napatech

2016 ANNUAL REPORT

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Editors
Napatech A/S
Tobaksvejen 23A
2860 Søborg

DEAR READER

With our successful expansion into new markets, regions and technologies, we are truly beginning to reap the fruits of our strategy.

2016 has been a year of continued progress for Napatech. While we have seen quarter-to-quarter variations, we concluded the year with a record-high performance in Q4. A series of significant design wins with industry-leading corporations has further underpinned our position in the market – and we are excited to be entering 2017 with the persistent ambition to innovate.

The industry is currently finding itself in an overwhelming time of transition. Data volumes are accumulating at aggressive rates: The Statistics Portal predicts an increase in the number of connected devices from 22.9 billion in 2016 to 50.1 billion in 2020. And with the cybercrime threat environment equally escalating – damage costs are expected to hit $6 trillion annually by 2021 (source: SCO) – there is a growing need to stay connected and be secure.

Helping the industry to achieve this has been one of the key drivers in our 2016 product lineup. With the launch of our compact 40 and 100 Gigabit Accelerator product lines, we have helped customers in their transition to high-speed networks – enabling them to handle massive amount of data without compromising on performance. All of this with the added benefits of reducing cost and carbon footprint.

Another key highlight of 2016 has been the successful market entry of our capture-to-disk network recorder, Pandion. This platform captures, stores and retrieves all network data on demand – a crucial capability for incident forensics. Our Pandion product line has seen a significant growth, delivering 12% of the overall revenue in Q4 – and we are anticipating a promising pipeline for 2017.

Napatech NFV solutions have also matured over the past year. While the industry is still facing a delay in the full realization of NFV, the pace seems to be picking up. Over the past year, we have engaged with various industry-leading players and demonstrated performance improvements that continue to exceed expectations thus helping them to achieve the required flexibility and cost savings without impacting on performance.

Across product lines, we are seeing a solid increase in design wins, working with the top-tier solution providers of our key verticals: telco, cloud & data centers, financial services and infrastructure & defense. We firmly believe that this success can be ascribed to our Smarter Data Delivery offerings, ensuring that the right data is delivered to the right place at the right time.

Another key contributor to our continued success is no doubt the close relationship we have with our customers and partners. A core element of our strategy is our co-creation model – an initiative which has already generated solid results in the market. Working closely with our partners, we build agile and future-proof solutions to solve their challenges. We are also seeing great results from our channel partner program, where the collaboration with companies like Dell OEM and Arrow helps to broaden our global reach.

With this successful expansion into new markets, regions and technologies, we are truly beginning to reap the fruits of our strategy. Entering 2017, we are confident that the unique creativity and enthusiasm of our employees will sustain this growth momentum.

Kind regards,

Henrik Brill Jensen
CEO

OUR STRATEGY

NAPATECH PRODUCTS SUPPORT MAJOR TRENDS WITHIN MOBILE, SECURITY AND VIRTUALIZATION

MARKET LEADER IN ACCELERATOR SOLUTIONS

MARKET LEADER FOR NETWORK RECORDER SOLUTIONS

FRONT-RUNNER IN ACCELERATING VIRTUALIZED SOLUTIONS

Our strategy is centered around executing on 3 clearly defined strategic areas, all based on our leading-edge core technology and capabilities.

An important part of the strategic execution is Co-Creation with market leading customers. We define Co-Creation as development of new solutions, products and value-adding services in close collaboration with selected market-leading and innovative customers. We do this to secure more optimal and faster product adoption in the market.

THE NAPATECH STORY

Napatech solutions allow more efficient and flexible data delivery in both physical and virtualized environments.

The volume, complexity, and velocity of data in networks are increasing at explosive rates. This puts ever increasing pressure on network management and security applications to perform effectively and efficiently; organizations must not only monitor and analyze data, but must also correlate that data and predict trends - in real time or on demand, to guarantee the operational success of their digital services.

Cisco (Cisco Visual Networking Index: 2) predicts that global IP traffic will increase nearly threefold over the next 5 years, and will have increased nearly 100-fold from 2005 to 2020. Overall, IP traffic will grow at a compound annual growth rate (CAGR) of 22 percent from 2015 to 2020; Napatech is positioned to be a fundamental player in the future landscape of network architecture. Our solutions focus on providing the required data, allowing our customers to focus on building the most comprehensive management and security applications. That's what we call Smarter Data Delivery.

These trends are forcing on network engineers, system integrators, product managers, CTOs, and executives to deliver smarter solutions that are faster, more efficient, and able to deliver information on-demand. At the same time, they must find ways to cut both costs and development time. Further complicating these challenges, in the future more data will be routed through the virtual environments of Software-Defined Networking (SDN) and Network Functions Virtualization (NFV) where networks are transformed into a programmable platform allowing appliances, services and applications to be moved in the blink of an eye.

In this future landscape of network architecture, data capture and delivery becomes pivotal for mobile apps to run quickly, videos stream smoothly, financial trades be executed fairly, and end-user data remain secure. Network management and security applications need Smarter Data Delivery.

SMARTER DATA DELIVERY

RIGHT DATA

Having access to all the right data is fundamental for network management and cybersecurity purposes. The applications that help service providers to monitor the health of their networks and safeguard it against malicious attacks, rely heavily on the availability of 100% accurate data. With the Napatech core technology, these applications can have complete visibility into the nature of the problem/event to determine the kind of response needed.

RIGHT PLACE

Our solutions are designed to deliver critical information about network performance to the right applications on the network infrastructure. Network architectures, topology and protocols are built for sharing information which is facilitated by the Napatech solutions.

RIGHT TIME

With our solutions, our customers can capture, specify and retrieve data when they want. We allow our customers to retrieve data in real time as well as travel back in time with exceptional precision and guarantee information availability at even the highest Gigabit line rates. With information available at the right time, customers can reduce the overall costs from network disruptions and security breaches.

THE PEOPLE

The solutions Napatech provides are made possible by a highly skilled team that is committed to. Serving our customers through the development of innovative Smarter Data Deliver products that lead the market. The Napatech team is committed to creating shareholder value by serving the rapidly growing market for these solutions. When demanding requirements necessitate close integration with our customers' technology, our teams engage in co-creating solutions with our market leading partners, to solve their challenges in unique ways. Our increased commercial focus

#1
DATA DELIVERY VENDOR

CUSTOMERS
150+
INTERNATIONALLY

INDUSTRY EXPERIENCE
14
YEARS

means a closer collaboration and engagement with our key customers and leads to deep, long term relationships.

THE TECHNOLOGY

Napatech solutions are designed to address the data delivery challenges of management and security vendors through innovative product design. Napatech accelerators use a combination of cutting-edge hardware based on Field Programmable Gate Array (FPGA) technology and an extensive range of software capabilities. This enables guaranteed visibility into high-speed data traffic on several networks, across applications and at multiple speed rates based on commercial off-the-shelf server platforms.

The Napatech Pandion product family uses our innovative accelerator technology as a foundation to deliver high-precision Gigabit capture, indexing and search of network data. The recorder software not only provides core functionality to deliver network data back in time, but also features an industry standard REST API that allows our customers to easily integrate their management and security applications taking advantage of the recorded network data.

THE BUSINESS STRATEGY

At Napatech, we strive to be the number one vendor for Smarter Data Delivery solutions for applications that ensure the quality and security of the network services upon which we all rely. This position will be attained by focusing on continued growth in our accelerator and network recorder business while expanding the application of Napatech technology and solutions in new markets starting with Napatech solutions for data delivery in physical and virtualized environments.

Today, Napatech Smarter Data Delivery solutions include our broad 1, 10, 40, 100 and 200Gigabit portfolios of accelerators, Napatech Pandion network recorders and Napatech NFV NIC solutions. With these solutions, we ensure the availability of reliable data for real-time and on-demand post analysis We have also made progress in extending these capabilities to virtual environments, with the Napatech NFV NIC, which is designed for more efficient and flexible data delivery solutions to virtual applications.

Virtualization is just one of many technology trends that are shaping the future for Napatech and our customers. The Internet of Things, Big Data Analytics and the increase in cybersecurity threats are also driving major innovation in new solutions and techniques. Napatech intends to be on the forefront of these developments by engaging with our market-leading customers to co-create new solutions that address their needs. These solutions are based on continued sustained innovation in Napatech core technology and capabilities that will ensure that we remain on the leading edge in our core technology areas.

In 2017, Napatech aims to further enhance our portfolio of solutions for efficient and flexible data delivery in virtualized environments.

The concept of Network Functions Virtualization (NFV) was first introduced in 2012 with the goal of accelerating time-to-market for new communication services using a centrally controlled, programmable virtualized network infrastructure based on cost-effective standard hardware.

Instead of using dedicated appliances based on expensive, proprietary hardware and requiring manual administration, NFV can use common hardware that can be used to host any virtual function.

In just a few short years, over 200 carriers and vendors from the telecom and IT industry have succeeded in realizing functioning NFV solutions. Despite this success, there are still a number of challenges that threaten to undermine the promise of NFV.

To realize fast time-to-market for new services, it is important that virtual functions can be instantiated, scaled, moved and deleted on-demand. This also optimizes cost as it reduces the amount of un-used CPU cores and servers.

Napatech NFV solutions will focus on improving the performance of NFV infrastructures and virtual switching without constraints on how and where virtual functions are deployed. The goal is to maintain virtual function mobility allowing the full promise of NFV to be realized.

With these initiatives, we intend to continuously enhance the value we bring to our customers as a supplier and strategic partner, ensuring they stay one step ahead.

Napatech strategy is to grow organically and through co-creation with the right technology partners. We aim to use our current position and strong capital base to enable sustainable growth while building the long-term relevance of our technology for customers and shareholders.

COMPANY PROFILE

Napatech is the world leader in accelerating network management and security applications. As data volume and complexity grow, the performance of these applications needs to stay ahead of the speed of networks to do their jobs. We make this possible, for even the most demanding financial, telecom, government, cloud and data center networks. Now and in the future, we enable our customers' applications to run faster than the networks they need to manage and protect.

OUR MISSION

To keep our customers one step ahead of the data growth curve by delivering data faster, more efficiently and on-demand to their applications, while also accelerating their time-to-market and reducing risk.

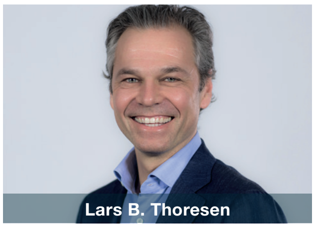
OUR VISION

To be the number one vendor for smarter data delivery solutions that ensure the quality and security of the applications and network services we all rely on.

Napatech. SMARTER DATA DELIVERY

BOARD AND MANAGEMENT PRESENTATION

BOARD OF DIRECTORS


Lars B. Thoresen


Bjørn Erik Reinseth


Howard Bubb

MANAGEMENT TEAM


Henrik Brill Jensen


Niels Hobolt


Jarrod J.S. Siket


Peter Ekner


Flemming Andersen


Andrew Patterson


Heidi Thisgaard

BOARD OF DIRECTORS

Lars B. Thoresen, Chairman. Directorships: Lt Invest AS – CEO/Chairman of the board, Verdane Capital – Senior Advisor, Arundo Analytics – Board Member, Arundo Analytics – Board Member, The Future Group – Board Member, Carn Capital – Board Member.
Bjørn Erik Reinseth, Board member. Directorships: Foinco AS – CEO, Zentuvo AS – Chairman of the board/CEO, AllieroGruppen AS – Chairman of the board, Norstat AS – Chairman of the board.
Howard Bubb, Board member. No other directorships or executive functions.

MANAGEMENT TEAM

Henrik Brill Jensen, CEO. **Niels Hobolt**, CFO. **Peter Ekner**, CTO. **Jarrod J.S. Siket**, CMO. **Flemming Andersen**, EVP of Engineering. **Andrew Patterson**, SVP Global Sales. **Heidi Thisgaard**, HR Manager.

KEY MARKETS

NAPATECH PRODUCTS ARE ESSENTIAL IN MARKETS WITH MASSIVE DATA USAGE

TELECOM OPERATORS

FINANCIAL SERVICES

CLOUD AND DATA CENTER SERVICES

INFRASTRUCTURE AND DEFENCE

We have selected four markets where we already have solid business, and where we believe there are great future potentials for Napatech to grow, and help our customer by solving their need for smarter data delivery.

Today, we have top tier customers in all four market areas, and the common denominators for these customers are that they are looking for data to be delivered: Faster, More Efficient and On-demand.

GROUP KEY FIGURES AND RATIOS

	2016	2015	2014	2013	2012
KEY FIGURES (DKK'000)					
Revenue	234,737	216,677	182,335	182,047	181,179
Gross profit	163,608	154,701	133,627	130,501	128,581
EBITDA	43,459	34,232	18,010	29,354	39,510
EBIT	6,001	5,465	(5,889)	7,998	18,289
Net finance income / (expense)	(60)	5,534	5,186	580	(1,007)
Profit / (loss) before tax	5,941	10,999	(703)	1,796	17,282
Profit / (loss) for the year	3,723	7,713	(981)	(509)	12,501
Investments in intangible assets	45,792	42,915	38,371	26,446	18,433
Investments in tangible assets	3,178	4,125	7,244	4,649	3,389
Net working capital	55,444	27,663	20,333	8,776	7,233
Total assets	261,399	247,552	224,829	232,648	122,459
Equity	204,409	197,002	189,619	190,364	89,868
Net cash flows from operating activities	15,176	33,226	10,665	23,538	49,267
Cash at the end of year	46,951	75,921	88,230	122,223	30,105
Free cash flow	(33,882)	(14,272)	(35,047)	(7,987)	27,372
Average number of employees	107	108	106	95	79
FINANCIAL REPORTING RATIOS (%)					
Gross profit margin	69.7%	71.4%	73.3%	71.7%	71.0%
EBITDA margin	18.5%	15.8%	9.9%	16.1%	21.8%
Current ratio	339.0%	360.3%	462.9%	461.9%	232.2%
Return on equity	1.9%	4.0%	-0.5%	-0.4%	15.5%
SHARE-RELATED RATIOS (DKK)					
Basic EPS*	0.16	0.33	(0.04)	(0.03)	0.90
Diluted EPS*	0.15	0.33	(0.04)	(0.03)	0.88
Free cash flow per share*	(1.41)	(0.61)	(1.51)	(0.51)	1.92
Cash flow per share*	0.63	1.43	0.46	1.50	3.46

* In accordance with the decision made on the Annual General Meeting held on 20 April 2016, Napatech conducted a split of shares in the ratio of 1:4. The nominal value of each share has been reduced from DKK 1.00 to DKK 0.25, whereby each shareholder holding one share with the nominal value of DKK 1.00 received four new shares with the nominal value of DKK 0.25. This principal has been applied on comparative figures in order to enable comparison and consistency of share-related ratios with previous periods.

KEY FIGURE AND RATIO EXPLANATIONS AND DEFINITIONS

The financial highlights and ratios are defined and calculated in accordance with the guidance from the Danish Finance Society regarding the calculation of financial highlights and ratios: ”Recommendations & Financial Ratios 2015”.

Ratio	Calculation formula	Explanation
Gross profit margin	$\frac{\text{Gross profit}}{\text{Revenue}} \times 100$	The ratio represents the percentage of the revenue less cost of goods sold to cover research and developent costs, selling and distribution costs, administrative expenses, depreciation and amortisation and finance costs.
EBITDA margin	$\frac{\text{EBITDA}}{\text{Revenue}} \times 100$	The ratio represents the Group’s operating profitability.
Current ratio	$\frac{\text{Current assets}}{\text{Current liabilites}} \times 100$	The ratio represents the percentage of the Groups resources to meet its liabilities over the next 12 months.
Return on equity	$\frac{\text{Profit for the year}}{\text{Average equity}} \times 100$	The ratio represents the Groups ability to generate return to shareholders taking into account own capital base.
Operating cash flow per share	$\frac{\text{Cash flows from operating activities}}{\text{Average number of diluted shares}} \times 100$	The ratio represents the Groups ability to generate cash flow from operating activities per the average number of diluted shares.
Free cash flow per share	$\frac{\text{Free cash flow}}{\text{Average number of diluted shares}} \times 100$	The ratio represents the Groups ability to generate cash flow from operating and investing activities per the average number of diluted shares.

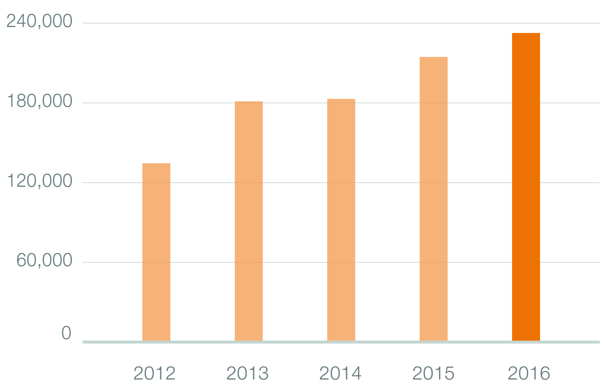
Net working capital represents the value of inventories, trade receivables of other current operating assets less trade payables and other current operating liabilities. Cash and cash equivalents and income tax receivable or payable are not part of the net working capital.

Cash flows from operating activities are profit or loss before tax added or deducted changes in the net working capital, added or deducted changes in provisions and added the yearly depreciation and amortisation.

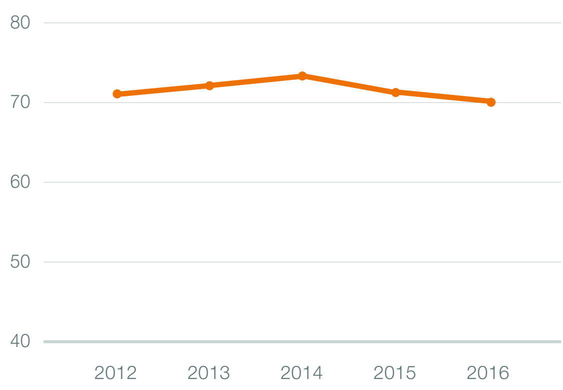
Free cash flow is net cash flow from operating activities added or deducted investing activities.

Groups basic and diluted earnings per share (EPS) is calculated in accordance with IAS 33 and specified in Note 13 to the consolidated financial statements.

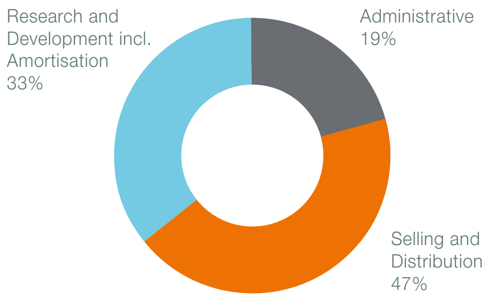
REVENUE in DKK'000



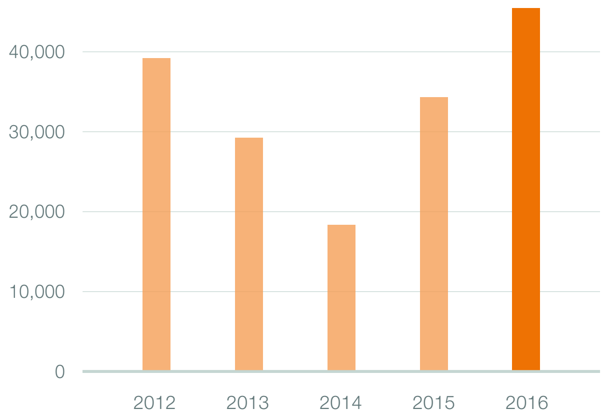
GROSS MARGIN IN %



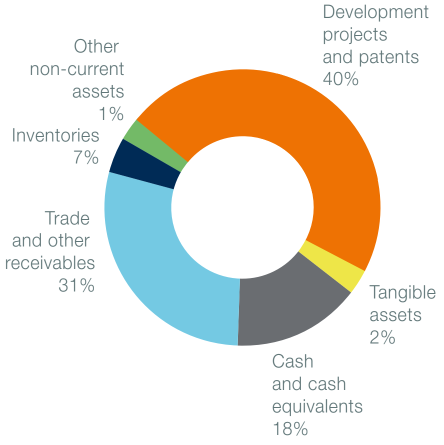
COST



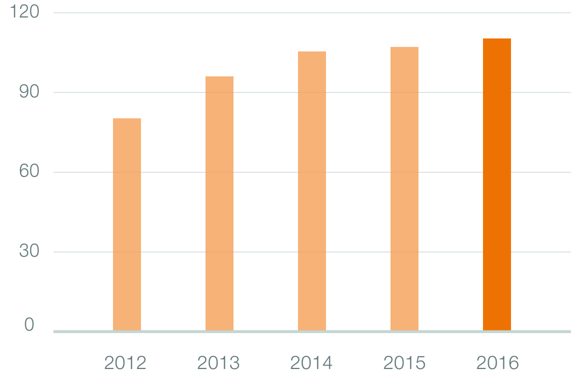
EBITDA IN DKK'000



ASSETS



AVERAGE NUMBER OF EMPLOYEES



BOARD OF DIRECTORS' REPORT 2016

Napatech aims to become the recognized standard for data delivery in the network appliance market.

SUMMARY

Napatech believes network traffic, as well as services and activities on the internet, will continue to increase rapidly in the future, resulting in both higher bandwidth and utilization. The former; easy but expensive to cope with, while the latter is difficult to handle.

The increasing network traffic, as well as the complexity of the traffic, will make it increasingly difficult for companies, people and governments to continue to deliver the same level of service and security.

Napatech's solutions are specifically designed to enable our customers to cope with very high line utilization, allowing their software to continue functioning even when line utilization reaches 100%.

Napatech has a range of solutions, branded under the umbrella Smarter Data Delivery, tailored to deliver network data to our customers' software solutions, smarter – hence Smarter Data Delivery. We call it smarter, with good reason. Our solution delivers the data exactly how the software wants to receive it, in the order the software needs it, and to the CPU cores that are ready to handle data processing – with extremely high speed and accuracy.

We believe that the need for Napatech's solutions will grow going forward, based on the trend of increasing network data.

Napatech's current solutions are developed and marketed in two different business areas. Firstly, our traditional network accelerators, which have been the core of the company since inception in 2003, and currently represents our largest business area. Secondly, the Network Recording (Pandion) business area, which is a complete solution platform for capturing and indexing 1000s of terabytes of data for rapid retrieval and analysis by third party software applications.

A typical customer for an Accelerator is a company that builds network equipment (OEM customers), ranging from security solutions to monitoring and analysis of the network itself.

Typical customers for Pandion are companies that needs a historical picture of the network traffic, like financial institutions, governments, cloud and enterprise data centers.

Napatech is a leading OEM supplier of smarter data delivery solutions, with a large portion of Tier 1 network equipment manufactures as customers. Napatech is constantly working towards expanding our engagement with existing customers, as well as adding new customers to our portfolio.

Our business objective is to grow by extending worldwide sales and support capabilities into new verticals and geographies, thus supporting the growth of our global customers while addressing local market needs. We plan to grow the business across current markets and customers by enhancing our product portfolio to stay one step ahead of market demands for next-generation network connectivity, while at the same time exploiting the latest server and industry standards.

Napatech has been a leading provider of advanced data delivery hardware and software since 2003. The Company is headquartered in Copenhagen, Denmark and has three offices in the United States, one in Japan, one in Taiwan, and one in South Korea.

GROUP ENTITIES

The United States subsidiary has offices in Andover, MA, Los Altos, CA, and Columbia, MD.
The Parent Company has a branch office in Seoul, South Korea. The subsidiary in Japan has an office in Tokyo.

SOLUTIONS

TELECOM OPERATORS

– WE KEEP TELECOM OPERATORS ONE STEP AHEAD OF THE DATA DELUGE

Our solutions deliver data faster, more efficiently and on-demand to applications that analyze, in real time, all the information going through telecom networks. This secures that operators can manage and operate their LTE networks with greater precision as well as enables them to tailor their solutions and offer new services that customers want to purchase.

FINANCIAL SERVICES

– WE DELIVER DATA FOR LATENCY ANALYSIS TO ENSURE TRADING RUNS SMOOTHLY

Financial information providers depend on the transport of critical market data with the lowest delay possible, without compromising delivery. In order to ensure that trading runs smoothly, exchanges, trading institutions, and service providers all need reliable data delivery to the analysis application. Our solutions deliver data, with nano second precision, to independent network monitoring systems that are able to visualize all transactions in real time.

CLOUD AND ENTERPRISE DATA CENTRE SERVICES

– WE HELP ENSURE QUALITY OF EXPERIENCE AND ENABLE NEW BUSINESS MODELS

Cloud and data center service providers need insight into their vast and complex networks. Our solutions deliver data to applications that provide impeccable quality of experience and security without compromising on data availability. Seeing trends within their traffic will allow cloud and data centers to offer innovative services, maximizing their business potential.

INFRASTRUCTURE AND DEFENCE

– WE HELP INFRASTRUCTURE AND GOVERNMENT NETWORKS RUN SMOOTHLY AND SAFELY

Government and infrastructure network managers face the challenge of exponential growth in data volume and complexity, as well as increased sophistication of attacks on public safety. Our solutions deliver data to security applications that protect public and private information, as well as critical infrastructure networks.

FINANCIAL DEVELOPMENT

(2015 FIGURES IN BRACKETS)

Net revenues in 2016 came in at DKK 234.7 million (DKK 216.7 million) representing a modest revenue growth. The Group experienced softness in the North American market as we saw delays in a couple of customers ordering pattern, APAC did show a limited growth for the year, but with good progress in the Chinese market, where we entered more focused during the year. The EMEA market showed significant improvements with growth of 71% for the year. The EBITDA for 2016 was DKK 43.5 million (DKK 34.2 million), and the profit before tax for the year was DKK 5.9 million (DKK 11.0 million).

The Group's equity at the end of the year was DKK 204.5 million (DKK 197.0 million).

The Group has in-house development resources, developing new products and new functionality (features). The group also engages external consultants for specific development projects. Development costs are capitalized in compliance with IFRS. DKK 45.8 million was capitalized in 2016 (DKK 42.9 million). The increase is due both to added internal resources and external costs in connection with the new hardware platforms, as well as our Pandion products.

The financial items were close to zero, with a negative DKK 60 thousands.

The Group had a negative cash flow of DKK 28.9 million (negative DKK 12.3 million), primarily due to the negative change in working capital, driven by the large increase in receivables due to increased activities during Q4. Total cash balance was DKK 47.0 million at the end of the year.

Total revenue, EBITDA and Pandion revenue for 2016 ended in line with our Q3 market guidance announced in November 2016 as follows:

Target	Realised 2016	Guidance 2016
Revenue Growth	8%	5-15%
EBITDA margin	19%	Around 20%
Pandion revenue (% of total revenue)	7%	Around 10%

FINANCIAL DEVELOPMENT IN THE PARENT COMPANY

Net revenues for the Parent Company in 2016 came in at DKK 198.0 million (DKK 183.1 million) representing a revenue increase of 8%. The EBITDA in the Parent Company for 2016 was DKK 43.6 million (DKK 29.4 million), and the profit for the year was DKK 5.2 million (DKK 4,4 million).

NET REVENUES

234.7

DKK MILLION

EBITDA

43.5

DKK MILLION

PROFIT BEFORE TAX

5.9

DKK MILLION

LEADING
200G
TECHNOLOGY

INDUSTRY AWARDS
20+
WORLDWIDE

GUARANTEED
100%
DATA DELIVERY

DEVELOPMENT ACTIVITIES AND KNOWLEDGE

The Company has historically focused on the development of new products and solutions within our Accelerator product line, both for existing markets and new markets, this work continued with high efforts through 2016. Additionally the Company invested significant resources on development of our new revenue stream, the Pandion product line for network recording, and finally we invested in the solutions for the Virtualised network functions. The network recording solutions are a fast engine for real-time capture, indexing and search of network data. The first products based on this technology is our Pandion 20 and Pandion Flex these 10-40 Gigabit recording solution, which allows Napatech customers to focus on software innovation for their management and security solutions. Napatech underlines its technology leadership by providing new and innovative products and functionality for our entire portfolio of 1, 10, 40 and 100 gigabit products.

Napatech spends a significant part of its development activity during the year targeting solutions for the growing mobile market and solutions within cybersecurity. The Napatech development team is organized in smaller cross-functional teams to secure optimal information sharing and agile product development. In addition, there is extensive use of IT tools that support the sharing of knowledge. All development activities are done in the Parent Company, at one location in Denmark, which ensures a high degree of collaboration, focus and operational excellence.

DIVIDEND

The Company has until now not distributed any dividends, and does not expect to do so in the near future.

CORPORATE GOVERNANCE

The Company's Board of Directors recognizes the importance of good corporate governance. This is ensured through interaction between shareholders, the Board of Directors, and the administration. Napatech's goal is that all interested parties are confident that the Group's activities are carried on in an acceptable way and that governing bodies have sufficient insight and influence to undertake their functions.

The communication between The Company and shareholders primarily takes place at the Company's annual general meeting, quarterly financial reporting and via Company announcements. The Company shareholders are encouraged to subscribe to our investor relation e-mail service to receive Company announcements as well as other news via e-mail.

Guidelines on Corporate Governance are approved annually by the Board of Directors in connection with the approval of the Financial Statements or when deemed necessary. The guidelines are based on the Norwegian Code of Practice for Corporate Governance, last revised on October 30th, 2014. The Norwegian Corporate Governance Board has decided not to amend the Norwegian Code of Practice for Corporate Governance in 2016. The Code of Practice are using the "follow or explain principle". The Company follows all the 14 recommendations.

The Board of Directors has established three committees within the Board; The Remuneration Committee, the Audit Committee and the Risk and Strategy Committee, of which all are sub-committees of the Board (the Board committees report to the Board of Directors) and operates according to the established internal procedures for each Committee decided by the Board of Directors.

The Remuneration Committee is composed of three members of the Board of the Directors and the CEO of the Company. Chairman Lars Thoresen is the chairman of the Remuneration Committee and Howard Bubb and Bjørn Erik Reinseth is member of the Committee. The Remuneration Committee handles the Company's remuneration policy and programs, including bonus programs and share-based schemes, and presents recommendations to the Board of Directors for decision according to its meeting protocols and underlying material prepared. The Committee normally evaluates annually the CEO's remuneration and presents recommendations to the Board of Directors for decision.

The Company's remuneration policy, when proposed changed, is subject to approval by the annual general meeting.

The Audit Committee is composed of two members of the Board of Directors. Bjørn Erik Reinseth is the chairman of the Committee and Lars Thoresen is a member of the Audit Committee. This Committee supports the Board of Directors in fulfilling its responsibilities, with respect to financial reporting, auditing matters, internal control, and risk matters.

The Risk and Strategy committee is composed of two members Board of Directors Chairman Lars Thoresen is the chairman of the Committee and Howard Bubb is a member. The Risk and Strategy Committee oversees Napatech's corporate strategic planning processes and reviews Napatech's enterprise risk management processes and related actions implemented by management.

The Company's Board of Directors shall have a diverse composition and competence tailored to meet the Company's needs. None of the Board members are employees of the Company and the Board of Directors' work complies with the Company's internal instructions, guidelines and procedures for the Board members. The Board normally also carries out a self-assessment of its own activities and competence.

The Board of Directors held 13 Board meetings in 2016, whereby 4 of the meetings were for the approval of the quarterly report and presentations.

The former Chairman of the Board Olav Stokke became ill around the year-end and resigned from his duties on the 19th of January 2017.

The Guidelines, incl. the annual corporate governance status, can be found on the Company's investor relations website, at www.napatech.com/investor

RISKS

The Group is, due to its normal course of business, exposed to a number of risk factors. The Group operates in a technology market that could change the needs for the solutions that the Group provides. The customers are mainly large tier one customers, with normal credit terms. The Group is not significantly exposed towards credit risks, but as some customers are large, the outstanding amounts can potentially be substantial.
The Group is exposed to operational risks, as the Group depends on suppliers to deliver both components and the finished products necessary to recognize revenue.
The Group's growth partly depends on the delivery and adoption of new products and functionalities by the market.

As the Group has all revenue in USD, and some assets in USD as well, there is a risk that fluctuations in USD exchange rate will affect the Groups financial performance.

RISK MANAGEMENT AND INTERNAL CONTROL

The risk management relating to the Group's financial performance is controlled by the Group's CFO. The Board of Directors receives monthly financial reports from the finance department, including financial and operational key performance indicators. The Company approves and presents quarterly reports to the market in accordance with IAS 34. Financial reports are prepared and issued by the finance department, and the financial responsibility for quality assurance of the financial reports lies with the CFO. The Group has, under careful consideration of its limited size, set up procedures to secure the best possible segregation of duties.

CORPORATE SOCIAL RESPONSIBILITY

The Group has not adopted any further specific policies regarding Corporate Social Responsibilities including policies for human rights, climate and environmental impact.

Companies in the Group do not generate higher levels of direct pollution or emissions than those that are normal for a company in the industry. The working environment is considered to be good, and the general wellbeing in the work place is good.

At Napatech we assign resources to ensure compliance with changing legislation. We make sure that working conditions are safe and that our workers are treated with fairness, respect, and dignity.
Any form of corruption, extortion, or embezzlement is strictly prohibited. No bribes or improper advantage are offered or accepted. Compliance to EICC's Code of Conduct is a matter of course. We have never received a single fine or penalty regarding corporate, employee, or environmental issues.

We are committed to conducting business operations in an environmentally responsible and ethical manner, and established a Conflict Mineral policy with the objective to only use 3TG that originate from conflict-free sources.

OUR PRODUCTS

Our products are assembled by contract manufacturers that share our ambitions for social responsibility.
We investigate each component regularly, and we declare that we are conformance with the EU RoHS directive and the REACH regulation.

Our products comply with EU directives and carry the CE-mark, as declared in our EU declaration of conformity. They carry the UL mark for recognized components, and they are manufactured under UL's inspection and follow-up service, ensuring that safety critical components are authenticated and handled according to UL's procedures.

OUR EMPLOYEES

The Groups' 107 average employees in 2016, and included 15 women (14%). The Group primarily employs engineers, and as women are underrepresented among engineers, it is considered a natural consequence that women are underrepresented in the Group. There is one woman in management, holding the position as responsible for HR. It is the groups policy is to increase the presence of womens in the management team, by including at least one woman in the field of the last five candidates. It is however always the best candidate for a specific position that will be chosen. The Board of Directors consists of men only. The Board of Directors has a goal to have at least 20% women on the Board, within the next 1 year, and to increase the presence of women throughout the organisation. It is, however, always the candidate which is deemed best suited for a position that will be offered said position.

The Group has a diversification strategy and has, in the Danish headquarter, employed 14 different nationalities. Salaries, positions and duties are determined on the basis of qualifications and experience.

OUR CLIMATE AND ENVIRONMENT

The Group's main impact on the environment is through the parent company and the US based subsidiary's consumption of electricity consumption and through the usage of Group's petrol driven cars. The Group has 6 different locations which is a fairly high number of locations compared to the size of the company with an average number of employees of 107 in 2016. Almost all emissions are Scope 2 emissions, with the exception of the emissions from the company fleet. The only Greenhouse gas emissions that Napatech has and accounts for is Carbon Dioxide.

The Group has its own internal environmental policies which oblige the Group to take reasonable steps in order to reduce the environmental impact. The group goal is to make measurements covering at least 85% of the employees in 2016.

LEGAL MATTERS

There are currently no legal proceedings which involve any company in the Napatech Group.

EVENTS AFTER YEAR-END

There are no material events after the year-end and until this date.

OUTLOOK

Napatech´s strategy is to be the #1 vendor of Smarter Data Delivery Solutions, based on market expansion, product line investment and strong Tier 1 customer penetration:

- Accelerator solutions, where the full potential has yet to be exploited
- Network recorders solutions, representing a fast growing market
- Virtualizations solutions, enabling new opportunities

Building on the growth of 8% in 2016, the company expects the revenue growth to continue in 2017, the company expects profitable revenue growth to continue in 2017, across the business areas. Consequently, the company provides the following guidance for 2017:

- Revenue growth of 10 to 20% compared to 2016
- Gross margin around 68%
- EBITDA margin around 20%

The progress from our new design-wins in both the Accelerator product line as well as our Pandion product line will drive this growth.

The company is exposed to risks that might affect our ability to reach our goals such as currency fluctuations, general market uncertainty, and material changes in our large OEM's needs for Napatech's products.

Napatech is comfortable with an accelerated growth path towards the ambition of 100 MUSD top-line by 2020, but underlines that the short term visibility is limited and will be affected by quarter-to-quarter order volatility and general business uncertainty.

EMPLOYEES
107
FULLTIME

WORLDWIDE
14
NATIONALITIES

LOCATIONS
7
WORLDWIDE

SHAREHOLDER INFORMATION

The Group has a policy of continuously keeping shareholders, employees and other stakeholders updated on the Group's operations.

At the end of the year, the Company had a total of 23,665,456 shares outstanding of a norminal value of DKK 0.25. The company owned 10,800 treasury shares at year end. The company had 377 shareholders and 50% of the shares were registered outside Norway. Total outstanding warrants at the end of the year were 1,414,984 warrants with an average exercise price of DKK 10.03. Napatech has one class of shares, and no restriction on the trading in the Company's shares.

The Group has a policy of continuously keeping shareholders, employees and other stakeholders updated on the Group's operations. This is achieved via open quarterly presentations and continuously updating the investor relations page on www.napatech.com

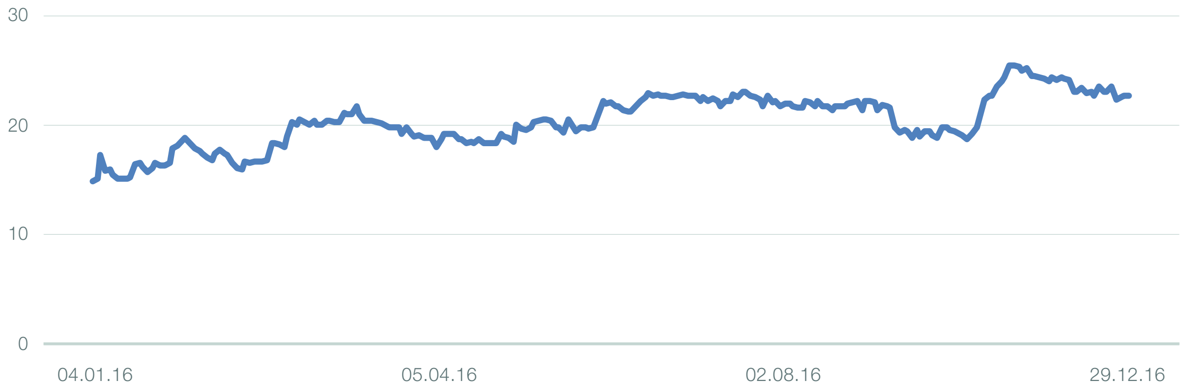
Napatech is a Danish company registred in the Danish company registered with 10109124. The ISIN number is DK0060520450, and the Company trades on Oslo Stock Exchange under the Ticker: NAPA.

In April 2016 the company conducted a share split 1:4, in order to increase the liquidity in the share.
During 2016 a number of releases have been announced on Oslo Stock market under the ticker: NAPA. For a complete overview, please see www.newsweb.no

The Company's financial calendar for the remainder of 2017 is:

Date	Activity	Venue
April 4, 2017	CMD	Oslo
April 20, 2017	Annual assembly	Copenhagen
May 9, 2017	Q1 2016 report	Oslo
Aug. 15, 2017	Q2 2016 report	Oslo
Nov. 7, 2017	Q3 2016 report	Oslo

NAPATECH SHARE PRICE DEVELOPMENT 2016 IN NOK

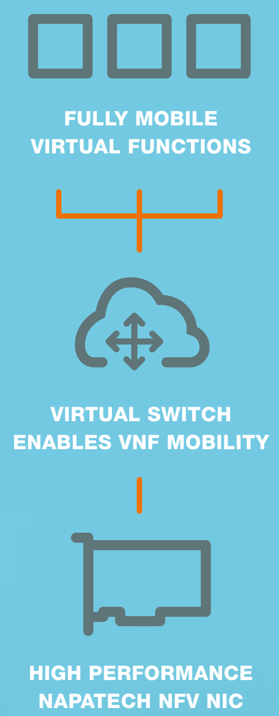


NAPATECH HAD BY 1ST MARCH 2017 THE FOLLOWING TOP 20 SHAREHOLDERS

Investor	Number of shares	% of total	Country
Verdane Capital VIII	5,172,844	21.72%	Denmark
Storebrand Vekst	2,361,216	9.92%	Norway
Arctic Funds PLC	2,270,021	9.53%	Irland
Silvercoin Industrie	1,381,122	5.80%	Norway
Verdipapirfondet DNB	1,228,543	5.16%	Norway
The Bank of New York	980,000	4.12%	Great Britain
DNB Nor Markets, AKS	950,000	3.99%	Norway
Vinterstua AS	935,900	3.93%	Norway
Danske Bank A/S	692,037	2.91%	Denmark
Sæter Haakon Morten	670,000	2.81%	Norway
Marstal AS	520,000	2.18%	Norway
Skandinaviska Enskilda	500,000	2.10%	Norway
DNB Luxenborg S.A.	360,177	1.51%	Luxemburg
Tigerstaden AS	347,783	1.46%	Norway
Nordea Bank Danmark	299,742	1.26%	Denmark
Nordnet Bank AB	294,204	1.24%	Sweden
Hobolt Niels	263,872	1.11%	Denmark
Perdersen Tore André	258,361	1.08%	Norway
Six-Seven AS	256,870	1.08%	Norway
Ekner Peter Dahl	247,200	1.04%	Denmark
Total owned by top 20	19,989,892	83.94%	
Total owned by 357 other	3,823,828	16.06%	
Total number of shares	**23,813,720**	**100.00%**	

NETWORK VIRTUALIZATION

TELECOM OPERATORS AND DATACENTERS ARE LOOKING FOR COST EFFECTIVE SOLUTIONS

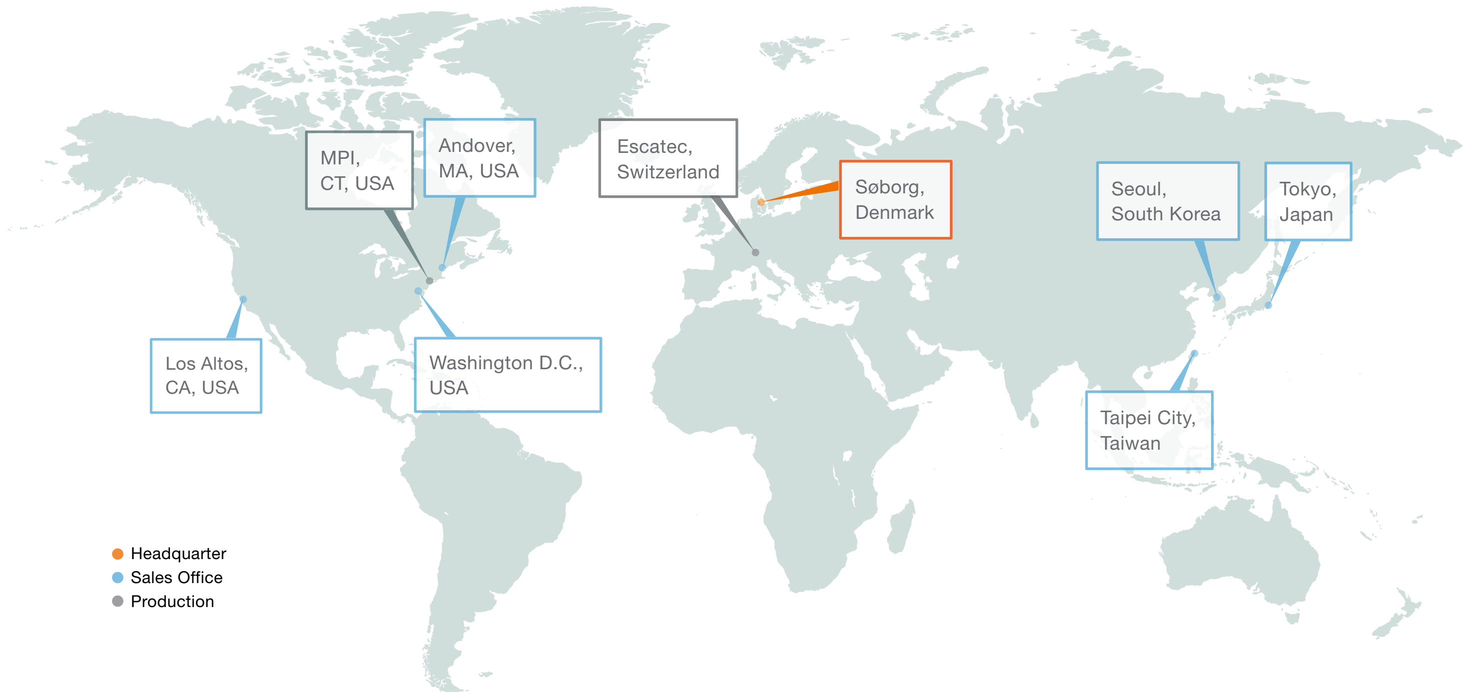


Napatech NFV NIC solution enables full optimization of datacenter server usage by allowing any function to be run anywhere with full throughput and flexibility. This unique solution also simplifies management and orchestration of virtual networks as there are no constraints or exceptions on where virtual functions can be deployed.

With the Napatech NFV NIC solution we make the dream of Network Functions Virtualization a reality.

GEOGRAPHICAL PRESENCE

We belive it is extremely important to be responsive and attentive to our customers, to accomplish that we har located in different offices around the world. In the map below, our presence and the locations of our outsourced production facilities are also shown.



FINANCIAL STATEMENTS

CURRENT ASSETS	NET OPERATING CASH FLOW	EQUITY
147.7	15.2	204.4
DKK MILLION	DKK MILLION	DKK MILLION

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2016

Note	In DKK '000	2016	2015
4	Revenue	234,737	216,677
	Cost of goods sold	(71,129)	(61,976)
	Gross profit	**163,608**	**154,701**
5, 6	Research and development costs	(15,164)	(15,094)
5	Selling and distribution expenses	(74,677)	(70,728)
5, 7, 8	Administrative expenses	(30,308)	(34,647)
	Operating profit before depreciation, amortisation and impairment (EBITDA)	**43,459**	**34,232**
9	Depreciation, amortisation and impairment	(37,458)	(28,767)
	Operating profit (EBIT)	**6,001**	**5,465**
10	Finance income	303	6,122
11	Finance costs	(363)	(588)
	Profit before tax	**5,941**	**10,999**
12	Income tax	(2,218)	(3,286)
	Profit for the year	**3,723**	**7,713**
13	**Earnings per share:**		
	Basic, DKK	0.16	0.33
	Diluted, DKK	0.15	0.33

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2016

Note	In DKK ’000	2016	2015
	Profit for the year	3,723	7,713
	Other comprehensive income to be reclassified to profit and loss in subsequent periods:		
	Exchange differences on translation of foreign operations	429	28
	Value adjustments on hedging instruments:		
	- Net gain / (loss) on cash cash flow hedges	743	(3,840)
	- Net (gain) / loss on cash cash flow hedges reclassified to revenue	(886)	2,594
	- Net (gain) / loss on cash cash flow hedges reclassified to finance costs	(163)	237
	- Income tax effect	53	237
	Net other income / (loss) to be reclassified to profit or loss in subsequent periods	176	(744)
	Total comprehensive income for the year, net of tax	**3,899**	**6,969**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2016

Note	In DKK '000	2016	2015
	ASSETS		
	Development projects, completed	75,689	70,087
	Development projects, in progress	22,488	12,439
	Patents	6,379	7,665
	Other intangible assets	489	1,202
14	**Intangible assets**	**105,045**	**91,393**
	Plant and equipment	5,186	7,435
	Leasehold improvements	1,173	1,049
15	**Tangible assets**	**6,359**	**8,484**
21	Leasehold deposits	2,312	2,224
	Other non-current assets	**2,312**	**2,224**
	Non-current assets	**113,716**	**102,101**
17	Inventories	18,675	14,341
18, 21	Trade receivables	75,119	48,254
18, 21	Other receivables	4,844	4,484
19	Income tax receivable	2,094	2,451
21	Cash and cash equivalents	46,951	75,921
	Current assets	**147,683**	**145,451**
	Total assets	**261,399**	**247,552**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2016

Note	In DKK '000	2016	2015
	EQUITY AND LIABILITIES		
20	Issued capital	5,916	5,822
20	Share premium	216,429	210,675
	Foreign currency translation reserve	510	81
20	Other capital reserves	39,830	9,209
	Retained earnings	(58,276)	(28,785)
	Equity	**204,409**	**197,002**
16	Deferred tax liability	8,427	5,182
21, 24	Interest-bearing loans and borrowings	5,000	5,000
	Non-current liabilities	**13,427**	**10,182**
21, 24	Interest-bearing loans and borrowings	-	637
21	Trade payables	25,978	18,645
21	Other payables	15,902	19,763
22	Derivative financial instruments	1,314	1,008
23	Provisions	369	315
	Current liabilities	**43,563**	**40,368**
	Total liabilities	**56,990**	**50,550**
	Total equity and liabilities	**261,399**	**247,552**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2016

Note	In DKK '000	Share capital	Share premium	Foreign currency translation reserve	Share based payment reserve	Cash flow hedge reserve	Reserve for development project costs	Retained earnings	Total equity
	At 1 January 2015	**5,812**	**210,675**	**53**	**12,101**	**-**	**-**	**(39,032)**	**189,619**
	Profit for the year	-	-	-	-	-	-	7,713	7,713
	Exchange differences on translation of foreign operations	-	-	28	-	-	-	-	28
	Net loss on cash cash flow hedges	-	-	-	-	(3,840)	-	-	(3,840)
	Net loss on cash cash flow hedges reclassified to revenue	-	-	-	-	2,594	-	-	2,594
	Net loss on cash cash flow hedges reclassified to finance costs	-	-	-	-	237	-	-	237
	Income tax effect	-	-	-	-	237	-	-	237
	Total comprehensive income	**-**	**-**	**28**	**-**	**(772)**	**-**	**7,713**	**6,969**
	Issue of shares	-	-	-	-	-	-	-	-
	Reversal, exercised and lapsed share options	-	-	-	(2,534)	-	-	2,534	-
7	Share-based payments	-	-	-	414	-	-	-	414
	Total transactions with shareholders	**-**	**-**	**-**	**(2,120)**	**-**	**-**	**2,534**	**414**
	At 31 December 2015	**5,822**	**210,675**	**81**	**9,981**	**(772)**	**-**	**(28,785)**	**197,002**
	Profit for the year	-	-	-	-	-	-	3,723	3,723
	Additions to project development costs, net of tax	-	-	-	-	-	33,244	(33,244)	-
	Exchange differences on translation of foreign operations	-	-	429	-	-	-	-	429
	Net gain on cash cash flow hedges	-	-	-	-	743	-	-	743
	Net gain on cash cash flow hedges reclassified to revenue	-	-	-	-	(886)	-	-	(886)
	Net gain on cash cash flow hedges reclassified to finance costs	-	-	-	-	(163)	-	-	(163)
	Income tax effect	-	-	-	-	53	-	-	53
	Total comprehensive income	**-**	**-**	**429**	**-**	**(253)**	**33,244**	**(29,521)**	**3,899**
	Issue of shares	94	2,939	-	-	-	-	-	3,033
	Reversal, exercised and lapsed share options	-	2,815	-	(2,845)	-	-	30	-
7	Share-based payments	-	-	-	475	-	-	-	475
	Total transactions with shareholders	**94**	**5,754**	**-**	**(2,370)**	**-**	**-**	**30**	**3,508**
	At 31 December 2016	**5,916**	**216,429**	**510**	**7,611**	**(1,025)**	**33,244**	**(58,276)**	**204,409**

CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended 31 December 2016

Note	In DKK '000	2016	2015
	Operating activities		
	Profit before tax	5,941	10,999
	Adjustments to reconcile profit before tax to net cash flows:		
	Finance income	(303)	(6,122)
	Finance costs	363	588
	Depreciation, amortisation and impairment	37,458	28,767
	Share-based payment expense	475	414
	Currency adjustment		
	Working capital adjustments:		
	Change in inventories	(4,334)	(4,864)
	Change in trade and other receivables	(29,319)	(13,261)
	Change in trade and other payables and provisions	2,735	9,793
	Cash flows from operating activities	**13,016**	**26,314**
	Currency gains and losses	299	3,374
	Interest received	4	120
	Interest paid	(363)	(588)
	Income tax received, net	2,220	4,006
	Net cash flows from operating activities	**15,176**	**33,226**
	Investing activities		
	Purchase of tangible assets	(3,178)	(4,125)
	Investments in intangible assets	(45,792)	(42,915)
	Investments in leasehold deposits	(88)	(458)
	Net cash from investing activities	**(49,058)**	**(47,498)**
	Free cash flow	**(33,882)**	**(14,272)**
	Financing activities		
	Issue of shares	3,033	-
	Repayment of borrowings	(637)	(643)
	Net cash flows from financing activities	**2,396**	**(643)**
	Net decrease in cash and cash equivalents	**(31,486)**	**(14,915)**
	Net foreign exchange difference	2,516	2,606
	Cash and cash equivalents at 1 January	75,921	88,230
	Cash and cash equivalents at 31 December	**46,951**	**75,921**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 CORPORATE INFORMATION

The consolidated financial statements of Napatech A/S and its subsidiaries (collectively, the Group) for the year ended were authorised for issue in accordance with the resolution of the management on 29 March 2017.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

General
The financial statements have been prepared in accordance International Financial Reporting Standards (IFRS), as adopted by the EU and additional requirements in the Danish Financial Statement Act.

The consolidated financial statements are prepared on a historical cost basis, except for derivative financial instruments, which are measured at fair value.

The consolidated financial statements are presented in thousand Danish kroner (DKK'000).

In 2016, the Group has created an equity reserve for capitalized development project costs in order to comply with a new provision in the Danish Financial Statements Act. This provision requires that capitalized amount less applicable amortization is recognised under a separate equity reserve, which cannot be used for distribution of dividend and/or coverage of losses.
If capitalized development project costs are subject to impairment, the corresponding amount must be deducted from the equity reserve for capitalized development project costs. If the impairment is reversed in a subsequent period, the corresponding amount under equity must result in recovery of the equity reserve for capitalized development project costs.

Effect of implementation of new and revised standards
During the financial year, the Group implemented all new IFRS standards, amendments to existing standards and annual improvements that have been approved by the EU for annual periods beginning on 1 January 2016. The standards, amendments and annual improvements to existing standards which are deemed relevant to the Group are enumerated below:

With the exception of the new standards, amendments to standards and basis for conclusions enumerated below, the accounting policies are consistent with those of last year.

The following standards, amendments to existing standards and interpretations have been implemented but have no effect on the company's Annual Report:

- IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation – Amendments to IAS 16 and IAS 38
- IAS 1 Disclosure Initiative – Amendments to IAS 1
- Annual Improvements to IFRSs 2012-14 Cycle

As none of the standards and interpretations impacted recognition and measurement in 2016, they neither impacted profit or loss for the year nor diluted earnings per share.

New and amended standards and interpretations that have not yet become operative
The IASB has issued a number new standards, amendments to existing standards which will become operative for financial statements covering periods beginning on or after 1 January 2017. New and amended standards are expected to be implemented by their effective dates.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Following standards, amendments to existing standards and interpretations are expected to affect Napatech A/S' future annual reports:

- IFRS 9 Financial instruments and amendments to IFRS 9, IFRS 7 and IAS 39
- IFRS 15 Revenue from Contracts with Customers
- IFRS 16 Leases

The analysis of the expected effect of the implementation of the above standards has not yet been completed.

IFRS 15 "Revenue from Contracts with Customers", which replaces the existing revenue standards (IAS 11 and IAS 18) and interpretations, creates a new model for revenue recognition and measurement of revenue from contracts with customers. The standard becomes effective for annual periods beginning on or after 1 January 2018.

The new model is based on a five-step process which must be applied to all contracts with customers in order to identify when and how revenue is to be recognised in the income statement.

Compared to the current practice, the most significant changes in IFRS 15 are:

- Sales transactions must be recognised as revenue in the income statement when control (either at a single point in time or over time) of the goods or services is transferred to the customer (the current concept of "risk and rewards" is replaced by a concept of control).
- New and more detailed guidance on how to identify the components of a transaction in a contract and how to recognise and measure the individual components.
- New and more detailed guidance on the recognition of revenue over time.

Napatech A/S has performed an analysis of the potential impact of the new standard on the Group. Based on analyses of the Group's current product mix and types of contracts, it is Napatech A/S' assessment that the new standard will not affect the recognition and measurement of the Group's sales types which primarily consist of goods for resale and finished goods.
Overall, based on the analyses performed, it is assessed that the effect on recognition and measurement is immaterial based on the current product mix and types of contract.

IFRS 9 Financial instruments: The Group has few derivative financial instruments, but besides these only traditional financial assets and liabilities which mainly relate to trade receivables on which only a few and immaterial losses have incurred in the past and trade payables.
The implementation of the standard which becomes effective for annual periods starting on or after 1 January 2018, is therefore expected to have only limited effect.

IFRS 16 Leases sets out the principles for the recognition, measurement presentation and disclosure of leases and requires lessees to account for all leases, with a few exceptions, under a single on-balance sheet model similar to the accounting for finance leases under IAS 17.
At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.
Lessor accounting under IFRS 16 is substantially unchanged from today's accounting under IAS 17.

The Group has operating leases with minimum lease payments of approx. DKK 14,730 thousand, corresponding to 5.6% of the Group's assets. Based on analyses of the Group's

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

operating lease contracts, it is Napatech A/S' assessment that the new standard will have some effect on the Group's balance and cash flow statement, but only immaterial effect on the consolidated income statement. The standard becomes effective for annual periods starting on or after 1 January 2019.

In addition, the IASB has issued a number of new standards, amendments to existing standards and interpretations which are not relevant to the company and which are therefore not expected to affect its future annual reports.

The consolidated financial statements
The consolidated financial statements comprise the parent company, Napatech A/S, and its subsidiaries. Subsidiaries are fully consolidated from the date of acquisition and/or incorporation, being the date on which the parent company obtains control, until the date when such control ceases. The financial statements of the subsidiary are prepared for the same reporting period as the parent company financial statements, using consistent accounting policies. The consolidated financial statements are prepared as a consolidation of the parent company's and the subsidiaries' financial statements, eliminating all intra-group balances, transactions, unrealised gains and losses and dividends.

Currency translation
Determination of functional currency and recognition of transactions denominated in foreign currencies
For each group entity, a functional currency is determined, and items recognised in the financial statements of the individual entities are measured using that functional currency. The functional currency is the currency used as primary currency for the activities of the reporting entity. Transactions denominated in currencies other than the functional currency are considered transactions denominated in foreign currencies.

On initial recognition, transactions denominated in foreign currencies are translated into the functional currency at the exchange rates at the transaction date. Foreign exchange differences arising between the exchange rates at the transaction date and at the date of payment are recognised in the income statement as financial income or financial expenses.

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rates at the reporting date. Any exchange difference arising on the translation is recognised in the income statement as financial income or financial expenses. Non-monetary assets and liabilities measured in terms of historical cost in a foreign currency are translated using the exchange rates at the date of the initial transaction.

Translation of group entities
On recognition in the consolidated financial statements of foreign entities with a functional currency different from the parent company's presentation currency (DKK), the income statement and the statement of cash flows are translated at the exchange rates at the transaction date, while the statement of financial position items are translated at the exchange rates at the reporting date. Any foreign exchange differences arising on the translation are recognised as other comprehensive income in a separate reserve. On full or partial disposal of a foreign entity, the share of the currency reserve relating to that particular foreign entity is recognised in the income statement.

Revenue
Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on delivery of the

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

goods. Revenue is recognised to the extent that it is probable that future economic benefits will flow to the group and the revenue can be reliably measured.

Revenue is measured at the fair value of the consideration received, excluding rebates and VAT.

Cost of goods sold
Cost of goods sold is incurred to generate the period's revenue. Cost of goods sold comprises costs relating to purchases of products that are to be resold.

Research and development costs
Development costs include costs incurred to develop new products.

Selling and distribution expenses
Selling and distribution expenses include costs related to the distribution of goods sold, sales campaigns, wages to sales and distribution staff, cars, advertising and exhibitions.

Administrative expenses
Administrative expenses comprise expenses relating to management and administration of the Group, including expenses related to administrative staff, offices and office expenses.

Finance income and cost
Finance income and costs comprise realised interest income and expenses, unrealised gains and losses on financial assets and liabilities in foreign currencies and realised gains and losses on fair value adjustments of derivative financial instruments.

For all financial instruments measured at amortised cost, interest income and expenses are recognised using the effective interest rate method. Financial income and expenses also comprise realised and unrealised exchange gains and losses on foreign currency transactions.

Tax for the year
Tax for the year, which comprises the current tax charge for the year and changes in the deferred tax charge, including changes arising from changes in the tax rate, is recognised in the income statement as regards the portion that relates to the profit or loss for the year and in other comprehensive income as regards the portion that relates to entries in other comprehensive income. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, by the reporting date, in the countries where the group operates and generates taxable income.

Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subjects to interpretation and establishes provisions where appropriate.

Share-based payments
The Group's employees and management receive consideration in the form of share-based payments. The share-based consideration is an equity-settled programme under which employees and management deliver services in return for share options. The share options are measured at fair value at the time of granting. The fair value of share options is determined using the Black-Scholes option pricing model.

Costs relating to equity-settled share-based payments are recognised in the income statement under administrative expenses and in equity over the vesting period. The total expense recognised for equity-settled share-based payments at the reporting date reflects the share of

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

the vesting period that has lapsed and management's best estimate of the number of equity instruments that will ultimately vest.

Where the terms for equity-settled programmes change, the minimum expense is the expense that would have been recognised had the terms not been changed, provided that the employee's or management's right had vested. In addition, an expense is recognised corresponding to the increase in the fair value of the share-based payment at the time at which the terms are changed.

Derivative financial instruments
The Group enters into forward exchange contracts to hedge the future value of its cash flows. Upon initiation of contracts, the Group classifies each contract that qualifies for hedge accounting as a hedge for a specific hedged financial transaction or firm commitment.

On initial recognition, all forward exchange contracts are measured at cost and subsequently re-measured at their fair value at the balance sheet date. The value adjustments on forward contracts designated as hedges are recognised directly in equity, given the hedge effectiveness. The value adjustments on those forward contracts that do not meet the requirements of IAS 39 for hedge accounting are recognised in the income statement under financial income/expenses.

Intangible assets
Intangible assets are initially recognised in the statement of financial position at cost. Subsequent to initial recognition, intangible assets are carried at cost less accumulated amortisation and impairment losses.

Intangible assets comprise development projects, patents and other intangible assets with finite useful lives.

Intangible assets with finite useful lives are amortised over their economic lives and tested for impairment whenever there is an indication that an asset might be impaired. Useful lives are reassessed on an annual basis. Changes in expected useful lives are accounted for as changes in accounting estimates. Amortisation and impairment losses are recognised in the income statement.

Gains and losses on disposal of intangible assets are determined by comparing the proceeds from disposal with the carrying amount of the asset and are recognised in the income statement.

Development projects
Research costs are recognised in the income statement as incurred. Development costs incurred for individual projects are recognised as an intangible asset when the Group can demonstrate the following:

- The technical feasibility of completing the development project so that it will be available for use or sale;
- The intention to complete the development project and the group's ability to use or sell it;
- The probability that the development project will generate future economic benefits;
- The availability of adequate technical, financial and other resources to complete the development project and to use or sell it; and
- The ability to measure the costs reliably.

Subsequent to initial recognition of the development costs as an intangible asset, the development project is recognised at cost less any accumulated amortisation and impairment losses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Amortisation of the intangible asset begins when the development of the asset has been completed and the asset is used as planned. The expected useful life of development projects is 3 - 5 years.

Patents

Patents are recognised as intangible assets at the time of acquisition. Patents are amortised over their useful lives, starting at the time when the patent takes effect. The useful life of patents is estimated at 10 years.

Tangible assets

Tangible assets include plant and equipment and leasehold improvements.
Items of tangible assets are measured at cost less accumulated depreciation and impairment losses, the cost being the acquisition price and costs directly related to the acquisition until such time when the asset is ready for use.

Depreciation is provided on a straight-line basis over the expected useful lives of the assets, as follows:

Plant and equipment	3 years
Leasehold improvements	5 years

Gains and losses on disposal of tangible assets are determined by comparing the proceeds from disposal with the carrying amount of the asset and are recognised in the income statement.

Residual values and useful lives are reassessed on an annual basis. Changes in useful lives or residual values are accounted for as changes in accounting estimates.

Leases

Leases are divided into finance leases and operating leases. A finance lease is a lease that in all essential respects transfers the risk and benefits associated with owning the leased asset to the lessee. Other leases are designated as operating leases.

Assets held under finance leases are measured at the lower of the fair value of the assets and the net present value of future minimum lease payments. For purposes of calculating the net present value, the internal rate of return is used as discount factor or an approximate value thereof. Financial liabilities include the capitalised residual obligation on finance leases, measured at amortised cost.

Lease payments concerning operating leases are recognised on a straight-line basis over the term of the lease.

Impairment of non-financial assets

In-progress development projects are tested for impairment once a year. Other long-term assets with finite useful lives are reviewed for impairment at each reporting date. Where indications of impairment are identified for in-progress development projects or other long-term assets with finite useful lives, the Group estimates the recoverable amount of the asset. The recoverable amount is determined for the individual asset or a group of assets constituting an integrated cash-generating unit. The recoverable amount is the higher of the asset or the cash-generating unit’s fair value less costs to sell and its value in use. Where the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount, the asset is considered impaired and the

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

carrying amount is reduced to the recoverable amount. The impairment loss is recognised in the income statement.

The value in use is calculated as the present value of expected future cash flows from the asset or the cash-generating unit of which the asset is a part. For purposes of determining the fair value less costs to sell, an appropriate valuation model is used.

Receivables
Receivables are measured at amortised cost less impairment losses. Where receivables are found to be impaired, their carrying amount is reduced to the estimated net realisable value.

Impairment losses are recognised in the income statement under administrative expenses.

Inventories
Inventories are measured at the lower of cost and net realisable value. The cost is determined using the first-in/first-out (FIFO) method.

The cost of goods for resale, raw materials and consumables comprises the purchase price plus delivery costs. The Group uses sub-suppliers for the primary production of goods for resale.

The net realisable value of inventories is determined as the selling price less costs of completion and costs incurred to generate the revenue, taking into account marketability, obsolescence and developments in the expected selling price.

Equity
Share premium
Share premium is the value in excess of the nominal value of the shares that is contributed to the company upon formation or a capital increase. The share premium is part of the distributable reserves.

Share-based payment reserve
The value of share options granted is recognised in equity under share based payment reserve over the vesting period as the employees deliver the relevant services. The reserve reflects the total value of share options granted based on the share of the vesting period that has lapsed and the group's best estimate of the number of equity instruments that will ultimately vest.
The reserve is part of the distributable reserves.

Foreign currency translation reserve
The foreign currency translation reserve comprises exchange differences arising upon translation of the financial statements of foreign operations from their functional currency to the parent company's presentation currency (DKK).

Upon full or partial realisation of the investment in the foreign operation, foreign exchange adjustments are recognised in the income statement in the same item as the gain/loss from the sale. The reserve is part of the distributable reserves.

Financial liabilities
Amounts owed to banks etc. are recognised at the date of borrowing at the amount of proceeds received net of transaction costs paid. In subsequent periods, the financial liabilities are measured at amortised cost using the effective interest method. Accordingly, the difference between the proceeds and the nominal value is recognised in financial expenses over the term of the loan.

Non-financial liabilities are measured at net realisable value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Provisions
Provisions include warranty commitments and are recognised when the group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are discounted to net present value where this has a significant effect on the measurement of the liability.

Income tax and deferred tax
Current tax liabilities and current tax receivable are recognised in the statement of financial position as the estimated tax charge for the period, adjusted for tax on previous years' taxable income and tax paid on account.

Deferred tax is measured, using the "balance sheet liability" method, of all temporary differences at the reporting date between the tax base and the carrying amount of assets and liabilities.

Deferred tax is recognised for all taxable temporary differences, except for taxable temporary differences associated with investments in subsidiaries where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences and all unutilised tax loss carry forward to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the unutilised tax loss carry forward can be used.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Unrecognised deferred tax assets are reviewed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will be available against which the deferred tax asset can be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantially enacted at the balance sheet date.

Deferred tax items are recognised in correlation to the underlying transaction either in other comprehensive income or directly in equity.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Statement of cash flows
The statement cash flows shows the Group's cash flows for the year, broken down into operating, investing and financing activities, the period's changes in cash and cash equivalents and the Group's cash and cash equivalents at the beginning and the end of the period.

Cash flows from operating activities are presented using the indirect method and are stated as the profit or loss for the year, adjusted for non-cash operating items, changes in working capital, paid and/or received interests and paid and/or received income taxes.

Cash flows from investing activities comprise payments related to purchases and/or proceeds of/from non-current assets.

Cash flows from financing activities comprise dividend distributed to shareholders, capital increases and/or reductions, repayments and/or proceeds of/from interest-bearing debt.

Cash and cash equivalents at end of reporting period include cash less bank overdrafts.

Segment information
The segment information is provided on geographical markets as the Group has only one business segment. The segmentation is based on the Group's internal financial reporting. The segment information has been prepared in accordance with the Group's accounting policies.

Income/expenses in the segments comprise the items directly attributable to the individual segments as well as the items that may be allocated to the individual segments on a reliable basis. As a measure of segment profit or loss, the Group uses gross profit.

NOTE 3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the consolidated financial statements requires the managements to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities. Below are presented significant accounting judgements, estimates and assumptions.

Accounting estimates and uncertainty of estimates
The valuation of certain assets and liabilities requires the management to make estimates and assumptions related to future events. The estimates and assumptions are based on historical experience and other factors that, according to the management's assessment, are reasonable, but also inherently subject to uncertainty and unpredictability. The assumptions may be incomplete and inaccurate, and unexpected events and/or circumstances may arise.

Furthermore, the Group is subject to risks and uncertainties that may cause the actual results to differ from these estimates, both positively and negatively. The Group's specific risks are discussed in the relevant sections of the management's review and in the notes to the consolidated financial statements.

The major assumptions concerning future events and other sources of estimation of uncertainties at the reporting date, which involve significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year, are presented below.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (CONTINUED)

Development projects
There is an ongoing assessment whether the development costs meet the criteria for capitaliation as set out in the summary of accounting policies, Note 2, whether the development projects will generate future economic benefits.

Development projects in progress are annually tested for impairment. Completed development projects are reviewed for impairment indicators. If there is evidance of impairment, an impairment test is carried out for the project concerned. The impairment test is prepared on the basis of factors such as the future use of the project, the present value of expected future income, interest and risk. The carrying amount of completed development projects is DKK 75,689 thousand at 31 December 2016 (31 December 2015: DKK 70,087 thousand).

The accounting judgements, estimates and assumptions that the management makes for development projects are consistent with previous years.

Judgements in relation to significant accounting policies
In applying the Group's accounting policies, the management makes judgements that may have a material impact on the values recognised in the consolidated financial statements.

When defining the Group's significant accounting policies, the management made the following judgements that have a significant impact of the values recognised in the consolidated financial statements:

Share-based payments
In February 2013, after the share options of the Group's employees and management had vested, but prior to the exercise date, the management made modifications to some of the share option agreeements concluded with employees and management. The managements treats the change of terms as modifications to the existing share option agreements. Accordingly, the fair value determined at the original grant date has been charged to the income statement over the original vesting period. In addition, an expense is recognised over the new vesting period, corresponding to the increase in the fair value of the share-based payments as a result of change of terms.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 OPERATING SEGMENTS

The following tables present revenue and gross profit information about the Group's operating segments for the years ended 31 December 2016 and 2015, respectively:

Year ended 31 December 2016:

DKK'000	EMEA	NAM	APAC	LAM	Consolidated
Revenue					
Total revenue	192,148	175,156	11,039	-	378,343
Inter-segment	(143,606)	-	-	-	(143,606)
Revenue, external customers	**48,542**	**175,156**	**11,039**	**-**	**234,737**
Cost of goods sold	(12,244)	(56,073)	(2,812)	-	(71,129)
Segment gross profit	**36,298**	**119,083**	**8,227**	**-**	**163,608**

Year ended 31 December 2015:

DKK'000	EMEA	NAM	APAC	LAM	Consolidated
Revenue					
Total revenue	174,977	177,408	10,867	68	363,320
Inter-segment	(146,643)	-	-	-	(146,643)
Revenue, external customers	**28,334**	**177,408**	**10,867**	**68**	**216,677**
Cost of goods sold	(7,377)	(52,173)	(2,401)	(25)	(61,976)
Segment gross profit	**20,957**	**125,235**	**8,466**	**43**	**154,701**

Explanation of abreviatons:
EMEA = Europe, Middle East and Africa
NAM = North America
APAC = Asia and Pacific
LAM = Latin America

Inter-segment revenues are eliminated upon consolidation and are reflected in the "Inter-segment" row.

Adjustments and eliminations
Research and development costs, selling and distribution expenses, administrative expenses, finance income and costs are not allocated to individual segments as they are managed on a group basis. Current taxes and deferred taxes are not allocated to individual segments as they are also managed on a group basis.

Transactions with major customers
Revenue from first significant customer amounted to DKK 42,967 thousand (2015: DKK 8,223 thousand) corresponding to 18% (2015: 4%) of the Group revenue. Revenue from this customer is arising from the sales in the NAM segment.

Revenue from second significant customer amounted to DKK 29,757 thousand (2015: DKK 33,913 thousand) corresponding to 13% (2015: 16%) of the Group revenue. Revenue from this customer is arising from the sales in the NAM segment.

Revenue from third significant customer amounted to DKK 14,793 thousand (2015: DKK 56,876 thousand) corresponding to 6% (2015: 26%) of the Group revenue. Revenue from this customer also arises from sales in the NAM segment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 EMPLOYEE BENEFITS EXPENSE

DKK'000	2016	2015
Employee benefits expense is reported as follows:		
Wages and salaries	92,212	99,376
Defined contribution schemes	10,954	10,850
Share-based payment expense (Note 7)	476	414
Social security costs	2,826	2,831
Allocated to development projects	(34,095)	(35,265)
Total employee benefits expense	**72,373**	**78,206**

DKK'000	2016	2015
Employee benefits expense is recognised in the consolidated income statement as follows:		
Research and development costs	9,966	12,577
Selling and distribution expenses	47,768	51,063
Administrative expenses	14,639	14,566
Total employee benefits expense	**72,373**	**78,206**
Average number of employees	**107**	**108**

Compensation of key management personnel of the Group is as follows:

	2016		2015	
DKK'000	Manage-ment	Board of Directors	Manage-ment	Board of Directors
Short-term staff benefits	8,270	792	10,551	825
Defined contribution schemes	566	-	487	-
Share-based payment expense	230	-	230	-
Total compensation of key management personnel	**9,066**	**792**	**11,268**	**825**

Of the total compensation to the Management the CEO received DKK 2.3 million (2015: DKK 2.9 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 RESEARCH AND DEVELOPMENT COSTS

Research and development costs including annual amortisation charge on completed development projects recognised in the consolidated income statement are DKK 44,211 thousand (2015: DKK 36,950 thousand). All research and development costs are incurred by the parent company.

NOTE 7 SHARE-BASED PAYMENTS

Employees and members of the management in both the parent company and the US-based subsidiary are eligable for share option schemes. They are granted a certain number of share options in the parent company in return for the services they provide to the Group.

Share options under these schemes are granted at fixed exercise prices. The right to share options can only be vested as long as the holder still is an employee of the Group.

In February 2013, after the share options of the Group's employees and management had vested but prior to the exercise date, the management made modifications to some of the share-based payment agreements with employees and management.

The management treats the change of terms as modifications to the existing share-based payment arrangements. Accordingly, the fair value determined at the original grant date has been charged to the income statement over the original vesting period.

In addition, an expense is recognised over the new vesting period, corresponding to the increase in the fair value of the share-based payment as a result of the change of terms. All granted share options are equity-based.

The share based payment expense is measured at fair value at the grant date using Black-Scholes model. The expense is recognised in the income statement with the counter item in the other reserves under the equity, and it is recognised over: (a) the period during share option holder has met the vesting conditions; or (b) the period in which an exercising event is likely to occur if this period is shorter.

In December 2013 the initial public offering (IPO) on the Oslo Stock Exchange (OSE) resulted in an exercising event in relation to all share option programmes. Therefore, the remaining vesting period of the share options has been accelerated.

The general terms for share options are summarised as follows:

Earliest exercise date	1 year from grant date
Latest exercise date	9 - 10 years from grant date

In may 2014 the Board of Directors decided to issue share options to key employees in the Group. A total of 101,000 share options have been issed for subscription of 101,000 shares of a nominal value of DKK 1 at an exercise price of NOK 48.70 (DKK 43.00 at 1 July 2014). The share options' life time is 5 years. The first 2 years from the date of issue is a lock-up period during which the share options may not be exercised. The exercise of these share options may take place in the 3rd, 4th and 5th year and they vest with 1/3 in each of these 3 years.

The general terms for the 2014 share options programme are summarised as follows:

Earliest exercise date	2 years from grant date
Latest exercise date	5 years from grant date

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 SHARE-BASED PAYMENTS (CONTINUED)

In February 2016 the Board of Directors decided to issue share options to key employees in the Group. A total of 23,000 share options have been issed for subscription of 23,000 shares of a nominal value of DKK 1 at an exercise price of NOK 63.50 (DKK 53.10 at 22 February 2016). The share options' life time is 5 years. The first 2 years from the date of issue is a lock-up period during which the share options may not be exercised. The exercise of these share options may take place in the 3rd, 4th and 5th year and they vest with 1/3 in each of these 3 years.

In accordance with the decision made on the Annual General Meeting held on 20 April 2016, Napatech conducted a split of shares in the ratio of 1:4. This means that the nominal value of each share has been reduced from DKK 1.00 to DKK 0.25, whereby each shareholder previously holding one share with the nominal value of DKK 1.00 received four new shares with the nominal value of DKK 0.25.

The 1:4 share split has no direct impact on the value of share options and share option programs. When share options are exercised, the share capital will be increased by the same nominal amount at the same exercise price per share of DKK 1.00 nominal (multiples of four shares at nominally DKK 0.25). Consequently, the number and value of share options increases/decreases with the same ratio of 1:4. The principals of the 1:4 share spli have been applied on comparative figures in order to enable comparison and consistency with previous periods.

Based on the decision made on General Assembly in April 2016 to issue 400,000 share options, the Board of Directors issued 145,000 share options in August 2016 with the nominal value of DKK 0.25 at an exercise price of NOK 22.00 (DKK 18.04). The share options' life time is 5 years, where the share options holders are subject to a lock-up periode in the first 2 years of the share options' life time. The share options vest with 1/3 in each of the remaining 3 years of the share options' life time.

The general terms for both 2016 share options programmes are summarised as follows:

Earliest exercise date	2 years from grant date
Latest exercise date	5 years from grant date

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 SHARE-BASED PAYMENTS (CONTINUED)

	2016					
	Executive Management		Other Employees		Total	
Share options	Number	Avg. ex. price	Number	Avg. ex. price	Number	Avg. ex. price
At 1 January 2016	1,032,848	8.60	620,780	8.80	1,653,628	8.67
Granted during the year	46,000	9.04	191,000	18.04	237,000	9.80
Transfer	(178,000)	8.00	178,000	8.00	-	-
Excercised/expired during the year	(186,300)	8.00	(289,344)	8.00	(475,644)	8.00
At 31 December 2016	**714,548**	**8.41**	**700,436**	**10.71**	**1,414,984**	**8.82**
Exercisable at 31 December 2016	**542,588**	**8.32**	**389,433**	**8.40**	**932,021**	**8.35**

	2015					
	Executive Management		Other Employees		Total	
Share options	Number	Avg. ex. price	Number	Avg. ex. price	Number	Avg. ex. price
At 1 January 2015	1,267,148	8.49	724,820	8.68	1,991,968	8.56
Granted during the year	-	-	-	-	-	-
Excercised/expired during the year	(234,300)	8.00	(104,040)	8.00	(338,340)	8.00
At 31 December 2015	**1,032,848**	**8.60**	**620,780**	**8.80**	**1,653,628**	**8.67**
Exercisable at 31 December 2015	**808,848**	**8.00**	**440,780**	**8.00**	**1,249,628**	**8.00**

In 2016, 386,568 share options were exercised and 89,076 lapsed (2015: nil exercised and 338,340 lapsed).
The following shows the exercise price of the outstanding share options and warrants:

	2016	2015
Number of share options at 31 December:		
Exercise price DKK 8.00	812,648	1,249,628
Exercise price DKK 10.75	365,336	404,000
Exercise price DKK 12.53	92,000	-
Exercise price DKK 18.04	145,000	-
Total number of outstanding share options	**1,414,984**	**1,653,628**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 SHARE-BASED PAYMENTS (CONTINUED)

The weighted average of the remaining contractual period of the outstanding share options from the 2013 share options programme at 31 December 2016 is 6 months (at 31 December 2015: 1 year and 6 months). The weighted average of the remaining contractual period of the outstanding share options from the 2014 share options programme at 31 December 2016 is 2 years and 6 months (at 31 December 2014: 3 years and 6 months). The weighted average of the remaining contractual period of the outstanding share options from the 2016 share options programmes at 31 December 2016 is 5 years and 3 months.

Assumptions for the calculation of the fair value of share options and warrants
The fair value of share options and warrants granted during 2013, 2014 and 2016 was estimated on the date of grant using the following assumptions:

	December 2013	May 2014	February 2016	August 2016
Volatility	47.92%	43.53% - 44.94%	49.00%	49.00%
Risk-free interest rate	1.65%	1.70% - 2.00%	0.50% - 0.60%	0.53% - 0.64%
Exercise price (DKK)	8.00	10.75	12.53	18.04
Exercise period (years)	2.27	3.00-5.00	3.00-5.00	3.00-5.00
Number of options	520,700	404,000	92,000	145,000

The volatility is calculated based on a peer group of 7 similar companies listed on Nasdaq Stock Exchange in the USA. The fair value of the share options is determined using the Black-Scholes option pricing model.

For 2016, the Group has recognised DKK 475 thousand of share-based payment expense in the income statement (2015: DKK 414 thousand). DKK 261 thousand was recognised in relation the Executive Management (2015: DKK 230 thousand) and DKK 214 thousand in relation to others (2015: DKK 184).

NOTE 8 AUDITORS' FEES

DKK'000	2016	2015
Ernst & Young:		
Statutory audit fee	266	273
Tax advisory fee	49	21
Fees for other services	125	127
Total auditors' fees	**440**	**421**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9 DEPRECIATION, AMORTISATION AND IMPAIRMENT

DKK'000	2016	2015
Depreciation, amortisation and impairment are reported as follows:		
Depreciation of plant and equipment	4,740	5,403
Depreciation of leasehold improvements	578	514
Total depreciation of tangible assets	**5,318**	**5,917**
Amortisation of patents	611	331
Impairment of patents	1,769	-
Amortisation of completed development projects	29,047	21,856
Amortisation of other intangible assets	713	663
Total amortisation and impairment of intangible assets	**32,140**	**22,850**
Total depreciation, amortisation and impairtment	**37,458**	**28,767**

NOTE 10 FINANCE INCOME

DKK'000	2016	2015
Interest receivable from banks	4	120
Foreign exchange gains	299	6,002
Total finance income	**303**	**6,122**

NOTE 11 FINANCE COSTS

DKK'000	2016	2015
Interest payable to banks	332	523
Finance charges payable under finance leases	19	44
Other finance costs	12	21
Total finance costs	**363**	**588**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12 INCOME TAX

DKK'000	2016	2015
Current tax recognised in the consolidated income statement:		
Current income tax	1,043	1,247
Current income tax carry back refund	(2,123)	(7,705)
Change in deferred tax	3,298	9,744
Total income tax	**2,218**	**3,286**

A reconciliation between tax expense and profit before tax multiplied by the applicable income tax rate for the Group for 2016 and 2015 is as follows:

DKK'000	2016	2015
Profit before tax	5,941	10,999
At the applicable Danish income tax rate for the Group, 22.0% (2015: 23.5%)	1,307	2,585
Tax effect of:		
Carry back refunded at 23.5% (2015: 25.0%)	113	(354)
Tax-deductable expenses	(37)	(237)
Non-deductible expenses	172	1,106
Effect of higher tax rates in the US and Japan	661	186
Other	2	-
At the effective income tax rate of 37% (2015: 30%)	**2,218**	**3,286**

NOTE 13 EARNINGS PER SHARE

DKK'000	2016	2015
Net profit attributable to equity holders of the parent company for basic earnings and the effect of dilution	**3,723**	**7,713**

	2016	2015
	Thousands	Thousands
Weighted average number of shares for basic earnings per share	23,520	23,288
Effect of dilution:		
Share options	594	4
Weighted average number of shares adjusted for the effect of dilution	**24,114**	**23,292**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 13 EARNINGS PER SHARE (CONTINUED)

In accordance with the decision made on the Annual General Meeting held on 20 April 2016, Napatech conducted a split of shares in the ratio of 1:4. The nominal value of each share has been reduced from DKK 1.00 to DKK 0.25, whereby each shareholder holding one share with the nominal value of DKK 1.00 received four new shares with the nominal value of DKK 0.25. The same principal has been applied on comparative figures from 2015 to enable comparison and consistency of EPS with previous periods.

NOTE 14 INTANGIBLE ASSETS

	Development projects, completed		Development projects, in progress		Patents		Other intangible assets		Total	
DKK'000	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
Cost at 1 January	170,480	132,872	12,439	8,687	8,185	6,795	2,139	1,974	193,243	150,328
Additions in the year	-	-	44,698	41,360	1,094	1,390	-	165	45,792	42,915
Transfers in the year	34,649	37,608	(34,649)	(37,608)	-	-	-	-	-	-
Cost at 31 December	**205,129**	**170,480**	**22,488**	**12,439**	**9,279**	**8,185**	**2,139**	**2,139**	**239,035**	**193,243**
Accumulated amortisation at 1 January	100,393	78,537	-	-	520	189	937	274	101,850	79,000
Amortisation for the year	29,047	21,856	-	-	611	331	713	663	30,371	22,850
Impairment for the year	-	-	-	-	1,769	-	-	-	1,769	-
Accumulated amortisation and impairment at 31 December	**129,440**	**100,393**	**-**	**-**	**2,900**	**520**	**1,650**	**937**	**133,990**	**101,850**
Carrying amount at 31 December	**75,689**	**70,087**	**22,488**	**12,439**	**6,379**	**7,665**	**489**	**1,202**	**105,045**	**91,393**

Within the completed development projects there are two material development projects with carrying amount of DKK 9,836 thousand and DKK 11,017 thousand at 31 December 2016 respectively (31 December 2015: nil and DKK 14,607 thousand respectively). The aim of the first project was to develop new 2 x 100G accelerator and the aim of the second project was to develop new 1 x 100G accelerator. The remaining amortisation periods of these two projects are 4 years and 11 months and 3 years respectively.

Within the in progress development projects there is one material development project with carrying amount of DKK 9,320 thousand. The aim of the project is to develop next generation of our network recording platform. The project is not yet completed and therefore has not been amortised.

At 31 December 2016, the Group tested the intangible assets for impairment. In relation to this, the Group identified patents on markets that are not expected to be utilised. Therefore, the Group recognised DKK 1,769 thousand as an impairment in respect of patents. There were no indications of impairment in respect of the Group's development projects and other intangible assets in the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15 TANGIBLE ASSETS

	Plant and equipment		Leasehold improvements		Total	
DKK'000	2016	2015	2016	2015	2016	2015
Cost at 1 January	32,224	28,111	3,970	3,844	36,194	31,955
Additions	2,488	4,068	690	104	3,178	4,172
Disposals in the period	(135)	(106)	(47)	-	(182)	(106)
Currency adjustment	45	151	17	22	62	173
Cost at 31 December	**34,622**	**32,224**	**4,630**	**3,970**	**39,252**	**36,194**
Accumulated depreciation at 1 January	24,789	19,341	2,921	2,388	27,710	21,729
Depreciation for the year	4,740	5,403	578	514	5,318	5,917
Disposals in the period	(135)	(59)	(47)	-	(182)	(59)
Currency adjustment	42	104	5	19	47	123
Accumulated depreciation at 31 December	**29,436**	**24,789**	**3,457**	**2,921**	**32,893**	**27,710**
Carrying amount at 31 December	**5,186**	**7,435**	**1,173**	**1,049**	**6,359**	**8,484**

The carrying amount of tangible assets held under finance leases is nil at 31 December 2016 (31 December 2015: DKK 328 thousand).
At 31 December 2016, the Group tested the tangible assets for impairment.
There were no indications of impairment of the Group's tangible assets in the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 DEFERRED TAX

	Consolidated statement of financial position		Consolidated income statement	
DKK'000	2016	2015	2016	2015
Tax losses carry-forwards	(11,361)	(11,361)	-	3,072
Intangible assets	21,830	18,777	3,053	4,581
Tangible assets	(1,863)	(1,987)	124	1,717
Provision for bad debts	(179)	(247)	68	137
Deferred tax liability and expense	**8,427**	**5,182**	**3,245**	**9,507**

DKK'000	2016	2015
Reconciliation of deferred tax libility / (asset) is as follows:		
Opening balance at 1 January	5,182	(4,325)
Recognised in consolidated income statement	3,298	9,744
Recognised in consolidated statement of comprehensive income	(53)	(237)
Closing balance at 31 December	**8,427**	**5,182**

NOTE 17 INVENTORIES

DKK'000	2016	2015
Consumables and components	1,259	5,364
Finished goods and goods for resale	17,416	8,977
Total inventories	**18,675**	**14,341**
Carrying value of inventories recognised at fair value	-	-

The cost of goods sold for the year is DKK 71,129 thousand (2015: DKK 61,976 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 TRADE AND OTHER RECEIVABLES

DKK'000	2016	2015
Receivables recognised in the consolidated statement of financial position:		
Trade receivables	75,119	48,254
Other receivables	4,844	4,484
Total current receivables	**79,963**	**52,738**

Movements in the provision for bad debts on trade receivables are as follows:

DKK'000	2016	2015
At 1 January	1,815	2,002
Reversed in the year	(480)	-
Written off in the year	-	(858)
Change in the year	768	671
At 31 December	**2,103**	**1,815**

Ageing analysis of past due but not impaired trade receivables is as follows:

DKK'000	2016	2015
Not past due	70,541	42,728
Past due for less than 30 days	1,373	1,912
Past due between 30 and 60 days	962	57
Past due between 60 and 90 days	152	266
Past due after 90 days	2,091	3,291
Total maximum credit risk	**75,119**	**48,254**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 19 INCOME TAX RECEIVABLE

DKK'000	2016	2015
At 1 January	2,451	-
Income tax carry back refund	2,094	7,705
Income tax carry back refund received during the year	(2,451)	(5,254)
At 31 December	**2,094**	**2,451**

NOTE 20 ISSUED CAPITAL AND RESERVES

In accordance with the decision made on the Annual General Meeting held on 20 April 2016, Napatech conducted a split of shares in the ratio of 1:4. The nominal value of each share has been reduced from DKK 1.00 to DKK 0.25, whereby each shareholder holding one share with the nominal value of DKK 1.00 received four new shares with the nominal value of DKK 0.25. The same principal has been applied on comparative figures from 2015 to enable comparison and consistency with previous periods.

	2016	2015
Authorised shares	Thousands	Thousands
Ordniary shares of DKK 0.25 each at 1 january	23,288	23,288
Increase in ordinary shares DKK 0.25 each	376	-
Ordiniary shares of DKK 0.25 each at 31 December	**23,664**	**23,288**

	2016	2016
Ordinary shares and fully paid	Thousands	DKK'000
At 1 January 2016	23,288	5,822
Exercise of share options for cash during the year	376	94
At 31 December 2016	**23,664**	**5,916**

DKK'000	2016	2015
Share premium		
At 1 January	210,675	210,675
Exercise of share options for cash in excess of cost of ordinary shares during the year	2,939	-
Reversals regarding exercised share options	2,815	-
At 31 December	**216,429**	**210,675**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 20 ISSUED CAPITAL AND RESERVES (CONTINUED)

Share-based payment reserve
Share-based payment reserve is issued to recognise the value of equity-settled share-based payments provided to employees, including key management personnel, as part of their remuneration. Refer to Note 7 for further details on this plan.

Movements in other capital reserves are as follows:

DKK'000	2016	2015
At 1 January	9,981	12,101
Share-based payment expense (Note 7)	475	414
Reversals regarding exercised and lapsed share options	(2,845)	(2,534)
At 31 December	**7,611**	**9,981**

NOTE 21 FINANCIAL ASSETS AND FINANCIAL LIABILITIES

DKK'000	2016	2015
Financial assets measured at amortised cost:		
Leasehold deposits	2,312	2,224
Trade receivables	75,119	48,254
Other receivables	4,844	4,484
Cash and cash equivalents	46,951	75,921
Total financial assets	**129,226**	**130,883**
Financial liabilities measured at amortised cost:		
Finance lease liability	-	637
Interest-bearing loans and borrowings	5,000	5,000
Trade payables	25,978	18,645
Derivatives designed as hedging instruments:		
Foreign exchange forward contracts	1,314	1,008
Total financial liabilities	**32,292**	**25,290**

Carrying amounts of financial assets and financial liabilities approximate their fair value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 22 DERIVATIVE FINANCIAL INSTRUMENTS

At 31 December 2016, the Group held forward exchange contracts to hedge part of the future budgeted sales covering a period of 12 months that is not naturally hedged by the costs denominated in USD.

The terms of the outstanding contracts at 31 December were as follows:

2016	Latest maturity date	Average exchange rate DKK/USD	Fair value	Unrealised gain/(loss)
			DKK'000	DKK'000
Forward exchange contracts to hedge expected future sales and costs USD 3,942 thousand	17/01/17	671.49	(1,314)	(1,314)

2015	Latest maturity date	Average exchange rate DKK/USD	Fair value	Unrealised gain/(loss)
			DKK'000	DKK'000
Forward exchange contracts to hedge expected future sales and costs USD 2,972 thousand	15/01/16	648.78	(1,008)	(1,008)

In the year ended 31 December 2016 the Group realised gain from the expiry of forward contracts held during the totalled DKK 1,048 thousand (2015: loss DKK 2,594 thousand).

Fair value hierarchy
The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation techniques:

Level 1: Quoted (unadjusted) prices in active markets for identical assets or liabilities.

Level 2: Other techniques for which all inputs which have significant effect on the revorded fair value are observable, either directly or indirectly.

Level 3: Techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

At 31 December 2016, the Group held solely derivative financial instruments that were measured at fair value using Level 2 valuation techniques. The Group enters into derivative financial contracts with various counterparties composed of financial institutions. The derivative financial instruments are measured using valuation techiques with market observable inputs. The most frequently applied techniques for valuation of forward contracts and interest swap contracts are present value calculations based on foreign exchange spot rates and interest rate curves among others. Fair values are based on fair value reports from financial institutions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 23 PROVISIONS

Provisions relate to guarantees associated with the sale of network adapters.
The movement in provisions is as follows:

DKK'000	2016	2015
At 1 January	315	309
Utilised during the year	(315)	(309)
Additions in the year	369	315
At 31 December	**369**	**315**

The provisions for guarantees are expected to be utilised within one year and are therefore classfied as current liabilities.

NOTE 24 COMMITMENTS AND CONTINGENCIES

Collaterals
The Group has issued a floating charge in the amount of DKK 10 million (2015: DKK 10 million) secured on receivables, inventories and tangible assets with carrying amount of DKK 36,794 thousand (2015: DKK 31,235 thousand) as collateral for bank debt.

Operating lease commitments
The Group's operating lease commitments relate to leasing of operating equipment, cars and office facilities. Future minimum payments under operating leases at 31 December are as follows:

		2016	
DKK'000	Cars	Office facilities	Total
Falling due within one year	71	7,464	7,535
Falling due between one and five years	-	7,195	7,195
Total	**71**	**14,659**	**14,730**

		2015	
DKK'000	Cars	Office facilities	Total
Falling due within one year	106	5,644	5,750
Falling due between one and five years	71	2,551	2,622
Total	**177**	**8,195**	**8,372**

The Group recorded DKK 106 thousand and DKK 5,644 thousand (2015: DKK 155 thousand and DKK 4,964 thousand) as operating lease expenses for cars and office facilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 24 COMMITMENTS AND CONTINGENCIES (CONTINUED)

Finance lease commitments
The Groups' finance lease commitments related to operating equipment used in the research and development department. At 31 December 2016 the Group has repaid all finance lease commitments relating to the operating equiment used in the research and development department.

NOTE 25 RELATED PARTY DISCLOSURES

Terms and conditions of related party transactions
Sales to and purchases from related parties are made on terms equivalent to those that prevail in arm's length transactions. Outstanding balances at the year-end are unsecured and interest-free and settlement occurs in cash. This assessment is undertaken each financial year through by examining the financial position of the related party.

Controlling influence
The Group has no shareholders with controlling influence, as the shareholders include one large venture capital company with significant influence and many small private and corporate shareholders.

Entity with significant influence over the Group
Entity with significant influence over the Group include the venture capital company Verdane Capital VIII. Verdane Capital VIII owns 21.9% (2015: 22.2%). Related parties also include the shareholders' portfolio companies as they are subject to the same significant influence as the Group. The Group had no transacitons with neither the shareholders nor their portfolio companies in 2015 or 2016.

Transactions with key management personnel
Remunerations, salaries and share-based payments to the Board of Directors and the Executive Management are reflected in Note 5. There were no other transactions with the Board of Directors or the Executive Management in 2015 and 2016.

NOTE 26 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial liabilities comprise loans and borrowings, finance lease liabilities, trade and other payables and guarantees for sale of network adapters. The main purpose of these financial liabilities is to finance the Group's operations and to provide guarantees to support its operations. The Group has trade and other receivables, cash and long-term leasehold deposits that derive directly from its operations. The Group does not hold any available-for-sale investments.

The Group is exposed to credit risk, liquidity risk, interest rate risk and foreign currency risk. The Group's senior management provides assurance that financial risks are identified, measured and managed in accordance with the Group's policies and risk objectives. It is the Group's policy not to undertake any trading in derivatives for speculative purposes. The Board of Directors reviews and agrees policies for managing each of these risks, which are summarised below.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 26 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Credit risk
Credit risk is the risk that a counterparty will not meet its obligations under a customer contract, leading to financial loss. The Group is exposed to credit risk from its operating activities, receivables and deposits with banks.

Trade receivables
Customer credit risk is managed at group level. Credit quality of a customer is assessed based on a review of available financial information. The Group's customers have 30 - 90 days as a standard payment term and historically the Group has not had material impairment for bad debts.

In 2016, the Group had 2 customers (2015: 2 customers) that each owed the Group more than 10% of all trade receivables. The credit risk associated with these customers has been assessed as low as they historically meet the Group standard payment terms of 30 - 90 days.

The need for an impairment is analysed each quarter on an individual basis for major customers. Additionally, a number of minor receivables are grouped into homogenous groups and assessed for impairment collectively. The calculation is based on actual incurred historical data.
The maximum exposure to credit risk at the reporting date is the carrying value disclosed in Note 18. The Group does not hold collateral as security. The Group evaluates the concentration of risk with respect to trade receivables as low, as its customers are located in several jurisdictions and operate independently. The customer credit risk related to the geographical segments in which the Group operates is similar and do not differ significantly.

Cash deposits
Credit risk from balances with banks is managed by the senior management in accordance with the Group's policy. Investments of surplus funds are mainly made to finance development projects. Development projects are reviewed by the senior management on a quarterly basis.
The Group's maximum exposure to credit risk for the components of the statement of financial position at 31 December 2016 and 2015 is the carrying amounts as illustrated in Note 21.

Liquidity risk
Liquidity risk is the risk that the Group is unable to repay its financial liabilities as they fall due.

The Group monitors cash flows on a monthly basis and maximum one year in advance.
The aim is to ensure sufficient cash from the operating acitivities to fund project development and the daily operations.

The Group's manufacturing policy is order production in order to ensure minimal amounts of cash being tied up in inventories. Furthermore, the suppliers' terms of payment are between 30 and 60 days, and the Group's customers standard terms of payment between 30 and 90 days.

The Group has access to unused credit facilities in the amount of DKK 17,637 thousand (2015: DKK 17,270 thousand) in a case of need for cash to finance its activities.

In line with previous reporting periods, the Group's policy for liquidity management is to ensure timely payments from customers and to balance suppliers' credit terms with the terms of payment offered to the customers.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 26 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

The Group's cash outflows arising from the financial liabilities recognised in the consolidated statement of financial position are due as follows:

	2016			
DKK'000	Jan - Mar	Apr - Dec	Over 1 year	Total
Finance lease liabilities	-	-	-	-
Interest-bearing loans and borrowings	-	-	5,000	5,000
Trade payables	25,978	-	-	25,978
Derivative financial instruments	1,314	-	-	1,314
Total financial liabilities	**27,292**	**-**	**5,000**	**32,292**

	2015			
DKK'000	Jan - Mar	Apr - Dec	Over 1 year	Total
Finance lease liabilities	80	557	-	637
Interest-bearing loans and borrowings	-	-	5,000	5,000
Trade payables	18,645	-	-	18,645
Derivative financial instruments	1,008	-	-	1,008
Total financial liabilities	**19,733**	**557**	**5,000**	**25,290**

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flow of a financial instrument will fluctuacte because of changes in market interest rates. The Group's exposure to the risk of changes in market interest rates relates mainly to the Group's interest-bearing loan in the amount of DKK 5,000 thousand (2015: DKK 5,000 thousand). This loan yield an interest rate of 3.70%. The Group's policy is to keep sufficient cash in place to mitigate adverse impacts caused by fluctuation in market interest rates. The Group's interest rate risk is immaterial.

Foreign currency risk

The parent company's functional currency is DKK. The Group's revenue and cost of goods sold are mainly denominated in USD. However, the majority of all other transactions are denominated in DKK. The Group's main currency risk is thus associated with fluctuations in USD against DKK. The Group has neglible transactions in other currencies.

Cash flow hedges

Foreign exchange forward contracts measured at fair value through other comprehensive income are designated as hedging instruments to hedge cash flow exposure in USD based on the part of the future budgeted sales in USD that is not naturally hedged by the costs denominated in USD. These forecast transactions are highly probable, and they comprise significant part the Group's net exposure in USD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 26 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Sensitivity analysis of presentation currency
The following demonstrates the sensitivity to a reasonably likely change in the DKK exchange rate, with all other variables held constant. The effect on the Group's profit before tax and equity is due to changes in the fair value of monetary assets and liabilities.

	Effect on profit before tax		Effect on equiy	
DKK'000	2016	2015	2016	2015
Change in DKK by +/- 2%	+/- 1,483	+/- 1,081	+/- 1,483	+/- 1,081

Capital management
Capital includes shares attributable to the equity holders of the parent company.

The primary objective of the Group's capital management is to ensure, in the short term, sufficient capital needed to fund the development of new products and new markets and thereby create healthy business platform to ensure return to the shareholders in the long term.

To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. The Group has not distributed any dividends, and it does not expect to do so in the near future.

The Group monitors capital using a gearing ratio, which is net debt divided by total capital plus debt. The Group's policy is to keep the gearing ratio below 10%. The Group's gearing ratios for 2015 and 2016 are negligable.

NOTE 27 EVENTS AFTER THE REPORTING PERIOD

There have been no significant events after 31 December 2016 that might affect the consolidated financial statements.

PARENT COMPANY INCOME STATEMENT

for the year ended 31 December 2016

Note	In DKK ’000	2016	2015
	Revenue	197,977	183,082
	Cost of goods sold	(70,574)	(62,764)
	Gross profit	**127,403**	**120,318**
2, 3	Research and development costs	(15,164)	(15,094)
2	Selling and distribution expenses	(38,977)	(41,187)
2, 4, 5	Administrative expenses	(29,615)	(34,647)
	Operating profit before depreciation, amortisation and impairment (EBITDA)	**43,647**	**29,390**
6	Depreciation, amortisation and impairment	(37,218)	(28,521)
	Operating profit (EBIT)	**6,429**	**869**
7	Finance income	303	6,016
8	Finance costs	(363)	(401)
	Profit before tax	**6,369**	**6,484**
9	Income tax	(1,175)	(2,039)
	Profit for the year	**5,194**	**4,445**

PARENT COMPANY STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2016

Note	In DKK '000	2016	2015
	Profit for the year	5,194	4,445
	Other comprehensive income to be reclassified to profit and loss in subsequent periods:		
	Value adjustments on hedging instruments:		
	- Net gain / (loss) on cash cash flow hedges	743	(3,840)
	- Net (gain) / loss on cash cash flow hedges reclassified to revenue	(886)	2,594
	- Net (gain) / loss on cash cash flow hedges reclassified to finance costs	(163)	237
	- Income tax effect	53	237
	Net other comprehensive loss to be reclassified to profit or loss in subsequent periods	(253)	(772)
	Total comprehensive income for the year, net of tax	**4,941**	**3,673**

PARENT COMPANY STATEMENT OF FINANCIAL POSITION

at 31 December 2016

Note	In DKK '000	2016	2015
	ASSETS		
	Development projects, completed	75,689	70,087
	Development projects, in progress	22,488	12,439
	Patents	6,379	7,665
	Other intangible assets	489	1,202
10	**Intangible assets**	**105,045**	**91,393**
	Plant and equipment	5,085	7,183
	Leasehold improvements	1,000	1,020
11	**Tangible assets**	**6,085**	**8,203**
12	Investments in subsidiaries	2,197	51
18	Leasehold deposits	2,072	2,012
	Other non-current assets	**4,269**	**2,063**
	Non-current assets	**115,399**	**101,659**
14	Inventories	18,675	13,893
15, 18	Trade receivables	12,034	9,139
15, 18	Receivables from group entities	79,210	61,411
15, 18	Other receivables	4,187	3,796
16	Income tax receivable	2,094	2,451
18	Cash and cash equivalents	23,823	49,249
	Current assets	**140,023**	**139,939**
	Total assets	**255,422**	**241,598**

PARENT COMPANY STATEMENT OF FINANCIAL POSITION

at 31 December 2016

Note	In DKK '000	2016	2015
	EQUITY AND LIABILITIES		
17	Issued capital	5,916	5,822
17	Share premium	216,429	210,675
17	Other capital reserves	39,830	9,209
	Retained earnings	(59,574)	(31,554)
	Equity	**202,601**	**194,152**
13	Deferred tax liability	8,427	5,182
18	Interest-bearing loans and borrowings	5,000	5,000
	Non-current liabilities	**13,427**	**10,182**
18	Interest-bearing loans and borrowings	-	637
18	Trade payables	25,978	18,645
18	Payables to group entities	86	-
18	Other payables	11,647	16,659
19	Derivative financial instruments	1,314	1,008
20	Provisions	369	315
	Current liabilities	**39,394**	**37,264**
	Total liabilities	**52,821**	**47,446**
	Total equity and liabilities	**255,422**	**241,598**

PARENT COMPANY STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2016

Note	In DKK '000	Share capital	Share premium	Share based payment reserve	Cash flow hedge reserve	Reserve for development project costs	Retained earnings	Total equity
	At 1 January 2015	**5,822**	**210,675**	**12,101**	**-**	**-**	**(38,533)**	**190,065**
	Profit for the year	-	-	-	-	-	4,445	4,445
	Net loss on cash cash flow hedges	-	-	-	(3,840)	-	-	(3,840)
	Net loss on cash cash flow hedges reclassified to revenue	-	-	-	2,594	-	-	2,594
	Net loss on cash cash flow hedges reclassified to finance costs	-	-	-	237	-	-	237
	Net loss on cash cash flow hedges	-	-	-	237	-	-	237
	Total comprehensive income	**-**	**-**	**-**	**(772)**	**-**	**4,445**	**3,673**
	Issue of shares	-	-	-	-	-	-	-
	Reversal, exercised and lapsed share options	-	-	(2,534)	-	-	2,534	-
5	Share-based payments	-	-	414	-	-	-	414
	Total transactions with shareholders	**-**	**-**	**(2,120)**	**-**	**-**	**2,534**	**414**
	At 31 December 2015	**5,822**	**210,675**	**9,981**	**(772)**	**-**	**(31,554)**	**194,152**
	Profit for the year	-	-	-	-	-	5,194	5,194
	Additions to project development costs, net of tax	-	-	-	-	33,244	(33,244)	-
	Net gain on cash cash flow hedges	-	-	-	743	-	-	743
	Net gain on cash cash flow hedges reclassified to revenue	-	-	-	(886)	-	-	(886)
	Net gain on cash cash flow hedges reclassified to finance costs	-	-	-	(163)	-	-	(163)
	Income tax effect	-	-	-	53	-	-	53
	Total comprehensive income	**-**	**-**	**-**	**(253)**	**33,244**	**(28,050)**	**4,941**
	Issue of shares	94	2,939	-	-	-	-	3,033
	Reversal, exercised and lapsed share options	-	2,815	(2,845)	-	-	30	-
5	Share-based payments	-	-	475	-	-	-	475
	Total transactions with shareholders	**94**	**5,754**	**(2,370)**	**-**	**-**	**30**	**3,508**
	At 31 December 2016	**5,916**	**216,429**	**7,611**	**(1,025)**	**33,244**	**(59,574)**	**202,601**

PARENT COMPANY STATEMENT OF CASH FLOWS

for the year ended 31 December 2016

Note	In DKK '000	2016	2015
	Operating activities		
	Profit before tax	6,369	6,484
	Adjustments to reconcile profit before tax to net cash flows:		
	Finance income	(303)	(6,016)
	Finance costs	363	401
	Depreciation, amortisation and impairment	37,218	28,521
	Impairments and reversal of impairments in subsidiaries	(2,146)	4,750
	Share-based payment expense	475	414
	Working capital adjustments:		
	Change in inventories	(4,782)	(4,758)
	Change in trade and other receivables and intercompany receivables	(21,085)	(12,362)
	Change in trade and other payables, intercompany payables and provisions	2,461	9,714
	Cash flows from operating activities	**18,570**	**27,148**
	Currency gains and losses	299	3,395
	Interest received	4	14
	Interest paid	(363)	(401)
	Income tax received, net	2,479	5,254
	Net cash flows from operating activities	**20,989**	**35,410**
	Investing activities		
	Purchase of tangible assets	(2,959)	(4,151)
	Investments in intangible assets	(45,792)	(42,915)
	Investments in subsidiaries	-	(756)
	Investments in leasehold deposits	(60)	(436)
	Net cash from investing activities	**(48,811)**	**(48,258)**
	Free cash flow	**(27,822)**	**(12,848)**
	Financing activities		
	Issue of shares	3,033	-
	Repayment of borrowings	(637)	(643)
	Net cash flows from financing activities	**2,396**	**(643)**
	Net decrease in cash and cash equivalents	**(25,426)**	**(13,491)**
	Net foreign exchange difference	-	2,606
	Cash and cash equivalents at 1 January	49,249	60,134
	Cash and cash equivalents at 31 December	**23,823**	**49,249**

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 1 SIGNIFICANT ACCOUNTING POLICIES

General
The financial statements for Napatech A/S (the parent company) have been prepared in accordance International Financial Reporting Standards (IFRS), as adopted by the EU, and requirements in the Danish Financial Statements Act.

The accounting policies for the Parent company are the same as for the Group as set out in Note 2 to the consolidated financial statements, except for the items listed below.

Dividends
Dividends from the investment in subsidiaries are recognised as income in the parent company's income statement in the year in which the the dividend is declared.

Investments in subsidiaries
Investments in subsidiaries are measured at cost. If there is evidence of impairment, an impairment test is performed. If the cost exceeds the recoverable amount, a write-down is made to such lower value.

Share-based payments to employees in subsidiaries
The value of share options to the employees in the US-based subsidiary Napatech Inc. is recognised as an increase in the investment in subsidiaries as the employees' services rendered in exchange for the share options are received in subsidiaries.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 2 EMPLOYEE BENEFITS EXPENSE

DKK'000	2016	2015
Employee benefits expense is reported as follows:		
Wages and salaries	69,754	76,918
Defined contribution schemes	10,954	10,850
Share-based payment expense (Note 5)	476	414
Social security costs	719	800
Allocated to development projects	(34,095)	(35,265)
Total employee benefits expense	**47,808**	**53,717**

DKK'000	2016	2015
Employee benefits expense is recognised in the parent company income statement as follows:		
Research and development costs	9,966	12,577
Selling and distribution expenses	23,202	26,574
Administrative expenses	14,640	14,566
Total employee benefits expense	**47,808**	**53,717**
Average number of employees	**85**	**86**

Compensation of key management personnel is set out in Note 5 to the consolidated financial statements of the Group.

NOTE 3 RESEARCH AND DEVELOPMENT COSTS

Research and development costs including annual amortisation charge on completed development projects recognised in the consolidated income statement are DKK 44,211 thousand (2015: DKK 36,950 thousand). All research and development costs are incurred by the parent company.

NOTE 4 AUDITORS' FEES

Auditors' fees for the parent company and the Group are the same. Details of the auditors' fees are disclosed in the Note 8 to the consolidated financial statements.

NOTE 5 SHARE-BASED PAYMENT EXPENSE

The share options decribed in Note 7 to the consolidated financial statements are issued by the parent company. The value of share options granted to employees in the wholly-owned US-based subsidiary is recognised as the cost of the investment in the subsidiary. Out of the Group's total share-based payment expense of DKK 475 thousand (2015: DKK 414 thousand), no value has been recognised as an additional cost of the investment in the subsidiary.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 6 DEPRECIATION, AMORTISATION AND IMPAIRMENT

DKK'000	2016	2015
Depreciation, amortisation and impairment are reported as follows:		
Depreciation plant and property	4,571	5,179
Depreciation of leasehold improvements	506	492
Total depreciation of tangible assets	**5,077**	**5,671**
Amortisation of patents	611	331
Impairment of patents	1,769	-
Amortisation of completed development projects	29,047	21,856
Amortisation of other intangible assets	714	663
Total amortisation and impairment of intangible assets	**32,141**	**22,850**
Total depreciation, amortisation and impairment	**37,218**	**28,521**

NOTE 7 FINANCE INCOME

DKK'000	2016	2015
Interest receivable from banks	4	14
Foreign exchange gains	299	6,002
Total finance income	**303**	**6,016**

NOTE 8 FINANCE COSTS

DKK'000	2016	2015
Interest payable to banks	332	336
Finance charges payable under finance leases	19	44
Other finance costs	12	21
Total finance costs	**363**	**401**

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 9 INCOME TAX

DKK'000	2016	2015
Current tax recognised in the parent company income statement:		
Current income tax carry back refund	(2,123)	(7,705)
Change in deferred tax	3,298	9,744
Total income tax	**1,175**	**2,039**

A reconciliation between tax expense and profit before tax multiplied by the applicable income tax rate for the parent company for 2016 and 2015 is as follows:

DKK'000	2016	2015
Profit before tax	6,369	6,484
At the applicable Danish income tax rate for the parent company, 22% (2015: 23.5%)	1,401	1,524
Tax effect of:		
Carry back refunded at 23.5% (2015: 25%)	113	(354)
Tax deductable expenses	(511)	(237)
Non-deductible expenses	172	1,106
At the effective income tax rate of 18% (2015: 31%)	**1,175**	**2,039**

NOTE 10 INTANGIBLE ASSETS

Intangible assets comprise patents and development projects. An overview over these assets is disclosed in Note 14 to the consolidated financial statements.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 11 TANGIBLE ASSETS

	Plant and equipment		Leasehold improvements		Total	
DKK'000	2016	2015	2016	2015	2016	2015
Cost at 1 January	30,800	26,751	3,734	3,632	34,534	30,383
Additions	2,473	4,049	486	102	2,959	4,151
Cost at 31 December	**33,273**	**30,800**	**4,220**	**3,734**	**37,493**	**34,534**
Accumulated depreciation at 1 January	23,617	18,438	2,714	2,222	26,331	20,660
Depreciation for the year	4,571	5,179	506	492	5,077	5,671
Accumulated depreciation at 31 December	**28,188**	**23,617**	**3,220**	**2,711**	**31,408**	**26,331**
Carrying amount at 31 December	**5,085**	**7,183**	**1,000**	**1,020**	**6,085**	**8,203**

The carrying amount of tangible assets held under finance leases is nil at 31 December 2016 (31 December 2015: DKK 328 thousand).

There were no indications of impairment of the parent company's tangible assets in the year.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 12 INVESTMENTS IN SUBSIDIARIES

DKK'000	2016	2015
Cost at 1 January	6,947	6,191
Additions	-	756
Cost at 31 December	**6,947**	**6,947**
Accumulated impairment at 1 January	6,896	2,146
Impairment for the year	-	4,750
Reversal of impairment losses	(2,146)	-
Accumulated impairment at 31 December	**4,750**	**6,896**
Carrying amount at 31 December	**2,197**	**51**

The parent company's investments in subsidiaries at 31 December 2016 and 2015 consist of the following:

		Ownership in %		Proportion of voting rights in %		
Name	**Country**	**2016**	**2015**	**2016**	**2015**	**Business activity**
Napatech Inc., USA	Andover, USA	100	100	100	100	Sale and distribution of the Group's products
Napatech Japan KK	Tokyo, Japan	100	100	100	100	Sale and distribution of the Group's products

Reversal of impairment losses relates to the investment in Napatech Inc., USA. Due to the positive market conditions in the USA the subsidiary has incurred profits whereby the value of net assets in the consolidated financial statements are above the cost of investment.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 13 DEFERRED TAX

	Statement of financial position		Income statement	
DKK'000	2016	2015	2016	2015
Tax losses carry-forwards	(11,361)	(11,361)	-	3,072
Intangible assets	21,830	18,777	3,053	4,581
Plant, property and equipment	(1,863)	(1,987)	124	1,717
Provision for bad debts	(179)	(247)	68	137
Deferred tax liability and expense	**8,427**	**5,182**	**3,245**	**9,507**

DKK'000	2016	2015
Reconciliation of deferred tax libility / (asset) is as follows:		
Opening balance at 1 January	5,182	(4,325)
Recognised in parent company income statement	3,298	9,744
Recognised in parent company statement of comprehensive income	(53)	(237)
Closing balance at 31 December	**8,427**	**5,182**

NOTE 14 INVENTORIES

DKK'000	2016	2015
Consumables and components	1,259	4,916
Finished goods and goods for resale	17,416	8,977
Total inventories	**18,675**	**13,893**
Carrying value of inventories recognised at fair value	**-**	**-**

The cost of goods sold for the year is DKK 70,574 thousand (2015: DKK 62,764 thousand).

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 15 TRADE AND OTHER RECEIVABLES

DKK'000	2016	2015
Receivables recognised in the parent company statement of financial position:		
Trade receivables	12,034	9,139
Receivables from group entities	79,210	61,411
Other receivables	4,187	3,796
Total current receivables	**95,431**	**74,346**

Movements in the provision for bad debts on trade receivables are as follows:

DKK'000	2016	2015
At 1 January	1,125	1,745
Utilised in the year	(487)	-
Written off in the year	-	(924)
Change in the year	174	304
At 31 December	**812**	**1,125**

Ageing analysis of past due but not impaired trade receivables is as follows:

DKK'000	2016	2015
Not past due	8,717	6,122
Past due for less than 30 days	1,310	886
Past due between 30 and 60 days	697	385
Past due between 60 and 90 days	124	23
Past due after 90 days	1,186	1,723
Total maximum credit risk	**12,034**	**9,139**

NOTE 16 INCOME TAX RECEIVABLE

Income tax receivable relates to income tax carry back refund based on the prevoius years tax losses as a result of investements in development projects. The movement in the income tax receivable is disclosed in Note 19 to the consolidated financial statements.

NOTE 17 ISSUED CAPITAL AND RESERVES

Information in relation to issued capital and reserves is disclosed in Note 20 to the consolidated financial statements.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 18 FINANCIAL ASSETS AND FINANCIAL LIABILITIES

DKK'000	2016	2015
Financial assets measured at amortised cost:		
Leasehold deposits	2,072	2,012
Trade receivables	12,034	9,139
Receivables from group entities	79,210	61,411
Other receivables	4,187	3,796
Cash and cash equivalents	23,823	49,249
Total financial assets	**121,326**	**125,607**
Financial liabilities measured at amortised cost:		
Finance lease liabilities	-	637
Interest-bearing loans and borrowings	5,000	5,000
Trade payables	25,978	18,645
Payables to group entities	86	-
Derivatives designed as hedging instruments:		
Foreign exchange forward contracts	1,314	1,008
Total financial liabilities	**32,378**	**25,290**

Carrying amounts of financial assets and financial liabilities approximate their fair value.

NOTE 19 DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments relate to forward exchange contracts in order to hedge the future budgeted sales in USD that is not naturally hedged by the costs denominated in USD covering a period of 12 months. The forward exchange contracts are held by the parent company and are disclosed in Note 22 to the consolidated financial statements.

NOTE 20 PROVISIONS

Provisions relate to guarantees associated with the sale of network adapters. These provisions are incurred by the parent company and are disclosed in Note 23 to the consolidated financial statements.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 21 COMMITMENTS AND CONTINGENCIES

Collaterals
The parent company (as the whole Group) has issued a floating charge in the amount of DKK 10 million (2015: DKK 10 million) secured on receivables, inventories and tangible assets with carrying amount of DKK 36,794 thousand (2015: DKK 31,235 thousand) as collateral for bank debt.

Operating lease commitments
The parent company's operating lease commitments relate to leasing of operating equipment, cars and office facilities. Future minimum payments under operating leases at 31 December are as follows:

		2016	
DKK'000	Cars	Office facilities	Total
Falling due within one year	71	5,164	5,235
Falling due between one and five years	-	2,582	2,582
Total	**71**	**7,746**	**7,817**

		2015	
DKK'000	Cars	Office facilities	Total
Falling due within one year	106	4,908	5,014
Falling due between one and five years	71	2,551	2,622
Total	**177**	**7,459**	**7,636**

Finance lease commitments
Finance lease commitments for the parent company are the same as for the Group. Disclosure in relation to the finance lease commitments is provided in Note 24 to the consolidated financial statements.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

NOTE 22 RELATED PARTY TRANSACTIONS

The parent company's related parties are the same as the Group's. Additional information is set out in Note 25 to the consolidated financial statements.

Related parties in which the parent company has a controlling influence include the company's subsidiaries as disclosed in Note 12 to the parent company financial statements.

The following provides the total amount of transactions that have been entered into with subsidiaries for the relevant financial year:

	Napatech Inc., USA		Napatech Japan KK, Japan	
DKK'000	2016	2015	2016	2015
Income statement:				
Sales to subsidiaries	138,513	143,881	-	-
Purchases from subsidiaries	-	-	3,230	2,762
Statement of financial position:				
Receivables from subsidiaries	79,210	61,292	-	119
Payables to subsidiaries	-	-	86	-

NOTE 23 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The parent company incurs external financial liabilities and settles its transactions in currencies other than the functional currency. The Groups' financial risks are therefore primarily related to the parent company. Relevant additional information is set out in Note 26 to the consolidated financial statements.

NOTE 24 EVENTS AFTER THE REPORTING PERIOD

There have been no significant events after 31 December 2016 that might affect the parent company financial statements.

STATEMENT BY THE BOARD OF DIRECTORS AND THE EXECUTIVE MANAGEMENT ON THE ANNUAL REPORT

The Board of Directors and the Executive Management have today discussed and approved the annual report of Napatech A/S for the financial year 1 January – 31 December 2016.

The annual report has been prepared in accordance with international Financial Reporting Standards as adopted by EU and additional requirements in the Danish Financial Statements Act.

It is our opinion that the consolidated financial statements and the Parent Company's financial statements give a true and fair view of the Group's and the Parent Company's financial position at 31 December 2016 and of the results of the Group's and the Parent Company's operations and cash flows for the financial year 1 January – 31 December 2016.

Further, in our opinion, the Management's review gives a fair review of the matters discussed in the Management's review.

We recommend that the annual report be approved at the annual general meeting.

Søborg, 29 March 2017

Executive Management

Henrik Brill Jensen, Chief Executive Officer

Board of Directors

Lars Thoresen, Chairman

Bjørn Erik Reinseth

Howard Bubb

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NAPATECH A/S

Opinion
We have audited the consolidated financial statements and the parent company financial statements of Napatech A/S for the financial year 1 January – 31 December 2016, which comprise an income statement, statement of comprehensive income, balance sheet, statement of changes in equity, cash flow statement and notes, including a summary of significant accounting policies, for the Group as well as for the parent company. The consolidated financial statements and the parent company financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements in the Danish Financial Statements Act.

In our opinion, the consolidated financial statements and the parent company financial statements give a true and fair view of the financial position of the Group and the parent company at 31 December 2016 and of the results of the Group's and the parent company's operations and cash flows for the financial year 1 January – 31 December 2016 in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements in the Danish Financial Statements Act.

Basis of opinion
We conducted our audit in accordance with International Standards on Auditing (ISAs) and additional requirements applicable in Denmark. Our responsibilities under those standards and requirements are further described in the "Auditors' responsibilities for the audit of the consolidated financial statements and the parent company financial statements" section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the additional requirements applicable in Denmark, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters
Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements and the parent financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements and parent financial statement as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matters is provided in that context.

We have fulfilled the responsibilities described in the "Auditors' responsibilities for the audit of the consolidated financial statements and the parent company financial statements" section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements, and parent company financial statements.

Recognition and valuation of development costs as intangible assets
Capitalised development costs amount to DKK 98.2 million net at 31 December 2016 in the accompanying consolidated financial statements and account for 37% of the Group's assets and 48% of the Group's equity.

Development costs mainly comprise hardware and software development. The Company capitalises eligible software and products development costs upon meeting the criteria as described in IAS 38. Capitalizstion criteria assessment under IAS 38 requires significant judgement and measurement uncertainty at inception and throughout the life of the project. Judgements involved in determining the eligibility of the costs for capitalisation and the subsequent measurement require detailed and sensitivity analyses.

Additional details on capitalised development costs are provided in note 14 to the consolidated Financial Statements.

Our audit procedures included an assessment of the eligibility of the development costs for capitalisation as intangible asset under IAS 38 and an evaluation of the assumptions and methodologies used by Management to test the impairment of these intangible assets. We have also assessed the design of the controls implemented by Management in respect of capitalisation of development costs and performed substantive test of details on the capitalised development costs, including on a sample basis testing to underlying evidence, including hour registration. Further, we have tested estimates for useful life and estimates relating to future economic cash flows.

We further evaluated the disclosures provided by management in the financial statements compared to applicable accounting standards.

Revenue recognition
The Group has expanded significantly over the past years and continue to have high growth expectations, and accordingly, we have identified the occurrence, completeness and measurement of revenue recognition as key audit matters.

We assessed and tested internal controls regarding revenue recognition, including the timing of the revenue recognition and the treatment of discounts. We also performed analytical procedures on margins, detailed sample testing of transactions and contracts.

Statement on the Management's review
Management is responsible for the Management's review.

Our opinion on the consolidated financial statements and the parent company financial statements does not cover Management's Review, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements and the parent company financial statements, our responsibility is to read Management's review and, in doing so, consider whether Management's Review is materially inconsistent with the consolidated financial statements and the parent company financial statements or our knowledge obtained during the audit, or otherwise appears to be materially misstated.

Moreover, it is our responsibility to consider whether the Management's review provides the information required under the Danish Financial Statements Act. Based on the work we have performed, we conclude that the Management's review is in accordance with the consolidated financial statements and the parent company financial statements and has been prepared in accordance with the International Financial Reporting Standards as adopted by the EU and additional requirements in the Danish Financial Statements Act. We did not identify any material misstatement of the Management's review.

Management's Responsibilities for the consolidated financial statements and the parent company financial statements
Management is responsible for the preparation of consolidated financial statements and the parent company financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements in the Danish Financial Statements Act, and for such internal control as Management considers necessary to enable the preparation of consolidated financial statements and parent company financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements and the parent company financial statements, Management is responsible for assessing the Group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting in preparing the consolidated financial statements and the parent company financial statements unless Management either intends to liquidate the Group or the parent Company or to cease operations, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the consolidated financial statements and the parent company financial statements
Our objectives are to obtain reasonable assurance about whether the consolidated financial statements and the parent company financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs and the additional requirements applicable in Denmark will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements and the parent company financial statements.

As part of an audit conducted in accordance with ISAs and the additional requirements applicable in Denmark, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and the parent company financial statements , whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and the parent company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Management.

- Conclude on the appropriateness of Management's use of the going concern basis of accounting in preparing the consolidated financial statements and the parent company financial statements and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and the parent company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements and the parent company financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group or the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and contents of the consolidated financial statements and the parent company financial statements, including the disclosures, and whether the consolidated financial statements and the parent company financial statements represent the underlying transactions and events in a manner that gives a true and fair view.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements and the parent company financial statements . We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate to them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Frederiksberg, 29 March 2017

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CVR no. 30 70 02 28

Eskild N. Jakobsen State Authorised Public Accountant	Alex Nissov State Authorised Public Accountant

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