



2016 Fourth Quarter Financial Report
&
December 2016 to February 2017 Activities Report

Highlights

- Conan Exiles sales have performed extremely well
 - It has sold more than 480.000 units the first 28 days after launch (net sales, after returns and chargebacks)
- The game is expected to reach its 12 month sales goal on PC of 487.000 units within the first 30 days after launch (goal as mentioned in the Q3 report)
- PR & Marketing activities were very successful, garnering millions of views on diverse channels and securing the game as the top seller on the Steam store for almost two weeks
- For the first time in modern Funcom history the direct project cost was covered in less than seven days and the game is now profitable and will continue to be so in foreseeable future.
- Direct project costs totaled around 4.5m USD for the launch of the game. These are considered to be those related to salaries, social security and equipment for the development, technology and marketing teams, external PR & Marketing expenses and other external consulting or licensing expenses directly attributable to the project.
- This huge initial success lays a very solid ground foundation for continuous success in 2017 and beyond.
- Additional investment in the 5 to 10m USD range will happen throughout 2017 and early 2018, to deliver technical and content updates, PR & marketing activities and campaigns, as well as support for Xbox One and Playstation 4 launches
- The Company considers Conan Exiles to have a very high lifetime revenue potential on all three planned platforms, as games in this genre typically have long tails of unit sales
- Conan Exiles is the third game under the new strategy, and so far all three have reached all internal goals. The company will continue to work under the new strategy of making smaller experimental projects like The Park and Hide & Shriek, as well as larger projects like Conan Exiles.
- Q4 financials are in line with internal forecasts and reflect the investment into Conan Exiles
- The Secret World will be relaunched during the first half of 2017, with several major changes to increase user acquisition and retention. The business model will also be changed with the story content to be made free.
- Relaunch activities will begin in late March.

Game activities in the period

While The Secret World team has been mostly focused on the aforementioned relaunch, the following was still added to the game in the recent months:

- Halloween Samhain Rider and Christmas Krampusnacht Events and respective store Bundle Sales
- A Limited Time Challenge System
- Thanksgiving Store Sale
- Hide and Shriek and NITE Team 4 tie in items

For Anarchy Online, the Item Store was revamped, a Winter celebration and a Christmas sale event were launched, several bugs and exploits were fixed and the game was released on Steam. No further significant work is expected to be done on this project going forward.

For Age of Conan, a Thanksgiving and a Christmas sale events were launched, new rewards were added to the Raid finder and the tie-in items with Conan Exiles were added. No further significant work is expected to be done on this project going forward.

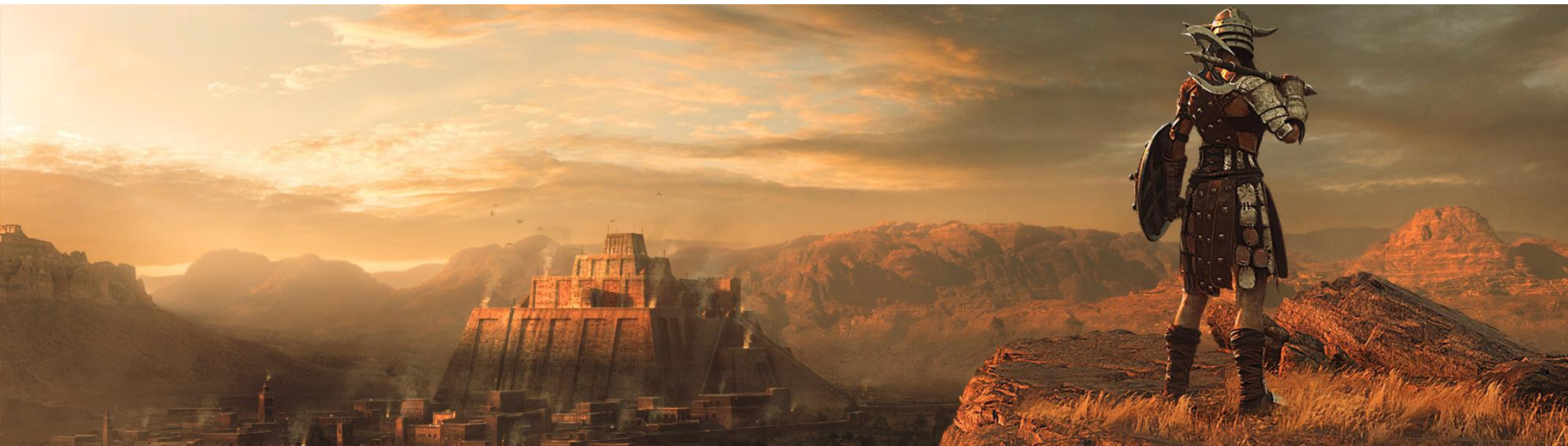
Hide & Shriek was announced on 4 October and released successfully on Steam on 25 October

- Similar to how *The Park* was a project to bring the Funcom Oslo team up to speed with Unreal Engine 4 and shorter development cycles, *Hide and Shriek* had the same objectives but for the team in Funcom Inc. in North Carolina
- In addition, this game allowed Funcom to obtain experience in localizing a game in 11 languages and bring a game to the attention of Streamers/Youtubers,



Game activities in the period

- Conan Exiles launched on 31 January 2017 in Early Access on Steam
- The business model in Conan Exiles is buy to play (B2P). You pay once and can play forever. We will evaluate offering paid Downloadable content (DLC) only after the game has exited Early Access and launched on all platforms.
- The game is planned to continue in Early Access for around 12 months after its initial Early Access launch on PC. Early Access is a concept provided by Steam where developers can launch fully playable games, but with less content than a full game. Bugs and technical issues must be expected as players under this concept develop the game together with the developers by providing valuable feedback on features, content and bugs.
- As with many other Early Access games, the company acknowledges that the game has technical issues and bugs in addition to the initial capacity problem we encountered that we are still working on mitigating. This is affecting player ratings negatively which currently stands at 68% positive on Steam user rating.
- The team is working extensively to fix these issues and the number one priority for the company, above all else, is to fix these issues and prepare the game for future updates.
- So far the team has delivered 18 larger and smaller updates to the game which has garnered praise from the players in the Early Access community. The speed of updates will be reduced in the coming weeks as the team enters into a more sustainable production rhythm.
- Games in this genre typically show a very long tail of sales with, for example, Rust launching in December 2013, selling 1 million units in the first 2 months and continuing to sell very well now, after more than 3 years (5+ million)
- Sales are driven by game updates, discounts and large events or platform launches
- In addition to the figures presented in the previous chart, the games that have launched on consoles have sold a significant number of units.
 - Ark sold a reported 1m units in the first week, 2m units in the first 6 months, on Xbox One. Sold 2m units on PS4 in a bit over 2 months
- Altogether this indicates that the potential number of sales in the first 2 to 3 years after the Early Access release on PC is very high



Financials

FINANCIAL SUMMARY

- The Live Games – *The Secret World*®, *Anarchy Online*®* and *Age of Conan*™ – were the major contributors to the revenues.
- Revenues in 4Q16 amount to USD 1,671 thousand compared to USD 2,617 thousand in 4Q15, following a gradual and expected decrease in the sales from the current Live Games.
- The company continued its cost-saving efforts in 4Q16 and realized operating cost savings of USD 793 thousand compared to 4Q15.
- Earnings before Interest, Tax, Depreciation and Amortization (EBITDA) for 4Q16 amount to USD -143 thousand compared to USD +10 thousand in 4Q15.
- Earnings before Interest and Tax (EBIT) for 4Q16 amount to USD -580 thousand compared to USD -747 thousand in 4Q15.
- The result for the period is a loss amounting to USD -936 thousand, compared to a loss amounting to USD -2,251 thousand reported for 4Q15.
- The total Equity of the Company decreased slightly from USD 3,278 thousand at the end of 3Q16 to USD 2,843 thousand at the end of 4Q16.
- The cash position decreased from USD 5,208 thousand at the end of 3Q16 to USD 3,848 thousand at the end of 4Q16 as a result of the investment made into *Conan Exiles* and *The Secret World* relaunch.

UPDATE ON THE FINANCIAL INSTRUMENTS

CONVERTIBLE BOND

- Outstanding principal: 6,899,194 bonds with a face value of USD 1 each, with a carrying amount of USD 6,830 thousand as of 31 December 2016
- Maturity date: 31 December 2018
- Conversion price: USD 0.1036 per share
- Interest rate: 3.5% per annum; accrued interest from 20 July 2016 onwards is due at maturity
- On 9 December 2016, USD 180 thousand (plus accrued interest) of the convertible bond was converted into 1,761,010 new shares in Funcom N.V. at a price of USD 0.1036 per share.
- Since this transaction, 6,899,194 bonds are outstanding under the same conditions.

CONVERTIBLE LOAN

- Funcom received notice to convert the outstanding USD 250 thousand convertible loan with maturity date 31 December 2016 into shares at the price of USD 0.1036 per share. The transaction was completed on 9 January 2017 with the issuance of 2,413,127 new shares in Funcom N.V.
- Since this transaction, no balance remains under the Convertible Loan, and the only remaining financial liability of the Company relates to the Convertible Bond mentioned here above.

WARRANTS

- On 19 January 2017 and on 3 February 2017, respectively 500,000 and 1,065,000 warrants were exercised giving rights to subscribe for the same amount of share at a price of USD 0.10 per share. In consequence, a total of 1,565,000 new shares in Funcom N.V. were issued.
- After these transactions, there is no outstanding warrant.

Strategy

THE FUNCOM STRATEGY

- The Company strategy is focused on different types of products and production cycles. It consists of:
 - Developing innovative games, focused on trying new concepts, experimenting with new technology and platforms and utilizing our IPs, while keeping the investment level low;
 - Developing larger games, focused on genres or game types where we can create products of higher production value than the competition, using our own or 3rd party IPs and drawing from the innovation and experimentation of the smaller products to lower the overall risk;
 - Upgrading the *Dreamworld Technology* to integrate with third party technologies;
 - Leveraging and growing the internal Intellectual Properties such as *Anarchy Online*, *The Longest Journey* and *The Secret World* for both internal and 3rd party licensing for both games and other non-interactive entertainment.
- As part of this strategy, market segments and platforms will be constantly evaluated as the trends in the gaming industry change very quickly and new opportunities are emerging such as “eSports”, “VR”, “AR”, among others.
- The product development and release plan for this strategy is a minimum of two games released per year, of which one is a larger game to be in development at all times per development studio.
- Additionally, the company will keep developing and supporting the existing MMORPGs as they are an important source of revenue and drive the internal IPs.
- The strategy is meant to reduce the overall risk exposure of the company, control costs through careful budgeting and increase the financial stability by having more revenue sources.
- The Oslo studio has fully switched to this strategy and the North Carolina studio will switch after the last large updates to *The Secret World* are released.

- The first game to be released under this new strategy was *The Park*, released on 27 October 2015. The first “larger” game is *Conan Exiles*, released in “Early Access” during January 2017.
- The above mentioned statements and objectives are forward looking and are subject to change along with industry trends. The Company strongly encourages all investors, analysts, press and others to investigate and analyze the gaming industry. The industry has drastically changed over the past few years. It is the Company’s clear goal to align itself with the market, leverage its technology and know-how and adapt its portfolio of products to address the current as well as future needs.

TECHNOLOGY

- The *Dreamworld Technology* is being upgraded to take advantage of the strengths of 3rd party engines, integrating these technologies with the existing modules and systems of the *Dreamworld Technology*.
- The Unreal Engine 4 is the first game engine being integrated with *Dreamworld Technology*. It allows content creators to use the advance toolchain of that engine while keeping the *Dreamworld Technology* unique systems such as multiplayer backend, deployment systems, workflow and productivity pipelines.

The way ahead

THE SECRET WORLD

The Secret World will be relaunched during the first half of 2017. The goal of the relaunch is to broaden the appeal of the game through:

- Redesigned new player experience
- Major improvements to gameplay including combat.
- Introduction of new retention systems such as daily rewards.
- Adjustments to the business model, including allowing access to the story content for free.

Relaunch activities will begin in late March.

- This relaunch has the potential to have a significant impact in the game and company's revenues
- As with any business model adjustments there is a significant risk attached to this change. For more information regarding risk see point 27 in the 2015 Annual report

CONAN EXILES

Due to the rapid success of Conan Exiles the Company has evaluated its investment level into the project and decided to increase it, as we believe this to represent the highest ROI for the next 12-24 months

- Some milestones have been moved as part of the additional investment plan, to maximize the quality and thus the revenue generated by those activities
- The additional investment will be in the 5 to 10m USD range throughout 2017 and early 2018, to deliver technical and content updates, PR & marketing activities and campaigns, as well as support for Xbox One and Playstation 4 launches
- As part of the evaluation to invest more in the console version, the fact that competition in the genre on both Xbox and PS4 is limited, has played a major part. So far only ARK and 7 Days to Die have been released on those consoles

Game development will revolve around 3 main tracks:

- Regular Patching, which will happen every one to two weeks
 - Performance and Stability updates
 - Bug Fixing to continuously polish the game experience
 - "Quick Win" small features and additions to the game to respond to the requests from the community

- Game Updates, which will happen less frequently but will contain more significant additions to the game
 - Examples of content are the Trebuchet/Siege weapons, Dye system, mounts, etc.
 - The current plan is for 4 - 6 Game Updates during the Early Access Period
 - 2-3 Game Updates during H1 2017
 - 2-3 Game Updates during H2 2017
 - 1 Game Update during Q1 2018
- Major Releases, for new platform launches and significant content updates
 - Xbox One Game Preview and an additional Biome during Q3 2017
 - Xbox Game Preview is similar to the Early Access program but on the Xbox platform
 - A "biome" is an addition to the existing game map with a different environment, adding new terrain, monsters, equipment, avatars, etc.
 - Full Release on PC, Xbox, and PS4 in Q1 2018

Future potential of the game is dependent of many factors, player and media reception of the game and the company are both factors investors should consider together with the potential the title has in its genre, together with its initial success and future full launch and launch on consoles. For more information regarding risk factors please see point 27 in the 2015 annual report

NEW PROJECTS

Two new projects are in early concept stages and will enter pre-production at the earliest during the second half of 2017:

- In Funcom Oslo, a new game concept using the "Conan the Barbarian" IP, whose pre-production has been delayed due to success of Conan Exiles
- In Funcom North Carolina, a new project that has been in early concepting stage and will continue after The Secret World relaunch

Final notes

MISCELLANEOUS

- At the extraordinary meeting on 5 October 2016, Mr. Michel Henri Georges Cassius resigned from his position of Chairman of the Board of Supervisory Directors. Mr. Ole Gladhaug was appointed as the Chairman of the Supervisory Board; Mr. Fredrik Malmberg, Mr. Egil Kvannli and Mr. Magnus Slåttekjær Grøneng were appointed as new Supervisory Directors.
- LEGO® *Minifigures Online*'s license agreement with LEGO expired on 1st October 2016 and the game's operations were terminated

Risk factors

- For information regarding risk factors for the Company and its games, please refer to note 27 in the 2015 Annual Report (http://www.funcom.com/investors/funcom_n.v._publishes_its_2015_annual_financial_statements).
- For evaluations of the risks related to Funcom games, Funcom encourages investors to seek information about the industry in general and Funcom in specific from analyst reports, industry reports, game reviews, etc.
- Several different financial scenarios should be evaluated when analyzing the potential of any existing or future games. The financial performance of new games and refined business models is uncertain.

Outlook

- The medium and long term financial performance of the Company looks very positive. A number of factors influence it, especially the performance of Conan Exiles on PC, Xbox and PS4 and the continued revenues of the older MMO games.
- The trend of slowly declining revenues on the current Live Game portfolio is expected to continue as in previous quarters due to the ageing of the games. The relaunch of The Secret World might temporarily have a positive impact on this trend short term. The Company will continue to support the current Live Games as long as they continue to contribute positively to the Company's results.
- Based on its current revenues, especially the revenue already generated by the new game *Conan Exiles*, its cost projections, and on the financial instruments at the disposal of the Company including but not restricted to financing and equity issues, the Company has the ability to fund its operations for the next twelve months after the end of 4Q16.

Badhoevedorp, The Netherlands, 27 February 2017

The Management Board of Funcom N.V.

- This report is also available at <http://www.newsweb.no>
Investors are encouraged to seek information regarding the Company and the industry.
- This report contains forward-looking statements. These statements are based on current estimates and projections of Funcom's management and currently available information. They are not guarantees of future performance, involve certain risks and uncertainties that are difficult to predict and are based upon assumptions as to future events that may not prove to be accurate. Many factors could cause the actual results, performance or achievements of Funcom to be materially different from those that may be expressed or implied by such statements. Such factors include inter alia those discussed in the Funcom's Annual Report 2015 note 27.
- For more information about Funcom, its games and its organization, please see www.funcom.com

* "Funcom", "The Secret World", "Anarchy Online", "The Park" and "Dreamworld Technology" are registered trademarks of Funcom Oslo AS.

FUNCOM N.V. - FOURTH QUARTER FINANCIALS OF 2016
PRELIMINARY, NOT AUDITED, FIGURES

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

| (Figures in TUSD) | Fourth Quarter | | Accumulated | | Full Year |
|--|----------------|---------------|---------------|---------------|---------------|
| | 2016 | 2015 | 2016 | 2015 | 2015 |
| Revenue | 1,671 | 2,617 | 7,165 | 10,238 | 10,238 |
| Operating expenses | -1,814 | -2,607 | -7,360 | -9,845 | -9,845 |
| Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA) | -143 | 10 | -194 | 393 | 393 |
| Depreciation, amortization and impairment charges | -437 | -757 | -1,811 | -6,571 | -6,571 |
| Total operating expenses | -2,251 | -3,364 | -9,170 | -16,417 | -16,417 |
| Operating result ("EBIT") from continuing operations | -580 | -747 | -2,005 | -6,179 | -6,179 |
| Share of result from equity-accounted entities | | | | -173 | -173 |
| Net financial items | -354 | -1,546 | -817 | -478 | -478 |
| Profit (loss) before income taxes from continuing operations | -934 | -2,293 | -2,822 | -6,829 | -6,829 |
| Income taxes | -2 | 42 | -3 | 40 | 40 |
| Profit (loss) for the period | -936 | -2,251 | -2,825 | -6,789 | -6,789 |
| Attributable to shareholders of Funcom N.V. | -936 | -2,251 | -2,825 | -6,789 | -6,789 |
| Earnings per share basic (USD) | 0.00 | -0.02 | -0.02 | -0.07 | -0.07 |
| Earnings per share fully diluted (USD) | 0.00 | -0.02 | -0.02 | -0.07 | -0.07 |

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | | | | | |
|--|-------------|---------------|---------------|---------------|---------------|
| Profit (loss) for the period | -936 | -2,251 | -2,825 | -6,789 | -6,789 |
| Foreign exchange translation difference | -52 | 1,239 | -357 | -1,415 | -1,415 |
| Total comprehensive income for the period | -988 | -1,012 | -3,182 | -8,204 | -8,204 |

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

| (Figures in TUSD) | 31 December | | 31 Dec. |
|-------------------------------------|---------------|---------------|---------------|
| | 2016 | 2015 | 2015 |
| ASSETS | | | |
| <u>Non-current assets</u> | | | |
| Intangible assets | 6,617 | 4,394 | 4,394 |
| Tangible fixed assets | 4 | 100 | 100 |
| Financial investments | 19 | 65 | 65 |
| Total non-current assets | 6,640 | 4,559 | 4,559 |
| <u>Current assets</u> | | | |
| Trade receivables | 628 | 1,443 | 1,443 |
| Prepayments and other assets | 466 | 506 | 506 |
| Cash and cash equivalents | 3,848 | 616 | 616 |
| Total current assets | 4,942 | 2,565 | 2,565 |
| Total assets | 11,582 | 7,124 | 7,124 |
| EQUITY AND LIABILITIES | | | |
| <u>Equity</u> | | | |
| Share capital | 11,808 | 4,802 | 4,802 |
| Reserves | 165,328 | 157,105 | 157,105 |
| Retained earnings | -174,293 | -171,468 | -171,468 |
| Total equity | 2,843 | -9,561 | -9,561 |
| <u>Liabilities</u> | | | |
| Deferred tax liabilities | 1 | 25 | 25 |
| Long-term liabilities | 7,019 | 3,434 | 3,434 |
| Deferred revenue | 605 | 1,037 | 1,037 |
| Short-term loans and borrowings | 48 | 10,150 | 10,150 |
| Other short term liabilities | 1,065 | 2,040 | 2,040 |
| Total liabilities | 8,739 | 16,685 | 16,685 |
| Total equity and liabilities | 11,582 | 7,124 | 7,124 |

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

| (Figures in TUSD) | Fourth Quarter | | Period ended 31 December | | Full Year |
|---|----------------|--------------|--------------------------|---------------|---------------|
| | 2016 | 2015 | 2016 | 2015 | 2015 |
| Cash flow from operating activities | | | | | |
| Profit (loss) before income tax | 647 | -2,293 | -2,822 | -6,829 | -6,829 |
| Adjustments for: | | | | | |
| Depreciation, amortization and impairment | -1,144 | 757 | 1,811 | 6,571 | 6,571 |
| Share-based payments | 121 | 112 | 346 | 814 | 814 |
| Share of result from equity-accounted entities | | | | 173 | 173 |
| Effect of exchange rate fluctuations | 516 | 4,119 | 365 | 442 | 442 |
| Changes in working capital | 97 | 248 | 1,056 | 466 | 466 |
| Net cash from operating activities | 237 | 2,943 | 755 | 1,637 | 1,637 |
| Cash flow from investing activities | | | | | |
| Purchase of equipment and investment in intangible assets | 187 | -756 | -4,304 | -3,412 | -3,412 |
| Investment in/loan to (from) equity-accounted entities | | | | 11 | 11 |
| Net cash from investing activities | 187 | -756 | -4,304 | -3,401 | -3,401 |
| Cash flow from financing activities | | | | | |
| Net proceeds from issue of share capital | | | 7,122 | 411 | 411 |
| Proceeds / repayments from (of) borrowings and leases | | | | -23 | -23 |
| Net cash from financing activities | | | 7,122 | 388 | 388 |
| Change in cash and cash equivalents | 424 | 2,187 | 3,573 | -1,376 | -1,376 |
| Cash and cash equivalents, beginning of period | 5,208 | 1,106 | 616 | 3,705 | 3,705 |
| Effect of exchange rate fluctuations | -1,784 | -2,678 | -341 | -1,714 | -1,714 |
| Cash and cash equivalents, end of period | 3,848 | 616 | 3,849 | 616 | 616 |

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| (Figures in TUSD) | 31 December | | Full Year |
|---|---------------|---------------|---------------|
| | 2016 | 2015 | 2015 |
| Opening balance | -9,561 | -2,756 | -2,756 |
| Total comprehensive income for the period | -3,182 | -8,204 | -8,204 |
| Equity issues | 14,609 | 411 | 411 |
| Granting of warrants | | 173 | 173 |
| Exercise of warrants | 157 | | |
| Equity portion of the new convertible loan | 394 | | |
| Equity portion of the additional convertible bond | 82 | | |
| Share-based payments | 346 | 814 | 814 |
| Closing balance | 2,843 | -9,561 | -9,561 |

NOTES TO THE INTERIM REPORT

1 Corporate information

Funcom N.V. is a limited company registered in The Netherlands, and the shares are publicly traded on the Oslo Stock exchange under the ticker "FUNCOM". The principal activity of the Company is to develop, market and carry on business in computer games in the broadest sense. The unaudited interim condensed consolidated financial statements for the Company for the twelve months ended 31 December 2016 were approved for issue by the Supervisory Board on 27 February 2017.

2 Basis for preparation and selected significant accounting policies

The financial result of the Company in 4Q16 reports slightly declining revenues from existing games and decreased operating costs compared to 4Q15 due to internal cost-saving measures. There were no pervasive or material changes in 4Q16 that could negatively affect the management's assumptions behind the forecasted financial performance of the Company. The funding of the operations for a period of at least one year after the date of this quarterly report is realistic and achievable. Therefore, management is of the opinion that the going concern assumption is justified and consequently the unaudited interim condensed consolidated financial statements of the Company for the twelve months ended 31 December 2016 have been prepared on a going concern basis. Notwithstanding the above, the Management Board of the Company emphasizes that the above assessments indicate the existence of material uncertainty concerning the performance of the games and the outcome of the current corporate developments in the Group. Therefore, the actual performance of the Company may deviate significantly from the projections.

The unaudited interim condensed consolidated financial statements of the Company for the twelve months ended 31 December 2016 have been prepared in accordance with IAS 34. The latter means that these interim financial statements do not include all information and disclosures required in annual financial statements but only selected significant information. The principles applied are consistent with those used in the 2015 Annual Report.

As of 1 January 2016, the Group has adopted the mandatory revised standards, amendments to existing standards and interpretations as adopted by the EU, applicable for this quarter. Their adoption has not had any significant impact on the amounts reported in this interim report but may affect the accounting for future transactions or arrangements. Management has not yet completed the evaluation of the impact on the financial statements of standards issued but which have an adoption date on 1 January 2017 or later.

All amounts are in USD thousand unless stated otherwise. There may be some minor rounding differences or the total may deviate from the total of the individual amounts. This is due to the rounding to whole thousands of individual amounts.

2.1 Basis of consolidation

The Company's Interim consolidated financial statements comprise of Funcom N.V. and companies in which Funcom N.V. has a controlling interest.

2.2 Intangible assets

Intangible assets are recognized in the balance sheet if it can be proven that there are probable future economic benefits that can be attributed to the assets that are owned by the Company, and the assets' cost price can be reliably estimated. Intangible assets are initially recognized at their cost price and subsequently measured using the cost method (i.e.

historical cost less accumulated amortization and accumulated impairment losses). A review to assess whether there are indicators of impairment is undertaken at the end of each reporting period. In addition, intangible assets not yet available for use are tested for impairment annually.

2.3 Equity

Transaction costs relating to equity transactions are recognized directly in equity after deducting tax.

2.4 Deferred revenues

Revenues from subscriptions are recognized over the subscription period that is from the date of subscription purchase until subscription end, normally 1 – 12 months.

In-game items are items that can be purchased on-line from in-game stores or are awarded as incentive or compensation. Revenue from sales of in-game items is recognized at the time of sale.

Revenues from the sales of game software, whether delivered via packaged goods (boxes) or via the Internet (game download) are recognized on a straight-line basis over the estimated customer life. The company enters into multiple-element revenue arrangements where it provides combinations of game software and subscription or subscription and in-game items. The Company accounts for revenues from each item separately following the revenue recognition policies above. Up-front payments for subscriptions and other up-front revenues are recognized in the statement of financial position as a liability.

3 Operating revenues

The revenues mainly consist of sales of game software, subscriptions, in-game items and royalties.

4 Operating expenses

Personnel cost, marketing, office rent and games operating cost are main elements of the operating expenses.

5 Depreciation, amortization and impairment charges

The Company amortizes investment in the development of technology and game assets on a systematic basis over their useful life, which normally does not exceed five years. The company applies the diminishing balance amortization method that reflects the pattern of consumption of the future economic benefits. If that pattern cannot be determined reliably, the company uses the straight-line method.

An adjustment was recorded on the year-to-date figures as of 30 September 2016 by decreasing the Depreciation, amortization and impairment charges with an amount of USD 1,581 thousand, and by increasing the Foreign exchange translation difference with the same amount. This adjustment has no impact on the Total comprehensive income for the period nor on the statement of financial position. The unaudited interim condensed consolidated financial statements for the Company for the twelve months ended 31 December 2016 are reported inclusive of the above mentioned adjustment.

6 Net financial items

Net financial items mainly consist of interest earned, exchange rate differences, and interest incurred on loans.

7 Taxes

In accordance with IAS 12, it is Funcom's assessment that no deferred tax asset can be recognized in the consolidated statement of financial position for the available tax losses carried forward. The accumulated unrecognized tax losses are primarily denominated in United States Dollars.

8 Financial investments

Financial investments consist of long-term receivables.

9 Liabilities

Long-term liabilities consist of USD 6,830 thousand convertible bond, USD 50 thousand rental deposits for the sublet of office space, and USD 139 thousand rental incentives.

On 20 July 2016, the bondholders agreed to modify the convertible bond by postponing the maturity date from 15 December 2016 to 31 December 2018, by decreasing the fixed interest rate from 5% to 3.5% per annum, by increasing the number of bonds from 62 to 6,200,000, by decreasing the face value of each bond from USD 100 thousand each to USD 1 each, and by decreasing the conversion price from USD 0.24 per share to USD 0.10 per share in accordance with the convertible bond agreement.

On 9 December 2016, USD 180,000 (plus accrued interest) of the convertible bond was converted into 1,761,010 new shares.

As of 31 December 2016, the bonds have a carrying amount of USD 6,830 thousand and an actual balance due of USD 6,899 thousand.

Short-term loans and borrowings consist of USD 48 thousand rental incentives. .

On 20 July 2016, the maturity date of the convertible loan was advanced from 30 June 2019 to 31 December 2016, and the related conversion price was decreased from USD 0.18 per share to USD 0.10 per share in accordance with the convertible loan agreement. The interest rate of 6% remained the same. Funcom received notice to convert the outstanding USD 250 thousand convertible loan with maturity date 31 December 2016 into shares at the price of USD 0.1036 per share. The transaction was completed on 9 January 2017 with the issuance of 2,413,127 new shares in Funcom N.V.

The carrying value of the interest-bearing debt at the end of 4Q16 amounts to approximately USD 6,830 thousand.

10 Cash flows

A significant part of Funcom's cash and cash equivalents are denominated in Norwegian kroner, in United States Dollar and in Euro. The Company's NOK, USD and EUR cash holdings are a natural hedge against the expectedly large proportion of future operating expenses arising in NOK, USD and EUR.

11 Average number of shares

| | Fourth quarter | | Twelve months | |
|--------------------------|----------------|--------|---------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Average number of shares | 249,282 | 92,140 | 180,291 | 91,615 |

12 Other comprehensive income

In accordance with IAS 21, the Company reported in 4Q16 under the 'Other comprehensive income' a foreign exchange loss amounting to USD 52 thousand mainly related to the reconciliation of intercompany balances in foreign currencies and to the translation of foreign operations into the reporting currency.

13 Equity

The equity of the Company decreased from USD 3,278 thousand at the end of 3Q16 to USD 2,843 thousand at the end of 4Q16. It is considered that the revenue potential of the current and future games as well as the continuation of the cost-saving measures that started in 4Q12 will improve the profitability of the Company and will lead to a future increase of the equity position. The company also evaluates various strategic options that could also lead to an increase of equity.

14 Segments

IFRS 8 requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess its performance. The reportable operating segments of the group are defined as:

- Online games – such as *Anarchy Online*, *The Secret World* and *Age of Conan*
- Offline games – such as *The Park*, *Dreamfall* and *The Longest Journey*

Segment information

| | Revenue from external customers | | Segment profit (loss) * | |
|--|---------------------------------|---------------|-------------------------|---------------|
| | January - December | | January - December | |
| | 2016 | 2015 | 2016 | 2015 |
| Online games | 5,796 | 8,979 | 2,060 | 3,571 |
| Offline games | 943 | 797 | 553 | 102 |
| Other activities | 426 | 462 | -37 | -49 |
| Total | 7,165 | 10,238 | 2,577 | 3,624 |
| General and administrative expenses | | | -2,771 | -3,229 |
| Depreciation, amortization and impairment charges | | | -1,811 | -6,571 |
| Share of result from equity-accounted entities | | | | -173 |
| Net financial items | | | -817 | -478 |
| Profit (loss) before tax (from continuing operations) | | | -2,822 | -6,829 |

| | Revenue from external customers | | Segment profit (loss) * | |
|--|---------------------------------|--------------|-------------------------|---------------|
| | October - December | | October - December | |
| | 2016 | 2015 | 2016 | 2015 |
| Online games | 1,338 | 2,063 | 328 | 540 |
| Offline games | 293 | 439 | 179 | 33 |
| Other activities | 40 | 115 | -5 | -7 |
| Total | 1,671 | 2,617 | 503 | 566 |
| General and administrative expenses | | | -644 | -554 |
| Depreciation, amortization and impairment charges | | | -438 | -757 |
| Share of result from equity-accounted entities | | | | |
| Net financial items | | | -354 | -1,546 |
| Profit (loss) before tax (from continuing operations) | | | -933 | -2,292 |

*) Segment profit (loss) is measured as revenue earned less personnel costs and other operating costs. General and administrative costs, depreciation, amortization, impairment charges, financial items and income tax are not allocated to the segments.

*) Other activities refer to Funcom Games Canada subleasing activities. Segment profit (loss) is measured as revenue earned less original rental expenses.

| | Online games | Offline games |
|---------------------------------------|--------------|---------------|
| Segment assets as at 31 December 2015 | 4,324 | |
| Segment assets as at 31 December 2016 | 6,252 | |

Segment assets only include the book value of the games. No other assets are allocated to the segments.

15 Subsequent events

On 31 January 2017, the game *Conan Exiles* was released in Early Access on the Steam platform. More than 320,000 units were sold worldwide within a week. All of the costs directly related to this game have been recouped and the project is operationally profitable.

The development team will continue to work on *Conan Exiles* and provide the necessary technical support and additional content as part of the Early Access plan, in order to ensure a positive reception of the game before executing a full launch on PC. The Company believes this to be a clear sign that the previously mentioned goal of entering the Top 10 of multiplayer open world survival games on Steam one year after launch will be achieved.

On 19 January 2017 and on 3 February 2017, respectively 500,000 and 1,065,000 warrants were exercised giving rights to subscribe for the same amount of share at a price of USD 0.10 per share. In consequence, a total of 1,565,000 new shares in Funcom N.V. were issued. After these transactions, there is no outstanding warrant.