26 February 2019

ASX ANNOUNCEMENT

Senetas Corporation Limited Half-Year Results Announcement For the six months to 31 December 2018

- 100Gbps sales growing, with new customers secured
- Votiro transaction finalised and 1st tranche of investment completed
- Gemalto distribution agreement signed for SureDrop, with pilots underway
- R&D pipeline building value for the future
- Strong balance sheet position and no debt

Senetas Corporation Ltd (ASX: SEN) (Senetas / the Company), announces its results for the six months ended 31 December 2018 (HY2019).

HY2019 financial highlights

Half year ended 31 December 2018 ($000's)	HY19 Post AASB15	HY19 Pre AASB15	HY18 Pre AASB15
Revenue from ordinary activities	9,862	10,123	10,301
Gross profit	7,494	7,756	8,190
Other income	303	303	215
PBT from ordinary activities	1,417	1,679	2,394
Write down of SAT	(1,893)	(1,893)	-
Share of loss of associate	(323)	(323)	
Statutory profit before tax	(799)	(537)	2,394
Tax expense	(385)	(256)	(754)
Net profit after tax	(1,184)	(794)	1,640

HY2019 results reflect first time application of the new AASB15 (*Revenue from Contracts with Customers*). HY2018 results were not subject to the new AASB15 and have not been restated. Pre AASB15 results for HY2019 are used in this release for the purposes of comparison to HY2018 results.

SENETAS CORPORATION LIMITED
312 Kings Way, South Melbourne, VIC, 3205, Australia
T +61 (03) 9868 4555 F +61 (03) 9821 4899 E info@senetas.com
www.senetas.com

- Operating revenue and net profit before tax (NPBT) was reduced by $0.26 million as a result of the first time application of new AASB15
- Pre AASB15 operating revenue was slightly below the prior period (HY2018: $10.30 million)
- Gross margin of 76% reflects increased sales of the higher cost 100Gbps encryptors
- The board of Senetas today confirmed with the Company's auditors the accounting treatment of its recent investment in Votiro Inc. The investment will be carried in Senetas's balance sheet as an investment in an associate, and its share of Votiro's loss for the period will be treated in the income statement as a share of loss of an associate. The accounting treatment will continue to be reviewed as Senetas transitions towards a majority interest in Votiro.
- Senetas's share of Votiro's losses for the period since Senetas made its investment in November 2018 of $0.32m was in line with expectations
- Pre AASB15 net loss before tax of $0.54 million includes a $1.89 million impairment of unlisted investments relating to the investment in SAT and the $0.32m share of the Votiro loss for the period since Senetas made its investment
- Pre AASB15 NPBT of $1.68 million prior to the SAT impairment and the share of Votiro's loss is at the high end of the guidance range announced in the market update released on 7 February 2019 (HY2018: $2.39 million)
- HY2019 expenses includes a re-measurement of contingent consideration relating to the earn out provisions of the agreement to acquire SureDrop in FY2017
- Strong balance sheet with $12.25 million of cash following the $6.37 million first tranche of the investment into Votiro and $4.00 million in relation to the FY2018 final and special dividends declared.

Commenting on the half year to 31 December 2018, Senetas CEO, Andrew Wilson, said: "The first half of FY2019 has seen good progress as we advance our vision to be the leading provider of security solutions, without compromising user experience or network performance.

"We completed the first tranche of our $US8 million in Votiro Cybersec, a leading Israeli content disarm and reconstruction (CDR) company. Votiro's patented CDR technology presents a significant opportunity for Senetas to expand its portfolio into a fast growing segment of the security market and to use its distribution relationships to accelerate Votiro's growth. Since completion in mid-November 2018, Votiro's pipeline is building and we look forward to updating the market with our full year results on Votiro's progress.

"The share of Votiro's loss at 31 December 2018 that was recognised in our HY2019 accounts was in line with our expectations of the performance of the business at the time of investment and in no way affects the confidence we have in the growth outlook for the business.

"Our new virtualised encryption products and SureDrop have undergone successful customer testing during the half, and Gemalto has agreed to distribute the SureDrop product. The next stage of product development is well advanced, to extend our virtual encryption products to public cloud environments and add multi-layer capability to our

hardware encryptors. This will significantly expand our product suite and addressable market.

"Early sales of the 100Gbps encryptor are tracking well and encouragingly they have also attracted 4 new customers that haven't previously purchased Senetas encryptors.

"The financial results for HY2019 reflect the first application of the new accounting standard AASB15 relating to the timing of recognition of revenue. AASB15 has had a negative impact on operating revenue reported in HY2019, however, underlying revenue prior to the impact of AASB15 was similar to the prior corresponding period.

"Disappointingly, some higher costs, the AASB15 changes, the impairment to our investment in Smart Antenna Technologies Ltd (SAT) and the share of Votiro's 31 December 2018 loss have resulted in a net loss after tax for the first half of FY2019. There is no impact on cash flows in comparison to the prior period.

"Senetas's balance sheet remains strong with no debt and $12.25 million of cash on hand at 31 December 2018. Pleasingly, Senetas's strong financial position and confidence in the business outlook allowed the board to declare a FY2018 final dividend and special dividend to shareholders during the half, the first dividends since the Company's comprehensive restructure in 2012."

Operational review

On a pre AASB15 basis, total operating revenue was marginally below the prior year. Revenue received from Senetas's global distribution partner Gemalto NV was in line with the prior period, with revenue from the ANZ region slightly lower. Good growth in 100Gbps sales in HY2019 was offset by lower sales of 10Gbps encryptors. The 100Gbps encryptor sales included 4 new customers that had not previously purchased Senetas encryptors.

HY2019 maintenance revenue was 36% of total revenue. This was slightly lower than FY2018 reflecting the previously announced transition of one of Senetas's key customers from Senetas SONET products to lower cost Senetas Ethernet products.

Gross margins were 76%, slightly lower than the prior period largely due to an increased proportion of sales from the higher cost 100Gbps encryptor. Margins on the 100Gbps encryptors are expected to increase over time as the cost of 100Gbps components reduces.

Sales of the 100Gbps encryptor during HY2019 have been encouraging, and the number of sales to new customers has highlighted its ability to attract important customers that haven't previously purchased Senetas encryption technologies.

The new virtualised products and SureDrop have undergone successful customer testing during HY2019 and feedback has been very positive. Senetas has recently signed an agreement with Gemalto in relation to the distribution of SureDrop and sales leads off the back of that agreement have already been encouraging.

Senetas's relationship with its global distribution partner Gemalto continues to strengthen, evidenced by Gemalto's recent adoption of the new virtualised technologies and SureDrop into its product portfolio. In addition, Senetas also has the partnership with ADVA in relation to the virtualised encryption technologies integrated into ADVA's Ensemble Connector network solutions. These relationships provide Senetas with strong

global distribution opportunities, as well as being important technology partnerships that have successfully developed unique security solutions for customers.

The SureDrop technology was acquired by Senetas in the second half of FY2017 on an earn out basis with no upfront consideration. With development of the SureDrop product complete, and sales now expected in the near term, Senetas has for the first time recognised a charge arising on re-measurement of contingent consideration in its P&L related to the SureDrop earn out provisions.

These new technologies, plus the benefit of expanded capabilities for Senetas's virtual products, and development of transport layer independence for hardware encryptors provide Senetas with a significantly expanded set of use cases and revenue growth opportunities.

R&D and new product development

R&D remains a significant source of value creation for Senetas. The major areas of R&D focus for FY2019 remain:

- Completion of the European certification process for Senetas's hardware encryptors;
- Further development of the virtualised encryption solutions to provide enhanced capabilities in public cloud environments; and
- Development of multi-layer capability for Senetas hardware encryptors

These projects are expected to increase R&D spend in the FY2019 year by between $0.5-$1.0 million over FY2018. The primary contributor to the increased R&D spend in FY2019 is the cost associated with European certification that will broaden the addressable market for Senetas products in that region.

Development of transport layer independence capabilities for Senetas's hardware products is expected to be completed before the end of FY2019, and enhanced capabilities for the virtualised encryption solutions is expected shortly thereafter.

The completion of these developments is expected to increase Senetas's addressable market for security solutions by more than 3 times and cover more than 85% of all network traffic.

Senetas does not expect any material financial impact from the new Australian R&D rules in effect from 1 July 2018.

Balance sheet and cash flow

Senetas' balance sheet remains strong with no debt and substantial cash reserves. Net assets reduced 20% to $19.00 million and the cash balance at 31 December 2018 was $12.25 million.

Net operating cash flow was negative $0.21 million in FY2019 reflecting higher cost of sales and an increase in Senetas's inventory level during the period.

Significant cash outflows during the period included the $6.37 million first tranche of the investment in Votiro and associated costs in November 2018, and the advance payment of $4.00 million into a dividend trust account in preparation for the FY2018 final and special dividends that were subsequently paid to shareholders on 4 January 2019.

The dividends reflect the Board's confidence in the Company's financial position and business outlook.

Outlook

Commenting on the Company's outlook, Mr Wilson said: "The past 2 years has seen Senetas transition from being solely a provider of hardware encryption products to becoming a trusted provider of high-assurance hardware and software cyber security solutions.

"With the development of our virtualised encryption solutions together with transport layer independence capabilities for both the virtual and hardware products we have significantly expanded our potential market opportunities beyond the specialist Layer 2 hardware encryption market with products that can now serve over 85% of all network traffic.

"Our relationship with Gemalto continues to strengthen and we continue to see opportunities arising from the merger of Thales and Gemalto once finalised. The new agreement with Gemalto for the distribution of SureDrop is another important development that we expect to contribute to revenue growth in the near term.

"The acquisition of a majority interest in Votiro also provides us with an exposure to the fast growing area of CDR technology which has application for all security conscious enterprises. With the assistance of Senetas's global business development resources and global distribution relationships we expect Votiro can grow revenue strongly over the next 12 months as distribution expands beyond its core Asian markets.

"Revenue will be driven largely by our traditional hardware encryption products until the new virtual, SureDrop and transport layer independent hardware products begin to develop sales momentum in FY2020 and beyond. Our 100Gbps devices developed some good sales growth in HY2019 and we are optimistic that it will continue to attract additional new customers to Senetas technologies, however, profit in FY2019 will continue to be impacted by higher costs, primarily related to Senetas's increased investments in R&D during the year.

Impact of AASB15

In accordance with the new standard, the Company is required to estimate and recognise the revenue expected to be earned from customer contracts, rather than waiting for the actual end sale before recognising the revenue.

The net accounting impact of the new AASB15 on Senetas's results in HY2019 is to reduce revenue and net profit before tax by $0.26m compared to what would have been recognised under the previous accounting standard. The reduction in HY2019 revenue is a result of lower inventory held by Gemalto at 31 December 2018 compared to the inventory Gemalto held at 30 June 2018.

Refer note 2.2(a) of the half-year financial report for further details.

Unlisted investments

Smart Antenna Technologies Ltd. (SAT)

Senetas announced on 16 January 2019 that it expected to recognise an impairment to the carrying value of its investment in SAT. Senetas holds a 5.52% interest in SAT that was initially acquired in December 2016.

The major shareholder and primary financier of SAT advised its intention to not proceed with additional funding due to disagreements with SAT management over future strategy. As a result, the board of SAT resolved to put the business into the hands of administrators.

Given the level of uncertainty surrounding the carrying value of the investment the board has resolved to write down the carrying value of the investment in SAT from $1.89 million to nil.

Investor and analyst conference call

The Company will be holding an investor and analyst conference call in relation to the HY2019 results at 11.00AM AEDT on Wednesday, 27 February 2019.

Dial in details: Participants can dial +61 2 9007 3187 or 1800 558 698 (toll free) to join the call. When prompted, please enter Conference ID: [654117]

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For further information please contact:
Chris Knorr
Market Eye
M: +61 417 033 623
E: chris.knorr@marketeye.com.au

ABOUT SENETAS CORPORATION LIMITED

Senetas, an Australian public listed company (ASX: SEN), is a leading developer of network data encryption and other security solutions for enterprise, government, defence and technology service providers. From certified high-assurance encryption hardware and virtualised encryption, to the most secure file sharing application providing data sovereignty control, all Senetas solutions are based on the same leading security, high performance and crypto-agile platform.

Senetas encryption solutions leverage state-of-the-art encryption key management and crypto-agility by design, providing long-term data protection in a post-Quantum computing world. They share the same designed-in data protection without compromising network and application performance or user experience.

- CN Series – certified high-assurance hardware encryptors for core IT and network infrastructure.

  The CN Series features crypto-agility, uncompromising performance and certifications by multiple independent authorities (C.C., FIPS and NATO), providing Senetas customers with the added confidence that CN Series solutions are state-of-the-art and provide maximum security essential for today's infrastructure.

- CV Series – strong virtualised encryption for large-scale extended and virtualised WANs.

  The CV Series virtual encryptor provides >1Gbps performance and is transport Layer agnostic. The CV Series enables rapid scalability, flexibility and cost-effective data protection, all the way to the virtual edge. The CV Series encryptor uses the same high-assurance Senetas CN Series hardware encryption platform.

- SureDrop – the most secure, "box"-type file sharing application with 100% data location control.

  SureDrop leverages Senetas's state-of-the-art encryption security to provide secure collaboration and data sovereignty. SureDrop provides the same Senetas crypto-agility, scalability and ease of use as the network data encryption solutions. It is also an ideal solution for service providers' large-scale deployment as a "Security-As-A-Service" customer solution.

Senetas encryptors have been trusted to protect much of the world's most sensitive information for nearly 20 years. They are used to protect everything from government and defence data and secrets, to intellectual property and business data, to financial transactions, CCTV networks, SCADA critical infrastructure control systems and citizen identities.

Senetas CN and CV Series encryptors provide optimised encryption security for everything from modest bandwidth requirements of 10Mbps to the ultra-fast 100Gbps networks required for aggregated Big Data, Cloud and data centre applications.

Senetas encryption solutions are used in more than 35 countries. Senetas encryptors are distributed and supported internationally by Gemalto, the world's largest data security company, under its SafeNet Identity and Data Protection products.

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