

8 December 2009

Alternative Networks plc

Preliminary Results for the year to 30 September 2009

Cash is king in turbulent times

	2009 £'000	2008 £'000	Change %
Statutory performance			
Turnover	89,676	93,707	-4%
Operating profit	7,031	8,755	-20%
EBITDA*	8,907	10,750	-17%
Profit before taxation	7,115	8,901	-20%
Earnings per share			
- basic	12.0p	14.3p	-16%
- diluted	11.6p	13.7p	-15%
Dividend per share ****	5.1p	4.6p	11%
Free cash flow per share*****	18.6p	16.8p	11%
Underlying performance			
Adjusted EBITDA **	9,642	11,053	-13%
Adjusted Operating profit **	8,986	10,433	-14%
Adjusted Earnings per share ***			
- basic	14.4p	16.5p	-13%
- diluted	13.9p	15.8p	-12%

* Earnings before interest, taxation, depreciation and amortisation.

** Adjustments for operating profit (and EBITDA) relate to amortisation of acquired intangible assets, share option costs and impairment to freehold property, as set out in Note 9.

*** Adjusted earnings per share are based on profits as set out in Note 9.

**** Dividend per share is the interim dividend paid and the final dividend proposed, divided by the number of shares in issue at the year end.

***** Free cash flow per share is calculated as the net cash inflow after taxation, capital expenditure, and net interest, but before cash flows from financing activities and acquisitions, divided by the weighted number of shares in issue in the year per Note 4.

Highlights

- Sales of £90m down 4%, as the economic impact of lower customer spending more than offsets market share gains.
- Gains in market share:
 - Mobile subscribers increased 6% to 55,299 (2008: 51,990).
 - Office based customers' lines/channels increased 29% to 67,587 (2008: 52,262).
 - System maintenance revenues increased 5% to £4.4m (2008: £4.2m).
 - High spending customers taking 3 or more products increased by 10%
- Swift cost reductions lead to £1m lower operating costs in the second half of the year, and underlying operating profits reduced 14% to £9.0m (2008: £10.4m).
- Strong balance sheet and excellent cash generation:
 - Free cash flow of £7.9m (2008: £7.6m).
 - Strong cash conversion at 110% adjusted EBITDA (2008: 94%)
 - Net funds of £8.1m (2008: £3.2m), after returning £1.3m surplus cash via buy backs.
- Proposed full year dividend increase of 11% to 5.1p supported by strong cash flow and high visibility of earnings (2008: 4.6p).

James Murray, CEO of Alternative Networks, commented:

“We finished the year in a strong position, after weathering a fierce downturn in customer spending, which began in the first quarter of 2009.

“Tight control of costs and strong cash management have been key to our ability to manage our way through this downturn. We continued to grow market share and ended the year meeting our revised targets, with the balance sheet stronger than ever and with a high degree of revenue visibility for 2010.

“Looking forward, we intend to focus on growing market share and increasing our revenue streams from different sources. The acquisition of Aurora Kendrick James is of significant strategic importance in this regard. It accelerates the development of our customer service portal, enhancing the existing service offering and creating opportunities for new revenue streams by working with third party telecoms and IT services providers.

“We remain cautious but optimistic, especially as we are better placed than previously to take advantage of any improvement in market conditions. We will also continue to examine value adding acquisition opportunities, where they promise clear shareholder value.”

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Chairman's Statement

Alternative Networks' performance for the year as a whole has been very creditable, given how customer spending declined as the full impact of the economic downturn began to be felt. This resulted in a reduction in sales of 4%, from £93.7m to £89.7m. EBITDA was reduced from £10.8m in 2008 to £8.9m in the year.

More importantly, the business has continued to be strongly cash generative. Free cash flow actually increased year on year, and the Group ended the year with net funds of £8.1m, more than double the position of £3.2m a year earlier. This was after returning £3.4m of cash to shareholders by way of share buy backs and dividends.

The strong cash position and continued high visibility of earnings has enabled the Board to increase the proposed full year dividend by 11% to 5.1p.

In response to the difficult market conditions, the Group's management took prompt and sensible action. £2.5m of expected annualised cost savings were implemented. We retained most of our considerable direct sales force and a concerted effort was made in deriving additional revenues from existing customers and in keeping customer attrition low; and a number of significant new customers were signed up. In addition, the earlier investment in internal systems and the restructuring put in place in the previous year were well timed, as it provided the infrastructure to make the business leaner and more efficient, without detracting from the quality of service. All of this has enabled the Group to achieve its revised targets for the year, which is a tribute to the hard work and commitment of all staff.

Despite this environment, the Group was able to increase its market share, with the number of mobile subscribers increasing by 6% and office based connections up 29%. The Group's ability to cross-sell its offering of services was reflected by a 10% increase in high spending customers taking three or more products.

Since the year end, the Group completed the acquisition of Aurora Kendrick James ("AKJ"), whose billing software and products have been an important tool in maintaining high standards of customer service for the Group. Bringing AKJ in-house will protect a key part of the Group's intellectual property, as well as creating additional sources of revenue. This has already been demonstrated through the signing of a new contract with a major network operator to manage the billing and customer services of over fifty larger customers. AKJ should also enable more efficient integration of future acquisitions.

The outlook for the Group is positive. Market conditions remain challenging but stable. With a strong balance sheet, a committed management team and a sound and proven strategy, we are optimistic of a favourable outcome for the current year.

Kenneth McGeorge

Non-Executive Chairman

7 December 2009

Chief Executive's Report

Overview

We are pleased to present a review of another successful year for the Group, albeit framed by a difficult economic environment.

This has been a challenging period of trading for the Group, as average revenues of business customers have reduced as the economy has slowed. Due to the speed and depth of the slow down particularly since January and February 2009, the impact of this reduction in customer spend has more than outweighed the impact of new customer wins. Moreover, the benefits of the cost cutting initiatives implemented in the early spring only emerged in the second half. Throughout the period, the Group has continued to win market share and has generated very healthy cash returns, and the proposed increase in dividend reflects the Board's confidence in the underlying business.

Financial Results

Group sales decreased 4% to £89.7m (2008: £93.7m). The differing product sets' results are analysed further below. Market share gains are being made in each product grouping, but these have been more than offset by revenue reductions due to lower customer usage, particularly in mobile services, and continuing price reductions for existing clients.

Gross profit margins are in line with expectations at 34.4% (2008: 35.0%), allowing for lower usage of higher margin revenues, due to diminished customer spend. Margins per product set are reviewed in detail below.

Adjusted operating profit of the Group reduced by 14% to £9.0m (2008: £10.4m).

On a statutory basis, pre-tax profits decreased 20% from £8.9m to £7.1m, with operating profits decreasing 20% from £8.8m to £7.0m.

Cash generation continues to be very strong and differentiates the Group from many of its peers. Net cash generated from operations was £10.6m (2008: £10.3m) which was 110% of adjusted EBITDA in the period (2008: 94%). Free cash flow was £7.9m (2008: £7.6m) enabling the Group to return a further £1.3m to shareholders during the year through a general share buy back programme, and finished the year with £9.0m cash (2008: £4.2m).

Adjusted earnings per share fell 13% and 12% in basic and diluted earnings respectively to 14.4p and 13.9p respectively. Statutory earnings per share fell 16% from 14.3p to 12.0p. A detailed reconciliation is set out below in the financial and business review.

The Board has proposed a final dividend of 3.5p (2008: 3.1p), making a total of 5.1p for the year (2008: 4.6p), a growth of 11%, in line with our progressive dividend policy.

Strategy

The Group has persistently pursued its twin strategy of organic and acquisitive growth with a stated ambition to become the leading Converged Communications partner of choice for the UK's small and medium sized businesses.

Acquisitions

The Group has reviewed a number of acquisition opportunities in the year, especially in the IT and data services space. The Group entered into the second round in around five competitive tenders, withdrew interest on two and were outbid on the remainder, which demonstrates our refusal to overpay. Since the year end, on 31 October, we acquired the entire share capital of Aurora Kendrick James Limited ('AKJ'), currently

our billing services partner, for a maximum consideration of £5.5m; the initial consideration consisting of £3.75m cash and £0.8m through the issue of 707,076 ordinary shares. The AKJ group is based in Chatham, Kent and has approximately 50 staff, of which 25 are IT developers. In the year ended 31 July 2009, AKJ increased sales by 4% to £3.6m, and the group made a pre tax profit of £0.3m, and underlying EBITDA of £0.6m. The gross assets of the business were £2.3m. The acquisition is expected to be moderately earnings enhancing for the Group for the year ended 30 September 2010.

The deal is relatively small but strategically important for the Group. The rationale for the acquisition was set out in the original announcement on 2 November. Briefly summarised this was:

- The Group has used AKJ's software for almost 10 years. We have invested considerable resource in applying it to provide customers with a bespoke simple and efficient mechanism to access and control the billing and usage of their communications equipment. Bringing the software in house will protect the Group's intellectual property and guarantees exclusivity on key elements of the software that are important for customer attraction and retention.
- The acquisition will also accelerate the development of the Group's customer service portal, enhancing the existing service offering and creating opportunities for new revenue streams by working with third party telecoms and IT services providers.
- The acquisition provides a platform for potential new revenue streams working with third party telecoms and IT service providers. The Group intends to develop the portfolio of services and products that it can offer to European based telecoms and IT service providers, systems integrators, resellers and dealers, based on AKJ's platform. AKJ's current customers include over 50 communications and IT service providers and the combined portfolio of services and resources of the Group will create the opportunity for exciting new revenue streams for both the Group and AKJ's partners.

As ever, we remain focussed on acquisitions which are the right fit, and at the right price. We are confident that our strong balance sheet and net cash of over £4m as at the balance sheet date after funding the acquisition above, as well as our £12m undrawn bank debt facilities keeps us in a strong position in the year ahead.

Review of Organic Growth factors – update on Key Performance Indicators

The four key organic growth factors supporting our strategy remain:

Focus on larger customers in SME space

The target customer in the market for the Group remains the business customer who spends between £1,000 and £10,000 per month.

The underlying success of increasing the number of higher spending customers is shrouded by the economic downturn. Over the year, there has been a net reduction of 25 customers spending over £1,000 with the total number of group customers spending over £1,000 per month being reduced to 1,249 at 30 September 2009 from 1,274 at 30 September 2008 (restated to eliminate duplication of Echo network customers). This net reduction has been caused by price erosion and decreases in traffic during the year pushing many customers below the £1,000 spend threshold.

However, the underlying success can be evidenced by the increase in the number of higher spending customers taking three or more products. The number of these customers has increased 10% by 66 to 722 customers.

Cross-selling

The Group has made solid progress in cross-selling the product set. Of the total customer base at 30 September 2009, over 40% took more than one product (2008: 36%).

Of all customers spending more than £1,000 per month, 75% (2008: 70%) took more than one product and, most encouragingly, 58% (2008: 50%) took three products or more. Mobile services are currently treated as one product whether data, voice or ancillary services.

Reduction in churn

2009 was a challenging year for reducing churn. Our key metric of mobile network subscriber churn was increased from 16.4% in 2008 to 19.7% in 2009, as more customers switched networks in search of better deals, and were more discerning in disconnecting surplus lines as they reduced headcount. Nonetheless this result remains in the Group's long held target band of 16-20%. Stripping out the increase in customers who switched networks but stayed with us, being around 1,400 connections, the network churn number is closer to 17%.

We also monitor customer attrition by value. This was much steadier and remained at a low level of 15% as also achieved in 2008.

Product Development

Our organic growth depends on widening our share of our customers' communications spend and we rely on using our strategic partnerships to consistently deliver new growth opportunities.

During the past year, our suppliers have each tried to bring their own unified communications ("UC") products to market; we have spent a lot of time with them establishing which ones fit into our portfolio, how they integrate with existing infrastructure, and reviewing the return on investment.

UC products launched, trialled, or evaluated include:

Supplier	Product	Status
Avaya	One-X	Launched
Mitel	Series-X, Unified Communicator Advanced, and Dynamic Extension	Launched
Cable & Wireless	FMC	Trial
Vodafone	One-net	Evaluation

A number of SIP trunking and Hosted IP telephony propositions are also in trial phase.

We look forward to bringing more of these products to market as we continue to improve our UC offering, and offer deeper and more flexible integration to our customers.

In the data space, we launched our offering of Cisco products, registering as a select partner, and gaining the assistance of a new contracted partner specialising in the more advanced UC arena, we have won our first customer.

Mobile communication has continued to be an area of vendor development:

The Blackberry 8520 "Curve", a lower-priced edition of the popular 8900 device which shares many of the same features, was the first device to feature the more robust trackpad instead of the trackball. This device has been a great success due to the challenging economic conditions, and has allowed us to push Blackberry connections further down the food chain within our customers.

New improved smartphones from HTC and Nokia both offering mobile applications to field operators, combined with the impending availability of the Apple "i-phone" through most mobile networks, and the revised models of the Blackberry "Storm" and "Bold" should help drive further growth in the number of converged devices in our customer base and lead to increased data revenues.

Finally, a key focus has been on our customer billing and service portal. We launched a range of updates to Clarity™ our online billing, reporting and asset management tool. Most notably, we have developed the ability to separate out 'business' from 'personal' calls, and manage this process using a hosted database with automated sign off.

The Group has planned a 24 month development roadmap to bring many new services through an Alternative Networks' branded portal to corporate customers, including estate management, diagnostics, hosted on-line services, and on-line interactive customer services. The acquisition of AKJ is expected to help deliver these faster and more effectively.

Business resilience

Last year, we spent some time reviewing the key characteristics of what makes this business so resilient: firstly, our strong balance sheet, strong cash flow, and low fixed asset base. Second we provide business critical services to a diverse number of UK businesses in a wide variety of industries, Finally, there is good visibility of future revenue streams as customers' contracts typically last at least two years. We also discussed how our products would help our customers save money in a downturn. This was within the context of the Group having industry leading suppliers, and a strong management team that has consistently delivered organic growth over 10 years together. We set some targets for modest growth in sales and profits.

The resilience of our business model was truly tested in the financial year, following a fierce downturn in customer spend over January and February 2009, which has remained flat at best since then. We took appropriate action:

- We cut costs quickly to adjust to the broader economic conditions. Savings expected to be £2.5m over a full year were implemented without cutting too deep.
- We set some revised targets for the business, based around a cost improvement plan.
- We have continued to win new business and have grown market share at the underlying level in all our product sets, albeit somewhat more slowly than previously. Winning major new accounts like Nestor Healthcare plc and Parfumes Christian Dior (UK) Limited, together with developing multi-product accounts like the Welsh Ambulance Service, MacMillan Cancer Support, Smiths Gore and Weightman solicitors have helped keep revenues at close to last year's levels, as well as offering more potential in future years.
- We have managed to cross sell more products into our existing customer base, which is expected to improve loyalty.
- We improved relations with key suppliers and that has helped keep margins in line with expectations in spite of the worse mix of revenues due to lower voice and data usage charges.
- In August 2009, we decided to invest further in the growth of our public sector and health ("Blue Lights") teams, recruiting sales, pre-sales and engineering expertise.

As a result of the above, we were able to achieve our revised targets. Our strategy has not wavered, and as we come into another year which offers similar economic uncertainty, we have a leaner platform and a stronger sales and service proposition than we did 12 months ago.

Outlook

Since the year end, we have acquired AKJ, which has sound strategic purpose, and we have won a multi million pound contract from a major network operator to service 50 of their high spending SME customers. Both are contributing well to group revenues.

We remain cautious in respect of our prospects of returning to rapid organic growth. This is due to the continued threat of possible further dip in spending by existing customers, and is dependent on the recovery of the UK economy. However, in the longer term, as we move out of recession, we will have an opportunity to grow revenues more quickly. We anticipate this may be accompanied by further acquisitions offering complementary services to our existing products. We therefore remain excited over the prospects for future growth.

James Murray
Chief Executive Officer
7 December 2009

Financial and Business review

Trading review by products

Mobile

	2009	2008
Turnover (£m)	41.6	43.6
Gross Profit (£m)	12.4	12.9
Gross Margin %	29.9%	29.7%
Subscribers at 30 Sept	55,299	51,990
Monthly ARPU (£)	53	60
Monthly average contract length	22m	22 m
Gross new connections in year	16,429	18,465
Network churn	20%	16%
Customer churn by value	15%	15%
% Subscribers in-contract	82%	85%
Data connections (included in above)	23,146	17,362
Data connections as % of total subscribers	41.9%	33.4%

- Group mobile revenues decreased by 5% to £41.6m (2008: £43.6m), as ARPU of existing customers declined 12%, but this was partly offset by new revenues arising from an encouraging net increase in customer numbers, as the Group made gains in market share.
- “ARPU” represents the average spend in line rental and usage charges per live connection per month. It has reduced by 12% to £53 in this period. In our interim announcement, we spent some time explaining the ARPU drop to £55, citing the reduced roaming of business employees abroad, increase in zero usage devices, with the balance of the negative impact on ARPU being attributed to the lower level of UK activity, and more competitive tariffs in the market place. When reviewing the impact over a full year, it is clear that over half the impact has come from lower international revenue whether roamed or originating in the UK.
 - ARPU levels for international call revenues are £4 lower on average. Nearly a third of the reduction seems to be due to lower volume of calls which were down nearly 4% year on year. The remainder is due to tariff changes. Some is due to the July 2009 regulatory reduction in EU SMS prices. But the majority is due to lower tariffs, set by the major operators.
 - The remainder of the reduction in ARPU was caused by lower use of mobile devices in the UK, and lower tariffs. The main tariffs introduced by the networks in 2009 brought in free calls between same network users and also total fleet bundles. Both had an ARPU reducing impact.

Assuming no pick up in economic activity, the trends on ARPU reduction are set to continue into 2010, but at a lower rate. The ARPU in September 2009 was £51.50.

- The business subscriber base for the Group has increased 6% from 51,990 to 55,299 subscribers :
 - Net additions in the year were 3,309 (2008: 6,270), reflecting continued gains in market share by the Group. Significant new clients included Fidessa plc and British Car Auctions Limited. The second half of the year was somewhat weaker than the first half, with only just over 1,000 net gains. Gross connection gains held up well in a quieter summer period with 7,900 compared to 8,500 in the first half. Overall new gross connections were 12% behind 2008, which is considered a solid performance when companies were contracting and new connections which previously arose from natural expansion had ceased. The lower level of net gains in the second half are reflected in the increased network churn as companies reduced their fleets due to downsizing their businesses.
 - Data connections grew rapidly and ahead of expectations. They now represent 41.9% (2008: 33.4%), of total connections. “Converged devices” (this is measured as a data connection which has passed voice traffic in the last three months e.g. BlackBerry/MS mail), continue to gain widespread currency with cheaper Blackberry models launched this year.

The number of converged devices has grown over 40% (2008: 50%) in the year to over 15,000 connections (2008: 10,700), and they now account for over one in four of existing connections. This trend is expected to continue over the year ahead. Data-only devices such as “dongles” increased to 8,100, up from over 6,000 last year. These continue to dilute ARPU but remain a core part of servicing and retaining business clients.

- Churn – it was a solid performance in keeping churn under control. Network churn for the Group was 19.7% up from 16% in 2008. Nearly 2.5% of this increase was due to customers switching networks in the hunt for lower prices, but remaining with the Group. It remained in line with expectations set by the Board. The customer churn by value we also measure was reassuringly consistent and low at 15% as in 2008.
- Gross margins performed well in spite of the drop in ARPU, and came in slightly ahead of 2008 and expectations. Margins on line rental and usage charges were each ahead of 2008, in spite of the reduced spend, due largely to better buying, and less discounting on the Networks’ new products. In the interim report, we highlighted the £0.3m lower level of network contributions than 2008 which was pulling margins down below 30%. This continued in the second half, but margins were helped by bundled tariffs which required lower hardware subsidies to customers. The outlook for margins remains steady and we look to remain in the target band of 29 – 31% we have occupied in the last four years.

Network Services

	2009	2008
Turnover (£m)	£33.8	£34.9
Gross Profit (£m)	£12.9	£14.4
Gross Margin %	38.2%	41.1%

Outbound KPIs

Outbound - Monthly ARPU (£)	1,080	1,101
WLR as a % of total Outbound revenues	40%	32%
Number of lines/channels	67,587	52,262
Average new customer contract length (months = "m")	19m	16 m

Inbound KPIs

Turnover (£m)	£6.9	£7.1
Gross Margin %	53.7%	58.4%

Group sales decreased marginally by 3% from £34.9m to £33.8m. As in prior periods, the decline in call revenues continues to overshadow the increased momentum in customer wins as is illustrated by the increased WLR base size.

Gross margins were overall down 2.9%, and were in line with revised expectations. The reasons for the decline were as follows :

- 1.2% was due to a change in outbound sales mix substituting £2m of minutes with new line rentals;
- 1% was due to reduced outbound minutes revenues, both tariff reductions and lower volumes.
- 0.3% due to loss of commissions due from BT for MPLS circuits: Echo used to receive commissions from BT, which were discontinued in late 2008. The gross profits and revenues in 2008 benefited from an additional £125,000 at 100% margin, which accounted for 0.3% margin reduction.

- 0.4% was due to modest margin erosion in the inbound 0870 revenues as the customer base substituted to less profitable products.

Outbound services

- Outbound revenues declined 3.5% to £26.8m (2008: £27.8m). Usage charges declined even further, falling 16% from £18.6m to £15.7m. Offsetting this was the growth in line rental revenues highlighted below. It is worth noting that while minutes revenues have continued to decline both in activity levels and prices, there was overall growth in revenues in the second half of 2009 against the first half, albeit marginal. Some major customer wins such as Hydrogen Group and Nestor Healthcare Group have helped reverse the prevailing economic trend.
- Usage revenues' decline has been reviewed in detail. It was noted that in spite of the number of lines growing by 29%, the number of minutes fell 5% year on year, indicating a significant economic reduction as well as the ongoing impact of changes in technology and the ascendancy of mobile in the workspace. The average call value fell 15% year on year, with price drops spread across the main destinations.
- Wholesale Line Rental revenues ('WLR') increased from £8.8m to £10.7m, an increase of 22%. The lines under contract grew 29% on a like for like basis across the group, with ISDN30 channels growing by the same rate and continuing to account for 53% total lines. WLR now accounts for 40% and at the year end, the run rate was for nearly £12m of WLR revenues.
- Monthly average revenue per customer "ARPU" has fallen £21 to £1,080 over the year. Essentially, it is holding fairly steady, with continued cross selling of WLR and the addition of larger customers to the base offsetting the impact of lower usage across the entire customer base.
- Average new contract lengths have increased to 19 months, as increasing numbers of customers also taking mobile services sign up for two years.

Inbound services

- Inbound services could not match its growth of 2008, when it was up 13% organically. In spite of new client wins and very few client losses, revenues were also down marginally, by 3% to £6.9m. The major impact on revenues was the migration by several of the top spending clients to lower revenues number ranges such as 0844 and 0845, and then the removal of 0870 revenue share in August 2009. This was long heralded. The run rate of revenues following the regulation changes in August 2009 and some key number translations is closer to £6m than £7m, albeit with slightly higher margins.

Advanced Solutions

	2009	2008
Turnover (£m)	£14.3	£15.2
Gross Profit (£m)	£5.5	£5.5
Gross Margin %	38.4%	36.1%

Sales breakdown

IP PBX Installs	7.7	8.8
IP PBX Support	4.6	4.4
Data circuit rentals	2.0	2.0
IP PBX support GP	4.2	4.2
Engineering cost base	(2.4)	(2.5)

- IP PBX install revenues were down £1.1m year on year from £8.8m to £7.7m in 2009. This was a good performance relative to the market. The larger installations (over £0.1m) have seen extended sales cycles with some defaults due to lack of availability of lease finance. Sales of enhancements ("add-ons") to existing customers' systems have reduced by over 25% year-on-year, as many larger enterprises put on hold upgrades to their systems and are reducing system requirements rather than adding to them. We are seeing a gradual increase in our pipeline as these customers tentatively return to the market. However, the impact of this has been reduced by solid sales of smaller IP based systems (less than £0.1m) which have been ahead of expectations, with many of these

vendor-financed or purchased for cash, justified by a rapid payback in terms of cheaper telecoms spend across many sites. Many of these new sales have been assisted by multi-product offerings and cross subsidies being built into our customer base.

- Maintenance revenues have increased 5% from £4.4m in 2008 to £4.6m in 2009. This was a positive performance after the loss of two of the largest Echo customers in 2008, which were serving out their final year's notice, at the time of the acquisition. The outlook for maintenance revenues, which continue to be a key focus for management, remains mixed. There are plenty of opportunities to win market share with some competitors focussed on other aspects of their business. However, there is continued pressure on renewal pricing and with customers continuing to close sites, churn has tracked slightly ahead of original management expectations last year, albeit still at a low level.
- Data circuit revenues have remained flat year on year at £2.0m. A range of managed services were provided for new customers, including MPLS, Ethernet, and ADSL being sourced from a selection of suppliers, including principally in this period, Telstra, Viatel and Easynet. The Group also sold its first Cisco deal. Data remains an area of obvious potential growth to the business, and the Group has recently established a specialist sales team to focus on selling into our existing customers.
- Margins have improved to 38.4%, up 2.3% on 2008. 1.4% of the increase is due to the change in sales mix as maintenance has much higher margins and was increased year on year. The remainder 0.9% was due to improved buying of data circuits and improved margins on hardware kit sold to smaller customers.
- In August 2009, the Group recruited a team of specialist sales and engineering skills to cover the "Blue lights" market, building on the success with London and Welsh Ambulance services and also to cover the NHS trusts. To date, three new accounts have been won and this is seen as an area of growth for the Group. The Group is currently waiting for the outcome of the renewal of the necessary PASA accreditation which is due March 2010.

Capital investment

The Group invested £0.34m (2008: £0.92m) in tangible fixed assets and intangible software assets during the year. Expenditure was kept within target, and a breakdown of spend is as follows:

	2009	2008
	£'million	£'million
New office space at Ivory House		0.1 **
New City & Manchester office space	0.1	
IT Hardware		0.1
CRM software	0.1	0.3
Clarity & Workflow software	0.1	0.1
IP Phone system and LAN upgrade		0.2 **
Other - motor, furniture etc		0.1

The items marked ** were identified last year as non-routine expenditure.

In July 2009, the Group moved its City of London operations from serviced offices in Bunhill Row to 105 Bishopsgate where it has taken a minimum three year term lease on larger and cheaper premises.

Capital expenditure in 2010 is expected to be less than £0.5m.

Freehold property

On 31 March 2009, the Board decided that Echo's former headquarters, previously held for resale would be partially brought back into use for storage and the upper floors of offices leased. To date there has been some interest at a discounted rent on the upper floors, but requiring a change of use planning application.

Recently, an unsolicited offer to purchase the freehold was received for £725,000, and the Board has decided it would be appropriate to revalue the property at that level and accordingly an impairment charge of £0.17m has been booked to the profit and loss account. The Board are considering this offer. The cost to the Group of the property was less than £0.7m, but was revalued to £0.88m on acquisition.

Cash flow

Cash inflow from operations was excellent bringing in £10.6m (2008: £10.3m), representing a cash conversion of 110% adjusted EBITDA (2008: 94%). This included a working capital inflow of £1.0m (2008: outflow of £0.7m), mainly due to increased provisions for £0.6m for mobile hardware (being the costs of renewal or acquisition of customer contracts), reduced trade debtors £0.5m, and reduced stock levels £0.2m. Up to £0.4m has been identified as potentially reversing as working capital outflows next year.

The healthy cash conversion continues to highlight the Group's strong control over working capital and its prudent accounting policies. The policy of writing off customer acquisition costs immediately to the income statement, often in respect of two year contracts, has meant a further increase in the provision from £1.6m in 2008 to £2.2m in 2009. The continuing increase in these provisions, together with the share option costs of £0.6m (2008: £0.3m), are the main contributors to the high cash conversion rate of EBITDA averaging around 100% in the last two years.

The operating cash flow of the Group was applied as follows:

	2009	2008
	£'million	£'million
Net operating inflow	10.6	10.3
Investment returns	0.1	0.1
Taxation	(2.5)	(1.9)
Capital expenditure	(0.3)	(0.9)
Free cash flow	7.9	7.6
Acquisitions/disposals	0.3	(0.3)
Dividends	(2.1)	(1.8)
Equity finance from staff options	0.1	-
Loan repayment	(0.1)	(0.6)
Share buy backs	(1.3)	(4.1)
Net cash inflow/(outflow)	4.8	0.8
Net funds at 30 September	8.1	3.2

Echo earn out and warranty claims

On 24 January 2009, the Group finalised the deferred consideration due to the sellers of The Telecom Centre Limited ("Echo"), with a payment agreed at £58,000. On 24 March 2009, the Group received £300,000 from the same sellers in respect of warranty claims. As a result of these two transactions, the cash flow statement shows a net receipt to the Group of £0.3m in respect of purchase of subsidiary undertakings ("Acquisitions/Disposals" above). The net balance has been allocated against goodwill arising on consolidation in the balance sheet.

Tax

The effective tax rate was 28.5% (2008: 27.0%). Note 2 below sets out the reconciliation back to the standard rate of profits being 28% in the year to 30 September 2009 (2008: 29%).

The main reason for the slightly higher than standard rate tax charge, was the disallowable operating costs, the largest of which was the provision for impairment to freehold property £0.17m.

Share Buy Backs

Pursuant to the authority granted at an EGM on 24 July 2008, the Group announced on 18 August 2008 that it would commence a programme of share repurchases, limited to 4,771,162 ordinary shares. Between 16 and 20 October 2008, the Group repurchased 387,500 shares, each at 135p and subsequently cancelled them. In addition, on 11 February 2009, the Group repurchased 129,149 ordinary shares, each at 140p and they were subsequently cancelled. Between 1 and 2 July 2009, the Group repurchased a further 650,154 ordinary shares, at 100p and they were subsequently cancelled.

During the year, in aggregate the Group returned £1.35m to shareholders (2008: £4.04m) at an average repurchase share price of 116 pence (2008: 140 pence).

The 1 million shares held in Treasury will continue to be held for potential use in satisfying share option exercises and equity issued as part of an acquisition.

The Board will continue to monitor levels of cash and whilst excess levels of cash these have historically been used for acquisitions, the possibility of returning excess levels of cash to shareholders via a special dividend or further share buybacks will remain under consideration. Since the year end, the Group has further repurchased and cancelled 320,000 shares at an average price of 112 pence.

Earnings per share

Fully diluted adjusted earnings per share ('EPS') have decreased by 12% to 13.9p (2008: 15.8p). Basic adjusted earnings per share have decreased 13% from 16.5p to 14.4p.

The statutory or unadjusted fully diluted earnings per share have decreased 15% from 13.7p to 11.6p, and the basic statutory earnings per share have decreased 16% from 14.3p to 12.0p.

Set out below is a reconciliation to show how the basic EPS reconciles to the adjusted EPS. The two main factors are the amortisation of acquired intangible assets (principally the effect of amortising Echo's intangibles), and the impairment of the freehold property, acquired with Echo.

Reconciliation of Basic EPS - Statutory to Adjusted	2009 pence	2008 pence
Reported basic EPS at 30 September	12.0	14.3
Amortisation on acquired assets/intangibles (taxed)	2.0	2.2
Impairment of freehold property	0.4	-
Adjusted Basic EPS at 30 September	14.4	16.5

In terms of share issues and share buy backs it has been a busy year:

Share issues/buy backs

Number of ordinary shares at 30 September 2008	44,963,355
Share options exercised	154,069
Share buy backs Oct-08	(387,500)
Share buy backs Feb-09	(129,149)
Share buy backs Jun-09	(540,000)
Share buy backs Jul-09	(110,154)
Number of ordinary shares at 30 September 2009	<u>43,950,621</u>
Shares held in treasury	1,000,000

The EPS enhancing benefits of the share buy backs in 2008 and 2009 are shrouded by a higher effective tax rate in 2009 and the increased share option costs in 2009. Adjusted EPS is calculated after deducting share option costs which are otherwise added back in our adjusted figures. These costs were increased from £0.3m to £0.6m in 2009.

In spite of lower rates of corporation tax (dropping from 29% composite rate in 2008 to 28% in 2009), the tax rate is up 1.5% to 28.5% - 1% of the increase is due to 2008 having a lower charge than normal due to prior year adjustment for Echo losses, and 2009's charge is 0.5% higher due to the disallowance of the freehold property impairment charge.

Assuming level tax rates, and if you add back the share option costs, adjusted EPS would have been 15.3p compared to 16.6p in 2008, which is only down 8% year on year, compared to profits down 14%.

Dividend per Share

The Board has proposed a final dividend of 3.5 pence per share (2008: 3.1 pence per share) making a total dividend of 5.1 pence per share for the full year (2008: 4.6 pence per share). The total dividend for the full year equates to approximately 35% of adjusted earnings per share (2008: 28%), which more appropriately reflect the cash earnings of the Group. The increase in payout to the upper end of the range set by the Group's policy is due to the continued strong cash generation by the Group, and when considering dividend per share progression, also takes into account the fewer shares ranking for dividend due to the share buy backs both before and after the balance sheet date. The dividend will be paid on 26 January 2010 to shareholders on the register as of 18 December 2009.

Edward Spurrier,
Chief Financial Officer
7 December 2009

CONSOLIDATED INCOME STATEMENT

For the year ended 30 September 2009

	Notes	Year ended 30 September 2009 £'000	Year ended 30 September 2008 £'000
Revenue		89,676	93,707
Cost of sales		(58,852)	(60,913)
Gross profit		30,824	32,794
Operating costs		(23,793)	(24,039)
Operating profit		7,031	8,755
Operating profit – analysed:			
Adjusted operating profit		8,986	10,433
Share based payments		(565)	(303)
Amortisation of purchased customer contracts and other intangibles (excluding computer software)		(1,220)	(1,375)
Impairment of freehold property		(170)	-
Operating profit		7,031	8,755
Finance income		105	223
Finance costs		(21)	(77)
Profit on ordinary activities before taxation		7,115	8,901
Taxation on profit on ordinary activities	2	(2,024)	(2,402)
Profit on ordinary activities after taxation		5,091	6,499
Attributable to:-			
Equity shareholders of the company		5,091	6,497
Minority interest		-	2
		5,091	6,499
Earnings per ordinary share:			
Basic	4	12.0p	14.3p
Diluted	4	11.6p	13.7p

CONSOLIDATED BALANCE SHEET

As at 30 September 2009

	Notes	30 September 2009 £'000	30 September 2008 £'000
ASSETS			
Non-current assets			
Intangible assets		17,755	19,416
Property, plant and equipment		2,708	2,204
Deferred tax asset		428	675
Assets held for resale		-	887
Property deposits		14	14
		20,905	23,196
Current assets			
Inventories		168	382
Trade and other receivables	5	12,535	14,450
Cash and cash equivalents		9,015	4,227
		21,718	19,059
Total assets		42,623	42,255
EQUITY AND LIABILITIES			
Equity			
Called up share capital	6	56	57
Share premium		4,855	4,721
Capital redemption reserve		4	3
Merger reserve		1,905	1,905
Treasury shares held		(1,422)	(1,422)
Retained earnings		16,607	14,791
		22,005	20,055
Current liabilities			
Borrowings		50	35
Contingent consideration		-	97
Current tax liabilities		1,335	1,380
Trade and other payables	7	17,269	18,391
		18,654	19,903
Non-current liabilities			
Borrowings		874	960
Deferred tax liabilities		1,090	1,337
		1,964	2,297
Total liabilities		20,618	22,200
Total equity and liabilities		42,623	42,255

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital	Share premium	Capital redemption reserve	Merger reserve	Shares held in treasury	Retained earnings	Total	Minority interest	Total equity
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Balance at 1 October 2007	60	4,577	-	1,905	-	12,217	18,759	7	18,766
Shares issued	-	19	-	-	-	-	19	-	19
IFRS2 share based payments	-	-	-	-	-	303	303	-	303
Share buy-back	(3)	-	3	-	(1,422)	(2,681)	(4,103)	-	(4,103)
Shares issued to purchase minority interest	-	188	-	-	-	-	188	(9)	179
Share expenses	-	(63)	-	-	-	-	(63)	-	(63)
Deferred tax on share options	-	-	-	-	-	266	266	-	266
Profit for the year	-	-	-	-	-	6,497	6,497	2	6,499
Dividends paid	-	-	-	-	-	(1,811)	(1,811)	-	(1,811)
Balance at 30 September 2008	57	4,721	3	1,905	(1,422)	14,791	20,055	-	20,055
Shares issued	-	134	-	-	-	-	134	-	134
IFRS2 share based payments	-	-	-	-	-	565	565	-	565
Share buy-back	(1)	-	1	-	-	(1,356)	(1,356)	-	(1,356)
Deferred tax on share options	-	-	-	-	-	(396)	(396)	-	(396)
Profit for the year	-	-	-	-	-	5,091	5,091	-	5,091
Dividends paid	-	-	-	-	-	(2,088)	(2,088)	-	(2,088)
Balance at 30 September 2009	56	4,855	4	1,905	(1,422)	16,607	22,005	-	22,005

The balance classified as share capital includes the proceeds arising on issue of the Company's equity share capital, comprising 0.125p ordinary shares and the cancellation of shares purchased during the year.

Capital redemption reserve arose from the purchase of own share capital.

The merger reserve results from the previous acquisitions of Integrated Communications for Business (UK) Limited and The Telecom Centre Limited and represents the difference between the value of the shares acquired (nominal value plus related share premium) and the nominal value of the shares issued.

Shares acquired in relation to the employee Share Incentive Plan are held in treasury until such time as the awards vest. At 30 September 2009 the number of shares held in treasury was 1,000,000 (2008: 1,000,000). These had a nominal value of £1,250 and a market value of £1.04 million.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 30 September 2009

	Notes	Year ended 30 September 2009 £'000	Year ended 30 September 2008 £'000
Cash flows from operating activities			
Cash generated from operations	8	10,605	10,335
Income tax paid		(2,458)	(1,940)
Interest paid		(21)	(77)
Net cash inflow from operating activities		8,126	8,318
Cash flows from investing activities			
Purchase of property, plant and equipment		(170)	(510)
Purchase of intangible assets (software)		(172)	(409)
Proceeds from sale of property, plant and equipment		45	-
Interest received		98	223
Purchase of subsidiary undertaking		(58)	(276)
Proceeds from vendors under sale and purchase agreement		300	-
Net cash generated / (used) in investing activities		43	(972)
Cash flows from financing activities			
Dividends paid	3	(2,088)	(1,811)
Proceeds from issue of share capital		134	19
Payments made for share buy-backs		(1,356)	(4,102)
Share expenses		-	(63)
Repayments of borrowings		(71)	(584)
Net cash used in financing activities		(3,381)	(6,541)
Increase in cash and cash equivalents			
Cash and cash equivalents at start of period		4,227	3,422
Cash and cash equivalents at end of period		9,015	4,227

NOTES TO THE FINANCIAL STATEMENTS

1 Basis of preparation

Alternative Networks plc is a company incorporated and domiciled in the United Kingdom under the Companies Act 2006. The address of the registered office is Chatfield Court, 56 Chatfield Road, London SW11 3UL.

These financial statements have been prepared in accordance with IFRS as adopted by the EU and IFRIC interpretations and the Companies Act 2006 applicable to companies reporting under IFRS. The financial statements have been prepared under the historical cost convention.

The financial information is abridged and does not contain the Group's full financial statements for the years ended 30 September 2008 and 2009.

Full financial statements for the year ended 30 September 2008 (which received an unqualified audit report) have been filed with the Registrar of Companies. Financial statements for the year ended 30 September 2009 will be presented to the Members at the forthcoming Annual General Meeting; the auditors have indicated that their report on these Financial Statements will be unqualified.

2 Taxation on profit on ordinary activities

	30 September 2009 £'000	30 September 2008 £'000
Current tax:		
Tax on profit in the year	2,413	2,595
Adjustments in respect of prior years	7	(158)
Total current tax	2,420	2,437
Deferred tax:		
Origination and reversal of timing differences	(396)	(407)
Utilisation of tax losses	-	372
Total deferred tax credit	(396)	(35)
Total tax charge	2,024	2,402

The current tax assessed for the period is higher (2008: lower) than the average rate of corporation tax in the UK of 28% (2008: 29%) applied to the profits before tax for the year. The differences are explained below:

	30 September 2009 £'000	30 September 2008 £'000
Profit on ordinary activities before tax	7,115	8,901
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 28% (2008: 29%)	1,992	2,581
Effects of:		
Expenses not deductible for tax purposes	14	12
Schedule 23 deduction in respect of share options	(26)	(27)
Impairment of freehold property	48	-
Other timing differences	(11)	(6)
Adjustments in respect of prior years	7	(158)
Total tax charge	2,024	2,402

3 Dividends

	30 September 2009 £'000	30 September 2008 £'000
2008 Final Paid - 3.10p (2007: 2.30p) per 0.125p ordinary share	1,383	1,096
2009 Interim Paid - 1.60p (2008: 1.50p) per 0.125p ordinary share	705	715
	2,088	1,811

The 2008 proposed final dividend of 3.10 pence per 0.125p ordinary share was paid on 29 January 2009. The amount of dividend paid was £1,383,000 (2007: £1,096,000).

The Directors also paid a 2009 interim dividend of 1.60 pence per 0.125p ordinary share, with a total payment value of £705,000 (2008: £715,000). This was paid on 17 July 2009 to shareholders on the register on 3 July 2009.

In addition, the Directors are proposing a final dividend in respect of the financial year ending 30 September 2009 of 3.50 pence per 0.125p ordinary share which will absorb an estimated £1,552,000 of shareholders' funds. Assuming it is approved by the shareholders at the Annual General Meeting on 25 January 2010, it will be paid on 26 January 2010 to shareholders who are on the register of members at 18 December 2009.

4 Earnings per share

The calculation of basic and fully diluted earnings per ordinary share is based on the profit attributable to equity holders of the company divided by the weighted average number of ordinary shares in issue during the year.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The Group has one category of potential ordinary shares: those share options granted to employees where the exercise price is less than the average price of the Company's ordinary share during the year.

The profit and weighted average number of shares used in the calculations are set out below:

Basic and fully diluted earnings per share	Profit attributable to	Weighted average of	Per share
	shareholders	£0.00125 ordinary	amount
	£'000	Number	Pence
2009 Earnings per share – basic	5,091	42,541,495	12.0
Potentially dilutive shares	-	1,292,806	(0.4)
2009 Earnings per share – diluted	5,091	43,834,301	11.6
2008 Earnings per share – basic	6,497	45,337,790	14.3
Potentially dilutive shares	-	1,955,157	(0.6)
2008 Earnings per share – diluted	6,497	47,292,947	13.7

The adjusted EPS is based on the adjusted profit before tax as set out in note 9, and the weighted average number of shares as described above.

Basic and fully diluted earnings per share	Adjusted profit	Weighted average of £0.00125 ordinary shares	Per share amount
	£'000	Number	Pence
2009 Earnings per share – basic	6,113	42,541,495	14.4
Potentially dilutive shares	-	1,292,806	(0.5)
2009 Earnings per share – diluted	6,113	43,834,301	13.9
2008 Earnings per share – basic	7,462	45,337,790	16.5
Potentially dilutive shares	-	1,955,157	(0.7)
2008 Earnings per share – diluted	7,462	47,292,947	15.8

Share option costs included within adjusted profit attributable to shareholders are reducing the earnings per share in 2009 by 0.9p (2008: 0.4p).

As in prior periods, the calculation of the weighted average number of shares in issue excludes the shares held by the Alternative Networks Employee Benefit Trust of 1,915,200. These shares are then added to the total of extant options when calculating the fully diluted weighted average number of shares.

There were 44,950,621 shares in issue at 30 September 2009 including 1,000,000 shares held in treasury. On 30 September 2008 there were 45,963,355 shares (inclusive of 1,000,000 shares held in treasury). The weighted average number of shares during the year was 42,541,495 (2008: 45,337,790).

The potentially dilutive shares figure does not include shares relating to the LTIP as these options include a total shareholder return test which is not being met as at 30 September 2009.

5 Trade and other receivables

	30 September 2009 £'000	30 September 2008 £'000
Trade receivables	5,024	5,522
Amounts owed by group undertakings	-	-
Prepayments	1,532	2,584
Accrued income	5,937	6,297
Other receivables	42	47
	12,535	14,450

6 Called up share capital

	30 September 2009 £'000	30 September 2008 £'000
Authorised 80,000,000 (2008: 80,000,000) ordinary shares of 0.125p (2008: 0.125p) each.	100	100
Allotted and fully paid up 44,950,621 (2008: 45,963,355) ordinary shares of 0.125p (2008: 0.125p) each.	56	57

Movement in shares in issue

	2009 Shares	2008 Shares
Ordinary shares of 0.125p each		
At 1 October	45,963,355	47,633,220
Allotted under share option schemes	154,069	78,400
Re-purchased and cancelled under buy-back scheme	(1,166,803)	(1,888,419)
Acquisition of 10% of AN Technical Services Limited	-	140,154
At 30 September	44,950,621	45,963,355

During the year 1,166,803 shares (representing approximately 3% of the issued share capital) were purchased by the company for £1,356,202 at an average cost per share of £1.16p.

The effect of the buyback programme is to enhance earnings per share in the current and future years.

During the year 154,069 shares were allotted under share option schemes as follows;

30,800 issued at 25p resulting in a share premium of £7,662.

123,269 issued at 102.5p resulting in a share premium of £126,197.

7 Trade and other payables

	30 September 2009 £'000	30 September 2008 £'000
Trade payables	7,627	8,289
Amounts owed to group undertakings	-	-
Other taxation and social security costs	947	1,489
Other payables	388	278
Accruals and deferred income	8,307	8,335
	17,269	18,391

8 Cash generated from operations

Group	Year ended 30 September 2009 £'000	Year ended 30 September 2008 £'000
Operating profit	7,031	8,755
Adjustments for;-		
Depreciation of property, plant and equipment	375	358
Impairment of freehold property	170	-
Amortisation of intangible assets	1,501	1,637
Employee share scheme charges	565	303
(Profit) / loss on sale of tangible assets	(44)	3
Movements in working capital;-		
Decrease in property deposits	-	51
Decrease / (increase) in inventories	214	(113)
Decrease /(increase) in trade and other receivables	1,915	(201)
(Decrease) in trade and other payables	(1,122)	(458)
Cash generated from operations	10,605	10,335

9 Reconciliation to adjusted performance

Reconciliation of adjusted EBITDA	30 September 2009	30 September 2008
	£'000	£'000
Profit before tax	7,115	8,901
Adjustments		
Amortisation of purchased customer contracts and other intangibles (excluding computer software)	1,220	1,375
Share based payments	565	303
Add back impairment of freehold property	170	0
Adjusted profit before tax	9,070	10,579
Finance income	(105)	(223)
Finance costs	21	77
Adjusted operating profit	8,986	10,433
Add: Depreciation of property, plant and equipment	375	358
Add: Amortisation of software (intangibles)	281	262
Adjusted EBITDA	9,642	11,053

Reconciliation of adjusted profits for earnings per share	30 September 2009	30 September 2008
	£'000	£'000
Adjusted profit before tax (see above)	9,070	10,579
Less: Share based payments	(565)	(303)
Less: Taxation per profit and loss accounts	(2,024)	(2,402)
Less: Taxation on amortisation of purchased customer contracts and other intangibles (excluding computer software)	(342)	(385)
Less: Exceptional deduction on exercise of AN share options	(26)	(27)
Adjusted profit after tax	6,113	7,462

Adjusted EPS is calculated on adjusted earnings after deduction of share option costs.

This analysis is provided as the Group considers it provides a truer reflection of the underlying performance of the business, and is common practice in the investment analyst community.