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EARNINGS ANNOUNCEMENT 1H 2017

Solution Dynamics Limited ("SDL" or "Company") produced an unaudited net profit after tax of $0.704 million for the half year. This represents 19.9% year-on-year growth on an after-tax basis and was modestly ahead of the Company's budget for the period. The underlying growth was mainly generated from Software & Technology gains and contained no unusual items or material one-off software licensing revenue. Digital Print and Document Handling revenues also showed pleasing growth. The Directors have declared an interim dividend of 3.5 cents per share, fully imputed, representing a payout ratio of 70%.

Operational Commentary

Operating revenue grew 31.3% to $10.19 million, however, much of this was from gains in low margin postage revenue and subcontracted printing in the UK where SDL earns low margins. The consequence of this changing revenue mix was a decline in the Company's gross margin percentage (although dollar gross margin continued to grow, increasing 14.6% to $3.839 million).

Software & Technology revenues increased 18.9% to $2.42 million as the Company's UK revenues continue to build, although the overall growth rate was moderately constrained by a small decline in development revenues versus the prior year and a reduced requirement for Déjar archival services by one major customer which now stores its own PDF documents (a trend we expect to see more broadly going forward).

Revenue rose 10% to $3.40 million year-on-year in the traditional digital print and document handling services market, a market which otherwise remains in overall decline. Growth is coming from a range of industry sectors including financial services, debt collection, retail, freight and distribution, and charities. SDL's web based, hybrid mail software offering (DéjarMail) has been instrumental in the capture of most of the new opportunities within our existing customers and securing a broadening range of new customers. Achieving overall digital print revenue growth was a positive result given the company saw a major customer (the same one referred to above with reduced Déjar requirements) also reducing the number of pages in its mailings (the number of mailings remained the same but each mailing contained fewer pages). Growth for SDL is expected to continue to come from both new business wins and incremental business from existing clients, offset by the ongoing industry trend of migrating volumes to electronic distribution. However, the electronic delivery of documents revenues grew in excess of 50% year on year and incoming mail processing (i.e. scanning services) revenues grew in excess of 70% year on year.

High asset utilisation of SDL's print imaging and document handling equipment coupled with ongoing cost efficiency gains saw modest improvement in imaging gross margin. The first customer under the Fuji Xerox DMS agreement commenced trial printing late in the first half and is expected to progressively move to full production volumes from early in the second half of FY2017.

The Company is seeing increasing interest in its software technology in the UK, particularly DéjarMail. In addition to the reseller that is bundling it into its own software for dental practices in the UK, mail resellers are also attracted to DéjarMail as a means of capturing desktop mail volumes. The company has now signed up two large mail resellers and is in

discussions with other mail service providers in the UK and Europe. The dental software provider is also working with SDL to bundle Bremy (marketing communications solution) into its offering as a tool to allow dental practices to more easily automate their marketing and run promotional campaigns.

Financial Performance

Earnings before interest, tax, depreciation and amortisation (EBITDA) improved by $147,000 (+15.8%) to $1.08 million on sales volumes that rose 31.3%.

Summary Financial Performance (all figures $000)	**1H FY17**	**1H FY16**	**Yr-on-Yr $ Change**	**Yr-on-Yr % Change**
Total Revenue	**10,187**	**7,760**	**2,427**	**31.3%**
Cost of Goods Sold	6,348	4,411	1,937	43.9%
Gross Margin	**3,839**	**3,349**	**490**	**14.6%**
Gross Margin (%)	37.7%	43.2%		
Selling, General & Admin Costs	2,761	2,418	343	14.2%
EBITDA	**1,078**	**931**	**147**	**15.8%**
EBITDA Margin (%)	10.6%	12.0%		
Depreciation	107	128	-21	-16.4%
Amortisation	32	5	27	540.0%
EBIT	**939**	**798**	**141**	**17.7%**
Net Interest	2	-6	8	-133.3%
Net Profit before Tax	**937**	**804**	**133**	**16.5%**
Taxation	233	217	16	n.a.
Net Profit after Tax	**704**	**587**	**117**	**19.9%**

The EBITDA result gain is partly the benefit of higher gross margin in both Digital Print and Software & Technology. Underlying Selling, General & Admin (SG&A) costs remain well managed; the SG&A increase is partly accruing for higher staff incentive payments as a result of improved operating results, partly from higher costs in relation to new business initiatives and partly from increasing resources dedicated to support and revenue growth in the UK market. The UK market has significant opportunity for SDL and the Company has invested in supporting channels and new customers as well as adding additional direct sales resource.

SDL's tax rate in 1H FY2017 was 24.8% versus 27.0% in the prior period. This lower tax rate partly represents an adjustment for FY2016 taxation but is mainly the effect of the Company working through the balance of its UK tax losses.

Revenue Analysis (all figures $000)	**1H FY17**	**1H FY16**	**Yr-on-Yr $ Change**	**Yr-on-Yr % Change**
Software & Technology	2,424	2,038	386	18.9%
Digital Print & Document Handling	3,398	3,088	310	10.0%
Outsourced Services	4,365	2,634	1,731	65.7%
Total Revenue	**10,187**	**7,760**	**2,427**	**31.3%**

The 18.9% growth rate for Software & Technology revenue streams in the first half was on target and our ongoing sales efforts in the UK market are likely to ensure Software & Technology has a number of years of solid revenue growth ahead. Several significant new opportunities have been identified, mainly for the DéjarMail solution in the UK, Poland, Sweden and Ireland. However, the Company is overly reliant on direct sales efforts and a small number of key customers in the UK; SDL's small size and geographic distance from what is presently our most important growth market presents ongoing difficulties. The Board is presently addressing this by increasing staff numbers in the UK and would also particularly like to commend SDL's New Zealand-based staff for their additional efforts in servicing an increasing number of out-of-time-zone clients.

SDL is seeing strong market share gains in terms of volume of lodged mail with NZ Post and we expect this trend to continue. New digital print business wins should begin to generate modest revenue growth during the second half although this is partly dependent on the timing of when the print work handover occurs.

Balance Sheet, Liquidity and Debt

SDL closed the half year with net cash on hand of $1.858 million. A bank overdraft facility of $0.2 million remains in placed but is presently unused. The Company's balance sheet remains very strong with half year net cash on hand (i.e. cash less interest bearing debt) of $1.858 million. Moderate capital expenditure was incurred in the half on upgrading some of SDL's internal IT systems, but in general, capital expenditure requirements appear modest in the near term.

Selected Balance Sheet and Cashflow Figures (all figures $000)	**1H FY17**	**1H FY16**	**Yr-on-Yr $ Change**	**Yr-on-Yr % Change**
Net Cash on Hand (net of debt)	1,858	1,350	508	37.6%
Non-current Assets	2,105	1,993	112	5.6%
Net Other Liabilities	-570	-412	-158	38.3%
Net Assets	**3,393**	**2,931**	**462**	**15.8%**
Cashflow from Trading	893	743	150	20.2%
Movement in Working Capital	61	-49	110	-224.5%
Cash Inflow from Operations	**954**	**694**	**260**	**37.5%**

Book value (net assets) has increased by 15.8% to $3.393 million. Working capital continues to be well managed. SDL made capital expenditure additions during the half of $190,000, the majority of which, as noted above, was for IT system upgrades.

In reviewing the above cash flow and working capital figures, a degree of seasonality should be noted. Historically, sales and earnings are higher in 1H compared to 2H and accordingly the movement in working capital is negative in 1H, and positive in 2H. With SDL's software revenues increasing, the extent of this seasonality is beginning to reduce.

We reiterate the Company's cautious approach to acquisitions and strong preference for organic growth. The directors are conscious of the risks involved in acquisitions. In addition to being careful not to overpay, acquisitions would typically either need to be "bolt ons" where removal of duplicated costs means the effective acquisition multiple is very low, or product extensions where the acquisition fills a gap in SDL's software portfolio plus SDL has the opportunity to sell its software into the acquired company's customer base.

In early 2014 SDL commenced an Employee Share Option Plan ("ESOP"). That ESOP has issued options over 580,000 shares and 500,000 of these options mature in March 2017 (the remaining 80,000 mature in March 2018). The holders of the 500,000 options then have 18 months to exercise and convert them into shares should they elect to do so.

Dividend

SDL is declaring an interim dividend of 3.5 cents per share, an increase of 0.5 cent per share or 16.7% on the prior year.

Earnings and Dividend per Share	1H FY17	1H FY16	Yr-on-Yr Change	Yr-on-Yr % Change
Basic Earnings per Share (cents)	5.01	4.18	0.83	19.9%
Dividend per Share (cents)	3.50	3.00	0.50	16.7%
Dividend proportion Imputed	100.0%	100.0%	n.a.	n.a.
Payout ratio	69.9%	71.9%	n.a.	n.a.

The dividend is fully imputed and the amount represents a payout ratio of 70% of earnings per share. An arrangement with NZ Trade and Enterprise in relation to helping fund UK market development requires the Company to cap the dividend payout ratio at less than 75% for the duration of the agreement.

FY 2017 Outlook

The interim result was very slightly ahead of budget and in line with SDL's earnings outlook issued on 20 December 2016, which also noted a number of factors affecting growth. The Company reiterates its forecast of around 25% growth in earnings for the full financial year, albeit with some contingency that the timing and ramp up rate of several new customers proceeds as expected during 2H FY2017.

Recent software wins in the UK and a new print client in Australia, coupled with the ongoing rollout of SDL's software technology by existing and recently won UK clients, should ensure that, subject to the usual risk caveats, earnings growth continues in FY2018.

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