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2017 Half Year Review

Enabling Connectivity

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2017 Half Year Statement of Results

HY2017 Financial Overview
The six months to 30 September 2016 (HY2017) was a difficult period for Rakon as revenue from global telecommunications equipment manufacturers declined. Telecommunications network operators continued to defer investment in infrastructure in HY2017, affecting sales to equipment manufacturers. Revenue of NZ$46.0 million was down NZ$12.0 million on the previous corresponding period.

The company reported an unaudited net loss after tax for HY2017 of NZ$5.7 million, a decline from the NZ$1.1 million unaudited profit after tax attained in the half year ending 30 September 2015 (HY2016). Rakon also reported HY2017 Underlying EBITDA[1] of NZ$0.6 million, a decline of NZ$5.6 million from HY2016 and an operating cash flow of NZ$-0.6 million.

Gross margin percentage declined in the period due to changes in product mix and the result was also negatively impacted by a stronger New Zealand dollar, compared to the prior year.

Bank borrowings increased to NZ$18.9 million, up NZ$6.9 million on HY2016. The increase reflects Rakon's continued commitment to investing in customer-driven research and development initiatives, and our purchase of a cornerstone shareholding in Internet of Things (IoT) network operator and service provider Thinxtra. In total, Rakon had cash outflows of NZ$6.3 million from investing activities in the period.

Operational Overview
As we announced to shareholders at our Annual Shareholders' Meeting in September, significant work has already been done to reduce Rakon's annual operating costs, which are 11.2% less than in HY2016. We remain on track to reduce annual operating costs by 20%; however, one-off costs associated with implementing the programme mean the full benefits will not flow through to the bottom line until FY2018.

We continue to focus on research and development, driven by our customers' requirements, with a particular focus on disruptive products in preparation for 4.5G and 5G. We anticipate 4.5G-related activity to ramp up over the next couple of years as part of the evolution to 5G.

Market Update
Telecommunications As mentioned, major network operators have continued to delay investing in infrastructure, particularly in deploying 4G networks, in favour of bidding for 5G spectrum. Consolidation in the global industry has led to significant rationalisation. To take one example, Nokia's takeover of Alcatel-Lucent entailed the cancellation of some Alcatel-Lucent product lines that featured Rakon components. While that has had an obvious effect on sales in the short term, we also believe it creates an enhanced opportunity for us to develop a relationship with Nokia that will serve us well in the future.

As we have said previously, the continued increase in demand for voice, video, and data services, plus the higher expectations around connectivity and speed, mean network operators can't indefinitely avoid investing in greater network capacity. Over the past quarter, we have started to see an increasing order book from our key Tier One customers.

We expect the negative trend of the past couple of years to slowly reverse in the second half of FY2017, based on the orders we are now seeing from Tier One customers and their forecasts. Operators are also starting to roll out time synchronisation, which is mandatory for 4.5G and 5G networks. These networks need to know time exactly – down to 1.5 microseconds – meaning each synchronisation node requires a timing device: an OCXO[2] or a TCXO[3]. Rakon has products in our existing portfolio designed to meet these requirements, and additional solutions currently in development.

Global Positioning The 27% revenue decline on HY2017 was predominantly due to the continued cannibalisation of personal navigation devices by smart phones, and uncharacteristically high revenue in HY2016 generated by a customer 'last time buy'.

The market continues to move away from commoditisation towards more specialised products, and we expect the current global TCXO shortage, due to the growth in mobile phones, will keep prices stable for the balance of the global positioning market.

The introduction of autonomous cars will increase the size of the global positioning market in the future. Development by traditional car manufacturers and technology companies continues apace, and Rakon is currently working on several opportunities with some major players in this area.

Space and Defence Revenue for the space and defence market was up 2% from HY2016, where an increase in defence revenue was partially offset by a decline in space revenue. We expect space and defence revenue to increase in the second half as has been the case with the business in France in recent years. Highlights include 16% growth in the emerging low orbit satellites segment and Rakon's qualification into a SpaceX rocket programme.

Asia and the US are potential growth areas; opportunities also exist for low orbit nano and micro satellites. These will take time to develop.

Revenue from Rakon's defence business was up 11% from HY2016, with solid growth in precision radar products as well as strong order bookings continuing over the past 9 to 12 months. The long lead times associated with this business mean it is only now that we are starting to deliver revenue from the prior increase in bookings, and we expect revenue will continue to improve going forward.

Rakon is the only company supplying commercial OCSOs[4], which enable aeroplane radar to 'see' twice as far as previously. This advanced technology provides strong prospects for growth in the US market.

Diversification and Expansion
The company continues to diversify through its investment in Thinxtra. The rapidly expanding IoT market is a natural place for Rakon to be. Thinxtra's progress and the continued growth in IoT applications, puts Rakon at the forefront of a truly radical change process and will generate significant opportunities for us.

Thinxtra is the exclusive Sigfox network operator for Australia and New Zealand, and has made significant progress on the roll-out of an IoT network. More than 60% of the population in Australia and New Zealand currently have outdoor coverage and the company is on target to achieve 85% population coverage by June 2017. In the past six months, Thinxtra has developed an active customer pipeline and signed its first significant connections deal to connect more than one million units via the long-range, low-power Sigfox network.

Half Year 2017 Performance Key Points

- Revenue declined 20.8% vs. HY2016 to NZ$46.0 million.
- Unaudited net loss after tax: NZ$5.7 million vs. NZ$1.1 million net profit after tax in HY2016.
- NZ$5.6 million decline in first half Underlying EBITDA[1]: NZ$0.6 million in HY2017 vs. NZ$6.2 million in HY2016 (down 89.6%).
- Positive reduction in operating expenses by 11.2% with actions initiated to achieve a 20% reduction from the beginning of FY2018.
- Operating cash flow of NZ$-0.6 million (down >100% vs. HY2016).
- Continued commitment to research and development with focus on developing products for 4.5G and 5G network technology.
- Defence market revenue increased 11% on prior year.
- Financial Year 2017 (FY2017) earnings guidance for Underlying EBITDA of between NZ$3 million and NZ$5 million.

In line with the commitments made to shareholders at the Annual Shareholders' Meeting, Rakon is currently working towards the appointment of one or two new Directors to the Board.

Outlook
Revenue in the second half of FY2017 is forecast to be between 12% and 15% higher than in the first half, due to seasonal and market factors. Cost reduction initiatives undertaken in the first half will benefit earnings; however this improvement will be offset to some degree by one-off costs associated with the restructure of the France business unit in the third quarter.

The company expects to report Underlying EBITDA of between NZ$3 million and NZ$5 million for the full year, FY2017.

Brent Robinson
CEO / Managing Director

Bryan Mogridge
Chairman

[1] **Disclosure of Non-GAAP Financial Information.** Rakon has used 'Underlying EBITDA' as a measure of non-GAAP financial information in this 2017 Half Year Review document and it is defined as: "earnings before interest, tax, depreciation, amortisation, impairment, employee share schemes, non-controlling interests, adjustments for associates and joint ventures' share of interest, tax & depreciation, loss on disposal of assets and other cash and non-cash items (Underlying EBITDA)."

Underlying EBITDA is a non-GAAP measure that has not been presented in accordance with GAAP. The Directors present Underlying EBITDA as a useful non-GAAP measure to investors, in order to understand the underlying operating performance of the Group and each operating segment, before the adjustment of specific non-cash charges and before cash impacts relating to the capital structure and tax position. Underlying EBITDA is considered by the Directors to be the closest measure of how each operating segment within the Group is performing. Management uses the non-GAAP measure of Underlying EBITDA internally, to assess the underlying operating performance of the Group and each operating segment.

The use of Underlying EBITDA in this document for the half year of FY2017 has been extracted from unaudited financial statements. The use of Underlying EBITDA in this document for FY2016 has been extracted from audited financial statements. This document should be read in conjunction with the Rakon Limited Interim Report September 2016. A detailed reconciliation of Underlying EBITDA to Net Loss After Tax is contained at Note 3 (Segment information) of the financial statements.

[2] OCXO Oven Controlled Crystal Oscillator.
[3] TCXO Temperature Compensated Crystal Oscillator.
[4] OCSO Oven Controlled SAW Oscillator.

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2017 Half Year Financial Summary

Summary of Revenue and Profit/(Loss)	Six months ended 30 September 2016 $000s	Six months ended 30 September 2015 $000s	Year ended 31 March 2016 $000s
Revenue	45,957	57,990	112,737
Underlying EBITDA[1]	**647**	**6,210**	**9,008**
Depreciation and amortisation	(2,800)	(3,113)	(6,620)
One off cash gains realised on derivatives closed out	(1,361)	–	–
Employee share schemes	(29)	(40)	(81)
Interest	(687)	(605)	(1,125)
Adjustment for associates and joint venture share of interest, tax and depreciation	(980)	(1,079)	(2,118)
Loss on asset sales/disposal	(4)	–	(120)
Other non-cash items	(215)	(136)	199
Income tax (expense)/credit	(269)	(157)	(874)
Net profit/(loss) for the period	**(5,698)**	**1,080**	**(1,731)**

[1]Refer to page 2 for explanation of Underlying EBITDA.

Summary Statement of Cash Flows	Six months ended 30 September 2016 $000s	Six months ended 30 September 2015 $000s	Year ended 31 March 2016 $000s
Net cash flow:			
– Operating activities	(612)	5,329	7,285
– Investing activities	(6,312)	(3,077)	(6,994)
– Financing activities	6,911	–	–
Net increase/(decrease) in cash and cash equivalents	**(13)**	**2,252**	**291**
Foreign currency translation adjustment	(114)	1,314	378
Cash and cash equivalents at the beginning of the period	(561)	(1,230)	(1,230)
Cash and cash equivalents at the end of the period	**(688)**	**2,336**	**(561)**

Balance Sheets	As at 30 September 2016 $000s	As at 30 September 2015 $000s	As at 31 March 2016 $000s
Current assets	59,076	71,200	62,910
Non-current assets	57,316	63,061	58,366
Total assets	**116,392**	**134,261**	**121,276**
Current liabilities	39,267	42,574	23,032
Non-current liabilities	2,599	4,906	14,816
Total liabilities	**41,866**	**47,480**	**37,848**
Net assets	**74,526**	**86,781**	**83,428**
Equity	74,526	86,781	83,428
Total equity	**74,526**	**86,781**	**83,428**