K3 Business Technology Group plc

Unaudited Half Yearly Report for the six months to 31 December 2013

World Class Software. World Class Service.

K3 Business Technology Group plc

K3 is the UK's leading supplier of integrated business systems encompassing Enterprise Resource Planning (ERP) software, Customer Relationship Management (CRM) software, Business Intelligence and e-commerce, hosting and managed services to the supply chain industry. Focussed on the Retail, Manufacturing and Distribution markets, we support more than 3,000 customers in over 20 countries.

AIM: KBT
k3btg.com

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Chairman's Statement

Results show a major turnaround in the performance of the business which largely reflect the early progress we are making with our new Microsoft Dynamics AX solution, "ax|is"

Overview

Results for the first six months to 31 December 2013 show a major turnaround in the performance of the business, with revenue up by 9% to £34.47m and adjusted profit before tax*[1] up by 26% to £3.16m. These encouraging results largely reflect the early progress we are making with our new Microsoft Dynamics AX solution, "ax|is" (developed under the project name "Gemstone"). We are enriching Microsoft's Dynamics AX solution with our own IP for those specific market segments within the retail sector where we already have significant expertise. Our flagship software product is "ax|is fashion" aimed at the fashion sector, the second largest sector in retail after food. We are pleased to report that we secured major new orders with high profile retailers for "ax|is fashion" in the first half. Our base of reference customers for the new solution is now widening and we are very encouraged by the level of demand we are seeing.

There is further investment in software development to come in the second half and one of our next major objectives is to widen our channel to market so that we sell "ax|is" internationally, maximising the value of our IP via a strategic partner channel. We already have an international partner channel for our Pebblestone Microsoft Dynamics product, which gives us access to approximately 27 countries, and believe there is significant scope to extend this. At the same time, we also intend to develop strategic partnerships with large systems integrators and other Microsoft Dynamics partners. Our investment in widening our channel to market has already started and will continue in the second half and beyond. We are also investing in a programme of global recruitment and training to ensure that we have skilled AX resource as we increase sales. Demand is currently high for this skill set.

Our established Microsoft Dynamics NAV retail solution is continuing to see some recovery in demand, reflecting the improving conditions in the retail sector. Having closed two large deals at the end of the last financial year, we closed a further significant deal in the first half and have further deals we would hope to close in the second half. The contracts we secured for our Dynamics AX and Dynamics NAV solutions meant that the Microsoft UK Division closed £9.3m of new order wins compared to £0.6m in the same period last year, with £8.3m of this total representing orders for "ax|is". Total major new orders won across the Group in the first half was £12.7m (2012: £3.1m). This matches the total secured across the whole of the last financial year.

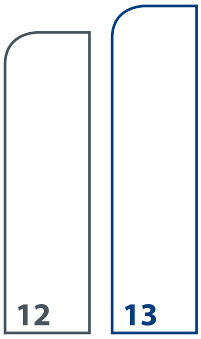
Our SYSPRO and Sage Division continues to deliver high levels of recurring income and good cash flows, with c. £5.5m of SYSPRO annual maintenance and support income benefiting the first half. New deals signed across the SYSPRO and Sage Division in the first half were up 29% to £2.64m helped by SYSPRO upgrades and Sage's X3 product. The disposal of a small non-core Sage business segment in May 2013 impacted reported revenue, and additional investment in resources also reduced profitability. It is worth noting that we are now delivering most new SYSPRO systems as part of a hosted cloud offering, with the hosting element of the sales being reported within Managed Services.

Our Managed Services Division benefited from the improved performance of our Microsoft UK Division and new SYSPRO sales, together with the recruitment of a small "operating system" team who have moved a legacy product offering into managed services. Revenues were up 15% over the prior year to £3.93m and the Division moved into profitability. As we have previously reported, the Division can now provide hosting solutions across all our major products and we have tailored our offering so that it is suitable for the needs of both large and small enterprises. This Division remains well positioned to benefit from further improvement in demand for our Microsoft and SYSPRO based solutions.

The Group continues to generate high levels of recurring revenues, from software licence renewals and support contracts, with recurring revenues increasing by 2% over the first half to £17.9m, which represented 52% of total revenues. Cash generation also remained robust and helped to support a 20% reduction in net debt at the period end to £9.91m compared to the same time in the prior year. This was after product investment of £1.95m and £0.58m of exceptional costs.

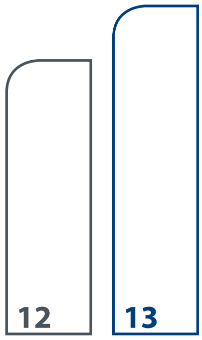
As we enter the second half year we continue to be encouraged by the Group's strong growth opportunities especially with our new Microsoft Dynamics AX based solution. The success we are having requires a major focus on the recruitment of quality resources, but we believe that our offering has the capability of becoming the "go-to" solution for retailers seeking a Microsoft AX solution and we are pleased to have Microsoft's support as we continue with our strategy to develop global channels to market.

*See note 8 on page 19 for further details



Revenue

£34.47m



Adjusted Profit
From Operations[*2]

£3.61m

Software sales increased by 53% to £5.69m (2012: £3.72m)

Adjusted eps rose by 18% to 7.7p (2012: 6.5p)

Financial Results

For the first six months to 31 December 2013, the Group generated revenues of £34.47m (2012: £31.55m), up by 9% on the prior period. Recurring revenues from software licence renewals and support contracts in the half year increased to £17.91m (2012: £17.60m) representing 52% (2012: 56%) of Group income. The growth of £0.3m was net of a disposal of £0.4m of non-core maintenance, indicating that the underlying growth in recurring revenue was 4%. Software sales increased by 53% to £5.69m (2012: £3.72m).

Adjusted profit from operations[*2] increased by 23% to £3.61m (2012: £2.94m). We incurred £0.58m (2012: £0.48m) of exceptional costs in relation to reorganisations in our Managed Services, Dynamics UK and Sage businesses. Further exceptional costs are expected in the second half relating to management changes since the period end. The charge for amortisation of intangibles was £1.71m (2012: £1.82m) with the reduction in charge due to certain acquisitions now being fully amortised.

Adjusted profit before tax[*3] rose by 26% to £3.16m (2012: £2.51m). Profit before tax increased to £0.88m (2012: £0.19m) reflecting the improvement in profit from operations and a broadly static finance cost year-on-year.

Adjusted earnings per share[*4] rose by 18% to 7.7p (2012: 6.5p) with basic earnings per share increasing to 2.9p (2012: 0.8p). Adjusted earnings per share[*4] is stated after amortisation of intangibles (net of tax) of £1.05m (2012: £1.22m), acquisition costs of £nil (2012: £0.03m) and reorganisation costs (net of tax) of £0.45m (2012: £0.36m). There was a net tax credit for the period of £0.02m (2012: £0.03m credit) after the benefit of a £0.45m deferred tax credit (2012: £0.34m) arising on the reversal of temporary tax timing differences and the reduction of tax rates in the UK.

*See note 8 on page 19 for further details

"Net debt reduced by 20% to £9.91m reflecting the Group's commitment to reduce borrowings"

Cash flow and banking

Net debt at the period end reduced by 20% to £9.91m (2012: £12.32m) reflecting the Group's commitment to reduce borrowings. Operating cash flow in the first half was £5.85m representing 162% of adjusted profit from operations*[5] (2012: £6.92m, representing 235%). The cash generation in the first half year is boosted by the SYSPRO licence and support contract renewals.

The expenditure on capitalised development increased to £1.95m (2012: £1.37m) but was in line with the expenditure in the second half of the year ended 30 June 2013 as the commitment to "ax|is" continued ahead of the launch of the first variant of the solution, "ax|is fashion", in November 2013.

Outstanding contingent consideration in respect of acquisitions in prior years has now reduced to £0.39m (2012: £1.04m). Whilst finance cost payments remained in line with prior year at £0.53m (2012: £0.52m) due to the impact of adverse foreign exchange movements, the Group benefited from £0.51m of tax repayments (2012: payments of £0.06m).

Dividend

In line with the Group's dividend policy, no interim dividend will be declared but the Directors intend to propose an increased final dividend with results for the full financial year, subject to the Group's trading performance.

The Directors intend to propose an increased final dividend subject to the Group's trading performance

*See note 8 on page 19 for further details

Operational Review

The financial results by operating division are summarised in the table below:

	Revenue Six months to 31 December 2013 £m	Revenue Six months to 31 December 2012 £m	Adjusted profit Six months to 31 December 2013 £m	Adjusted profit Six months to 31 December 2012 £m
Microsoft UK Division	**10.98**	8.47	**(0.18)**	(1.26)
International Division	**5.44**	5.39	**0.40**	0.47
Total Microsoft	**16.42**	13.86	**0.22**	(0.79)
SYSPRO and Sage Division	**14.12**	14.60	**3.67**	4.11
Managed Services Division	**3.93**	3.09	**0.10**	(0.16)
Head office costs	**–**	–	**(0.38)**	(0.22)
Total	**34.47**	31.55	**3.61**	2.94

Microsoft-based activities

The K3 Microsoft business, comprising our Microsoft UK Division and International Division, is working together on global initiatives to generate additional intellectual property, cost effective resourcing and improved channels to market. Revenue for the total Microsoft business has increased by 18% year-on-year to £16.42m (2012: £13.86m) and returned to profit, delivering £0.22m of adjusted profit from operations*6 (2012: adjusted loss from operations*6 of £0.79m).

The Division signed **four major orders** worth a combined **£8.3m**

Microsoft UK Division

The Division's performance recovered very strongly over the first half, fuelled by "ax|is" and improving retail sentiment. Divisional revenue increased by 30% to £10.98m (2012: £8.47m) and adjusted loss from operations*7 reduced by 86% to £0.18m (2012: £1.26m).

Having secured a number of pilot orders for our "ax|is" product at the end of the last financial year, the Division signed four major orders worth a combined £8.3m in the period, in both "ax|is fashion" and our core "ax|is" solution. These AX wins give the Division a good level of services income as we move into the second half of the year. Total order wins (including orders for our traditional NAV solution) for the first half amounted to £9.3m – a significant increase on the prior year (2012: £0.6m).

What has helped to drive our new AX orders is our IP, which has created a richer more enhanced enterprise resource planning ("ERP") solution for retailers. The product's excellent reception at the Microsoft Convergence conference in Barcelona in November 2013 was encouraging and helps our ongoing marketing efforts. It is worth noting that the average size of AX orders is significantly larger than for our traditional Microsoft Dynamics NAV business and that delivery is also over a more extended period. We are working closely with Microsoft on product releases and this relationship on product development is benefiting our overall stance in the marketplace.

Whilst our focus has been on the AX proposition, our traditional Dynamics NAV business has also recovered with a major £0.5m contract secured at the end of the half year, and with our NAV pipeline containing further significant deals. We are also investing in a product upgrade path for existing customers to provide additional functionality for solutions purchased in previous years.

Software recognised in H1 of £2.75m compared to £0.97m in the prior period. These sales are from a mix of traditionally structured deals and Microsoft Enterprise Agreements. Enterprise Agreements are used by Microsoft on larger contracts and under these agreements K3 receives a "commission" for the software delivered to the customer combined with follow-on services. We estimate that the software value would have been £3.34m without Enterprise Agreements.

*See note 8 on page 19 for further details

Services revenue has been growing steadily, with a monthly run rate at 31 December 2013 of £0.7m which was 75% or £0.3m higher than at the same point in 2012. The first half year has seen a significant increase in demand for AX which has in turn created a surge in demand for skilled AX resource. We have initiatives in place to meet the needs arising from our business growth. These will involve significant short term investment as we embark on an accelerated programme of global recruitment, including offshoring and near-shoring, and training to equip our staff. Recurring maintenance income of £3.89m is up 8% over the period (2012: £3.59m) reflecting the impact of new deals and initiatives to encourage customer retention.

At 31 December 2013, the pipeline for the Division was at £40.2m (2012: £36.0m). This includes £4.8m from recent wins which have yet to be delivered.

The smaller units in the Division, which sell a mixture of non-retail NAV and non-retail AX, performed in line with expectations with some growth being seen in the RSG business that focuses on the "events sector", utilising the Microsoft RMS product.

International Division

The International Division includes our Dutch Microsoft Dynamics reseller business, our Point of Sale business focussed on smaller retailers, and our ISV (software author and channel management company).

It has been a challenging half year as the Dutch economy is still coming out of recession and small retailers, which represent the majority of the local customer base in our Dutch reseller business, are reluctant to commit to new deals. Our Inter IKEA Systems B.V. (the owner and franchisor of the IKEA concept and the largest customer in the Group) business however has been encouraging with good levels of services income on store openings and projects, with further potential business to come. We have retrained a number of our staff so that they can be deployed on Inter IKEA Systems-related work, anticipating continued strong demand in the next six months.

Revenues at £5.44m were marginally ahead of the prior year (2012: £5.39m) however adjusted profit from operations*8 at £0.40m was slightly down (2012: £0.47m). This reflected our investment in Dynamics AX resource as well as the recruitment of two senior executives (both previously at Microsoft). Software levels were up 14% or £0.1m at £0.8m although services revenues were flat at £2.4m. Reductions in the cost of service delivery together with higher sales of our own intellectual property improved margin to 49.5% from 45.3%. Overhead costs increased by £0.3m to £2.3m due to investment in sales and marketing personnel to build our channel team, together with higher development amortisation. The Division secured a total of £0.79m major order wins (2012: £0.53m). The prospects pipeline, excluding potential business anticipated in a long term plan with Inter IKEA Systems B.V., currently amounts to £5.2m of orders (2012: £7.1m). The reduction year-on-year reflects the delivery of projects and a heavily qualified pipeline.

The ISV performed in line with the prior period, focusing on its traditional "Pebblestone" Microsoft Dynamics product set. However, more importantly, it continued to work closely with our UK Division on our "ax|is" product. The business is also progressing on the further development of an International distribution channel via partners for the product, as we believe that this represents a significant opportunity for K3. Investment here will be ongoing.

The Unisoft business is performing in line with our expectations with its RVE Point of Sale product gaining traction, especially in the area of subscription-based licences and solutions, whilst the market remains difficult. We are looking at the wider potential sales opportunities for this product.

The business is progressing on the further development of an international distribution channel via partners for the "ax|is" product as we believe this represents a significant opportunity for K3

*See note 8 on page 19 for further details

"The business has been recently named as Sage ERP X3 Business Partner of the Year"

SYSPRO and Sage Division

Revenue reduced by £0.5m to £14.12m (2012: £14.60m), with the reduction reflecting the disposal of a small non-core Sage business in May 2013. Excluding this disposal, like-for-like sales increased by 5%. Adjusted profit from operations[*9] decreased by 11% to £3.67m (2012: £4.11m), reflecting the increased cost base as we invested in sales, marketing and finance resource in the Sage business.

Software sales remained robust at £1.93m (2012: £1.92m) and services increased by £0.1m to £2.62m (2012: £2.52m).

Maintenance and support revenues reduced by £0.56m to £9.4m with a margin impact of £0.2m. The reduction primarily reflected the disposal of the Sage business referenced above. SYSPRO maintenance and support levels remained strong with a 97% renewal rate (2012: 98%). Approximately £5.5m of SYSPRO maintenance income is recognised in the first half year from 430 customers. This results in significant cash inflows before the half year end (together with annual customer support billings) which helps to underpin the Group's overall cash performance for the half year. Overhead costs of £5.4m were up £0.3m (2012: £5.1m) due to the recruitment noted above. The pipeline of prospects for the Division totalled £14.8m (2012: £14.0m).

The SYSPRO operation is the exclusive UK and sole European SYSPRO partner with a rolling 5 year distribution agreement. It has over £1.0m of income from own IP products covering functional requirements which are usually found only in significantly more expensive software. The business remains strong with high levels of recurring income, excellent management of opportunities and encouraging levels of new business wins. These increasingly involve elements of hosted services. SYSPRO order wins totalled £1.44m, a rise of 20% on the prior period (2012: £1.2m).

Our Sage operation reorganised its delivery and support operations at the beginning of the year and is now moving forward. In October 2013 we recruited a new Sales Director (ex Sage) and we are starting to see more order wins and stronger monthly services revenues. Total order wins were £1.2m (2012: £0.84m). The business has a higher profile in the market, having been recently named as Sage CRM Business Partner of the Year, Sage ERP X3 Business Partner of the Year, and Sage Mid-Market Europe Business Partner of the Year. The X3 award is particularly significant as this is the product around which Sage is building its Enterprise ERP strategy.

*See note 8 on page 19 for further details

Managed Services Division

Managed Services revenues rose by £0.5m to £3.93m (2012: £3.43m) and made an adjusted profit from operations*[10] of £0.1m (2012: loss of £0.06m) having incurred losses of £0.5m in the second half of the prior financial year. The elimination of these losses was a key objective for the business and we are delighted that this has been achieved quickly through a combination of increased recurring revenues and lower operating costs. At the beginning of the year we recruited a small team of "operating system" consultants, who are delivering managed services for a number of our retail clients who were reported in our Microsoft UK division. Prior year comparatives for divisional results have not been restated as the impact is not material to the Group.

The hosting business has started to benefit from the input of new management and a significantly reduced cost base following a reorganisation in the first quarter, together with a review of all aspects of the business model. We have focused very strongly on widening the product offering to include "network as a service", "platform as a service" and "infrastructure as a service", in addition to our traditional "ERP as a service" model. Our ability to host multi-site overseas customers offers significant growth opportunities with deal wins of this nature in both AX and SYSPRO in the last six months.

Head Office

Head office costs*[11] have increased by £0.16m due to consultancy costs incurred on product strategy and increased payroll costs.

The Board

In January 2014, we announced that after nearly 14 years as Chief Executive, Andy Makeham was leaving the Group and that Chief Finance Officer David Bolton, who had led the Group's expansion with Andy, was assuming the role of Chief Executive. I would like now, on behalf of K3, to formally welcome David to his new position and to thank Andy for his substantial contribution to K3. Andy played a significant role in the successful development and expansion of the business, and we wish him well in his future ventures.

David, who has previously been Chief Finance Officer at K3 for over 15 years, is supported by the senior management team, which includes the heads of the Group's major operating businesses and the Group Operations Director, a newly created role. Brian Davis, who has worked for six years as Head of Finance, has assumed the role of Chief Financial Officer. We welcome Brian to his new role.

Outlook

The investments we made over the last 18 months in Microsoft technology are starting to yield real benefits for the Group. We believe that there is significant long term potential to accelerate and widen sales as we develop a global channel to market for our AX solutions and release new product, enriched with our own IP and tailored for specific retail market segments.

We plan over the next year to invest across the Group to support wider growth opportunities over a 3-5 year timescale. Notwithstanding, continuing momentum with Microsoft Dynamics sales together with the improving performance of the Managed Services Division, will help to underpin forecasts for the full financial year.

Tom Milne
Chairman

"The investments we made over the last 18 months in Microsoft technology are starting to yield real benefits for the Group"

*See note 8 on page 19 for further details

Consolidated Income Statement

for the six months ended 31 December 2013

	Notes	Unaudited Six months to 31 December 2013 £'000	Unaudited Six months to 31 December 2012 £'000	Audited Year to 30 June 2013 £'000
Revenue		**34,469**	31,547	63,513
Profit from operations before amortisation of acquired intangibles, acquisition costs and exceptional items		**3,608**	2,940	5,094
Amortisation of acquired intangibles		**(1,708)**	(1,817)	(3,182)
Acquisition costs		**–**	(27)	–
Exceptional reorganisation costs		**(581)**	(476)	(727)
Profit from operations		**1,319**	620	1,185
Finance income		**2**	2	2
Finance expense		**(446)**	(437)	(725)
Profit before taxation		**875**	185	462
Tax income	2	**19**	31	780
Profit for the period		**894**	216	1,242

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

Earnings Per Share	3			
Basic		**2.9p**	0.8p	4.3p
Diluted		**2.8p**	0.7p	4.2p

Consolidated Statement of Comprehensive Income

for the six months ended 31 December 2013

	Unaudited Six months to 31 December 2013 £'000	Unaudited Six months to 31 December 2012 £'000	Audited Year to 30 June 2013 £'000
Profit for the period	**894**	216	1,242
Other comprehensive (expense) income			
Items that may be reclassified into profit or loss			
Exchange differences on translation of foreign operations	**(409)**	218	692
Net investment hedge	**24**	(40)	(148)
Other comprehensive (expense) income, net of tax	**(385)**	178	544
Total comprehensive income for the period	**509**	394	1,786

All of the total comprehensive income for the period is attributable to equity holders of the parent.

Consolidated Statement of Financial Position

as at 31 December 2013

	Notes	Unaudited As at 31 December 2013 £'000	Unaudited As at 31 December 2012 £'000	Audited As at 30 June 2013 £'000
ASSETS				
Non-current assets				
Property, plant and equipment		**2,631**	2,886	2,927
Goodwill		**44,362**	44,300	44,610
Other intangible assets		**20,338**	20,354	21,040
Deferred tax assets		**648**	702	723
Available-for-sale investments		**98**	98	98
Total non-current assets		**68,077**	68,340	69,398
Current assets				
Trade and other receivables		**26,246**	24,885	25,251
Cash and cash equivalents		**1,244**	2,236	272
Total current assets		**27,490**	27,121	25,523
Total assets		**95,567**	95,461	94,921
LIABILITIES				
Non-current liabilities				
Long-term borrowings	4	**23**	19	32
Other non-current liabilities	5	**257**	860	225
Deferred tax liabilities		**3,728**	4,458	4,267
Total non-current liabilities		**4,008**	5,337	4,524
Current liabilities				
Trade and other payables	6	**28,517**	27,284	25,081
Current tax liabilities		**164**	908	140
Short-term borrowings	4	**11,127**	14,539	14,051
Total current liabilities		**39,808**	42,731	39,272
Total liabilities		**43,816**	48,068	43,796
EQUITY				
Share capital		**7,891**	7,146	7,859
Share premium account		**9,281**	7,286	9,183
Other reserves		**10,448**	10,448	10,448
Translation reserve		**912**	931	1,297
Retained earnings		**23,219**	21,582	22,338
Total equity attributable to equity holders of the parent		**51,751**	47,393	51,125
Total equity and liabilities		**95,567**	95,461	94,921

Consolidated Statement of Cash Flows

for the six months ended 31 December 2013

	Notes	Unaudited Six months to 31 December 2013 £'000	Unaudited Six months to 31 December 2012 £'000	Audited Year to 30 June 2013 £'000
Cash flows from operating activities				
Profit for the period		**894**	216	1,242
Adjustments for:				
Share based payments charge		**14**	36	70
Depreciation of property, plant and equipment		**468**	400	932
Amortisation of intangible assets and development expenditure		**2,458**	2,351	4,347
Loss on sale of property, plant and equipment		**–**	–	(19)
Finance income		**(2)**	(2)	(2)
Finance expense		**446**	437	725
Tax income		**(19)**	(31)	(780)
(Increase) decrease in trade and other receivables		**(2,065)**	5,483	6,395
Increase (decrease) in trade and other payables		**3,660**	(1,972)	(4,888)
Cash generated from operations	7	**5,854**	6,918	8,022
Finance expense paid		**(533)**	(515)	(822)
Income taxes received (paid)		**511**	(62)	(1,217)
Net cash generated from operating activities		**5,832**	6,341	5,983
Cash flows from investing activities				
Acquisition of subsidiaries, net of cash acquired	7	**–**	(195)	(531)
Acquisition of other business units	7	**–**	(1,089)	(1,410)
Development expenditure capitalised		**(1,951)**	(1,371)	(3,563)
Purchase of property, plant and equipment		**(229)**	(528)	(1,050)
Proceeds from sale of property, plant and equipment		**–**	–	24
Finance income received		**2**	2	2
Net cash absorbed by investing activities		**(2,178)**	(3,181)	(6,528)
Cash flows from financing activities				
Net proceeds from issue of share capital		**103**	83	2,677
Proceeds from long-term borrowings		**–**	866	842
Payment of long-term borrowings		**(1,673)**	(1,902)	(3,641)
Payment of finance lease liabilities		**(8)**	(26)	(35)
Dividends paid		**–**	–	(286)
Net cash absorbed from financing activities		**(1,578)**	(979)	(443)
Net change in cash and cash equivalents		**2,076**	2,181	(988)
Cash and cash equivalents at start of period		**(833)**	21	21
Exchange gains on cash and cash equivalents		**1**	34	134
Cash and cash equivalents at end of period		**1,244**	2,236	(833)

Consolidated Statement of Changes in Equity

for the six months ended 31 December 2013

	Share capital £'000	Share premium £'000	Other reserve £'000	Translation reserve £'000	Retained earnings £'000	Total equity £'000
At 1 July 2012	7,120	7,239	10,448	753	21,345	46,905
Changes in equity for six months ended 31 December 2012						
Share-based payment credit	–	–	–	–	11	11
Options exercised	26	47	–	–	–	73
Movement in own shares held	–	–	–	–	10	10
Profit for the period	–	–	–	–	216	216
Other comprehensive income for the period	–	–	–	178	–	178
At 31 December 2012	7,146	7,286	10,448	931	21,582	47,393
Changes in equity for six months ended 30 June 2013						
Share-based payment credit	–	–	–	–	32	32
Issue of shares for cash	713	1,897	–	–	–	2,610
Movement in own shares held	–	–	–	–	(16)	(16)
Dividends to equity holders	–	–	–	–	(286)	(286)
Profit for the period	–	–	–	–	1,026	1,026
Other comprehensive income for the period	–	–	–	366	–	366
At 30 June 2013	7,859	9,183	10,448	1,297	22,338	51,125
Changes in equity for six months ended 31 December 2013						
Share-based payment credit	–	–	–	–	14	14
Options exercised	32	98	–	–	–	130
Movement in own shares held	–	–	–	–	(27)	(27)
Profit for the period	–	–	–	–	894	894
Other comprehensive income for the period	–	–	–	(385)	–	(385)
At 31 December 2013	7,891	9,281	10,448	912	23,219	51,751

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 2014 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 2013. 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 2014 or are expected to be adopted and effective at 30 June 2014. 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 2013 and the six months ended 31 December 2012 has neither been audited nor reviewed pursuant to guidance issued by the Auditing Practices Board. The financial information for the year ended 30 June 2013 does not constitute the full statutory accounts for that period. The Annual Report and Financial Statements for the year ended 30 June 2013 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 2013 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.

Notes to the Unaudited Half Yearly Report continued

2 Tax expense (income)

	Unaudited Six months to 31 December 2013 £'000	Unaudited Six months to 31 December 2012 £'000	Audited Year to 30 June 2013 £'000
Current tax expense (income)			
UK corporation tax and income tax of overseas operations on profits for the period	**463**	311	346
Adjustment in respect of prior periods	**(35)**	–	(478)
Total current tax expense (income)	**428**	311	(132)
Deferred tax expense			
Origination and reversal of temporary differences	**(182)**	(183)	(465)
Effect of change in rate of deferred tax	**(265)**	(159)	(183)
Total deferred tax credit	**(447)**	(342)	(648)
Total tax income	**(19)**	(31)	(780)

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 2013 Number of shares	Unaudited Six months to 31 December 2012 Number of shares	Audited Year to 30 June 2013 Number of shares
Weighted average number of shares:			
For basic earnings per share	**31,317,823**	28,403,955	29,216,238
Effects of employee share options and warrants	**234,925**	503,263	312,488
For diluted earnings per share	**31,552,748**	28,907,218	29,528,726

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 2013			Unaudited six months to 31 December 2012			Audited year to 30 June 2013		
	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)	**894**	**2.9**	**2.8**	216	0.8	0.7	1,242	4.3	4.2
Amortisation of acquired intangibles (net of tax)	**1,051**	**3.4**	**3.3**	1,221	4.3	4.2	2,273	7.7	7.7
Acquisition costs (net of tax)	**–**	**–**	**–**	27	0.1	0.1	–	–	–
Exceptional reorganisation costs (net of tax)	**450**	**1.4**	**1.4**	363	1.3	1.3	580	2.0	2.0
Adjusted eps	**2,395**	**7.7**	**7.5**	1,827	6.5	6.3	4,095	14.0	13.9

Notes to the Unaudited Half Yearly Report continued

4 Loans and borrowings

	Unaudited As at 31 December 2013 £'000	Unaudited As at 31 December 2012 £'000	Audited As at 30 June 2013 £'000
Non-current			
Finance lease creditors	**23**	19	32
	23	19	32
Current			
Bank overdrafts	**–**	–	1,105
Bank loans (secured)	**10,470**	13,885	12,290
Finance lease creditors	**17**	14	16
Loans from related parties	**640**	640	640
	11,127	14,539	14,051
Total borrowings	**11,150**	14,558	14,083

The bank loans and other facilities include a multi-option facility which expires in December 2014.

5 Other non-current liabilities

	Unaudited As at 31 December 2013 £'000	Unaudited As at 31 December 2012 £'000	Audited As at 30 June 2013 £'000
Contingent consideration	**–**	421	–
Deferred consideration	**–**	191	–
Accruals	**257**	248	225
	257	860	225

6 Trade and other payables

	Unaudited As at 31 December 2013 £'000	Unaudited As at 31 December 2012 £'000	Audited As at 30 June 2013 £'000
Trade payables	**4,248**	4,108	5,702
Other payables	**584**	433	555
Deferred consideration	**–**	90	–
Accruals	**6,958**	7,027	5,728
Total financial liabilities, excluding loans and borrowings, classified as financial liabilities measured at amortised cost	**11,790**	11,658	11,985
Contingent consideration	**390**	341	392
Other tax and social security taxes	**4,149**	3,977	2,135
Deferred revenue	**12,188**	11,308	10,569
	28,517	27,284	25,081

Notes to the Unaudited Half Yearly Report continued

7 Notes to the cash flow statement

Cash generated from operations is stated after acquisition costs and exceptional reorganisation costs arising as a result of acquisitions in previous years. 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 2013 £'000	Unaudited Six months ended 31 December 2012 £'000	Audited Year ended 30 June 2013 £'000
Cash generated from operating activities	**5,854**	6,918	8,022
Add:			
Acquisition costs	**–**	27	–
Exceptional reorganisation costs	**511**	318	637
Adjusted cash generated from operations	**6,365**	7,263	8,659

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

	Unaudited Six months ended 31 December 2013 £'000	Unaudited Six months ended 31 December 2012 £'000	Audited Year ended 30 June 2013 £'000
Initial consideration	**–**	–	(10)
Contingent and deferred consideration paid	**–**	(1,284)	(1,931)
	–	(1,284)	(1,941)

8 Notes to the Chairman's Statement

*1 Group adjusted profit before tax is calculated before amortisation of acquired intangibles of £1.71m (2012: £1.82m), acquisition costs of £nil (2012: £0.03m) and exceptional reorganisation costs of £0.58m (2012: £0.48m).

*2 Group adjusted profit from operations is calculated before amortisation of acquired intangibles of £1.71m (2012: £1.82m), acquisition costs of £nil (2012: £0.03m) and exceptional reorganisation costs of £0.58m (2012: £0.48m).

*3 Group adjusted profit before tax is calculated before amortisation of acquired intangibles of £1.71m (2012: £1.82m), acquisition costs of £nil (2012: £0.03m) and exceptional reorganisation costs of £0.58m (2012: £0.48m).

*4 Group adjusted earnings per share is calculated before amortisation of acquired intangibles (net of tax) of £1.05m (2012: £1.22m), acquisition costs (net of tax) of £nil (2012: £0.03m) and exceptional reorganisation costs (net of tax) of £0.45m (2012: £0.36m).

*5 Group adjusted profit from operations is calculated before amortisation of acquired intangibles of £1.71m (2012: £1.82m), acquisition costs of £nil (2012: £0.03m) and exceptional reorganisation costs of £0.58m (2012: £0.48m).

*6 Microsoft Division adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.49m (2012: £0.67m) and exceptional reorganisation costs of £0.24m (2012: £0.01m).

*7 Microsoft UK Division adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.24m (2012: £0.30m) and exceptional reorganisation costs of £0.03m (2012: £nil).

*8 International Division adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.25m (2012: £0.37m) and exceptional reorganisation costs of £0.21m (2012: £0.01m).

*9 SYSPRO and Sage Division adjusted profit from operations is calculated before amortisation of acquired intangibles of £1.07m (2012: £1.07m) and exceptional reorganisation costs of £0.01m (2012: £0.15m).

*10 Managed Services Division adjusted profit from operations is calculated before amortisation of acquired intangibles of £0.15m (2012: £0.08m) and exceptional reorganisation costs of £0.18m (2012: £nil).

*11 Head office costs are calculated before acquisition costs of £nil (2012: £0.03m) and exceptional reorganisation costs of £0.15m (2012: £0.31m).

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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