

PIPEX COMMUNICATIONS PLC

RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2004

PIPEX Communications plc

Chairman's statement

PIPEX's half-year results consolidate the considerable progress which has been made over the last two years. The Company is for the first time reporting positive EBITDA in the first half, of £4.9 million, and is bottom line profitable, before goodwill amortisation. The acquisition of Host Europe in April 2004 was followed by that of Nildram in August. These, along with previous acquisitions, have created a leading integrated telecommunications services business. The Company is now strongly positioned in the fastest growing sectors of the telecommunications market.

In the period we have seen increased growth in broadband customer numbers, domain name registrations and shared-hosting customers. Following the period end, the addition of Nildram brought a significant number of SME business broadband customers.

With these areas now growing strongly, over the next 12 months the Company will be focusing on selling our current products to existing and new customers, developing and launching new services and the integration of the business processes and systems which have passed into PIPEX ownership through acquisitions. It is expected that this integration will lead to further economic benefits and improved customer service.

Results

Turnover for the half-year was £43.6 million (2003: £11.1 million) a four-fold increase that primarily reflects the PIPEX and Host Europe acquisitions as well as strong growth in these core businesses. Gross profit of £20.3 million (2003: £4.4 million) generated a gross margin of 46.5%, a 7 percentage point improvement over 2003. EBITDA profits were £4.9 million against a loss of £1.9 million at this time last year, and were achieved despite the inclusion of one time re-structuring costs. The loss for the half year of £1.9 million (2003: loss of £3.8 million) includes £3.9 million of goodwill amortisation (2003: £0.3 million) and £2.3 million of depreciation (2003: £1.5 million). Loss per ordinary share was reduced to 0.1p, an improvement from 0.5p loss per share in 2003.

At the end of the first half of the year, the Company had cash balances of £16.0 million (2003: £5.1 million) and net debt of £4.4 million (2003: £2.5 million).

Operational Review

Broadband

Broadband continues to see strong growth, with total customers of 170,000 at the end of August 2004, which includes 35,000 customers from the Nildram acquisition. Since this acquisition we have seen an improvement in the mix between business and residential customers.

Shared Hosting and Domain Names

Shared hosting and domain name revenue continues to progress in line with our expectations and it is expected to continue to grow as broadband penetration to the mass market continues. As internet consumers become increasingly sophisticated in the way they use the Internet, demand for more web content and web based storage also increases. PIPEX's position within the SME hosting market has been strengthened by the acquisition of Host Europe plc, the UK's market leading hosting solutions provider to the small and medium businesses (Netcraft June 2004 report). With Host Europe as part of the Group, the number of hosting customers is now 142,000.

Host Europe has also strengthened PIPEX's position as the largest domain name suppliers of UK domains with over 800,000 domain names hosted on our network. Domain names are the starting point and basic requirement for anybody wishing to take on a hosting solution on the Internet.

Corporate Services

At the top end of our range, dedicated hosting and leased lines, together with security and VPNs, provide a fully integrated product set. This comprises best of breed solutions from the companies acquired by PIPEX since October 2002, namely, GX Networks, XTM and Firstnet that all now sit on the Fibernet IRU. We are now beginning to see the benefits from this integration.

Strategy

Since the end of the first half, PIPEX has been further strengthened by the acquisition of AccentUK – best known for its Nildram brand – which, in addition to a £14 million revenue stream, gives us greater presence at the top end of the broadband access market. This last deal has completed a major transformational phase for PIPEX, which is best understood through our improved revenue mix.

- Broadband now accounts for 42% of revenues, compared to 10% at this stage last year
- Hosting and domain names contribute 26% of group turnover, up from 8% in the first half of 2003.
- Leased lines, which last year produced 61% of our turnover, now account for 15% of total sales

We now have three clear objectives for the balance of the year:

- First, we plan to continue the streamlining and integration processes of these acquisitions
- Our second goal is to continue to grow the business organically through focused marketing. PIPEX has market-leading products for each of its key sectors and, while our growth rates are good, we need to increase the Company's share of those markets.
- Third, we can improve our position in the marketplace by implementing new and integrated customer facing systems throughout the Company. It is our intention to enhance customer retention through a combination of improved customer service and broader ranges of attractive products and services.

Outlook

PIPEX operates in a fast moving and competitive market, and the management is always alert to the potential offered by new and emerging technologies. The Company holds wireless telecommunication licences in two very interesting spectrum ranges, namely 3.6 to 4.2Ghz (national) and 28Ghz (London, Manchester and Birmingham) and is currently examining different options for exploiting these, while retaining the Company's capex-light structure. The Internet also offers considerable potential for low-cost voice communications, and the Company is currently running trials of a Voice over Internet service (VoIP).

PIPEX is well positioned. Un-encumbered by high cost legacy infrastructure and strategy, we have the right products, brands and financial resources for strong future growth. We have demonstrated the Group's ability to not only make acquisitions but also integrate and drive value from them, confirmed by the growth in margins and revenues. The business is performing in line with our expectations and we continue to grow revenues whilst extracting cost synergies from within the business.

Peter Dubens
Chairman
7 September 2004

**Consolidated profit and loss account (unaudited)
for the six months to 30 June 2004**

	6 months to 30 June 04			Continuing	Continuing
	Existing £'000	Acquisitions £'000	Total £'000	6 months to Jun-03 £'000	Year to Dec-03 £'000
Turnover	38,444	5,183	43,627	11,141	35,218
Cost of sales	(22,094)	(1,257)	(23,351)	(6,736)	(19,893)
Gross profit	16,350	3,926	20,276	4,405	15,325
Operating expenses	(17,939)	(3,713)	(21,652)	(8,104)	(24,828)
Operating (loss)/profit	(1,589)	213	(1,376)	(3,699)	(9,503)
Other interest receivable and similar income			231	-	79
Interest payable and similar charges			(748)	(109)	(469)
Loss on ordinary activities before taxation			(1,893)	(3,808)	(9,893)
Tax on loss on ordinary activities			(9)	-	-
Loss for the financial period			(1,902)	(3,808)	(9,893)
Loss per ordinary share			0.1p	0.5p	0.9p

**Consolidated balance sheet (unaudited)
at 30 June 2004**

	At 30 June 2004	At June 2003	At 31 Dec 2003
	Unaudited	Unaudited	Audited
	£'000	£'000	£'000
Fixed Assets			
Intangible Assets			
Positive Goodwill	87,897	8,617	63,522
Negative Goodwill	(206)	(432)	(319)
Patents	-	-	9
	87,691	8,185	63,212
Tangible Assets	19,422	11,592	16,264
	107,113	19,777	79,476
Current Assets			
Stock	197	-	218
Debtors	10,388	1,457	9,264
Cash at bank and in hand	15,968	5,083	13,267
	26,553	6,540	22,749
Creditors: amounts falling due within one year	(39,920)	(15,714)	(36,476)
Net current liabilities	(13,367)	(9,174)	(13,727)
Total assets less current liabilities	93,746	10,603	65,749
Creditors: amounts falling due after one year	(11,373)	(2,750)	(13,541)
Provisions for liabilities and charges	(889)	(390)	(828)
Net Assets	81,484	7,463	51,380
Capital and Reserves			
Called up share capital	21,641	9,530	18,141
Share capital to be issued	-	-	2,540
Share Premium account	83,497	20,173	52,451
Capital reserve	207	207	207
Other reserves	10,045	3,472	10,045
Profit and loss account	(33,906)	(25,919)	(32,004)
Equity Shareholders' funds	81,484	7,463	51,380

**Consolidated cash flow statement (unaudited)
for the six months to 30 June 2004**

	6 months to 30 June 2004 Unaudited £'000	6 months to 30 June 2003 Unaudited £'000	Year to 31 Dec 03 Audited £'000
Cash Inflow/(Outflow) from operating activities	886	(4,075)	(7,553)
Return on investment and servicing of finance			
Interest received	231	18	-
Interest paid	(605)	-	(4)
Interest element of finance lease	(143)	(55)	(217)
	(517)	(37)	(221)
Tax			
Tax repaid/(paid)	238	-	(344)
Capital expenditure and financial investment			
Purchase of fixed assets	(2,654)	(623)	(1,245)
Sale of assets	796	-	93
	(1,858)	(623)	(1,152)
Acquisitions			
Purchase of subsidiary undertakings	(23,115)	-	(39,745)
Management of liquid resources			
Cash withdrawn from deposit	-	199	304
Financing			
Issue of ordinary share capital	33,000	5,029	45,169
Expenses on issue of ordinary share capital	(1,227)	(184)	(1,933)
Exercise of share options	233	-	99
Capital element of finance lease repayment	(1,878)	(395)	(1,381)
Repayment of loans	(3,061)	-	(40)
Drawdown of new loan	-	-	15,000
	27,067	4,450	56,914
Increase/(Decrease) in cash in the period	2,701	(86)	8,203

**Reconciliation of operating loss to operating cash flow
for the six months to 30 June 2004**

	6 months to 30 June 2004 Unaudited £'000	6 months to 30 June 2003 Unaudited £'000	Year to 31 Dec 03 Audited £'000
Operating loss	(1,376)	(3,699)	(9,503)
Depreciation	2,344	1,476	3,736
Amortisation	3,889	349	1,726
Loss (profit) on sale of assets	(35)	-	16
UITF 17	-	-	577
Increase in working capital	(3,828)	(1,839)	(4,054)
Non cash credit in respect of provisions	(108)	(362)	(51)
Cash Inflow/(Outflow) from operating activities	886	(4,075)	(7,553)

**Reconciliation of net cash flow to movement in net funds/(debt)
(unaudited)
for the six months to 30 June 2004**

	6 months to 30 June 2004 Unaudited £'000	6 months to 30 June 2003 Unaudited £'000	Year to 31 Dec 2003 Audited £'000
Increase/(Decrease) in cash in the period	2,701	(86)	8,203
Net movement in liquid resources	-	(199)	(304)
Conversion of loan stock	-	175	1,570
New loan drawdown	-	-	(15,000)
Repayment of loans	1,561	-	40
Repayment of loan notes	1,500	-	-
Repayments of lease financing	1,878	127	1,381
Loans acquired with subsidiaries	-	-	(1,919)
Finance leases acquired	(410)	-	(3,126)
Movement in net funds	7,230	17	(9,155)
Opening net debt	(11,655)	(2,500)	(2,500)
Closing net debt	(4,425)	(2,483)	(11,655)

**Reconciliation of movements in shareholders' funds (unaudited)
for the six months to 30 June 2004**

	6 months to 30 June 2004	6 months to 30 June 2003	Year to 31 Dec 2003
	Unaudited £'000	Unaudited £'000	Audited £'000
Loss for the financial period	(1,902)	(3,808)	(9,893)
New share capital subscribed (net of issue costs)	31,773	4,845	51,905
Conversion of loan stock	-	175	-
Share capital to be issued	-	-	2,540
Exercise of share options	233	-	-
Granting of options	-	-	577
Net increase in shareholders' funds	30,104	1,212	45,129
Opening shareholders' funds	51,380	6,251	6,251
Closing shareholders' funds	81,484	7,463	51,380

Notes

1. Financial information

The financial information contained in this interim report does not constitute statutory accounts within the meaning of Section 240 of the Companies Act 1985. Financial information is presented on the basis of the accounting policies of the Group as set out in the Annual Report for the year ended 31 December 2003.

The consolidated profit and loss account and cash flow statements for the 6 months to 30 June 2004 and 30 June 2003 and the consolidated balance sheets at 30 June 2004 and 30 June 2003 are unaudited. The financial information for the year ended 31 December 2003 has been extracted from the statutory accounts filed with the Registrar of Companies which contained an unqualified audit report and no adverse statement under Section 237 (2) or (3) of the Companies Act 1985.

2. Dividend

The directors do not recommend the payment of an interim dividend (2003: nil).

3. Loss per share

	6 months to 30 June 2004	6 months to 30 June 2003	Year to 31 December 2003
Loss for the financial period attributable to shareholders	<u>£1,902,000</u>	<u>£3,808,000</u>	<u>£9,893,000</u>
Weighted average number of equity shares in issue	<u>1,920,949,152</u>	<u>839,342,596</u>	<u>1,106,864,224</u>
Basic loss per equity share	<u>0.1p</u>	<u>0.5p</u>	<u>0.9p</u>

4. Acquisition

On 2 April 2004 the Company made a cash offer to Host Europe PLC shareholders on the basis of 2.549p for each Host Europe share, valuing Host Europe at approximately £31.18 million. On the same date, the Company acquired 155,480,000 Host Europe shares at a price of 2.53p per share in the market, representing approximately 13.2% of the issued share capital of Host Europe. Certain Host Europe directors, their family members and one other member of staff had irrevocably undertaken to accept the offer in respect of their beneficial holdings amounting in aggregate to 463,122,141 Host Europe shares, representing approximately 39.3% of the issued share capital. At 2 April 2004 the Company therefore owned, or had commitments to sell, a combined 52.5% of Host Europe's share capital. In addition, the Company had, and exercised, dominant influence over the operating and financial policies of the Host Europe business from this date, as evidenced by action taken by Host Europe in favour of PIPEX. Consequently Host Europe's results have been consolidated from the date on which control was transferred to the Company, being 2 April 2004.

The acquisition was financed by the issue of 314,285,715 new ordinary shares at a price of 10.5p per share raising approximately £33.0 million (before expenses). The cost of the acquisition was £31,396,000 (including expenses).

The goodwill of £28,124,000 arising on the acquisition is being amortised over 10 years, the useful life as estimated by the directors.

The acquisition contributed £5,183,000 of turnover in the period to 30 June 2004, an operating profit of £213,000 (after goodwill amortisation of £703,000).

The turnover and operating loss of Host Europe for the year ended 31 December 2003 were £17,119,000 and £134,000 respectively. The net assets of the Company at 31 December 2003 were £12,927,000.

Details of the fair values of the assets and liabilities acquired are set out below:

	Book value of assets acquired £'000	Fair value adjustments £'000	Fair value of assets acquired £'000
Fixed assets	3,571	-	3,571
Stock	5	-	5
Debtors	1,588	-	1,588
Cash	5,584	-	5,584
Creditors	(7,306)	-	(7,306)
Provisions	<u>(170)</u>	<u>-</u>	<u>(170)</u>
Net Assets	<u>3,272</u>	<u>-</u>	<u>3,272</u>
Goodwill			<u>28,124</u>
Consideration			<u>31,396</u>
Satisfied by:			
Cash			31,181
Costs of acquisition			<u>215</u>
			<u>31,396</u>

Fair values

Adjustments to fair values of net assets from previous acquisitions have been made amounting, in aggregate, to £98,000 decreasing value of assets. Fair values with respect to acquisitions made in 2003 and in 2004 to date remain provisional.

5. Post balance sheet events

Acquisitions

On 6 August 2004, the Company acquired AccentUK Limited, which trades as Nildram, one of the UK's leading independent broadband internet service providers. The total consideration paid in respect of the acquisition was £12.9 million in cash, funded out of The Company's debt facilities with the Bank of Scotland.

Independent review report by KPMG Audit Plc to PIPEX Communications plc

We have been engaged by the company to review the financial information set out on pages 4 to 10 and 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 the terms of our engagement. Our review has been undertaken so that we might state to the company those matters we are required to state to it in this report and for no other purpose. To the fullest extent by law, we do not accept or assume responsibility to anyone other than the company for our review work, for this report or for the conclusions we have reached.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors.

Review work performed

We conducted our review in accordance with guidance contained in the 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 and presentation have been consistently applied unless otherwise disclosed. A review is substantially less in scope than an audit performed in accordance with Auditing Standards 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 June 2004.

KPMG Audit Plc
Chartered Accountants
London

7 September 2004