AFT pharmaceuticals

*Working to improve your health*

# AFT ANNUAL FINANCIAL STATEMENTS FY2017

**Contents**

# INDEPENDENT AUDITORS' REPORT
to the shareholders of AFT Pharmaceuticals Limited

The consolidated financial statements comprise:

- the consolidated balance sheet as at 31 March 2017;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

## Our opinion

In our opinion, the consolidated financial statements of AFT Pharmaceuticals Limited (the Company), including its subsidiaries (the Group), present fairly, in all material respects, the financial position of the Group as at 31 March 2017, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

## Basis for opinion

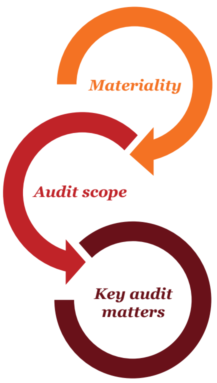
We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs NZ) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Other than in our capacity as auditor we have no relationship with, or interests in, the Group.

## Our audit approach




### Overview

An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement.

Overall group materiality: $900,000, which represents 5% of loss before tax.

We chose loss before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is measured by users, and is a generally accepted benchmark.

We agreed with the Audit and Risk Committee that we would report to them misstatements identified during our audit above $40,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

We have identified one key audit matter being the accounting treatment of research and development costs.

# INDEPENDENT AUDITORS' REPORT (CONTINUED)
to the shareholders of AFT Pharmaceuticals Limited

### Materiality
The scope of our audit was influenced by our application of materiality.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the consolidated financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the consolidated financial statements as a whole.

### Audit scope
We designed our audit by assessing the risks of material misstatement in the consolidated financial statements and our application of materiality. As in all of our audits, we also addressed the risk of management override of internal controls including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Full scope audits were conducted on the Australian and New Zealand operating segments. The remaining segments were subject to audit procedures that were considered appropriate for the size and nature of those segments.

## Key audit matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

## Key audit matter

### Treatment of research and development costs
As disclosed in note 6, the Group is involved in the research and development of new products and variants of existing products in order to expand their commercial offerings.

All research and development costs incurred during the year to 31 March 2017, totalling $11.2m, have been expensed through the Income Statement.

Our audit focussed on this area due to the value of the research and development costs incurred, and the fact that there is judgment involved in assessing whether the criteria set out in the accounting standards for expensing or capitalising these costs has been met. In particular, a key consideration that impacts whether costs should be capitalised is the technical feasibility of completing the development of a new product. Typically, a key element of demonstrating technical feasibility is the approval of the product by the relevant market regulatory authority.

Management assesses the status of each project based on progress against clinical trial contracts and the relevant regulatory approval process to determine the appropriate accounting treatment.

## How our audit addressed the key audit matter

Our audit procedures included:

- Gaining an understanding of the business process undertaken by management to assess the appropriate accounting treatment for each project.
- Assessing whether the Group's accounting policies in relation to the treatment of research and development expenditure were consistent with requirements of the relevant accounting standards.
- Obtaining an analysis from management as to the status of each individual project, corroborating these status assessments with the operational management team (as distinct from the financial management function).
- Testing a sample of costs expensed to supporting documentation such as clinical trial agreements, contracts and invoices, and payment records to verify the amounts being expensed and the status of the project.
- Challenging whether managements treatment of expensing the costs was appropriate based on the results of the audit work performed over each of the related projects.

The results of our procedures did not identify any inconsistencies in management's treatment of the research and development costs.

# INDEPENDENT AUDITORS' REPORT (CONTINUED)

to the shareholders of AFT Pharmaceuticals Limited

## Information other than the financial statements and auditor's report

The Directors are responsible for the annual report. Our opinion on the consolidated financial statements does not cover the other information included in the annual report and we do not express any form of assurance conclusion on the other information.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard, except that not all other information was available to us at the date of our signing.

## Responsibilities of the Directors for the consolidated financial statements

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the consolidated financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities for the audit of the consolidated financial statements

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

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at:

https://xrb.govt.nz/Site/Auditing_Assurance_Standards/Current_Standards/Page1.aspx

This description forms part of our auditor's report.

## Who we report to

This report is made solely to the Company's shareholders, as a body. Our audit work has been undertaken so that we might state those matters which we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Pip Cameron.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants Auckland

24 May 2017

# CONSOLIDATED INCOME STATEMENT

For the year ended 31 March 2017

| $NZ000's | Note | 2017 | 2016 |
|---|---|---|---|
| Revenue | 4 | 69,205 | 64,014 |
| Cost of sales | | (43,207) | (40,435) |
| **Gross Profit** | | **25,998** | **23,579** |
| | | | |
| Other income | 5 | 2,659 | 2,295 |
| Selling and distribution expenses | 6(a) | (25,964) | (19,634) |
| General and administrative expenses | 6(a) | (5,851) | (6,804) |
| Research and development expenses | 6(a) | (11,227) | (8,092) |
| Equity accounted loss of joint venture entity | 13(b) | (414) | (302) |
| **Operating Loss** | | **(14,799)** | **(8,958)** |
| | | | |
| Finance income | | 347 | 291 |
| Finance costs | 6(a) | (3,878) | (2,019) |
| IPO, listing and capital raising costs | | - | (2,623) |
| **Loss before tax** | 6,7 | **(18,330)** | **(13,309)** |
| | | | |
| Tax benefit/(expense) | 7 | (58) | 42 |
| **Loss after tax attributable to owners of the parent** | | **(18,388)** | **(13,267)** |
| | | | |
| Basic and diluted earnings per share ($) | 25 | (0.19) | (0.48) |

# CONSOLIDATED STATEMENT OF COMPREHESIVE INCOME

For the year ended 31 March 2017

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **Loss after tax** | **(18,388)** | **(13,267)** |
| | | |
| **Other comprehensive income** | | |
| May be subsequently reclassified to profit and loss: | | |
| Foreign currency translation reserve | 356 | (530) |
| **Other comprehensive income/(loss) for the year, net of tax** | **356** | **(530)** |
| **Total comprehensive loss for the year attributable to owners of the parent** | **(18,032)** | **(13,797)** |

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 March 2017

| $NZ000's | Note | Share capital | Cash flow hedge reserve | Share options reserve | Foreign currency translation reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|---|
| **Balance 31 March 2015** | | **12,892** | **(305)** | **-** | **166** | **(10,732)** | **2,021** |
| Loss after tax | | - | - | - | - | (13,267) | (13,267) |
| Reclassification of FCTR to retained earnings | | - | - | - | 264 | (264) | - |
| Transfer to current year earnings | | - | 305 | - | - | - | 305 |
| Other comprehensive income | | - | - | - | (530) | - | (530) |
| Issue of share capital | 17 | 42,067 | - | - | - | - | 42,067 |
| Movement in share options reserve | | - | - | 65 | - | - | 65 |
| Capital raising expenses | 17 | (1,057) | - | - | - | - | (1,057) |
| Dividends paid and provided | | - | - | - | - | (1,374) | (1,374) |
| **Balance 31 March 2016** | | **53,902** | **-** | **65** | **(100)** | **(25,637)** | **28,230** |
| Loss after tax | | - | - | - | - | (18,388) | (18,388) |
| Other comprehensive income | | - | - | - | 356 | - | 356 |
| Issue of redeemable preference shares | 17 | 9,124 | - | - | - | - | 9,124 |
| Capital Raising Expenses | 17 | (82) | - | - | - | - | (82) |
| Movement in share options reserve | | - | - | 230 | - | - | 230 |
| **Balance 31 March 2017** | | **62,944** | **-** | **295** | **256** | **(44,025)** | **19,470** |

# CONSOLIDATED BALANCE SHEET

As at 31 March 2017

| $NZ000's | Note | 2017 | 2016 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Inventories | 8 | 18,718 | 16,499 |
| Trade and other receivables | 9 | 19,362 | 17,475 |
| Cash and cash equivalents | 10 | 15,980 | 28,055 |
| Current income tax asset | | - | 26 |
| **Total current assets** | | **54,060** | **62,055** |
| **Non-current assets** | | | |
| Property, plant and equipment | 11 | 386 | 407 |
| Intangible assets | 12 | 2,548 | 2,111 |
| Deferred income tax assets | 7 | 610 | 546 |
| Investment in joint venture entity | 13(b) | 627 | 185 |
| **Total assets** | | **58,231** | **65,304** |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 14 | 11,069 | 10,428 |
| Provisions | 15 | 3,950 | 3,083 |
| Current income tax liability | | 112 | - |
| Derivative liabilities | 20 | 204 | 402 |
| **Total current liabilities** | | **15,335** | **13,913** |
| **Non-current liabilities** | | | |
| Interest bearing liabilities | 16 | 23,426 | 23,161 |
| **Total liabilities** | | **38,761** | **37,074** |
| **EQUITY** | | | |
| Share capital | 17 | 62,944 | 53,902 |
| Retained earnings | | (44,025) | (25,637) |
| Share options reserve | 19(b) | 295 | 65 |
| Foreign currency translation reserve | | 256 | (100) |
| **Total equity** | | **19,470** | **28,230** |
| **Total liabilities and equity** | | **58,231** | **65,304** |
| Net tangible assets per ordinary share | | $0.17 | $0.95 |

For and on behalf of the Board who authorised these financial statements for issue on 24 May 2017.

**David Flacks**
Chairman

**Hartley Atkinson**
Managing Director and
Chief Executive Officer

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 March 2017

| $NZ000's | Note | 2017 | 2016 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Receipts from customers | | 69,877 | 63,237 |
| Interest received | | 347 | 241 |
| Payments to suppliers and employees | | (86,429) | (74,679) |
| Tax received | | 16 | 47 |
| Interest and finance cost paid | | (2,873) | (2,788) |
| **Net cash used in operating activities** | 18 | **(19,062)** | **(13,942)** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Purchases of property, plant and equipment | | (122) | (148) |
| Sale of property, plant and equipment | | - | 10 |
| Purchases of intangible assets | | (620) | (556) |
| Investment in joint venture | | (856) | (487) |
| **Net cash used in investing activities** | | **(1,598)** | **(1,181)** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Proceeds from issue of share capital | | 9,124 | 42,037 |
| Share issue costs | | (82) | (3,680) |
| Dividends paid | | - | (1,652) |
| **Net cash generated from financing activities** | | **9,042** | **36,705** |
| Net (decrease)/increase in cash | | (11,618) | 21,582 |
| Impact of foreign exchange on cash and cash equivalents | | (457) | 1,773 |
| Opening cash and cash equivalents | | 28,055 | 4,700 |
| **Closing cash and cash equivalents** | | **15,980** | **28,055** |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 March 2017

## 1. GENERAL INFORMATION

AFT Pharmaceuticals Limited (the 'Company') is a company which is incorporated and domiciled in New Zealand. It is registered under the Companies Act 1993. These financial statements comprise AFT Pharmaceuticals Limited and its subsidiaries (together referred to as the Group). The group is a pharmaceutical distributor and developer of pharmaceutical intellectual property.

The financial statements of the Group have been prepared in accordance with the requirements of the Companies Act 1993, Financial Reporting Act 2013 and the Financial Markets Conduct Act 2013. As group financial statements are prepared and presented for AFT Pharmaceuticals Ltd and its subsidiaries, separate financial statements for AFT Pharmaceuticals Ltd are not required to be prepared under the Companies Act 1993.

These financial statements are authorised for issue on 24 May 2017 by the Directors.

## 2. STATEMENT OF ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention with the exception of derivative instruments revalued to fair value.

### (a) Basis of preparation

The consolidated financial statements of the group have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP). The group is a for-profit entity for the purposes of complying with NZ GAAP. The consolidated financial statements comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), other New Zealand accounting standards and authoritative notices that are applicable to entities that apply NZ IFRS. The consolidated financial statements also comply with International Financial Reporting Standards (IFRS), and interpretations issued by the IFRS Interpretations Committee (IFRS IC) applicable to companies reporting under IFRS.

The accounting policies presented below have been applied consistently to all periods presented in these consolidated financial statements.

The reporting currency used in the preparation of these consolidated financial statements is New Zealand dollars, rounded where necessary to the nearest thousand dollars.

Certain FY16 comparatives have been reclassified to conform to the current period presentation. Refer to note 9 and note 18.

### (b) Principles of consolidation

**Subsidiaries**

The consolidated financial statements incorporate the assets and liabilities of the parent and the results of its subsidiaries controlled at year end.

Subsidiaries are all entities over which the group has control. The group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases.

The acquisition method of accounting is used to account for the subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the Group's share of the fair value of the identifiable net assets of the subsidiary acquired, the difference is recognised directly in the statements of comprehensive income.

Inter-company transactions, balances and unrealised gains on transactions between subsidiary company are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred.

**Joint Venture**

Where the company does not hold a controlling stake in a Joint venture, the principles of Equity accounting are adopted. In these cases, the company's investment is recognised in the balance sheet and its share of after tax profits less losses of the joint venture are recognised in the Profit and Loss, with the value of the company's investment carrying value adjusted accordingly.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## (c) Critical accounting estimates and judgements

In preparing these financial statements the Group made estimates and assumptions concerning the future. These estimates and assumptions may differ from the subsequent actual results. Estimates and judgements are continually evaluated and are based on historical experience and other factors including expectations or future events that are believed to be reasonable under the circumstances. The main critical estimate and judgement used is the recognition of deferred tax, detailed within Note 7. It is not expected that this estimate and judgement will have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

## (d) Foreign currency translation

### (i) Functional and presentation currency

Items included in the financial statements of the subsidiaries' operations are measured using the currency of the primary economic environment in which it operates (the 'functional currency'). The consolidated financial statements are presented in New Zealand dollars, which is the Company's functional currency and the Group's presentation currency.

### (ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Income Statement.

### (iii) Foreign operations

The results and balance sheets of all foreign operations (none of which has the currency of a hyperinflationary economy) that have a functional currency different from New Zealand dollars are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each statement of comprehensive income are translated at average exchange rates, unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions.

## (e) Revenue recognition

Revenue comprises the fair value for the sale of goods and royalties due, excluding Goods and Services Tax, rebates and discounts.

- The sales of goods are recognised when the product is delivered to customers.
- Royalties are recognised when licencees have made sales of product which attract royalties to the company.

## (f) Other income recognition

Other income comprises of research and development grant and licensing income:

- **Research and development grant**

  Research and development grant income is recognised when eligible research and development expenses are incurred and conditions relating to the grant are satisfied.

- **Licencing income**

  Licencing income comprises milestone payments due under out-licencing agreements. Milestone payments represent a minor portion of the economic benefits of the out-licencing agreements (the primary benefits being the sale of product and royalties earned on licensee sales). The milestones are recognised as income depending on the terms of each out-licencing agreement.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 2. STATEMENT OF ACCOUNTING POLICIES (Continued)

### (g) Finance income recognition

Finance income comprises of interest income which is recognised on a time-proportion basis using the effective interest method.

### (h) Property, plant & equipment

All plant and equipment is stated at historical cost less depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the diminishing value method which is apportions the cost of the assets over their useful lives. The Group has the following classes of property, plant & equipment and depreciation rates:

| Category | Depreciation Rate (%) |
|---|---|
| Plant & machinery | 21% to 80% |
| Fixtures & fittings | 9% to 60% |
| Vehicles | 26% to 36% |

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposal are determined by comparing proceeds to carrying amounts and are included in the statements of comprehensive income.

### (i) Intangible assets

**Finite Useful Life**

Acquired patents have a finite life and are carried at cost less accumulated amortisation. Patents are amortised over a useful economic life of 20 years.

**Indefinite Useful Life**

Acquired trademarks are considered to have an indefinite useful life whilst they continue to protect revenue streams. Trademarks are carried at cost less accumulated impairment. Indefinite useful life assets are tested for impairment annually or when impairment indicators exist. The assets' carrying amount is written down immediately to its recoverable amount if the assets carrying amount is greater than its estimated recoverable amount.

### (j) Goods & services tax

The Income Statement and the Statement of Comprehensive Income have been prepared so that all components are stated exclusive of New Zealand, Australian and Malaysian GST. All items in the Balance Sheet are stated net of GST, with the exception of accounts receivable and payable which include GST invoiced. All components of Statement of Cash Flows are stated exclusive of GST.

### (k) Income tax

The income tax expense recognised for the period is based on the accounting profit or loss, adjusted for non-taxable and non-deductible differences.

Current tax is calculated by reference to the amount of income tax payable calculated using tax laws that are enacted or substantively enacted at balance date.

Deferred income tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset or liability is settled. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

### (l) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a weighted average cost basis. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

### (m) Leased assets

Operating leases are those in which all the risks and rewards are substantially retained by the lessor. Lease payments are charged in the income statement on a straight line basis over the term of the lease.

### (n) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost, less provision for doubtful debts. Bad debts are written off in the year in which they are identified. Collectability of trade receivables is reviewed on an on-going basis. Debts which are known to be uncollectible are written off. A provision for doubtful receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the Statements of Comprehensive Income.

### (o) Trade payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial period which are unpaid. These amounts are incurred and are usually paid within 30 days of recognition.

### (p) Borrowings

Borrowings are initially recognised at fair value plus transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (plus transaction costs) and the redemption amount is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date. Borrowing costs are expensed as incurred.

### (q) Share capital

Ordinary shares are classified as equity. Preferred shares are classified as equity, they attract a dividend yield and do not have ordinary share voting rights.

### (r) Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short term investments with original maturities of twelve months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

### (s) Employee entitlements

Liabilities for wages and salaries, including non monetary benefits, annual leave, and accumulating sick leave expected to be settled within 12 months of the reporting date are recognised in trade payables or provisions in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and measured at the rates paid or payable. The liability for employee entitlements is carried at the present value of estimated future cash flows. Staff share options are valued at fair value as calculated independently using the Black Scholes model.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 2. STATEMENT OF ACCOUNTING POLICIES (Continued)

### (t) Impairment of non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Indefinite useful life assets are tested for impairment annually and whenever there are indicators of impairment while finite useful life assets are tested only when there are indicators of impairment.

### (u) Derivative financial instruments

The Group benefits from the use of derivative financial instruments to manage foreign currency exposures.

The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts in place and the actual exchange rate at year-end, considered level 2 of the fair value hierarchy.

For the purposes of hedge accounting, hedges are classified as cash flow hedges where they hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss is recognised in the Income Statement.

### (v) Research and development

Research is the original and planned investigation undertaken with the prospect of gaining new knowledge and understanding. This includes: direct and overhead expenses for research, pre-clinical trials and costs associated with clinical trial activities. All research costs are expensed when incurred.

Development is the application of research findings to a plan or design for the production of new or substantially improved processes or products prior to the commencement of commercial production. When a project reaches the stage where it is reasonably certain that future expenditure can be recovered through the process or products produced, expenditure that is directly attributable or reasonably allocated to that project is recognised as a development asset. The asset will be amortised from the date of commencement of commercial production of the product to which is relates on a straight line basis over the period of expected benefit. Development assets are reviewed annually for any impairment in their carrying value.

### (w) Earnings per share

Basic earnings per share is computed by dividing net earnings by the weighted average number of ordinary shares outstanding during each period. Preferred shares are considered to be anti-dilutive for the earnings per share calculation.

Diluted earnings per share is computed by dividing net earnings adjusted for the share options cost, by the diluted weighted average number of ordinary shares (as if all options have been exercised).

## 3. STANDARDS OR INTERPRETATIONS NOT YET EFFECTIVE

No new standards that have been issued and are effective for the periods beginning 1 April 2016 are considered to materially impact the recognition, measurement or disclosure of these financial statements. The below are new standards and amendment that have been issued that are not yet effective:

NZ IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of NZ IFRS 9 was issued in September 2014. It replaces the guidance in NZ IAS 39 that relates to the classification and measurement of financial instruments. NZ IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income and fair value through profit or loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in other comprehensive income not recycling.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 3. STANDARDS OR INTERPRETATIONS NOT YET EFFECTIVE (Continued)

There is now a new expected credit losses model that replaces the incurred loss impairment model used in NZ IAS 39. For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. NZ IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under NZ IAS 39. The standard is effective for accounting periods beginning on or after 1 January 2018. Early adoption is permitted. The group intends to adopt NZ IFRS 9 on its effective date however no impact is expected as no derivatives used by the company currently qualify for hedge accounting.

NZ IFRS 15, 'Revenue from contracts with customers' deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces NZ IAS 18 'Revenue' and NZ IAS 11 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after 1 January 2017 and earlier application is permitted. The group intends to adopt NZ IFRS 15 on its effective date but does not believe there will be any material impact.

IFRS 16 'Leases' was issued by The International Standards Board in January 2016 and replaces the previous leases Standard, IAS 17 Leases, and related interpretations. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases.

IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. As a result all leases are treated in a similar way to finance leases applying IAS 17. Leases are 'capitalised' by recognising the present value of the lease payments as an asset. If lease payments are made over time, a company also recognises a financial liability representing its obligation to make future lease payments. As such the most significant effect of the new requirements in IFRS 16 will be an increase in the lease assets and liabilities. IFRS 16 is effective from 1 January 2019 with early adoption allowable if IFRS 15 also adopted. The group intends to adopt NZ IFRS 16 on its effective date but has not yet quantified the estimated impact of adoption.

There are no other NZ IFRSs or NZ IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Group.

## 4. REVENUE FROM OPERATIONS

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Sale of goods | 69,047 | 64,014 |
| Royalty income | 158 | - |
| **Total revenue** | **69,205** | **64,014** |

## 5. OTHER INCOME

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Research and development grant | 512 | 465 |
| Licensing income | 1,597 | 1,830 |
| Insurance recovery | 550 | - |
| **Total other income** | **2,659** | **2,295** |

The company purchased emergency supplies of Metoprolol at a cost of $823,000, which was damaged in transit and written off as part of Cost of Sales during the year. An insurance recovery of $550,000 has been made against this cost which is required to be reported as other income.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 6(a). NET OPERATING PROFIT

| $NZ000's | Note | 2017 | 2016 |
|---|---|---|---|
| **Loss before tax** | | **(18,330)** | **(13,309)** |
| **After charging the following specific expenses:** | | | |
| Finished goods material component of cost of goods sold | | 41,671 | 39,817 |
| Inventory write off | | 1,536 | 618 |
| Audit fees and review of financial statements | 6(b) | 149 | 134 |
| Rental expense | | 502 | 532 |
| Operating leases | | 422 | 382 |
| Share options expense | | 230 | 65 |
| **Short term employee emoluments:** | | | |
| Selling and distribution expenses | | 6,233 | 6,046 |
| General and administrative expenses | | 1,594 | 2,084 |
| Research and development expenses | | 1,362 | 1,113 |
| | | 9,189 | 9,243 |
| **Research and development expenses:** | | | |
| Product development | | 9,222 | 5,867 |
| New market development | | 2,005 | 2,225 |
| | | 11,227 | 8,092 |
| **Depreciation:** | | | |
| Plant and machinery | | 99 | 103 |
| Furniture and fixtures | | 29 | 29 |
| Vehicles | | 15 | 22 |
| | | 143 | 154 |
| **Amortisation:** | | | |
| Patents | | 99 | 91 |
| Software | | 84 | 23 |
| | | 183 | 114 |
| **Finance costs:** | | | |
| Interest | | 3,186 | 3,436 |
| Foreign exchange losses/(gains) | | 710 | (1,405) |
| Other financing costs | | (18) | (12) |
| | | 3,878 | 2,019 |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 6(b). FEES PAID TO AUDITORS

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **Audit of financial statements** | | |
| Audit of annual financial statements – PwC | 126 | 93 |
| Review of half year financial statements – PwC | 23 | 41 |
| **Total fees for audit services** | **149** | **134** |
| | | |
| **Other services** | | |
| Performed by PwC: | | |
| Tax due diligence services | - | 28 |
| Assurance report on ASX pro forma balance sheet | - | 18 |
| IPO and capital raising assurance services and accounting advice | - | 160 |
| **Total other services** | **-** | **206** |
| **Total fees paid to auditor** | **149** | **340** |

In 2017, no fees (2016:$160k) were paid to PricewaterhouseCoopers in relation to IPO and capital raising assurance services. Of these costs nil (2016:$141k) were included within IPO, Listing and Capital raising costs expense in that year with none (2016:$19k) being attributed to the cost of issue of shares and offset in contributed equity.

## 7. INCOME TAX

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **(a) Tax expense** | | |
| **Loss before tax** | **(18,330)** | **(13,309)** |
| | | |
| Tax calculated at domestic tax rates applicable | (5,049) | (3,752) |
| Expenses not deductible | 84 | 830 |
| Current year losses not recognised | 5,094 | 2,715 |
| Previous year losses now recognised | (197) | - |
| NRWT expense | 121 | - |
| Prior year adjustment | 5 | 165 |
| **Tax expense/(benefit)** | **58** | **(42)** |
| | | |
| **Comprising:** | | |
| Current tax | 117 | 96 |
| Deferred tax | (59) | (138) |
| | **58** | **(42)** |

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **(b) Deferred tax balance** | | |
| Provisions | 610 | 546 |
| | **610** | **546** |

Deferred tax assets relating to unused tax loss carry-forwards and to deductible temporary differences are recognised if it is probable that they can be offset against future taxable profits or existing temporary differences. As at 31 March 2017, the Group recognised deferred tax assets on temporary differences totalling $610,000 (2016: $546,000) since it was foreseeable that temporary differences could be offset against future taxable profits. On the basis of the approved business plans of subsidiaries, AFT Pharmaceuticals Limited considers it probable that temporary differences can be offset against future taxable profits. There is no expected change in capital structure in the near future which is expected to affect the recoverability of the recognised deferred tax assets.

The amount of tax losses carried forward that is available for future utilization is $39,815,000 (FY 2016: $21,531,000). No deferred tax asset has been recognized in relation to these losses.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 7. INCOME TAX (Continued)

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **(c) Imputation and franking credits available for use** | | |
| NZD | 600 | 600 |
| AUD | 319 | 319 |

## 8. INVENTORIES

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Inventory on hand | 19,046 | 16,930 |
| Provision for obsolescence | (328) | (431) |
| | **18,718** | **16,499** |

Inventory on hand comprises pharmaceutical goods ready for resale.

The value of inventory is transferred to cost of sales in the income statement when sold.

## 9. TRADE AND OTHER RECEIVABLES

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Trade receivables (see note below) | 17,403 | 15,446 |
| Prepayments (see note below) | 1,959 | 2,029 |
| | **19,362** | **17,475** |

### Ageing of overdue trade debtors but not considered impaired

| $NZ000's | 1-30 Days | 31-60 Days | 61-90 Days | 90+ Days | Total |
|---|---|---|---|---|---|
| 31 March 2017 | 323 | 167 | 3 | - | **493** |
| 31 March 2016 | 2,641 | 87 | - | 31 | **2,759** |

All balances are expected to be settled within the next 12 months.

Note: FY 2016 comparatives have been reclassified $1,187,000 from inventory to reflect stock purchase deposits as prepayments.

## 10. CASH AND CASH EQUIVALENTS

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Cash at bank | 15,876 | 7,936 |
| Cash on hand | 29 | 44 |
| | **15,905** | **7,980** |
| Cash on term deposit | 75 | 20,075 |
| **Total cash** | **15,980** | **28,055** |

Cash at bank earns on average less than 1% of interest.

Term deposits are at various interest rates and maturity dates, all within 12 months.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 11. PROPERTY PLANT & EQUIPMENT

| $NZ000's | Plant and Machinery | Furniture and Fixtures | Vehicles | Total |
|---|---|---|---|---|
| **(a) Cost** | | | | |
| **Balance 31 March 2015** | **576** | **362** | **267** | **1,205** |
| Additions | 118 | 34 | - | 152 |
| Disposals | - | - | (49) | (49) |
| **Balance 31 March 2016** | **694** | **396** | **218** | **1,308** |
| Additions | 104 | 18 | - | 122 |
| Disposals | - | - | - | - |
| **Balance 31 March 2017** | **798** | **414** | **218** | **1,430** |
| **(b) Depreciation** | | | | |
| **Balance 31 March 2015** | **(434)** | **(163)** | **(197)** | **(794)** |
| Depreciation | (103) | (29) | (22) | (154) |
| Disposals | - | - | 47 | 47 |
| **Balance 31 March 2016** | **(537)** | **(192)** | **(172)** | **(901)** |
| Depreciation | (99) | (29) | (15) | (143) |
| Disposals | - | - | - | - |
| **Balance 31 March 2017** | **(636)** | **(221)** | **(187)** | **(1,044)** |
| **(c) Carrying amounts** | | | | |
| **Balance 31 March 2016** | **157** | **204** | **46** | **407** |
| **Balance 31 March 2017** | **162** | **193** | **31** | **386** |

## 12. INTANGIBLE ASSETS

| $NZ000's | Trademarks | Patents | Software | Total |
|---|---|---|---|---|
| **(a) Cost** | | | | |
| **Balance 31 March 2015** | **278** | **1,602** | **241** | **2,121** |
| Additions | 161 | 377 | 19 | 557 |
| Disposals | - | (1) | - | (1) |
| **Balance 31 March 2016** | **439** | **1,978** | **260** | **2,677** |
| Additions | 171 | 204 | 254 | 629 |
| Disposals | - | (9) | - | (9) |
| **Balance 31 March 2017** | **610** | **2,173** | **514** | **3,297** |
| **(b) Amortisation** | | | | |
| **Balance 31 March 2015** | **-** | **(247)** | **(205)** | **(452)** |
| Amortisation | | (91) | (23) | (114) |
| Disposals | - | - | - | - |
| **Balance 31 March 2016** | **-** | **(338)** | **(228)** | **(566)** |
| Amortisation | - | (99) | (84) | (183) |
| Disposals | - | - | - | - |
| **Balance 31 March 2017** | **-** | **(437)** | **(312)** | **(749)** |
| **(c) Carrying amounts** | | | | |
| **Balance 31 March 2016** | **439** | **1,640** | **32** | **2,111** |
| **Balance 31 March 2017** | **610** | **1,736** | **202** | **2,548** |

Trademarks are acquired to protect the current and future revenue streams of the group.

They are considered to have an indefinite useful life whilst they continue to protect revenue streams.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 13(a). INVESTMENT IN SUBSIDIARIES

| | Interest Held | | | |
|---|---|---|---|---|
| | 2017% | 2016% | Country of Incorporation | Principal Activities |
| AFT Pharmaceuticals (AU) Pty Ltd | 100% | 100% | Australia | Distribution of pharmaceuticals in Australia |
| AFT Pharmaceuticals Singapore Pte Ltd | 100% | 100% | Singapore | Registration of pharmaceuticals in Singapore |
| AFT Pharmaceuticals (S.E. Asia) Sdn Bhd | 100% | 100% | Malaysia | Distribution of pharmaceuticals in Malaysia |
| AFT Orphan Pharmaceuticals Limited | 65% | 65% | New Zealand | No activity |
| AFT Limited Partner Limited | 100% | 100% | New Zealand | Partner in Dermatology Specialties LP |
| AFT Dermatology Limited | 100% | 100% | New Zealand | Distribution of pharmaceuticals |

Investment comprises ordinary shares held at cost.

All subsidiaries have a balance date of 31 March.

## 13(b). INVESTMENT IN JOINT VENTURE PARTNERSHIP

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Interest in joint venture company, at cost | 1,343 | 487 |
| Equity accounted earnings of joint venture partnership | (716) | (302) |
| **Net equity investment in joint venture partnership** | **627** | **185** |

The joint venture partnership of the Group and its activities are as follows:

| | 2017 % Interest held | 2016 % Interest held |
|---|---|---|
| Dermatology Specialties LP | 50% | 50% |

Principal activities: Development and distribution of pharmaceuticals

Dermatology Specialties LP was incorporated on 22 June 2015. Movements in investment in the joint venture partnership during the year comprise:

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Balance at start of year | 185 | - |
| Investment during the year | 856 | 487 |
| Share of current year loss | (414) | (302) |
| Dividend received | - | - |
| **Balance at end of year** | **627** | **185** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

The following table summarises the financial information relating to the Group's joint venture partnership, and represents 100% of the joint venture partnership net assets, revenues and net profits.

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **Extracts from joint venture partnership balance sheet (unaudited)** | | |
| Current assets | - | - |
| Non-current assets | 2,175 | 2,169 |
| Current liabilities | (95) | (117) |
| Non-current liabilities | - | - |
| **Net assets** | **2,080** | **2,052** |
| | | |
| **Extracts from joint venture partnership income statement (unaudited)** | | |
| Revenue | - | - |
| Net profit after taxation | (828) | (604) |

The joint venture did not have any contingent liabilities or capital commitments at balance date (2016: nil).

## 14. TRADE AND OTHER PAYABLES

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Trade payables | 7,348 | 8,140 |
| GST payable | 1,161 | 616 |
| Employee entitlements | 615 | 621 |
| Other payables | 1,945 | 1,051 |
| | **11,069** | **10,428** |

## 15. PROVISIONS

| $NZ000's | 2017 | Additional Provisions | Utilised | 2016 | Additional Provisions | Utilised | 2015 |
|---|---|---|---|---|---|---|---|
| Customer rebates | 3,386 | 3,386 | (2,422) | 2,422 | 2,422 | (998) | 998 |
| Supplier rebates | 564 | 564 | (661) | 661 | 661 | (892) | 892 |
| | **3,950** | **3,950** | **(3,083)** | **3,083** | **3,083** | **(1,890)** | **1,890** |

Customer rebates are based on the customers' ability to achieve certain sales targets and are computed using the expected rebate percentage for sales made during the period.

Supplier rebates are based on profit sharing arrangements with suppliers which are estimated on achieving expected set margin targets, and are expected to be utilised within the next 12 months.

## 16. INTEREST BEARING LIABILITIES

| $NZ000's | 2017 | 2016 |
|---|---|---|
| CRG (Capital Royalty Partners) loans | 23,426 | 23,161 |
| | **23,426** | **23,161** |

The term loan agreement with CRG commenced in May 2014 and has a facility to be drawn down up to US$30million. It is for a six year term for which the first four years only interest is payable, some of which may be compounded, with the principal to be repaid in equal quarterly instalments in years five and six.

The loan has a general security over the assets of the Group together with a group guarantee. Interest is fixed at 13.5% p.a. Details of the two covenants relevant to the loan are in note 24 Management of Capital.

The carrying amount of the CRG loan is substantially in line with the fair market value as per balance sheet date. The interest rate of the contract is in line with the market interest rate.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 17. SHARE CAPITAL

| | 2017 Number | 2016 Number | 2017 $'000 | 2016 $'000 |
|---|---|---|---|---|
| Ordinary share capital | 96,834,838 | 96,834,838 | 55,994 | 55,994 |
| Less capital raising costs | - | - | (2,174) | (2,092) |
| Redeemable Preference Shares | 3,330,000 | - | 9,124 | - |
| | **100,164,838** | **96,834,838** | **62,944** | **53,902** |

| $NZ000's | 2017 $'000 | 2016 $'000 |
|---|---|---|
| Share capital at beginning of the year | 53,902 | 12,892 |
| Issue of Redeemable Preference Shares | 9,124 | - |
| Issue of Series B Preferred Shares | - | 9,392 |
| IPO | - | 32,675 |
| Less capital raising costs | (82) | (1,057) |
| | **62,944** | **53,902** |

**FY 2016**

During May, June and July 2015 the Group issued 54,120 new Series B Preferred Shares at US$129 each to existing shareholders, Directors and a group of specialist pharmaceutical investors. These were fully subscribed and increased equity by NZD$9.4million. The series B Preferred shares carried a yield of net 5% payable in cash quarterly.

The Series B Preferred Shares converted 1:1 automatically immediately before the closing of the public offering of shares in the company which resulted in a market capitalisation of the company of at least US$150million. The Series B Preferred Shares did not carry voting rights other than on class matters particular to the Series B Preferred Shares.

In December 2015, the company completed an Initial Public Offering (IPO), culminating with dual listing on both the New Zealand Stock Exchange (NZX) and the Australian Stock Exchange (ASX) on 22 December 2015. This IPO involved raising $32.6m of new equity, all being Ordinary shares, the conversion of all Preference shares (both A and B) to Ordinary shares, and the sell down by the Atkinson Family Trust of 1.07 million shares. In addition 7,700 Ordinary shares were issued to staff at nil consideration.

At 31 March 2016 there were 96,834,838 Ordinary shares on issue.

In addition, staff of AFT Pharmaceuticals Limited were issued with 861,000 options to purchase one ordinary share per option in the company at the issue price of NZ$2.80 per share. 166,963 of these options may be exercised after 22 December 2017 with the balance exercisable on 22 December 2018 or later.

**FY 2017**

On 24 March 2017, the company issued 3,330,000 Redeemable Preference shares at $2.74 each. These shares attract a dividend of 9.4% accruing quarterly which may be satisfied in cash or with additional redeemable preference shares at the company's option.

They do not carry any right to vote except at meetings of an "interest group" of holders of redeemable shares.

They may be redeemed at the option of the company at any time two years or more after issue. On redemption, the company would pay the issue price plus dividends accrued to the date of redemption.

After three years from issue, they may be converted to ordinary shares at the option of the holder in multiples of 100,000. The holder would receive one ordinary share for every redeemable share held and a number of ordinary shares calculated by dividing the amount of any accumulated dividends by the issue price.

Optional conversion events arise if one of a number of conditions occur. These conditions were notified to NZX and ASX at the time of issue of the Redeemable Preferences Shares, and are available on the company website.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 18. RECONCILIATION OF PROFIT AFTER TAX WITH NET CASH FLOW FROM OPERATING ACTIVITIES

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Loss after tax | (18,388) | (13,267) |
| **Non-cash items:** | | |
| Depreciation | 143 | 154 |
| Amortisation | 183 | 114 |
| Impact of foreign exchange on cash and cash equivalents | 456 | (1,773) |
| Share options expense (see note below) | 230 | 65 |
| **Movement in working capital:** | | |
| (Increase)/Decrease in inventories | (2,219) | (200) |
| (Increase)/Decrease in trade and other receivables | (1,887) | (6,409) |
| Increase/(Decrease) in trade and other payables (see note below) | 2,282 | 7,450 |
| Increase/(Decrease) in income tax | 138 | (76) |
| **Net cash used in operating activities** | **(19,062)** | **(13,942)** |

Note : In FY 2016 , the share options expense was included in other payables.

## 19. RELATED PARTIES

The Group had related party relationships with the following entities:

| Related party | Nature of relationship |
|---|---|
| Redvers Limited | Common Director |
| Mainz Consulting Limited | Common Director |
| CRG (Capital Royalty Partners) | Shareholder |

The following transactions were carried out with these related parties:

### (i) Consultation fees

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Redvers Limited | - | 113 |
| Mainz Consulting Limited | - | 21 |
| **Total consultation fees** | **-** | **134** |

### (ii) Loans

| $NZ000's | 2017 | 2016 |
|---|---|---|
| CRG (Capital Royalty Partners) – refer to note 16 | 23,426 | 23,161 |
| **Total loan balances** | **23,426** | **23,161** |

### (iii) Key management compensation

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Directors' fees | 289 | 187 |
| Other Director remuneration | - | 134 |
| Executive salaries | 1,092 | 1,067 |
| Short term benefits | 238 | 39 |
| **Key management compensation** | **1,619** | **1,427** |

Key management includes external Directors, the Chief Executive Officer, the Chief of Staff, the Chief Financial Officer and the Director of International Business Development. These positions are mainly responsible for the planning, controlling and directing the activities of the business. The Chief of Staff is the spouse of the Chief Executive Officer.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 19(b). STAFF SHARE OPTIONS

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | Average exercise price $ per share | Options '000's | Average exercise price $ per share | Options '000's |
| **Balance at beginning of year** | 2.80 | 861 | - | - |
| Issued | - | - | 2.80 | 861 |
| Forfeited | - | (11) | - | - |
| Exercised | - | - | - | - |
| Lapsed | - | - | - | - |
| **Balance at end of year** | **2.80** | **850** | **2.80** | **861** |

Weighted average share price for options exercised during the period $nil (2016: $nil).

Of the 850,000 outstanding options, nil are currently exercisable (2016: nil)

Share options outstanding at the end of the year have the following expiry dates, exercise dates and exercise prices:

| Expiry Month | Exercise Month | Exercise Price | 2017 | 2016 |
|---|---|---|---|---|
| April 2020 | December 2017 | 2.80 | 151,629 | 155,296 |
| April 2020 | December 2018 | 2.80 | 698,371 | 705,704 |
| **Total share options outstanding** | | | **850,000** | **861,000** |

The weighted average remaining contractual life of options outstanding at the end of the period was 3 years (2016: 4 years)

### Share options reserve

| $NZ000's | 2017 | 2016 |
|---|---|---|
| **Balance at beginning of year** | (65) | - |
| Current year amortisation | (230) | (65) |
| **Balance at end of year** | **(295)** | **(65)** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 20. FINANCIAL RISK MANAGEMENT

### (a) Managing financial risk

The Company's activities expose it to various financial risks as detailed below.

- **Market risk**

  Management is of the opinion that the Group's exposure to market risk at balance date is defined as:

| Risk Factor | Description | Sensitivity |
|---|---|---|
| (i) Currency risk | Exposure to changes in foreign exchange rates on assets and liabilities of the subsidiary | As below |
| (ii) Interest rate risk | Exposure to changes in interest rates on borrowings | As below |
| (iii) Other price risk | No commodity securities are bought, sold or traded | Nil |

- **Foreign exchange risk**

  The Group purchase goods and services from overseas suppliers in a number of currencies, primarily, NZD, AUD, USD, EUR and GBP, and has borrowings which are denominated in US Dollar amounts. This exposes the Group to foreign currency risk. The Group manages foreign currency risk through use of derivative arrangements, in particular forward exchange contracts. The exposure is monitored on a regular basis based on Group foreign exchange policies. Future revenues from markets outside Australasia will be denominated primarily in USD and EUR which will provide a natural hedge against these costs.

  In the current year (FY 2017) Foreign Exchange losses totaled $710k (2016 -$1,405k gain) of which $260k (2016: -$1,614k losses) were unrealised gains on the USD denominated CRG loan. Future revenues from markets outside Australasia will be derived in USD which will be used towards repaying this debt as it falls due. The balance of the losses are derived from the restatement of the cash balances at the spot rate on the year end balance date of 31 March 2017 and the change in spot rates during the time between when expenses are recorded in the general ledger and when they are paid.

  A 1% increase or decrease in foreign exchange rates on assets and liabilities will reduce/increase equity by $53,000 (2016: $113,000) and reduce/increase the profit or loss by $341,000 (2016: $296,330).

The following forward foreign exchange contracts were held at the end of the 2017 financial year:

| Forward Foreign Exchange Contracts | | | | |
|---|---|---|---|---|
| Buy Currency | Buy Currency Amount ('000) | Sell Amount $NZ000's | Buy Amount 31-Mar-17 $NZ000's | Fair Value $NZ000's |
| EUR | 3,012 | 4,806 | 4,956 | (150) |
| GBP | 544 | 1,027 | 1,075 | (48) |
| USD | 2,730 | 3,902 | 3,895 | 7 |
| AUD | (750) | (807) | (794) | (13) |
| **Total exposure as at 31 March 2017:** | | | | **(204)** |

All contracts mature within one year from 31 March 2017.

The following forward foreign exchange contracts were held at the end of the 2016 financial year:

| Forward Foreign Exchange Contracts | | | | |
|---|---|---|---|---|
| Buy Currency | Buy Currency Amount ('000) | Sell Amount $NZ000's | Buy Amount 31-Mar-16 $NZ000's | Fair Value $NZ000's |
| EUR | 3,500 | 5,914 | 5,815 | (99) |
| GBP | 610 | 1,358 | 1,278 | (80) |
| USD | 5,755 | 8,626 | 8,403 | (223) |
| **Total exposure as at 31 March 2017:** | | | | **(402)** |

All contracts matured within one year from 31 March 2016.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 20. FINANCIAL RISK MANAGEMENT (Continued)

- **Interest rate risk**

Borrowings are at a fixed interest rate which exposes the group to fair value interest rate risk. There are no specific derivative arrangements to manage this risk

- **Credit risk**

Financial instruments which potentially subject the Group to credit risk principally consist of accounts receivable. Regular monitoring is undertaken to ensure that the credit exposure remains within the Group's normal terms of trade.

The Group has one significant concentration of credit risk at 31 March 2017 with the largest debtor being $7,640,667 (2016: $4,525,638). There has been no past experience of default and no indications of default in relation to this debtor. There are no impaired receivables at 31 March 2017 (2016: nil). Refer to Note 21.

The Group's cash and short term deposits are placed with high credit quality financial institutions. Accordingly, the Group has no significant concentration of credit risk other than bank deposits with 23.9% of total assets at the Bank of New Zealand (2016: 32.3%), 3.3% at NAB Bank (2016: 2.7%) and 0% with ANZ (2016: 7.6%). The carrying value of financial assets represents the maximum exposure to credit risk.

- **Liquidity risk**

Liquidity risk is the risk that the Group may encounter difficulty in raising funds at short notice to meet its commitments and arises from the need to borrow funds for working capital. The Directors monitor the risk on a regular basis and actively manage the cash available to ensure the net exposure to liquidity risk is minimised. Since May 2014, there has been a $1million BNZ overdraft immediately available.

The liquidity/maturity profile of the liabilities is as follows:

| Liquidity Profile | | | | | |
|---|---|---|---|---|---|
| **$NZ000's<br>31 March 2017** | **< 1 Year** | **1-2 Years** | **2-5 Years** | **> 5 Years** | **Total** |
| Trade and other payables | (11,069) | - | - | - | (10,567) |
| Borrowings | (2,144) | (14,454) | (13,283) | - | (29,881) |
| Derivative liabilities (outbound) | (9,132) | - | - | - | (9,132) |
| Derivative liabilities (inbound) | 8,928 | - | - | - | 8,928 |
| **Totals** | **(13,417)** | **(14,454)** | **(13,282)** | **-** | **(41,154)** |
| **31 March 2016** | | | | | |
| Trade and other payables | (11,220) | - | - | - | (11,220) |
| Borrowings | (2,623) | (2,168) | (28,529) | - | (33,320) |
| Derivative liabilities (outbound) | (15,496) | - | - | - | (15,496) |
| Derivative liabilities (inbound) | 15,094 | - | - | - | 15,094 |
| **Totals** | **(14,245)** | **(2,168)** | **(28,529)** | **-** | **(44,942)** |

### (b) Fair Values

The carrying value of financial assets and liabilities (trade receivables and trade payables) approximates their fair value. Trade receivables are valued net of provision and trade payables are valued at their original amounts by contract.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 21. SEGMENT REPORTING

| | Operating Segments | | | | |
|---|---|---|---|---|---|
| **$NZ000's 31 March 2017** | **Australia** | **New Zealand** | **Asia** | **Rest of World** | **Total** |
| **Revenue** | **37,064** | **29,168** | **1,005** | **1,968** | **69,205** |
| Other income | - | 550 | - | 2,109 | 2,659 |
| Depreciation and amortisation | 25 | 294 | 7 | - | 326 |
| **Loss before tax** | **(3,633)** | **(5,782)** | **(689)** | **(8,226)** | **(18,330)** |
| Finance income | - | 347 | - | - | 347 |
| Finance costs | (2) | (3,184) | - | - | (3,186) |
| Other gains/(losses) | (24) | (544) | (124) | - | (692) |
| **Total assets** | **22,837** | **33,774** | **1,620** | **-** | **58,231** |
| Property, plant and equipment | 54 | 317 | 15 | - | 386 |
| Intangible assets | - | 2,548 | - | - | 2,548 |
| **Capital expenditure** | **19** | **722** | **10** | **-** | **751** |
| **31 March 2016** | | | | | |
| **Revenue** | **31,224** | **31,135** | **648** | **1,007** | **64,014** |
| Other income | - | 1 | - | 2,294 | 2,295 |
| Depreciation and amortisation | 30 | 233 | 5 | - | 268 |
| **Loss before tax** | **(3,233)** | **(4,902)** | **(1,015)** | **(4,159)** | **(13,309)** |
| Finance income | - | 291 | - | - | 291 |
| Finance costs | (13) | (3,424) | - | - | (3,437) |
| Other gains/(losses) | - | 1,412 | 6 | - | 1,418 |
| **Total assets** | **18,578** | **46,515** | **211** | **-** | **65,304** |
| Property, plant and equipment | 61 | 334 | 11 | 1 | 407 |
| Intangible assets | - | 2,111 | - | - | 2,111 |
| **Capital expenditure** | **54** | **648** | **2** | **-** | **704** |

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (CODM). For the purposes of NZ IFRS 8 the CODM is a group comprising the Board of Directors together with the Chief Executive Officer, the Chief of Staff, the Chief Financial Officer and the Director of International Business Development. This has been determined on the basis that it is this group which determines the allocation of the resources to segments and assesses their performance.

The Group has four operating segments based on geographical location reportable under NZ IFRS 8, as described below, which are the Group's strategic groupings of business units. The following summary describes the operations in each of the Group's reporting segments:

**New Zealand** – Includes the Head Office function for the Group, supplier relationships and procurement of all stock for the group, all regulatory activity, all marketing activity and all finance activity. The sales and distribution activity principally relates to the New Zealand market.

**Australia** – Includes the sales and distribution activity relating to the Australian market.

**Asia** – Includes the sales and distribution activity relating to the Asian market (Brunei, Hong Kong, Malaysia, Philippines, Singapore and Vietnam).

**Rest of World** – Includes the out licensing of IP developments to markets in which AFT does not have a presence and the export of products to export markets (Balkans, Iraq, Pacific Islands, Saudi Arabia, UAE). The costs of research and development and new market development activity not specific to the other segments are expensed to this segment.

**Major Customers** – Revenues from one customer of the Australian segment (being a licensed wholesaler) represent approximately NZ$15.5million (2016: NZ$11.99million) and from one customer of the New Zealand segment (also being a licensed wholesaler) represent approximately $13.9million (2016: $12.91million) of the Group's total revenues.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 22. CONTINGENT LIABILITIES

In May 2015, AFT Pharmaceuticals Ltd signed as guarantor of AFT Pharmaceuticals Pty Ltd for its 5-year lease contract with Shannon Wicks Pty Ltd for the premises occupied in Sydney, Australia. The company has placed NZD$75,000 on term deposit with the BNZ. This sum is security for a guarantee issued by the BNZ in favour of the NZX, should the company ever default on any of its payment obligations to NZX.

## 23. COMMITMENTS

### (a) Capital Commitments

The Group has no capital commitments at 31 March 2017 (2016: nil).

### (b) Lease Commitments

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Due within one year | 890 | 888 |
| Due later than one year but within five years | 2,261 | 643 |
| Due later than 5 years | 1,750 | - |
| | **4,901** | **1,531** |

The above includes leases for property, vehicles and equipment.

### (c) Other Commitments

The company has entered into contracts to complete clinical trials overseas. These contracts call for stage or milestone payments to be made progressively when those stages or milestones are achieved. Certain conditions allow for the termination of the trials, with future obligations extinguished. The aggregate expected amounts likely to be paid under these contracts is NZ$4.0million (2016: $9.8million).

The Group leases the business premises in Takapuna, Auckland, New Zealand for $421,000 plus GST (including operating expenses) per annum. The lease has been renewed with final expiry on 12 April 2026. The Group also leases premises in North Ryde, Sydney Australia for AUD$106,177 (including operating expenses) per annum. It has an initial term of 5 years which will expire on 15 May 2020 with one right of renewal for another 5 years with final expiry on 14 May 2025. The Group also leases a number of motor vehicles and office equipment which all have a final expiry date not exceeding 3 years 9 months.

## 24. MANAGEMENT OF CAPITAL

The Group's objectives when managing capital are:

- to safeguard the Group's ability to continue as a going concern so that it can continue to provide returns to its shareholders, and
- to maintain a strong capital base to support the development of its business.

The Group meets these objectives through a mix of equity capital and borrowings. The level and mix of capital is determined by the Group's internal Corporate Governance Policies.

The long term debt in the form of the CRG Loan was used to replace the trade facility from the BNZ in May 2014.

Under the CRG Loan Agreement there are two covenants. The first requires a minimum bank balance of NZ$4million at each month end and a minimum balance of NZ$1million at any one time. The second is for Revenues (inclusive of Licensing income) to exceed NZ$67.75million for the 2017 financial year (2016: NZ$64.5million). This revenue covenant was reduced from its previous level of $74.5m in November 2016. On 24 May 2017, CRG removed the revenue covenants from the loan agreement for 2018 and 2019. Under the BNZ facility there is a covenant requirement that the facility comprising an overdraft and letter of credit facility must not exceed the total of 70% of acceptable debtors plus 40% of acceptable stock.

The Group has complied with both the CRG and BNZ covenants during the 2017 financial year.

In May 2015 the group raised $9.4m of further equity through the issuance of Preference B Shares. In December 2015 a further $32.6m was raised through an initial public offering of shares which are jointly listed on both the NZX and ASX. In March 2017 the Group issued 3,330,000 Redeemable Preference Shares raising $9.1m. Details are covered in Note 17.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the year ended 31 March 2017

## 25. EARNINGS PER SHARE

| $NZ000's | 2017 | 2016 |
|---|---|---|
| Loss after tax | (18,388) | (13,267) |
| Weighted average ordinary shares | 97,112,340 | 27,573,214 |
| Basic and diluted earnings/(loss) per share ($) | (0.19) | (0.48) |

Basic earnings per share is computed by dividing net earnings by the weighted average number of ordinary shares outstanding during each period (assuming that Redeemable Preference Shares have converted to ordinary shares). For FY 2016 Preferred shares are considered to be anti-dilutive for the earnings per share calculation.

Diluted earnings per share is computed by dividing net earnings adjusted for the share options cost, by the diluted weighted average number of ordinary shares (as if all options have been exercised).

## 26. DIVIDENDS PER SHARE

No dividends have been declared to the ordinary shareholders of the parent company during the current year, nor in the FY 2016.

## 27. SUBSEQUENT EVENTS

On 24 May 2017, the directors confirmed an offer to existing shareholders to subscribe for up to NZ$15,000 of new shares at a price discounted from market price. This is expected to raise up to NZ$1.25 million.

On 24 May 2017, CRG removed the revenue covenants from the loan agreement for 2018 and 2019.

AFT pharmaceuticals

Working to improve your health