and cash equivalents		**11**	(17)	(109)
Cash and cash equivalents at end of period		**2,118**	1,366	1,895

Consolidated Statement of Changes in Equity

for the six months ended 31 December 2015

	Share capital £'000	Share premium £'000	Other reserve £'000	Translation reserve £'000	Retained earnings £'000	Total equity £'000
At 1 July 2014	7,930	9,412	10,448	229	24,586	52,605
Changes in equity for six months ended 31 December 2014						
Share-based payment credit	–	–	–	–	9	9
Options exercised	16	45	–	–	–	61
Movement in own shares held	–	–	–	–	(17)	(17)
Profit for the period	–	–	–	–	1,219	1,219
Other comprehensive income for the period	–	–	–	(421)	–	(421)
At 31 December 2014	7,946	9,457	10,448	(192)	25,797	53,456
Changes in equity for six months ended 30 June 2015						
Share-based payment credit	–	–	–	–	9	9
Options exercised	3	5	–	–	–	8
Dividends to equity holders	–	–	–	–	(397)	(397)
Profit for the period	–	–	–	–	2,224	2,224
Other comprehensive income for the period	–	–	–	(1,805)	–	(1,805)
At 30 June 2015	7,949	9,462	10,448	(1,997)	27,633	53,495
Changes in equity for six months ended 31 December 2015						
Share-based payment credit	–	–	–	–	4	4
Options exercised	16	62	–	–	–	78
Movement in own shares held	–	–	–	–	13	13
Profit for the period	–	–	–	–	1,872	1,872
Other comprehensive income for the period	–	–	–	703	–	703
At 31 December 2015	7,965	9,524	10,448	(1,294)	29,522	56,165

Notes to the Unaudited Half Yearly Report

1 Basis of preparation

The consolidated interim financial information has been prepared in accordance with the accounting policies that are expected to be adopted in the Group's full financial statements for the year ending 30 June 2016 which are not expected to be significantly different to those set out in Note 1 of the Group's audited financial statements for the year ended 30 June 2015. These are based on the recognition and measurement principles of IFRS in issue as adopted by the European Union (EU) and are effective at 30 June 2016 or are expected to be adopted and effective at 30 June 2016. The financial information has not been prepared (and is not required to be prepared) in accordance with IAS 34. The accounting policies have been applied consistently throughout the Group for the purposes of preparation of this financial information.

The financial information in this statement relating to the six months ended 31 December 2015 and the six months ended 31 December 2014 has neither been audited nor reviewed pursuant to guidance issued by the Auditing Practices Board. The financial information for the year ended 30 June 2015 does not constitute the full statutory accounts for that period. The Annual Report and Financial Statements for the year ended 30 June 2015 have been filed with the Registrar of Companies. The Independent Auditors' Report on the Annual Report and Financial Statement for the year ended 30 June 2015 was unqualified, did not draw attention to any matters by way of emphasis, and did not contain a statement under 498(2) or 498(3) of the Companies Act 2006.

2 Tax expense

	Unaudited Six months to 31 December 2015 £'000	Unaudited Six months to 31 December 2014 £'000	Audited Year to 30 June 2015 £'000
Current tax expense			
UK corporation tax and income tax of overseas operations on profits for the period	**542**	693	597
Adjustment in respect of prior periods	**–**	–	103
Total current tax expense	**542**	693	700
Deferred tax expense			
Origination and reversal of temporary differences	**(136)**	(119)	(249)
Effect of change in rate of deferred tax	**–**	–	(15)
Total deferred tax income	**(136)**	(119)	(264)
Total tax expense	**406**	574	436

3 Earnings per share

The calculations of earnings per share are based on the profit for the financial period and the following numbers of shares:

	Unaudited Six months to 31 December 2015 Number of shares	Unaudited Six months to 31 December 2014 Number of shares	Audited Year to 30 June 2015 Number of shares
Weighted average number of shares:			
For basic earnings per share	**31,683,967**	31,620,805	31,637,381
Effects of employee share options and warrants	**508,458**	452,602	590,623
For diluted earnings per share	**32,192,425**	32,073,407	32,228,004

Adjusted earnings per share calculations have been computed because the directors consider that they are useful to shareholders and investors. These are based on the following profits and the above number of shares:

	Unaudited six months to 31 December 2015			Unaudited six months to 31 December 2014			Audited year to 30 June 2015		
	Earnings £'000	Per share amount basic p	Per share amount diluted p	Earnings £'000	Per share amount basic p	Per share amount diluted p	Earnings £'000	Per share amount basic p	Per share amount diluted p
Earnings per share (eps)	**1,872**	**5.9**	**5.8**	1,219	3.9	3.8	3,443	10.9	10.7
Amortisation of acquired intangibles (net of tax)	**1,275**	**4.0**	**4.0**	1,285	4.1	4.0	2,240	7.1	7.0
Acquisition costs (net of tax)	**–**	**–**	**–**	–	–	–	138	0.4	0.4
Exceptional reorganisation costs (net of tax)	**678**	**2.1**	**2.1**	125	0.4	0.4	323	1.0	1.0
Adjusted eps	**3,825**	**12.0**	**11.9**	2,629	8.4	8.2	6,144	19.4	19.1

Notes to the Unaudited Half Yearly Report continued

4 Loans and borrowings

	Unaudited As at 31 December 2015 £'000	Unaudited As at 31 December 2014 £'000	Audited As at 30 June 2015 £'000
Non-current			
Bank loans (secured)	**9,127**	10,400	10,525
Finance lease creditors	**4**	6	6
	9,131	10,406	10,531
Current			
Bank loans (secured)	**2,796**	2,377	2,797
Finance lease creditors	**4**	17	6
Loans from related parties	**640**	640	640
	3,440	3,034	3,443
Total borrowings	**12,571**	13,440	13,974

The bank loans and other facilities include a multi-option facility which expires in August 2017.

5 Other non-current liabilities

	Unaudited As at 31 December 2015 £'000	Unaudited As at 31 December 2014 £'000	Audited As at 30 June 2015 £'000
Contingent consideration	**–**	25	25
Accruals	**494**	631	857
	494	656	882

6 Trade and other payables

	Unaudited As at 31 December 2015 £'000	Unaudited As at 31 December 2014 £'000	Audited As at 30 June 2015 £'000
Trade payables	**5,887**	4,652	7,602
Other payables	**292**	556	665
Accruals	**8,302**	8,246	7,875
Total financial liabilities, excluding loans and borrowings, classified as financial liabilities measured at amortised cost	**14,481**	13,454	16,142
Contingent consideration	**56**	18	75
Deferred consideration	**25**	25	25
Other tax and social security taxes	**4,194**	4,780	3,556
Deferred revenue	**10,775**	10,598	9,607
	29,531	28,875	29,405

7 Notes to the cash flow statement

Cash generated from operations is stated after exceptional reorganisation costs. The adjusted cash generated from operations has been computed because the directors consider it more useful to shareholders and investors in assessing the underlying operating cash flow of the Group. The adjusted cash generated from operations is calculated as follows:

	Unaudited Six months ended 31 December 2015 £'000	Unaudited Six months ended 31 December 2014 £'000	Audited Year ended 30 June 2015 £'000
Cash generated from operating activities	**4,973**	4,300	9,600
Add:			
Exceptional reorganisation costs	**847**	158	311
Adjusted cash generated from operations	**5,820**	4,458	9,911

Acquisition of subsidiaries and other business units, net of cash acquired comprises:

	Unaudited Six months ended 31 December 2015 £'000	Unaudited Six months ended 31 December 2014 £'000	Audited Year ended 30 June 2015 £'000
Initial consideration	**–**	(694)	(2,580)
Cash balances acquired	**–**	236	582
Contingent and deferred consideration paid	**(25)**	–	–
	(25)	(458)	(1,998)

Notes to the Unaudited Half Yearly Report continued

8 Notes to the Chairman's Statement and Operational Review

*1 Group adjusted profit before tax is calculated before amortisation of acquired intangibles of £1.60m (2014: £1.61m) and exceptional reorganisation costs of £0.85m (2014: £0.16m).

*2 Overhead costs are calculated before amortisation of acquired intangibles of £1.60m (2014: £1.61m) and exceptional reorganisation costs of £0.85m (2014: £0.16m).

*3 Group adjusted profit from operations is calculated before amortisation of acquired intangibles of £1.60m (2014: £1.61m) and exceptional reorganisation costs of £0.85m (2014: £0.16m).

*4 Group adjusted earnings per share is calculated before amortisation of acquired intangibles (net of tax) of £1.28m (2014: £1.29m) and exceptional reorganisation costs (net of tax) of £0.68m (2014: £0.13m).

*5 Group adjusted cash from operations is calculated before exceptional reorganisation costs of £0.85m (2014: £0.16m).

*6 Retail adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.31m (2014: £0.32m) and exceptional reorganisation costs of £0.65m (2014: £0.05m).

*7 Manufacturing and Distribution adjusted profit from operations is calculated before amortisation of acquired intangibles of £1.29m (2014: £1.29m) and exceptional reorganisation costs of £0.20m (2014: £0.10m).

*8 Starcom adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.10m.

9 The above information is being sent to the shareholders and is available from the Company's website, www.k3btg.com, and from its registered office: Baltimore House, 50 Kansas Avenue, Manchester M50 2GL.

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