Redstone plc

Interim Report
30 September 2005

redstone

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Chief Executive's Statement

I am pleased to report that during the six month period to 30 September 2005, Redstone has made excellent progress towards implementing a strategy to transform itself into a significant player in the wider Telecom and IT Solutions marketplace. It has been a time of major change during which we have significantly reduced overheads, redeployed and refocused resources, strengthened financial controls, and completed the acquisition of Xpert Group Limited ("Xpert") ("the acquisition") on 28 April 2005.

Financial highlights

The Xpert acquisition contributed, for the five months post acquisition, revenues in excess of £10 million, bringing about an increase in the Group's gross profit margin. It has also enabled the Group to make significant synergistic savings including a reduction of people related costs of approximately £1.1 million in the period, and £5.5 million on an annualised basis.

- Combined revenues were £33.5 million, compared with £27.5 million for the corresponding period last year.
- Gross profit margin increased from 31% to 36%.
- EBITDA loss before restructuring costs of £2.2 million (£2.0 million prior to adjustments for IFRS) compared with an EBITDA loss of £1.0 million for the corresponding period last year.
- Goodwill impairment charge of £16.1 million resulting from the restructuring of the business, all relating to historical Redstone acquisitions.
- The loss for the period, after the goodwill impairment charge of £16.1 million and restructuring costs of £4.1 million, was £23.2 million compared to £1.2 million for the corresponding period last year.
- Cash balances are £7.4 million compared with £8.5 million at 31 March 2005 and £11.9 million at 30 September 2004. Debtor collections were high at the period end, and although the restructuring is now complete, of the £4.1 million of costs reported, £1.9 million were paid in the period, and £2.2 million were paid following the period end.

In order to give the Group a stable platform for growth, the Board identified four core actions that needed to be completed during the first half year:

- The integration of Xpert and Redstone;
- The implementation of all available synergies;
- The reorganisation of the business so as to deliver profitability and cash generation from normal trading activities; and
- The creation of a group structure that allows effective management control of the enlarged business and its planned expansion.

Chief Executive's Statement (continued)

Operational highlights

Restructure

The Group has been restructured into four autonomous operating units supported by a small head office team:

- **Redstone Telecom** – specialising in selling value added inbound and outbound minutes along with other associated products;
- **Redstone Converged Solutions** – the combination of Xpert Communications and Redstone's Solutions businesses as a converged IP solutions provider, with expertise in contact centres, voice and video, IP networks and security;
- **Redstone Managed Solutions** – specialising in providing managed IT solutions such as bespoke secure internet access, remote monitoring, back-up and hosting services along with application development and support; and
- **Redstone Technology** – previously Xpert Technology, an HP Preferred Partner, Red Hat Advanced Partner and recently appointed StorageTek Premier Plus Partner specialising in providing business-critical server solutions, storage area networks and complex server clusters.

The impact of this restructuring has allowed the Group to significantly reduce its overhead base in both headcount and occupancy costs. Redstone has now reduced headcount from approximately 460 to 360 through non-replacement and redundancy. In addition, of the 14 sites previously operated within the UK, six have closed leaving eight occupied.

The total annualised savings achieved from the above restructuring will amount to £7.0 million, being £5.5 million per annum from headcount related savings and £1.5 million per annum from property related savings. The restructuring commenced in mid July and consultation with staff was completed at the end of August. The cost savings highlighted above have now been fully implemented.

Strengthening the Board and Senior Management team

Since the period end, Redstone has further strengthened both the Board and its Senior Management team. It has today appointed Ashvin Pathak and Gerard Spencer as non-executive Directors of the Redstone plc Board, both of whom bring valuable industry experience to the Group. It has also appointed Peter Deacon as head of its Converged Solutions Division.

Outlook

The Directors are optimistic about the Group's prospects, and the performance of the business is in line with their expectations. The Group is now much stronger following the restructuring, with the creation of focused autonomous business units and the £7.0 million annualised reduction in its cost base. It will continue to reduce costs where appropriate. The Group has a strong platform from which to generate future growth in both revenue and profit, is debt free and expects to be cash generative by the fourth quarter of this financial year. The management focus is now firmly on growing the business both organically and acquisitively in the developing and consolidating Telecoms and IT Solutions marketplace.

Martin Balaam
Chief Executive

28 November 2005

Consolidated Income Statement

	Note	Six months ended 30 September 2005 £000	Six months ended 30 September 2004 £000	Year ended 31 March 2005 £000
Continuing operations				
Revenue		**33,493**	27,464	49,577
Cost of sales		**(21,286)**	(18,941)	(32,063)
Gross profit		**12,207**	8,523	17,514
Other operating income		**210**	145	389
Selling and distribution costs		**(8,026)**	(3,710)	(7,479)
Administrative expenses		**(23,767)**	(6,414)	(17,721)
Restructuring costs		**(4,062)**	–	–
Operating loss before goodwill impairment, intangibles amortisation and restructuring costs		**(2,802)**	(1,395)	(2,943)
Goodwill impairment charge	4	**(16,078)**	–	(4,236)
Amortisation of intangible assets		**(496)**	(61)	(118)
Restructuring costs	4	**(4,062)**	–	–
Operating loss		**(23,438)**	(1,456)	(7,297)
Finance income		**138**	258	469
Finance cost		**(43)**	(12)	(17)
Loss on ordinary activities before taxation		**(23,343)**	(1,210)	(6,845)
Tax on loss on ordinary activities		**137**	–	–
Loss for the period		**(23,206)**	(1,210)	(6,845)
Basic and diluted earnings per share	5	**(3.49)p**	(0.43)p	(2.45)p
Gross profit %		**36.4**	31.0	35.3
EBITDA before restructuring costs		**(2,189)**	(975)	(2,084)
EBITDA per share before restructuring costs		**(0.33)p**	(0.35)p	(0.75)p

Consolidated Balance Sheet

	30 September 2005 £000	30 September 2004 £000	31 March 2005 £000
Assets			
Non-current assets			
Goodwill	**26,157**	25,370	21,134
Intangible assets	**9,050**	149	125
Property, plant and equipment	**2,826**	2,580	2,621
Other non-current assets	**581**	429	429
	38,614	28,528	24,309
Current assets			
Inventories	**938**	905	683
Trade and other receivables	**13,848**	9,430	7,994
Cash at bank and in hand	**7,382**	11,942	8,513
	22,168	22,277	17,190
Total assets	**60,782**	50,805	41,499
Equity and liabilities			
Equity			
Called up share capital	**13,022**	8,472	8,472
Share premium account	**208,099**	185,336	185,336
Other reserves	**256**	216	216
Retained earnings	**(193,327)**	(164,727)	(170,313)
	28,050	29,297	23,711
Current liabilities			
Trade and other payables	**24,636**	18,255	14,843
Provisions	**2,188**	1,016	816
	26,824	19,271	15,659
Non-current liabilities			
Provisions	**2,680**	2,237	2,129
Loan notes	**643**	–	–
Deferred tax liability	**2,585**	–	–
	5,908	2,237	2,129
Total liabilities	**32,732**	21,508	17,788
Total equity and liabilities	**60,782**	50,805	41,499

Consolidated Cash Flow Statement

	Note	**Six months ended 30 September 2005 £000**	Six months ended 30 September 2004 £000	Year ended 31 March 2005 £000
Cash outflow from operating activities				
Cash outflow from operations	6	**(4,089)**	(939)	(4,034)
Borrowing costs		**–**	(3)	(6)
Interest element of finance lease payments		**–**	(9)	(11)
Corporation taxes		**(6)**	–	–
Net cash flows from operating activities		**(4,095)**	(951)	(4,051)
Cash flows from investing activities				
Proceeds from sale of property, plant and equipment		**–**	7	7
Interest received		**155**	265	484
Purchase of property, plant and equipment		**(418)**	(541)	(1,056)
Acquisition of a subsidiary, net of cash acquired		**(21,268)**	–	–
Net cash flows used in investing activities		**(21,531)**	(269)	(565)
Cash flows from financing activities				
Proceeds from issue of shares		**26,045**	–	–
Transaction costs of issuing shares		**(1,507)**	–	–
Payment of finance lease liabilities		**(2)**	(29)	(62)
Interest paid		**(41)**	–	–
Net cash flows from/(used in) financing activities		**24,495**	(29)	(62)
Net decrease in cash and cash equivalents		**(1,131)**	(1,249)	(4,678)
Cash and cash equivalents at 1 April		**8,513**	13,191	13,191
Cash and cash equivalents at 30 September/31 March		**7,382**	11,942	8,513

1 Basis of preparation

The interim report is unaudited but has been reviewed by the auditors, Ernst & Young LLP, and their report to Redstone plc is set out on page 12.

The consolidated interim financial statements have been prepared in accordance with the principal accounting policies set out in the document entitled 'Restated Financial Information under International Financial Reporting Standards', which was issued by Redstone plc on 24 November 2005. These interim financial statements should be read in conjunction with that document. The document can be found on the Company's website, **www.redstone.co.uk**, or can be obtained by writing to the Company Secretary at Redstone plc, 80 Great Eastern Street, London, EC2A 3RS.

This interim financial information has been prepared on the assumption that all IFRS statements, including International Accounting Standards (IAS), Standing Interpretations Committee (SIC) interpretations and International Financial Reporting Interpretations Committee (IFRIC) interpretations issued by the International Accounting Standards Board (IASB) as effective for 2005 reporting will be endorsed by the European Commission. These are subject to ongoing review and possible amendment by the IASB and subsequent endorsement by the European Commission and therefore may change. Further standards and interpretations may also be issued that will become applicable for the Group's financial year ending 31 March 2006. In 2005 the Group has adopted IFRS for the first time. The date of transition is 1 April 2004. IAS 34 'Interim Financial Reporting' has not been applied to this interim financial information.

The financial information does not constitute statutory accounts as defined in Section 240 of the Companies Act 1985. Statutory accounts for the year ended 31 March 2005, which were prepared under accounting policies generally accepted in the UK, have been filed with the Registrar of Companies. The auditors' report on those accounts was unqualified and did not contain a statement made under Section 237(2) or Section 237(3) of the Companies Act 1985.

The interim report was approved by the Board on 28 November 2005.

2 Segment reporting

(i) For the six months ended 30 September 2005

	Telecoms £000	Converged Solutions £000	Managed Solutions £000	Technology £000	Other £000	**Total £000**
Revenue	14,065	14,814	2,033	2,581	–	**33,493**
Result						
Segment result	1,161	(3,303)	115	162	–	**(1,865)**
Central costs *						**(21,436)**
Net interest						**95**
Loss for the period						**(23,206)**
Assets and liabilities						
Segment assets	7,779	37,416	4,785	1,104	–	**51,084**
Unallocated assets **						**9,698**
Total assets						**60,782**
Segment liabilities	6,804	13,016	1,800	1,127	–	**22,747**
Unallocated liabilities						**9,985**
Total liabilities						**32,732**
Other segment information						
Capital expenditure						
Property, plant and equipment	–	63	144	7	204	**418**
Depreciation	48	109	187	16	253	**613**
Amortisation	–	447	–	–	49	**496**

* Central costs include the goodwill impairment charge of £16,078k and amortisation of intangible assets of £496k.

** Unallocated assets include cash of £7,382k.

The secondary segment reporting under IFRS requires a geographical split. All revenues are generated outside the Group. The Group derives approximately 89% of its revenues in the UK, with the remainder from the Ireland Technology division (8%) and the consumption of telephony calling cards in various other countries (3%).

Assets and capital expenditure are split between those held and consumed in the UK and those held and consumed in Ireland. The UK asset base makes up 98% of the Group. Capital expenditure is 98% consumed in the UK with the remainder in Ireland.

2 Segment reporting

(ii) For the six months ended 30 September 2004

	Telecoms £000	Converged Solutions £000	Managed Solutions £000	Other £000	**Total £000**
Revenue	17,432	8,090	1,568	374	**27,464**
Result					
Segment result	1,003	(1,985)	(596)	122	**(1,456)**
Net interest					**246**
Loss for the period					**(1,210)**
Assets and liabilities					
Segment assets	5,356	3,769	2,169	–	**11,294**
Unallocated assets *					**39,511**
Total assets					**50,805**
Segment liabilities	7,824	4,099	1,731	–	**13,654**
Unallocated liabilities					**7,854**
Total liabilities					**21,508**
Other segment information					
Capital expenditure					
Property, plant and equipment	21	177	95	248	**541**
Depreciation	11	7	129	277	**424**
Amortisation	–	–	–	61	**61**

* Unallocated assets include goodwill of £25,370k and cash of £11,942k.

The secondary segment reporting under IFRS requires a geographical split. Redstone derives approximately 95% of its revenue in the UK. Revenues are generated outside of the UK through the consumption of telephony calling cards. All assets and capital expenditure are held and consumed in the UK.

2 Segment reporting
(iii) For the year ended 31 March 2005

	Telecoms £000	Converged Solutions £000	Managed Solutions £000	Other £000	**Total £000**
Revenue	30,802	14,554	3,677	544	**49,577**
Result					
Segment result	2,050	(4,414)	(801)	104	**(3,061)**
Central costs *					**(4,236)**
Net interest					**452**
Loss for the year					**(6,845)**
Assets and liabilities					
Segment assets	4,498	3,325	1,689	–	**9,512**
Unallocated assets **					**31,987**
Total assets					**41,499**
Segment liabilities	6,267	2,923	1,478	–	**10,668**
Unallocated liabilities					**7,120**
Total liabilities					**17,788**
Other segment information					
Capital expenditure					
Property, plant and equipment	35	405	286	330	**1,056**
Depreciation	21	17	282	543	**863**
Amortisation	–	–	–	118	**118**

* Central costs relate to goodwill impairment of £4,236k.

** Unallocated assets include goodwill of £21,134k and cash of £8,513k.

The secondary segment reporting under IFRS requires a geographical split. Redstone derives approximately 95% of its revenue in the UK. Revenues are generated outside of the UK through the consumption of telephony calling cards. All assets and capital expenditure are held and consumed in the UK.

3 Business combinations

On 28 April 2005 Redstone plc acquired Xpert Group Limited for a total consideration including costs of £27 million, such consideration being satisfied as to £2,775,000 by the issue of Redstone plc ordinary shares, €940,952 by the issue of Loan Notes and with the balance satisfied in cash. The Company issued 416,726,337 ordinary shares for the Placing and Open Offer as at 28 April 2005 and a further 38,275,862 ordinary shares as part consideration for the acquisition as noted above. The ordinary issued share capital as at 30 September 2005 is £7,339,093 comprising 733,909,263 ordinary shares.

The fair value of the assets acquired was £5.8 million resulting in goodwill of £21.2 million.

4 Restructuring costs and goodwill impairment charge

During the period the Group restructured its operations resulting in total costs of £4,062,000, being one-off employee related costs of £2,022,000 and property costs of £2,040,000.

Following the restructuring, the Group re-assessed the carrying value of historical goodwill and concluded that it was impaired. Accordingly an impairment charge of £16,078,000 has been recorded to bring down the carrying value of the goodwill to its recoverable amount.

5 Loss per share

Basic and diluted loss per share are both calculated using a loss of £23,206,000 (30 September 2004: £1,210,000, 31 March 2005: £6,845,000) and a weighted average number of shares of 664,291,440 (31 March 2005 and 30 September 2004: 278,907,064).

There was no dilutive effect of share options at 30 September 2005, 31 March 2005 or 30 September 2004.

6 Net cash flows from operating activities

	Six months ended 30 September 2005 £000	Six months ended 30 September 2004 £000	Year ended 31 March 2005 £000
Operating loss	**(23,438)**	(1,456)	(7,297)
Adjustments for:			
Depreciation of property, plant and equipment	**613**	424	863
Amortisation of intangible assets	**496**	61	118
Goodwill impairment charge	**16,078**	–	4,236
Share based payments	**192**	24	73
Profit on disposal of property, plant and equipment	**–**	(4)	(4)
Movements in working capital:			
Decrease/(increase) in inventories	**128**	(286)	(64)
(Increase)/decrease in trade and other receivables	**(496)**	1,205	2,634
Increase/(decrease) in trade and other payables	**566**	(446)	(3,824)
Increase in non-current assets	**(151)**	–	–
Increase/(decrease) in provisions	**1,923**	(461)	(769)
Cash outflow from operations	**(4,089)**	(939)	(4,034)

7 Consolidated statement of changes in equity

	Share Capital £000	Share Premium £000	Other reserves: Merger Reserve £000	Other reserves: Translation Reserve £000	Retained Earnings £000	**Total Equity £000**
Equity as at 31 March 2005	8,472	185,336	216	–	(170,313)	**23,711**
Loss for the period	–	–	–	–	(23,206)	**(23,206)**
Share based payments	–	–	–	–	192	**192**
Currency translation differences	–	–	–	40	–	**40**
Issue of shares	4,550	24,270	–	–	–	**28,820**
Costs associated with share issue	–	(1,507)	–	–	–	**(1,507)**
Equity as at 30 September 2005	**13,022**	**208,099**	**216**	**40**	**(193,327)**	**28,050**

Independent Review Report to Redstone plc

Introduction

We have been instructed by the Company to review the financial information for the six months ended 30 September 2005 which comprises the Consolidated Income Statement, Consolidated Balance Sheet, Consolidated Cash Flow Statement and the related notes 1 to 7. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the Company in accordance with guidance contained in Bulletin 1999/4 'Review of interim financial information' issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim report in accordance with the Listing Rules of the Financial Services Authority.

As disclosed in note 1, the next annual financial statements of the Group will be prepared in accordance with those IFRSs adopted for use by the European Union. This interim report has been prepared in accordance with IFRS 1 'First Time Adoption of International Financial Reporting Standards'.

The accounting policies are consistent with those that the directors intend to use in the next financial statements. There is, however, a possibility that the directors may determine that some changes to these policies are necessary when preparing the full annual financial statements for the first time in accordance with those IFRSs adopted for use by the European Union. Any changes will be as a result of new or revised IFRSs.

Review work performed

We conducted our review in accordance with guidance contained in Bulletin 1999/4 'Review of interim financial information' issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of Group management and applying analytical procedures to the financial information and underlying financial data, and based thereon, assessing whether the accounting policies have been applied. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with International Standards on Auditing (UK and Ireland) and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 September 2005.

Ernst & Young LLP
London

28 November 2005

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