**17 March 2020**

**Gamma Communications plc**
**Results for the year ended 31 December 2019**

**Strong execution against all strategic priorities**

Gamma Communications plc ("Gamma" or "the Group"), a leading, technology based provider of communication services to the business markets in the UK and the Netherlands, is pleased to announce its results for the year ended 31 December 2019.

| | **Year ended 31 December** | | |
|---|---|---|---|
| | **2019** | **2018** | **Change (%)** |
| Revenue | £328.9m | £284.9m | 15% |
| Gross profit | £166.5m | £132.2m | 26% |
| *Gross margin* | *51%* | *46%* | |
| Profit from operations | £45.5m | £34.4m | 32% |
| Adjusted EBITDA | £63.5m | £48.3m | 31% |
| PBT | £45.2m | £34.5m | 31% |
| Adjusted PBT | £48.1m | £34.9m | 38% |
| EPS (Fully Diluted, "FD") | 36.1p | 30.0p | 20% |
| Adjusted EPS (FD) | 40.8p | 30.3p | 35% |
| Total dividend per share | 10.5p | 9.3p | 13% |
| Cash generated by operations | £54.0m | £40.6m | 33% |
| *Cash generated by operations / adjusted EBITDA* | *85%* | *84%* | |

*All adjusted measures set out above and throughout this document which are described as "adjusted" represent Alternative Performance Measures ("APMs") and are separately presented within the statement of comprehensive income or reconciled in the Financial Review section or segment note and are applied consistently. Where reference is made to adjusted EPS this is stated on a fully diluted basis. Definitions of APMs are included in the Financial Review. Our policy on the use of APMs is included in note 2.*

**Key Highlights**

Continued strong growth across the major product groups in the United Kingdom:

- The number of installed SIP Trunks increased from 856,000 at 31 December 2018 to 1,016,000 at 31 December 2019 (+19%).
- The number of Horizon (Cloud PBX) users increased from 435,000 to 522,000 (+20%). The main growth area was in the SME segment which is Gamma's target market segment.
- Collaborate, the fully integrated Unified Communications upgrade to Horizon which was launched in March 2019, already has over 9,000 users.
- To support our UCaaS strategy, in November we acquired Telsis Direct Limited, Telsis Communication Services Limited, Telsis Services Limited and Telsis GmbH (together "Telsis") which brings a development capability and will enable us to launch a fully integrated cloud contact centre solution in late 2020.
- Our connectivity products have continued to perform well as part of our overall solution strategy. Broadband has increased from 94,000 units (at 31 December 2018) to 111,000 (+18%) and Ethernet from 8,370 to 13,900 (+66%). Mobile connections have increased from 50,000 to 62,000 (+24%).

The main business units continued to perform well:

- The UK Indirect business continues to grow strongly with a focus on the existing partner base. Gross profit increased from £97.5m in 2018 to £119.1m in 2019 (+22%).
- The UK Direct business continues to deliver very positive growth, with gross profit up from £32.8m in 2018 to £38.2m in 2019 (+17%).
- In February 2020, we acquired Exactive Holdings Ltd ("Exactive"), a unified communications specialist with expertise in Microsoft Teams. Exactive will help us address a part of the market that is already embedded in a Microsoft ecosystem and this will be an essential part of our UCaaS strategy. Following the acquisition of Telsis this is another key step in Gamma's strategy to become the leading provider of Unified Communications as a Service ("UCaaS").
- In our Overseas business, the integration of our Dutch businesses went well in the year. In the first half we had reported a greater than expected drop off in ISDN revenue. We are pleased to say that the second half performance was stronger. Gross profit increased from £1.9m in 2018 to £9.2m in 2019. This represents a full year of DX Groep which was acquired in October 2018 and the benefit of Nimsys which was acquired in February 2019. The number of Cloud seats at the end of 2019 was over 22,000 and the mobile base added 7,000 connections in 2019.
- In February 2020 we made an offer to acquire VozTelecom OIGAA360, SA ("Voz Telecom") in Spain which will give us access to the attractive Spanish market. We expect the acquisition to complete in April.

Andrew Taylor, Chief Executive Officer, commented,

*"We have delivered a strong business performance and an excellent set of financial results for 2019, with both our UK Indirect and UK Direct businesses continuing to grow well. Despite an increasingly competitive market, our product performance was positive, and during the period we continued to strengthen our market capabilities, through the development and launch of new products and services. Our Dutch business continues to build market share and we will shortly be operating in Spain following the acquisition of Voz Telecom. Through the acquisition of both Telsis and Exactive, we are executing against our UCaaS strategy, while ensuring that we continue to strengthen both our direct and indirect channel propositions."*

**Enquiries:**


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## Notes to Editors

Gamma is a leading supplier of Unified Communications as a Service (UCaaS) to the business markets in the UK and the Netherlands. Providing a range of Unified Communications, Mobile and Connectivity services, Gamma provides robust and secure solutions that enable organisations to communicate, collaborate and offer a better customer experience.

Gamma's largest market is in the UK where the company's network-based services are supplied to the SME, public sector and enterprise markets, through a large network of over 1000 channel partners and its own direct sales and support capabilities. In addition, Gamma owns UK-based Unified Communications infrastructure provider Telsis, which also has a small presence in Germany, and Exactive, which specialises in Microsoft Teams.

In the Netherlands, Gamma owns DX Groep which owns Dean One (a telecom and internet provider supplying VoIP, Mobile and Broadband services through over 600 channel partners), Nimsys (an ICT specialist for workspaces and multi-tenancy buildings) and Schiphol Connect (the communications and high speed internet service provider at Schiphol Airport in the Netherlands).

Gamma is expanding its UCaaS presence in Europe and has a desire to grow its family of businesses with a focus on digital automation, delivering Gamma-powered services to SME customers largely via a network of channel partners.

**Chairman's statement**

**Overview of results**

Group revenue for the year ended 31 December 2019 increased by £44.0m to £328.9m (2018: £284.9m) an increase of 15% on the prior year. Adjusted EBITDA for the group increased by 31% to £63.5m (2018: £48.3m). Fully diluted earnings per share for the year increased by 20% to 36.1p (2018: 30.0p). Adjusted fully diluted earnings per share for the year increased by 35% to 40.8p (2018: 30.3p). On a statutory basis PBT and profit from operations both increased by over 30%.

The cash generated by operations for the year was £54.0m compared to £40.6m in 2018. The closing cash balance for the year was £53.9m compared to £35.5m at the end of December 2018. This cash balance has been increased whilst investing £12.4m on capital items, £7.5m on acquisitions and paying £9.2m in dividends.

**Overview of the year**

As outlined in this report, the year has been a period of strong strategic execution for Gamma with highlights including: –

- We launched Collaborate and a new Call Recording platform to expand our UCaaS offering, in November, we acquired Telsis which will enable us to develop a Contact Centre solution for release towards the end of 2020.

- Strong growth in our key products in the UK of SIP Trunking (units increase by 19%) and Cloud PBX (units increased by 20%).

- In addition, in March 2020, we acquired Exactive which enables us to support enterprise and public sector customers who choose solutions using Microsoft Teams. This represents a fundamental part of our UCaaS strategy.

- In the Netherlands we grew our Cloud seats to over 22,000. We also acquired Nimsys in February 2019, its integration has gone well and Nimsys is growing strongly. The performance of Dean One in the second half improved following a disappointing first half.

- We continue to focus on European expansion and throughout 2019 we conducted discussions with a number of potential acquisitions. In February 2020, we made an offer for Voz Telecom in Spain which (when complete) will provide us with a foothold into the Spanish market which is set to grow significantly over the coming years.

**Board and employees**

I was delighted to welcome Henrietta Marsh to the board on 16 April 2019. She brings a wealth of experience gained from serving on the boards of both private and listed companies. Henrietta will chair the Remuneration Committee after the upcoming AGM. Gamma has a strong and experienced Board. We have improved our diversity on the Board and within the Senior Management Team in the last year but there is more to do and we will consider this with future appointments.

The business now has 1,176 employees. We continue to invest in all our employees and in particular we assist apprentices to gain valuable work experience, to continue their education and to obtain nationally recognised qualifications. At present, we have 24 apprentices employed in IT, HR, Infrastructure Support, Software Development, Sales and Customer Service. We have a good track record of offering permanent employment at the end of these apprenticeships and expanding opportunities for apprentices across the business remains a priority for Gamma. We consider diversity to be an important part of our culture at Gamma and run a number of programmes across our business to support and promote this.

We encourage all employees to own shares in the company and in July 2019, we used our SIP Trust to award £500 of free shares to all of our UK employees. The company also offered a sharesave scheme for the fourth year. Once again, it was particularly pleasing to see the exceptionally high take up, with 459 staff choosing to participate in the scheme (2018: 257). Finally, we have launched an “Evergreen SIP” scheme which gives employees another opportunity to buy shares in the company in a tax efficient way.

The Board recognises the high levels of support and commitment from its staff through a period of significant strategic planning and implementation and would like to express its thanks for their dedication, hard work and enthusiasm.

**Dividend**

Gamma remains committed to a progressive dividend policy which has increased between 10-15% every year since we listed in 2014. Gamma has paid one third of the dividend as an interim dividend with the final two thirds paid as a final dividend once the results for the full year are known.

The Board is pleased to propose a final dividend, in respect of the year ended 31 December 2019, of 7.0 pence per share (2018: 6.2 pence) an increase of 13%. Subject to shareholder approval at the forthcoming AGM, this will be payable on Thursday 18 June 2020 to shareholders on the register on Friday 29 May 2020. When added to the 3.5 pence interim dividend (2018: 3.1 pence) this makes a total dividend declared of 10.5 pence for the year as a whole (2018: 9.3 pence).

**Governance**

During 2018 we adopted the QCA Corporate Governance Code (2018 edition) (the ‘QCA Code’).

**Environmental**

As a business which enables other companies to reduce their carbon footprint by communicating and collaborating from multiple sites and thereby avoiding travel, we continue to challenge ourselves on our own environmental credentials. We run a certified CarbonNeutral© network and we have also now committed to supporting the UN Sustainable Development Goals.

The Board has considered the emerging effects of climate change on the future of the business and we consider them to be low risk.

**Outlook**

The Board is positive about the outlook for the Group in 2020 and beyond.

We have discussed the potential impact of Covid-19 on the business which (to date) has been very limited. Notwithstanding, this remains a matter of close attention for the Board. In particular we will take measures to ensure the safety of our channel partners, customers, employees and other stakeholders. We are taking regular advice and following guidance from the government and public bodies. We have a sub-group of our Senior Leadership Team who are monitoring the situation on a daily basis and communicating the latest advice to staff.

With respect to our day-to-day operations we are able (should it become necessary) to operate our business with almost all staff working from home. We have stress tested our network to ensure that this is achievable. We believe we will be able to continue to support our customers fully.

The potential impact of the Covid-19 health crisis on the short-term results is difficult to assess at this time. We have a resilient business model and at this point we have seen little effect on our business. We suspect that we may see fewer orders as channel partners and end customers are beginning to introduce travel and meeting restrictions which will make customer visits and lead generation more difficult. With respect to existing orders, installations which require engineers to visit a site are also likely to be delayed and hence revenues will be delayed. At the time of writing it is impossible to know how long this situation is likely to continue for. We have a strong balance sheet and a robust business model and we expect to be able to weather the crisis.

In the longer term, our product set is well suited to organisations that wish to be able to work remotely or as part of their disaster recovery plans. Whilst the current crisis is not desirable, we believe that the experience will demonstrate the advantages of UCaaS to businesses of all sizes across all industries.

As a predominantly channel-focused business, Gamma will continue to concentrate efforts and investment on strengthening our relationship and capabilities to support the channel to be successful both in the UK and mainland Europe. We will also ensure that in the direct business, we continue to focus on growth with larger enterprises and the public sector, and on building on an already strong reputation for operational excellence and service quality. Our support for enterprise customers may involve offering solutions which will include products from other suppliers (for example Microsoft Teams) as well as our own product set.

**Richard Last**
**Chairman**

**Chief Executive Review**

I am pleased to report another excellent set of financial results for 2019 which demonstrates the initial success of the strategy which we set out at the start of 2019.

As well as executing against our short-term commitments, throughout 2019 we focused heavily on planning and executing against our medium and longer-term growth strategy for Gamma.

Both our Direct and Indirect channel businesses have continued to perform strongly, and throughout 2019 we were awarded several new multi-year customer and partner contracts. This has enabled us to strengthen both our contracted backlog and revenue and margin visibility, ensuring that we continue to benefit from a very high percentage of recurring revenue and margin.

We have continued to invest and strengthen our sales, service and delivery capabilities across Gamma, and our continued focus and investment on product development will deliver new and exciting product launches during 2020, including a cloud contact centre offering. Development of a cloud contact centre offering is a frequent request from channel partners and end users and will open up a part of the market in the larger SME space. Supporting the success of our indirect channel partners is a priority, and we continue to develop and strengthen our self-serve partner portal, while ensuring that our digital platforms (Gamma Academy and Gamma Accelerate) enable our partners to create new opportunities, win market share and drive increased levels of revenue and margin for both their businesses and Gamma.

The Gamma Academy delivered 19,992 training courses to channel partners during 2019 (2018: 16,602). Gamma Accelerate delivered a significant increase in marketing campaigns run by channel partners during the period with 870 of Gamma's partners now actively using the platform (2018: 732).

We offer a product set which can be used by other businesses to reduce their carbon footprint and we are proud that we are certified CarbonNeutral©. Notwithstanding, we continue to work hard to reduce our energy consumption. We last monitored our CO2 emissions between July 2017 to June 2018 which were 2,332 tonnes of CO2. This was a reduction of 5% compared to the previous twelve months.

**Strategy**

Our strategy has four key elements.

***Evolve our strong cloud telephony position into the Unified Communications as a Service ("UCaaS") market***

We focus on the UCaaS market in the UK and Europe and this is expected to grow by 12% annually over the coming five years.

We continue to execute well in the UK and are one of the market leaders in both our core products of SIP and Cloud PBX. In SIP Trunking we have now increased our market share to 31% in the UK. In Cloud PBX we have increased the number of seats from 435,000 to 522,000 which gives us a market share of 11%.

As a first stage in building a broader UCaaS proposition, we launched a suite of Collaboration services in the first half of 2019. Gamma Collaborate launched as a fully integrated bolt-on to our market leading Horizon product and now has 9,000 users. We also launched a new integrated Gamma call recording service and a Subscription Management Service, which enables our partners to better manage their estate of seats on the platform.

In November 2019, we acquired Telsis for £4.3m which brings additional product and software development capabilities to Gamma, and which will allow us to launch a fully integrated cloud contact centre module into our UCaaS suite later in 2020.

In the Netherlands we have increased Cloud seats to 22,000 and in February 2020, we made an offer to acquire Voz Telecom in Spain which (if accepted by the shareholders) will give us 40,000 Cloud PBX seats in the Spanish market.

By growing our base of SIP and Cloud customers and developing new integrated modules we are able to upsell and cross-sell into our existing customer base as well as selling to end users who require more functionality.

Where enterprise customers require the functionality of Microsoft Teams, we have now launched a variant of our SIP product which is technically better suited to Teams. This has a commercial wrap which will enable our indirect channel partners to sell SIP more easily alongside Teams. We also acquired Exactive in February 2020 which provides us with the capability to deploy Teams into customers who require this solution.

***Build on our Fixed and Mobile Telecom strength to differentiate our proposition from pure "Over the Top" (OTT) players***

As part of our detailed analysis of the marketplace and our long term strategy development during the year, we reinforced our view that being able to offer a fully integrated suite of connectivity products will be a key differentiator for us from other Cloud PBX providers who only offer an "over the top" software solution.

We continue to offer data access services (Broadband and Ethernet) in the UK and we ended the year with 111,000 Broadband circuits and 13,900 Ethernet circuits.

The business focused Data services market is undergoing a change, driven by the investment in fibre services from the current large players, such as BT and TalkTalk, and new infrastructure providers such as CityFibre. This is effectively developing a model where services such as Fibre to the Premises ("FTTP") and Fibre to the Cabinet ("FTTC") can provide high bandwidth broadband services at a cost-effective price that will meet the requirements of the majority of SME businesses. Ethernet services will be used to support larger SME / Midmarket customers as they will move to the higher bandwidth services which Ethernet offers to future proof their requirements. Gamma continues to work with BT, TalkTalk and other suppliers to ensure that we can offer a full suite of high bandwidth services to customers as the market evolves.

Some users will access our service over mobile data links (either in addition to or instead of fixed fibre). In the UK we have an agreement with Three UK and started a project to move to a new platform which will give customers increased functionality (for example 5G) but at a reduced cost to Gamma. We expect the new service to go live in early 2021 and for cost savings to be recognised towards the end of 2021.

In the Netherlands, we signed a long term strategic partnership with T-Systems in December 2018 which has enabled us to strengthen our proposition and market position with both our direct customers and indirect channel partners. In the course of the first year we have added 7,000 mobile users.

***Expand to Europe to gain continued growth and scale***

We were disappointed with the performance of our Dutch business in the first half of 2019 as the announcement by the incumbent of the imminent closure of ISDN as a product resulted in revenues falling more rapidly than expected in this legacy part of the business. However, performance was better in the second half and our largest Dutch business (Dean One) continues to increase its Cloud seats and Mobile connections. Throughout 2019, we focused on strengthening both our product and partner proposition across the Dutch market. In order to provide additional scale and capability, we also acquired Nimsys in February 2019, which has performed particularly well, and we are also happy with the performance of Schiphol Connect.

As highlighted previously, we have made an offer to acquire Voz Telecom, which is the fourth largest Cloud PBX business in Spain (after the established telecoms providers such as the Mobile Network Operators "MNOs"). The acquisition of Voz Telecom will provide us with an important foundation within a key cloud growth market, which represents a key part of our European expansion strategy. Voz Telecom supplies c40,000 Cloud PBX seats which equates to a market share of c5%.

With an overall market size of c18m PBX seats (slightly smaller than the UK market) and a cloud penetration of only c5%, the Spanish market for Cloud PBX is forecast to grow rapidly in the future.

We continue to monitor and assess other acquisition opportunities in both the Dutch and Spanish markets, which will complement and strengthen our position in both countries. In addition, and as part of our stated strategy, we continue to assess acquisition opportunities in both the German and French markets, both of which are characterised with low cloud penetration levels and significant future growth potential.

We do not expect Brexit to affect our plans for expansion or, indeed, to have a materially detrimental effect on the existing business.

***Continue to build on our digital capabilities to assure agility and sustain competitiveness***

We continue to invest in key programmes which will enable our digital transformation.

Our strategic aim is to build a digital platform that will enable us to manage our business and to serve our customers more effectively and efficiently. The first objective is to scale and grow economically by taking as many manual processes out of our back-office systems. The second objective is to maintain our position of being easy to do business with. We will build systems which will allow partners and end users to self-order, provision and serve.

In 2019 we deployed Release 1 of the "Gamma Hub", our whole business digital platform that will underpin the continued rapid growth of our direct business. Release 1 is the foundation stage of a four-year programme that will transform us into a digital-first organisation and assure agility and sustain competitiveness through intelligent automation and customer self-serve.

In this release, we delivered a single customer support and ticketing platform which will support direct customers across all of our market segments and all of our products and services, with a rich engagement and support tool. This allows us to create deeper more meaningful relationships with each and every customer. Additionally, we deployed a new customer CRM tool with market-leading sales and marketing automation allowing us to track, nurture and develop opportunities and customers, from our very first engagement, through to in-life support.

In 2020 we will be implementing Release 2, which will start to transform our customer delivery and service management processes creating one seamless and 'digitally connected' experience across the whole customer lifecycle. As part of this phase, we will be streamlining our operating model to lay the foundations for delivering a consistent, high quality yet tailored service experience at scale across all our customer segments.

**Gamma values**

During 2019 we surveyed our staff to understand the values which underpin Gamma as an organisation. We were delighted with the level of engagement and response from our staff, and that a number of common themes emerged across all groups of staff at all locations. We have distilled all of these contributions to agree Gamma's core Values:

- Aim high
- Consider others
- Think differently
- Stronger together

These values were launched in early 2020 as part of a companywide values program, which included a full brand refresh and the launch of our new Gamma websites. We also introduced a new company strapline "Working Smarter Together" which seeks to sum up our aspirations as a business. In addition to this, we also refurbished our offices across Gamma with a particular focus on our Manchester and Glasgow offices.

**Environmental considerations**

We take our responsibilities to the wider environment seriously. As a business which is based on multiple sites, we encourage our people not to travel but rather to use our own collaborative communications tools which both reduces our carbon emissions and promotes employee wellbeing. One of our core values is "Consider Others" and as part of this we aim to reduce both our waste and our carbon footprint. We are conscious of our power consumption and seek to buy capital equipment which uses less power than the legacy items it replaces.

**Summary and outlook**

I continue to be very pleased with the execution of both our short-term business objectives and our longer term 2023 strategy, which we outlined during January 2019 – the business is in good shape and our outlook is positive. We have a robust business model with a high level of recurring revenue and margin, and we continue to stay focused on developing the products and services which enable our customers and our channel partners to be successful and win market share in their respective markets. We continue to see competition across all core market segments, including the UCaaS, data and mobile product areas, where we believe we will see continued price pressure. However, the quality and competitiveness of our products and the strength of our direct and indirect channel businesses provides confidence that we will continue to execute against our commitments.

Throughout 2020 we will build on each of our strategic pillars:

- In UCaaS we will strengthen our partner and end-customer proposition through the launch our fully integrated cloud contact centre module and continue to develop the roadmap for our UCaaS product suite.
- We will work with our strategic partners to deliver quality access technologies (ethernet, broadband and mobile) at competitive prices
- We will continue to build our business in the Netherlands and continue to look for additional suitable acquisition opportunities to further develop our business across continental Europe.
- We will further develop our portals internally and externally to give our customers and staff the best digital experience within our industry.

As a final point, I would like to personally thank our staff, partners and customers for their contribution and ongoing support. Our performance during 2019 has been strong, and we remain optimistic about Gamma's future growth prospects.

The Chairman's outlook statement provides our current assessment of the impact of Covid-19 on our future performance.

**Andrew Taylor**
**Chief Executive Officer**

**Financial review**

Gamma has performed well during the year, increasing revenue by 15% to £328.9m and gross profit by 26% to £166.5m. We have seen this strong performance across all the main areas of the business. This has resulted in adjusted EPS of 40.8p, an increase of 35% from the prior year.

**Revenue and gross profit**

*UK Indirect*

| | 2019 | 2018 | Increase |
|---|---|---|---|
| | £m | £m | |
| Revenue | 230.1 | 210.6 | +9.3% |
| Gross Profit | 119.1 | 97.5 | +22.2% |
| Gross Margin | 51.8% | 46.3% | |

Within the UK Indirect business, the gross profit from the traditional business (which includes calls and lines and trade with other carriers) has seen a slight increase from the previous period which is contrary to the trends seen over the past few years. The call and lines part of the business continues to decline but Gamma is now providing IP telephony services to other carriers which is offsetting this.

We group our data, mobile, SIP and Cloud PBX products as our “growth” products and revenue from growth product sales increased from £162.7m to £186.5m (+15%) and gross profit grew from £85.6m to £106.7m (+25%). The gross margin grew from 53% to 57%, which reflects the fact that the main contributors to this growth were SIP Trunking and our Cloud PBX product (Horizon) which have higher margins than other products. Despite price pressure in Cloud PBX, margins are holding up due to fewer calls being used within bundled offerings.

*UK Direct*

| | 2019 | 2018 | Increase |
|---|---|---|---|
| | £m | £m | |
| Revenue | 83.6 | 70.9 | +17.9% |
| Gross Profit | 38.2 | 32.8 | +16.5% |
| Gross Margin | 45.7% | 46.3% | |

The UK Direct business continues to grow strongly. The growth was mainly attributable to sales to enterprise customers increasing by £8.3m. In Mid-Market revenue increased by £2.4m and public sector grew by £2.1m. This business continues to move from selling to smaller customers to larger enterprise businesses and public sector customers on multi-year deals. The order book remains strong with significant customer wins anticipated in the second half.

The gross margin fell slightly because the margin on larger customers tends to be lower and also more of the new business wins have a higher proportion of access sales (typically Ethernet) which has a lower margin than the voice applications suite of products.

*Overseas*

| | 2019 | 2018 | Increase |
|---|---|---|---|
| | £m | £m | |
| Revenue | 15.2 | 3.4 | +347.1% |
| Gross Profit | 9.2 | 1.9 | +384.2% |
| Gross Margin | 60.5% | 55.9% | |

Gamma acquired DX Groep in October 2018 and Nimsys in February 2019. Consequently, it should be noted that the growth in the overseas business is not organic. As reported at the half year, the performance of the DX Groep business in the first half was below expectations as a significant amount of legacy ISDN business ceased due to changes made by the incumbent network provider in the Netherlands. In the second half, the performance of the business has improved and sales of Cloud PBX and Mobile were strong. Nimsys has also exceeded our expectations.

The initial acquisition price for DX Groep was £11.5m and no further consideration will be paid due to a greater than expected drop off of ISDN revenue in 2019. As a result, the liability for contingent consideration has been reduced to nil with an equivalent reduction in the carrying value of associated assets. This is discussed under exceptional items below.

The initial acquisition price for Nimsys was £3.7m with up to a further £3.2m payable dependent on performance in 2019 and 2020. Given the performance of Nimsys in 2019, we now estimate that all of the contingent consideration is likely to be paid. Therefore, the aggregate consideration for the two Dutch businesses is likely to be £18.4m.

**Operating expenses**

Operating expenses grew from £97.8m to £121.0m.

We break these down as follows:

| | **2019 £m** | **2019 £m** | **2018 £m** | **2018 £m** | **Growth** |
|---|---|---|---|---|---|
| Expenses included within cash generated from operations | | | | | |
| - UK Indirect Business | 64.9 | | 60.6 | | +7.1% |
| - UK Direct Business | 20.1 | | 16.4 | | +22.6% |
| - Overseas Business | 8.9 | | 2.3 | | +287.0% |
| - Central Costs | 6.5 | | 2.7 | | +140.7% |
| | | 100.4 | | 82.0 | |
| Depreciation and amortisation | | | | | |
| – tangible and intangible assets | 13.4 | | 12.1 | | +10.7% |
| – right of use assets | 1.7 | | 1.4 | | +21.4% |
| – acquisition | 2.0 | | 0.4 | | +400.0% |
| | | 17.1 | | 13.9 | |
| Share based payments | | 2.6 | | 1.9 | +36.8% |
| Exceptional items | | 0.9 | | - | |
| **Operating expenses** | | **121.0** | | **97.8** | **+23.7%** |

Movements in cash based expenses were driven by:

- Within the UK Indirect Business, operating expenses have grown by 7.1% (compared to Gross Profit growth of 22.2%). This demonstrates the success of programmes we have undertaken historically to ensure that we are running the business more efficiently.
- In the UK Direct business, overhead increased by 22.6% (compared to Gross Profit growth of 16.5%). The level of increase is mainly driven by our investment in our digital strategy programme, but we also continue to invest in additional sales heads to grow the business.
- The increase in overseas costs is reflective of the inorganic growth and a full year of the DX Groep.
- Central Costs have increased significantly year on year, which is due to a number of factors. The first is that we are building a group function in anticipation of operating several businesses around Europe over the coming years. A second factor is the cost of our strategy project. Finally, we have incurred significant due diligence costs on acquisitions - some of which have completed whilst some were rejected.

Depreciation and amortisation on tangible and intangible assets has increased from £12.1m in 2018 to £13.4m in 2019. This is driven by increased capital expenditure over the past few years. The annual depreciation charge is now in line with the annual capital expenditure spend and is not expected to increase significantly.

Share based payment costs have increased during the year because more executives have been included within the scheme and the rising share price has made the costs of employers NI for share grants higher than in previous years.

**Exceptional Items**

There were a number of exceptional transactions in the year, but all relate to the acquisition of either the DX Groep or Nimsys (both in the Netherlands).

*DX Groep*

An exceptional item relates to the contingent consideration which is due for the acquisition of the DX Groep. In preparing the statutory accounts for 2018 we made our best estimate of the contingent consideration. During 2019 a higher than expected attrition rate of legacy customers taking ISDN caused the revenues to be lower than expected. It should be noted that the margins made on ISDN in the Netherlands (c.40%) are much higher than in the UK and therefore this acceleration of churn from legacy products has had a disproportionate effect on profit. This means that we have both revised our estimate of the contingent consideration due and have also considered whether the intangible assets and goodwill which were acquired with the business require reduction.

As a result of the above there are three exceptional items:

- A credit of £8.1m arising from the release of the contingent consideration.
- A debit of £3.9m arising from the reduction in carrying value of the intangible assets.
- A debit of £4.2m arising from the reduction in carrying value of goodwill.
- .

In addition to the exceptional items a credit of £1.0m relating to deferred tax movements in connection with the reduction in carrying value of intangible assets has been included within "adjusting tax items".

*Nimsys*

With respect to Nimsys, the opposite had occurred – the business had performed better than originally expected which meant our initial estimate of contingent consideration was too low and therefore it now needs to be increased.

Following the initial recognition of Nimsys contingent consideration in February 2019, the contingent consideration has been remeasured at the reporting date. The overall balance due has increased by £0.9m which we have charged to the statement of comprehensive income. There is no tax effect.

None of the items relating to either transaction are cash items. The alternative performance measures referred to herein have been adjusted for all of these items.

**Alternative performance measures**

Our policy for alternative performance measures is set out in note 2.

The tables below reconcile the alternative performance measures used in this document:

***2019***

| Measure | Statutory basis | Amortisation of intangibles | Adjusting tax items | Exceptional items** | Adjusted basis |
|---|---|---|---|---|---|
| EBITDA* (£m) | 62.6 | - | - | 0.9 | 63.5 |
| PBT (£m) | 45.2 | 2.0 | - | 0.9 | 48.1 |
| PAT (£m) | 34.5 | 2.0 | 1.6 | 0.9 | 39.0 |
| EPS (FD) (p) | 36.1 | 2.1 | 1.7 | 0.9 | 40.8 |

***2018***

| Measure | Statutory basis | Amortisation of intangibles | Adjusting tax items | Exceptional items** | Adjusted basis |
|---|---|---|---|---|---|
| EBITDA* (£m) | 48.3 | - | - | - | 48.3 |
| PBT (£m) | 34.5 | 0.4 | - | - | 34.9 |
| PAT (£m) | 28.4 | 0.4 | (0.1) | - | 28.7 |
| EPS (FD) (p) | 30.0 | 0.4 | (0.1) | - | 30.3 |

** Profit from Operations is the nearest equivalent statutory measure to EBITDA and is reconciled on the Consolidated Statement of Comprehensive Income and Note 3 (Segmental Analysis).*
*** See note 4 for further details.*

**Adjusted EBITDA and EBITDA**

The combination of increasing sales of new products and operational improvements means that EBITDA grew from £48.3m in 2018 to £62.6m or 30% and adjusted EBITDA grew from £48.3m in 2018 to £63.5m or 31%.

**Taxation**

The effective tax rate for 2019 was 24% (2018: 18%). This rate is inflated by adjusting tax items of £1.6m and tax on business combinations of £0.5m – neither of these are cash items. The underlying tax rate (ignoring these adjustments) would have been 19%.

**Cash flows**

The cash balance at the end of the year was £53.9m, up from £35.5m at the end of the previous year.

The ratio of adjusted EBITDA to cash generated from operations was 85% (2018: 84%).

Significant non-operational spend items were:

- Capital spend was £12.4m, which is a decrease from £12.7m in the comparative period. This is discussed below.
- £7.5m was paid for acquisitions net of cash acquired (2018: £11.1m) of which £3.4m was paid for the acquisition of Nimsys and £4.1m for Telsis
- £9.2m was paid as dividends (2018: £8.1m)

Capital spend in 2019 was £12.4m (2018: £12.7m) as follows:

- Regular spend on maintaining and increasing capacity on the core network was £12.4m (2018: £11.6m):
    - £9.9m was the cost of increasing capacity and development of the core network as well as other minor items such as IT and fixtures and fittings (2018: £9.1m).
    - £1.4m was the capitalisation of development costs incurred during the period (2018: £1.3m).
    - £1.1m was spent with third party software vendors for the software which underpins our Cloud PBX product (2018: £1.2m).

- Project spend in the current period was £nil (2018: £1.1m was spent on the national network).

The Group continues to have no external debt and a number of lenders have indicated that they would be willing to support the Group with debt were it to be required for capital expenditure programmes or M&A activity.

**Adjusted EPS (FD) and EPS (FD)**

Adjusted EPS (FD) increased from 30.3p to 40.8p (35%). The growth in adjusted EPS (FD) has been significant due to the strong trading described earlier. Adjusted EPS is EPS as adjusted for exceptional items as defined in note 4 and this is shown in the table above.

EPS (FD) grew from 30.0p to 36.1p (20%). The growth is lower than the adjusted metric because, in the current period, there is an increase in the exceptional amortization relating to business combinations as well as charge for change in value of deferred consideration which was not present in the prior year. There was also an abnormal tax charge relating to a prior year adjustment in the deferred tax balance. These items are in part offset by an exceptional tax credit relating to the reduction in intangibles.

**Dividends**

The Board has proposed a final dividend of 7.0p (2018: 6.2p). This is an increase of 13% and is in line with our progressive dividend policy.

Subject to shareholder approval, the final dividend is payable on Thursday 18 June 2020 to shareholders on the register as at Friday 29 May 2020.

**Andrew Belshaw**
**Chief Financial Officer**

# Consolidated statement of comprehensive income

For the year ended 31 December 2019

| | Note | **2019 £m** | 2018 £m |
|---|---|---|---|
| **Revenue** | 3 | **328.9** | 284.9 |
| Cost of sales | | **(162.4)** | (152.7) |
| **Gross profit** | | **166.5** | 132.2 |
| Operating expenses | | **(121.0)** | (97.8) |
| **Earnings before depreciation, amortisation and exceptional items** | | **63.5** | 48.3 |
| Exceptional items | 4 | **(0.9)** | - |
| **Earnings before depreciation and amortisation** | | **62.6** | 48.3 |
| Depreciation and amortisation (excluding business combinations) | | **(15.1)** | (13.5) |
| Amortisation arising due to business combinations | | **(2.0)** | (0.4) |
| **Profit from operations** | | **45.5** | 34.4 |
| Finance income | | **0.1** | 0.3 |
| Finance expense | | **(0.4)** | (0.2) |
| **Profit before tax** | | **45.2** | 34.5 |
| Tax expense | 5 | **(10.7)** | (6.1) |
| **Profit after tax** | | **34.5** | 28.4 |
| Other comprehensive loss | | **(0.4)** | (0.2) |
| **Total comprehensive income attributable to the owners of the parent** | | **34.1** | 28.2 |
| **Earnings per share** | | | |
| Basic per Ordinary Share (pence) | 6 | **36.6** | 30.3 |
| Diluted per Ordinary Share (pence) | 6 | **36.1** | 30.0 |

*Adjusted earnings per share is shown in note 6*

# Consolidated statement of financial position

As at 31 December 2019

| | Note | 2019 £m | 2018 £m |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 8 | **32.1** | 31.8 |
| Right of use assets | | **11.4** | 4.2 |
| Intangible assets | 9 | **37.4** | 38.0 |
| Deferred tax asset | | **3.0** | 4.4 |
| Trade and other receivables | | **15.0** | 11.9 |
| | | **98.9** | 90.3 |
| **Current assets** | | | |
| Inventories | | **8.1** | 6.2 |
| Trade and other receivables | | **77.5** | 62.8 |
| Cash and cash equivalents | | **53.9** | 35.5 |
| | | **139.5** | 104.5 |
| **Total assets** | | **238.4** | 194.8 |
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Other payables | | **0.2** | 0.3 |
| Provisions | | **0.8** | 1.2 |
| Lease liabilities | | **11.3** | 2.9 |
| Contract liabilities | | **9.1** | 8.5 |
| Contingent consideration | | **1.1** | 8.1 |
| Deferred tax | | **3.9** | 3.9 |
| | | **26.4** | 24.9 |
| **Current liabilities** | | | |
| Trade and other payables | | **46.1** | 37.2 |
| Provisions | | **0.9** | 1.0 |
| Lease liabilities | | **1.3** | 1.5 |
| Contract liabilities | | **8.0** | 7.9 |
| Contingent consideration | | **1.5** | - |
| Current tax | | **1.7** | 0.6 |
| | | **59.5** | 48.2 |
| **Total liabilities** | | **85.9** | 73.1 |
| **Issued capital and reserves attributable to owners of the parent** | | | |
| Share capital | | **0.2** | 0.2 |
| Share premium reserve | | **6.6** | 4.6 |
| Merger reserve | | **2.3** | 2.3 |
| Share option reserve | | **3.8** | 3.2 |
| Foreign exchange reserve | | **(0.6)** | (0.2) |
| Own shares | | **(0.7)** | (0.8) |
| Retained earnings | | **140.9** | 112.4 |
| **Total equity** | | **152.5** | 121.7 |
| **Total equity and liabilities** | | **238.4** | 194.8 |

# Consolidated statement of cash flows
For the year ended 31 December 2019

| | Note | 2019 £m | 2018 £m |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Profit for the year before tax | | **45.2** | 34.5 |
| | | | |
| Adjustments for: | | | |
| Depreciation of property, plant and equipment | 8 | **9.8** | 8.7 |
| Depreciation of right of use asset | | **1.7** | 1.4 |
| Amortisation and reduction in value of intangible assets | 9 | **13.7** | 3.8 |
| Change in fair value of consideration | | **(7.2)** | - |
| Share based payment expense | | **2.6** | 1.9 |
| Interest income | | **(0.1)** | (0.3) |
| Finance cost | | **0.4** | 0.2 |
| | | **66.1** | 50.2 |
| | | | |
| (Increase) in trade and other receivables | | **(16.7)** | (1.7) |
| (Increase) in inventories | | **(1.9)** | (3.0) |
| Increase/(Decrease) in trade and other payables | | **6.3** | (5.7) |
| Increase in contract liabilities | | **0.7** | 0.4 |
| (Decrease)/Increase in provisions and employee benefits | | **(0.5)** | 0.4 |
| | | | |
| **Cash generated by operations** | | **54.0** | 40.6 |
| Taxes paid | | **(7.5)** | (4.3) |
| **Net cash flows from operating activities** | | **46.5** | 36.3 |
| | | | |
| **Investing activities** | | | |
| Purchase of property, plant and equipment | 8 | **(9.9)** | (10.2) |
| Purchase of intangible assets | 9 | **(2.5)** | (2.5) |
| Interest received | | **0.1** | 0.3 |
| Acquisition of subsidiaries net of cash acquired | | **(7.5)** | (11.1) |
| **Net cash used in investing activities** | | **(19.8)** | (23.5) |
| | | | |
| **Financing activities** | | | |
| IFRS16 liability repayments | | **(1.1)** | (1.6) |
| Share issues | | **2.0** | 0.8 |
| Dividends | | **(9.2)** | (8.1) |
| **Net cash used in financing activities** | | **(8.3)** | (8.9) |
| | | | |
| **Net increase in cash and cash equivalents** | | **18.4** | 3.9 |
| Cash and cash equivalents at beginning of the year | | **35.5** | 31.6 |
| | | | |
| **Cash and cash equivalents at end of the year** | | **53.9** | 35.5 |

# Consolidated statement of changes in equity
For the year ended 31 December 2019

| | Share capital | Share premium reserve | Merger reserve | Share option reserve | Foreign exchange reserve | Own shares | Retained earnings | Total equity |
|---|---|---|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m | £m | £m | £m |
| 1 January 2018 | 0.2 | 3.8 | 2.3 | 2.8 | - | (0.8) | 87.0 | 95.3 |
| Change in accounting policy | - | - | - | - | - | - | 3.8 | 3.8 |
| Issue of shares | - | 0.8 | - | (1.0) | - | - | 1.0 | 0.8 |
| Recognition of share based payment expense | - | - | - | 1.4 | - | - | - | 1.4 |
| Tax on share based payment expense | | | | | | | | |
| - Current | - | - | - | - | - | - | 0.7 | 0.7 |
| - Deferred | - | - | - | - | - | - | (0.4) | (0.4) |
| Dividends paid | - | - | - | - | - | - | (8.1) | (8.1) |
| **Transactions with owners** | - | 0.8 | - | 0.4 | - | - | (3.0) | (1.8) |
| Profit for the year | - | - | - | - | - | - | 28.4 | 28.4 |
| Other comprehensive loss | - | - | - | - | (0.2) | - | - | (0.2) |
| **Total comprehensive income** | - | - | - | - | (0.2) | - | 28.4 | 28.2 |
| **31 December 2018** | **0.2** | **4.6** | **2.3** | **3.2** | **(0.2)** | **(0.8)** | **112.4** | **121.7** |
| 1 January 2019 | 0.2 | 4.6 | 2.3 | 3.2 | (0.2) | (0.8) | 112.4 | 121.7 |
| Issue of shares | - | 2.0 | - | (1.4) | - | - | 1.3 | 1.9 |
| Investment in own shares | - | - | - | - | - | 0.1 | - | 0.1 |
| Recognition of share based payment expense | - | - | - | 2.0 | - | - | - | 2.0 |
| Tax on share based payment expense | | | | | | | | |
| - Current | - | - | - | - | - | - | 1.0 | 1.0 |
| - Deferred | - | - | - | - | - | - | 0.9 | 0.9 |
| Dividends paid | - | - | - | - | - | - | (9.2) | (9.2) |
| **Transactions with owners** | - | 2.0 | - | 0.6 | - | 0.1 | (6.0) | (3.3) |
| Profit for the year | - | - | - | - | - | - | 34.5 | 34.5 |
| Other comprehensive (loss)/income | - | - | - | - | (0.4) | - | - | (0.4) |
| **Total comprehensive income** | - | - | - | - | (0.4) | - | 34.5 | 34.1 |
| **31 December 2019** | **0.2** | **6.6** | **2.3** | **3.8** | **(0.6)** | **(0.7)** | **140.9** | **152.5** |

# Notes to the consolidated financial statements

For the year ended 31 December 2019

## 1. Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board ('IASB') as adopted by the European Union ('adopted IFRS').The financial statements are presented in sterling and, unless otherwise stated, have been rounded to the nearest 0.1 million (£m).

The financial statements have been prepared on a historical cost basis.

The financial information contained in this statement does not constitute statutory financial statements within the meaning of the Companies Act 2006. They are an extract from the full accounts for the year ended 31 December 2019 on which the auditor has expressed an unqualified opinion and do not include any statement under section 498 of the Companies Act 2006. The full accounts contain a detailed statement of the accounting policies which have been used to prepare this summary. The accounts will be posted to shareholders on or before 10 April 2020 and subsequently filed at Companies House.

There are no additional standards or interpretations requiring adoption that are applicable to the Group for the accounting period commencing 1 January 2020.

A full set of the audited statutory accounts will be available at:

www.gammacommunicationsplc.com/investors/financial-results-and-shareholder-communications/

## 2. Accounting policies

The accounting policies adopted are consistent with those followed in the preparation of the audited statutory financial statements for the year ended 31 December 2019.

*Critical accounting estimates and judgements*

Some of the critical accounting judgements and estimates require management to make difficult, subjective or complex judgements or estimates. The policies which management consider critical because of the level of complexity, judgement or estimation involved in their application and their impact on the financial information are consistent with the year ended 31 December 2018 and are available in the Annual Report for that year.

*Alternative Performance Measures*

Adjustments to Profit from Operations, EBITDA, PBT, PAT and EPS (fully diluted) have been presented because the Group believes that adjusted measures provide valuable additional information for users of the financial statements in assessing the Group's performance. Moreover, they provide information on the performance of the business that management is more directly able to influence in the short-term and on a basis comparable from year to year.

The measures are adjusted for the following items:

(a) Amortisation on intangibles arising on acquisition

This adjustment is made to improve the comparability between acquired and organically grown operations, as the latter cannot recognise internally generated intangible assets. Adjusting for amortisation provides a more consistent basis for comparison between the two.

(b) Depreciation and amortisation

Depreciation and amortisation relate to the assets which were acquired by the Group. These are omitted from adjusted operating expenses to allow users of the accounts to compare against other external data sources.

(c) Exceptional items

The Group treats certain items which are considered to be one-off or not representative of the underlying trading of the Group as exceptional in nature.

The Directors apply judgement in assessing the particular items, which by virtue of their scale or nature should be classified as exceptional items. The Directors consider that separate disclosure of these items is relevant to an understanding of the Group's financial performance.

Changes in deferred consideration, reduction of intangible assets and goodwill are considered to be exceptional as they are not representative of the underlying trade of the Group as the nature of the Group's business is as a technology-based provider of communications services not an investment company.

(d) Adjusting tax items

Where movements to tax balances arise and these do not relate to the underlying trading current year tax charge, these are adjusted in determining certain APMs as they do not reflect the underlying performance in that year.

## 3. Segment information

The Group's main operating segments are outlined below:

→ UK Indirect – This division sells Gamma's products and services to channel partners and contributed 70% (2018: 74%) of the Group's external revenue;

→ UK Direct – This division sells Gamma's products and services to end users in the Mid-Market, enterprise and public sectors. They contributed 25% (2018: 25%) of the Group's external revenues.

→ Overseas – This division consists of sales made in the Netherlands, by DX Groep B.V and its subsidiary companies, contributing 5% (2018: 1%) of the Group's external revenues; and

→ Central functions – This is not a revenue generating segment but is made up of the central management team and wider Group costs.

*Factors that management used to identify the Group's reportable segments*

The Group's reportable segments are strategic business units that offer products and services into different markets. They are managed separately because each business requires different marketing strategies and are reported separately to the Board and management team.

*Measurement of operating segment profit or loss, assets and liabilities*

The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies.

The Group evaluates performance on the basis of profit or loss from operations but excluding non-recurring losses, such as goodwill impairment, and exceptional income.

Inter-segment sales are priced along the same lines as sales to external customers, with an appropriate discount being applied to encourage use of Group resources at a rate acceptable to local tax authorities. This policy was applied consistently throughout the current and prior period.

| | UK Indirect £m | UK Direct £m | Overseas £m | Central functions £m | Total £m |
|---|---|---|---|---|---|
| **2019** | | | | | |
| **Total revenue from external customers** | **230.1** | **83.6** | **15.2** | **-** | **328.9** |
| *Inter-segment revenue* | *21.5* | - | - | - | 21.5 |
| *Timing of revenue recognition* | | | | | |
| At a point in time | 16.4 | 5.6 | - | - | 22.0 |
| Over time | 213.7 | 78.0 | 15.2 | - | 306.9 |
| | 230.1 | 83.6 | 15.2 | - | 328.9 |
| **Total gross profit** | **119.1** | **38.2** | **9.2** | **-** | **166.5** |
| Operating expenses | (81.5) | (20.3) | (12.7) | (6.5) | (121.0) |
| **Operating profit before depreciation, amortisation and exceptional items** | **51.6** | **18.1** | **0.3** | **(6.5)** | **63.5** |
| Exceptional items | - | - | (0.9) | - | (0.9) |
| **Operating profit before depreciation and amortisation** | **51.6** | **18.1** | **(0.6)** | **(6.5)** | **62.6** |
| Depreciation and amortisation (excluding business combinations) | (13.9) | (0.2) | (1.0) | - | (15.1) |
| Amortisation arising on business combinations | (0.1) | - | (1.9) | - | (2.0) |
| **Profit from operations** | **37.6** | **17.9** | **(3.5)** | **(6.5)** | **45.5** |
| Interest income | 0.1 | - | - | - | 0.1 |
| Interest expense | (0.4) | - | - | - | (0.4) |
| **Group profit before tax** | **37.3** | **17.9** | **(3.5)** | **(6.5)** | **45.2** |
| Tax | (9.7) | (3.7) | 1.5 | 1.2 | (10.7) |
| **Group profit after tax** | **27.6** | **14.2** | **(2.0)** | **(5.3)** | **34.5** |
| Other comprehensive income | - | - | (0.4) | - | (0.4) |
| **Total comprehensive income attributable to the owners of the parent** | **27.6** | **14.2** | **(2.4)** | **(5.3)** | **34.1** |

External customer revenue has been derived principally from the United Kingdom and no single customer contributes more than 10% of revenue.

| **2019** | UK Indirect £m | UK Direct £m | Overseas £m | Central functions £m | Total £m |
|---|---|---|---|---|---|
| Additions to non-current assets | 11.6 | - | 0.8 | - | 12.4 |
| Reportable segment assets | 190.4 | 23.0 | 25.0 | - | 238.4 |
| Reportable segment liabilities | 62.0 | 12.4 | 11.5 | - | 85.9 |

| | UK Indirect | UK Direct | Overseas | Central functions | Total |
|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m |
| **2018** | | | | | |
| **Total revenue from external customers** | **210.6** | **70.9** | **3.4** | **-** | **284.9** |
| *Inter-segment revenue* | 52.5 | - | - | - | 52.5 |
| | | | | | |
| *Timing of revenue recognition* | | | | | |
| *At a point in time* | 19.9 | 3.7 | - | - | 23.6 |
| *Over time* | 190.7 | 67.2 | 3.4 | - | 261.3 |
| | 210.6 | 70.9 | 3.4 | - | 284.9 |
| | | | | | |
| **Total gross profit** | 97.5 | 32.8 | 1.9 | - | 132.2 |
| | | | | | |
| Operating expenses | (75.4) | (16.8) | (2.9) | (2.7) | (97.8) |
| | | | | | |
| **Operating profit before depreciation and amortisation** | 35.0 | 16.4 | (0.4) | (2.7) | 48.3 |
| Depreciation and amortisation (excluding business combinations) | (12.9) | (0.4) | (0.2) | - | (13.5) |
| Amortisation arising on business combinations | - | - | (0.4) | - | (0.4) |
| | | | | | |
| **Profit from operations** | 22.1 | 16.0 | (1.0) | (2.7) | 34.4 |
| Interest income | 0.3 | - | - | - | 0.3 |
| Interest expense | (0.2) | - | - | - | (0.2) |
| **Group profit before tax** | **22.2** | **16.0** | **(1.0)** | **(2.7)** | **34.5** |
| Tax | (4.0) | (2.8) | 0.2 | 0.5 | (6.1) |
| **Group profit after tax** | 18.2 | 13.2 | (0.8) | (2.2) | 28.4 |
| Other comprehensive income | - | - | (0.2) | - | (0.2) |
| **Total comprehensive income attributable to the owners of the parent** | 18.2 | 13.2 | (1.0) | (2.2) | 28.2 |

External customer revenue has been derived principally from the United Kingdom and no single customer contributes more than 10% of revenue.

| **2018** | UK Indirect | UK Direct | Overseas | Central functions | Total |
|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m |
| Additions to non-current assets | 12.5 | 0.2 | 24.9 | - | 37.6 |
| Recognition on transition to IFRS 16 | 6.0 | 0.2 | - | - | 6.2 |
| Reportable segment assets | 146.1 | 22.0 | 26.7 | - | 194.8 |
| Reportable segment liabilities | 46.0 | 12.4 | 14.7 | - | 73.1 |

The UK Indirect revenue and gross profit is further split between traditional and growth products below:

| | 2019 £m | 2018 £m |
|---|---|---|
| **Year ended 31 December** | | |
| Traditional products and services | **43.6** | 47.9 |
| Growth (being strategic and enabling) products and services | **186.5** | 162.7 |
| **Total revenue from external customers** | **230.1** | 210.6 |
| | | |
| Traditional products and services | **12.4** | 11.9 |
| Growth (being strategic and enabling) products and services | **106.7** | 85.6 |
| **Total gross profit** | **119.1** | 97.5 |

The UK Direct revenue is detailed below:

| | 2019 £m | 2018 £m |
|---|---|---|
| Mid Markets | **27.5** | 25.1 |
| Enterprise | **36.1** | 27.8 |
| Public Sector | **18.6** | 16.5 |
| The Loop | **1.4** | 1.5 |
| | **83.6** | 70.9 |

## 4. Exceptional items

| | **2019** | 2018 |
|---|---|---|
| | **£m** | £m |
| Contingent consideration adjustment – DX Groep | **8.1** | - |
| Reduction of goodwill carrying value | **(4.2)** | - |
| Reduction of intangible assets carrying value | **(3.9)** | - |
| Exceptional items related to DX Groep acquisition | **-** | - |
| Contingent consideration adjustment - Nimsys | **(0.9)** | - |
| Total Exceptional Items | **(0.9)** | - |

The exceptional items relate to the contingent consideration which is due on acquisitions.

In preparing the statutory accounts for 2018, the best estimate of the contingent consideration in respect of the DX Groep was made. During 2019, a higher than expected attrition rate of legacy customers taking ISDN caused the revenues to be lower than expected. Therefore, the estimated contingent consideration due has been revised and the associated intangible assets including goodwill have been reduced.

Following the initial recognition of Nimsys deferred consideration in February 2019, we have remeasured the contingent consideration at the reporting date and updated the balance due. The overall balance due has increased by £0.9m which we have charged to the statement of comprehensive income.

## 5. Taxation on profit on ordinary activities

| | **2019** | 2018 |
|---|---|---|
| | **£m** | £m |
| **Current tax expense** | | |
| Current tax on profits for the year | **9.9** | 4.9 |
| Adjustment in respect of prior year | **(0.6)** | 0.1 |
| Overseas tax | **0.7** | 0.2 |
| **Total current tax** | **10.0** | 5.2 |
| **Deferred tax expense** | | |
| Origination and reversal of temporary differences | **(1.2)** | 0.9 |
| Adjustment in respect of prior years | **0.5** | - |
| Tax rate change | **(0.2)** | - |
| Adjusting tax items | **1.6** | - |
| **Total deferred tax** | **0.7** | 0.9 |
| **Total tax expense** | **10.7** | 6.1 |

The reasons for the difference between the actual tax charge for the period and the standard rate of corporation tax in the United Kingdom applied to profits for the period are as follows:

| | **2019** | 2018 |
|---|---|---|
| | **£m** | £m |
| Profit before income taxes | **45.2** | 34.5 |
| Expected tax charge based on the standard rate of United Kingdom corporation tax at the domestic rate of 19% (2018: 19%) | **8.6** | 6.6 |
| Effects of: | | |
| Tax effect of expenses that are not deductible in determining taxable profit | **0.5** | - |
| Effect of different tax rates of subsidiaries operating in other jurisdictions | **(0.2)** | - |
| Tax rate change | **(0.2)** | - |
| Tax on business combinations | **0.5** | - |
| Adjusting tax items | **1.6** | - |
| Adjustment in respect of prior years | **(0.1)** | (0.5) |
| **Total tax expense** | **10.7** | 6.1 |

Deferred tax was calculated based on the tax laws and rates that were enacted or substantively enacted at the balance sheet date. The Finance Act 2019 included provision for the main rate of corporation tax to reduce to 17% from 1 April 2020. Following the UK Budget 2020 on 11 March 2020, the main rate of corporation tax is expected to remain at 19%, however this change had not been substantively enacted at the balance sheet date and therefore has not been reflected in the deferred tax balances recorded.

## 6. Earnings per share

| | **2019** | 2018 |
|---|---|---|
| Earnings per Ordinary Share – basic (pence) | **36.6** | 30.3 |
| Earnings per Ordinary Share – diluted (pence) | **36.1** | 30.0 |

The calculation of the basic and diluted earnings per share is based on the following data:

| | **2019** | 2018 |
|---|---|---|
| | **£m** | £m |
| **Earnings** | | |
| Profit after tax | **34.5** | 28.4 |
| | | |
| **Shares** | **Number** | Number |
| Basic weighted average number of Ordinary Shares | **94,370,938** | 93,646,411 |
| Effect of dilution resulting from share options | **1,246,648** | 1,108,034 |
| Diluted weighted average number of Ordinary Shares | **95,617,586** | 94,754,445 |

On 28 February 2020, the group acquired Exactive; £0.9m of Ordinary Shares will be paid as part consideration by 15 April 2020.

Adjusted earnings per share is detailed below:

| | **2019** | 2018 |
|---|---|---|
| Adjusted earnings per Ordinary Share – basic (pence) | **41.3** | 30.6 |
| Adjusted earnings per Ordinary Share – diluted (pence) | **40.8** | 30.3 |

Adjusted profit used in the calculation of adjusted earnings per share is detailed below:

| | **2019** | 2018 |
|---|---|---|
| | **£m** | £m |
| **Earnings** | | |
| Profit for the year | **34.5** | 28.4 |
| Amortisation arising on business combinations | **2.0** | 0.4 |
| Exceptional items (change in value of deferred consideration) | **0.9** | - |
| Adjusting tax items | **1.6** | (0.1) |
| Adjusted profit after tax for the year | **39.0** | 28.7 |

## 7. Dividends

An interim dividend of 3.5p was paid on 24 October 2019 (2018: 3.1p).

A final dividend of 7.0p will be proposed at the Annual General Meeting but has not been recognised as it requires approval (2018: 6.2p). The total amount of dividends proposed is 10.5p (2018: 9.3p). The payment of these dividends do not have any tax consequences for the Group.

## 8. Property, plant and equipment

| | Network assets | Computer equipment | Fixtures and fittings | Total |
|---|---|---|---|---|
| | £m | £m | £m | £m |
| **Cost** | | | | |
| At 1 January 2019 | 76.8 | 7.5 | 1.1 | 85.4 |
| Additions | 7.8 | 1.7 | 0.4 | 9.9 |
| Acquisition of subsidiary | 0.1 | - | - | 0.1 |
| Disposals | (16.9) | (0.1) | (0.1) | (17.1) |
| Exchange differences | 0.1 | - | - | 0.1 |
| **At 31 December 2019** | 67.9 | 9.1 | 1.4 | 78.4 |
| **Depreciation** | | | | |
| At 1 January 2019 | 47.1 | 5.7 | 0.8 | 53.6 |
| Charge for the year | 8.4 | 1.2 | 0.2 | 9.8 |
| Disposals | (16.9) | (0.1) | (0.1) | (17.1) |
| **At 31 December 2019** | 38.6 | 6.8 | 0.9 | 46.3 |
| **Net book value** | | | | |
| At 1 January 2019 | 29.7 | 1.8 | 0.3 | 31.8 |
| **At 31 December 2019** | **29.3** | **2.3** | **0.5** | **32.1** |

## 9. Intangible assets

| | Goodwill | Customer contracts | Brand | Development costs | Software | Total |
|---|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m | £m |
| **Cost** | | | | | | |
| At 1 January 2019 | 19.7 | 17.2 | 0.9 | 8.9 | 11.4 | 58.1 |
| Additions | - | - | - | 1.4 | 1.1 | 2.5 |
| Acquisition of subsidiary | 4.5 | 5.9 | 0.2 | - | 0.9 | 11.5 |
| Exchange differences | (0.2) | (0.7) | - | - | - | (0.9) |
| **At 31 December 2019** | **24.0** | **22.4** | **1.1** | **10.3** | **13.4** | **71.2** |
| **Amortisation** | | | | | | |
| At 1 January 2019 | 4.5 | 2.5 | - | 6.4 | 6.7 | 20.1 |
| Charge for the year | - | 1.7 | 0.2 | 1.4 | 2.3 | 5.6 |
| Impairment | 4.2 | 3.8 | 0.1 | - | - | 8.1 |
| **At 31 December 2019** | **8.7** | **8.0** | **0.3** | **7.8** | **9.0** | **33.8** |
| **Net book value** | | | | | | |
| At 1 January 2019 | 15.2 | 14.7 | 0.9 | 2.5 | 4.7 | 38.0 |
| **At 31 December 2019** | **15.3** | **14.4** | **0.8** | **2.5** | **4.4** | **37.4** |

Due to a fall in ISDN revenues from Dean One (part of our Dutch business), the values of goodwill, customer contracts and brand have been reduced by £4.2m, £3.8m and £0.1m respectively. These amounts have been charged to the statement of comprehensive income through the “exceptional items” line and have been included within the “Overseas Business” in the segmental analysis in Note 3.

At 30 June 2019, the customer contracts and brand were valued using a multiple-period excess earnings model and a relief from royalty model, respectively. Given the proximity of the original acquisition of Dean One, a fair value less costs to sell approach was used to determine the recoverable amount of goodwill. The valuation techniques utilise Level 2 inputs. The key assumptions used were in respect of the customer contract valuation model and were: the implied rate of return of 21.5%, revenue growth of 12% in the first 5 years followed by 2% to the end of the assets useful economic life and attrition rates of 8%.

## 10. Business combinations

*Summary of acquisition*

The Group acquired 100% of the issued share capital of Nimsys Groep B.V. ("Nimsys") on the 4th February 2019. 100% of the share capital of Telsis Direct Limited, Telsis Communication Services Limited, Telsis Services Limited and Telsis GmbH were acquired on 25th November 2019, and are treated as one acquisition referred to as "Telsis".

Nimsys is a provider of internet, cloud telephony and associated IT services primarily to the operators and tenants of premium multi-tenant office buildings across the Netherlands. Telsis provides carriers and solution providers with Telephony and Contact Centre applications that can form the core platform for a service providers' go-to-market offering.

Details of the purchase consideration, the net assets acquired and goodwill at acquisition are as follows:

| | Nimsys | Telsis | Total |
|---|---|---|---|
| | £m | £m | £m |
| Cash paid | 3.7 | 4.3 | 8.0 |
| Contingent consideration | 1.8 | - | 1.8 |
| **Total purchase consideration** | **5.5** | **4.3** | **9.8** |

*Contingent consideration at 31 December 2019*

*Nimsys*

The contingent consideration is based on the EBITDA and EBITDA growth percentage for 2019 and 2020.

The potential undiscounted amount payable under the agreement is between £0.3m (€0.35m) for EBITDA in the year ended 31 December 2019 of less than £1.16m (€1.365m) and EBITDA growth is less than 5% and £1.5m (€1.8m) for EBITDA of £1.39m (€1.63m) and growth is greater than or equal to 25%. Sterling values have been translated at the closing exchange rate of 1.1757.

The fair value of the contingent consideration at acquisition of £1.8m was based on Nimsys achieving €1.6m EBITDA representing a 24% increase for 2019 giving €1.3m contingent consideration and €1.7m EBITDA in 2020 representing an 8% increase, giving contingent consideration of €0.6m. Values were translated at the rate at acquisition of 1.1433.

Nimsys B.V. is performing above expectations and therefore the fair value of contingent consideration has increased to £2.6m (€3.1m using a closing exchange rate of 1.1757) which was estimated by calculating the present value of future expected cash flows. The estimates are based on the group's cost of borrowings and 2019 and 2020 EBITDA €1.64m and €1.9m respectively, and growth of 26% and 15.6% respectively. In the event that the maximum pre-determined EBITDA is achieved by the subsidiary for the year ended 31 December 2020, additional consideration of up to €0.4m may be payable in cash in the first half of 2021.

*Telsis*

There is no contingent consideration for this transaction.

The assets and liabilities recognised as a result of the acquisition are as follows:

| | Nimsys | Telsis | Total |
|---|---|---|---|
| | £m | £m | £m |
| Cash | 0.3 | 0.2 | 0.5 |
| Trade receivables | 0.3 | 0.2 | 0.5 |
| Tangible fixed assets | 0.1 | - | 0.1 |
| Intangible – software | - | 0.8 | 0.8 |
| Intangible – customer contracts | 3.5 | 2.4 | 5.9 |
| Intangible – brand | 0.2 | - | 0.2 |
| Trade payables | (0.1) | (0.1) | (0.2) |
| Other receivables | 0.1 | 0.5 | 0.6 |
| Other payables | (0.1) | (1.3) | (1.4) |
| Current tax | (0.1) | - | (0.1) |
| Deferred tax liability/asset | (0.9) | (0.7) | (1.6) |
| Net identifiable assets acquired | 3.3 | 2.0 | 5.3 |
| Add: Goodwill | 2.2 | 2.3 | 4.5 |
| **Net assets acquired** | 5.5 | 4.3 | 9.8 |

**Valuations of intangible assets**
Customer relations were valued under the Income Method and the brand under the Relief from Royalty Method.

**Acquired receivables**
The fair value of acquired trade receivables for Nimsys and Telsis is £0.3m and £0.2m respectively. The gross contractual amount for trade receivables due is £0.3m and £0.2m respectively, of which £nil is expected to be uncollectible.

**Revenue and profit contribution (unaudited)**
Nimsys contributed revenues of £3.1m and profit after tax of £1.0m to the Group for the period from 4 February 2019 to 31 December 2019.

If the acquisition had occurred on 1 January 2019, consolidated pro-forma revenue and profit for the year ended 31 December 2019 would have been £3.4m and £1.2m respectively. These amounts have been calculated as follows:

| | Revenue | Profit |
|---|---|---|
| | £m | £m |
| For the year ended 31 December 2019 | 3.4 | 1.1 |
| Add: Transaction costs | - | 0.1 |
| For the year ended 31 December 2019 if the acquisition occurred on 1 Jan 2019 | 3.4 | 1.2 |

Telsis contributed revenues of £0.3m and profit after tax of nil to the Group for the period from 25 November 2019 to 31 December 2019.

If the acquisition had occurred on 1 January 2019, consolidated pro-forma revenue and profit for the year ended 31 December 2019 would have been £2.9m and £0.8m respectively. These amounts have been calculated as follows:

| | Revenue | Profit |
|---|---|---|
| | £m | £m |
| For the year ended 31 December 2019 | 2.9 | 0.4 |
| Add: Transaction costs | - | 0.4 |
| For the year ended 31 December 2019 if the acquisition occurred on 1 Jan 2019 | 2.9 | 0.8 |

**Goodwill**
The goodwill of £4.5m (Nimsys £2.2m, Telsis £2.3m) is attributable to the acquired entities. The goodwill is not deductible for tax purposes.

*Purchase consideration – cash outflow*

| | Nimsys | Telsis | Total |
|---|---|---|---|
| | £m | £m | £m |
| Cash paid | 3.7 | 4.3 | 8.0 |
| Less: cash acquired | (0.3) | (0.2) | (0.5) |
| **Net outflow of cash – investing activities** | **3.4** | **4.1** | **7.5** |

In the year ended 31 December 2018, the group acquired 100% of the issued share capital of DX Groep B.V., a provider of telephony services.

**11. Events after the reporting date**

On the 18 February 2020 the Group made an offer to acquire the entire issued and to be issued share capital of Voz Telecom. Voz Telecom is admitted to trading on the Mercado Alternativo Bursátil in Spain. Accordingly, the Offer will be implemented by means of a takeover offer under the relevant Spanish legislation. The offer values the entire issued and to be issued ordinary share capital of Voz Telecom at approximately €25.3 million (£21.0 million) on a fully diluted basis. The cash consideration payable pursuant to the Offer will be financed from the Gamma group's existing cash resource (which was £53.8 million as at 31 December 2019). Voz Telecom's net debt at 31 December (adjusted for convertible bonds) was approximately €5.2m which would imply an enterprise value of c€30.5 million (c£25.3 million).

On the 28 February 2020 the group acquired Exactive for an initial consideration of £5.0m of which £3.6m is in cash payable immediately, £0.5m held in escrow for 24 months and £0.9m will be in Gamma shares payable by 15 April 2020. Exactive is a leading UK Microsoft Gold Partner and specialist Microsoft Teams UCaaS provider with an excellent reputation and track record. With a growing number of larger business and public sector organisations adopting Microsoft Teams as their collaboration solution, Exactive's expertise and 'Cloud UCX platform' will enable us to address this market segment and business opportunity more effectively.

Due to the proximity of the acquisition to the publication of these accounts and given the materiality of the transaction, the Group has not yet completed the purchase price allocation and it is impractical to give further information.