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ESI Group

French limited company with a share capital of EUR 17 865 216
Headquarter offices : 100/102 Avenue de Suffren, 75015 Paris
Paris Trade and Company Register (RCS) number 381 080 225

2016 Half year financial report

As of July 31, 2016

First half of 2016 fiscal year, which ends January 31, 2017

Content

1 Half year management report, ended July 31, 2016

Preamble:
The financial information below presents the activity and the financial statements of ESI Group and its subsidiaries, together referred to as "the Group".

1.1. Overall presentation

ESI Group is a leading innovator in Virtual Prototyping software and services. Specialist in material physics, ESI has developed a unique proficiency in helping industrial manufacturers replace physical prototypes by virtually replicating the fabrication, assembly and testing of products in different environments. Today, coupled with Virtual Reality, animated by systems models, and benefiting from data analytics, Virtual Prototyping becomes immersive and interactive: ESI's clients can bring their products to life, ensuring reliable performance, serviceability and maintainability. ESI solutions help world-leading OEM's and innovative companies make sure that their products will pass certification tests - before any physical prototype is built - and that new products are competitive in their market space. Virtual Prototyping addresses the emerging need for products to be smart and autonomous and supports industrial manufacturers in their digital transformation.
Today, ESI's customer base spans nearly every industry sector. The company employs about 1100 high-level specialists worldwide to address the needs of customers in more than 40 countries.

The Group ESI, founded in 1973, has for parent company ESI Group, French limited and listed company, registered in France and governed by the provisions of French law. Created in 1991, ESI Group incorporates the software publishing activity of the Group as well as the marketing and consulting activities, distributed across the world.
The company's headquarters (ESI Group and its subsidiaries) are located 100-102, avenue de Suffren, 75015 Paris, France. The company is listed in compartment C of NYSE Euronext Paris, under the ISIN code: FR 0004110310.

1.2. Revenues and consolidated financial statements

Consolidated half year results

Half year closed on July 31

In € millions	H1-FY 16	H1-FY 15	Δ (actual)	Currency effects
Total sales	**56.0**	**48.4**	**+7.6** (+15.7%)	0.7
Licenses	40.2	34.7	+5.5 (+15.7%)	0.5
Services	15.8	13.7	+2.1 (+15.4%)	0.2
Gross margin	**39.1**	**32.3**	**+6.8** (+21.1%)	0.8
% of sales	*69.8%*	*66.7%*		
EBITDA*	**-0.3**	**-2.5**	**+2.2**	1.2
% of sales	*-0.6%*	*-5.2%*		
Current Operating Profit	**-1.8**	**-3.7**	**+1.9**	1.2
% of sales	*-3.3%*	*-7.7%*		
EBIT	**-2.8**	**-4.6**	**+1.7**	1.2
% of sales	*-5.1%*	*-9.5%*		
Attributable net profit/loss	**-3.5**	**-3.6**	**+0.1**	0.8
% of sales	*-6.2%*	*-7.4%*		
Available cash	**19.3**	**10.0**	**+9.3**	

These figures were approved by the Board of Directors on September 16, 2016.
(*) EBITDA excluding non-recurrent income, including the impact of capitalization of development expenses and impairment allowances/reversals on client receivables.
Acquisitions over the period: "Mineset" was added to the scope of consolidation on February 5, 2016.
Reminder: the strong seasonal nature of the ESI Group's Licenses business results in the recognition of the largest share of annual revenue and results in the fourth quarter of the year. The annual closing date is January 31.

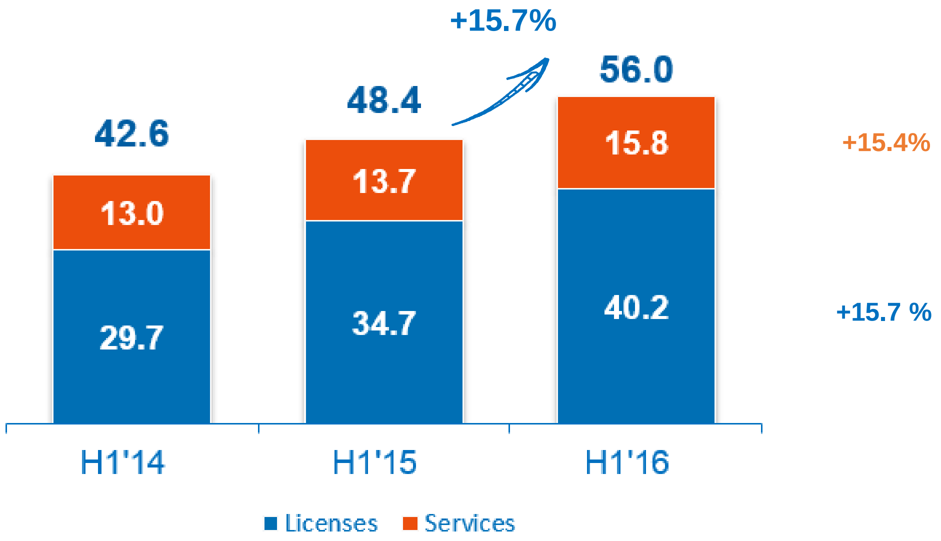
Changes in revenue by quarter

In € millions	Q1 2016 ended April 30	Q1 2015	% chg.	% chg. (cer*)	Q2 2016 ended July 31	Q2 2015	% chg.	% chg. (cer*)
Licenses	19.5	17.1	**+14.3%**	*+14.3%*	20.6	17.6	**+17.1%**	*+14.0%*
Services	7.9	7.0	**+12.3%**	*+12.4%*	7.9	6.7	**+18.7%**	*+16.4%*
Total	**27.4**	**24.1**	**+13.7%**	*+13.8%*	**28.6**	**24.3**	**+17.6%**	*+14.7%*

* cer: at constant exchange rates

First half 2016 revenue: sustained and balanced growth

H1 2016 Total revenue - Revenue for the first half was €56.0 million, an increase of +15.7% at current rates. Revenue from acquisitions was €3.1 million, primarily from the business activities of ESI ITI GmbH which was consolidated on January 6, 2016. The positive exchange impact over the period was moderate at €0.7 million. It was tied to the net strengthening of the Japanese yen compared to the euro, that more than compensated the unfavorable change in other currencies, primarily the Korean won, the Indian rupee, the US dollar and the pound sterling.
The product mix remained stable with Licensing accounting for 71.8% of total revenue compared to 71.7% for the same period of the previous fiscal year.



H1 2016 Licenses - Revenue generated by the Licenses business grew strongly at +15.7% at current exchange rates ('cer') compared to the first half of the previous fiscal year, notably sustained by strong performance in Asia. New business grew significantly, up +24.5% (+11.1% in organic terms) and confirmed the momentum seen during 2016 first quarter. Recurring growth in the installed base was up +14.4% at current rates (+8.6% in organic terms). It was particularly dynamic following positive performance in the first half of 2015 (+26.9% at current rates). The rate of repeat business therefore remained high at 91.8%.

H1 2016 Services - Revenue growth in Services was up +15.4%, spurred by ongoing strategic development in high added value engineering studies, the core of our innovative business and an essential competitive advantage, which grew by +18.2%. This trend was particularly apparent in Japan and is supported and accentuated by our recent acquisitions. It also confirms the relevance of our business model which promotes robust growth in Licensing fostered by a solid Services business that supports and sustains the innovative and functional value of our proposed solutions.

H1 2016 geographical mix - The geographical distribution of total revenues over the period reflects the stronger trend in the Licenses business in Asia (which represented 45.6% versus last year's 41.1% at current exchange rates) in comparison with the Americas (now 16.5% vs last year's 20.4%) and Europe (stable at 38.0% vs last year's 38.5%). Revenue from the BRIC regions grew by +8.9% to end the period at 11.2% of the total revenue (vs last year's 12.2%), negatively affected by the difficult regional economic context in Russia and Brazil.

First half 2016 results: a continued improvement in profitability

Increase in H1 gross margin

Gross Margin increased significantly reaching 69.8% of revenue versus 66.7% in the first half of 2015. The growth was sustained by steady improvements in the gross margins of both Licensing and Services activities, the latter benefiting from the added focus on high value engineering studies and advanced innovative projects.

Operations cost control and ongoing investments

Over the period, the cost of Sales and Marketing (S&M) and General and Administrative costs (G&A) increased globally by +6.4%, compared to the revenue growth of +15.7%. These costs represent respectively 33.8 % and 16.0 % of total revenues, a 432 basis points drop from the previous semester. This development reflects a continuous cost control discipline during the period.

In line with our strategy based on technology innovation, R&D investments increased by +11.7% at current exchange rates. R&D expenses reached €15.5 million (excluding the French Research Tax Credit, 'CIR') and accounted for 38.7% of Licenses revenue over the period, a 140 basis points drop from the previous semester. This high first semester relative rate needs to be put into perspective given the strong seasonality of the licenses business. The continuous investment was for existing technologies as well as for the latest external growth activities. The total amount of R&D posted to the P&L income statement after taking the CIR and capitalization of development costs into account was €13.1 million at current exchange rates, up +33.0% compared to the first half of 2015, notably due to the lesser impact of organic R&D, and to the increased release of new software versions.

Marked improvement in EBITDA and operational profitability

EBITDA increased significantly to -€0.3 million, up +€2.2 million compared to the first half of 2015. This performance was nevertheless impacted by the lower capitalization of R&D costs.

Core Operating Profit (ROC) was -€1.8 million, with a -3.3% to the revenue margin, a marked improvement over the previous year.

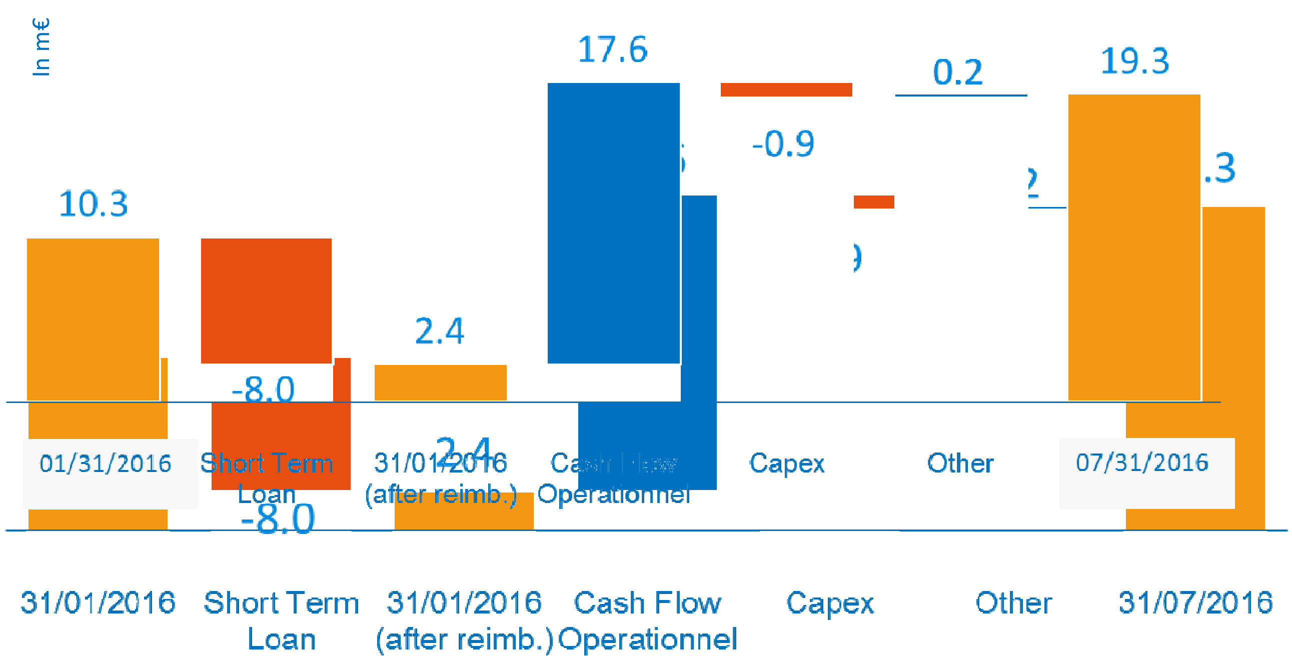
EBIT was -€2.8 million, that is, a margin of -5.1% on revenue, also up considerably compared to the first half of 2015. The increase is more limited than for EBITDA and ROC, primarily consequent to non-recurring costs linked to amortization of the intangible assets of ESI ITI GmbH.

Attributable net profit/loss was -€3.5 million, that is, a net margin of -6.2% on revenue. It consists primarily of tax income of +€1.4 million and financial loss of -€1.6 million. The latter was impacted by the negative revaluation of certain foreign currency hedging tools, especially following the strong Yen increase in the six months period.

1.3. Cash-flows

Available cash amounts to €19.3 million at July 31, 2016 versus €10.0 million at July 31, 2015 and €10.3 million at January 31, 2016.

Restated from the €8 million repayment of the revolving credit used at end 2015, cash flow over the period is positive and amounts to €16.9 million, to be compared with €5,6 million on 2015 first half.



Excluding currency effects, this variation is mainly due to:

- A positive operational cash flow of €17.6 million: despite an EBITDA close to zero for the first half, cash collection from clients related to revenue booked during 2015 last quarter leads to a significantly positive cash flow over the period. This flow was €7.8 million on 2015 first half, as revenue booked during 2014 last quarter was lower than those booked during 2015 last quarter. Moreover, good performance in Japan during 2016 first quarter also contributes to the improvement of operational cash flow, as related cash collection from Japanese clients is achieved at the end of the first half,
- A moderated level of capital expenditures of €0.9 million (versus €1.5 million during 2015 first half), mostly due to IT purchases (servers, computers…).

The acquisition of Mineset Inc. has been fully financed through the syndicated credit line.

1.4. Balance sheet

Net debt amounts to €23.7 million at July 31, 2016 and gearing (debt-to-equity ratio) is at 26.7% due to recent acquisitions.

1.5. Significant events of the period

On February 5, 2016, ESI Group acquired 100% of shares of the US company Mineset Inc., specialized in machine learning. The syndicated credit signed on November 2015 has been used to finance this acquisition.
Furthermore, during 2016 first half, some minority interests of CyDesign Labs Inc and ESI Services Tunisie have been acquired.

1.6. Outlook

The very solid performance over the period, as measured by our economic indicators, clearly and again illustrates the market relevance of our unique strategic positioning based on Immersive Virtual Engineering (IVE[1]) of the full lifecycle of industrial products.
At IVE's core are our Virtual Prototyping and Virtual Reality integrated solutions which are now being extended to include "Big Data", "Machine Learning" and "IoT[2]". Leveraging our recent acquisitions our proven Physics based modelling may now be coupled with the end-to-end management of the product full lifecycle, i.e. from design and development (traditional "CAD-CAE-PLM[3]") to performance in operation, a critical step towards aided and autonomous products (the new disruptive "PPL[4]").
During this first semester Licenses sales experienced solid growth, in particular with new business and high level of repeat business. In parallel the significant progression in high valued-added services demonstrates the specific need to support industrialists, adapted to their maturity level in transition to IVE. The continued improvement of our profitability indicators confirms that our continuously monitored discipline of execution allows us to combine the dynamics of profitable and sustainable growth with high level of investments.
In this demanding global context and accounting for the renewed challenges of the timely integration of our several recent acquisitions, we expect our dynamic sales trend to continue with solid, diversified and balanced growth.

[1] *IVE: Immersive Virtual Engineering*

[2] *IoT: Internet of Things*

[3] *CAD-CAD-PLM: Computer Aided Design – Computer Aided Engineering – Product Lifecycle Management)*

[4] *PPL: Product Performance Lifecycle*

1.7. Risk factors

A detailed analysis of the different risk factors can be found in the 2015 Registration Document (registered by the AMF on May 20, 2016) in the section 2.5 « Risk factors ».
The Group has not identified other risk factors over the period.

1.8. Transactions with related parties

Transactions with related parties consist mainly of royalties paid by the Group's subsidiaries.
These royalties are proportionate to their Licensing revenue and based on the practices observed between software's publishers and distributors in the sector covered by ESI Group.
The nature of the transactions with related parties has not changed materially during the first half of 2016, as compared to January 31, 2016.

1.9. Information on shareholding

Breakdown of share capital and voting rights as of July 31, 2016 :

	Number of shares	% of capital	Number of voting rights	% of voting rights
Famille de Rouvray	1 824 385	30,47%	3 554 425	46,05%
Succession Dubois Jacques	410 419	6,86%	806 838	10,45%
FOUNDING GROUP SUB-TOTAL *(registered shares)*	**2 234 804**	**37,33%**	**4 361 263**	**56,50%**
Chaillou Vincent	13 597	0,23%	26 293	0,34%
des Isnards Charles-Helen	3 751	0,06%	6 552	0,08%
d'Hotelans Éric	1 589	0,03%	2 667	0,03%
MEMBERS OF THE BOARD OF DIRECTORS (EXCL. FOUNDERS) *(registered shares)*	**18 937**	**0,32%**	**35 512**	**0,46%**
Public *(registered shares)*	98 142	1,64%	116 308	1,51%
Public *(bearer shares)*	3 205 956	53,55%	3 205 956	41,53%
PUBLIC SUB-TOTAL	**3 304 098**	**55,19%**	**3 322 264**	**43,04%**
Treasury shares	429 153	7,17%	-	0,00%
TOTAL	**5 986 992**	**100,00%**	**7 719 039**	**100,00%**

The company has no knowledge of any other shareholders holding directly or indirectly, alone or in concert, 5% or more of the share capital or voting rights.

Declaration of the shares movements leading to the crossing of the threshold by the Corporate Officers:
During 2016 first half, no Corporate Officer declared to have crossed the threshold to the upward nor downward direction.

Transactions following the half year closing:
Nothing to report.

2 Half year consolidated condensed financial statements

2.1. Consolidated income statement

(In thousands of euros)	Note	July 31, 2016[1]	July 31, 2015	January 31, 2016
Licenses and maintenance		40,169	34,705	97,038
Consulting		15,161	13,486	26,524
Other		647	208	1,155
TOTAL REVENUE	4.1	55,977	48,398	124,718
Cost of revenue		(16,905)	(16,125)	(34,305)
Research and development costs	5.2	(13,058)	(9,818)	(22,772)
Selling and marketing expenses		(18,913)	(18,041)	(38,611)
General and administrative costs		(8,940)	(8,133)	(17,223)
CURRENT OPERATING RESULT		(1,839)	(3,720)	11,807
Other operating income and expenses	3.2	(992)	(861)	(2,454)
Total operating expenses		(58,808)	(52,979)	(115,365)
INCOME FROM OPERATIONS		(2,831)	(4,581)	9,353
INCOME (LOSS) FROM FINANCIAL ACTIVITIES	6.2	(1,579)	(18)	(950)
Share of profit of associates		(283)	(284)	123
INCOME BEFORE INCOME TAX EXPENSE AND MINORITY INTERESTS		(4,693)	(4,882)	8,527
Provision for income tax	7.1	1,425	1,361	(3,157)
NET INCOME BEFORE MINORITY INTERESTS		(3,268)	(3,521)	5,370
Minority interests		195	56	40
NET INCOME		**(3,463)**	**(3,577)**	**5,330**
Earnings per share (in euros)		(0.59)	(0.65)	0.96
Diluted earnings per share (in euros)		(0.59)	(0.65)	0.96

[1] *Half year consolidated financial statements are subject to a limited review by statutory auditors (not an audit).*

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

Statement of comprehensive income

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Net income before minority interest	(3,268)	(3,521)	5,370
OTHER COMPREHENSIVE INCOME RECYCLED TO INCOME			
Change in the fair value of hedging instruments	(3)	10	23
Currency translation adjustment	(72)	262	61
OTHER COMPREHENSIVE INCOME (LOSS) NOT RECYCLED TO INCOME			
Actuarial gains and losses on pension obligations	-		43
Income and expenses recorded directly in equity	(75)	271	127
COMPREHENSIVE INCOME	**(3,343)**	**(3,250)**	**5,497**
Attributable to Group equity holders	(3,535)	(3,313)	5,454

Attributable to minority interests	192	63	44

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

2.2. Balance sheet

(In thousands of euros)	Note	July 31, 2016	July 31, 2015	January 31, 2016
ASSETS				
NON-CURRENT ASSETS		120,889	92,768	112,966
Goodwill	3.1	41,045	23,945	38,508
Intangible assets	5.1	56,527	50,241	54,623
Non-current assets		4,138	3,827	4,266
Investment in associates		553	493	859
Deferred tax assets	7.2	14,435	11,690	10,548
Other non-current assets		4,123	2,441	4,072
Cash-flow hedge instruments		68	131	90
CURRENT ASSETS		68,976	56,318	94,049
Short term receivables		32,300	31,326	67,676
Other current receivables		13,939	12,247	12,692
Prepaid expenses		3,416	2,697	3,355
Cash and cash equivalents		19,321	10,048	10,327
TOTAL ASSETS		**189,865**	**149,086**	**207,015**
EQUITY AND LIABILITIES				
CONSOLIDATED EQUITY		88,909	83,398	91,727
Equity attributable to parent company owners		**87,882**	**82,653**	**90,842**
Share capital		17,961	17,863	17,865
Additional paid in capital		25,125	24,933	24,938
Reserves and retained earnings		46,510	41,406	40,882
Net income (loss)		(3,463)	(3,577)	5,330
Currency translation difference		1,748	2,027	1,827
Minority interests		**1,027**	**745**	**884**
NON-CURRENT LIABILITIES		49,390	20,482	44,040
Long-term share of financial debt	6.1	36,238	11,709	32,597
Provision for employee benefits		7,489	7,196	6,820
Deferred tax liabilities	7.2	3,773	633	3,281
Cash-flow hedge instruments		463	198	21
Other long-term debt		1,426	745	1,321
CURRENT LIABILITIES		51,567	45,206	71,248
Short-term share of financial debt	6.1	6,789	5,787	13,967
Trade payables		6,084	6,229	8,073
Accrued compensation and income tax expense, and other short-term liabilities		19,214	14,800	26,593

Provisions for contingencies, risks and disputes		1,130	2,031	1,551
Deferred income		18,350	16,360	21,064
TOTAL EQUITY AND LIABILITIES		**189,865**	**149,086**	**207,015**

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

2.3. Consolidated statement of changes in equity

(In thousands of euros except for the number of shares)	Number of shares	Share capital	Additional paid in capital	Net income, reserves and retained earnings	Currency translation difference	Equity attributable to parent company owners	Equity attributable to minority interests	Total Equity
AS AT JANUARY 31, 2015	5, 948,422	17,845	24,899	41,879	1,773	86,396	457	86,853
Hedging instruments fair value				23		23		23
Currency translation difference					54	54	7	61
Actuarial gains and losses on pension obligations				46		46	(3)	43
Recognized income and expense directly in equity				69	54	123	4	127
Net income				5,330		5,330	40	5,370
COMPREHENSIVE INCOME				5,399	54	5,454	44	5,497
Capital increase	6,650	20	39			59		59
Treasury stock				(229)		(229)		(229)
Share-based payments				286		286		286
Transactions with non-controlling interests				(1,123)		(1,123)	384	(740)
AS AT JANUARY 31, 2016	**5, 955,072**	**17,865**	**24,938**	**46,212**	**1,827**	**90,842**	**884**	**91,727**
Hedging instruments fair value				(3)		(3)		(3)
Currency translation difference					(69)	(69)	(3)	(72)
Actuarial gains and losses on pension obligations								
Recognized income and expense directly in equity				(3)	(69)	(72)	(3)	(75)
Net income				(3,463)		(3,463)	195	(3,268)
COMPREHENSIVE INCOME				(3,465)	(69)	(3,535)	192	(3,343)
Capital increase	31,920	96	187			283		283
Treasury stock				10		10		10
Share-based payments				131		131		131
Transactions with non-controlling interests				160	(10)	151	(49)	102
AS AT JULY 31, 2016	**5, 986,992**	**17,961**	**25,125**	**43,048**	**1,748**	**87,882**	**1,027**	**88,909**

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

2.4. Consolidated statement of cash flows

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Net income before minority interests	**(3,268)**	**(3,521)**	**5,370**
Share of profit of associates	283	284	(123)
Depreciation and provisions	2,357	2,263	3,860
Net impact of capitalization of research & development costs	(1,018)	(2,753)	(3,456)
Income taxes (current and deferred)	(1,425)	(1,361)	3,157
Income taxes paid[1]	(1,177)	(954)	(2,817)
Unrealized financial gains and losses [1]	722	447	1,190
Share-based payment transactions	131	143	286
Loss (gain) on sales of assets	13	9	14
CASH FLOWS[1]	**(3,382)**	**(5,444)**	7,481
Trade and other receivables [1]	35,474	29,026	(7,573)
Trade payables	(1,823)	(1,578)	211
Other receivables and other liabilities [1]	(12,640)	(14,240)	(445)
Changes in working capital[1]	**21,011**	**13,209**	**(7,807)**
NET CASH FROM OPERATING ACTIVITIES	**17,630**	**7,765**	(326)
Purchase of intangible assets	(143)	(2,362)	(2,590)
Purchase of tangible assets	(861)	(1,405)	(2,637)
Proceeds from the sale of assets	-	16	24
Acquisition of subsidiaries, net of cash acquired	(4,361)	(257)	(17,552)
Other investment operations	(20)	(490)	(2,112)
NET CASH USED FOR INVESTING ACTIVITIES	**(5,384)**	**(4,498)**	(24,866)
Proceeds from loans	4,558	2,808	47,916
Repayment of borrowings	(8,368)	(7,925)	(24,222)
Proceeds from issue of shares	272	52	59
Sale (purchase) of treasury stock	10	(203)	(229)
NET CASH USED IN FINANCING ACTIVITIES	**(3,529)**	**(5,268)**	23,523
Effect of exchange rate changes on cash and cash equivalents	278	108	55
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**8,994**	**(1,892)**	**(1,613)**
Begining of year	10,327	11,940	11,940
End of year	19,321	10,048	10,327
NET CHANGE IN CASH AND CASH EQUIVALENTS	**8,994**	**(1,892)**	**(1,613)**

(1) July 31, 2015 data have been reclassified for a better comparability with July 31, 2016 – €1.3 million from Changes in working capital to Cash flows.

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

2.5. Notes to the consolidated financial statements

Note 1. Accounting principles

Note 1.1. General information

ESI Group is a pioneer and world-leading provider in Virtual Prototyping that takes into account the physics of materials. ESI developed a unique and innovative know-how to help the industrialists to replace the real prototypes by virtual prototypes, allowing them to make, to assemble and to test their products in different environments.

It should be noted that the Group activity is submitted to important seasonal fluctuations. As typically observed in the software industry, revenue, operating income and net income are historically higher in the second half year.

ESI Group is registered in France, with headquarters at 100-102, avenue de Suffren, 75015 Paris, France. The company is listed in compartment C of NYSE Euronext Paris, under the ISIN code: FR 0004110310.

Half year consolidated condensed financial statements of ESI Group have been validated by the Board of Directors on September 16, 2016.

Note 1.2. Accounting standards applied

The condensed interim consolidated financial statements for the six months ended July 31, 2016 have been prepared in accordance with IAS 34 “Interim Financial Reporting”. As condensed financial statements, they do not include all the information required by IFRS for the preparation of the annual financial statements and must therefore be read in conjunction with the Group consolidated financial statements for the year ending at January 31, 2016.

The accounting methods applied are identical to those applied when preparing the consolidated financial statements for the year ended January 31, 2016, except as regards new standards, amendments and interpretations effective in the European Union and mandatory for annual periods beginning on or after February 1, 2016:

- Amendments to IFRS 11 “Accounting for Acquisitions of Interests in Joint Operations” published by the IASB in May 2014 and applicable to periods beginning from January 1, 2016 forward;
- Amendments to IAS 16 and IAS 38 “Clarification of Acceptable Methods of Depreciation and Amortization” published by the IASB in May 2014 and applicable to periods beginning from January 1, 2016 forward;
- Annual improvements - 2012-2014 cycle, published by the IASB in September 2014 and applicable to periods beginning from January 1, 2016 forward;
- Amendments to IAS 1 “Disclosure Initiative” published by the IASB in December 2014 and applicable to periods beginning from January 1, 2016 forward;
- Amendments to IAS 27 – “Equity Method in Separate Financial Statements”, published by the IASB in August 2014 and applicable to periods beginning from January 1, 2016.

These amendments have no significant impact on the half year consolidated financial statements at July 31, 2016.

Note 1.3. Use of estimates and assumptions

The preparation of the half year consolidated financial statements requires the use of various estimates and assumptions made by the Group's management. These estimates and assumptions have an impact on the valuation of assets and liability, as well as on the amounts recorded as income or expenses over the period. Estimates include, but are not limited to, assumptions used to determine the impact of options granted to employees, business combinations, revenue recognition, depreciation of non-current assets, valuation of deferred tax assets, valuation of hedging instruments, capitalized R&D costs, provisions for doubtful receivables, taxes, risks and disputes, as well as provisions for employee benefits.
Estimates used in half year consolidated financial statements at July 31, 2016 may be amended at 2016 year-end.

Note 2. Significant events of the period

On February 5, 2016, ESI Group acquired 100 % of shares of the US company Mineset Inc., specialized in machine learning. The syndicated credit signed on November 2015 has been used to finance this acquisition.

Note 3. Scope of consolidation

Note 3.1. Goodwill

(In thousands of euros)	January 31, 2016	Increase	Decrease	Foreign exchange gain/(loss)	July 31, 2016
Gross amounts	38,508	2,626		(89)	41,045
TOTAL NET VALUES	**38,508**	**2,626**		**(89)**	**41,045**

Acquisition of Mineset Inc.

In February 2016, ESI Group acquired 100% of shares of the US company Mineset Inc., specialized in machine learning. The preliminary allocation of the acquisition price of €4,017 thousand led to the recognition of a goodwill amounting to €2,626 thousand.

(In thousands of euros)	Preliminary allocation
Capitalized Research and Development costs	1,885
Deferred tax liabilities on intangible assets	(716)
Deferred tax assets on previous years losses	191
Carrying amount of net assets prior to the acquisition	32
NET ASSET VALUE AT ACQUISITION DATE (100%)	**1,392**

Acquisition of ITI

There is no change at July 31, 2016 to the preliminary allocation of ITI acquisition price done at January 31, 2016:

(In thousands of euros)	Preliminary allocation
Customer Relationship	3,044
Capitalized Research and Development costs	1,469
Deferred tax liabilities on intangible assets	(1,354)
Deferred tax assets on previous years losses	220
Carrying amount of net assets prior to the acquisition	174
NET ASSET VALUE AT ACQUISITION DATE (100%)	**3,553**

Minority shareholder has two put options, which have been recorded as a decrease in Equity for €748 thousand.

Acquisition of Civitec

There is no change in the definitive allocation of Civitec acquisition price as compared to the preliminary allocation done in 2015:

(In thousands of euros)	Definitive allocation	Preliminary allocation
Deferred tax assets on previous years losses	272	272
Provision for employee benefits	(9)	(9)
Carrying amount of net assets prior to the acquisition	863	863
NET ASSET VALUE AT ACQUISITION DATE (100%)	**1,125**	**1,125**

Minority shareholder has a put option, which has been recorded as a decrease in Equity for €225 thousand.

Note 3.2. Non-recurring result

Other operating income and expenses are mostly composed of acquisition costs incurred during the period, as well as amortization costs related to intangible assets acquired as part of a business combination.

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Amortization of acquired intangibles assets	(833)	(385)	(1,160)
Acquisition costs	(181)	(476)	(1,294)
Others external income and expenses	22		-
TOTAL OPERATING INCOME AND EXPENSES	**(992)**	**(861)**	**(2,454)**

Increase in amortization costs is mainly related to 2015 acquisitions.

Note 3.3. List of entities in the scope of consolidation

The table below presents the dates of entry into the scope of consolidation, headquarters and the percentage of capital directly or indirectly held of Group subsidiaries:

Subsidiaries	Date of creation or acquisition	Subsidiary headquarters	% Ownership		
			July 31, 2016	July 31, 2015	January 31, 2016
FULLY CONSOLIDATED SUBSIDIARIES					
Calcom ESI SA	December 2002	Lausanne, Switzerland	99 %	99 %	99 %
ESI ITI GmbH	January 2016	Dresden, Germany	**96 %**	-	96 %
ITI Southern Europe	January 2016	Rungis, France	**96 %**	-	96 %
Mineset Inc	February 2016	Milpitas, United States	**100 %**	-	-
Civitec	March 2015	Versailles, France	80 %	80 %	80 %
CyDesign Labs, Inc.	October 2013	Palo Alto, United States	**100 %**	99 %	99 %
CyDesign LTD	October 2013	West Midlands, United Kingdom	**100 %**	99 %	99 %
Efield AB	December 2011	Kista, Sweden	100 %	100 %	100 %
Engineering System International	April 1973	Paris, France	100 %	100 %	100 %
Engineering System International GmbH	July 1979	Eschborn, Germany	100 %	100 %	100 %
ESI Group Beijing Co., Ltd	October 2010	Beijing, China	100 %	100 %	100 %
ESI Group Hispania Sl	February 2001	Madrid, Spain	100 %	100 %	100 %
ESI Italia Srl	September 2008	Bologna, Italy	100 %	100 %	100 %
ESI North America, Inc.	March 1992	Troy, Michigan, United States	100 %	100 %	100 %
ESI South America Comercio e Servicios de Informatica, Ltda	June 2008	Sao Paulo 015, Brazil	95 %	95 %	95 %
ESI Software (India) Private Limited	February 2004	Bangalore, India	100 %	100 %	100 %
ESI Services Tunisie	April 2009	Hammam Lif, Tunisia	**95 %**	90 %	90 %
ESI UK Limited	January 2002	London, United Kingdom	100 %	100 %	100 %
ESI US Holding, Inc.	August 2002	Dover, Delaware, United States	49 %	49 %	49 %
ESI US R&D, Inc.	August 2002	San Diego, California, United States	74 %	74 %	74 %
ESI-ATE Holdings Limited	July 2006	Hong Kong, China	100 %	100 %	100 %

ESI-ATE Technology (China), Ltd	August 2006	Beijing, China	100 %	100 %	100 %
ESI US, Inc.	February 2012	Farmington Hills, United States	100 %	100 %	100 %
ESI Services Vietnam Co., Ltd	December 2013	Ho Chi Minh City, Vietnam	100 %	100 %	100 %
ESI Software Germany GmbH	August 2011	Stuttgart, Germany	100 %	100 %	100 %
Hankook ESI Co., Ltd.	September 1995	Seoul, South Korea	99 %	99 %	99 %
Hong Kong ESI CO., Limited	February 2004	Hong Kong, China	100 %	100 %	100 %
Mecas ESI Sro	May 2001	Plzen, Czech Republic	95 %	95 %	95 %
Nihon ESI K.K.	July 1991	Tokyo, Japan	97 %	97 %	97 %
OpenCFD Limited	September 2012	Berkshire, United Kingdom	100 %	100 %	100 %
Pacific Mindware Engineering Private Limited	December 2008	Maharashtra, India	100 %	100 %	100 %
Straco	April 2001	Compiègne, France	98 %	98 %	98 %
Zhong Guo ESI Co., Ltd	February 2004	Guangzhou, China	100 %	100 %	100 %
SUBSIDIARY ACCOUNTED FOR USING THE EQUITY METHOD					
AVIC ESI (Beijing) Technology Co., Ltd	February 2014	Beijing, China	45 %	45 %	45%

ESI US Holdings is fully consolidated, as ESI Group has exclusive control.

Note 4. Operating data

Note 4.1. Revenue

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
TOTAL LICENSES AND MAINTENANCE	40,169	34,705	97,038
Consulting	15,161	13,486	26,524
Other	647	208	1,155
TOTAL SERVICES	15,809	13,694	27,680
CONSOLIDATED REVENUE	**55,977**	**48,398**	**124,718**
Total co-financed research and development projects in revenue from services	*2,120*	*1,638*	*3,209*

Note 4.2. Information by geographic area

Revenue is distributed over the regions where it is effectively earned.

(In thousands of euros)	EMEA	Asia-Pacific	America	Eliminations	Consolidated
HALF YEAR ENDED JULY 31, 2016					
Out of Group customers	21,244	25,507	9,226	-	55,977
Affiliate companies	28,001	4,063	3,634	(35,698)	-
NET SALES	49,244	**29,570**	**12,860**	(35,698)	55,977
YEAR ENDED JANUARY 31, 2016					
Out of Group customers	57,098	44,291	23,329	-	124,718
Affiliate companies	76,535	8,206	6,944	(91,685)	-

NET SALES	**133,633**	**52,497**	**30,273**	**(91,685)**	**124,718**
HALF YEAR ENDED JULY 31, 2015					
Out of Group customers	18,650	19,887	9,862	-	48,398
Affiliate companies	26,963	4,036	3,482	(34,482)	-
NET SALES	**45,613**	**23,923**	**13,344**	**(34,482)**	**48,398**

Note 4.3. Personnel costs

Personnel costs are presented by destination in the income statement. Their split by nature is as follows:

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Salaries	(31,453)	(29,015)	(61,739)
Payroll taxes	(8,311)	(7,646)	(15,994)
Share-based payment	(131)	(143)	(286)
Long term employee benefits	(304)	(347)	(575)
TOTAL PERSONNEL COSTS	**(40,200)**	**(37,152)**	**(78,594)**

Note 5. Intangible assets

Note 5.1. Change in the gross value, amortization and net value of intangible assets

(In thousands of euros)	January 31, 2016	Change in scope of consolidation	Increase	Decrease	Foreign exchange gain/loss	July 31, 2016
GROSS AMOUNTS						
Research and development costs	49,166	1,885	13,843	(56)	21	64,859
Intangible assets with an indefinite useful life	12,044					12,044
Other intangible assets	22,556		93	(132)	4	22,521
TOTAL	**83,766**	**1,885**	**13,936**	**(188)**	**25**	**99,424**
AMORTIZATION						
Research and development costs	(15,626)		(12,826)	56		(28,396)
Intangible assets with an indefinite useful life	(73)					(73)
Other intangible assets	(13,444)		(1,100)	132	(16)	(14,429)
TOTAL	**(29,143)**		**(13,925)**	**188**	**(16)**	**(42,897)**
NET CARRYING AMOUNTS						
Research and development costs	33,539	1,885	1,018	-	21	36,463
Intangible assets with an indefinite useful life	11,971					11,971
Other intangible assets	9,112		(1,007)	-	(12)	8,093
TOTAL	**54,623**	**1,885**	**(11)**	**-**	**8**	**56,527**

Note 5.2. Research and development costs

NET IMPACT OF THE CAPITALIZATION OF RESEARCH AND DEVELOPMENT COSTS

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Research and development costs capitalized during the period	13,843	13,031	23,556

Research and development costs amortized during the period	(12,826)	(10,278)	(20,100)
NET IMPACT OF THE CAPITALIZATION OF RESEARCH AND DEVELOPMENT COSTS	**1,018**	**2,753**	**3,456**

RECONCILIATION OF R&D COSTS INCURRED AND ACCOUNTED FOR TO THE INCOME STATEMENT

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
R&D costs incurred during the period	**(15,550)**	**(13,921)**	**(29,109)**
R&D costs capitalized during the period	13,843	13,031	23,556
R&D costs amortized during the period	(12,826)	(10,278)	(20,100)
French R&D tax credit	1,475	1,350	2,881
TOTAL R&D COSTS ACCOUNTED FOR DURING THE PERIOD	**(13,058)**	**(9,818)**	**(22,772)**

Note 6. Financing

Note 6.1. Financial debt

At July 31, 2016	Maturity at July 31					
(In thousands of euros)	2017	2018	2019	2020	2021 and beyond	Total
Syndicated loan	4,291	4,291	4,291	4,291	20,383	37,547
Other bank borrowings	2,253	267	121	2		2,643
Factoring of French R&D tax credit for 2014			1,991			1,991
Profit-sharing funds	159					159
Other long-term liabilities	86	313	94	65	129	687
TOTAL	**6,789**	**4,871**	**6,497**	**4,358**	**20,512**	**43,027**
CURRENT : 6,789		NON-CURRENT : 36,238				

At January 31, 2016	Maturity at January 31					
(In thousands of euros)	2017	2018	2019	2020	2021 and beyond	Total
Syndicated loan	3,777	3,777	3,777	3,777	17,940	33,048
Short-term revolving loan	8,000					8,000
Other bank borrowings	2,058		258			2,316
Factoring of French R&D tax credit for 2014				1,991		1,991
Profit-sharing funds	25	155				179
Repayable advances		272				272
Other long-term liabilities	108	129	328	65	129	759
TOTAL	**13,967**	**4,333**	**4,363**	**5,833**	**18,069**	**46,566**
CURRENT: 13,967		**NON-CURRENT: 32,597**				

Changes in the financial debt over 2016 first half are mostly related to the repayment of the revolving credit used for €8 million at January 31, 2016, and the financing of Mineset Inc. acquisition for €4.5 million.

All financial liabilities are denominated in Euros.

Note 6.2. Financial income and expenses

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Interest on borrowings	(507)	(165)	(552)
Interest income	3	15	30
Foreign exchange gains and losses	(574)	380	314
Other financial expenses	(501)	(248)	(742)
Financial result	**(1,579)**	**(18)**	**(950)**

Interest on borrowings are composed of interests paid on bank loans and costs related to hedging instruments related to the syndicated loan. The increase results from a higher syndicated loan debt as compared to 2015 first half.

During this half year, the Group used the same derivative instruments to manage its exposure to fluctuations in exchange rates than on previous years. At July 31, 2016 the market value of foreign currency derivatives is €-369 thousand. Its decrease in value results mainly from the strong appreciation of the Japanese yen during first half year.

Other financial expenses include the reevaluation of the 0% floor included in our syndicated loan (cost of €273 thousand versus a cost of €258 thousand in 2015).

Note 7. Income tax

Note 7.1. Income tax expense

The income tax recorded in the consolidated income statement is as follows:

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Current taxes	(2,155)	(1,411)	(3,254)
Deferred taxes	3,580	2,772	97
TOTAL	**1,425**	**1,361**	**(3,157)**

As explained in note 1.1, the Group activity is subject to important seasonal fluctuations that generate deferred tax assets at July 31, 2016.

Note 7.2. Deferred taxes

BREAKDOWN OF DEFERRED TAXES

(In thousands of euros)	July 31, 2016	July 31, 2015	January 31, 2016
Tax loss carryforwards	6,647	5,303	1,616
Temporary differences related to the treatment of maintenance	3,083	3,279	4,411
Provisions for employee benefit commitments	2,401	2,244	2,196
Others	(1,468)	231	(956)
NET DEFERRED TAX	**10,662**	**11,057**	**7,267**

Note 8. Subsequent events

Nothing to report.

3 Statutory auditors' review report on the 2016 half year financial information

PricewaterhouseCoopers Audit
63, rue de Villiers
92208 Neuilly-sur-Seine Cedex
S.A. au capital de € 2.510.460

Commissaire aux Comptes
Membre de la compagnie
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ERNST & YOUNG Audit
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92400 Courbevoie – Paris-La Défense 1
S.A.S à capital variable

Commissaire aux Comptes
Membre de la compagnie
régionale Versailles

This is a free translation into English of the Statutory Auditors' review report issued in French and it is provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

ESI Group

Period of February 1, 2016 to July 31, 2016

In accordance with our appointment as statutory auditors by the General Shareholders' Meeting, and in application of article L.451-1-2 III of the French monetary and financial code, we hereby report to you on:

- the review of the accompanying condensed half year consolidated financial statements of ESI Group SA, for the period from February 1, 2016 to July 31, 2016;
- the verification of the information contained in the half year management report.
-

These condensed half year consolidated financial statements were prepared under the responsibility of the Board of Directors. Our role is to express a conclusion on these financial statements, based on our review.

1. Conclusion on the financial statements

We conducted our review in accordance with professional standards applicable in France.
A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. These procedures are less in scope than those required for an audit conducted in accordance with professional standards applicable in France. Consequently, a review does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.
Based on our review, nothing has come to our attention that causes us to believe that the condensed half year consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34, the IFRS standard as adopted by the European Union applicable to interim financial information.

2. Specific verification

We have also verified the information presented in the half-year management report on the condensed half year consolidated financial statements that were subject to our review.
We have no matters to report with respect to its fair presentation and consistency with the condensed half year consolidated financial statements.

Neuilly-sur-Seine and Paris-La Défense, September 21, 2016

The Statutory Auditors

French original signed by

PricewaterhouseCoopers Audit
Thierry Charron

ERNST & YOUNG Audit
Frédéric Martineau

G.FC.16.038A

4 Declaration by the person responsible for the 2016 half year financial report

« I hereby declare that, to the best of my knowledge, the half year financial statements have been prepared in accordance with applicable accounting standards and that they give a fair view of the assets, financial position and results of the Company and all consolidated companies making up the Group., and that this Half year Activity Report includes a fair review of the important events which occurred during the first six months of the year, their impact on the half year financial statements and the main transactions between related parties, together with a description of the principal risks and uncertainties that they face in the remaining six months of the year. »

Paris, September 22, 2016

Alain de Rouvray
Chairman and Chief Executive Officer of ESI Group