

# NAPATECH

2<sup>ND</sup> QUARTER 2018  
INTERIM REPORT

CONTENTS

Management Statement..... 3

Letter from the CEO..... 4

Management’s Review..... 5

    Highlights..... 5

    Financial Review..... 6

Interim Consolidated Income Statement ..... 9

Interim Consolidated Statement of Comprehensive Income..... 9

Interim Consolidated Statement of Financial Position..... 10

Interim Consolidated Statement of Changes in Equity..... 12

Interim Consolidated Statement of Cash Flows..... 14

Notes to the Interim Consolidated Financial Statements..... 15

## MANAGEMENT STATEMENT

The Board of Directors and the Executive Management have discussed and approved the interim report of Napatech Group for the three months' period from April 1 to June 30, 2018.

The interim report has been prepared in accordance with IAS 34 Interim Financial Reporting, as adopted by the EU, and additional interim reporting requirements for listed companies.

In our opinion, the interim report gives a true and fair view of the Napatech Group's assets, liabilities and financial position at June 30, 2018, and of the results of the Napatech Group's operations and cash flows for the three months' period April 1 to June 30, 2018 and the six months period from January 1 to June 30, 2018.

We also find that the Management's review provides a fair statement of developments in the activities and financial situation of the Group, financial results for the period and the general financial position of the Group, and describes the major risks and elements of uncertainty faced by the Group. The term Company below refers as well to the Group.

The interim report has not been subject to audit or review by our auditors.

Oslo, August 14, 2018

Executive Management

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Ray Smets, CEO

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Carsten Kaalund, CFO

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Henrik Brill Jensen, COO

Board of Directors

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Lars Boilesen, Chairman

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Howard Bubb

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Lars B. Thoresen

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Henry Wasik

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Bjørn Erik Reinseth



## LETTER FROM THE CEO

Dear shareholders,

This is my first quarterly report as the CEO of Napatech. I am very excited to join the company, and I look forward to reviewing our Q2 results and elaborating about the great opportunities that lie ahead. Our markets have gone through a significant transformation over the past 18 months which has impacted our results. At the same time, we have adjusted our product-market strategy to align with the largest players in the FPGA market and are targeting solutions with large markets and high growth. We will begin to see the early stages of market progress as we move through the second half of 2018. As part of our corporate repositioning, we have taken action to improve our internal cost structure and efficiency, reducing cash break-even revenue from 10 MUSD to 8 MUSD on a quarterly basis, with full effect from the beginning of 2019, with savings already being seen in Q3 and Q4 of 2018. We have also taken action to improve our cash position to assure we can weather the near-term volatility within our markets, and position Napatech to win the emerging opportunities we see. In the baseline case, we expect to be fully funded throughout 2019 and to become cash generating towards the end of 2019.

Generally, a significant portion of our revenue comes from partners who have integrated our solution within their products. This has been one of our primary paths to the market. As our partners and others have reported in various market sectors, many of these appliance companies have experienced volatility within their markets as their customers assess their internal strategies moving away from buying hardware centric solutions to buying software solutions that operate on commercial off-the-shelf servers.

As previously communicated, we expect a notable improvement in revenues in the second half of 2018 compared to the temporary weakness experienced in the first half. As such, we currently expect sale for the second half of 2018 at 12 MUSD within a range of 10 to 15 MUSD, in comparison, we had sales of 7.9 MUSD in the first half of 2018. However, as the transition from hardware centric solutions to software centric solutions continues, we expect the quarter-to-quarter order volatility to remain as customers sort out their technology buying strategies.

The direction of Napatech's strategy is to provide solutions that focus on building FPGA hardware components and the software systems to accelerate performance. As one of the few companies in the world with the expertise to deliver world-class FPGA-based application-driven solutions, Napatech is perfectly positioned to take advantage of the market shift to reconfigurable computing platforms and the rapidly increasing volume of servers deployed in the market. We will win the emerging opportunities by:

- Aligning product and technology plans by partnering with the leading suppliers of FPGA technologies and tools.
- Aligning the global sales force and technical support in the North American regions that represent the highest concentrations of customer growth and

organizing around unique customer segments, who benefit from reconfigurable computing.

- Focus on key strategic alliances and channel partnerships to further leverage external resources to extend our reach to the emerging set of end-user customers who require our solutions.
- Expansion of Napatech's product portfolio to include more software offerings and professional services, enabling Napatech products to be deployed in any open and standard server platform.

As demonstrated by these actions, the company, together with our customers, are undergoing a transformation from a hardware-centric to a software centric world of software-defined networking. The way networks are built, managed and operated have radically changed, creating incredible new opportunities for IT organizations of every size to reimagine their businesses. As a result of the major market trends, FPGA technology has now become pervasive, and are widely available to more users and applications, in many more network types and locations.

Napatech's strategy is to be the global leader in reconfigurable computing solutions. Our strategy is founded on four main pillars providing a firm foundation to win the emerging opportunities:

- Dominate: Napatech will continue to dominate the packet capture market and maintain the strategic relationships established with market leading key customers and partners.
- Expand: Napatech is engaged with key customers on defining reconfigurable computing solutions that expand beyond packet capture use cases, such as inline cyber security solutions.
- Establish: Napatech is establishing a beachhead in the virtualization solutions market based on current engagements with leading telecom carriers and vendors.
- Explore: Napatech is exploring the potential for delivering compute offload solutions that leverage FPGA technology deployed by cloud vendors or server ODMs.

Napatech is expecting growth in new initiatives through 2022 to be a combination of:

- Cybersecurity solutions for both existing and new customers. Today, this is a large market with medium growth. This market is expected to contribute with up to 60% of future, long-term revenues.
- Virtualization solutions primarily for new customers. Today, this is a small market with massive growth. This market is expected to contribute with up to 60% of future, long-term revenues.
- Compute offload solutions for new customers. Today, this is a small market with massive growth. This market is expected to contribute with up to 20% of future, long-term revenues.
- New 5G wireless networks are being designed and will demand new virtualized architectures, new powerful applications and computing power with greater scale. This market evolution is expected to add a significant growth potential in building hyperscale networks in the Service Provider domain.

As a result of the changes that the markets, customers and Napatech are going through, the long-term outlook is promising as Napatech products and services become applicable to not only our current, but also new market segments. In other terms, we see a long-term potential significantly larger than our current business as we move to broader markets and support more applications, but underline that the short term visibility is limited and will be affected by quarter-to-quarter order volatility and general

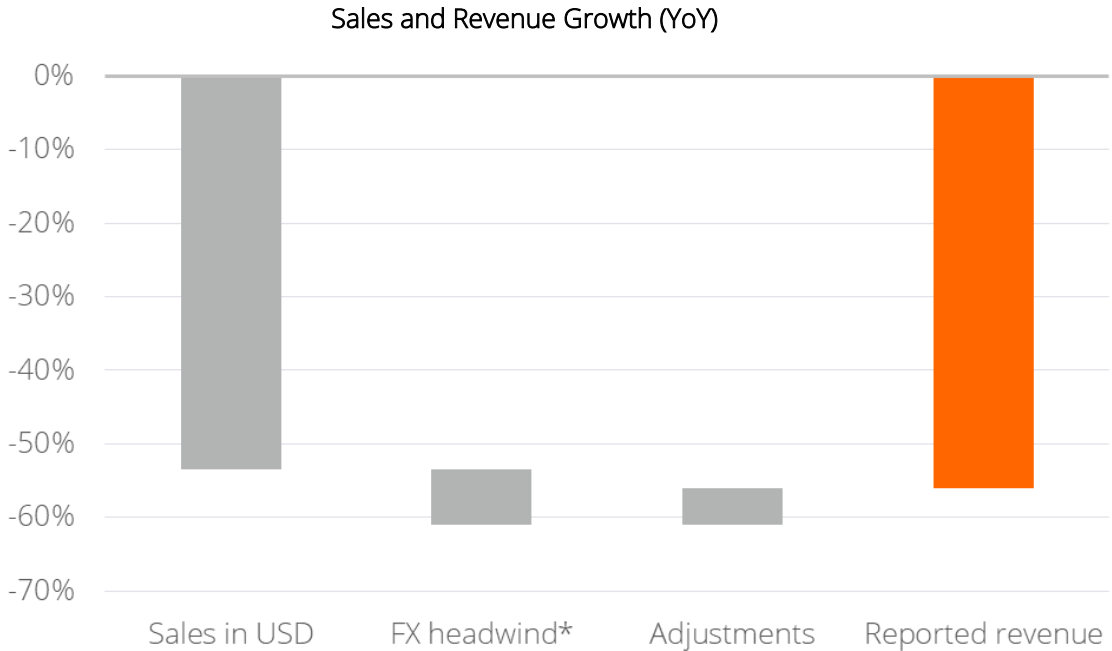
business uncertainty. However, we are taking the right steps in these transformative times and are looking forward to the return of customer demand in the second half of 2018.

Best regards,  
Ray Smets, Chief Executive Officer

MANAGEMENT'S REVIEW

Highlights:

- Revenue for the second quarter of 2018 amounted to DKK 24.7 million, a decline of 56% compared to last year, but increased by 11% compared to the first quarter of 2018.
- Gross margin for the second quarter of 2018 was 70% compared to 71% in the second quarter of 2017.
- EBITDA for the second quarter of 2018 amounted to negative DKK 16.2 million, a decline from DKK 9.6 million in the second quarter of 2017.
- EBITDA margin for the second quarter of 2018 was -65%, a decline from 17% in the second quarter of 2017.
- EBIT for the second quarter amounted to negative DKK 28.0 million compared to DKK 0.1 million in the second quarter of 2017.
- Cash decreased to DKK 1.6 million in the second quarter of 2018. Including unused credit facilities, the total available funds are approximately DKK 7.4 million.



\*Average bank rates

This is Napatech

Napatech helps companies to reimagine their business by bringing Hyperscale computing benefits to IT organizations of every size. We enhance open and standard virtualized servers to boost innovation and release valuable computing resources that improve services and increase revenue. Our reconfigurable computing platform™ is based on a broad set of FPGA software for leading IT compute, network and security applications that are supported on a wide array of FPGA hardware designs.

## MANAGEMENT'S REVIEW (CONTINUED)

### Napatech operations.

The statements below are related to Napatech's development in the second quarter of 2018 compared to the second quarter of 2017, unless as otherwise stated. Additional information is available at [www.napatech.com/investor](http://www.napatech.com/investor).

#### Key figures and ratios.

	2 <sup>nd</sup> Quarter		YTD June	
	2018	2017	2018	2017
Revenue, DKK'000	24,723	56,462	47,021	114,012
Gross profit margin, %	70%	71%	69%	72%
EBITDA, DKK'000	(16,158)	9,572	(31,965)	18,954
EBITDA margin, %	-65%	17%	-68%	17%
(Loss) / profit before tax, DKK'000	(26,763)	(4,266)	(54,874)	(6,258)
EPS basic, DKK (please ref. Note 5)	(0.87)	(0.14)	(1.79)	(0.21)
EPS diluted, DKK	(0.85)	(0.14)	(1.74)	(0.21)
Equity, DKK'000	137,185	206,153	137,185	206,153
Cash and cash equivalents, DKK'000	1,628	33,997	1,628	33,997

## Financial Review

### Revenue

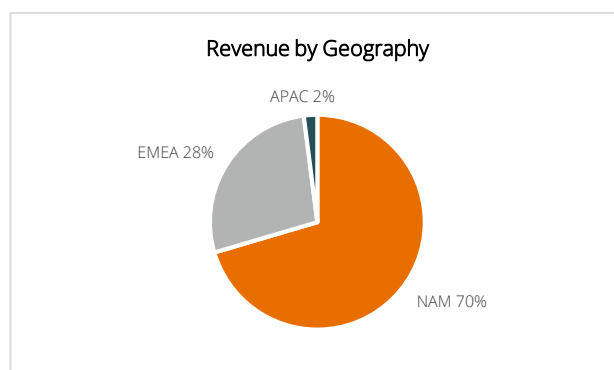
Napatech reports revenue of DKK 24.7 million in the second quarter of 2018, a decrease of 56% compared to the same period in 2017. The revenue for the period has been negatively influenced by the postponement of customer projects and inventory reductions. The sales are in line with the previously communicated expectations for the quarter.

This quarter showed a decline in our Pandion business and in our SmartNIC business due to fluctuations in our customers ordering pattern and inventory management. Pandion represented 16% of total sales in the quarter, compared to 9% in Q2 2017.

Sales were distributed with 70% in NAM, 28% in EMEA and the remaining 2% in APAC. The sales in NAM are lower than expected due to postponement of customer projects and inventory reductions.

### Gross Margin

Napatech's gross margin for the quarter was 70%, down from 71% in the same period last year. The gross margin is dependent on the product mix, and the sales reported this quarter includes sale of accessory products with lower margin than normal.



## MANAGEMENT'S REVIEW (CONTINUED)

### Financial review (continued)

#### Costs

Total costs for the second quarter of 2018 were DKK 33.4 million, compared to DKK 30.4 million for the second quarter of 2017. The increase in total costs is primary due to one-time costs related to the cost reduction program implemented in the second quarter of 2018.

R&D costs for the second quarter of 2018 were DKK 5.2 million, compared to DKK 3.9 million in the second quarter of 2017. The level of the R&D costs is primary related to the timing of our development projects.

Sales and distribution costs for the period were DKK 17.6 million, compared to DKK 17.2 million in the same period last year. The Sales and distribution costs in Q2 2018 were in line with our expectations.

Administrative expenses for the quarter were DKK 10.6 million compared to DKK 9.3 million in the second quarter of 2017. Administrative expenses in Q2 2018 were in line with our expectations.

#### EBITDA

EBITDA was negative DKK 16.2 million in the second quarter of 2018, compared to DKK 9.6 million in the second quarter of 2017. The decrease is driven by lower sales and lower margins than last year.

#### Depreciation and amortization

Depreciation and amortization for the quarter was DKK 11.8 million, compared to DKK 9.5 million in the second quarter of 2017. Depreciations are affected by the timing of completion of the company's development projects, and past investment levels.

#### EBIT

EBIT for the second quarter of 2018 was negative DKK 28.0 million, a decrease compared to DKK 0.1 million in the second quarter of 2017. The decrease is primarily driven by the revenue decline in the quarter.

#### Financial Items

Financial items for the second quarter of 2018 were an income of DKK 1.2 million, compared to an expense of DKK 4.3 million in the second quarter of 2017. The financial items are primarily affected by the change in USD exchange rate, and it has increased during the second quarter of 2018, compared to end of 2017 resulting in this income.

#### Taxes

Taxes for the second quarter of 2018 are an income of DKK 5.9 million. The effective tax rate for the year is thus 22%.

#### Investments

Total investments in the second quarter of 2018 were DKK 10.3 million, primarily related to new product development (capitalized development), representing DKK 9.8 million of total investments in the quarter. In the second quarter of 2017, total investments were DKK 12.6 million, of which DKK 12.3 million was related to internal product development.

In the second quarter of 2018, there were several ongoing development projects related to the Pandion product, the SmartNIC portfolio and development of our virtualization product.

#### Cash Flow

For the second quarter of 2018, net cash flow from operating activities was negative DKK 19.2 million, compared to negative DKK 11.0 million from the second quarter of 2017.

Cash flow from investing activities was negative DKK 10.3 million in the second quarter of 2018, compared to negative DKK 12.6 million in the second quarter of 2017.

Net cash from financing activities, was improved by DKK 10.8 million due to increase in borrowings.

The total cash position of the Company was DKK 1.6 million by the end of the second quarter of 2018, a decrease of DKK 32.4 million compared to the end of the second quarter of 2017. The negative cash flow is driven by the investment activities conducted by the company, as the current business has not fully supported the investment level needed for securing the future growth.

Napatech has unused credit facilities of DKK 5.8 million at the end of the second quarter of 2018. Thus, the Company has available total funds of approximately DKK 7.4 million at the end of the second quarter of 2018.



## MANAGEMENT'S REVIEW (CONTINUED)

### Financial review (continued)

#### Shareholders and Share Information

Napatech as of June 30, 2018 had 23,923,220 shares outstanding at DKK 0.25 each. The share capital is 5,980,805 DKK divided among the 404 shareholders.

Investor	Number of shares	% of total	TYPE	Country
VERDANE CAPITAL VIII	5.172.844	21,62%	Ordinary	DNK
ARCTIC FUNDS PLC	2.270.021	9,49%	Ordinary	IRL
STOREBRAND VEKST VER	1.502.364	6,58%	Ordinary	NOR
VERDIPAPIRFONDET DNB	1.388.024	5,80%	Ordinary	NOR
SILVERCOIN INDUSTRIE	1.307.223	5,46%	Ordinary	NOR
DNB NOR MARKETS, AKS	1.219.500	5,10%	Ordinary	NOR
THE BANK OF NEW YORK	980.000	4,10%	Nominee	GBR
DANSKE BANK A/S	913.927	3,82%	Nominee	DNK
SÅETER HAAKON MORTEN	688.439	2,88%	Ordinary	NOR
UBS SWITZERLAND AG	673.498	2,82%	Nominee	CHE
HOLTA INVEST AS	655.272	2,74%	Ordinary	NOR
DANSKE BANK A/S	583.269	2,44%	Nominee	DNK
VINTERSTUA AS	580.521	2,43%	Ordinary	NOR
TIGERSTADEN AS	520.108	2,17%	Ordinary	NOR
MARSTAL AS	420.000	1,76%	Ordinary	NOR
NORDEA BANK AB	285.021	1,19%	Nominee	DNK
HOBOLT NIELS	281.749	1,18%	Ordinary	DNK
NORDNET BANK AB	252.240	1,05%	Nominee	SWE
EKNER PETER DAHL	247.200	1,03%	Ordinary	DNK
SIX-SEVEN AS	239.457	1,00%	Ordinary	NOR
<b>Total number owned by top 20</b>	<b>20.180.677</b>	<b>84,36%</b>		
<b>Total 384 other shareholders</b>	<b>3.742.543</b>	<b>15,64%</b>		
<b>Total number of shares</b>	<b>23.923.220</b>	<b>100,00%</b>		

#### Significant events after the end of the period

After the end of the period, the company has as of August 2, 2018 completed a private placement raising gross proceeds of NOK 40 million. The private placement was divided into two tranches. Tranche 1 consists of 2,392,000 offer shares. Tranche 2 consists of 5,608,000 offer shares. After the private placement, the new share capital of the company is DKK 7,980,805 divided into 31,923,220 shares, each with a nominal value of DKK 0.25.

#### Outlook for 2018

Napatech's strategy is to be the global leader in reconfigurable computing solutions. Our strategy is to focus on delivering the solutions, technologies and expertise necessary to enable all organizations that rely on IT for their business to reap the benefits of reconfigurable computing. Our goal is to become the number one vendor of reconfigurable computing solutions.

The company expects a notable improvement in revenues in the second half of 2018 compared to the weakness experienced in the first half. As such, the company currently expects sales for the second half of 2018 at 12 MUSD within a range of 10 to 15 MUSD. In comparison the company had sales of 7.9 MUSD in the first half of 2018.

The company still underlines that the short-term visibility is limited and will be affected by quarter-to-quarter order volatility and general business uncertainty. As also outlined previously, the business transition toward a more software focused business will take longer than expected.

In the first half of 2018, Napatech has implemented a cost reduction program to ensure investment focus on growth initiatives until revenues improve as expected in the second half of 2018. As a result, cash break even revenue is reduced from 10 MUSD to 8 MUSD on a quarterly basis as from the beginning of 2019.

With new equity of 40 MNOK and the company's baseline case, Napatech expects to be fully funded throughout 2019 and to become cash generating towards the end of 2019. For revenues in the lower end of the 2018 revenue range the company will make cost optimizations to counteract the revenue shortfall.

2018 guidance for the company is the following:

- Sales of 18 to 23 MUSD
- Gross margin around 68%

The initiatives established during 2017 and being executed on during 2018 demonstrate the ongoing transition with our customers from a hardware-centric to a software-centric world of software defined networking. As a result of the changes that the markets, customers and Napatech are going through, the long-term outlook is exceedingly bright as Napatech products and services become applicable to not only our current, but also new market segments. In other words, Napatech will serve an increasing addressable market going forward. Thus, as an established leader in FPGA technology, Napatech believes that it will see renewed and increased growth at the other side of the current transition.

#### Disclaimer

This report contains statements regarding the future in connection with Napatech growth initiatives, profit figures, outlook, strategies and objectives. In particular, the section Outlook for 2018 contains forward-looking statements regarding the Group's expectations. All statements regarding the future are subject to inherent risks and uncertainties, and many factors can lead to actual profits and developments deviating substantially from what has been expressed or implied in such statements.

Oslo, August 14, 2018

The Board of Directors of Napatech A/S

## INTERIM CONSOLIDATED INCOME STATEMENT

For the period ended 30 June 2018

DKK'000	Note	2 <sup>nd</sup> Quarter		YTD June	
		2018	2017	2018	2017
Revenue	3	24,723	56,462	47,021	114,012
Costs of goods sold		(7,478)	(16,483)	(14,708)	(32,259)
Gross profit		17,245	39,979	32,313	81,753
Research and development cost		(5,182)	(3,923)	(8,930)	(7,644)
Selling and distribution expenses		(17,583)	(17,194)	(35,969)	(37,433)
Administrative expenses	4	(10,638)	(9,290)	(19,379)	(17,722)
Operating profit before depreciation and amortisation (EBITDA)		(16,158)	9,572	(31,965)	18,954
Depreciation and amortisation		(11,837)	(9,520)	(22,397)	(18,970)
Operating profit / (loss) (EBIT)		(27,995)	52	(54,362)	(16)
Finance income		-	-	-	-
Finance costs		1,232	(4,318)	(512)	(6,242)
Profit / (loss) before tax		(26,763)	(4,266)	(54,874)	(6,258)
Income tax		5,888	939	12,072	1,377
Profit / (loss) for the period		(20,875)	(3,327)	(42,802)	(4,881)
Earnings per share:	5				
Basic, DKK		(0.87)	(0.14)	(1.79)	(0.21)
Diluted, DKK		(0.85)	(0.14)	(1.74)	(0.21)

## INTERIM CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the period ended 30 June 2018

DKK'000	Note	2 <sup>nd</sup> Quarter		YTD June	
		2018	2017	2018	2017
Loss for the period		(20,875)	(3,327)	(42,802)	(4,881)
Other comprehensive income to be reclassified to profit or loss in subsequent periods:					
Exchange differences on translation of foreign operations		252	(233)	136	(235)
Net movement on cash flow hedges		(5,414)	6,620	(5,414)	6,622
Income tax effect		-1,191	(1,456)	1,191	(1,456)
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		(3,971)	4,931	(4,087)	4,931
Total comprehensive income for the period		(24,846)	1,604	(46,889)	50

## INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June 2018

### ASSETS

DKK'000	Note	30 June 2018	31 December 2017	30 June 2017
Development projects, completed		83,493	68,416	61,443
Development projects, in progress		32,470	46,342	45,334
Patents		5,248	5,412	5,676
Other intangible assets		23	50	133
<b>Intangible assets</b>	<b>6</b>	<b>121,234</b>	<b>120,220</b>	<b>112,586</b>
Plant and equipment		4,020	5,166	5,304
Office improvements		825	1,079	1,376
<b>Tangible assets</b>	<b>7</b>	<b>4,845</b>	<b>6,245</b>	<b>6,680</b>
Deferred tax asset		5,912	-	-
Leasehold deposits		2,415	2,283	2,294
<b>Other non-current assets</b>		<b>8,327</b>	<b>2,283</b>	<b>2,294</b>
<b>Non-current assets</b>		<b>134,406</b>	<b>128,748</b>	<b>121,560</b>
Inventories		40,119	36,124	38,511
Trade receivables	8	29,123	51,938	55,140
Other receivables	8	3,129	3,899	3,382
Income tax receivable	8	5,500	5,500	2,231
Derivative financial instruments	9	-	-	5,309
Cash and cash equivalents		1,628	39,967	33,997
<b>Current assets</b>		<b>79,499</b>	<b>137,428</b>	<b>138,570</b>
<b>Total assets</b>		<b>213,905</b>	<b>266,176</b>	<b>260,130</b>

## INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June 2018

### EQUITY AND LIABILITIES

DKK'000	Note	30 June 2018	31 December 2017	30 June 2017
Share capital	10	5,981	5,969	5,953
Share premium	10	220,405	219,729	217,584
Foreign currency translation reserve		127	(9)	275
Other reserves		1,104	6,361	63,961
Retained earnings		(90,432)	(48,883)	(81,620)
<b>Equity</b>		<b>137,185</b>	<b>183,167</b>	<b>206,153</b>
Deferred tax liability		-	7,425	7,657
Interest-bearing loans and borrowings		-	-	15,000
<b>Non-current liabilities</b>		<b>-</b>	<b>7,425</b>	<b>22,657</b>
Interest-bearing loans and borrowings		45,801	35,109	-
Trade payables		11,313	26,130	18,275
Other payables		13,739	13,855	12,500
Derivative financial instruments	9	5,414	-	-
Provisions		453	490	545
<b>Current liabilities</b>		<b>76,720</b>	<b>75,584</b>	<b>31,320</b>
<b>Total liabilities</b>		<b>76,720</b>	<b>83,009</b>	<b>53,977</b>
<b>Total equity and liabilities</b>		<b>213,905</b>	<b>266,176</b>	<b>260,130</b>

## INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the period ended 30 June 2018

DKK'000	Share capital	Share premium	Foreign currency translation reserve	Share based payment reserve	Cash flow hedge reserve	Retained earnings	Total equity
At 1 January 2017	5,916	216,429	510	7,611	(1,025)	(25,032)	204,409
Profit / (loss) for the period	-	-	-	-	-	(1,554)	(1,554)
Exchange differences on translation of foreign operations	-	-	(2)	-	-	-	(2)
Cash flow hedges	-	-	-	-	2	-	2
Income tax effect	-	-	-	-	-	-	-
Total comprehensive income	-	-	(2)	-	2	(1,554)	(1,554)
Issue of shares	37	1,155	-	-	-	-	1,192
Reversal, exercised and lapsed share options	-	-	-	-	-	-	-
Share-based payments	-	-	-	289	-	-	289
Total transactions with shareholders	37	1,155	-	289	-	-	1,481
At 31 March 2017	5,953	217,584	508	7,900	(1,023)	(26,586)	204,336
Profit / (loss) for the period	-	-	-	-	-	(3,327)	(3,327)
Exchange differences on translation of foreign operations	-	-	(233)	-	-	-	(233)
Cash flow hedges	-	-	-	-	6,620	-	6,620
Income tax effect	-	-	-	-	(1,456)	-	(1,456)
Total comprehensive income	-	-	(233)	-	5,164	(3,327)	1,604
Issue of shares	-	-	-	-	-	-	-
Reversal, exercised and lapsed share options	-	-	-	-	-	-	-
Share-based payments	-	-	-	213	-	-	213
Total transactions with shareholders	-	-	-	213	-	-	213
At 30 June 2017	5,953	217,584	275	8,113	4,141	(29,913)	206,153

## INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the period ended 30 June 2018

DKK'000	Share capital	Share premium	Foreign currency translation reserve	Share based payment reserve	Cash flow hedge reserve	Retained earnings	Total equity
At 1 January 2018	5,969	219,729	(9)	6,361	-	(48,883)	183,167
Profit / (loss) for the period	-	-	-	-	-	(21,927)	(21,927)
Exchange differences on translation of foreign operations	-	-	(116)	-	-	-	(116)
Cash flow hedges	-	-	-	-	-	-	-
Income tax effect	-	-	-	-	-	-	-
Total comprehensive income	-	-	(116)	-	-	(21,927)	(22,043)
Issue of shares	12	366	-	-	-	-	378
Reversal, exercised and lapsed share options	-	310	-	(994)	-	684	-
Share-based payments	-	-	-	264	-	-	264
Total transactions with shareholders	12	676	-	(730)	-	684	642
At 31 March 2018	5,981	220,405	(125)	5,631	-	(70,126)	161,766
Profit / (loss) for the period	-	-	-	-	-	(20,875)	(20,875)
Exchange differences on translation of foreign operations	-	-	252	-	-	-	252
Cash flow hedges	-	-	-	-	(5,414)	-	(5,414)
Income tax effect	-	-	-	-	1,191	-	1,191
Total comprehensive income	-	-	252	-	(4,223)	(20,875)	(24,846)
Issue of shares	-	-	-	-	-	-	-
Reversal, exercised and lapsed share options	-	-	-	(569)	-	569	-
Share-based payments	-	-	-	265	-	-	265
Total transactions with shareholders	-	-	-	(304)	-	569	265
At 30 June 2018	5,981	220,405	127	5,327	(4,223)	(90,432)	137,185



## INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS

For the period ended 30 June 2018

DKK'000	Note	2 <sup>nd</sup> Quarter		YTD June	
		2018	2017	2018	2017
Operating activities					
Profit / (loss) before tax		(26,763)	(4,266)	(54,874)	(6,258)
Adjustments to reconcile profit before tax to net cash flows:					
Finance income		-	-	-	-
Finance costs		(1,232)	4,318	512	6,242
Amortisation, depreciation and impairment	6, 7	11,837	9,520	22,397	18,970
Share-based payment expense		265	213	529	502
Working capital adjustments:					
Change in inventories		(564)	(5,660)	(3,995)	(19,836)
Change in trade and other receivables		(130)	(7,822)	23,322	16,368
Change in trade and other payables and provisions		(2,277)	(5,630)	(14,631)	(10,908)
Cash flows from operating activities		(18,864)	(9,327)	(26,740)	5,080
Cash flow hedges in financial items					
Interest received		-	(719)	-	(1,132)
Interest paid		(374)	(71)	(746)	(134)
Income tax received, net		11	(950)	(74)	(950)
Net cash flows from operating activities		(19,227)	(11,067)	(27,560)	2,864
Investing activities					
Purchase of tangible assets	7	(2)	(316)	(425)	(2,922)
Investments in intangible assets	6	(10,401)	(12,299)	(21,576)	(23,938)
Investments in leasehold deposits		139	(18)	132	(18)
Net cash used from investing activities		(10,264)	(12,633)	(21,869)	(26,878)
Financing activities					
Issue of shares	10	-	-	378	1,192
Increase of borrowings		10,801	10,000	10,692	10,000
Net cash flows from financing activities		10,801	10,000	11,070	11,192
Net change in cash and cash equivalents		(18,690)	(13,700)	(38,359)	(12,822)
Net foreign exchange difference		144	729	20	(132)
Cash and cash equivalents at the beginning of the period		20,174	46,968	39,967	46,951
Cash and cash equivalents at the end of the period		1,628	33,997	1,628	33,997

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 1 SIGNIFICANT ACCOUNTING POLICIES

The interim consolidated financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting, as adopted by the EU and additional Danish disclosure requirements for listed companies.

The accounting policies are, except for the following, consistent with those applied to the consolidated financial statements for 2017.

The consolidated financial statements for 2017 contain a full description of accounting policies.

#### **New standards, interpretations and amendments adopted by the Group**

With effect as of 1 January 2018 Napatech A/S has adopted the following standards, interpretations and amendments:

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

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 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:

- Focus on identifying the performance obligations in a contract and determine if the goods or services are distinct.
- 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.
- Considerations on how to identify the variable considerations in a contract.

The Group has adopted IFRS 15 using the cumulative effect method, but as the implementation of IFRS 15 has not had significant effect on the Group's financial statements, as revenue recognition under IFRS 15 is already in line with the Group's current revenue recognition policies, no effect has been recognised in equity 1 January 2018. This is due to the fact that the Group's sales types which primarily consist of goods for resale and finished goods and there are no complex discount agreements, variable considerations or other elements that could result in significant reversals of revenue already recognized.

IFRS 9 Financial instruments replaces IAS 39 Financial Instruments: Recognition and Measurement bringing together all three aspects of the accounting for financial instruments: classification and measurement, impairment and hedge accounting. As there is no significant impact on recognition and measurement for the Group, no effect has been recognised in equity 1 January 2018. That is due to the fact, that the Group on a historical basis has experienced very low losses on Trade receivables due to the fact that the Trade receivables is towards large companies with high solvency ratio.

#### **New and amended standards and interpretations**

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 2019. New and amended standards are expected to be implemented by their effective dates. The following standard is expected to affect Napatech A/S' future annual reports:

- IFRS 16 Leases

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

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.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Group has operating leases with minimum lease payments of approximately DKK 7,581 thousand corresponding to 3.5% of the Group's assets. Based on analyses of the Group's 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 and interim reports.

#### **The interim consolidated financial statements**

The interim 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 interim financial statements of the subsidiaries are prepared for the same reporting period as the parent company interim financial statements, using consistent accounting policies. The interim consolidated financial statements are prepared as a consolidation of the parent company's and the subsidiaries' interim financial statements, eliminating all intra-group balances, transactions, unrealized gains and losses and dividends.

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

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

### 2 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the interim consolidated financial statements requires the management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities.

The accounting judgements, estimates and assumptions that management make are the same for these interim consolidated financial statements as for the consolidated financial statements for 2017.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 3 OPERATING SEGMENTS

#### 2<sup>nd</sup> Quarter 2018:

DKK'000	EMEA	NAM	APAC	Consolidated
Revenue				
Total revenue	13,579	17,367	512	31,458
Inter-segment	(6,735)	-	-	(6,735)
Revenue, external customers	6,844	17,367	512	24,723
Cost of goods sold	(1,910)	(5,420)	(148)	(7,478)
Gross profit	4,934	11,947	364	17,245

#### 2<sup>nd</sup> Quarter 2017:

DKK'000	EMEA	NAM	APAC	Consolidated
Revenue				
Total revenue	45,946	46,534	1,506	93,986
Inter-segment	(37,524)	-	-	(37,524)
Revenue, external customers	8,422	46,534	1,506	56,462
Cost of goods sold	(2,234)	(13,983)	(266)	(16,483)
Gross profit	6,188	32,551	1,240	39,979

#### Explanation of abbreviations

EMEA	= Europe, Middle East and Africa
NAM	= Northern America
APAC	= Asia and Pacific

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 3 OPERATING SEGMENTS

YTD June 2018:

DKK'000	EMEA	NAM	APAC	Consolidated
Revenue				
Total revenue	17,824	28,585	2,070	48,479
Inter-segment	(1,458)	-	-	(1,458)
Revenue, external customers	16,366	28,585	2,070	47,021
Cost of goods sold	(4,139)	(10,045)	(524)	(14,708)
Gross profit	12,227	18,540	1,546	32,313

YTD June 2017:

DKK'000	EMEA	NAM	APAC	Consolidated
Revenue				
Total revenue	90,841	89,978	6,570	187,389
Inter-segment	(73,377)	-	-	(73,377)
Revenue, external customers	17,464	89,978	6,570	114,012
Cost of goods sold	(4,057)	(26,870)	(1,332)	(32,259)
Gross profit	13,407	63,108	5,238	81,753

Explanation of abbreviations

EMEA	= Europe, Middle East and Africa
NAM	= Northern America
APAC	= Asia and Pacific

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 4 SHARE-BASED PAYMENTS

Employees and members of the management in both the parent company and the US-based subsidiary are eligible 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 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 concluded 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 issued 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

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 issued 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.



## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 4 SHARE-BASED PAYMENTS (CONTINUED)

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 split 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 period 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.

Based on the same decision made on General Assembly in April 2016 to issue 400,000 share options, the Board of Directors issued 150,000 share options in May 2017 with the nominal value of DKK 0.25 at an exercise price of NOK 24,50 (DKK 19.41). The share options' life time is 5 years, where the share options holders are subject to a lock-up period 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.

Based on the same decision made on General Assembly in April 2016 to issue 400,000 share options, the Board of Directors issued the remaining share options in November 2017 with the nominal value of DKK 0.25 at an exercise price of NOK 19.00 (DKK 14.90). The share options' life time is 5 years, where the share options holders are subject to a lock-up period 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 all issues based on the 2016 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 INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 4 SHARE-BASED PAYMENTS (CONTINUED)

Share options	Management		Others		Total	
	Number	Average exercise price (DKK)	Number	Average exercise price (DKK)	Number	Average exercise price (DKK)
At 1 January 2018	793,200	11.77	664,568	11.54	1,457,768	11.66
Exercised / expired during the period	(109,548)	8.90	(124,000)	11.28	(233,548)	10.16
At 30 June 2018	683,652	12.23	540,568	11.60	1,224,220	11.95
Exercisable at 30 June 2018	372,895	8.75	315,679	9.34	688,574	9.02
At 1 January 2017	714,548	8.41	700,436	10.71	1,414,984	8.82
Granted during the period	150,000	19.41	-	-	150,000	19.41
Exercised / expired during the period	(87,396)	8.00	(60,868)	8.00	(148,264)	8.00
At 30 June 2017	777,152	11.13	639,568	11.35	1,416,720	11.23
Exercisable at 30 June 2017	455,756	8.38	326,857	8.45	782,613	8.41

In the period ended 30 June 2018, no share options were exercised and 93,500 lapsed (period ended 30 June 2017: no share options were exercised or lapsed).

The following shows the exercise price of the outstanding share options and warrants:

Number of share options	As at 30 June 2018	As at 30 June 2017
Exercise price DKK 8.00	433,552	667,052
Exercise price DKK 10.75	336,668	362,668
Exercise price DKK 12.53	92,000	92,000
Exercise price DKK 18.04	102,000	145,000
Exercise price DKK 19.41	150,000	150,000
Exercise price DKK 14.90	110,000	-
Total number of outstanding stock options	1,224,220	1,416,720

The weighted average of the remaining contractual period of the outstanding share options from the 2014 share options program at 30 June 2018 is 1 year and 3 months (at 30 June 2017: 2 years). The weighted average of the remaining contractual period of the outstanding share options from the 2016 share options program at 30 June 2018 is 3 years and 9 months (at 30 June 2017: 4 years).

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 4 SHARE-BASED PAYMENTS (CONTINUED)

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, 2016 and 2017 was estimated on the date of grant using the following assumptions:

	December 2013	May 2014	February 2016	August 2016	May 2017	November 2017
Volatility	47.92%	43.53% - 44.94%	49.00%	49.00%	50.50%	47.30% - 48.40%
Risk-free interest rate	1.65%	1.70% - 2.00%	0.50% - 0.60%	0.53% - 0.63%	0.80% - 1.10%	0.70% - 1.00%
Exercise price (DKK)	8.00	10.75	12.53	18.04	19.41	14.90
Exercise period (years)	2.27	3.00-5.00	3.00-5.00	3.00-5.00	3.00-5.00	3.00-5.00
Number of options	520,700	404,000	92,000	145,000	150,000	105,000

The volatility is calculated based on a peer group of seven 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 2<sup>nd</sup> quarter of 2018, the Group has recognized DKK 265 thousand of share-based payment expense in the income statement (2<sup>nd</sup> quarter 2017: DKK 213 thousand).

### 5 EARNINGS PER SHARE

DKK'000	2 <sup>nd</sup> Quarter		YTD June	
	2018	2017	2018	2017
Net income attributable to equity holders of the parent company for basic earnings and the effect of dilution	(20,875)	(3,327)	(42,802)	(4,881)

DKK'000	2 <sup>nd</sup> Quarter		YTD June	
	2018	2017	2018	2017
	Thousand	Thousand	Thousand	Thousand
Weighted average number of shares for basic earnings per share	23,923	23,812	23,915	23,763
Effect of dilution:				
Share options	667	-	667	-
Weighted average number of shares adjusted for the effect of dilution (nominal value of DKK 0.25)	24,590	23,812	24,582	23,763

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 6 INTANGIBLE ASSETS

DKK'000	Development projects, completed	Development projects, in progress	Patents	Other intangible assets	Total
Cost at 1 January 2018	229,165	46,342	9,791	2,139	287,437
Additions in the period	-	21,409	167	-	21,576
Disposals in the period	-	(373)	-	-	(373)
Transfers in the period	34,908	(34,908)	-	-	-
Cost at 30 June 2018	264,073	32,470	9,958	2,139	308,640
Accumulated amortization and impairment at 1 January 2018	160,749	-	4,379	2,089	167,217
Amortization for the period	19,831	-	331	27	20,189
Accumulated amortization and impairment at 30 June 2018	180,580	-	4,710	2,116	187,406
Carrying amount at 30 June 2018	83,493	32,470	5,248	23	121,234

Within the completed development projects there are three material development projects with carrying amounts of DKK 13,393 thousand, DKK 6,835 thousand and DKK 5,508 thousand at 30 June 2018 respectively (30 June 2017: nil, DKK 8,836 thousand and DKK 9,181 thousand respectively). The aim of the first project is to develop the next generation of our network recording platform, the aim of the second project is to develop a new 2 x 100G accelerator and the aim of the third project is to develop a new 1 x 100G accelerator. The remaining amortisation periods of these three projects are 2 years and 6 months, 3 years and 5 months and 1 year and 6 months respectively.

Within the inprocess development projects there is one material development project with a carrying amount of DKK 14,359 thousand. The aim of the project is to develop our new product aimed at the virtualization market primarily focused towards telecom and cloud providers. The project is not yet completed and therefore has not been amortized.

The annual impairment test for the intangible assets will be performed at 31 December 2018. As per 30 June 2018 the management has assessed, that there were no indications of impairment in relation to the Group's intangible assets in the reporting period.

### 7 TANGIBLE ASSETS

DKK'000	Plant and equipment	Leasehold improvements	Total
Cost at 1 January 2018	33,400	5,105	38,505
Additions in the period	425	-	425
Disposals in the period	(349)	-	(349)
Currency adjustment	-	11	11
Cost at 30 June 2018	33,476	5,116	38,592
Accumulated depreciation at 1 January 2018	28,234	4,026	32,260
Depreciation for the period	1,532	254	1,786
Disposals in the period	(349)	-	(349)
Currency adjustment	39	11	50
Accumulated depreciation at 30 June 2018	29,456	4,291	33,747
Carrying amount at 30 June 2018	4,020	825	4,845

The annual impairment test for the tangible assets will be performed at 31 December 2018. As per 30 June 2018 the management has assessed, that there were no indications of impairment in relation to the Group's tangible assets in the reporting period.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 8 TRADE AND OTHER RECEIVABLES

DKK'000	30 June 2018	30 June 2017
Receivables recognized in the consolidated statement of financial position:		
Trade receivables	29,123	55,140
Other receivables	3,129	3,382
Income tax receivable	5,500	2,231
<b>Total current receivables</b>	<b>37,752</b>	<b>60,753</b>

The provision for bad and doubtful receivables is as follows:

DKK'000	2018	2017
At 1 January	1,360	2,103
Change in the period	41	(162)
<b>At 30 June</b>	<b>1,401</b>	<b>1,941</b>

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

DKK'000	30 June 2018	30 June 2017
Not past due	17,766	50,901
Past due less than 30 days	4,848	2,387
Past due between 30 and 60 days	1,599	80
Past due between 60 and 90 days	544	332
Past due after 90 days	4,366	1,440
<b>Total maximum credit risk</b>	<b>29,123</b>	<b>55,140</b>

### 9 DERIVATIVE FINANCIAL INSTRUMENTS

DKK'000	30 June 2018	30 June 2017
Derivative financial instruments at fair value, assets / (liabilities)	(5,414)	5,309

Derivative financial instruments are classified as Level 2 instruments in accordance with the IFRS fair value hierarchy. The fair value of the derivative financial instruments is based on observable market data, such as forward exchange rates. The fair value of derivative financial instruments approximates their carrying values.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### 10 ISSUED SHARE CAPITAL AND RESERVES

Authorised shares	2018	2017
	Thousand	Thousand
Ordinary shares of DKK 0.25 each at 1 January	23,877	23,664
Increase in ordinary shares DKK 0.25 each	46	148
Ordinary shares of DKK 0.25 each at 30 June	23,923	23,812

### 11 COMMITMENTS AND CONTINGENCIES

#### Collaterals

The Group has issued a floating charge in the amount of DKK 30 million secured on receivables, inventories and equipment as collateral for bank debt.

#### Operating lease commitments

The Groups' operating lease commitments relate to cars and office facilities. Future minimum payments under operating leases at 30 June 2018 are DKK 7,581 thousand.

#### Finance lease commitments

The Groups has repaid all finance lease commitments relating to the equipment used in the research and development department.



# Napatech A/S

Tobaksvejen 23A, 1  
DK-2860 Søborg  
Denmark

Phone: +45 4596 1500

[www.napatech.com](http://www.napatech.com)