

29 August 2016

## ASX ANNOUNCEMENT

### Senetas Corporation Limited Full-Year Results Announcement For the year to 30 June 2016

#### Senetas delivers record profit driven by strong revenue growth

Senetas Corporation Limited (ASX: SEN), a leading global developer and manufacturer of multi-certified, defence-grade data encryption solutions, is pleased to announce its results for the year ended 30 June 2016 (FY2016).

#### FY2016 highlights:

- Operating revenue up 19% to \$19.34 million (FY2015: \$16.21 million);
- Net profit before tax up 17% to \$7.02 million (FY2015: \$6.02 million);
- Net profit after tax up 30% to \$5.22 million (FY2015: \$4.02 million);
- Margins were very strong with gross profit margin at 83%, pre-tax profit margin at 36% and after tax net profit margin at 27%;
- Cash flow was excellent, with net operating cash flow of \$5.19 million;
- Sound, unleveraged balance sheet
  - No debt;
  - Cash on hand at 30 June 2016 of \$20.85 million (FY2015: 15.90 million);
  - Net assets up 41% to \$18.53 million; and
  - Return on Equity at 33%
- All new product development projects are on track and the new 100Gbps encryptor is currently undergoing certification in order to progress customer testing.

Commenting on the Company's results, Senetas CEO Andrew Wilson said, "The 2016 full year profit is a record for the Company and was achieved despite a \$1.43 million increase in R&D expenditure during the period and lower than expected sales in the first half of the year as a result of the integration of SafeNet into Gemalto.

"Revenue growth was balanced across both product sales and maintenance revenue and it is particularly pleasing to note the increasing share of revenue represented by commercial customers who now represent over 50% of operating revenue.



NATO Classification  
Restricted - Green



“These results continue to reflect the market’s rapidly growing awareness of the critical need for high assurance encryption solutions in order to protect data in transit.

“The result also reflects benefits from the more enhanced supportive role Senetas is now playing in the sales, marketing and business development partnership with Gemalto and our other distribution partners, as well as the aforementioned progress that has been made in the integration of Senetas’ global distributor SafeNet with Gemalto during the second half of the fiscal year.

“Progress on Senetas’ key new product development initiatives was accelerated during the year with a significant increase in R&D expenditure. Additional permanent and contract resources were employed in order to fast track R&D projects with particular focus on the new 100Gbps encryptor that is now undergoing certification.

“Subject to completion of the certification and customer testing processes, sales of the 100Gbps encryptor are expected to impact operating revenue in the first half of calendar 2017.

“Senetas’ financial position remains extremely sound, with net assets up 41% during the period, no debt, and cash on hand of almost \$21 million.

“This result is a strong endorsement of both the quality of the Company’s personnel and product solutions, as well as its ability to identify and meet the critical security needs of our end customers and business partners.”

## **Revenue Growth**

Revenue growth was driven by 19% growth in both product sales and maintenance revenue during the period.

Product sales to commercial customers grew robustly and more than offset slower sales to government customers. Sales continue to be weighted towards late in each half year and commercial sector sales, in particular, were significantly stronger than projected in the 6 month period ended 30 June 2016.

Delayed commercial customer sales at 31 December 2015 were completed as expected during the second half of the fiscal year; however, some of the delayed US Federal Government sales will now not proceed as some agencies move from a SONET to Ethernet network over the next 3-4 years. Growth in Senetas’ maintenance revenue from FY2017 may moderate as the higher cost SONET maintenance contracts roll off throughout that period. However, the Company expects that its lower cost Ethernet encryptors will replace the existing SONET encryptors in those updated networks.

The company is working closely with Gemalto to significantly improve its Government business.



## **Research and Development**

A highly innovative and responsive R&D capability remains the Company's core focus and will be the major driver of growth prospects and increased profitability going forward.

Senetas substantially increased its investment in R&D during FY2016 in order to fast-track initiatives that will build new capability and drive revenue growth in FY2017 and beyond. R&D expenditure during the year was \$1.43 million higher than the prior period and reflected a total R&D investment aggregating approximately 29% of operating revenue.

The key focus during the year was development of the 100Gbps encryptor that is on track to be available for sale by the end of this calendar year or early in 2017. The certification process commenced mid-year and customer testing is due to be completed within the next two or three months.

Senetas' custom encryption algorithm product ("CEAP") is also currently undergoing customer testing and certification. Subject to the timing of certification and export approval, it is expected that the CEAP will become available for sale late in FY2017. Development of Senetas' virtual encryption technologies ("VET") is ahead of schedule and is now available for customer testing.

Senetas is continuing to work actively with its customers, master distribution partner (Gemalto) and technology partners in order to identify new product/service opportunities that will create significant ongoing revenue growth for Senetas in the future.

Senetas expects R&D expenditure in FY2017 will be at a similar level to FY2016.

## **Balance Sheet and Cash Flow**

Senetas' balance sheet continues to strengthen and provides significant capacity to support both organic growth and investment. Net assets increased 41% to \$18.53 million and the cash balance at 30 June 2016 was \$20.85 million.

Net operating cash flow remained strong at \$5.19 million in FY2016 but was lower than FY2015. The key contributing factors to the lower cash flow versus the prior period were:

1. Tax payable of \$1.25 million during FY2016 compared to nil in the prior period; and
2. Higher receivables at 30 June 2016 due to the shift in weighting of product sales to later in the fiscal year and the higher R&D rebate due in FY2017.

The Board periodically reviews its capital management policy and in so doing takes into account a variety of factors including R&D and other investment opportunities, financial returns, risk and liquidity considerations which might impact Senetas' business.

As a rapidly growing R&D technology company, the Board continues to implement a conservative capital management policy in order to conserve capital for continued investment in attractive R&D



product development, as well as to ensure that Senetas is well positioned to take advantage of other compelling investment opportunities.

Senetas has a substantial R&D product roadmap that leverages its engineering skills. These products when brought to market in the mid term have the potential to add significantly to the company's revenues and profits. The board considers that the company needs to maintain a strong cash balance to allow for the possibility to extend its engineering capability and where necessary to add resources to bring products to market earlier than planned if required.

### **R&D Rebate**

Senetas currently receives a tax rebate of 45% from the Australian Government for eligible R&D expenditure. The rebate is currently recorded as Other Income and is received in cash in the following financial year net of any corporate income tax payable. Eligible R&D expenditure is not deductible for the purposes of calculating Senetas' corporate income tax liability.

The R&D rebate is available to Senetas whilst its operating revenue remains below \$20 million per annum. Should Senetas' annual operating revenue exceed \$20 million in future years the R&D rebate will no longer be available. Instead, the R&D rebate converts into a tax offset equal to 40% of eligible R&D expenditure. The R&D expenditure would remain non-deductible for the purposes of calculating Senetas' corporate income tax liability.

If the current R&D rebate is unavailable going forward, Senetas' Other Income and Profit Before Tax would be lower by the amount of the R&D tax rebate previously available (\$2.1 million in FY2016); however, tax expense would be reduced by an offset equal to 40% of its eligible R&D expenditure. Senetas currently estimates that in those circumstances its effective tax rate would be in the low to mid 20s as a percentage of Profit Before Tax.

Senetas very strongly believes that the threshold for R&D tax rebate should be significantly increased in order to maximise the incentive for successful smaller enterprises to invest in critical R&D expenditure. The Company is working with government at all levels to bring broader awareness and urgency in order to accomplish this important incentive for the future benefit of the Australian economy.

### **Tax Expense**

Tax expense in 2016 was reduced by a credit of \$0.94 million (FY2015: \$0.45 million) recognised in relation to the use of carried forward tax losses.

An additional tax credit of \$0.21 million (FY2015: nil) was also booked to recognise the remaining carried forward tax losses available to be utilised against taxable income in the 2017 year and beyond. Utilisation of the remaining tax losses is restricted such that only a portion can be utilised in any year; however, it is expected that the losses will be fully utilised within the next 3-4 years.



## Outlook

Commenting on the Company's growth outlook, Mr Wilson said:

"Continued growth in data flows across Layer 2 networks combined with increasing recognition of the need for high assurance encryption solutions creates significant opportunities for the sale of Senetas' existing products and those under development.

"Whilst the growth outlook for the sector remains extremely positive, Senetas' future sales growth rates remain difficult to predict accurately. Sales lead times are long and customers are generally reluctant to disclose detail about the timing and scale of planned purchases.

"The addition of the new 100Gbps encryptor to the Senetas product portfolio later in FY2017 is an exciting opportunity for the Company. While at this stage it is too early to predict the scale of initial sales for the 100Gbps encryptor, the initial interest from Senetas' largest customers remains very strong.

Mr Wilson added, "In addition we expect to commence sales in the March quarter of FY2017 for our custom algorithm and virtual encryption appliances. We expect these sales will add to our overall growth in FY2017."

END.

### Investor and analyst conference call

The Company will be holding an investor and analyst conference call at 11.00AM AEDT today.

Dial in details: Participants can dial +61 2 9007 8048 or 1800 908 299 (toll free) to join the call. When prompted, please enter Conference ID: 661031

For further information, please contact:

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