17 September 2019

Smart Metering Systems plc

Interim results

Smart Metering Systems plc (AIM: SMS, the Group), the UK's largest integrated installer for independent energy suppliers and manager of smart meters, has published its half year results for the six months ended 30 June 2019.

£'000	H1 2019	H1 2018
Group revenue	54,205	46,741
Pre-exceptional EBITDA[1]	25,823	23,626
EBITDA	20,616	23,405
(Loss)/profit before taxation	(1,725)	10,124
Underlying profit before taxation[2]	4,644	11,404
Underlying basic EPS (p)[3]	3.40	8.40
Basic EPS (p)	(1.28)	7.45
Dividend per share (p)	2.30	2.00
Net debt	186,592	141,989

1 Pre-exceptional EBITDA is statutory EBITDA excluding exceptional items.

2 Underlying profit before taxation is profit before taxation excluding exceptional items and amortisation of intangibles.

3 Underlying basic EPS is underlying profit after taxation divided by the weighted average number of ordinary shares for the purpose of basic EPS.

A reconciliation between reported and underlying performance is detailed in the Financial Review section below.

Key points

- Long term index-linked annualised recurring revenue (ILARR) growth of 14.1% to £85.9m – ahead of the Board's expectations
- Group's domestic smart portfolio now above 1 million – a net increase of 156,000 domestic smart meters installed in H1
- Industry-wide technical issues slowed installation in H1, signs of expected recovery emerging
- Significant cash and unutilised debt facility to support rollout of smart meters
- Financial, technical and human resources in place to support 2 million meter order book as mass SMETS2 rollout commences
- Revenues and ILARR for the current financial year are anticipated to be ahead of market expectations whilst pre-exceptional EBITDA is expected to be marginally below current market expectations with a consequent impact on underlying profit before tax
- In discussions about sale of a minority of meter assets. If completed, at an appropriate value, this transaction will provide significant additional liquidity and demonstrate the inherent value of the Group's metering asset base

Alan Foy, Chief Executive Officer, commented:

"We have continued to grow our annualised recurring revenue, our key financial metric, ahead of expectations and now have over 3.46 million metering and data assets under management of which over 1 million are smart.

"The widely reported industry-wide installation issues are now substantially addressed and the mass rollout of SMETS2 can now commence - this is expected to result in a pick up in the installation run-rate both in the latter part of 2019 and into 2020.

"With over 500 engineers and significant cash and debt facilities, we have the engineering and financial resources to handle our order book of approximately 2 million meter installations with headroom for further growth.

"We are in discussions about a sale of a minority of our meter asset portfolio, which, if completed at an appropriate value, would provide significant additional liquidity and demonstrate the inherent value of our substantial asset base."

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Notes to editors

SMS plc (www.sms-plc.com) installs smart meters and data loggers that facilitate effective energy management and a low carbon future. Established in 1995, SMS provides a full end-to-end service for metering financing, installation, management and maintenance, with a highly skilled workforce and deep engineering expertise.

SMS had installed 3.46 million meter and data assets as of 30 June 2019. SMS's smart meter expertise also enables the Company to provide consultancy services that allow organisations and corporates to enhance long term efficiency and effectiveness in the management of energy.

SMS's energy management and asset installation services also include infrastructure design, installation, consultancy and project management services for new gas, electricity, water and telecoms connections for licensed energy and telecoms suppliers, end consumers and the UK's licensed electricity Distribution Network Owners (DNOs).

SMS employs in excess of 1,200 people across the UK who support the installation and ongoing management of metering assets.

SMS plc is headquartered in Glasgow with 12 locations across the UK.

SMS's shares are listed on AIM.

Overview

The Group has seen continued growth in its gas and electricity meter portfolio, with a net increase of 156,000 domestic smart meters installed in H1 2019, taking the domestic smart meter portfolio alone through the 1 million meter milestone.

The Group's total number of metering and data assets under management, including third-party assets, increased by c.10.5% to 3.46 million (31 December 2018: 3.13 million) with 3,023,000 (31 December 2018: 2,658,000) meter assets under management at 30 June 2019, of which 1,002,000 are smart meters (31 December 2018: 846,000).

The UK energy market is changing rapidly and SMS is well placed to be at forefront of these developments with strong cross-sell potential into SMS's existing customer base. The Group purchased Solo Energy to establish new long-term revenue streams from new asset classes enabled by smart meters; further opportunities continue to be explored.

Index-linked recurring revenues

The Group's portfolio of meter and data assets generate index-linked, recurring revenues for its lifetime, supplemented with the provision of support and other continuing service opportunities.

ILARR, SMS's key financial metric for long term growth, increased by c.14.1% to £85.9m at 30 June 2019 (31 December 2018: £75.3m). ILARR from the domestic smart meter portfolio grew 19.6% to £32.4m, whilst ILARR from traditional domestic meters grew 14.4% to £19.6m. ILARR from industrial and commercial (I&C) meters grew c.10.6% to £21.0m and from data assets grew 5.7% to £12.9m.

This growth in ILARR is supported by continued momentum in contract wins; most recently the Group secured framework agreements with both British Gas Business and Opus Energy to install smart meters across their I&C customer base. Active engagement with these and other energy suppliers continues to be a key focus of the Group. The Group has an order book of c.2 million domestic smart meters which represents a c.£40m ILARR opportunity.

Through its existing customers alone, there is an opportunity to exchange a further c.4 million meters which represents an additional c.£80m ILARR opportunity. Beyond these, there is further potential ILARR from the ongoing targeting of additional energy suppliers.

In August, SMS acquired approximately c.72,000 SMETS1 domestic smart meters from an existing energy supply customer, increasing the Group's ILARR by c.£1.6m.

SMETS2 rollout

As previously announced, the Group's installation run rates in H1 2019 were behind initial expectations due to wider industry issues and UK government figures released at the end of August showed that the rate of domestic smart meter installations had fallen across the industry in the first six months of 2019.

Specifically, the rollout of SMETS2 meters was slowed by technical issues, primarily rooted in radiofrequency interference of smart meters in the North of England and Scotland, which caused compatibility issues in those regions. As a result, many energy suppliers have not yet been able to offer SMETS2 meters to all of their customers, limiting the portfolio available for exchange.

These issues have now been substantially resolved and the Group's customers are nearing full SMETS2 readiness. The Group is prepared for further increases through the remainder of the year, and into 2020 and beyond, as the smart meter programme progresses.

Positioned for accelerated installations

In line with its longer term growth strategy, the Group has retained, and continued to invest in, the financial, technical and human resources necessary to support a substantial increase in activity in H2 and beyond. SMS now has over 500 full time engineers.

The Group is therefore well placed to significantly increase the installation run rate in the latter part of 2019 and into 2020, as industry-wide activity accelerates. The Group also has ample financial resources to support such an acceleration with significant cash and unutilised credit facilities. H1 net debt rose to £186.6m due to increased inventory and capital expenditure, in line with the management's expectations.

Monetising of a minority of the Group's meter assets

The Group is in discussions with a number of specialist infrastructure investors with UK expertise about the sale of a minority of the Group's meter assets. If completed, at an appropriate value, this transaction will generate significant proceeds, demonstrate the value of part of the SMS' substantial asset base and will help fund future growth plans. However, there is no certainty that SMS will proceed with any such sale. A further update on the possible sale will be provided as and when appropriate.

Current trading and outlook

SMS is focused on continuing to deliver the mandated smart meter rollout on behalf of its energy supplier customers, which have a significant backlog of end consumers requiring a conversion to smart. The Group's significant contracted pipeline is for the conversion of c.2 million meters to smart, with opportunity to exchange an additional c.4 million meters.

With SMETS2 technical issues now substantially resolved and customer readiness for a mass rollout of SMETS2 meters, SMS expects engineering efficiency and installation run rates to continue to improve during the remainder of H2 2019 and into 2020.

In order to meet this opportunity, SMS has continued to invest in its engineering capacity. SMS has a scalable and secure data infrastructure, already operating over 3.46 million meter and data assets and, as a result of the investment made in H1, the installation capacity to fit over 50,000 smart meters a month.

SMS is now well positioned to be able to exploit these substantial opportunities in both the short and medium term.

The Group has an additional carrying cost as a result of the under utilisation of engineers previously disclosed. However, it is expected that approximately half of these costs will be mitigated in FY2019 by additional meter rental income. Overall, whilst revenues and ILARR are anticipated to be ahead of market expectations, the Board now expects pre exceptional EBITDA for the current financial year to be marginally below current market expectations due to an expected c.£3m additional net engineering cost, with a consequent impact on underlying profit before tax.

SMS's mission remains unchanged, striving to deliver the future of smart energy. Whilst the immediate focus is on the UK Domestic smart market opportunity, SMS is continuing to develop its capabilities to deliver innovative and integrated energy solutions to its customers, leveraging a growing installed smart meter base to enhance the Group's service position.

Operational review

Meter assets and data
ILARR has grown to £85.9m, largely as a result of the continued investment in smart meters and, in part, supported by an increase in traditional meter rental rates for deemed non-contracted customers to reflect the shorter expected lifespan for such meters.

There was also continued growth in the Group's customer order book following contract wins with British Gas Business and Opus Energy in respect of their I&C smart meter customers.

The Group's contracted pipeline of c.2million smart meters is expected to generate c.£40m additional ILARR, with a potential further c.4million smart meters generating c.£80m available from opportunities with existing contracted energy suppliers. The Group is also active within the market, with ongoing targeting of additional energy suppliers to further enhance the portfolio.

Full ILARR and unit movements from December 2018 to June 2019 are summarised as follows:

By unit type

	June 2019		December 2018		Change	
	ARR (£m)	**Units[1]**	ARR (£m)	Units[2]	ARR (£m)	Units
Domestic traditional	19.6	369,000	17.1	377,000	2.5	(8,000)
I&C	21.0	261,000	19.0	253,000	2.0	8,000
Smart	32.4	1,002,000	27.1	846,000	5.3	156,000
Data	12.9	434,000	12.1	477,000	0.8	(43,000)
Total	**85.9**	**2,066,000**	75.3	1,953,000	10.6	113,000

1Excludes 1,391,00 third-party meter management appointments.

2 Excludes 1,181,000 third-party meter management appointments.

By utility type

	30 June 2019 units	31 December 2018 units	Percentage change
Gas meter portfolio[1]	2,375,000	**2,106,000**	13%
Electricity meter portfolio	648,000	**552,000**	17%
Gas data portfolio	133,000	**131,000**	2%
Electricity data portfolio	301,000	**345,000**	(13%)
Total meter portfolio[1]	3,023,000	**2,658,000**	14%
Total data portfolio	434,000	**476,000**	(9%)
Total gas and electricity metering and data assets	3,457,000	**3,134,000**	10%

1 Includes third-party meter management appointments.

With BEIS having confirmed the proposed adoption and enrolment of SMETS1 meters into the central Data Communications Company (DCC), the Group continues to support its customers with this process, which is expected to start at the end of September.

All energy suppliers are mandated to bring such meters forward for adoption within a 12 month period. The Group's entire SMETS1 portfolio is capable of being adopted into the DCC, whether operating in smart or traditional mode.

SMS continued to work closely with the industry to resolve the teething SMETS2 technical issues, primarily associated with radiofrequency interference of smart meters in the North of England and Scotland. In addition, SMS has continued to work closely with its customers, who are at varied states of readiness for the full rollout of these second-generation meters as a result of the industry-wide issues outlined above. The issues are reflected in an 8.6% drop in industry-wide smart installations in H1 compared to H2 2018, with small energy suppliers only able to convert 9.4% of their customer base to smart compared with 29% for larger suppliers.

An increasing number of energy suppliers are now ready and able to release their customer portfolio for SMETS2 meter installation and the UK smart metering industry is anticipating a recovery in the installation rate.

SMS expects to see an increase in its smart meter installation run rate now that these technical and energy supplier readiness issues are largely resolved and has sufficient SMETS2 metering stock to support these requirements, as well as installation capacity.

The Group has also seen continued growth in data recurring revenue to £12.9m, largely driven by a focus on half-hourly services to the electricity I&C market. The Group's overall data portfolio has decreased as a result of a commercial decision to step back from appointments to third-party traditional meter points requiring low margin manual meter reads. This will enable the Group to focus on delivery of data services to smart and advanced meter portfolios across both the I&C and Domestic market segments.

Asset installation

The Group has continued to invest in its engineering work force, now with over 500 smart trained dual fuel engineers.

The challenges experienced in the transition to SMETS2 meter installations have impacted on engineering efficiency, such that on average c.26k smart meters were installed per month in H1 2019.

Coinciding with the SMETS1 end date on 15 March 2019 (with stock depleted for such installations accordingly), these industry-wide technical and energy supplier issues have also restricted access to customer portfolios and impacted on the length of time taken onsite to install smart meters.

SMS is focused on continuing to fully mobilise its customers into SMETS2 rollouts, balancing regional engineering capacity with customer portfolios to maximise installation efficiency, and working closely with energy suppliers to convert their customers to smart accordingly.

The Group's training centres remain central to this endeavour, both to support future increases in engineering capacity and support the future installation of other asset classes (such as electric vehicle charging points, PV generation and battery storage solutions) and the Group remains at the forefront of compliance and health and safety initiatives within the industry.

Energy services

SMS's Energy services business has performed ahead of expectations in the first half of the year. Opportunities have continued to be commercialised to help customers reduce their energy expenditure and carbon footprint, building on the Group's half-hourly

(HH) data analytics services to identify and deliver energy-saving opportunities. Trials for HH data management for water metering are continuing.

Substantial rollout of LED energy-efficiency lighting programmes has continued, sponsored by a leading UK hotel chain, with over 100 sites completed in H1 2019. The Group is developing these services for wider energy-efficiency delivery around heating and air conditioning control and optimisation.

SMS has acquired Solo Energy, a block chain energy flexibility IT platform. The acquisition enables SMS to utilise Solo's strong platform to establish new long term revenue streams from new asset classes. Solo Energy's platform has an established government and local authority sponsored battery, EV charging and solar installation energy project for residential and commercial buildings. Solo is currently working on four residential and commercial projects, representing c.2,000 homes and businesses.

The Group has also continued to invest in developing SMS's range of capabilities, using data and technology to drive analytics and control of both energy usage and, in the future, battery storage, electric vehicle and generation solutions.

The energy market is already changing and SMS is at the forefront of these developments. With strategic importance placed on controlling the data and revenue streams from these new asset classes, the Group is of the view that, in conjunction with its engineering installation capability, it has a significant platform for growth beyond the immediate smart metering rollout opportunity.

Financial review

Reconciliation of reported to underlying results

SMS uses alternative performance measures, defined at the end of the financial review, to present users of the accounts with a clear view of what the Group considers to be the results of its underlying, sustainable business operations, to enable consistent period-on-period comparisons.

A reconciliation of these performance measures is disclosed below:

	Period ended 30 June 2019 £m	Period ended 30 June 2018 £m	Percentage change
Annualised recurring revenue	**85.9**	69.3	24%
Group revenue	**54.2**	46.7	16%
Statutory profit from operations	**2.4**	12.3	
Amortisation of intangibles	**1.1**	1.1	
Depreciation	**17.2**	10.0	
Statutory EBITDA	**20.6**	23.4	(12%)
Exceptional items (EBITDA related)	**5.2**	0.2	
Pre-exceptional EBITDA	**25.8**	23.6	9%
Net interest (excl. exceptional)	**(4.0)**	(2.2)	
Depreciation	**(17.2)**	(10.0)	
Underlying profit before taxation	**4.6**	11.4	(59%)
Exceptional items (EBITDA)	**(5.2)**	(0.2)	
Exceptional items (interest)	**(0.1)**	-	
Amortisation of intangibles	**(1.1)**	(1.1)	
Statutory (loss)/profit before taxation	**(1.7)**	10.1	(117%)
Taxation	**0.3**	(1.8)	
Statutory (loss)/profit after taxation	**(1.4)**	8.3	(117%)
Amortisation of intangibles	**1.1**	1.1	
Exceptional items (EBITDA and interest)	**5.3**	0.2	
Tax effect of adjustments	**(1.1)**	(0.2)	
Underlying profit after taxation	**3.9**	9.4	(59%)
Weighted average number of ordinary shares (basic)	**112,495,520**	112,353,015	
Underlying basic EPS (pence)	**3.40**	8.40	
Weighted average number of ordinary shares (diluted)	**113,409,293**	113,544,391	
Underlying diluted EPS (pence)	**3.37**	8.32	

Revenue

	30 June 2019 £'m	30 June 2018 £'m	Percentage change
Asset management	**39.4**	31.6	25%
Asset installation	**10.2**	12.1	(16%)
Energy management	**4.6**	3.0	53%
Group revenue	**54.2**	46.7	16%

Total ILARR increased by 14% to £85.9m as at 30 June 2019 compared to 31 December 2018, ahead of expectations. This growth reflects the flow through impact of new contract wins and growth in the meter estate, together with the combined effect of increases in RPI and rental rates for deemed non-contracted customers.

Group revenue rose 16%, driven primarily by performance in the Asset management and Energy management divisions, offset by a decline in Asset installation revenues, as explained further below. Whilst installation run rates have been slower than anticipated, the domestic smart meter portfolio has still increased, generating additional revenue.

Together with a favourable increase in the RPI in April 2019, and a pricing increase on deemed non-contracted customers, revenue has increased by 25% in the Asset management division to £39.4m (2018: £31.6m).

Energy management revenue has increased 53% to £4.6m (2018: £3.0m), which continues to be attributable to the energy-efficient lighting project in progress for a large hotel chain, with over 100 sites completed in H1 2019.

Asset installation revenue was £10.2m (2018: £12.1m) due to legacy installation-only work for third parties coming to an end in H1, in line with the Group's decision to reallocate internal engineering resource to fit the SMS portfolio of smart meters.

The decline in Asset installation revenue has been partially offset by higher volumes of emergency work on SMS's portfolio of traditional meters, which have required direct replacement whilst energy suppliers become SMETS2 ready.

EBITDA

Pre-exceptional EBITDA increased to £25.8m (2018: £23.6m) with statutory EBITDA decreasing to £20.6m (2018: £23.4m), with the increase in revenue offset by specific costs incurred to create capacity to support future growth.

The Group has continued to invest in its engineer workforce, through recruitment, training and in the successful set up of a dedicated contact centre to help drive the business through the smart meter rollout.

In addition, the Group has continued to develop the IT platforms that underpin its end-to-end service offering.

Cost of sales and general overheads have increased as a result, but lower installation volumes and industry-wide radiofrequency interference issues in the North have reduced engineer utilisation rates. Despite these additional costs, pre-exceptional EBITDA continued to grow.

Statutory EBITDA has fallen due to the above factors and the exceptional costs of £5.2m, £4.1m of which relate to losses on the removal of traditional meters and the removal of a proportion of SMETS1 compliant smart meters, caused by the temporary industry transition period.

SMS shows these meter removals and the associated termination income as an exceptional item, as the removal profile is outside its control and there is inherent volatility in the associated financial impact. Of these losses, the majority relates to the removal of SMETS1 meters.

Technical communication issues for some SMETS1 meters on supplier churn have continued in H1, with the enrolment and adoption process into DCC due to take place over a 12 month period, commencing for certain meters on 30 September 2019.

As a result, and consistent with the prior year end, the Group has continued to treat the loss of these meters as exceptional due to this temporary industry transition period.

Other material operating exceptional items include payments relating to deferred remuneration arising from the acquisition of a subsidiary in 2016, and the subsequent issuance of shares for nil consideration (£0.9m).

Gross margins

The cash gross margin decreased by 8% to 60% (2018: 68%). SMS includes depreciation on revenue-generating assets within cost of sales and removing this from the margin analysis provides a better comparison of underlying trading performance year on year.

The Group's decision to invest in capacity to support the smart meter rollout and more infrastructure-type projects means sales activity will grow, albeit at a lower margin, caused by this changing mix.

The gross profit margin has also been impacted by the higher than expected proportion of installation costs that are unable to be capitalised.

The depreciation-adjusted gross margin for Asset management has increased to 92% (2018: 89%) reflecting the growth in the underlying asset base. The gross margin, including depreciation, has decreased by 6% from 59% to 53%, primarily as a result of changes to depreciation-related accounting estimates, made with effect from 1 January 2019, in relation to SMS's meter assets.

As a result, there is an additional £2.9m, recognised within depreciation in cost of sales – see note 1(a).

The Asset installation business reported a negative gross profit margin (2018: positive 26%). This reflects the Group-wide strategy to focus its internal resources on the smart meter rollout, with legacy external installation contracts coming to an end at the beginning of the year. This margin has also been significantly impacted by the capacity investment detailed above.

The Energy management gross margin has stayed constant at 22%, as a result of no significant changes in active contracts within this segment. The Group is continuing to successfully deliver on a large-scale energy-efficient lighting contract, which delivers a lower gross margin overall.

Operational and pre-tax losses/profits

Depreciation costs on general property, plant and equipment, excluding meter assets, have increased by £1.3m to £1.7m (2018: £0.4m). This is largely driven by the decision to purchase the Group's fleet of vans, previously leased on an operating basis. £0.5m

of additional depreciation has also been recognised as a result of the implementation of IFRS 16 and the addition of c.£4.4m of right-of-use assets, see Note 10.

The net interest charge is £4.1m (2018: £2.2m), reflecting higher average net debt as a result of the continued investment in assets.

Effective tax rate
The current forecast of the effective tax rate for the full year is 17.78% (30 June 2018: 17.21%). The increase in the effective rate is driven primarily by an increase in permanent differences from disallowable items.

Earnings per share (EPS)
Underlying basic EPS, which excludes exceptional costs, amortisation and their associated tax effect, is 3.40p (2018: 8.40p), reflecting the underlying profitability of the Group.

As a result of incurring statutory losses after taxation of £1.4m, basic EPS is negative at 1.28p (30 June 2018: +7.45p).

Diluted EPS does not vary significantly from basic EPS; a small decrease is seen as a result of the dilutive impact of shares issuable in the future to settle the Group's share scheme obligations.

Dividend
The Group is paying an interim dividend of 2.30p per ordinary share (2018: 2.00p), a 15% increase in line with the Group's progressive dividend policy.

This interim dividend will be paid on 22 November 2019 to shareholders on the register at 25 October 2019, with an ex-dividend date of 24 October 2019.

Cash flow
The Group generated an operating cash inflow of £15.0m (2018: £21.6m). The decrease in operating cash flow is mainly due to the higher working capital outflows with an outflow of £11.5m in H1 2019 compared to £2.2m in H1 2018.

There has been a significant increase in inventory, with the strategic purchasing of SMETS2 meters to ensure SMS can meet forecast installations in H2. Several of these purchases were made close to the period end, concurrently driving an increase in trade and other payables.

Capital expenditure on property, plant and equipment was £48.4m (2018: £80.8m). Of this, £43.4m has been used to purchase revenue-generating assets. This capital expenditure is lower than the prior period as a result of the decline in installation run rates but is expected to increase in H2 as installation demand recovers.

A further £3.7m investment has been made in intangible assets. This includes development of software to support the installations business, together with investment in a Group-wide Enterprise Resource Planning system that will consolidate, integrate and update various systems and processes to ensure that the Group can effectively manage the increasing volumes of transactions and complexity of data.

As a result of the refinancing of the loan facility, there has been a £65.4m net cash injection from drawdowns in the period. £5.3m of finance costs have also been paid (2018: £2.4m), including £3.1m of arrangement fees in relation to the new facility.

Financial resources
With further growth anticipated as the UK domestic smart meter rollout continues, SMS has access to sufficient funding to accelerate installation in line with market demand.

On 21 December 2018 a new banking facility was signed, providing the business access to £420m on a fully revolving basis over the next five years therefore removing any amortisation in that period. The first drawdown under this new facility was on 3 January 2019, and at that date the Group's obligations under the existing facility were settled.

At 30 June 2019, utilisation of the new facility totalled £236.3m, net of £2.8m arrangements fees which will be amortised over the term of the facility. No principal repayments are required until 2022, providing us with greater flexibility during the current industry transition period.

Net debt was £186.6m at 30 June 2019, £44.6m higher than at 31 December 2018, as a result of the increase in inventory and capital expenditure mentioned above and which is consistent with our own expectations.

At 30 June 2019 the Group's available cash and unutilised element of the revolving credit facility stood at £233.4m (2018: £138.0m). The Group had cash in bank of £49.7m at 30 June 2019 (30 June 2018: £46.8m).

Definitions of alternative performance measures

Alternative performance measure	Definition
Index-Linked Annualised recurring revenue	The revenue being generated from meter rental and data contracts at a point in time. Includes revenue from third-party managed meters.
Pre-exceptional EBITDA	Statutory EBITDA excluding exceptional items.[1]
Underlying profit before taxation	Profit before taxation excluding exceptional items and amortisation of intangibles.
Underlying profit after taxation	Profit after taxation excluding exceptional items and amortisation of intangibles and the tax effect of these adjustments.
Underlying basic EPS	Underlying profit after taxation divided by the weighted average number of ordinary shares for the purposes of basic EPS.
Underlying diluted EPS	Underlying profit after taxation divided by the weighted average number of ordinary shares for the purposes of diluted EPS.

1 Exceptional items are those material items of income and expense which, because of the nature or expected infrequency of the events giving rise to them, merit separate presentation on the consolidated income statement.

Consolidated interim income statement and statement of comprehensive income

For the period ended 30 June 2019

		Unaudited					
		Six months ended 30 June					
	Notes	**2019 Before exceptional items £'000**	**2019 Exceptional items[1] £'000**	**2019 Total £'000**	2018 Before exceptional items £'000	2018 Exceptional items[1] £'000	2018 Total £'000
Revenue	3	**54,205**	**-**	**54,205**	46,741	-	46,741
Cost of sales		**(37,295)**	**-**	**(37,295)**	(24,281)	-	(24,281)
Gross profit		**16,910**	**-**	**16,910**	22,460	-	22,460
Administrative expenses		**(11,359)**	**(5,207)**	**(16,566)**	(11,053)	(221)	(11,274)
Other operating income		**2,019**	**-**	**2,019**	1,127	-	1,127
Profit from operations		**7,570**	**(5,207)**	**2,363**	12,534	(221)	12,313
Finance costs		**(4,098)**	**(103)**	**(4,201)**	(2,332)		(2,332)
Finance income		**113**	**-**	**113**	143	-	143
Profit/(loss) before taxation		**3,585**	**(5,310)**	**(1,725)**	10,345	(221)	10,124
Taxation		**(637)**	**919**	**282**	(1,789)	34	(1,755)
Profit/(loss) for the period and total comprehensive income attributable to owners of the parent[1]		**2,948**	**(4,391)**	**(1,443)**	8,556	(187)	8,369

1 Refer to note 4 for details of exceptional items.

The profit from operations arises from the Group's continuing operations.

Earnings per share attributable to owners of the parent during the period:

	Notes	**Six months ended 30 June 2019 Unaudited**	Six months ended 30 June 2018 Unaudited
Basic earnings per share (pence)	5	**(1.28)**	7.45
Diluted earnings per share (pence)	5	**(1.27)**	7.37

Consolidated interim statement of financial position

As at 30 June 2019

	Notes	**Unaudited 30 June 2019 £'000**	Audited 31 December 2018 £'000
Assets			
Non-current assets			
Intangible assets		**19,604**	17,138
Property, plant and equipment	7	**385,636**	356,732
Investments		**75**	75
Trade and other receivables		**328**	402
Total non-current assets		**405,643**	374,347
Current assets			
Inventories		**17,556**	11,261
Other assets		**—**	3,105
Trade and other receivables		**39,506**	30,640
Income tax recoverable		**290**	292
Cash and cash equivalents		**49,709**	30,027
Total current assets		**107,061**	75,325
Total assets		**512,704**	449,672
Liabilities			
Current liabilities			
Trade and other payables		**39,320**	36,348
Lease liabilities		**935**	—
Other liabilities		**—**	3,105
Bank loans and overdrafts	8	**1,586**	172,016
Total current liabilities		**41,841**	211,469
Non-current liabilities			
Bank loans	8	**234,716**	—
Lease liabilities		**2,970**	—
Deferred tax liabilities		**11,963**	12,070
Total non-current liabilities		**249,649**	12,070
Total liabilities		**291,490**	223,539
Net assets		**221,214**	226,133
Equity			
Share capital		**1,127**	1,125
Share premium		**159,702**	158,861
Other reserve		**9,562**	9,562
Own share reserve		**(668)**	(588)
Retained earnings		**51,491**	57,173
Total equity attributable to owners of the parent		**221,214**	226,133

Consolidated interim statement of changes in equity

For the period ended 30 June 2019

	Share capital £'000	Share premium £'000	Other reserve £'000	Own share reserve £'000	Retained earnings £'000	Total £'000
As at 1 January 2018	1,124	158,592	9,562	(697)	59,040	227,621
Adjustment on initial application of IFRS 9	—	—	—	—	(49)	(49)
Restated as at 1 January 2018	1,124	158,592	9,562	(697)	58,991	227,572
Total comprehensive income for the period	—	—	—	—	8,369	8,369
Transactions with owners in their capacity as owners						
Dividends (note 6)	—	—	—	—	(3,892)	(3,892)
Shares issued	1	269	—	—	—	270
Movement in own shares	—	—	—	(64)	—	(64)
Share-based payments	—	—	—	—	271	271
Income tax effect of share options	—	—	—	—	(185)	(185)
As at 30 June 2018	1,125	158,861	9,562	(761)	63,554	232,341
Total comprehensive income for the period	—	—	—	—	(3,905)	(3,905)
Transactions with owners in their capacity as owners						
Dividends (note 6)	—	—	—	—	(2,251)	(2,251)
Shares issued	—	—	—	—	—	—
Movement in own shares	—	—	—	173	(339)	(166)
Share-based payments	—	—	—	—	937	937
Income tax effect of share options	—	—	—	—	(823)	(823)
As at 31 December 2018	1,125	158,861	9,562	(588)	57,173	226,133
Total comprehensive income for the period	**—**	**—**	**—**	**—**	**(1,443)**	**(1,443)**
Transactions with owners in their capacity as owners						
Dividends (note 6)	**—**	**—**	**—**	**—**	**(4,485)**	**(4,485)**
Shares issued	**2**	**841**	**—**	**—**	**—**	**843**
Movement in own shares	**—**	**—**	**—**	**(80)**	**(47)**	**(127)**
Share-based payments	**—**	**—**	**—**	**—**	**386**	**386**
Income tax effect of share options	**—**	**—**	**—**	**—**	**(93)**	**(93)**
As at 30 June 2019	**1,127**	**159,702**	**9,562**	**(668)**	**51,491**	**221,214**

Consolidated interim statement of cash flows

For the period ended 30 June 2019

	Six months ended 30 June 2019 Unaudited £'000	Six months ended 30 June 2018 Unaudited £'000
Operating activities		
Profit before taxation	**(1,725)**	10,124
Finance costs	**4,098**	2,332
Finance income	**(113)**	(143)
Exceptional items[1]	**5,131**	44
Depreciation	**17,195**	9,999
Amortisation of intangibles	**1,058**	1,093
Share-based payment expense	**318**	271
Loss on disposal of property, plant and equipment	**502**	177
Movement in inventories	**(6,032)**	(2,334)
Movement in trade and other receivables	**(8,818)**	(1,616)
Movement in trade and other payables	**3,352**	1,717
Cash generated from operations	**14,966**	21,664
Income tax received/(paid)	**-**	(64)
Net cash generated from operations	**14,966**	21,600
Investing activities		
Payments to acquire property, plant and equipment	**(48,421)**	(80,849)
Proceeds on disposal of property, plant and equipment	**1,864**	722
Payments to acquire intangible assets	**(3,713)**	(2,317)
Finance income received	**113**	143
Net cash used in investing activities	**(50,157)**	(82,301)
Financing activities		
New borrowings	**65,386**	70,440
Borrowings repaid	**—**	(107,458)
Principal elements of lease payments	**(614)**	—
Finance costs paid	**(5,300)**	(2,351)
Net proceeds from share issue	**13**	270
Purchase of own shares	**(127)**	(64)
Dividends paid	**(4,485)**	(3,892)
Net cash generated from/(used in) financing activities	**54,873**	(43,055)
Net increase/(decrease) in cash and cash equivalents	**19,682**	(103,756)
Cash and cash equivalents at the beginning of the period	**30,027**	150,600
Cash and cash equivalents at the end of the period	**49,709**	46,844

1 Non-cash material exceptional items include £4,115,000 for losses on our meter portfolio and £898,000 of deferred remuneration arising on the acquisition of a subsidiary in 2016 settled in shares in April 2019.

Notes to the interim report

For the period ended 30 June 2019

1 Basis of preparation

This condensed consolidated interim financial report for the half-year reporting period ended 30 June 2019 has been prepared in accordance with Accounting Standard IAS 34 Interim Financial Reporting. The Company is a public limited company incorporated and domiciled in Scotland whose shares are quoted on AIM, a market operated by the London Stock Exchange.

The financial information contained in this half-yearly financial report does not constitute statutory accounts as defined in section 434 of the Companies Act 2006. It does not therefore include all the information and disclosures required in the annual financial statements and should be read in conjunction with the Group's annual financial statements for the year ended 31 December 2018.

The financial information for the six months ended 30 June 2019 is also unaudited.

The comparative information for the year ended 31 December 2018 has been extracted from the Group's published financial statements for that year, which were prepared in accordance with International Financial Reporting Standards (IFRSs) as endorsed by the European Union and have been delivered to the Registrar of Companies. The report of the auditor on these accounts was unqualified and did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

Management prepares budgets and forecasts on a rolling 24-month basis. These forecasts cover operational cash flows and investment capital expenditure and are prepared based on management's estimation of installation run rates through the UK smart meter rollout.

On 21 December 2018 a new banking facility was signed, providing the business access to £420m over the next five years. The first drawdown under this new facility was on 3 January 2019, at which point the Group's obligations under the existing £280m facility of £172m were settled. These transactions were settled concurrently on a net cash basis.

Based on the current projections and facilities in place, the Directors consider it appropriate to continue to prepare the financial statements on a going concern basis.

The accounting policies adopted in the preparation of the interim condensed consolidated financial statements are consistent with those followed in the preparation of the Group's annual consolidated financial statements for the year ended 31 December 2018, except for the adoption of new and amended standards as set out in note 1(b) below. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

1(a) Significant accounting policies

As required in AIM Rule 18, the interim financial report for the half-year reporting period ended 30 June 2019 is presented and prepared in a form consistent with that which will be adopted in the annual statutory financial statements for the year ended 31 December 2019 and having regard to the IFRS applicable to such annual accounts.

The accounting policies adopted are consistent with those of the previous financial year and corresponding interim period except for the adoption of new and amended standards as set out in note 1(b) below. In addition, the following changes in estimates have been made with regards to property, plant and equipment:

Changes in estimates with effect from 1 January 2018

The following changes were made in the latter half of the year ended 31 December 2018, with effect from 1 January 2018. They are therefore consistent with the accounting estimates applied in the previous financial year but are not consistent with those applied in the interim period ended 30 June 2018:

- A review concluded that there should be a change to the I&C electric estimate of useful life from 15 years to 20 years on the basis that these meters are no longer subject to a certification period and fall under the same considerations as smart meters.
- The I&C gas portfolio has seen the estimate of residual value reduce to 0% to reflect revised customer terms in new customer contracts.
- With respect to the domestic traditional meter asset portfolio, the useful life of all opening assets was extended to five years to reflect the fact that the expected end date for the domestic smart meter rollout is likely to be at the end of 2022. It is accepted that the rate of meter exchange to smart meters will vary year by year as the rollout proceeds but there is currently no reliable basis on which to predict the annual profile. Accordingly, a straight line approach to depreciation of these assets continues to be adopted.

Changes in estimates with effect from 1 January 2019

- Subsequent to the impairment review carried out at 31 December 2018, the estimate of residual value on the domestic traditional meter asset portfolio has been reduced to 0% to reflect management's updated forecasts and assumptions regarding the recoverability of value on these assets. As a result, the income statement has been charged with an additional £2.9m, recognised within depreciation in cost of sales.

1(b) New and amended standards adopted by the Group

Several new or amended standards became applicable for the current reporting period, and the Group had to change its accounting policies as a result of adopting IFRS 16 Leases.

The impact of the adoption of IFRS 16 is disclosed in note 10. The other new and amended standards did not have any impact on the Group's accounting policies and did not require adjustments.

2 Segmental reporting

For management purposes, the Group is organised into three core divisions, as follows:

- Asset management, which comprises management of gas meters, electricity meters and ADM™ units within the UK.
- Asset installation, which comprises installation of domestic and I&C gas meters and electricity meters throughout the UK.
- Energy management, which comprises the provision of energy consultancy services.

The Group's chief operating decision maker (CODM), being the SMS plc Board, receives certain management information at a granular "utility" level. Asset management includes reporting on gas meter rental, electricity meter rental, gas data and electricity data. Asset installation includes reporting on gas transactional work and electricity transactional work. However, whilst the Group has the ability to analyse its underlying information in this way, this information is only used to assess performance for the Group as a whole. These utility levels are thus combined within Asset management and Asset installation, respectively, on the basis that they have similar long term economic characteristics – they derive from the same asset, use similar delivery processes, have consistent customers and have similar long-term gross margins.

For the purpose of making decisions about resource allocation and performance assessment, it is the operating results of the three core divisions listed above that are monitored by management and the CODM. It is these divisions, therefore, that are defined as the Group's reportable operating segments.

Segment performance is evaluated based on gross profit.

The following segment information is presented in respect of the Group's reportable segments together with additional balance sheet information.

30 June 2019	**Asset management £'000**	**Asset installation £'000**	**Energy management £'000**	**Unallocated £'000**	**Total operations £'000**
Segment revenue	**39,368**	**28,253**	**4,617**	—	**72,238**
Inter-segment revenue	—	**(18,033)**	—	—	**(18,033)**
Revenue from external customers	**39,368**	**10,220**	**4,617**	—	**54,205**
Cost of sales	**(18,554)**	**(15,156)**	**(3,585)**	—	**(37,295)**
Segment gross profit/(loss)	**20,814**	**(4,936)**	**1,032**	—	**16,910**
Other operating costs/income	—	—	—	**(6,569)**	**(6,569)**
Depreciation	**(661)**	—	—	**(1,052)**	**(1,713)**
Amortisation of intangibles	**(1,058)**	—	—	—	**(1,058)**
Exceptional items	**(4,114)**	—	—	**(1,093)**	**(5,207)**
Profit/(loss) from operations	**14,981**	**(4,936)**	**1,032**	**(8,714)**	**2,363**
Net finance costs: exceptional	**(103)**	—	—	—	**(103)**
Net finance costs: other	**(3,927)**	—	—	**(58)**	**(3,985)**
Profit/(loss) before tax	**10,951**	**(4,936)**	**1,032**	**(8,772)**	**(1,725)**
Tax credit	—	—	—	**282**	**282**
Profit/(loss) for the period	**10,951**	**(4,936)**	**1,032**	**(8,490)**	**(1,443)**

30 June 2018	Asset management £'000	Asset installation £'000	Energy management £'000	Unallocated £'000	Total operations £'000
Segment revenue	31,642	23,636	2,992	—	58,270
Inter-segment revenue	-	(11,529)	—	—	(11,529)
Revenue from external customers	31,642	12,107	2,992	—	46,741
Cost of sales	(13,013)	(8,924)	(2,344)	—	(24,281)
Segment gross profit	18,629	3,183	648	—	22,460
Other operating costs/income	—	—	—	(8,370)	(8,370)
Depreciation	—	(48)	—	(415)	(463)
Amortisation of intangibles	(1,093)	—	—	—	(1,093)
Exceptional items	—	—	—	(221)	(221)
Profit from operations	17,536	3,135	648	(9,006)	12,313
Net finance costs: exceptional	—	—	—	—	—
Net finance costs: other	(2,189)	—	—	—	(2,189)
Profit before tax	15,347	3,135	648	(9,006)	10,124
Tax expense	—	—	—	(1,755)	(1,755)
Profit for the period	15,347	3,135	648	(10,761)	8,369

Inter-segment revenue relates to installation services provided by the Asset installation segment to the Asset management segment.

Depreciation of £15.5m (30 June 2018: £9.5m) associated with meter assets has been reported within cost of sales as the meter assets directly drive revenue.

All revenues and operations are based and generated in the UK.

Segment assets and liabilities

30 June 2019	Asset management £'000	Asset installation £'000	Energy management £'000	Unallocated £'000	Total operations £'000
Assets reported by segment					
Intangible assets	**16,106**	**3,498**	**—**	**—**	**19,604**
Property, plant and equipment	**372,752**	**5,324**	**—**	**7,560**	**385,636**
Inventories	**16,810**	**746**	**—**	**—**	**17,556**
Contract assets	**—**	**—**	**20**	**—**	**20**
	405,668	**9,568**	**20**	**7,560**	**422,816**
Assets not by segment					**89,888**
Total assets					**512,704**
Liabilities by segment					
Contract liabilities	**1,117**	**1,795**	**225**	**—**	**3,137**
Lease liabilities	**1,137**	**—**	**—**	**2,768**	**3,905**
Bank loan	**236,302**	**—**	**—**	**—**	**236,302**
	238,556	**1,795**	**225**	**2,768**	**243,344**
Liabilities not by segment					**48,146**
Total liabilities					**291,490**

31 December 2018	Asset management £'000	Asset installation £'000	Energy management £'000	Unallocated £'000	Total operations £'000
Assets reported by segment					
Intangible assets	13,643	3,495	—	—	17,138
Property, plant and equipment	350,360	2,463	—	3,909	356,732
Inventories	10,762	499	—	—	11,261
Contract assets	2	20	—	—	22
	374,767	6,477	—	3,909	385,153
Assets not by segment					64,519
Total assets					449,672
Liabilities by segment					
Contract liabilities	1,010	1,801	418	—	3,229
Bank loans	172,016	—	—	—	172,016
	173,026	1,801	418	—	175,245
Liabilities not by segment					48,294
Total liabilities					223,539

3. Disaggregation of revenue from contracts with customers

The Group reports the following segments: Asset management, Asset installation and Energy management, in accordance with IFRS 8 Operating Segments. We have determined that, to meet the objective of the disaggregation disclosure requirement in paragraph 114 of IFRS 15, which is to disaggregate revenue from contracts with customers into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors, further disaggregation is required into the major types of services offered. The following table thus discloses segmental revenue by type of service delivered and timing of revenue recognition, including a reconciliation of how this disaggregated revenue ties in with the asset management, asset installation and energy management segments, in accordance with paragraph 115 of IFRS 15.

Period ended 30 June 2019	Asset management £'000	Asset installation £'000	Energy management £'000	Total operations £'000
Major service lines				
Metering	**35,750**	**—**	**—**	**35,750**
Data management	**3,618**	**—**	**—**	**3,618**
Utility connections	**—**	**4,113**	**—**	**4,113**
Transactional meter works	**—**	**5,802**	**—**	**5,802**
Energy management	**—**	**305**	**4,617**	**4,922**
	39,368	**10,220**	**4,617**	**54,205**
Timing of revenue recognition				
Services transferred at a point in time	**—**	**5,677**	**—**	**5,677**
Services transferred over time	**39,368**	**4,543**	**4,617**	**48,528**
	39,368	**10,220**	**4,617**	**54,205**

Period ended 30 June 2018	Asset management £'000	Asset installation £'000	Energy management £'000	Total operations £'000
Major service lines				
Metering	28,214	—	—	28,214
Data management	3,429	—	—	3,429
Utility connections	—	4,100	—	4,100
Transactional meter works	—	7,709	—	7,709

Energy management	—	297	2,992	3,289
	31,643	12,106	2,992	46,741
Timing of revenue recognition				
Services transferred at a point in time	—	6,952	—	6,952
Services transferred over time	31,643	5,154	2,992	39,789
	31,643	12,106	2,992	46,741

4 Exceptional items

There are total exceptional items on the consolidated income statement of £5,310,000. Exceptional material operating costs comprise £4,115,000 for losses on our meter portfolio and £898,000 of deferred remuneration arising on the acquisition of a subsidiary in 2016 settled in shares in April 2019.

Exceptional finance costs of £103,000 include £92,000 accelerated amortisation of loan arrangements fees in relation to the refinancing of the loan facility and £11,000 of bank break fees.

In the period ended 30 June 2018, exceptional items of £221,000 predominantly relate to costs associated with the reorganisation of the installation business.

5 Earnings per share (EPS)

The calculation of EPS is based on the following data and number of shares:

	Six months ended 30 June 2019 Unaudited £'000	Six months ended 30 June 2018 Unaudited £'000
Profit for the period used for calculation of basic EPS	**(1,443)**	8,369

Number of shares	**Six months ended 30 June 2019 Unaudited**	Six months ended 30 June 2018 Unaudited
Weighted average number of ordinary shares for the purposes of basic EPS	**112,495,520**	112,353,015
Effect of potentially dilutive ordinary shares:		
– share options	**913,773**	1,191,376
Weighted average number of ordinary shares for the purposes of diluted EPS	**113,409,293**	113,544,391
EPS:		
– basic (pence)	**(1.28)**	7.45
– diluted (pence)	**(1.27)**	7.37

6 Dividends

	Six months ended 30 June 2019 Unaudited £'000	**Six months ended 30 June 2019 Per share (pence)**	Six months ended 30 June 2018 Unaudited £'000	Six months ended 30 June 2018 Per share (pence)	Year ended 31 December 2018 Unaudited £'000	Year ended 31 December 2018 Per share (pence)
Paid final dividend	**4,485**	**3.98**	3,892	3.46	3,892	3.46
Paid interim dividend	**—**	**—**	—	—	2,251	2.00
Total dividends	**4,485**	**3.98**	3,892	3.46	6,143	5.46

An interim cash dividend for 2019 of 2.30p per share (2018: 2.00p) has been declared by the Directors, which has not been accrued as a liability at 30 June 2019 in accordance with IAS 8. The dividend will be paid on 22 November 2019.

7 Property, plant and equipment

	Freehold/ leasehold property £'000	Meter assets £'000	Plant and machinery £'000	Fixtures, fittings and equipment £'000	Motor vehicles £'000	Right-of-use assets (note 10) £'000	Total £'000
Cost							
As at 1 January 2018	2,300	299,815	317	3,065	83	—	305,580
Additions	236	128,173	187	1,230	2,817	—	132,643
Disposals	—	(17,860)	—	(47)	(86)	—	(17,993)
As at 31 December 2018	2,536	410,128	504	4,248	2,814	—	420,230
Additions	60	43,412	463	1,497	2,990	4,394	52,816
Disposals	(136)	(9,099)	—	(860)	(32)	—	(10,127)
As at 30 June 2019	**2,460**	**444,441**	**967**	**4,885**	**5,772**	**4,394**	**462,919**

Depreciation							
As at 1 January 2018	392	37,820	71	1,868	83	—	40,234
Charge for year	127	20,390	162	794	323	—	21,796
Impairment	—	5,612	—	—	—	—	5,612
Disposals	—	(4,056)	—	(44)	(44)	—	(4,144)
As at 31 December 2018	519	59,766	233	2,618	362	—	63,498
Charge for period	49	15,482	123	560	477	504	17,195
Impairment	—	—	—	—	—	—	—
Disposals	(136)	(2,402)	—	(840)	(32)	—	(3,410)
As at 30 June 2019	**432**	**72,846**	**356**	**2,338**	**807**	**504**	**77,283**
Net book value							
As at 30 June 2019	**2,028**	**371,595**	**611**	**2,547**	**4,965**	**3,890**	**385,636**
As at 31 December 2018	2,017	350,362	271	1,630	2,452	—	356,732
As at 1 January 2018	1,908	261,995	246	1,197	—	—	265,346

Meter assets have been disclosed separately, previously disclosed within plant and machinery in the financial statements at 30 June 2018, to align with management reporting. Included within the closing meter assets net book value of £371,595,000 (31 December 2018: £350,362,000) is £36,951,000 (31 December 2018: £43,049,000) relating to the traditional domestic meter portfolio. In accordance with our accounting policy these assets will be written down to zero by 2022. In the H1 2019 consolidated financial statements the traditional domestic meter portfolio generated c.£8,296,000 revenue with a corresponding £5,489,000 depreciation charge. £15,951,000 annualised recurring revenue as at 30 June 2019 arises from the owned traditional and domestic meter portfolio.

The assets are secured by a bond and floating charge.

For the purpose of impairment testing the traditional meter asset portfolio recognised within meter assets is assessed as a standalone cash-generating unit (CGU) and its carrying amount is compared with the recoverable amount. The recoverable amount is determined based on a value in use calculation, which uses the following key assumptions:

- estimated future cash flows from rental income, which are assumed to decline on a straight line basis;
- estimated future cash flows from termination income, which are derived using historical data and analysis around the risk of churn between contracted and non-contracted customers; and
- a pre-tax discount rate of 2.61%, which reflects the risk attached to the time value of these specific cash flows and is deemed to be best represented by the Group's incremental cost of borrowing on the basis that cash flows are secured by the installed meter and the risk inherent in the decline of the cash flows is already accounted for through the assumptions detailed above.

As a result of this impairment test, it was identified that the value in use exceeded the carrying value of the traditional meter assets CGU and, therefore, no impairment has been recognised in the period to 30 June 2019. Whilst no impairment charge was recognised in the period to 30 June 2018, an impairment charge of £5.6m was recognised in the full year financial statements to 31 December 2018.

No impairment on other meter assets was recognised in the period to 30 June 2019.

8 Bank loans

	30 June 2019 £'000	31 December 2018 £'000
Current		
Bank loans	**1,586**	172,016
	1,586	172,016
Non-current		
Bank loans	**234,716**	—
	234,716	—

Bank loans at 31 December 2018 relate to the Group's previous revolving credit facility of £280m.

On 21 December 2018, the Group entered into a new revolving credit facility agreement with a syndicate of banks for £420m, available for five years (the new facility). This new facility comprises a different banking structure, gives rise to a significant increase in the Group's borrowing capacity and discharged the Group's obligations under the previous facility with effect from the first utilisation on 3 January 2019. It is thus deemed to be an extinguishment.

On 3 January 2019, the first drawdown was made under the new facility for £200m. This was used to settle the Group's outstanding obligations under the previous facility of £172m and fund additional capital investment. The drawdown pattern changes under the new facility to quarterly in advance, rather than monthly in arrears. The balance of unamortised arrangement fees on the previous facility of £0.09m has been accelerated and recognised as an exceptional finance cost in the consolidated income statement for the six months ended 30 June 2019.

Transaction costs on the new facility of £3.1m, recognised within other assets at 31 December 2018, were reclassified to bank loans on 3 January 2019 and are amortised over the term of the new facility. At 30 June 2019, £0.3m of transaction costs had been recognised within the consolidated income statement.

The Group had a total outstanding principal of £237.5m at 30 June 2019. Accrued interest of £1.6m has been recognised as part of the carrying value of bank loans at 30 June 2019 together with a deduction of £2.8m for unamortised transaction costs.

9 Post balance sheet events

On 8th August 2019 the Group acquired c.72,000 SMETS1 domestic smart meters. These meters are installed at the time of purchase and will therefore immediately benefit our annualised recurring revenue.

On 5th September 2019 the Group acquired the entire share capital in Solo Energy Limited (company number 566746), a block chain energy flexibility IT platform. The acquisition enables SMS to utilise Solo's strong IT platform to establish new long term revenue streams from a decentralised electricity grid.

10 Changes in accounting policies

This note explains the impact of the adoption of IFRS 16 Leases on the Group's financial statements and discloses the new accounting policies that have been applied from 1 January 2019 in note 10(b) below.

The Group has adopted IFRS 16 retrospectively from 1 January 2019 but has not restated comparatives for the 2018 reporting period, as permitted under the specific transitional provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 January 2019.

10(a) Adjustments recognised on adoption of IFRS 16

The change in accounting policy affected the following items in the consolidated balance sheet on 1 January 2019:

- Right-of-use assets – increased by £4,050,000, recognised within property, plant and equipment
- Lease liabilities – increased by £4,098,000 (of which £3,173,000 were non-current), recognised separately on the consolidated balance sheet
- Prepayments and accruals – decreased by £140,000 and £187,000 respectively

On adoption of IFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as "operating leases" under the principles of IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 4%.

There was no net impact to retained earnings on 1 January 2019 and thus no impact to taxation on transition.

For the six months ended 30 June 2019 there has been no material impact on operating profit or EBITDA but a portion of expense previously recognised within administrative expenses has been recognised as a finance cost under IFRS 16.

The Group had no leases previously classified as finance leases at 1 January 2019.

Differences between the operating lease commitments disclosed at 31 December 2018, discounted using the incremental borrowing rate at the date of initial application of IFRS 16, and the lease liabilities recognised in the consolidated balance sheet at 1 January 2019 comprise adjustments for prepayments and rent-free periods together with short term and low-value leases recognised on a straight line basis as administrative expenses.

The associated right-of-use assets for leases were measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the balance sheet as at 31 December 2018. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

The recognised right-of-use assets relate to the following types of assets:

	At 30 June 2019 £'000	At 1 January 2019 £'000
Properties	**3,715**	3,806
Motor vehicles	**175**	244
Total right-of-use assets	**3,890**	4,050

(i) Impact on segment disclosures and earnings per share

The Asset management EBITDA, segment assets and segment liabilities for June 2019 all increased as a result of the change in accounting policy.

Lease liabilities and corresponding right-of-use assets are now included in the Asset management segment liabilities and assets to the extent they relate to motor vehicles and properties directly attributable to the provision and management of meter assets:

	Segment assets at 30 June 2019 £'000	**Segment liabilities at 30 June 2019 £'000**
Asset management impact	**1,560**	**1,137**

All other right-of-use assets relate to corporate assets that are not allocated to a segment.

The increase in EBITDA and EPS was not material for the six months ended 30 June 2019.

(ii) Practical expedients applied

In applying IFRS 16 for the first time, the Group has used the following practical expedients permitted by the standard:

- the use of a single discount rate to a portfolio of leases with reasonably similar characteristics;
- reliance on previous assessments on whether leases are onerous;
- the accounting for operating leases with a remaining lease term of less than twelve months as at 1 January 2019 as short term leases;
- the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application; and

- the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

10(b) The Group's leasing activities and how these are accounted for

Group as lessor

Under IAS 17 it was concluded that the Group acts as a lessor in its arrangements to provide meter assets to energy suppliers. These leases were classified as operating leases as the Group did not transfer substantially all the risks and rewards of ownership of the meter assets. The related meter income was recognised on a straight line basis per the meter rental income policy.

Upon implementation of IFRS 16, the Group has reassessed these arrangements under the standard's revised definition of control. It has been concluded that these no longer contain a lease under IFRS 16, due to other parties taking a significant amount of the output from the meters and due to the Group being unable to substantially control either the operation of, or the physical access to, the meters. This revised management judgement also ensures commonality with the wider industry. There is no impact on the recognition and measurement of charges earned from the provision of meter assets as a result of this change.

Under IFRS 15, the provision of meter assets to energy suppliers (MAP services), together with the initial installation, is considered a distinct and single performance obligation on the basis that, as MAP, the Group has an obligation to its customers to provide a fitted meter. This is a separately identifiable service to which a standalone selling price is typically allocated. Over the course of the contract term, which runs into perpetuity, the Group delivers a series of monthly services for which benefits are simultaneously received and consumed by the customer. MAP charges are calculated daily based on the number of installed meters and invoiced to customers monthly once validation checks have been completed. As revenue from MAP charges is attributed to services provided daily, revenue is always based on the actual level of service provided and, therefore, any uncertainty at the end of each reporting period is limited to the extent that validation checks are still being completed. Revenue is thus recognised over time based on our right to invoice and includes contract inflation uplifts.

As a result of industry regulations, and subject to specific contract terms with a customer, the Group may be required to make payments to customers for shortfalls in the level of service provided. These charges are directly related to the service being provided to the customer and thus recognised as a reduction to revenue in the month in which the service failure occurred. Where service levels are set based on annual targets, charges are estimated monthly and subsequently finalised at the end of the year. Uncertainty, as it pertains to these payments to customers, is thus resolved at the end of the reporting period.

In most circumstances, if a MAP contract is cancelled termination fees are levied on the energy supplier. There has been no change in the accounting of these termination fees and they continue to be classified as other operating income unless they have arisen on the loss of the meter assets, in which case they are reported within administrative expenses as a component of net gain or loss on disposal.

Group as a lessee

The Group leases various offices, warehouses and motor vehicles. Rental contracts are typically made for fixed periods of three to ten years but may have extension or early termination options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

Until 1 January 2019, leases of property, plant and equipment were classified as either finance or operating leases and, as at 1 January 2019, all leases were classified as operating leases. Payments (net of any incentives received from the lessor) were charged to profit or loss on a straight line basis over the period of the lease.

From 1 January 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight line basis.

In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option, or not exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated). The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payments that are based on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be determined, the lessee's incremental borrowing rate is used, being the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability;
- any lease payments made at or before the commencement date less any lease incentives received;
- any initial direct costs; and
- restoration costs.

Payments associated with short term leases and leases of low-value assets are recognised on a straight line basis as an expense in profit or loss. Short term leases are leases with a lease term of twelve months or less. Low-value assets comprise IT equipment and small items of office furniture, where the value of the asset on inception is less than c.US$5,000.

Payments for services are separated from the lease components of a contract and accounted for as an administrative expense.

11 The half-yearly financial report was approved by the Board of Directors on 17 September 2019.

12 A copy of this half-yearly financial report is available by visiting our website at www.sms-plc.com.