Adept4 plc

(“Adept4”, the “Group” or the “Company”)

Final results for the year ended 30 September 2018

Adept4 plc (AD4) the AIM quoted provider of IT as a Service is pleased to announce final results for the year ended 30 September 2018.

Financial Summary

- Revenue in line with last year at £10.2m (FY17: £10.3m) with 70% from recurring customer base, demonstrating strength of customer relationships
- Gross profit of £5.7m (FY17: £6.2m) representing gross profit margin of 56% (FY17: 60%)
- Trading Group EBITDA[1] of £0.6m (FY17: £1.2m)
- Loss after tax of £3.8m (FY17: £0.6m) after significant non-recurring items, including an impairment charge of £2.6m against goodwill
- Net debt[2] at 30 September 2018 of £2.7m (FY17: £2.0m)

Operational Summary

- Successful settlement of legal case against vendors of Adept4 Managed IT Limited in the sum of £1.6m, of which £0.6m was receivable in cash
- Strengthening of management team leading to improved technical and service levels
- Increased utilisation of cloud technology by customers resulting in a reduced requirement for remote based and field workers leading to a reduction in the operating cost base towards the end of the year
- Post-year end decision to focus on existing customers with less emphasis on new business acquisition
- Further cost savings identified and being implemented to protect the cash reserves whilst the Board assesses strategic options

Simon Duckworth, Chairman of Adept4, commented:

"Despite it being a challenging year for the business, we have made progress against each of our key areas of strategic development including the strengthening of our senior operational management team and development of our technology partnerships. We have improved our levels of service delivery leading to high levels of customer satisfaction, though the investment made in the new sales team has not yet delivered the results we had hoped for. Maintaining our strong relationships with existing customers, together with protecting the Group’s cash balances and shareholder value are our key objectives while we explore the strategic options for the Group."

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This announcement contains inside information.

[1] earnings before net finance costs, tax, depreciation, amortisation, plc costs, separately identifiable items and share-based payments

[2] Net debt at 30 September 2018 comprises cash balances of £1.4m, less the fair value of the BGF loan notes of £4.1m.

Chairman's statement

Overview
I am pleased to comment upon the results of the Group for the year ended 30 September 2018 ("FY18") and to provide the market with an update on our current performance and strategy. As outlined in the 2017 Annual Report, that year was one of consolidation for the Group, when we integrated the three companies previously acquired into one single operating platform. We also set out our key areas of strategic development for 2018 to enable us to build on those foundations: the strengthening of our senior operational management team; the development of our partnership with Microsoft and our other technology partners and the development of our IT security offering. We have made progress against each of these key objectives during FY18.

The year has, however, seen us face some significant challenges. The progress we have made in establishing a stronger management team (with the appointments of a Chief Technology Officer, Director of Operations and, towards the end of the financial year, a Sales Director) and the subsequent ground work we have laid to improve our technology, our delivery and our service levels has been tempered by both disappointing progress with our new-business sales in the year and also by a significant legal claim we were forced to bring against the vendors of one of the acquired businesses. This claim was brought against the vendors of the Adept4 MIT Limited ("MIT") business in respect of breach of warranties given by the vendors at the time of our acquisition of the MIT business. This was a necessary but expensive and distracting exercise, not only in terms of legal and professional fees incurred and management time expensed on the claim itself, but also in respect of M&A activities which were put on hold as a result of the issues which led to the legal action and which have subsequently been resolved. We are pleased that this issue is now behind us, with a successful settlement in the Company's favour of £1.6m (£0.6m cash received post-year end and £1.0m waiver of deferred consideration) before legal fees and other related costs.

In assessing the level of settlement of the warranty claim which would be acceptable to the Company, various issues were considered, including a historic licencing review of the acquired business being undertaken by Microsoft. The Company has, post-year end, reached agreement with Microsoft in relation to this review, and this will result in a payment of £0.4m to Microsoft post-year end. The liability in respect of this sum is provided for in these results.

This legal issue also had a direct impact on our sales function during the year, not least because it brought about the exit of the former MIT management team sooner than we had planned, creating an enforced change in sales leadership. It took us longer than planned to recruit a new sales director and therefore we spent much of the year without effective sales leadership in place. We have, towards the end of the financial year, made significant changes to the sales team, improving both its quality and experience; however we have yet to see the results of this in pipeline conversion and revenue growth post-year end.

Despite the challenges we faced during the year, revenue remained consistent year on year at £10.2m (FY17: £10.3m) with 70% of revenue coming from our recurring revenue base, demonstrating the strength of our existing customer relationships. As a result of the move of certain customers to Cloud based solutions, and as further explained in the Financial Review, our gross profit margins fell from 60% to 56%. The fall in margins contributed to a reduced Trading Group EBITDA[1] for the year of £0.6m (FY17: £1.2m). After all costs and income, including, *inter alia*, the warranty settlement and related costs, the Microsoft settlement and an impairment charge of £2.6m in respect of the Group's goodwill in its acquired businesses (see Note 7), the operating loss for the year was £3.4m (FY17: nil) with a retained loss of £3.8m (FY17: loss of £0.6m).

People
In March 2018, we announced that Ian Winn, Chief Financial Officer and M&A director, had stepped down from the Board to pursue other interests. At the same time, Nick Deman was appointed to the Board as Interim Finance Director for a six-month period to the end of the financial year. Jill Collighan, one of our existing directors, has assumed the role of CFO following Nick's departure. We would like to place on record our thanks to Nick for his efforts and support during the period.

Given the enormous change which has taken place within Adept4 in the past year, I would like to take this opportunity to thank our dedicated staff. There have been many examples of our people simply continuing to work very hard to produce great outcomes for our customers despite the significant challenges we have faced, and I would like to assure them of the Board's appreciation.

Outlook
As detailed above, the past twelve months have been extremely challenging for the business. The investment made in the new sales team has not yet delivered the results we had hoped for, with progress further hindered by the general level of caution which is evident in our markets as the uncertainly surrounding Brexit continues to delay decisions and customer spend. The Board does not see this situation improving in the short-term.

Detailed work has already gone into right-sizing the Group's cost base, with a significant reduction in operating costs achieved towards the end of FY18. However, given the continued delay in new sales in the current financial year, the Group continues to see monthly Trading Group EBITDA and cash losses following the investment made in the sales and marketing functions. The Group's cash balance at 31 January 2019 was £0.9m.

Maintaining our strong relationships with existing customers, together with protecting the Group's cash balances and shareholder value are the key objectives of the Board. We have therefore taken the decision to focus on our existing customer base with less emphasis on new business acquisition, which has an upfront cost to the business and takes time to come through. This is designed to protect the cash reserves of the Group whilst the Board considers the strategic options open to the Company. This will lead to reduced revenue and gross profit but requires a significantly lower operating cost base, which should enable the Group to return to profitability and positive cash generation. To that end, further cost savings have been identified which are in the process of being implemented.

The Board will update the market as it continues to explore its strategic options.

Simon Duckworth
Non-Executive Chairman
14 February 2019

Business overview

What we do
Adept4 delivers IT as a Service to small and medium-sized businesses across the UK. Through the provision of our modular managed services, customers can create a bespoke service to suit their requirements based on proven technologies from providers such as Microsoft, complemented by the Group's operational and technical teams, to provide guaranteed support with defined service levels. As a result of the flexible nature of our approach, our customers can start with any or all of the services available and can expand these as their needs and demands change.

As many of the technologies which underpin our product suite can be provided "as a service", we provide our clients with exactly what is required to support their needs in accordance with business demands, billed on a monthly basis, based on what is consumed. Effectively, we provide the UK small to medium enterprise ("SME") market with enterprise-level IT on a pay as you go ("PAYG") basis. Our 24/7 UK response team, together with our strategic consulting, professional services and software development teams provide exactly what businesses need from IT at any given time.

The revenue generated by Adept4 typically comes from three core areas of our business: contracted recurring managed services, professional services and the sale of associated hardware and other products.

Our market
Adept4 predominantly sells services into the SME market. The Group's customer base spans all aspects of the SME market and the requirements for each can be quite different. We typically see small businesses more inclined to look for a single organisation to provide as many services as possible across IT, telephony and connectivity providing them with a "one stop shop" approach. As we move towards the medium enterprise clients, we typically see these look to a more specialist provider for different aspects of the services they require. These customers will generally start with a specific service from Adept4 which addresses a particular business need and will then engage in additional solution discussions once the initial service is being successfully delivered. With the depth and breadth of our technology offering, together with our specialist teams and our flexible service options, we are ideally placed to grow our existing medium enterprise accounts whilst continuing to service and support our overall base.

In addition to its SME customer base, the Group has a number of public sector clients and we have experienced an increase in requests to transact business through a recognised government procurement framework. We were therefore pleased that during FY18, we were successful in securing a place on the government's Digital Outcomes and Specialist 3 ("DOS3") framework which went live in October 2018. This further underpins our credentials for our core professional and managed services capabilities within the public sector arena. Further supporting our competencies in this area, during the year we were successful in winning a number of projects in the higher education sector including a £0.3m telephony upgrade for an existing customer ranked in the top 25 universities worldwide (QS World Rankings 2017/18).

Our technology
As part of our drive to be recognised as "trusted advisors" to our customers, we have continued the development of our technical skills, our competencies and our engagement with key vendor partners across both our IT and telephony managed service sectors.
We utilise industry leading technology products and services from a number of vendor partners, including Microsoft, Mitel and Fortinet in delivering our managed service offering.

One of our core technology partners is Microsoft and during the year we have been awarded "Gold Cloud Platform" partner status, a certification that validates our high level of competency in cloud technologies, identity management, systems management, virtualisation, storage and networking. We have also secured the coveted Microsoft "P-Seller" status which is designed to create a deeper relationship between Microsoft partners and the Microsoft product teams, in order to provide highly-skilled solution specialists to Microsoft customers.

Telephony services continue to drive strong opportunities for the Group, in both the traditional telecoms market - where we sell, install and support systems from Mitel, a market leading voice technology company - and in new technologies, such as integrated solutions from Microsoft based on their Skype for Business technology, now branded as Microsoft Teams. We increasingly see customers looking to introduce the Microsoft voice and collaboration suite of products into their business, consolidating their technology to a single platform. We have added further functionality to our offering, with the introduction of a contact centre product called Anywhere365. This software application, which works directly with Microsoft Teams, provides additional multichannel communication functionality. With the Group's capability across the telephony market, we are ideally placed to continue to sell to and support clients requiring traditional infrastructure and also provide a migration strategy for those that want to move to the new collaboration platforms.

In relation to our security proposition, during the year we were granted exclusivity to sell the Nyotron security portfolio in the UK. Nyotron's next generation cybersecurity solution distinguishes between legitimate operating system behaviour of IT users versus threatening activities carried out by attackers. This provides real-time protection from any attack without foreknowledge of the exploit. We very quickly saw significant interest for this next-generation technology and we have identified a strong pipeline of opportunities for the product, with a number of pilot schemes being undertaken during the year. Whilst we have been disappointed with the speed at which the product has been adopted by the market as a whole, we remain confident that Nyotron could become a strong revenue stream for Adept4.

Additionally, in the cyber security market, during the year we started to sell a security and threat detection solution from Fortinet, a leading global provider of network security solutions. We have sold this as both a stand-alone solution and also as a managed service to, amongst others, a multi-site vehicle dealership in a security solution including a monthly reporting pack of key activity, both in terms of threats and usage. Given our sales success, we are now regarded as a key Fortinet development partner and have a healthy pipeline in this area.

Our software development team continue to deliver strong revenues from our existing clients and we have also added new customer revenues for application redevelopment work and Power BI reporting during the year. This included a new £0.3 million contract for application development for a global provider of customer contact centres.

The need to interrogate data from multiple applications and information stores and bring this together to provide analytical intelligence is driving new conversations in our customer base and is expected to provide the Group with new revenue streams. We have a team of in-house developers and additionally, we have agreed a partnership with a "nearshore" development provider to supplement our own software development capabilities in a cost efficient and scalable manner to allow us to maximise revenue opportunities.

Management team and operational development

A number of new key operational leadership appointments were made during the year, ultimately bringing about a new management team across the business. Our three key appointments were a new Sales Director, a Director of Operations and a new Chief Technology Officer. These appointments, together with our existing executives, provide us with an effective team to guide the business through its next phase of development and they have already effected some significant improvements within the business.

One of the biggest areas of improvement in the year has been in our technical operations and support teams, who provide the technical services and back end support to our customers. Through feedback from customers and members of the sales and services teams, we identified a series of operational changes that were required to improve how we dealt with support requests and also how we captured client sentiment and dealt with this.

Following a review by the newly appointed Director of Operations, it was clear that the business required a fresh approach to customer support and we identified a new Head of Service Operations to join the Group and run the service desk teams. Processes were improved which quickly reduced the number of outstanding support requests, improved the response times of the service desk teams, reduced the number of repeat inbound calls to the service desk and provided a platform to allow us to score every engagement that was made with the service desk. The current position is that we have a much faster ticket resolution process with more tickets closed on the first day than at any point in the previous three years, resulting in customers more willing to engage with discussions to acquire additional products and services from the Group.

Within our sales pipeline, we are also seeing an increase in our existing customers' appetite to understand how they can embrace digital transformation, i.e. how they can utilise cloud technology to drive business agility, improve time to market, understand and predict client behaviour and make better use of their business data. We are seeing a steady increase in these early discussions with customers on how to approach such a significant change in their business and how Adept4 can assist in doing so. As part of digital transformation, customers typically see a change in the profile of their IT spend with an increase in upfront professional services to make the journey from "traditional to cloud" but then a reduction in infrastructure hardware and monthly recurring spend as they have less infrastructure for us to support.

This model of PAYG cloud computing has also brought about some changes to the way managed services are delivered and priced. With the cloud infrastructure being hosted in a vendor's datacentre (Microsoft Azure / Amazon AWS), any hardware support is provided by the vendor as part of their service. This means that we no longer need to provide the support for this hardware but there is an additional cost from the vendor for the provision of these services. For this reason, and as detailed in the Financial Review, our gross profit margin has fallen during the year. We do however see the benefit of operational cost savings as under this model, our responsibility is focused on the operating systems support as well as the configuration and management of the virtual servers which is carried out by our desk based technical teams. We therefore have a reduced requirement for remote based or field workers with associated high travel and expense costs. Towards the end of the financial year, the Group's operating cost base was reduced accordingly; the impact of this will be seen in the new financial year. This will be supplemented by further cost reductions which have been identified and are in the process of being implemented.

Summary and outlook

As detailed above, we have made progress against our key objectives during the year, but this was tempered by certain challenges faced by the Group. Going forward our priorities are to maintain our strong relationships with existing customers, and to protect the Group's cash balances and shareholder value. Our focus is therefore on continuing to deliver high levels of service to our existing customer base whilst placing less emphasis on new business acquisition which has an upfront cost to the business and takes time to come through. This is designed to safeguard the cash reserves of the Group whilst the Board considers the strategic options open to the Company.

Financial review

Revenue and gross margin
Group revenue for the year to 30 September 2018 was in line with that generated in the previous financial year, at £10.2m (FY17: £10.3m). This produced a gross profit of £5.7m (FY17: £6.2m) representing a gross margin of 56% (FY17: 60%). The reduction in margin predominantly relates to the recurring services segment, as explained below.

We continue to see strong recurring revenue performance with 70% (FY17: 70%) of all revenues coming from ongoing contracts for services. The analysis of revenue and gross profit from each of our operating segments of recurring services, product sales and professional services is shown in Note 3 and is detailed below.

Recurring services
Revenues from recurring services were £7.1m (FY17: £7.2m), generating a gross profit of £4.2m (FY17: £4.6m) and a gross margin of 60% (FY17: 64%). We continue to see a reduction in the gross profit from recurring services due to the migration of certain services from our infrastructure to that of a third party (such as Microsoft), in line with our asset-light strategy. Whilst initially resulting in some margin reduction, this strategy reduces risk and cost of ownership for us and allows us to provide customers with best-of-breed solutions with the ability to sell a wider range of services to the customer. This transition also means that we need fewer staff to support the in-house solutions, which has enabled us to undertake a cost rationalisation programme in the year to reduce our overhead base.

We continue to focus on generating recurring revenues by promoting our consumptive pricing and "pay-as-you-go" IT model. The proportion of our total revenue derived from recurring services was 70% (FY17: 70%), providing a strong and visible future revenue base.

Product sales
Revenues from product sales were consistent with those in FY17 at £2.0m (FY17: £2.0m) generating a gross profit of £0.4m (FY17: £0.4m) and gross margin of 22% (FY17: 22%). Product revenue during the year included telephone system sales of £0.7m (FY17: £0.5m), with notable Mitel telephone system upgrades to universities and local government organisations totalling £0.5m.

Professional services
Revenues from professional services were £1.1m (FY17: £1.2m) generating a gross profit of £1.0m (FY17: £1.2m) as permanent employee costs are included in overheads. Digital transformation projects were undertaken during the year for five key customers generating £0.5m of professional services revenues. In addition, over 540 new orders were placed during the financial year for chargeable professional services work, demonstrating the quality of our professional services offering.

Operating performance, costs and EBITDA
Aside from revenue, gross profit and cash balances, one of our main financial key performance indicators is our Trading Group EBITDA[1] - our operational trading performance before plc costs.

Excluding plc costs of £0.5m (FY17: £0.6m), our trading overheads during the year were £5.1m (FY17: £5.0m), of which staff costs comprised 88% (FY17: 81%). Given the level of gross profit generated from recurring revenue this meant that we achieved 83% (FY17: 91%) coverage of the trading overhead base from our recurring services. Our resultant Trading Group EBITDA[1] for the year was £0.6m (FY17: £1.2m).

Separately identifiable items
During the year we incurred certain costs and income which were not directly related to the generation of revenue and trading profits. Given their size and nature, they have been classified as separately identifiable items within the Consolidated Income Statement. These items totalled a net cost of £2.4m and can be summarised as follows:

- income of £1.6m in relation to the settlement of the warranty claim with the vendors of Adept4 Managed IT Limited ("MIT");
- costs in relation to the warranty claim and other M&A activities of £0.5m;
- settlement of a historic Microsoft licence review, cost of £0.4m;
- impairment charge in respect of goodwill of £2.6m;
- integration and reorganisation costs of £0.3m; and
- costs in relation to the disposal of Pinnacle CDT Limited of £0.2m.

During FY18, the Company brought a warranty claim against the vendors of the MIT business, The Company was successful with this claim and agreed a settlement in the sum of £1.6 million. £0.6m of the settlement was payable to the Company in cash post-year end, with the balance extinguishing the Company's liability to pay the MIT vendors deferred consideration of £1.0m. Costs of £0.5m were incurred by the Company in relation to the warranty dispute and also in respect of corporate activity which was put on hold as a result of certain matters which led to the legal action and which have subsequently been resolved.

In assessing the level of settlement of the warranty claim which would be acceptable to the Company, various issues were considered, including a historic licencing review of the acquired business being undertaken by Microsoft. The Company has, post year end, reached agreement with Microsoft in relation to this review, which resulted in a payment of £0.4m due to Microsoft. The liability in respect of this sum is provided for in these results.

As a result of the warranty claim and current performance levels, the Board has assessed the carrying value of the Group's goodwill and an impairment charge of £2.6m (FY17: £0.2m) has been made against goodwill. Further details are given in Note 7.

After the successful integration of the service-desk team into a single site in July 2017 and a number of efficiencies gained as a result of the investment in a single operating system, together with the migration of certain services from our own infrastructure to third party vendors, the Group was able to reduce the ongoing annualised cost base for the business by £0.6m by way of a restructure. The restructure incurred one-off costs in relation to redundancy, holiday pay and payments in lieu of notice. The cost reductions took place towards the end of the financial year and therefore the benefit of these will be seen in FY19 along with the benefit of the additional cost savings currently being implemented.

In addition, the Group incurred a charge of £0.2m in relation to the disposal in 2016 of the trade and assets of one of its subsidiary companies. Further details are provided in Note 4.

Net finance expenses
During the year the Group incurred net finance costs of £0.6m (FY17: £0.8m). £0.4m of this was a cash cost in relation to the interest on the Business Growth Fund ("BGF") loan notes and £0.2m related to the release to the income statement of the fair value adjustments in respect of these loan notes.

Loss for the period
The Group incurred non-cash costs including total amortisation and depreciation charges of £1.0m (FY17: £1.0m) and a share-based payments charge of £0.1m (2017: £0.2m).

After accounting for a deferred tax credit of £0.2m (2017: £0.2m) the reported loss for the year after tax was £3.8m (FY17: £0.6m).

Statement of Financial Position and cash
Cash balances at 30 September 2018 were £1.4m (FY17: £2.9m) whilst net debt was £2.7m (FY17: £2.0m). Net debt comprises cash balances of £1.4m less the fair value of the BGF loan notes of £4.1m.

The main components of the Group's cash flows during the year were as follows:

- cash used in operating activities of £0.9m (after the payment of separately identifiable costs of £0.6m and plc costs of £0.5m);
- purchase of tangible fixed assets of £0.1m;
- £0.1m settlement of Chess dispute paid in October 2017; and
- financing interest payments of £0.4m;

Trade and other receivables at the period end were £2.9m (FY17: £2.3m). The increase in this category is primarily due to the £0.6m cash element of the warranty claim settlement which was received in November 2018.

Net assets at 30 September 2018 were £4.0m (FY17: £7.7m).

Consolidated income statement

for the year ended 30 September 2018

	Note	**2018 £'000**	2017 £'000
Continuing operations			
Revenue	3	**10,185**	10,301
Cost of sales		**(4,480)**	(4,137)
Gross profit	3	**5,705**	6,164
Administrative expenses		**(5,598)**	(5,575)
Amortisation of intangible assets	8	**(907)**	(880)
Depreciation	9	**(136)**	(162)
Separately identifiable (costs)/income	4	**(2,390)**	626
Share-based payments		**(48)**	(162)
Operating (loss)/profit		**(3,374)**	11
Interest receivable	5	**7**	—
Interest payable	5	**(609)**	(842)
Net finance expense		**(602)**	(842)
Loss before taxation		**(3,976)**	(831)
Taxation		**169**	248
Loss and total comprehensive loss for the year attributable to owners of the parent		**(3,807)**	(583)
Loss per share			
Basic and fully diluted	7	**(1.68)p**	(0.26)p

	Note	**2018 £'000**	2017 £'000
Non-statutory measure : Trading Group EBITDA[1]			
Operating (loss)/profit		**(3,374)**	11
Plc costs		**482**	570
Amortisation of intangible assets	8	**907**	880
Depreciation	9	**136**	162
Separately identifiable costs/(income)	4	**2,390**	(626)
Share-based payments		**48**	162
Trading Group EBITDA[1]		**589**	1,159

[1] earnings before net finance costs, tax, depreciation, amortisation, plc costs, separately identifiable items and share-based payments

Consolidated statement of financial position

as at 30 September 2018

	Note	**30 September 2018 £'000**	30 September 2017 £'000
Non-current assets			
Intangible assets	8	**8,282**	11,804
Property, plant and equipment	9	**146**	228
Total non-current assets		**8,428**	12,032
Current assets			
Inventories		**26**	66
Trade and other receivables	10	**2,900**	2,349
Cash and cash equivalents		**1,427**	2,905
Total current assets		**4,353**	5,320
Total assets		**12,781**	17,352
Current liabilities			
Short-term borrowings		**(32)**	(1,012)
Trade and other payables		**(1,102)**	(1,203)
Other taxes and social security costs		**(377)**	(490)
Accruals and deferred income		**(1,937)**	(1,590)
Total current liabilities	11	**(3,448)**	(4,295)
Non-current liabilities			
Long-term borrowings	11	**(4,117)**	(3,914)
Deferred tax liability		**(1,248)**	(1,416)
Total non-current liabilities		**(5,365)**	(5,330)
Total liabilities		**(8,813)**	(9,625)
Net assets		**3,968**	7,727
Equity			
Share capital		**2,271**	2,271
Share premium account		**11,337**	11,337
Capital redemption reserve		**6,489**	6,489
Merger reserve		**1,997**	1,997
Other reserve		**1,649**	1,601
Retained earnings		**(19,775)**	(15,968)
Total equity		**3,968**	7,727

Consolidated statement of changes in equity

for the year ended 30 September 2018

	Share capital £'000	Share premium £'000	Capital redemption reserve £'000	Merger reserve £'000	Other reserve £'000	Retained earnings £'000	Total £'000
At 1 October 2016	2,271	11,337	6,489	1,997	1,439	(15,385)	8,148
Loss and total comprehensive loss for the period	—	—	—	—	—	(583)	(583)
Transactions with owners							
Share-based payments	—	—	—	—	162	—	162
Total transactions with owners	—	—	—	—	162	—	162
Total movements	—	—	—	—	162	(583)	(421)
Equity at 30 September 2017	**2,271**	**11,337**	**6,489**	**1,997**	**1,601**	**(15,968)**	**7,727**

	Share capital £'000	Share premium £'000	Capital redemption reserve £'000	Merger reserve £'000	Other reserve £'000	Retained earnings £'000	Total £'000
At 1 October 2017	2,271	11,337	6,489	1,997	1,601	(15,968)	7,727
Loss and total comprehensive loss for the period	—	—	—	—	—	(3,807)	(3,807)
Transactions with owners							
Share-based payments	—	—	—	—	48	—	48
Total transactions with owners	—	—	—	—	48	—	48
Total movements	—	—	—	—	48	(3,807)	(3,759)
Equity at 30 September 2018	**2,271**	**11,337**	**6,489**	**1,997**	**1,649**	**(19,775)**	**3,968**

Consolidated statement of cash flows

for the year ended 30 September 2018

	2018 £'000	2017 £'000
Cash flows from operating activities		
Loss before taxation	**(3,976)**	(831)
Adjustments for:		
Depreciation	**136**	162
Amortisation	**907**	880
Share-based payments	**48**	162
Net finance expense	**602**	842
Settlement of Warranty Claim	**(1,578)**	—
Write back of contingent consideration	—	(1,122)
Impairment of goodwill	**2,644**	200
Increase in trade and other receivables	**73**	(781)
Decrease/(increase) in inventories	**40**	(44)
Increase in trade payables, accruals and deferred income	**195**	480
Net cash used in operating activities	**(909)**	(52)
Cash flows from taxation	—	(383)
Cash flows from investing activities		
Purchase of property, plant and equipment	**(70)**	(248)
Payment of deferred consideration	**(8)**	—
Interest received	**7**	—
Net cash used in investing activities	**(71)**	(248)
Cash flows from financing activities		
Finance lease income received	**56**	16
Payment of finance lease liabilities	**(44)**	(30)
Interest paid	**(410)**	(404)
Net cash used in financing activities	**(398)**	(418)
Cash flows from discontinued operations		
Acquisition of remaining shares in Accent Telecom North Limited	—	(260)
Settlement of dispute with Chess ICT Limited	**(100)**	—
Net cash used in discontinued operations	**(100)**	(260)
Net decrease in cash	**(1,478)**	(1,361)
Cash at bank and in hand at beginning of period	**2,905**	4,266
Cash at bank and in hand at end of period	**1,427**	2,905
Comprising:		
Cash at bank and in hand	**1,427**	2,905

Notes to the consolidated financial information

1. General information
Adept4 plc is a public limited company incorporated in England and Wales under the Companies Act 2006. The Board of Directors approved this preliminary announcement on 14 February 2019. Whilst the financial information included in the preliminary announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("IFRS") as endorsed by the European Union, this announcement does not itself contain sufficient information to comply with all the disclosure requirements of IFRS and does not constitute statutory accounts of the Company for the years ended 30 September 2018 and 2017.

The financial information for the period ended 30 September 2017 is derived from the statutory accounts for that year which have been delivered to the Registrar of Companies. The statutory accounts for the year ended 30 September 2018 will be delivered to the Registrar of Companies following the Company's annual general meeting. The auditors have reported on those accounts; their reports were unqualified and did not contain a statement under s498(2) or s498(3) of the Companies Act 2006.

2. Basis of Preparation
The consolidated financial statements have been prepared in accordance with applicable International Financial Reporting Standards (IFRSs) as adopted by the EU and in accordance with the Companies Act 2006. The measurement bases and principal accounting policies of the Group are set out below. These policies have been consistently applied to all years presented unless otherwise stated.

3. Segment reporting
The Chief Operating Decision Maker ("CODM") has been identified as the directors of the Company and its subsidiaries, who review the Group's internal reporting in order to assess performance and to allocate resources. The CODM assess profit performance principally through adjusted profit measures consistent with those disclosed in the Annual Report and Accounts. The Board believes that the Group comprises a single reporting segment, being the provision of IT managed services to customers. Whilst the CODM reviews the revenue streams and related gross profits of three categories separately (Recurring Services, Product and Professional Services), the operating costs and operating asset base used to derive these revenue streams are the same for all three categories and are presented as such in the Group's internal reporting. Accordingly, the segmental analysis below is therefore shown at a revenue and gross profit level in line with the CODM's internal assessment, based on the following reportable operating segments:

Recurring Services	–	This segment comprises the provision of continuing IT services which have an ongoing billing and support element.
Product	–	This segment comprises the resale of solutions (hardware and software) from leading technology vendors
Professional Services	–	This segment comprises the provision of highly skilled resource to consult, design, install, configure and integrate IT technologies.

All revenues are derived from customers within the UK and no customer accounts for more than 10% of external revenues.
Inter-segment transactions are accounted for using an arm's length commercial basis.

3.1 Analysis of continuing results

The operating segments for 2017 have been restated to reflect the definitions used in 2018, in particular the Professional Services operating segment, which now includes all separable Professional Services revenues associated with Product and Recurring Services revenues, which have been unbundled to measure the contribution of our skilled technical resources. All revenues from continuing operations are derived from customers within the UK. This analysis is consistent with that used internally by the CODM and, in the opinion of the Board, better reflects the nature of the revenue.

3.1.1 Revenue

	2018 £'000	2017 £'000
Recurring Services	**7,100**	7,173
Product	**1,987**	1,957
Professional Services	**1,098**	1,171
Total Revenue	**10,185**	10,301

3.1.2 Gross Profit

	2018 £'000	2017 £'000
Recurring Services	**4,231**	4,566
Product	**439**	433
Professional Services	**1,035**	1,165
Total Gross Profit	**5,705**	6,164

4. Separately identifiable (costs)/income

Items which are material and non-routine in nature are presented as separately identifiable items in the Consolidated Income Statement.

	2018 £'000	2017 £'000
Settlement of warranty claim	**1,578**	—
Costs in relation to the warranty claim and other M&A activities	**(481)**	—
Settlement of historic Microsoft licence review	**(376)**	—
Impairment of goodwill (Note 8)	**(2,644)**	(200)
Integration and restructure costs	**(271)**	(121)
Costs in relation to disposal of Pinnacle CDT Limited	**(196)**	(100)
Write back of contingent consideration	—	1,122
Termination payment	**—**	(75)
Separately identifiable (costs)/income	**(2,390)**	626

The acquisition of Adept4 Managed IT Ltd ("MIT") on 26 May 2016 was for a total consideration of up to £7m, including up to £1.5m of contingent consideration, based on the financial performance of the Group in the calendar year to December 2017 and payable in March 2018. The performance targets for the contingent consideration were not achieved and this element of the consideration, the fair value of which was £1.1m, was credited to the Consolidated Income Statement in FY17.

During FY18, the Company brought a warranty claim against the vendors of the MIT business. The Company was successful with this claim and agreed a settlement in the sum of £1.6 million, in addition to confirmation that the contingent consideration was not payable. £0.6m of the settlement was payable to the Company in cash post-year end, with the balance extinguishing the Company's liability to pay the MIT vendors deferred consideration of £1.0m. Costs of £0.5m were incurred by the Company in relation to the warranty dispute and also in respect of corporate activity which was put on hold as a result of certain matters which led to the legal action and which have subsequently been resolved.

In assessing the level of settlement of the warranty claim which would be acceptable to the Company, various issues were considered, including a historic licencing review of the acquired business being undertaken by Microsoft. The Company has, post-year end, reached agreement with Microsoft in relation to this review, which resulted in a payment of £0.4m due to Microsoft in FY19. The liability in respect of this sum is provided for in these results.

Subsequent to the warranty claim and the non-achievement of the performance criteria in relation to the MIT earn out, the Board has assessed the carrying value of the Group's goodwill. Following an assessment of current budgets and forecasts for the Group, an impairment charge of £2.6m (FY17: £0.2m) has been made.

After the successful integration of the service-desk team into a single site in July 2017 and a number of efficiencies gained as a result of our investment in a single operating system, we were able to reduce the ongoing annualised cost base for the business by £0.6m by way of a restructure. The restructure incurred one-off costs of £0.3m in relation to redundancy costs, holiday pay and payments in lieu of notice. The cost reductions took place towards the end of the financial year and therefore the benefit of these will be seen in FY19.

In 2017, the Company identified the need for a provision following a dispute which related to the recovery of an asset included in the sale of the trade and assets of Pinnacle CDT Limited, a subsidiary of Adept4, to Chess ICT Limited ("Chess"). We resolved this dispute in September 2017, and this resulted in a payment of £0.1m by the Company in October 2017. In accordance with the settlement agreement, as the asset in question was not recovered by 30 September 2018, a further £0.1m became payable to Chess in October 2018. This liability has been provided for in these financial statements. Under the terms of the settlement agreement, we continue to pursue the asset on behalf of Chess, but the Company has no further liability.

5. Finance income and finance costs

Finance cost includes all interest-related income and expenses. The following amounts have been included in the Consolidated Income Statement line for the reporting periods presented:

	2018 £'000	2017 £'000
Interest income resulting from short-term bank deposits	**7**	**—**
Finance income	**7**	**—**
Interest expense resulting from:		
Finance leases	**10**	4
BGF loan notes	**400**	400
Effective interest on liability element of the BGF Loan Notes	**199**	199
Effective interest on deferred consideration relating to Adept4 Managed IT Ltd	**—**	239
Finance costs	**609**	842

6. Operating (loss)/profit

	2018 £'000	2017 £'000
Operating (loss)/profit is stated after charging:		
Depreciation of owned assets	**136**	162
Amortisation of intangibles	**907**	880
Operating lease rentals:		
– Buildings	**105**	114
Auditor's remuneration:		
– Audit of parent company	**20**	14
– Audit of subsidiary companies	**37**	36
– Audit costs relating to prior year	**28**	—
– Audit-related assurance services	**6**	5
– Corporation tax services	**16**	18

7. Loss per share

	2018 £'000	2017 £'000
Loss attributable to ordinary shareholders	**(3,807)**	(583)

	Number	Number
Weighted average number of Ordinary Shares in issue, basic and diluted	227,065,100	227,065,100
Basic and diluted loss per share	(1.68)p	(0.26)p

8. Intangible assets

Intangible assets	Goodwill £'000	IT, billing and website systems £'000	Brand £'000	Customer lists £'000	Total £'000
Cost					
At 1 October 2016	4,312	—	1,157	7,580	13,049
Additions	—	113	—	—	113
Adjustments to provisional fair values	135	—	—	—	135
At 1 October 2017	4,447	113	1,157	7,580	13,297
Additions	—	29	—	—	29
At 30 September 2018	**4,447**	**142**	**1,157**	**7,580**	**13,326**
Accumulated amortisation					
At 1 October 2016	—	—	(35)	(378)	(413)
Charge for the year	—	(7)	(115)	(758)	(880)
At 1 October 2017	—	(7)	(150)	(1,136)	(1,293)
Charge for the year	—	(20)	(115)	(772)	(907)
At 30 September 2018	**—**	**(27)**	**(265)**	**(1,908)**	**(2,200)**
Impairment					
At 1 October 2016	—	—	—	—	—
Charge in the year	(200)	—	—	—	(200)
At 1 October 2017	**(200)**	**—**	**—**	**—**	**(200)**
Charge in the year	(2,644)	—	—	—	(2,644)
At 30 September 2018	**(2,844)**	**—**	**—**	**—**	**(2,844)**
Carrying amount					
At 30 September 2018	**1,603**	**115**	**892**	**5,672**	**8,282**
At 30 September 2017	4,247	106	1,007	6,444	11,804
Average remaining amortisation period		**2.8 years**	**6.6 years**	**6.6 years**	**6.6 years**

In determining whether intangible assets including goodwill were impaired, the directors estimated the discounted future cash flows associated with the intangible assets over a ten year period. The directors also considered the release of the contingent consideration, the impact of the issues underlying the warranty claim and the reduction in Trading EBITDA during the year as indicators that the intangible assets were impaired. The goodwill was impaired by £2.6m during the year.

9. Property, plant and equipment

	IT equipment £'000	Fixtures, fittings and leasehold improvements £'000	Plant, machinery and motor vehicles £'000	Total £'000
Cost of assets				
At 1 October 2016	188	127	14	329
Additions	114	21	—	135
Disposals	—	—	(14)	(14)
At 30 September 2017	302	148	—	450
Additions	70	—	—	70
Disposals	(16)	—	—	(16)
At 30 September 2018	**356**	**148**	**—**	**504**
Depreciation				
At 1 October 2016	41	22	11	74
Charge for the year	111	48	3	162
Disposal	—	—	(14)	(14)
At 30 September 2017	152	70	—	222
Charge for the year	79	57	—	136
At 30 September 2018	**231**	**127**	**—**	**358**
Net book value				
At 30 September 2018	**125**	**21**	**—**	**146**
At 30 September 2017	150	78	—	228

10. Trade and other receivables

	2018 £'000	2017 £'000
Trade receivables	**1,343**	1,476
Warranty settlement (see Note 4)	**600**	—
Other Debtors	**36**	209
Prepayments and accrued income	**921**	664
Trade and other receivables	**2,900**	2,349

11. Trade and other payables

11.1 Current

	2018 £'000	2017 £'000
Trade payables	**1,102**	1,203
Accruals and deferred income	**1,937**	1,590
Finance leasing liability – short-term element	**32**	25
Other taxes and social security costs	**377**	490
Deferred consideration	**-**	987
Total current liabilities	**3,448**	4,295

11.2 Non-current

	2018 £'000	2017 £'000
BGF Loan Notes repayable to the BGF between three and seven years	**5,000**	5,000
Less fair value adjustment relating to the BGF Loan Notes	**(929)**	(1,128)
Fair value of BGF Loan Notes	**4,071**	3,872
Finance leasing liability – long-term element	**46**	42
Total non-current liabilities	**4,117**	3,914

12. Financial instrument

On 26 May 2016, the Company issued £5m unsecured loan notes ("Loan Notes") to the BGF with a seven-year term (although redemption is permissible from the third anniversary) with repayment between the fifth and seventh anniversaries in equal semi-annual repayments that carry interest at 8% per annum ("Coupon"). Assuming that the Loan Notes were held for seven years and not redeemed early, the maximum credit exposure at 30 September 2018, including interest, is £6.4m (FY17: £6.8m), of which £1.4m (FY17: £1.8m) relates to interest. As previously described, the Company also agreed to grant the BGF an option to subscribe for 50,000,000 Ordinary Shares of 1p at a subscription price of 6p any time before 26 May 2031. As the Loan Notes are unsecured, no collateral was offered to the BGF as security. The Loan Notes are not exposed to market interest rate increases over the term.

In accordance with IAS 32, the BGF Loan Note and share warrant elements were linked and treated as a single financial instrument and shown at fair value.

The fair value of the share options at 26 May 2016 (date of grant) has been calculated using the Black Scholes pricing model incorporating the following key assumptions:

- share price volatility of 40%;
- spot price of 6p per share;
- risk-free rate of 0.9%; and
- option period, aligned with the maximum amount of time the loan can remain outstanding.

Based on the assumptions above, the Black Scholes pricing model provided a fair value for the share option of 2.89p per share, which implied a total fair value for the share option of £1.4m. Based on the expected Coupon payments and repayment profile under the Loan Notes, this implies an effective borrowing rate of 15%. This resulted in a fair value of the loan amount at 26 May 2016 of £3.6m. The difference between the Coupon rate and the effective interest charge at 15% is charged through the Consolidated Income Statement over the life of the Loan Notes, and increases the outstanding Loan Note balance over time to match actual Coupon and capital cash repayments relating to the Loan Notes.

	Loan Note balance £'000	Carrying value Loan Notes £'000	8% interest payable £'000
Cash received from the BGF on 26 May 2016 for Loan Notes at 8% per annum interest	5,000	—	—
At 30 September 2017	5,000	3,872	—
Interest on Loan Notes at 8% per annum for the year to 30 September 2018	—	—	400
Notional interest on liability element of the BGF Loan Notes to 30 September 2018	—	199	—
At 30 September 2018	**5,000**	**4,071**	**400**

13. Post-balance sheet events

Maintaining strong relationships with existing customers, together with protecting the Group's cash balances and shareholder value are the key objectives of the Board. The Board has therefore taken the decision to focus on the existing customer base with less emphasis on new business acquisition, which has an upfront cost to the business and takes time to come through. This is designed to protect the cash reserves of the Group whilst the Board considers the strategic options open to the Company. This will lead to reduced revenue and gross profit but requires a significantly lower operating cost base, which should enable the Group to return to profitability and positive cash generation. To that end, post year end, further cost savings have been identified which are in the process of being implemented.