

24 March 2017

Matomy Media Group | 2016 Final Results

Final results for the year ended 31 December 2016

Matomy Media Group Ltd., a world-leading media company, announces its final results for the year ended 31 December 2016.

Matomy continues to expand and strengthen its leading mobile, video and programmatic offerings

Non-GAAP Financial Highlights¹

Overview of results (\$ millions)	2016	2015	Change
Revenue	276.6	271.0	2.1%
Adjusted gross profit	78.3	76.5	2.4%
Adjusted gross margin	28.3%	28.2%	0.3%
Adjusted EBITDA	17.1	25.7	(34)%
Adjusted net income (loss)	(6.3)	2.3	(374)%

GAAP Financial Highlights

Overview of results (\$ millions, except EPS)	2016 GAAP	2015 GAAP	Change GAAP
Revenue	276.6	271.0	2.1%
Gross profit	56.9	62.3	(8.7)%
Operating income / (loss)	(1.3)	12.1	(111)%
Pre-tax income / (loss)	(3.3)	9.9	(134)%
Net income / (loss)	(8.1)	7.2	(212)%
Net income / (loss) attributable to Matomy	(11.7)	6.6	(277)%
Earnings / (loss) per share	\$(0.13)	\$0.07	(286)%

¹ Non-GAAP related definitions

Adjusted gross profit

Adjusted gross profit is a non-GAAP financial measure that Matomy defines as revenues less direct media costs, which are the direct costs associated with the purchase of digital media. These costs include: payments for digital media based on the revenues Matomy generates from its customers on a revenue-sharing basis; payments for digital media on a non-revenue-sharing basis (CPC or CPM); and serving fees for third-party platforms.

Matomy believes that adjusted gross profit is a meaningful measure of operating performance because it is frequently used for internal management purposes, indicates the performance of Matomy's solutions in balancing the goals of delivering results to its customers whilst meeting margin objectives, and facilitates a more complete understanding of factors and trends affecting Matomy's underlying revenues performance.

Adjusted EBITDA

Adjusted EBITDA is a non-GAAP financial measure that Matomy defines as net income before taxes on income, financial expenses (income), net, equity losses of affiliated companies, net, depreciation and amortisation, share-based compensation expenses and exceptional items (as described below). Adjusted EBITDA is a key measure Matomy uses to understand and evaluate its core operating performance and trends, to prepare and approve its annual budget, to develop short- and long-term operating plans and to determine bonus payments to management. In particular, Matomy believes that by excluding share-based compensation expenses, adjusted EBITDA provides a useful measure for period-to-period comparisons of Matomy's core business.

Adjusted net income

Adjusted net income is a non-GAAP financial measure that Matomy defines as net income before share based compensation expenses and any exceptional items.

**** The 2016 and 2015 results include amortisation charges of \$6.2 million and \$1.9 million, respectively, attributable to the major acquisitions made by Matomy since the start of 2015. Without the effect of these adjustments, the non-GAAP results would have been as follows:**

(\$ millions)	2016	2015	Change
Gross profit	60.9	63.8	(4.6)%
Operating profit	4.9	14.0	(65)%
Pre-tax profit	2.9	11.8	(76)%
Net income / (loss)	(3.4)	8.2	(143)%

Business and operating highlights

A year of transition marked by investment in data-driven technologies, with continued focus around superior proprietary Video, Mobile and other Programmatic solutions

- In 2016, Matomy made a major shift. After conducting successful acquisitions – Mobfox and Team Internet (both in 2014) and Optimatic in late 2015 – the company decided to enhance its product development budget to accelerate the transformation into a leading data-driven, programmatic media company focusing on Mobile and Video.
- In 2016, revenues generated from mobile in app activity (Mobfox) increased approximately **104%** to **\$36.6 million** (2015: \$17.9 million).
- Matomy took decisive action over the past 18 months to shift activity from desktop display advertising, and toward Video, Mobile and Native-based advertising, which generate higher quality and more sustainable long-term revenues with enhanced user engagement. This supports the company’s ability to replace, in a controlled fashion, the continued industry-wide decline in revenues from desktop display activity. As a result, the company recognizes the following benefits:
 - In 2016, revenues generated from aggregate programmatic advertising activity across all media channels increased 30% and accounted for approximately 79% of Matomy's 2016 revenues. (2015: 60%)
- To support growth and leadership around Mobile, the company took the following important steps:
 - Matomy launched myDSP, a data-driven, mobile self-serve demand side platform (DSP), thereby empowering media buyers to optimize their advertising spending, while enhancing the development of the company’s central data management platform (DMP).
 - Matomy introduced mtmy, a full-service data-driven advertising agency, providing cross-channel optimization with focus on social, search and programmatic.
 - Matomy established offices in China and South Korea in April 2016 to access the fast-growing APAC market. In 2016, revenues generated from activity in Asia increased 56% to \$17.9 million (2015: \$11.5 million).
- In 2016, revenues generated from video activity increased 55% to \$111.9 million (2015: \$72.3 million).
- Matomy continued to benefit from the strong industry trend for programmatic advertising spend in the second half of the year. As a result, H2 represented 54% of Matomy's full year revenue and 65% of its adjusted EBITDA (H1 2016: 46% revenue, 35% adjusted EBITDA).
- In 2016, revenues generated from domain monetisation increased 17% to \$63.3 million (2015: \$54.3 million).
- In 2016, Research and development expenses increased by \$4.7 million, or 60%, to \$12.6 million (FY2015: \$7.9 million). This reflects both the consolidation of Optimatic for a full year, which added \$1.4 million to R&D expenses, and additional investment in programmatic proprietary technologies.
- In 2016, Sales and marketing expenses increased by \$4.4 million, or 17%, to \$30.6 million (FY2015: \$26.2 million).
- In 2016, general and administrative expenses decreased by \$1.2 million, or 9.9%, to \$14.9 million (FY2015: \$16.1 million).

- Despite the increased investment and transition detailed above, Matomy succeeded in increasing full-year revenue by 2.1% to \$276.6 million (2015: \$271.0 million).

Ofer Druker, Chief Executive Officer of Matomy, said:

“The best companies evolve with their industry. We spent the past year bolstering our proprietary technology and data-driven capabilities to strengthen our leading marketing technology platforms. In 2016, Matomy underwent a transition with the goal of maximizing today’s technologies in preparation for tomorrow’s opportunities.

“A primary initiative we began in July of 2016 was our strategic plan to increase investment in research and development. By enhancing our proprietary technology enabling programmatic mobile and video advertising, Matomy built on the successful acquisitions of Mobfox and Optimatic with additional capabilities added to our existing leading marketing technology platforms.

“Our ongoing investment in our regional sales and marketing capabilities builds on our successful strategy we began in 2015. Within the past 18 months, Matomy has significantly increased the number of staff, the pace of sales and partnership opportunities with U.S. based companies. Likewise, in both China and South Korea, Matomy added considerably to our existing market presence in these regions.

“In 2016, Matomy aligned both people and resources behind our business units supporting programmatic mobile and video advertising. These actions have already begun to deliver new opportunities for Matomy.

“Combined with our focus on serving the needs of advertisers and publishers in the areas of programmatic mobile and video advertising, demonstrable progress on these key initiatives positions Matomy for a strong year ahead. We look forward to building on these successes in 2017 and generating the growth based on our proprietary technological platforms.”

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[A copy of this announcement will be available on the Matomy website, www.Matomy.com, today from 7.00am GMT.](#)

Matomy will host an analyst conference call at 14:00 BST / 10:00 EDT Monday 27 March 2017 to discuss these results. For more information visit on <http://investors.matomy.com/rns.aspx>

CHAIRMAN'S and CHIEF EXECUTIVE OFFICER'S STATEMENT

Introduction

As the advertising industry continues to mature, so too must Matomy. To do so, we made the strategic decision to invest in order to improve. We expanded our mobile, video and programmatic offerings, strengthened our data-driven capabilities and widened our reach in the Asian-Pacific market. Matomy is now positioned to leverage advanced technology in a global market in order to drive our current and future revenue. We look forward to seeing the return on our investments in 2017.

In 2016, Matomy invested in two primary areas to be a partner of choice and set the company on a successful path for the future. First, Matomy invested in development by adding proprietary technology supporting programmatic mobile and video advertising capabilities. This enabled us to move ahead of our competition by introducing two new services - myDSP and mtmy - that complement our existing portfolio while strengthening core programmatic capabilities. Secondly, the company significantly strengthened its footprint in the Asian-Pacific market adding capabilities to locations in both China and South Korea.

While the media and advertising industry continue to evolve, Matomy is well positioned to succeed in this environment. Our technological differentiation continues to attract top-tier advertisers and publishers, and Matomy will continue to invest in people and capabilities in areas that represent the largest advertising market opportunities.

2016 operating performance

2016 saw Matomy continue its successful transition in the direction of programmatic mobile and video advertising. Anticipating the evolution of advertising towards mobile and video and away from desktop display, Matomy delivered several key initiatives to cement our leadership position serving the needs of advertisers and publishers and positioning the company for a strong 2017. For 2016, we reported a 2% increase in revenue to \$276.6 million on a GAAP basis (FY2015: \$271.0 million), driven primarily by our identified strategic growth areas of mobile, video and domain monetisation. Adjusted EBITDA decreased by 34%, primarily due to additional investments in research and development activities, mainly on Mobfox and Optimatic, as well as to strengthen Matomy's sales force in light of the new technologies, shifting geographical focus and investment around our APAC expansion.

Geographically, Matomy is seeing the strongest growth in the US, which is Matomy's largest market, with revenue in that region increasing 10.1% (\$16.4 million) to \$180.0 million (FY2015: \$163.6 million). This was driven by our increased focus on the US market, due to the ongoing industry-wide shift towards real-time bidding and programmatic advertising, as well as increased video advertiser demand.

Revenues from Asia climbed 56% (\$6.4 million) to \$17.9 million for the year ended 31 December 2016 as we initiated our expansion into Asia. The first stage indicates very encouraging preliminary results. This is a market that we believe holds great promise and we are continuing to direct resources toward further increasing our presence there in the near future.

Matomy's video activity continued to contribute the largest portion of the group's overall global revenue, at 40%.

The Mobile in app (Mobfox) segment experienced the largest percentage revenue growth in 2016, rising 104% to \$36.6 million (2015: \$17.9 million). This increase was primarily driven by enhanced technological developments and the successful launch of new features.

The group's domain monetisation also saw significant growth, increasing by \$9 million, or 17%, to \$63.6 million. This increase was partially driven by publisher growth and the acquisition of the NameDrive domain parking business, as well as the introduction of new ad types to Tonic (formerly called DNTX), our DSP, SSP and self-service ad network for desktop and mobile traffic sources.

2017 Priorities

Our key priorities for 2017 are as follows:

- Continue to focus business and development efforts around programmatic mobile and video advertising capabilities.
- Invest in developing direct and indirect data capabilities to support our offering through Mobfox and Optimatic.
- Continue to strengthen our presence in the North American advertising market.
- Following the successful entry into China and South Korea, accelerate APAC expansion strategy with a focus on mobile activity.
- Advance with our Strategic Review, as announced on 18 October 2016.

Outlook

The Company is entering 2017 with its mobile, programmatic, video and domain monetization offerings, based on its own proprietary technologies, continuing to grow and increase. The business continues to diversify geographically, in particular following the initial successful entry and continued expansion into APAC. These actions reflect the strategic decision of the company to shift focus away from the declining display segment and focus on its core growth areas of mobile and video programmatic-based activities. As a result, the Board remains confident that its actions will lead to continued growth and improved business focus for full year 2017.

Trading for the beginning of 2017 has been encouraging, and the Company currently anticipates an improved trading outcome compared with its previous expectations.

Harel Beit-On
Non-executive Chairman

Ofer Druker
Chief Executive Officer

OPERATIONAL REVIEW*

Revenues by Media Channel

The following table sets out Matomy's revenues by media channel for the years ended 31 December 2016 and 2015.

	Year ended 31 December		
(\$ millions)	2016	2015	
Mobile in-app ⁽¹⁾	36.6	17.9	104%
Video	111.9	72.3	55%
Domain monetisation	63.3	54.3	17%
Email	27.5	34.4	(20)%
Web display	25.4	61.1	(58)%
Mobile web display ⁽¹⁾	3.2	8.5	(62)%
Social	4.7	12.8	(63)%
Other ⁽²⁾	4.0	9.7	(58)%
Total	276.6	271.0	

- (1) Mobile media channel revenues relate solely to revenues generated from mobile web and in-app activities as opposed to aggregate mobile traffic which refers to traffic from mobile devices across all media channels. Aggregate mobile traffic across all media channels contributed approximately 40% of Matomy's revenues in 2016 (FY2015: 30%).

- (2) Primarily comprised of revenues from the search and virtual currency media channels.

*based on consolidated GAAP financial data

Mobile in-app

Mobile in-app media channel revenues increased by \$18.7 million, or 104%, to \$36.6 million for the year ended 31 December 2016 (FY2015: \$17.9 million). This increase was driven primarily by Matomy's successful recruitment and on-boarding of new direct supply and demand partners to Mobfox (Matomy's mobile SSP) and the development and introduction of technological improvements, infrastructure and features such as self-learning automated optimisation of media sources, inventory allocation and bandwidth management.

Video

Video media channel revenues increased by \$39.6 million, or 55%, to \$111.9 million for the year ended 31 December 2016 (FY2015: \$72.3 million). This reflects in part the first full year of revenues from Optimatic (recently measured by ComScore as the 4th largest video SSP in the US), combined with technological improvements to Matomy's video advertising capabilities and supported by strongly increased advertiser demand.

Domain monetisation

Domain monetisation media channel revenues increased by \$9.0 million, or 17%, to \$63.3 million for the year ended 31 December 2016 (FY2015: \$54.3 million), due to continuing investment in research and development, ensuring sustainable competitive advantage, focus on mobile users and fully automated self-service platforms for advertisers and publishers supporting three different profitable and attractive businesses: ParkingCrew, monetization services to website owners; TONIC, a DSP, SSP and self-service ad network for desktop and mobile traffic sources and a domain registration engine.

Email

Email media channel revenues decreased by \$6.9 million, or 20%, to \$27.5 million for the year ended 31 December 2016 (FY2015: \$34.4 million). The decrease was driven mainly by a strategic decision to focus on

running email budget campaigns on Matomy's proprietary platforms, which generate higher and more sustainable revenues on account of a decrease in the email affiliate activity, even at the price of reduced volumes.

Web display

Web display media channel revenues decreased by \$35.7 million, or 58%, to \$25.4 million for the year ended 31 December 2016 (FY2015: \$61.1 million). The web display media channel continues to be affected by changes in the digital advertising ecosystem and the shift towards mobile and video based advertising.

Mobile web display

In line with the industry trend, and the continued erosion of web display activity in all formats, mobile web display media channel revenues decreased by \$5.3 million, or 62%, to \$3.2 million (FY2015: \$8.5 million).

Social

Social media channel revenues decreased by \$8.1 million, or 63%, to \$4.7 million for the year ended 31 December 2016 (FY2015: \$12.8 million). This decrease is mainly attributable to increased Facebook regulation, a shift to an agency model, according to which the fees are recognised on a net basis (not including media costs), which was less customary in 2015. However, without the effect of net reporting of revenues, Matomy would have recorded an additional \$10.5 million revenues in 2016 and \$3.3 million revenues in 2015.

Other media channels

Other media channel revenues decreased by \$5.7 million, or 58%, to \$4.0 million for the year ended 31 December 2016 (FY2015: \$9.7 million). This decrease reflects Matomy's focus on its growth engines, such as mobile in-app and video, and decreasing focus on less strategic activities such as virtual currency and search.

Revenues by Geography

The following table sets out Matomy's revenues by geographical region for the years ended 31 December 2016 and 2015.

	Year ended 31 December		
(\$ millions)	2016	2015	Change
USA	180.0	163.6	10.1%
Europe	44.1	54.5	(19)%
Asia	17.9	11.5	56%
Other	34.6	41.4	(17)%
Total	276.6	271.0	

USA

Revenue from the US market increased by \$16.4 million, or 10.1%, to \$180.0 million for the year ended 31 December 2016 (FY2015: \$163.6 million), representing 65% of global revenues, up from 60% in 2015. This increase reflects our increased focus and investment in the US market due to the ongoing industry-wide shift towards real-time bidding and programmatic advertising, as well as increased video and mobile advertiser demand.

Europe

European revenues decreased by \$10.4 million, or 19%, to \$44.3 million for the year ended 31 December 2016 (FY2015: \$54.5 million), mainly due to challenging conditions and the Company's shift of focus towards higher quality activities in the US and Asia.

Asia

Asia revenues increased by \$6.4 million, or 56%, to \$17.9 million for the year ended 31 December 2016

(FY2015: \$11.5 million) due to Matomy's increased focus and investments in the Far East market, especially around mobile advertising, and the establishment of Matomy's Chinese and Korean offices during the second quarter of 2016. These offices have made a substantial contribution to Matomy's offering and attractiveness to China- and Korea-based app developers, enabling them to better distribute and monetise their applications and media inventory.

FINANCIAL REVIEW

Revenue

Revenues in 2016 increased by \$5.6 million, or 2.1%, to \$276.6 million (FY2015: \$271.0 million). Several factors contributed to this growth, with a continued shift in the revenue mix towards Matomy's growth engines of programmatic video and mobile, reflecting an effective growth of 23% in revenues from media channels other than overall web display activity. These revenues are considered more sustainable and higher quality. Revenues also reflected the 2015 acquisitions which were consolidated for their first full year.

Cost of revenues

<u>\$ millions, except as otherwise indicated</u>	<u>2016</u>	<u>2015</u>
Direct media costs.....	198.3	194.5
Other cost of revenues	21.5	14.2
Cost of revenues	219.8	208.7
Gross margin (%).....	20.6%	23.0%
Adjusted gross margin (non-GAAP) (%)	28.3%	28.2%

Cost of revenues increased by \$11.1 million, or 5.3%, to \$219.8 million (79% of total revenues) for the year ended 31 December 2016 from \$208.7 million (77% of total revenues) the year prior.

Matomy's cost of revenues primarily consists of direct media costs, and therefore the majority of the increase in cost of revenues in 2016 was driven by revenue growth, with adjusted gross margin remaining stable.

Cost of revenues also reflected an increase in allocated costs, in particular amortisation of technology assets from the 2015 acquisitions, which added \$2.5 million to cost of revenues in 2016, and around \$4.9 million increase in server costs due to the consolidation of Optimatic for a full year (adding \$2.8 million) and constant increase in the traffic on Mobfox's servers. All of the above led to a decrease in gross margin.

Operating expenses

<u>\$ millions</u>	<u>2016</u>	<u>2015</u>
Research and development	12.6	7.9
Sales and marketing.....	30.6	26.2
General and administrative	14.9	16.1
Total operating expenses	58.1	50.2
Total operating expenses as a percentage of revenues	21%	19%

Operating expenses increased by \$7.9 million or 16%, to \$58.1 million for the year ended 31 December 2016 (FY2015: \$50.2 million). Operating expenses as a percentage of revenues increased 2% to 21% for 2016 (FY2015: 19%) resulting in an operating margin of (0.5%) (2015: 4.5%).

Operating expenses increased primarily as a result of the strategic investment plan announced in July 2016, which authorised \$3.3 million of additional expenditure to be invested in research and development activities, as well as to strengthen Matomy's sales force in light of the new technologies and shifting geographical focus.

Research and development expenses increased by \$4.7 million, or 60%, to \$12.6 million (FY2015: \$7.9 million). This reflects both the consolidation of Optimatic for a full year, which added \$1.4 million to R&D expenses, and additional investment in programmatic proprietary technologies leading to increased R&D headcount in 2016 compared to 2015, as Matomy becomes a more technologically focused company.

Sales and marketing expenses increased by \$4.4 million, or 17%, to \$30.6 million (FY2015: \$26.2 million).

This increase includes the effect of customer relationship amortisation costs, which increased by \$1.1 million in 2016 compared to 2015, due to the first full year of amortisation of the 2015 acquisitions. In addition, Matomy invested considerable resources in both sales and marketing, under the strategic investment plan referred to above, in particular in establishing and strengthening Matomy's presence in Asian markets through its Chinese and Korean offices.

General and administrative expenses decreased by \$1.2 million, or 9.9%, to \$14.9 million (FY2015: \$16.1 million). While \$2.2 million expenses were added by the 2015 acquisitions, these were offset by continued efficiencies as well as adjustments to future liabilities in the sum of approximately \$0.8 million, which impacted on G&A expenses.

Financial expenses

Financial expenses, net, decreased by \$0.1 million to \$2.1 million for the year ended 31 December 2016 (FY2015: \$2.2 million). Financial expenses related to adjustments to accretion of earnout payments increased year on year by \$0.6 million, while expenses from foreign exchange rate fluctuations, net of hedging transactions, decreased by \$0.8 million due to more stable exchange rates during 2016.

Taxes on income

Taxes on income increased by \$2.0 million to \$4.7 million for the year ended 31 December 2016 (FY2015: \$2.7 million).

Matomy is subject to corporate tax on its income, principally in Israel, the United States and Germany, as well as other jurisdictions in which Matomy has operations. Matomy's effective corporate tax rate was -140% (minus 140 percent) in the year ended 31 December 2016, and 27% in the year ended 31 December 2015.

Matomy's effective corporate tax rate was lower in 2016 compared to 2015 primarily due to valuation allowance totalling \$4.2 million recorded on carry forward losses in both the parent company and few of its subsidiaries.

The Israeli statutory corporate tax rate was 25% in 2016 and 26.5% in 2015. Excluding the effect of the valuation allowance, Matomy's effective corporate tax rate on its taxable profits is higher than the Israeli statutory corporate tax rate because most earnings were generated under US and German jurisdictions with higher prevailing tax rates.

In 2016, Matomy's US operations had taxable income resulting in a liability for both federal and state tax.

Team Internet is subject to German corporate and trade taxes. The effective tax rate of Team Internet on a standalone basis was 31% in 2016 (32% in 2015).

Amortisation of intangible assets

Amortisation expenses amounted to \$15.2 million for the year ended 31 December 2016, an increase of \$3.8 million from amortisation expenses of \$11.4 million for the year ended 31 December 2015. This increase was primarily due to the first full year of amortisation of the intangible assets acquired during 2015.

Net income / (loss)

Net income / (loss) decreased by \$15.3 million to a \$8.1 million net loss for the year ended 31 December 2016 (FY2015: \$7.2 million net income), primarily due to the significantly increased amortisation costs, share-based compensation expenses and tax effects as described above.

Net income / (loss) attributable to Matomy Media Group shareholders was \$3.6 million lower than group net income / (loss) (FY2015: \$0.6 million lower). This difference was primarily due to improved performance and revenues of Team Internet, resulting in an increased redeemable non-controlling interest on account of the put options of the minority shareholder.

Revaluation of redeemable non-controlling interests

As of 31 December 2016, Matomy's \$37.5 million in redeemable non-controlling interests consisted of:

- \$36.8 million relating to Team Internet;
- \$0.6 million relating to Matomy Social; and
- \$0.1 million relating to Avenlo.

Of the above amount, \$13.8 million relating to Team Internet is presented in current liabilities on account of the consideration for the put option which is due to be paid during the first half of 2017.

Redeemable non-controlling interests are classified as mezzanine equity, separate from permanent equity, on the consolidated balance sheets and measured at each reporting period at the higher of their redemption amount or the non-controlling interest book value.

Exceptional items

Matomy views the following items, which were recorded in profit and loss, as exceptional as they are material to the financial statements and non-recurring and therefore were excluded from non-GAAP measures.

- One-time adjustments to M&A related earnout liabilities
- Impairments to intangible assets
- Transaction costs associated with M&A activity in 2015

Liquidity and cash flows

The following table sets out selected cash flow information for Matomy for the years ended 31 December 2016 and 2015.

\$ millions	Year ended 31 December	
	2016	2015
Net cash provided by (used in) operating activities	(0.2)	18.7
Net cash used in investing activities	(6.9)	(29.5)
Net cash provided by (used in) financing activities	1.5	(9.9)
Effect of exchange rate differences on cash	-*	-*
Increase (decrease) in cash and cash equivalents	(5.6)	(20.7)
Cash and cash equivalents at beginning of period	27.3	48.0
Cash and cash equivalents at end of period	21.7	27.3

* Represents amounts less than \$0.1 million.

(A) *Net cash used in / provided by operating activities*

Matomy's net cash used in / provided by operating activities decreased by \$18.9 million to a \$0.2 million outflow for the year ended 31 December 2015 (FY2015: \$18.7 million inflow).

In 2016, net cash provided by operating activities consisted of a net loss of \$8.1 million and \$9.6 million relating to net changes in working capital, offset by \$17.5 million relating to non-cash expenses. Non-cash expenses were primarily depreciation and amortisation of \$16.5 million, significantly higher than prior years due to amortisation related to the 2015 acquisitions, stock-based compensation expense of \$1.9 million, less decreases in deferred tax assets of \$1.0 million.

For the year ended 31 December 2015, Matomy's net cash provided by operating activities consisted of \$7.2 million in net income and \$11.3 million relating to non-cash expenses, and \$0.2 million relating to net changes in working capital. Non-cash expenses were primarily depreciation and amortisation of \$12.6 million, significantly higher than prior years due to amortisation related to the 2014 and 2015 acquisitions, stock-based compensation expense of \$0.9 million, less decreases in deferred taxes of \$2.2 million.

Net changes in working capital in 2016 were mainly driven by a decrease of \$3.3 million in trade receivables, offset by the effects of increases in assets including domains held for sale (\$4.2 million) and other receivables (\$1.7 million), as well as decreases in liabilities including trade payables (\$5.2 million). The remaining amount consisted of smaller movements in various other assets and liabilities.

The decrease in trade receivables was primarily due to the erosion of revenues generated from display activity and the transition to mobile and video programmatic based revenues, which are generally more sustainable higher quality revenues, resulting in a decrease in the trade receivables of around \$3.8 million in comparison to the same period in 2015, partially offset by the successful penetration into APAC, which has extended payment approvals processes compared to the other geographies where Matomy operates.

The increase in domains held for sale reflects the growth of the domain monetisation activity and as a result an increased investment in the purchase of domains.

The decrease in trade payables was primarily driven by a change in the payment terms of some publishers, mainly in connection with video activity, which was made in order to help maintain Matomy's leading position and ensure that it stays competitive and attractive to publishers.

(B) *Net cash used in investing activities*

Net cash used in investing activities decreased by \$22.6 million to \$6.9 million for the year ended 31 December 2016 (FY2015: \$29.5 million). In 2016, net cash used in investing activities primarily included a \$5.1 million capitalised investment in R&D and \$1.6 million investment in property and equipment.

For the year ended 31 December 2015, net cash used in investing activities included a \$17.9 million investment in Optimatic, a \$5.6 million investment in Avenlo, \$2.7 million paid to acquire an advertiser list, and a \$3.3 million investment in property and equipment including capitalised R&D costs.

(C) *Net cash provided by / used in financing activities*

Net cash provided by / used in financing activities increased by \$11.4 million to a \$1.5 million inflow for the year ended 31 December 2016 (FY2015: \$9.9 million outflow).

In 2016, net cash provided by / used in financing activities related primarily to a \$2.0 million net increase in outstanding term loans and overdrafts and \$2.4 million of proceeds from option exercises during the year, less \$3.0 million total payments to non-controlling interests and earnout payments.

For the year ended 31 December 2015, net cash provided by / used in financing activities related primarily to a \$5.3 million net decrease in outstanding term loans, \$5.8 million total payments to non-controlling interests and earnout payments, less \$1.2 million of proceeds from option exercises during the year.

As of 31 December 2016, Matomy had \$13.5 million in term loans. Of those, \$6.9 million are due within one year.

NOTES TO FINANCIAL STATEMENTS

Goodwill

Goodwill represents the excess of the purchase price in a business combination over the fair value of the net tangible and intangible assets acquired.

Matomy's goodwill was created mainly through the 2013, 2014 and 2015 acquisitions.

Matomy has two reporting units and performs an annual impairment test during the fourth quarter of each fiscal year, or more frequently if indicators of potential impairment exist, to determine whether the net book value of each reporting unit exceeds its estimated fair value. During the years ended 31 December 2015 and 2016, no impairment losses were identified.

Segments

Our chief operating decision-maker is our Chief Executive Officer. On a monthly basis, the CEO reviews revenue and adjusted EBITDA at Group level, as well as revenue at the level of media channels, for the purposes of allocating resources and evaluating financial performance.

As a result, Matomy operates in a single reportable segment as a provider of marketing services.

Acquisitions

On 13 November 2015, Matomy completed the acquisition of 100% of the issued and outstanding shares of Optimatic Media Inc. ('Optimatic') for a total consideration of \$33.6 million, as estimated at closing (including contingent consideration). Optimatic is a leading programmatic technological video platform company that enables top-tier publishers to manage their inventory programmatically and a full suite of digital video Supply Side Platform capabilities. Optimatic developed a unique proprietary video platform and is considered a leader in the video space.

On 15 April 2015, Matomy completed the acquisition of 70% of the issued and outstanding shares of a newly formed company, Avenlo Media Group Inc. ('Avenlo') that has purchased the principal business activity and operations of Maven Marketing Group Inc., for a total consideration of \$22.9 million, as estimated at closing

(including contingent consideration). On 8 March 2016, Matomy signed an amendment to the purchase agreement, revising the total consideration to \$10.8 million as estimated at that date (including contingent consideration). Avenlo is a performance email marketing and ad targeting company, incorporated in Canada. The payment to the minority shareholder in Team Internet was made after the balance sheet date, following the exercise by the minority shareholder in Team Internet of the first of three options it holds, resulting in Matomy acquiring an additional 10% of the issued and outstanding shares of Team Internet AG ('Team Internet') for a consideration of \$10.4 million.

Earnings (loss) per share

Matomy's basic earnings (loss) per share decreased by \$0.20, or 286%, to a loss per share of \$0.13 for the year ended 31 December 2016 (FY2015: \$0.07 EPS). This change was influenced primarily by the decrease in after-tax profit, for the reasons noted above. In addition, there was a 2% increase in the weighted average number of outstanding shares mainly due to exercise of share-based incentives in 2016.

Treasury shares

As of 31 December 2016, Matomy has a total of 10,970,111 treasury shares, of which, 1,211,237 shares are held by Team Internet. Team Internet's minority shareholder is entitled to 80% share from gains derived from these shares, which is classified as a redeemable non-controlling interest.

Financial Obligations and Covenants

Matomy's financial obligations and commitments as at 31 December 2016 were as follows:

<u>\$ million</u>	<u>Due within 1 year</u>	<u>Due >1 year</u>	<u>Total</u>
Bank loans	6.9	6.6	13.5
Operating lease obligations	2.4	5.5	7.9
Total	9.3	12.1	21.4

In June 2014, Matomy entered into a \$21.6 million term loan agreement with an Israeli bank. In relation to this loan, Matomy is required to comply with certain covenants, as defined in the loan agreement and its amendments. As of 31 December 2016, Matomy was in full compliance with the financial covenants.

Matomy also has access to a line of credit from the same bank for total borrowings of up to \$13.0 million of which \$6 million is secured. As of 31 December 2016, it had utilised \$2.4 million of the line of credit. This line of credit is unsecured and available to the Company based on meeting certain account receivable conditions.

The line of credit and loans are secured by way of: (i) a fixed charge over Matomy's unpaid equity; (ii) a floating charge over certain of its assets of Matomy and (iii) mutual guarantees between the Israeli companies in the group.

In September 2016, Matomy entered into a \$4.0 million term loan agreement with a U.S. bank. As security, Matomy US and its subsidiary have granted a first priority lien on and security interest in all of the assets of Matomy US, and provided cross guaranties. Matomy US and its subsidiary are required to comply with certain covenants, as defined in the term loan and line of credit agreement and its amendments. As of 31 December 2016, the Company was in full compliance with the financial covenants.

Matomy's subsidiary Team Internet has entered into two further loan agreements with German banks, for \$1.3 million and \$3.0 million respectively.

Financial reporting

This financial information has been prepared under US GAAP principles and in accordance with Matomy's accounting policies. There have been no material changes to Matomy's accounting policies during the year ended 31 December 2016.

Going concern

The Directors confirm that, after making an assessment, they have reasonable expectation that the group has adequate resources to meet its obligations for the foreseeable future.

Principal risks

The Directors assess and monitor the key risks of the business on an ongoing basis. The principal risks and uncertainties that could have a material effect on the Group's performance as set out in detail in the section entitled 'Risk Factors' of the Group's IPO prospectus (the 'Prospectus') dated 9 July 2014 and updated from time to time. These include, *inter alia*, the following:

- Certain internet and technology companies may intentionally or unintentionally adversely affect Matomy's operations, mainly due to announced or unannounced changes and restrictions by such companies.
- The delivery of digital ads and the recording of the performance of digital ads are subject to complex regulations, legal requirements and industry standards, including with respect to fraud, transparency, privacy and data protection, viewability and overall ad quality.
- Matomy's ability to achieve strategic objectives depends on how we react to competitive forces. Matomy faces competition in each of our businesses. Matomy seeks to differentiate its products and services, however many of them are competing with some of the most prevalent digital platforms. Accordingly, failure to achieve these objectives could result in a material adverse effect on Matomy's earnings, cash flows and financial condition.
- Certain elements of Matomy's business may depend on its ability to collect and use data to deliver and optimize the delivery of digital advertisements, and to disclose data relating to the performance of advertisements. Any limitations imposed on Matomy's right and ability to collect, use or disclose this data could diminish the value of its operations.
- The digital advertising industry is highly competitive and fragmented and currently experiencing consolidation, resulting in increasing competition.
- Matomy is dependent on relationships with certain third parties with significant market positions.
- Matomy manages its businesses to deliver strong cash flows to fund operations for profitable growth, however Matomy is exposed to liquidity risks and failure to generate the required level of cash could have a material adverse effect on Matomy's funding level of future liabilities, and could also increase balance sheet liabilities.
- Matomy relies on the continued compatibility of the Matomy Performance Platform with third-party operating systems, software and content distribution channels, as well as newly-acquired systems. Part of Matomy's solutions rely on third-party open source software components, and failure to comply with the terms of the underlying open source software licenses could restrict Matomy's ability to use these developments.
- Matomy may be subject to third-party claims brought against it. Matomy operates in various jurisdictions and is subject to government regulations concerning its employees, including wage-hour laws and taxes.
- A key part of Matomy's growth strategy relates to acquisitions and the ability to effectively integrate and manage them.
- Matomy is an Israeli-domiciled company having its shares admitted to trading on the High Growth Segment of the London Stock Exchange plc's Main Market and on the Tel Aviv Stock Exchange. As such the rights and obligations of shareholders are governed by Israeli law and differ in some respects from English law and share trading is subject to certain settlement mechanics between the UK and Israel.
- Changes in tax laws affecting us and other market participants could have a material adverse effect on Matomy's business.
- Matomy's technology development efforts may be inefficient or ineffective, which may impair our ability to attract buyers and sellers.

Forward-looking statements

Certain statements in this full-year report are forward looking. Although the Group believes that the expectations reflected in these forward looking statements are reasonable, we can give no assurance that these expectations will be fulfilled. Because these statements contain risks and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements. We undertake no obligation to update any forward-looking statements, whether as a result of new information, future events or

otherwise.

Directors' responsibility

The Directors confirm that to the best of their knowledge the condensed set of final audited financial statements, which has been prepared in accordance with US GAAP principles, gives a true and fair view of the assets, liabilities, financial position and profit of the undertakings included in the consolidation as a whole as required by DTR 4.1.

Ofer Druker

Chief Executive Officer

Sagi Niri

Chief Operating Officer

Reconciliation of GAAP measures to non-GAAP measures

The following table presents a reconciliation of adjusted gross profit to gross profit and to revenues, the most directly comparable financial measures calculated in accordance with US GAAP, for the periods indicated:

\$ million	Year ended 31 December	
	2016	2015
Revenues	276.6	271.0
Direct media costs	(198.3)	(194.5)
Adjusted gross profit	78.3	76.5
Adjusted gross margin (%)	28.3%	28.2%
Other cost of revenues	(21.4)	(14.4)
Gross profit	56.9	62.1

The following table presents a reconciliation of adjusted EBITDA to net income, the most directly comparable financial measure calculated in accordance with US GAAP, for the periods indicated:

\$ million	Year ended 31 December	
	2016	2015
Net income	(8.1)	7.2
Taxes on income	4.7	2.7
Financial expenses (income), net	2.1	2.2
Equity (gains)/ losses of affiliated companies, net	0.1	—
Depreciation and amortisation	16.5	12.6
Share-based compensation expenses	1.9	0.8
Exceptional items	(0.1)	0.2
Adjusted EBITDA	17.1	25.7

The following table presents a reconciliation of adjusted net income (loss) to net income, the most directly comparable financial measure calculated in accordance with US GAAP, for the periods indicated:

\$ million	Year ended 31 December	
	2016	2015
Net income	(8.1)	7.2
Exceptional items	(0.1)	0.2
Share-based compensation expenses	1.9	0.8
Adjusted net income (loss)	(6.3)	8.2

MATOMY MEDIA GROUP LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF 31 DECEMBER 2016

IN US DOLLARS IN THOUSANDS

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The Board of Directors Matomy Media Group Ltd.

Re: Report of Independent Auditors

We have audited the accompanying consolidated financial statements of Matomy Media Group Ltd. ("the Company") and its subsidiaries, which comprise the consolidated balance sheets as of 31 December 2016 and 2015, and the related consolidated statements of income (operations), changes in shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries at 31 December 2016 and 2015 and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

CONSOLIDATED BALANCE SHEETS

US dollars in thousands

	31 December	
	2016	2015
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 21,671	\$ 27,271
Trade receivables, net	54,900	58,168
Domains held for sale	9,965	5,814
Other receivables and prepaid expenses	5,502	3,838
<u>Total current assets</u>	<u>92,038</u>	<u>95,091</u>
LONG-TERM ASSETS:		
Property and equipment, net	9,032	4,861
Deferred tax assets	-	3,609
Investment in affiliated companies	1,957	2,017
Other intangible assets, net	36,577	50,342
Goodwill	97,015	96,643
Other assets	398	317
<u>Total long-term assets</u>	<u>144,979</u>	<u>157,789</u>
<u>Total assets</u>	<u>\$ 237,017</u>	<u>\$ 252,880</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

US dollars in thousands

	31 December	
	2016	2015
CURRENT LIABILITIES:		
Redeemable non-controlling interest	\$ 13,776	\$ -
Short-term bank credit and current maturities of bank loans	8,960	6,382
Trade payables	43,982	49,165
Contingent payment obligation related to acquisitions	7,166	6,123
Employees and payroll accrual	4,386	3,870
Accrued expenses and other liabilities	5,531	7,823
<u>Total current liabilities</u>	<u>83,801</u>	<u>73,363</u>
LONG-TERM LIABILITIES:		
Deferred tax liabilities	11,148	15,597
Contingent payment obligation related to acquisitions	10,192	11,968
Bank loans, net of current maturities	6,661	7,357
Other liabilities	821	1,030
<u>Total long-term liabilities</u>	<u>28,822</u>	<u>35,952</u>
REDEEMABLE NON-CONTROLLING INTEREST	<u>23,691</u>	<u>35,365</u>
EQUITY:		
Matomy Media Group Ltd. shareholders' equity:		
Ordinary shares	247	240
Additional paid-in capital	101,066	96,837
Accumulated other comprehensive loss	(3,174)	(3,174)
Retained earnings	8,795	20,528
Treasury shares	(6,231)	(6,231)
<u>Total equity</u>	<u>100,703</u>	<u>108,200</u>
<u>Total liabilities and equity</u>	<u>\$ 237,017</u>	<u>\$ 252,880</u>

The accompanying notes are an integral part of the consolidated financial statements.

24 March 2017

Date of approval of the
financial statements

Ofer Druker

Chief Executive Officer

Sagi Niri

Chief Financial Officer

CONSOLIDATED STATEMENTS OF INCOME (OPERATIONS)**US dollars in thousands except earnings per share data**

	Year ended	
	31 December	
	2016	2015
Revenues	\$ 276,631	\$ 270,976
Cost of revenues	219,781	208,696
Gross profit	56,850	62,280
Operating expenses		
Research and development	12,624	7,871
Selling and marketing	30,630	26,210
General and administrative	14,882	16,083
<u>Total operating expenses</u>	<u>58,136</u>	<u>50,164</u>
Operating (loss) income	(1,286)	12,116
Financial expenses, net	2,057	2,179
Income (loss) before taxes on income	(3,343)	9,937
Taxes on income	4,689	2,681
Income (loss) before equity losses of affiliated companies	(8,032)	7,256
Equity losses of affiliated companies	73	24
Net (loss) income	(8,105)	7,232
Revaluation of redeemable non-controlling interest	(3,141)	(76)
Net income attributable to redeemable non-controlling interests	(487)	(545)
Net loss attributable to other non-controlling interests	-	2
Net (loss) income attributable to Matomy Media Group Ltd.	<u>\$ (11,733)</u>	<u>\$ 6,613</u>
Basic and diluted (loss) earnings per ordinary share	<u>\$ (0.13)</u>	<u>\$ 0.07</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY
US dollars in thousands, except share data

	Ordinary shares		Additional paid-in capital	Accumulated other comprehensive loss	Retained earnings	Treasury shares	Total Matomy Media Group Ltd. shareholders' equity	Non- controlling interests	Total equity
	Number	Amount							
Balance as of 1 January 2015	90,290,596	\$ 236	\$ 93,977	\$ (3,165)	\$ 13,915	\$ (6,231)	\$ 98,732	\$ 711	\$ 99,443
Stock-based compensation	-	-	850	-	-	-	850	-	850
Exercise of options	1,293,124	3	1,193	-	-	-	1,196	-	1,196
Issuance of shares for Avenlo's acquisition	298,670	1	871	-	-	-	872	-	872
Change in parent's ownership interest in subsidiary	-	-	(54)	-	-	-	(54)	(709)	(763)
Other comprehensive income	-	-	-	(9)	-	-	(9)	-	(9)
Net income	-	-	-	-	6,613	-	6,613	(2)	6,611
Balance as of 31 December 2015	91,882,390	240	96,837	(3,174)	20,528	(6,231)	108,200	-	108,200
Stock-based compensation	-	-	1,854	-	-	-	1,854	-	1,854
Exercise of options and vesting of restricted share units	2,694,068	7	2,375	-	-	-	2,382	-	2,382
Net loss	-	-	-	-	(11,733)	-	(11,733)	-	(11,733)
Balance as of 31 December 2016	<u>94,576,458</u>	<u>\$ 247</u>	<u>\$ 101,066</u>	<u>\$ (3,174)</u>	<u>\$ 8,795</u>	<u>\$ (6,231)</u>	<u>\$ 100,703</u>	<u>\$ -</u>	<u>\$ 100,703</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS**US dollars in thousands**

	Year ended 31 December	
	2016	2015
<u>Cash flows from operating activities:</u>		
Net (loss) income	\$ (8,105)	\$ 7,232
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortisation	16,511	12,621
Stock-based compensation	1,854	850
Impairment of intangible assets	396	-
Deferred tax, net	(1,039)	(2,226)
Change in accrued interest and effect of foreign exchange differences on long term loans	(266)	(83)
Equity losses of affiliated companies, net	73	24
Decrease in trade receivables	3,268	4,985
Increase in domains held for sale	(4,151)	(3,786)
Increase (decrease) in other receivables and prepaid expenses	(1,664)	794
Decrease (increase) in other assets	(82)	11
Decrease in trade payables	(5,183)	(1,552)
Decrease in fair value of contingent payment obligation related to acquisitions	(821)	-
Accretion of contingent payment obligation related to acquisitions	712	122
Increase in employees and payroll accrual	516	619
Increase (decrease) in accrued expenses and other liabilities	(2,243)	(883)
Other	55	(4)
Net cash provided by (used in) operating activities	<u>(169)</u>	<u>18,724</u>
<u>Cash flows from investing activities:</u>		
Purchase of property and equipment	(1,653)	(1,055)
Capitalization of research and development costs	(5,106)	(2,195)
Acquisition of technology and database	(158)	(164)
Acquisition of advertiser list	-	(2,666)
Acquisition of Avenlo Media Group	-	(5,570)
Acquisition of Optimatic Media, net of cash acquired	-	(17,896)
Repayment of loan from affiliate	-	88
Bank deposits	-	(58)
Net cash used in investing activities	<u>\$ (6,917)</u>	<u>\$ (29,516)</u>

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

US dollars in thousands

	Year ended	
	31 December	
	<u>2016</u>	<u>2015</u>
<u>Cash flows from financing activities:</u>		
Short-term bank credit, net	\$ 2,093	\$ -
Receipt of bank loans	7,021	1,330
Repayment of bank loans	(6,966)	(6,625)
Expenses related to IPO	-	(139)
Additional payments related to previous acquisitions	(624)	(1,611)
Acquisition of redeemable and non-redeemable non-controlling interest	(565)	(1,328)
Dividend paid to redeemable non-controlling interest	(1,863)	(2,741)
Exercise of options	2,382	1,196
	<u>1,478</u>	<u>(9,918)</u>
Net cash provided by (used in) financing activities		
Effect of exchange rate differences on cash	<u>8</u>	<u>(7)</u>
Decrease in cash and cash equivalents	(5,600)	(20,717)
Cash and cash equivalents at beginning of period	<u>27,271</u>	<u>47,988</u>
Cash and cash equivalents at end of period	<u>\$ 21,671</u>	<u>\$ 27,271</u>
<u>Supplemental disclosure of cash flow activities</u>		
Cash paid during the year for:		
Income taxes, net	<u>\$ 6,336</u>	<u>\$ 5,162</u>
Interest paid	<u>\$ 642</u>	<u>\$ 667</u>

The accompanying notes are an integral part of the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 1:- GENERAL

- a. Matomy Media Group Ltd together with its subsidiaries (collectively - "the Company") provides digital performance-based marketing services to customers which include primarily advertisers, advertising agencies, Apps developers, domain owners and other businesses around the world that promote or sell products and/or services to consumers through digital media, such as websites, mobile apps, video and social media networks. The Company offers its customers a solution for reaching and acquiring their target digital consumer audience across devices. Matomy Media Group Ltd. was incorporated in 2006. The Company's markets are located primarily in the United States and Europe.

The Company's technological platforms provide its customers with access to a wide range of digital media channels, and enable to combine internal media capabilities, data analytics and advanced optimization technologies to ensure meeting the standards and requirements set by its customers. These capabilities also support improved targeting, user acquisition and revenue results for both advertisers and media partners.

The Company manages and optimises its customers' digital marketing campaigns and its media partners' inventory through proprietary technological platforms, maximising their accessibility to their target audience. These technologies also support and provide data analytics capabilities, business intelligence, programmatic media buying and Real-Time-Bidding (RTB) on mobile, video and web. The Company also provides a media management platform (SSP) and offers publishers end to end solution with hundreds of global demand partners.

The Company currently operates across several media channels, including mobile, video, domain monetisation and email. The domain monetisation activity is held in Team Internet, a 70% owned subsidiary, located in Germany (see Note 8).

Since July 2014 the Company is traded in the "London Stock Exchange". On 16 February 2016, the Company's shares commenced trading also on the Tel Aviv Stock Exchange ("TASE") in accordance with the Company's TASE Dual Listing Application pursuant to the Israeli Dual-Listing Law.

- b. The Company adopted a contingency plan, which was approved by the Board, to be effected, in whole or in part, at its discretion, to provide alternative sources of liquidity to allow the Company to meet its cash obligations, all to the extent required. The Company and the Board believes that its existing capital resources and other future measures that may implemented, if so required, will be adequate to satisfy its expected liquidity requirements, including its available credit lines and loans obtained subsequent to 31 December 2016 (see note 17), in the foreseeable future.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("US GAAP"). The significant accounting policies are applied in the preparation of the consolidated financial statements on a consistent basis, as follows:

a. Principles of consolidation:

The consolidated financial statements include the accounts of Matomy Media Group Ltd and its subsidiaries. Intercompany transactions and balances have been eliminated upon consolidation.

Changes in the parent's ownership interest in a subsidiary with no change of control are treated as equity transactions, with any difference between the amount of consideration paid and the change in the carrying amount of the non-controlling interest recognised in equity.

Redeemable non-controlling interests are classified as mezzanine equity, separate from permanent equity, on the consolidated balance sheets and measured at each reporting period at the higher of their redemption amount or the non-controlling interest book value, in accordance with the requirements of Accounting Standards Codification ("ASC") 810 "Consolidation" and ASC 480-10-S99-3A, "Distinguishing Liabilities from Equity".

b. Use of estimates:

The preparation of the consolidated financial statements in conformity with US GAAP requires management to make estimates, judgments and assumptions. The Company's management believes that the estimates, judgments and assumptions used are reasonable based upon information available at the time they are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

On an ongoing basis, the Company's management evaluates estimates, including those related to accounts receivable, fair values of financial instruments, intangible assets and goodwill, fair values of stock-based awards, deferred taxes and income tax uncertainties, and contingent liabilities, among others. Such estimates are based on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities.

c. Financial statements in US dollars:

The US dollar is the currency of the primary economic environment in which Matomy Media Group and most of its subsidiaries operate.

A substantial portion of the revenues and expenses of the Company are generated in US dollars. In addition, financing activities including equity transactions and cash investments are made in US dollars, as well as the Company's forecasted budget, which is

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

prepared in US dollars. Thus, the functional and reporting currency of the Company is the US dollar.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

Accordingly, monetary accounts maintained in currencies other than the US dollar are remeasured into US dollars in accordance with ASC 830, "Foreign Currency Matters". All transaction gains and losses of the remeasured monetary balance sheet items are reflected in the statements of income as financial income or expenses, as appropriate.

d. Cash and cash equivalents:

Cash equivalents are short-term highly liquid investments that are readily convertible into cash with original maturities of three months or less at acquisition.

e. Accounts receivable and allowance for doubtful accounts:

Accounts receivable are stated at realisable value, net of an allowance for doubtful accounts. The Company evaluates specific accounts where information indicates the Company's customers may have an inability to meet financial obligations. Allowance for doubtful accounts as of 31 December 2016 and 2015 were \$ 1,704 and \$ 3,191, respectively.

During the years ended 31 December 2016 and 2015 bad debt expenses were \$ 1,794 and \$ 1,384, respectively, and the write offs of balances included in allowances for doubtful accounts amounted of \$ 2,806 and \$ 790 in the years ended 31 December 2016 and 2015, respectively. During 2016 recoveries amounted to \$ 475 of amounts previously included allowance for doubtful accounts.

f. Domains held for sale:

As part of its operating business, the Company holds domains portfolios available for sale, with an indefinite life. The domains portfolio is used to generate revenues. The domains are stated at cost, are not amortized and are subject to an annual impairment test. At the end of each reporting period domains write-down is measured as the difference between the cost of the domain and market based upon assumptions of revenue multiplier, and is charged to the cost of sales. During the year ended 31 December 2016 and 2015 no write-downs were recorded. Due to the fact that domains portfolio are highly tradeable and there is a general high level of demand and interest from prospective domains portfolio purchasers the domains portfolios are classified as a short term asset.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

g. Property and equipment, net:

Property and equipment are stated at cost, net of accumulated depreciation and amortisation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, at the following annual rates:

	<u>%</u>
Computers and software	33
Office furniture and equipment	6-10
Electronic equipment	10-15
Capitalized research and development costs	33
Leasehold improvements	Over the shorter of related lease period or the life of the improvement

h. Other intangible assets, net:

Other intangible assets are stated at cost, net of accumulated amortisation.

Other intangible assets consist of technology, customer relationships, database and trade name. Customer relationships and trade name are amortised over their estimated useful lives in proportion to the economic benefits realised. This accounting policy results in accelerated amortisation of such customer arrangements and trade name. Technology and database are amortised over their estimated useful lives on a straight-line basis.

Amortisation is calculated using the following annual rates:

	<u>Weighted average %</u>
Technology	23
Customer relationships	19
Database	10
Trade name	20

For impairment of intangible assets, see also note 2k.

i. Goodwill:

Goodwill represents the excess of the purchase price in a business combination over the fair value of the identifiable net tangible and intangible assets acquired. Under ASC 350, goodwill is not amortised, but rather is subject to an annual impairment test.

Following the acquisition of Team Internet, the Company operates in one operating segment, comprised of two reporting units – Matomy and Domain Monetisation. The Company performs an annual impairment test during the fourth quarter of each fiscal year, or more frequently if indicators of potential impairment exist, to determine whether the net book value of a reporting unit exceeds its estimated fair value.

The Company did not recognise any impairment charges related to goodwill during 2016

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

and 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

j. Business combinations:

The Company accounts for business combinations in accordance with ASC 805, "Business Combinations" which requires allocating the purchase price of acquired companies to the identifiable tangible and intangible assets acquired and liabilities assumed and any non-controlling interest at fair value as of the acquisition date. ASC 805 also requires the estimation of fair value of potential contingent consideration at the acquisition date and restructuring and acquisition-related costs to be expensed as incurred.

k. Impairment of long-lived assets:

The Company's long-lived assets are reviewed for impairment in accordance with ASC 360, "Property, Plant, and Equipment" and ASC 350, "Intangibles - Goodwill and other", whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In assessing the recoverability of long-lived assets, the Company makes judgments regarding whether impairment indicators exist based on legal factors, market conditions and operating performances of assets or asset groups. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the future undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognised is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets.

For the year ended 31 December 2016, the Company recognized impairment of technology acquired in Avenlo acquisition, in the amount of \$ 396, which is included in general and administrative expenses on the statements of income (operations). See also note 5c.

For the year ended 31 December 2015, no impairment loss was recorded.

l. Investments in affiliated companies:

Investments in companies in which the Company holds less than 20%, and does not have the ability to exercise significant influence over their operating and financial policies, are stated at cost. Investments in companies in which the Company holds more than 20% (and less than 50%) or has the ability to exercise significant influence over their operating and financial policies are measured using the equity method.

The Company's investments in affiliated companies are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the investment may not be recoverable. For the years ended 31 December 2016 and 2015, no impairment losses were recorded.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

m. Severance pay:

Effective September 2007, the Company's agreements with employees in Israel are generally in accordance with section 14 of the Severance Pay Law - 1963 which provide that the Company's contributions to severance pay fund shall cover its entire severance obligation with respect to period of employment subsequent to September 2007. Upon termination, the release of the contributed amounts from the fund to the employee shall relieve the Company from any further severance obligation and no additional payments shall be made by the Company to the employee. As a result, the related obligation and amounts deposited on behalf of such obligation are not stated on the balance sheet, as the Company is legally released from severance obligation to employees once the amounts have been deposited, and the Company has no further legal ownership on the amounts deposited.

Severance expenses during the years ended 31 December 2016 and 2015 were \$ 1,311 and \$ 1,406, respectively.

n. Employee benefit plan:

The Company's U.S. operations maintain a retirement plan (the "U.S. Plan") that qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. Participants in the U.S. Plan may elect to defer a portion of their pre-tax earnings, up to the Internal Revenue Service annual contribution limit. The Company matches 25% of each participant's contributions, up to 6% of employee deferral. There is also a vesting period for the employer match which is based on the employee date of hire and years of service. Contributions to the U.S. Plan are recorded during the year contributed as an expense in the consolidated statement of income (operations).

Total employer 401(k) contributions for the years ended 31 December 2016 and 2015 were \$ 54 and \$ 0, respectively.

o. Revenue recognition:

The Company provides smart marketing services through customized performance and programmatic solutions supported by internal media capabilities, big data analytics, and optimization technology. Matomy empowers advertising and media partners to meet their evolving growth-driven goals across several media channels, including mobile, video, domain monetisation and email, for multiple industry verticals, such as games and entertainment, healthcare and pharmaceuticals, finance and education, and on a wide variety of devices and operating systems.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

The Company generates a large part of its revenues when its customers' ad campaigns achieve certain predefined measurable and validated results on a per-action basis such as cost-per-acquisition ("CPA"), cost-per-sale ("CPS"), cost-per-lead ("CPL"), cost-per-download ("CPD"), cost-per-view ("CPV"), cost-per-install ("CPI") and pay per call ("PPC"). The Company also generates revenues based on a metric that predefines a certain amount of ad views based on a cost per thousand advertising impressions ("CPM").

The Company recognises revenue when all four of the following criteria are met: persuasive evidence of an arrangement exists; service has been provided; customer fees are fixed or determinable; and collection is reasonably assured. Revenue arrangements are evidenced by executed terms and conditions as part of an insertion order, with an advertiser or an advertising agency.

The Company evaluates whether its revenues should be presented on a gross basis, which is the amount that a customer pays for the service, or on a net basis, which is the customer payment less amounts the Company pays to suppliers. In making that evaluation, the Company considers indicators such as whether the Company is the primary obligor in the arrangement and assumes risks and rewards as a principal or an agent, including the credit risk, whether the Company has latitude in establishing prices and selects its suppliers and whether it changes the products or performs part of the service.

The Company records deferred revenues for unearned amounts received from customers for services that were not recognised as revenues. Deferred revenues amounted to \$ 1,737 and \$ 2,878 at 31 December 2016 and 2015, respectively, and are included within accrued expenses and other liabilities on the balance sheets.

p. Cost of revenues:

Cost of revenues consists primarily of direct media costs associated with the purchase of digital media, data centre costs, amortisation of technology and internally developed software and allocation of attributable personnel and associated costs.

q. Comprehensive income:

The Company accounts for comprehensive income in accordance with ASC 220, "Comprehensive Income". Comprehensive income generally represents all changes in shareholders' equity during the period except those resulting from investments by, or distributions to, shareholders. The Company's items of other comprehensive income relate to foreign currency translation adjustments, which were immaterial for the years 2016 and 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

r. Research and development costs:

Research and development costs are charged to the statement of income (operations) as incurred, except for certain costs relating to internally developed software, which are capitalized and amortized on a straight line basis over their estimated useful life once the asset is ready for its intended use.

s. Internally Developed Software:

The Company capitalizes certain internal software development costs, consisting of direct labor associated with creating the internally developed software. Software development projects generally include three stages: the preliminary project stage (all costs expensed as incurred), the application development stage (costs are capitalized) and the post implementation/operation stage (all costs expensed as incurred). The costs capitalized in the application development stage primarily include the costs of designing the application, coding and testing of the system. Capitalized costs are amortized using the straight line method over the estimated useful life of the software, generally 3 years, once it is ready for its intended use. The Company believes the straight line recognition method best approximates the manner in which the expected benefit will be derived. During 2016 and 2015, the Company capitalized software development costs, net of \$ 5,106 and \$ 2,195, respectively. Amortization expense for the related capitalized internally developed software in 2016 and 2015 totaled \$ 1,179 and \$ 233, respectively, and is included in cost of revenues in the accompanying consolidated statements of income (operations). Management evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets. Capitalized software development costs of \$ 6,058 and \$ 2,149 are included in property and equipment in the consolidated balance sheets as of 31 December 2016 and 2015, respectively (see Note 4).

t. Accounting for stock-based compensation:

The Company accounts for stock-based compensation under ASC 718, "Compensation - Stock Compensation", which requires the measurement and recognition of compensation expense based on estimated fair values for all share-based payment awards made to employees and directors. ASC 718 requires companies to estimate the fair value of equity-based awards on the date of grant, using an option-pricing model. The value of the portion of the award that is ultimately expected to vest, is recognized as an expense over the requisite service periods in the Company's consolidated statement of income (operations). ASC 718 requires forfeitures to be estimated at the time of grant, and revised if necessary in subsequent periods, if actual forfeitures differ from those estimates.

The Company recognizes compensation expenses for the value of its awards, which have graded vesting based on service conditions, using the accelerated attribution method, over the requisite service period of each of the awards, net of estimated forfeitures. Estimated

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

forfeitures are based on actual historical pre-vesting forfeitures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

1. The Company estimates the fair value of stock options granted to its employees and directors using the Black-Scholes-Merton option-pricing model. The Black-Scholes-Merton model requires a number of assumptions, of which the most significant are the fair value of its ordinary shares, the expected stock price volatility, expected option term, risk-free interest rates and expected dividend yield, which are estimated as follows:
 - *Volatility* - the Company's ordinary shares had not been publicly traded for long enough to accurately evaluate volatility, and therefore the volatility assumption is based on the volatilities of other publicly-traded companies that are comparable to the Company, as in previous periods.
 - *Expected option term* - the expected term of the options represents the period of time that the options are expected to be outstanding and is based on the simplified method, which is the midpoint between the vesting date and the end of the contractual term of the option.
 - *Risk-free interest* - the risk-free interest rate assumption is based on the yield from zero-coupon US government bonds appropriate for the expected term of the Company's employee stock options.
 - *Dividend yield* - the Company estimates its dividend yield based on historical pattern, however the Company currently intends to invest funds in business development and not to distribute dividends.

The fair value of the Company's stock options granted to employees and directors for the years ended 31 December 2016 and 2015 was estimated using the following weighted average assumptions:

	Year ended	
	31 December	
	2016	2015
Volatility	43%	45%
Expected option term (in years)	6.3	6.3
Risk-free interest rate	1.3%	1.55%
Dividend yield	0%	0%

2. The Company estimates the fair value of restricted share units ("RSUs") granted to employees according to the fair value of the Company's share at the grant date.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

u. Income taxes:

The Company is subject to income taxes in Israel, Germany, the United States and numerous other jurisdictions. The Company accounts for income taxes in accordance with ASC 740, "Income Taxes". This topic prescribes the use of the liability method, whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company provides a valuation allowance, if necessary, to reduce deferred tax assets to the amount that is more likely than not to be realized. In such determination, the Company considers future reversal of existing temporary differences, future taxable income, tax planning strategies and other available evidence in determining the need for a valuation allowance.

The Company implements a two-step approach to recognise and measure uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% (on a cumulative basis) likely to be realised upon ultimate settlement. The Company classifies interest incurred payable to tax authorities as interest expenses.

v. Concentrations of credit risks:

Financial instruments that could potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade receivables.

Cash and cash equivalents are managed in major banks, mainly in Israel, the United States, United Kingdom and Germany.

The Company's trade receivables are derived from sales to customers located mainly in Europe and the United States. The Company performs ongoing credit evaluations of its customers and a specific allowance for doubtful accounts is provided.

w. Fair value of financial instruments:

The Company applies ASC 820, "Fair Value Measurements and Disclosures". Under this standard, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

In determining fair value, the Company uses various valuation approaches. ASC 820 establishes a hierarchy for inputs used in measuring fair value that maximises the use of observable inputs and minimises the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company can access at the measurement date.

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 - Unobservable inputs for the asset or liability.

x. Derivative instruments:

The Company accounts for derivatives and hedging based on ASC 815, "Derivatives and Hedging", which requires recognizing all derivatives on the balance sheet at fair value. If the derivatives meet the definition of a cash flow hedge and are so designated, depending on the nature of the hedge, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period, or periods, during which the hedged transaction affects earnings. The ineffective portion of a derivative's change in fair value, if any, is recognized in earnings, as well as gains and losses from a derivative's change in fair value that are not designated as hedges are recognized in earnings immediately.

In order to mitigate the potential adverse impact on cash flows resulting from fluctuations in the exchange rate of the New Israeli Shekels ("NIS"), the Company started to hedge portions of its forecasted expenses denominated in NIS with options contracts. The Company does not speculate in these hedging instruments in order to profit from foreign currency exchanges, nor does it enter into trades for which there are no underlying exposures.

The options contracts were not designated as hedging instruments and therefore gains or losses resulting from the change of their fair value are recognized in "financial expenses, net". As of 31 December 2016 and 2015, the Company had derivative liability of \$ 33 and \$ 110, respectively, representing the fair value of outstanding options contracts. The Company measured the fair value of these contracts in accordance with ASC 820, "Fair Value Measurement and Disclosures", and they were classified as level 2.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

Net gain (loss) from hedging transactions recognized in financial expenses, net, during 2016 and 2015, was (\$ 673) and \$ 197, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

The notional value of the Company's derivative instruments as of 31 December 2016 and 2015, amounted to \$ 7,504 and \$ 8,911, respectively. Notional values in USD are translated and calculated based on the spot rates for options. Gross notional amounts do not quantify risk or represent assets or liabilities of the Company, however, they are used in the calculation of settlements under the contracts.

y. Basic and diluted earnings per share:

Basic earnings per share are computed based on the weighted average number of ordinary shares outstanding during each year. Diluted earnings per share are computed based on the weighted average number of ordinary shares outstanding during each year, plus dilutive potential ordinary shares outstanding during the year, in accordance with ASC 260, "Earnings Per Share".

The total weighted average number of shares related to the outstanding options excluded from the calculations of diluted earnings per share, since they would have an anti-dilutive effect, was 10,159,124 and 2,751,352 for the years ended 31 December 2016 and 2015, respectively.

z. Treasury shares:

In accordance with ASC 505-30, the Company shares held by the Company and/or its subsidiaries are recognized at cost of purchase and presented as a deduction from equity. Any gain or loss arising from a purchase, sale, issue or cancellation of treasury shares is recognized directly in equity.

aa. Reclassification:

Certain amounts in prior years' financial statements have been reclassified to conform to the current year's presentation. The reclassification had no effect on previously reported net income (loss) or shareholders' equity.

ab. Recently issued accounting standards:

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which amends the existing accounting standards for revenue recognition. In July 2015, FASB deferred the effective date by one year to December 15, 2017 and permitting early adoption of the standard, but not before the original effective date of December 15, 2016. The FASB also agreed to allow entities to choose to adopt the standard as of the original effective date. In March 2016, the FASB issued Accounting Standards Update No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net) (ASU 2016-08) which clarifies the implementation guidance on principal versus agent considerations. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to the customers.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The new standard also permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the modified retrospective method). The Company is still evaluating the effect that this guidance will have on its consolidated financial statements and related disclosures.

In 2014, the FASB issued ASU 15-2014, Presentation of Financial Statements-Going Concern (Subtopic 205-40): Disclosure of uncertainties about an entity's ability to continue as a Going Concern, which defines management's responsibility to assess an entity's ability to continue as a going concern, and to provide related footnote disclosures if there is substantial doubt about its ability to continue as a going concern. The update is effective for annual period ending 15 December 2016.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (Topic 842) (ASU 2016-02), which generally requires companies to recognize operating and financing lease liabilities and corresponding right-of-use assets on the balance sheet. The standard is effective for the Company for 2020. Early adoption is permitted. The Company is still evaluating the effect that this guidance will have on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting. The new guidance will require all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It will allow an employer to repurchase more of an employee's shares than it can today for tax withholding purposes without triggering liability accounting. It also will allow an employer to make a policy election to account for forfeitures as they occur. The update is effective for fiscal years beginning after 15 December 2016, including interim periods within reporting period, with early adoption permitted. The Company is still evaluating the effect that this guidance will have on its consolidated financial statements and related disclosures.

In November 2016, the FASB issued Accounting Standards Update No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (ASU 2016-18), which requires companies to include amounts generally described as restricted cash and restricted cash equivalents in cash and cash equivalents when reconciling beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This guidance will be effective for the Company 1 January 2018 and early adoption is permitted. The Company is still evaluating the effect that this guidance will have on its consolidated financial statements and related disclosures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 3:- ACQUISITIONS**

a. Acquisition of Avenlo Inc.:

On 15 April 2015, the Company completed the acquisition of 70% of the issued and outstanding shares of a newly formed company, Avenlo Media Group Inc. ("Avenlo") that has purchased the principal business activity and operations of Maven Marketing Group Inc., for a total consideration of \$ 22,860. On 8 March 2016, the Company signed an amendment to the purchase agreement, setting the total consideration on the amount of \$ 10,790. As a result of the amendment, the Company reassessed the fair value of the purchased assets and the assumed liabilities within the measurement period as defined in ASC 805, and adjusted the fair values as of the acquisition date.

The purchase price of Avenlo's shares is composed as follows:

	<u>Amount</u>
Cash consideration	\$ 5,570
Issuance of Company shares	872
Contingent consideration *)	2,859
Redeemable non-controlling interest **)	<u>1,489</u>
Total purchase price	<u>\$ 10,790</u>

*) The contingent consideration will be paid upon achieving certain milestones of future savings, revenue momentum and EBITDA over a period of 4 years following the acquisition date.

As of 31 December 2016, the contingent consideration was estimated at \$ 638 (as of 31 December 2015, the liability amounted to \$ 1,347).

***) According to the agreement, Avenlo's shareholders have the right to individually transfer all of their remaining shareholding, (being 30% in aggregate) to the Company in three equal instalments of 10% every year starting 21 April 2017 ("the Put Options"). The Put Options' exercise prices are calculated based on Avenlo's EBITDA multiplied by a changing multiplier as defined in the agreement. In addition, The Company will have corresponding call options to the put options.

Avenlo is a leading performance email marketing and ad targeting company, and is incorporated under the laws of Canada. The acquisition was accounted for by the acquisition method and accordingly, the purchase price has been allocated according to the estimated fair value of the assets of Avenlo acquired and the liabilities assumed. In performing the purchase price allocation, management has considered, inter alia, Avenlo's business model and its value drivers, its historical financial performance and estimates of future performance. The fair value of the intangible assets was assessed assuming a market participant acquirer utilising the income approach.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 3:- ACQUISITIONS (Cont.)**

The following table summarises the fair values of the assets acquired as of the acquisition date:

Database	\$ 5,451
Technology *)	2,119
Customer relationships	406
Goodwill	<u>2,814</u>
Total assets acquired	<u><u>10,790</u></u>

*) For impairment recorded in 2016, refer to note 5c.

The acquired customer relationships are amortised over their estimated useful lives in proportion to the economic benefits realised (3 year weighted-average useful life). The Database and the technology is amortised over its estimated useful life of 10 and 4 years, respectively, on a straight-line basis.

The results of Avenlo's operations have been included in the consolidated financial statements commencing 1 April 2015. Management estimates that the difference between the consolidation date and the acquisition date has an immaterial effect on its results of operations.

b. Acquisition of Optimatic Media:

On 13 November 2015, the Company acquired the entire share capital of Optimatic Media Inc. ("Optimatic") by way of a reverse triangular merger, pursuant to the terms and conditions of the Agreement and Plan of Merger dated 13 November 2015, for a total consideration of \$ 33,571. Optimatic is a leading programmatic technological Video Platform company that enables top-tier publishers to manage their inventory programmatically and a full suite of digital video Supply Side Platform capabilities. Optimatic developed a unique proprietary video platform and is considered a leader in the video space. Optimatic is incorporated under the laws of USA.

The purchase price of Optimatic's shares is composed as follows:

	<u>Amount</u>
Cash consideration	\$ 20,000
Contingent consideration *)	<u>13,571</u>
Total purchase price	<u><u>\$ 33,571</u></u>

*) The contingent consideration is calculated based on Optimatic's expected EBITDA for the years 2016 to 2018. As of 31 December 2016 and 2015, the contingent consideration amounted to \$ 13,421 and \$ 13,571, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 3:- ACQUISITIONS (Cont.)

The acquisition was accounted for by the acquisition method and accordingly, the purchase price has been allocated according to the estimated fair value of the assets of Optimatic acquired and the liabilities assumed. In performing the purchase price allocation, management has considered, inter alia, Optimatic's business model and its value drivers, its historical financial performance and estimates of future performance. The fair value of the intangible assets was assessed assuming a market participant acquirer utilising the income approach.

The following table summarises the fair values of the assets acquired and liabilities assumed as of the acquisition date:

Cash	\$ 2,104
Deposits	124
Trade receivables	13,838
Other receivables and prepaid expenses	541
Property and equipment	7
Customer relationships	7,028
Trade name	3,468
Technology	13,490
Goodwill	<u>18,735</u>
 Total assets acquired	 59,335
 Trade payables	 (15,345)
Accrued expenses and other liabilities	(667)
Deferred tax liability	<u>(9,752)</u>
 Total liabilities assumed	 <u>(25,764)</u>
 Net assets acquired	 <u><u>33,571</u></u>

The acquired customer relationships and trade name are amortised over their estimated useful lives in proportion to the economic benefits realised (6 and 5 year weighted-average useful life, respectively). The Technology is amortised over its estimated useful life of 5 years, on a straight-line basis.

The results of Optimatic's operations have been included in the consolidated financial statements commencing 1 November 2015. Management estimates that the difference between the consolidation date and the acquisition date has an immaterial effect on its results of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 3:- ACQUISITIONS (Cont.)

In 2016, during the measurement period, the Company completed the purchase price allocation, and updated the goodwill related to Optimatic acquisition in \$ 372, and recorded the following adjustments:

Goodwill	\$ 372
Customer relationships	457
Accrued expenses and other liabilities	(642)
Deferred tax liability	<u>(187)</u>
	<u><u>-</u></u>

Unaudited pro forma condensed results of operations:

The following represents the unaudited pro forma condensed results of operations for the year ended on 31 December 2015, assuming the acquisitions of Avenlo and Optimatic occurred on 1 January 2015. The pro forma information is not necessarily indicative of the results of operations that would have actually occurred had the acquisitions been consummated on this date, nor does it purport to represent the results of operations for future periods.

	Year ended 31 December 2015 Unaudited
	<u><u> </u></u>
Revenues	\$ 327,732
Net income attributable to Matomy Media Group Ltd.	<u><u>4,170</u></u>
Basic net earnings per share	<u><u>0.05</u></u>
Diluted net earnings per share	<u><u>0.04</u></u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 4:- PROPERTY AND EQUIPMENT, NET**

a. Cost:

	31 December	
	2016	2015
Computers and software	\$ 2,895	\$ 4,689
Office furniture and equipment	1,247	820
Electronic equipment	249	188
Capitalized research and development costs	7,488	2,382
Leasehold improvements	1,240	1,190
	<u>13,119</u>	<u>9,269</u>
Accumulated depreciation and amortization:		
Computers and software	1,624	3,147
Office furniture and equipment	358	284
Electronic equipment	126	112
Capitalized research and development costs	1,430	233
Leasehold improvements	549	632
	<u>4,087</u>	<u>4,408</u>
Property and equipment, net	<u>\$ 9,032</u>	<u>\$ 4,861</u>

b. Depreciation and amortization expense amounted to \$ 2,527 and \$ 1,442 for the years ended 31 December 2016 and 2015, respectively.

In 2016 and 2015, the Company wrote off property and equipment in the amount of \$ 2,927 and \$ 1,169, respectively, that were fully depreciated.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 5:- OTHER INTANGIBLE ASSETS, NET

- a. Other intangible assets:

	31 December	
	2016	2015
Original amounts:		
Technology	\$ 28,840	\$ 28,715
Customer relationships *)	27,714	27,257
Database	5,572	5,539
Trade name	3,468	3,468
	<u>65,594</u>	<u>64,979</u>
Accumulated amortisation:		
Technology	12,960	6,369
Customer relationships	14,216	7,758
Database	979	415
Trade name	862	95
	<u>29,017</u>	<u>14,637</u>
Other intangible assets, net	<u><u>\$ 36,577</u></u>	<u><u>\$ 50,342</u></u>

*) The customer relationship was adjusted during the measurement period of Optimatic acquisition. See also note 3b.

- b. Amortisation expense amounted to \$ 13,984 and \$ 11,179 for the years ended 31 December 2016 and 2015, respectively.
- c. During the years ended 31 December 2016 and 2015 the Company recorded an impairment charges in the total amount of \$ 396 and \$ 0, respectively. The impairment charges were attributed to technology related to Avenlo acquisition. The Company updated its revenue forecast based on this technology, and revalued the fair value of the technology based on the future discounted cash flow and royalty savings in the upcoming years.
- d. The estimated future amortisation expense of other intangible assets as of 31 December 2016 is as follows:

2017	\$ 12,359
2018	9,603
2019	6,376
2020	4,981
2021 and after	<u>3,258</u>
	<u><u>\$ 36,577</u></u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 6:- GOODWILL

Changes in goodwill for the years ended 31 December 2016 and 2015 are as follows:

	Year ended 31 December	
	2016	2015
Goodwill at beginning of year	\$ 96,643	\$ 75,094
Acquisitions	-	21,549
Adjustment to goodwill during the measurement period *)	372	-
	<u>\$ 97,015</u>	<u>\$ 96,643</u>

*) See also note 3b.

NOTE 7:- FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table present liabilities measured at fair value on a recurring basis as of 31 December 2016 and 2015:

	31 December 2016			
	Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Liabilities:				
Contingent consideration in connection with acquisitions	\$ -	\$ -	\$ 17,358	\$ 17,358
Derivative liabilities	-	33	-	33
Total financial liabilities	<u>\$ -</u>	<u>\$ 33</u>	<u>\$ 17,358</u>	<u>\$ 17,391</u>
	31 December 2015			
	Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Liabilities:				
Contingent consideration in connection with acquisitions	\$ -	\$ -	\$ 18,091	\$ 18,091
Derivative liabilities	-	110	-	110
Total financial liabilities	<u>\$ -</u>	<u>\$ 110</u>	<u>\$ 18,091</u>	<u>\$ 18,201</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 7:- FAIR VALUE OF FINANCIAL INSTRUMENTS (Cont.)

The following table summarizes the changes in the Company's liabilities measured at fair value using significant unobservable inputs (Level 3), during the year ended 31 December 2016 and 31 December 2015:

	<u>2016</u>	<u>2015</u>
Total fair balance at the beginning of the year	18,091	3,050
Increase in contingent liability due to new acquisitions	-	16,430
Accretion of contingent liability related to acquisitions	712	122
Changes in fair value recognized in earnings *)	(821)	-
Payment of consideration during the period	<u>(624)</u>	<u>(1,511)</u>
Total fair value at the end of year	<u>17,358</u>	<u>18,091</u>

*) The Company updated its forecast related to Optimatic future results, and recorded a decrease in its contingent liability accordingly.

NOTE 8:- REDEEMABLE NON-CONTROLLING INTEREST

The following table provides the movement in the redeemable non-controlling interests:

	Year ended	
	31 December	
	<u>2016</u>	<u>2015</u>
Redeemable non-controlling interest at beginning of year	\$ 35,365	\$ 34,062
Increase in redeemable non-controlling interests due to new subsidiary	-	1,489
Decrease in redeemable non-controlling interests due to change in ownership in subsidiaries *)	(565)	(565)
Revaluation of redeemable non-controlling interest in subsidiaries	3,141	76
Net income attributable to redeemable non-controlling interests	487	545
Dividend declaration to non-controlling interests	(961)	(242)
Classification of redeemable non-controlling interest into current liabilities **)	<u>(13,776)</u>	<u>-</u>
	<u>\$ 23,691</u>	<u>\$ 35,365</u>

*) In November 2016 and October 2015, the non-controlling interest of Matomy Social exercised their put option, and sold 10% of Matomy Social to the Company. As of 31 December 2016 and 2015, the Company holds 90% and 80% of Matomy Social, respectively.

**) During the fourth quarter of 2016, the non-controlling interest of Team Internet exercised their put option and sold 10% of Team Internet to the Company. The payment was made after balance sheet date, and therefore the Company classified the respective amount from redeemable to current liabilities. Following the exercise of the put option, the Company holds 80% of Team Internet shares.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 8:- REDEEMABLE NON-CONTROLLING INTEREST (Cont.)**

Out of the closing balance as of 31 December 2016, an amount of \$ 12,072 is exercisable during the year 2017.

NOTE 9:- BANK LOAN AND CREDIT LINE

- a. On 16 June 2014, the Company signed a term loan agreement with an Israeli bank in an amount of \$ 21,600. The loan agreement requires repayment of 85% of the principal in 12 equal payments every three months commencing 16 September 2014, and 15% of the principal in 4 equal payments every three months commencing 16 September 2017. The loan bore an initial interest of three months USD LIBOR plus 4.5%, which was reduced in January 2015 to USD LIBOR plus 3.5% to be paid together with the relevant portion of the principal. In relation to this loan, the Company is required to comply with certain covenants, as defined in the loan agreement and its amendments. In connection with the new loan obtained in January 2017 (see note 17), the covenants were amendment. As of 31 December 2016, the Company was in full compliance with the financial covenants.
- b. As of December 31, 2016, the Company has line of credit with Israeli banks for total borrowings of up to \$13,000 million, out of which, it utilized \$ 2,409. The Company presented the bank credit, net of cash deposits in the amount of \$ 2,093, at the same bank account.

The line of credit is unsecured and available to the Company based on meeting certain account receivable conditions. Interest rate of the credit line is USD LIBOR plus 3.25% as of 31 December 2016. The Company is in compliance with the agreed account receivable condition.

The line of credit and the loan describes in (a) above secured by way of: (i) a fixed charge over the unpaid equity of the Company; and (ii) a floating charge over all the assets of the Company; and (iii) mutual guarantees between the Israeli companies.

- c. On 11 July 2013, Team Internet borrowed \$ 547 (EUR 450 thousand) from a German bank pursuant to a loan agreement requiring repayment after two years (30 September 2015). The interest rate on the loan was 2.65% and is payable every three months commencing 30 September 2013. The loan was repaid in full on 30 September 2015.
- d. On 20 August 2015, Team Internet signed a term loan agreement with a German bank in an amount of \$ 1,297 (EUR 1,192 thousand). In accordance with the loan agreement, repayment of the principal shall be made in 54 equal monthly payments, commencing 31 March 2016. The loan is indexed to the Euro and bears an interest of 1.8% to be paid on a monthly basis, commencing 31 August 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 9:- BANK LOAN AND CREDIT LINE (Cont.)**

- e. On 28 April 2016, Team Internet signed a loan agreement with a German bank in an amount of \$ 3,021 (EUR 2,660 thousand). In accordance with the loan agreement, repayment of the principal shall be made in 20 equal quarterly payments, commencing 30 September 2016. The loan is indexed to the Euro and bears an interest of 1.1% to be paid on a quarterly basis, commencing 30 June 2016.
- f. On 28 September 2016, the Company's subsidiary in the US ("Matomy US") signed a loan agreement with a bank in the US in an amount of \$ 4,000, and an unsecured line of credit in the amount of \$ 1,000. The term loan agreement requires repayment of principal and interest every 3 months commencing 28 December 2016. The loan bears an initial interest of three months USD LIBOR plus 3.65% and the line of credit bears a monthly interest of LIBOR plus 3.25%. As of 31 December 2016 the credit line was unused. As security, Matomy US and its subsidiary have granted a first priority lien on and security interest in all of the assets of Matomy US, and provided cross guaranties. Matomy US and its subsidiary, Optimatic, are required to comply with certain covenants, as defined in the term loan and line of credit agreement and its amendments. As of 31 December 2016, the Company was in full compliance with the financial covenants.
- g. As of 31 December 2016, the aggregate principal annual maturities according to the loan agreement are as follows:

2017 (current maturities)	\$	6,867
2018		3,794
2019		1,840
2020		747
2021		280
		<hr/>
Total	\$	<u>13,528</u>

NOTE 10:- COMMITMENTS AND CONTINGENT LIABILITIES

- a. The Company rents its facilities under operating lease agreements with an initial term expiring in 2021. Future minimum lease commitments under non-cancellable operating leases for the year ended 31 December 2016 were as follows:

2017	\$	2,403
2018		1,929
2019		1,723
2020		1,638
2021 and thereafter		186
		<hr/>
	\$	<u>7,879</u>

Rent expenses for the years ended 31 December 2016 and 2015, were \$ 2,337 and \$ 2,105, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

The Company has provided guarantees for rent expenses in the amount of \$ 1,060.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 10:- COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

The Company leases its motor vehicles under cancellable operating lease agreements until July 2019. The minimum payment under these operating leases, upon cancellation of these lease agreements, was \$ 16 as of 31 December 2016.

Lease expenses for motor vehicles for the years ended 31 December 2016 and 2015 were \$ 133 and \$ 106, respectively.

- b. From time to time, the Company is party to ordinary and routine litigation incidental to its business. As of December 2016 the Company does not expect the outcome of any such litigation to have a material effect on its consolidated financial position, results of operations, or cash flows.

NOTE 11:- EQUITY

- a. The Company's equity is composed of shares of NIS 0.01 par value each, as follows:

	31 December 2016			31 December 2015		
	<u>Authorised</u>	<u>Issued</u>	<u>Outstanding</u>	<u>Authorised</u>	<u>Issued</u>	<u>Outstanding</u>
	<u>Number of shares</u>					
Ordinary Shares *)	<u>430,500,000</u>	<u>105,546,569</u>	<u>94,576,458</u>	<u>430,500,000</u>	<u>102,852,501</u>	<u>91,882,390</u>

- *) The Ordinary Shares confer upon the holders thereof the right to receive notices and to attend general meetings of the Company, to be present thereat and to participate in and vote at such meetings, the right to participate in all distributions of dividends (whether of cash, assets or in any other lawful way) made by the Company and the right to participate with the other shareholders in the distribution of the surplus of assets of the Company which remains available for distribution on winding-up.

- b. Warrants to investors:

As of 31 December 2016, there are 1,239,735 fully vested outstanding warrants with exercise price of \$ 1.11 which were granted to investors in the past, and are exercisable through August 2017.

- c. Options issued to employees and directors:

Under the share plan as approved in 2012 options and Restricted Share Unit ("RSU") may be granted to employees, directors, officers and consultants of the Company. As of 31 December 2016, the Company reserved for issuance 36,275,287 Ordinary shares. Each option granted under the Plans is fully exercisable up to 4 years and expires in between 7 to 10 years from the date of grant. The 2012 plan is in accordance with section 102 to Israel's

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

Income Tax Ordinance. In 2012, the Company adapted the US Sub-plan which set the grants and tax to employees in the US.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 11:- EQUITY (Cont.)

Any options, which are forfeited or not exercised before expiration, become available for future grants.

As of 31 December 2016, there were 998,534 options available for future grants under the plan.

A summary of the activity in options granted to employees and directors is as follows:

	Number of options	Weighted- average exercise price	Weighted- average remaining contractual term (in years)	Aggregate intrinsic value
Outstanding at 1 January 2016	8,713,947	\$ 1.44	4.4	2,821
Granted	1,838,281	\$ 1.36		
Exercised	(2,349,068)	\$ 1.02		
Forfeited	<u>(793,315)</u>	\$ 2.28		
Outstanding at 31 December 2016	<u>7,409,845</u>	<u>\$ 1.46</u>	<u>5.1</u>	<u>1,480</u>
Vested and expected to vest at 31 December 2016 *)	<u>7,204,878</u>	<u>1.45</u>	<u>5.01</u>	<u>1,465</u>
Exercisable at 31 December 2016	<u>4,093,158</u>	<u>\$ 1.34</u>	<u>2.23</u>	<u>1,261</u>

*) The expected to vest options are the result of applying pre-vesting forfeiture rate assumptions to unvested options outstanding

As of 31 December 2016, the total compensation cost related to options granted to employees and directors, not yet recognized amounted to \$ 1,589.

The aggregate intrinsic value of the outstanding stock options at 31 December 2016 and 2015, represents the intrinsic value of 5,225,268 and 7,358,134 outstanding options that are in-the-money as of such dates. The remaining 2,189,577 and 1,350,813 outstanding options are out-of-the-money as of 31 December 2016 and 2015, and their intrinsic value was considered as zero.

Total intrinsic value of options exercised during the years ended 31 December 2016, and 2015 was \$ 1,088 and \$ 814, respectively

The weighted average grant date fair values of options granted for the years ended 31 December 2016 and 2015, were \$ 1.08 and \$ 0.85, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 11:- EQUITY (Cont.)**

d. Options to non-employees:

The Company's outstanding options to non-employees as of 31 December 2016 were as follows:

<u>Issuance date</u>	<u>Options for Ordinary shares</u>	<u>Exercise price per share</u>	<u>Options exercisable</u>	<u>Exercisable through</u>
January 2010	32,044	0.21	32,044	December 2017

No stock-based compensation expense was recorded in respect of options granted to non-employees in the years ended 31 December 2016 and 2015.

In 2016 and 2015, 0 and 23,900 options to non-employees were exercised, respectively.

e. Restricted Share Units ("RSU") issued to employees and directors:

	<u>Number of RSU's</u>
Unvested at 1 January 2016	<u>640,000</u>
Granted	1,215,000
Vested	(345,000)
Forfeited	<u>(37,500)</u>
Unvested at 31 December 2016	<u>1,472,500</u>
RSU expected to vest after 31 December 2016	<u>1,370,917</u>

RSU expected to vest after 31 December 2016 reflect estimated forfeiture rate.

The weighted average grant date fair value per share for the year ended 31 December 2016 and 2015 was \$ 1.35 and \$ 1.54, respectively.

As of 31 December 2016, the total compensation cost related to RSUs granted to employees, not yet recognized amounted to \$ 1,225.

f. Treasury shares

As of 31 December 2016 and 2015, treasury shares amounted to 10,970,111 shares of which 1,211,236 shares are held by Team Internet.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 12:- EARNINGS PER SHARE**

The following table sets forth the computation of basic and diluted earnings per share:

	31 December	
	2016	2015
Basic and diluted net income (loss) attributable to Matomy Media Group Ltd.	<u>\$ (11,733)</u>	<u>\$ 6,613</u>
Weighted average ordinary shares outstanding (in thousands)	92,884	92,269
Dilutive effect:		
Employee stock options and RSUs (in thousands)	<u>-</u>	<u>3,698</u>
Diluted weighted average ordinary shares outstanding (in thousands)	<u>92,884</u>	<u>95,967</u>
Basic and diluted (loss) earnings per ordinary shares (in dollars)	<u>\$ (0.13)</u>	<u>\$ 0.07</u>

NOTE 13:- TAXES ON INCOME

a. Israeli taxation:

1. Corporate tax rates in Israel:

The Israeli corporate income tax rate was 25% in 2016 and 26.5% in 2015.

In January 2016, the Law for Amending the Income Tax Ordinance (No. 216) (Reduction of Corporate Tax Rate), 2016 was approved, which includes a reduction of the corporate tax rate from 26.5% to 25%, effective from 1 January 2016.

In December 2016, the Israeli Parliament approved the Economic Efficiency Law (Legislative Amendments for Applying the Economic Policy for the 2017 and 2018 Budget Years), 2016 which reduces the corporate income tax rate to 24% (instead of 25%) effective from 1 January 2017 and to 23% effective from 1 January 2018.

2. Tax benefits under the Israeli Law for the Encouragement of Capital Investments, 1959 ("the Law"):

The Company obtained a ruling from the Israeli tax authorities, under which, Matomy Media Group received a "Preferred Enterprise" status through 31 December, 2016, which provides certain benefits, including reduced tax rates. Income not eligible for Preferred Enterprise benefits is taxed at a regular rate. The tax rates applicable for preferred enterprise income are 16% in 2015 and thereafter.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 13:- TAXES ON INCOME (Cont.)**

The entitlement to the above benefits is conditional upon the Company's fulfilling the conditions stipulated by the Law and regulations published thereunder. Should the Company fail to meet such requirements in the future, income attributable to its

Preferred Enterprise program could be subject to the statutory Israeli corporate tax rate and the Company could be required to refund a portion of the tax benefits already received, with respect to such programs. As of 31 December 2016, management believes that the Company is in compliance with all the conditions required by the Law. The Company is considering applying for a new ruling.

As of 31 December 2016, the Company had \$ 5,819 of tax-exempt income attributable to its Privileged Enterprise program resulting from 2012. The Company does not intend to distribute any amounts of its undistributed tax-exempt income as dividends as it intends to reinvest its tax-exempt income within the Company. Accordingly, no deferred income taxes have been provided on income attributable to the Company's Privileged Enterprise programs as the undistributed tax-exempt income is essentially permanent in duration. If such tax exempt income is distributed, it would be taxed at the reduced corporate tax rate applicable to such profits (25%) and an income tax liability of approximately \$ 1,455 would be incurred as of 31 December 2016.

3. Carryforward operating tax losses of the Israeli parent total to \$ 10,318 as of 31 December 2016 and may be used indefinitely.

b. Income taxes on non-Israeli subsidiaries:

Non-Israeli subsidiaries are taxed according to the tax laws in their respective country of residence. The Company's main non-Israeli subsidiaries are located in Germany and in the United States, and are subject to tax rate of approximately 33% and 35%, respectively.

Carryforward operating tax losses of its Canadian subsidiary total approximately \$ 4,000 as of 31 December 2016 which can be carried forward and offset against taxable income up to 20 years, expiring between fiscal 2035 and fiscal 2036.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 13:- TAXES ON INCOME (Cont.)**

c. Deferred tax assets and liabilities:

Deferred taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts recorded for tax purposes. Significant components of the Company's deferred tax assets and liabilities are as follows:

	Year ended 31 December	
	2016	2015
Deferred tax assets:		
Carry forward losses	\$ 2,799	\$ 737
Research and development expenses	542	966
Allowance for doubtful debts	892	763
Intangible assets	1,003	844
Other	420	771
	<u>5,656</u>	<u>4,081</u>
Deferred tax liabilities:		
Intangible assets	\$ 9,218	\$ 12,861
Gain on achieving control	2,022	2,330
Deductible goodwill	1,207	804
Other	73	48
	<u>12,520</u>	<u>16,043</u>
Valuation allowance	<u>(4,284)</u>	<u>(26)</u>
Deferred tax liabilities, net	<u>\$ (11,148)</u>	<u>\$ (11,988)</u>

The net change in the valuation allowance primarily reflects an increase in deferred tax assets on net operating losses and other temporary differences for which full valuation allowance is recorded.

d. Income (loss) before taxes on income is comprised as follows:

	Year ended 31 December	
	2016	2015
Domestic	\$ (6,859)	\$ 4,979
Foreign	3,516	4,958
	<u>\$ (3,343)</u>	<u>\$ 9,937</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 13:- TAXES ON INCOME (Cont.)**

- e. Taxes on income (tax benefit) are comprised as follows:

	Year ended 31 December	
	2016	2015
Current		
Domestic	\$ 268	\$ 1,078
Foreign	5,452	3,827
	<u>5,720</u>	<u>4,905</u>
Deferred		
Domestic	1,731	181
Foreign	(2,762)	(2,405)
	<u>(1,031)</u>	<u>(2,224)</u>
	<u>\$ 4,689</u>	<u>\$ 2,681</u>

- f. A reconciliation of the beginning and ending amount of unrecognised tax benefits related to uncertain tax positions is as follows:

	Year ended 31 December	
	2016	2015
Beginning balance	\$ 139	\$ 136
Increase related to tax positions taken during prior years	66	3
Increases related to tax positions taken during the current year	103	-
Reductions to unrecognized tax benefits as a result of a lapse of the applicable statute of limitations	<u>(139)</u>	<u> </u>
Ending balance	<u>\$ 169</u>	<u>\$ 139</u>

The entire amount of unrecognised tax benefits as of 31 December 2016, if recognised, would reduce the Company's annual effective tax rate.

As of 31 December 2016, the Company and its subsidiaries in Israel and in USA received final, or considered final, tax assessments through 2012.

Team Internet received final tax assessments through 2013.

The Company does not expect uncertain tax positions to change significantly over the next 12 months, except in the case of settlements with tax authorities, the likelihood and timing of which is difficult to estimate.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 13:- TAXES ON INCOME (Cont.)

During the years ended 31 December 2016 and 2015, the Company did not record any interest and exchange rate differences expenses related to prior years' uncertain tax positions, since the amount was immaterial.

The Company believes that it has adequately provided for any reasonably foreseeable outcome related to tax audits and settlement. The final tax outcome of its tax audits could be different from that which is reflected in the Company's income tax provisions and accruals. Such differences could have a material effect on the Company's income tax provision and net income (loss) in the period in which such determination is made.

g. Reconciliation of the theoretical tax expenses:

Reconciliation between the theoretical tax expenses, assuming all income is taxed at the statutory rate in Israel and the actual income tax as reported in the statements of income (operations) is as follows:

	Year ended 31 December	
	2016	2015
Income before taxes as reported in the statements of income	\$ (3,343)	\$ 9,937
Statutory tax rate in Israel	25%	26.5%
	\$ (836)	\$ 2,633
Increase (decrease) in taxes resulting from:		
Effect of "Preferred Enterprise" status *)	729	(20)
Increase in valuation allowance	4,258	23
Tax adjustment in respect of different tax rate of foreign subsidiaries	493	(105)
Non-deductible expense	394	22
Effect of foreign exchange rate ***)	(55)	65
Decrease due to decrease of statutory tax rate	(308)	-
Others	14	63
	<u>\$ 4,689</u>	<u>\$ 2,681</u>
*) Basic earnings per share amounts of the benefit resulting from "Privileged Enterprise" or "Preferred Enterprise" status	<u>\$ -</u>	<u>\$ **)</u>
Diluted earnings per share amounts of the benefit resulting from "Preferred Enterprise" status	<u>\$ -</u>	<u>\$ **)</u>

**) Represents an amount lower than \$ 0.01

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 13:- TAXES ON INCOME (Cont.)

***) Results for tax purposes are measured under, Measurement of results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985, in terms of earnings in NIS. As explained in Note 2c, the financial statements are measured in U.S. dollars. The difference between the annual changes in the NIS/dollar exchange rate causes a difference between taxable income and the income before taxes shown in the financial statements. In accordance with ASC 740-10-25-3(F), the Company has not provided deferred income taxes in respect of the difference between the functional currency and the tax bases of assets and liabilities.

NOTE 14:- REPORTABLE SEGMENTS

a. Reportable segments:

The Company applies ASC 280, "Segment Reporting". While the Company has offerings in multiple media channels, the Company's business operates in one segment, and the Company's chief operating decision maker evaluates the Company's financial information and resources and assesses the performance of these resources on a consolidated basis.

b. Revenues from media channels:

Total revenues from external customers divided on the basis of the Company's media channels are as follows:

	Year ended 31December	
	2016	2015
Display and video *)	\$ 137,288	\$ 133,430
Domain monetisation	63,282	54,268
Email	27,510	34,382
Mobile	39,789	26,412
Social and search	7,529	18,990
Virtual currency	1,233	3,494
Total	<u>\$ 276,631</u>	<u>\$ 270,976</u>

*) Revenues from display and video are integrated to one media channel, since video ads appear before, during or after the display of video content and video is considered one of multiple formats of display.

c. Geographical information:

Revenues by geography are classified based on the location where the consumer completed the action that generated the relevant revenues. The following table sets out the Company's revenues from external customers and property and equipment, net by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

geography for the years ended 31 December 2016 and 2015:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 14:- REPORTABLE SEGMENTS (Cont.)**

1. Revenues from external customers:

	Year ended 31 December	
	2016	2015
United States	\$ 180,048	\$ 163,580
Europe	44,132	54,499
Asia	17,922	11,474
Israel	200	287
Other	34,329	41,123
	<u>\$ 276,631</u>	<u>\$ 270,976</u>

2. Property and equipment, net:

	Year ended 31 December	
	2016	2015
Israel	\$ 5,665	\$ 3,237
United states	1,908	556
Germany	1,335	737
Other	124	331
	<u>\$ 9,032</u>	<u>\$ 4,861</u>

- d. In the year ended 31 December 2016, one customer contributed 20% of the Company's revenues, while no other customer contributed more than 10%.

In the year ended 31 December 2015, one customer contributed 19% of the Company's revenues, while no other customer contributed more than 10%.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**US dollars in thousands****NOTE 15:- FINANCIAL EXPENSES, NET**

	Year ended 31 December	
	2016	2015
Financial income:		
Interest income	\$ 45	\$ 13
Foreign currency remeasurement, net	659	-
Hedging transactions	-	197
Other	32	-
	<u>736</u>	<u>210</u>
Financial expenses:		
Bank fees	(662)	(453)
Interest expense	(746)	(780)
Foreign currency remeasurement, net	-	(1,034)
Hedging transactions	(673)	-
Accretion of contingent payment obligation related to acquisitions	(712)	(122)
	<u>(2,793)</u>	<u>(2,389)</u>
	<u>\$ (2,057)</u>	<u>\$ (2,179)</u>

NOTE 16:- RELATED PARTIES

The Company has activity with related parties as part of its ordinary business. The majority of the related parties' transactions include domain monetisation activity with the non-controlling interest of Team Internet.

Revenues from related parties amounted to \$ 711 and \$ 2,407 for the years ended 31 December 2016 and 2015, respectively. Cost of revenues to related parties amounted to \$ 2,552 and \$ 2,489 for the years ended 31 December 2016 and 2015, respectively.

Trade receivables from related parties amounted to \$ 132 and \$ 354 for the years ended 31 December 2016 and 2015, respectively. Trade payables to related parties amounted to \$ 268 and \$ 243 for the years ended 31 December 2016 and 2015, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

US dollars in thousands

NOTE 17:- SUBSEQUENT EVENTS

On 3 January 2017, after the balance sheet date, the Company signed a term loan agreement with an Israeli bank in an amount of \$ 2,000. In accordance with the loan agreement, repayment of the principal and the interest shall be made in 12 equal monthly payments, commencing 10 April 2017. The loan bears an annual initial interest of three months USD LIBOR plus 4.6%.

After the balance sheet date, the Company signed a secured line of credit in the amount of \$ 5,000 with a bank in the USA. The line of credit bears an interest rate of LIBOR plus 3.25%, and an interest of 0.35% on the unused credit line.

During March 2017 the Company entered in a credit line facility agreement with its Israeli bank securing \$ 6,000 out of the aggregate \$13,000 credit facility, without any additional terms.

During March 2017 the Company updated its credit line facility agreement with the bank in the US, securing the \$ 1,000 credit line. The line of credit bears an unused credit line interest rate of 0.35%.
