Lenovo Group Limited 聯想集團有限公司

*(Incorporated in Hong Kong with limited liability)*

**(Stock Code: 992)**

# FY2016/17 FIRST QUARTER RESULTS ANNOUNCEMENT

## QUARTERLY RESULTS

The board of directors (the "Board") of Lenovo Group Limited (the "Company") announces the unaudited results of the Company and its subsidiaries (the "Group") for the three months ended June 30, 2016 together with comparative figures for the corresponding period of last year, as follows:

### FINANCIAL HIGHLIGHTS

- **Group revenue of US$10.1B, down 6% YTY, down 4% YTY excluding currency impact**
- **Group profit before taxation of US$206M and Group profit attributable to equity holders of the Company of US$173M**
- **Group PTI before non-cash M&A-related accounting charges was US$281M, up 97% YTY (non-cash M&A-related accounting charges of US$75M comprise mainly intangible asset amortization and imputed interest expense of promissory notes)**
- **Group net income before non-cash M&A-related accounting charges was US$248M, up 27% YTY**

| | **3 months ended June 30, 2016 (unaudited)** ***US$'million*** | **3 months ended June 30, 2015 (unaudited)** ***US$'million*** | **Year-on-year change** |
|---|---|---|---|
| Revenue | 10,056 | 10,716 | (6)% |
| Gross profit | 1,534 | 1,647 | (7)% |
| Gross profit margin | 15.3% | 15.4% | (0.1) pts |
| Operating expenses | (1,289) | (1,551) | (17)% |
| Operating profit | 245 | 96 | 157% |
| Other non-operating expenses - net | (39) | (44) | (9)% |
| Profit before taxation | 206 | 52 | 297% |
| Profit for the period | 168 | 102 | 65% |
| Profit attributable to equity holders of the Company | 173 | 105 | 64% |
| Earnings per share attributable to equity holders of the Company | | | |
| Basic | US 1.57 cents | US 0.95 cents | US 0.62 cents |
| Diluted | US 1.56 cents | US 0.94 cents | US 0.62 cents |

## BUSINESS REVIEW AND OUTLOOK

### Business Review

During the three months ended June 30, 2016, the slow macro environment and uncertainties in global economy continued to affect the demand in the PC and tablet markets, as well as the smartphone market. Nevertheless, the PC market performed slightly better than expected due to stronger performance in mature markets.

Amidst these market challenges, Lenovo managed to deliver profit growth from its businesses, driven by efficiency improvements resulting from its previous decisive actions to realign the business. For the three months ended June 30, 2016, the Group's consolidated revenue decreased by 6 percent year-on-year to US$10,056 million. Excluding currency impact, the revenue decrease would be 4 percent compared to the same quarter last year. Revenue of the Group's PC and Smart Device business was US$6,992 million, representing a year-on-year decline of 7 percent, or 6 percent decline excluding currency impact. Revenue of the Mobile business decreased 6 percent year-on-year to US$1,706 million, or 1 percent decline excluding currency impact. Revenue of Data Center business increased 1 percent year-on-year to US$1,086 million, or increased 4 percent excluding currency impact. Meanwhile, revenue of other goods and services was US$272 million.

The Group's gross profit for the three months ended June 30, 2016 was US$1,534 million, a decrease of 7 percent year-on-year, while gross margin decreased 0.1 percentage point year-on-year to 15.3 percent largely due to the revenue decline. Operating expenses reduced by 17 percent year-on-year to US$1,289 million, and the expense-to-revenue ratio was 12.8 percent. Decline of expense-to-revenue ratio was mainly attributable to the business realignment actions that led to better expense control, despite incurring additional spending in branding and promotion to prepare for new product launches, especially in smartphone, and gain on monetizing certain non-core assets. The Group's profit before taxation before non-cash M&A related accounting charges was US$281 million, an increase of 97 percent year-on-year. The Group's net income before non-cash M&A related accounting charges was US$248 million, an increase of 27 percent year-on-year. The non-cash M&A related accounting charges included intangible asset amortization, imputed interest expense of the three-year promissory note issued as part of the transaction to acquire Motorola, and others. The Group's profit before taxation was US$206 million, up 297 percent year-on-year. The Group's net income was US$173 million, up 64 percent year-on-year.

### Performance of Product Business Groups

During the three months ended June 30, 2016, Lenovo continued to build a more balanced product portfolio to drive growth. This is the first report under the new organization structure the Group announced in early 2016, and the like-for-like comparison is on a pro-forma basis. For details of the organization structure changes, please refer to the related release of the Group.

### PC and Smart Device Business Group (PCSD)

During the period under review, while the global PC industry continued to decline due to macroeconomic forces and currency fluctuations, the PC market performed slightly better than expected due to stronger performance in mature markets. Despite the market challenges, the Group continued to outperform the PC market through solid execution of its strategy and further solidified its number one position. The Group's global PC unit shipments declined 2 percent year-on-year to 13.2 million, against market decline of 4 percent. Lenovo's market share continued to increase. Its worldwide PC market share was 21.1 percent for fiscal quarter one, an increase of 0.4 percentage point year-on-year, according to preliminary industry estimates.

The Group's commercial PC unit shipments increased 1 percent year-on-year, largely in line with the market for the period under review. Lenovo's market share in the worldwide commercial PC market has decreased by 0.1 percentage point year-on-year to 21.8 percent. The Group's consumer PC unit shipments declined by 7 percent year-on-year, against the market decline of 10 percent year-on-year during the period under review. Its latest market share for fiscal quarter one reached a record high market share at 20.2 percent, an increase of 0.8 percentage point year-on-year, according to preliminary industry estimates.

The Group's tablet shipments also performed well during the period under review. Shipments increased 3 percent year-on-year to 2.5 million against a market decline of 11 percent. As a result, its market share was up 0.9 percentage point year-on-year to hit 6.5 percent, according to the preliminary industry estimates.

To capture the potential high growth opportunities of smart devices, the Group has announced at Tech World in June its innovative P-HAB2 Pro which is the world's first augmented reality (AR) capable smart device. The device demonstrates the Group's strong R&D capability with its comprehensive camera and motion sensing technology. This innovative product will be available for sales in the fiscal quarter two under the tentative plan.

For the three months ended June 30, 2016, revenue of the Group's PCSD business was US$6,992 million, representing approximately 69 percent of the Group's total revenue, and a year-on-year decline of 7 percent, or 6 percent decline excluding currency impact. The business group recorded a pre-tax profit of US$370 million, up 2 percent year-on-year. This is the first time in the last several quarters that the business group showed a profit growth. Pre-tax profit margin was 5.3 percent, up 0.5 percentage point year-on-year, thanks to efficiency improvements and the profitability improvement in its business, especially in Americas.

**Mobile Business Group (MBG)**

During the period under review, the Group's mobile business slightly improved its momentum from the previous quarter and improved its profitability year-on-year. The Group's worldwide smartphone shipments declined 31 percent year-on-year but increased 3 percent quarter-by-quarter to 11.2 million. Lenovo's market share in the worldwide smartphone market decreased by 1.5 percentage points year-on-year to 3.2 percent, according to preliminary industry estimates. The Group's transformation strategy – focusing on higher price bands and expanding its channel structure – is on track, which was shown in the improvement in average selling price and sequential sales revenue.

In China, the Group continued to execute its business transformation plan, leveraging its ZUK brand to focus on mid-price band, user experience improvement and expanding its presence in retail and online channel coverage. Shipments in China declined year-on-year as the Group continued to shift away from low price band, but it was up sequentially, resulting in higher average selling price and sales revenue.

Meanwhile, the business from rest of world (ROW) continued to be stable. Smartphone shipments continued its growth momentum in Asia Pacific and Eastern Europe, which was up 5 and 19 percent year-on-year, respectively.

Representing approximately 17 percent of the Group's total revenue, revenue from Mobile business decreased 6 percent or 1 percent excluding currency impact year-on-year to US$1,706 million for the three months ended June 30, 2016. Nevertheless, the revenue increased by 10 percent quarter-on-quarter, driven by the strategic initiative to increase average selling price by streamlining the product portfolio and focusing on higher price bands. The Group's mobile business recorded an operational loss before taxation of US$163 million and a negative 9.6 percent pre-tax profit margin, if excluding the non-cash M&A related accounting charges.

**Data Center Business Group (DCG)**

Data center business revenue represented approximately 11 percent of the Group's total revenue. During the quarter under review, Lenovo's data center business continued to demonstrate healthy revenue growth in China, while it is still in the process in improving its business outside of China.

For the three months ended June 30, 2016, revenue of the data center business was US$1,086 million, an increase of 1 percent year-on-year or 4 percent year-on-year excluding currency impact. Its strong performance in China continued with revenue up 14% year-on-year. However, competition in markets outside China remained keen while the Group continued its plan to increase sales coverage and product competiveness, while ramping up partnership contributions, which resulted in slower than expected revenue growth. For the fiscal quarter under review, the Group's data center business recorded an operational loss before taxation of US$31 million and a negative 2.9 percent pre-tax profit margin, if excluding the non-cash M&A related accounting charges.

**Lenovo Capital and Incubator Group (LCIG) and Others**

The Group's Capital and Incubator Group began at the start of the fiscal year with a mission to drive innovation through investment in startups and exploring new technologies. During the quarter under review, the Group has completed a number of investment projects and set up its accelerator in Shenzhen and Hong Kong to explore more future opportunities for the Group.

Revenue from ecosystem and other products such as consumer electronic businesses from previous acquisitions was US$272 million, representing approximately 3 percent of the Group's total revenue.

**Performance of Geographies**

Performance of each geography includes a combination of PCSD, data center and mobility businesses. The profitability figures of geographies disclosed in the following paragraphs have excluded the impact of non-cash M&A related accounting charges for the period under review.

**China**

China accounted for 28 percent of the Group's total revenue. The Group maintained its strong number one position in China PC market with market share of 37.8 percent, according to preliminary industry estimates, and continued to uphold its profitability by leveraging its leadership position despite the market challenges.

Competition in China smartphone market remained very keen while demand remained soft due to the slow economy. The Group has taken actions to shift its product portfolio towards mid to higher price bands and expand its coverage in the retail and online channels to turn around its China business over time. Meanwhile it will continue to leverage its ZUK brand to improve user experience, and the launch of its new ZUK 2 products during the quarter has received initial good market feedback.

The data center business continued to record strong growth in revenue driven by the hyperscale business. Its revenue grew by 14 percent year-on-year, continued to grow faster than the market.

Profit before taxation was US$138 million and pre-tax profit margin was 4.8 percent, flattish year-on-year.

**Americas (AG)**

Americas accounted for 30 percent of the Group's total revenue. The Group's PC unit shipments in AG increased by 9 percent year-on-year, outperforming the market by a 10-point premium. The Group's AG market share increased by 1.4 percentage points from a year ago to 14.4 percent, according to preliminary industry estimates. The solid performance was driven by the strong growth of its PC unit shipments in the U.S., which grew by 15 percent year-on-year against a market growth of 4 percent. This brought its U.S. market share to 14.2 percent in fiscal quarter one, up 1.3 percentage points year-on-year.

The Group's smartphone shipments remained slow due to product transition in the region and macroeconomic challenges in Latin America. The Group data center business continued its investment in building its sales force and developing new product solutions while leveraging its partnerships to improve its revenue momentum over time.

The Group recorded a profit before taxation of US$38 million in the region, versus a loss before taxation of US$131 million recorded in same period last year, and its pre-tax profit margin was 1.3 percent. The improved performance was enhanced by better profit recovery in Brazil/Latin America.

**Asia Pacific (AP)**

Asia Pacific accounted for 17 percent of the Group's total revenue. The Group's PC shipments grew at a 2-point premium to the market during the period and its market share in AP increased by 0.4 percentage points year-on-year, to 16.4 percent for fiscal quarter one, according to preliminary industry estimates. The Group has made significant progress in ASEAN, achieving a 9-point premium growth to the market.

The Group continued its solid shipments performance in smartphones during the period under review, and momentum has been particularly strong in India and Indonesia, with a double-digit growth premium to the market. The Group's data center business continued its actions in driving future revenue and profitability improvement.

Profit before taxation was US$17 million and pre-tax profit margin was 1.0 percent, against 2.2 percent in the same period last year, mainly due to the contraction in Japan PC market and impact from currency fluctuation.

**Europe-Middle East-Africa (EMEA)**

EMEA accounted for 25 percent of the Group's total revenue. Lenovo's PC unit shipments in EMEA declined by 7 percent year-on-year, against a market decline of 5 percent year-on-year, impacted by macroeconomic issues and currency fluctuations. The Group's market share declined by 0.4 percentage point year-on-year to 19.5 percent in EMEA, according to preliminary industry estimates.

The Group's smartphone shipments were down year-on-year largely due to product transitions. Performance in Eastern Europe remained solid and continued to outgrow the market. The Group continued its actions in enhancing its sales force and investment in product portfolio in its data center business to pursue better growth overtime.

The Group incurred US$49 million losses before taxation in EMEA during the period under review against a profit of US$40 million in the same period last year, with pre-tax profit margin declining by 3.5 percentage points year-on-year to negative 2.0 percent.

**Business Realignment Plan Update**

The Group announced a plan to execute a series of business realignment actions since financial quarter two of 2016, to enable the Group to focus resources, sharpen its business model and efficiently capitalize on the most attractive market opportunities in mobile, PC and data center. Executions of these actions by the Group have been on track and as a result a total savings target of US$1.35 billion for the year was achieved by the Group in the end of the fiscal quarter one.

**Outlook**

Looking forward, despite uncertainties in the macroeconomic environment, the Group expects its business transformation will gradually deliver the planned benefits. The efficient organization structure, coupled with the competitive cost structure across all of its businesses, together with its solid execution, positions the Group well to sustain its growth even in the current challenging market environment.

In PCSD business, the Group will continue to outgrow the PC market by leverage the consolidation trend to gain more share and drive profitable growth. Even more, Lenovo will leverage its innovation leadership in the expanded PC market, such as detachables, convertibles, and 2-and-1. The Group has the leading product offerings to win in this growing segment. The commercial replacement cycle is expected to pick up as Windows 10 becomes more accepted. As a result, the Group remains confident it will continue to deliver profitable growth in PCs over time. On the smart device side, the Group will continue its innovation and drive business growth overtime.

In mobile business, the Group will continue to execute the strategy to resume its growth. In mature markets, new products – including Moto Z & Moto Mods – will strengthen product competiveness and drive future growth. In the rest of the world, the Group will focus on promoting products in higher price bands in key high growth countries. In China, the Group will keep driving the strategy to continue to expand online channels and retailer coverage and leverage ZUK Z2 model to rebuild the end-to-end competitiveness. The Group will continue to focus on the business transformation to drive innovative product design and higher average selling price across its product portfolio while also improving its earnings quality through a more efficient cost structure.

In data center business, the Group has reorganized its structure to sharply focus on the market, and continue to enhance its end-to-end capabilities and ownership for everything from innovation through operations and technical support. The Group is expanding its solution portfolio, with its own innovation and integrating partner technologies, to compete in a larger percentage of the total market opportunity. In the meantime, the Group has actions in place to enhance the sales team to accelerate the business in markets outside China, and will increase its investments to increase solutions and services to improve margin performance over time.

The Capital and Incubator Group will continue to invest in core-technology and Internet related areas, including cloud computing, big data, artificial intelligence, robotics and Internet services, to enhance its Internet service and intelligence ecosystem.

The Group has started its monetization exercise in selling some of its non-core assets in fiscal quarter one. By monetizing and unlocking value in the non-core assets, the Group will be able to improve its working capital position and get additional funds to invest in the growth areas of its business. The Group will continue to look for such asset monetization opportunity in the future.

Lenovo will continue to invest in areas it believes are important to its future success. Lenovo remains fully committed to its protect and attack strategy, supported by its proven execution capabilities, to lead the Group on its ongoing journey towards building a respected global tech leadership position in every business the Group enters and to drive profitable growth that, in turn, creates better value for shareholders.

## FINANCIAL REVIEW

***Results for the three months ended June 30, 2016***

| | **3 months ended June 30, 2016 (unaudited)** ***US$'million*** | 3 months ended June 30, 2015 (unaudited) *US$'million* | Year-on-year change |
|---|---|---|---|
| Revenue | **10,056** | 10,716 | (6)% |
| Gross profit | **1,534** | 1,647 | (7)% |
| Gross profit margin | **15.3%** | 15.4% | (0.1) pts |
| Operating expenses | **(1,289)** | (1,551) | (17)% |
| Operating profit | **245** | 96 | 157% |
| Other non-operating expenses – net | **(39)** | (44) | (9)% |
| Profit before taxation | **206** | 52 | 297% |
| Profit for the period | **168** | 102 | 65% |
| Profit attributable to equity holders of the Company | **173** | 105 | 64% |
| Earnings per share attributable to equity holders of the Company | | | |
| Basic | **US 1.57 cents** | US 0.95 cents | US 0.62 cents |
| Diluted | **US 1.56 cents** | US 0.94 cents | US 0.62 cents |

For the three months ended June 30, 2016, the Group achieved total sales of approximately US$10,056 million. Profit attributable to equity holders for the period was approximately US$173 million, representing an increase of US$68 million as compared with the corresponding period of last year. Gross profit margin for the period was 0.1 point down from 15.4 percent reported in the corresponding period of last year. Basic earnings per share and diluted earnings per share were US1.57 cents and US1.56 cents, representing an increase of US0.62 cents as compared with the corresponding period of last year.

The Group adopts geographical segments as the reporting format. Geographical segments comprise China, AP, EMEA and AG. Sales by segment are as follows:

| | **3 months ended June 30, 2016** ***US$'000*** | 3 months ended June 30, 2015 *US$'000* |
|---|---|---|
| China | **2,854,788** | 3,165,253 |
| AP | **1,679,890** | 1,619,726 |
| EMEA | **2,466,575** | 2,661,878 |
| AG | **3,054,833** | 3,268,982 |
| | **10,056,086** | 10,715,839 |

Further analyses of sales by segment are set out in Business Review and Outlook.

Operating expenses analyzed by function for the three months ended June 30, 2016 and 2015 are as follows:

| | **3 months ended June 30, 2016** *US$'000* | 3 months ended June 30, 2015 *US$'000* |
|---|---|---|
| Other income – net | **-** | 1,653 |
| Selling and distribution expenses | **(589,021)** | (565,577) |
| Administrative expenses | **(458,591)** | (565,655) |
| Research and development expenses | **(355,743)** | (389,547) |
| Other operating income/(expenses) – net | **113,973** | (31,929) |
| | **(1,289,382)** | (1,551,055) |

Operating expenses for the period decreased by 17 percent as compared with the corresponding period of last year. Employee benefit costs decreased by US$76 million as a result of reduced headcount subsequent to the business realignment actions. The net other operating income for the period is mainly attributable to research and development related government grants and other incentives, and gain on monetizing certain non-core assets, offset with the net exchange loss. The impact of currency fluctuations during the period presented a challenge, the Group recorded a net exchange loss of US$23 million (2015/16: US$31 million) for the period. Key expenses by nature comprise:

| | **3 months ended June 30, 2016** ***US$'000*** | 3 months ended June 30, 2015 *US$'000* |
|---|---|---|
| Depreciation of property, plant and equipment and amortization of prepaid lease payments | **(39,980)** | (39,179) |
| Amortization of intangible assets | **(112,087)** | (116,700) |
| Employee benefit costs, including | **(744,358)** | (820,367) |
| - *long-term incentive awards* | ***(33,070)*** | *(28,430)* |
| Rental expenses under operating leases | **(18,442)** | (20,746) |
| Net foreign exchange loss | **(22,822)** | (30,847) |
| Advertising and promotional expenses | **(182,180)** | (172,509) |
| Gain on disposal of property, plant and equipment and prepaid lease payments | **131,712** | 2,922 |
| Others | **(301,225)** | (353,629) |
| | **(1,289,382)** | (1,551,055) |

Other non-operating expenses (net) for the three months ended June 30, 2016 and 2015 comprise:

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Finance income | **6,140** | 9,010 |
| Finance costs | **(55,477)** | (51,041) |
| Share of profits/(losses) of associates and joint ventures | **9,837** | (1,558) |
| | **(39,500)** | (43,589) |

Finance income mainly represents interest on bank deposits.

Finance costs for the period increased by 9 percent as compared with the corresponding period of last year. This is mainly attributable to interest expense of US$8 million (2015/16: US$2 million) in relation to the 5-Year RMB4 billion notes, issued in June 2015, bearing annual interest at 4.95% due in June 2020.

Share of profits/(losses) of associates and joint ventures represents operating profits/(losses) arising from principal business activities of respective associates and joint ventures.

**Capital Expenditure**

The Group incurred capital expenditure of US$114 million (2015/16: US$153 million) during the peiod ended June 30, 2016, mainly for the acquisition of property, plant and equipment, additions in construction-in-progress and intangible assets.

**Liquidity and Financial Resources**

At June 30, 2016, total assets of the Group amounted to US$25,219 million (March 31, 2016: US$24,933 million), which were financed by equity attributable to owners of the Company of US$3,290 million (March 31, 2016: US$3,000 million), non-controlling interests (net of put option written on non-controlling interest) of US$21 million (March 31, 2016: US$26 million), and total liabilities of US$21,908 million (March 31, 2016: US$21,907 million). At June 30, 2016, the current ratio of the Group was 0.84 (March 31, 2016: 0.82).

The Group had a solid financial position. At June 30, 2016, bank deposits, cash and cash equivalents totaled US$2,064 million (March 31, 2016: US$2,079 million), of which 20.2 (March 31, 2016: 41.7) percent was denominated in US dollar, 51.5 (March 31, 2016: 29.5) percent in Renminbi, 5.4 (March 31, 2016: 5.3) percent in Euro, 5.8 (March 31, 2016: 7.7) percent in Japanese Yen, and 17.1 (March 31, 2016: 15.8) percent in other currencies.

The Group adopts a conservative policy to invest the surplus cash generated from operations. At June 30, 2016, 99.9 (March 31, 2016: 92.6) percent of cash are bank deposits, and 0.1 (March 31, 2016: 7.4) percent of cash are investments in liquid money market funds of investment grade.

Although the Group has consistently maintained a very liquid position, banking facilities have nevertheless been put in place for contingency purposes.

The Group entered into a 5-Year loan facility agreement with syndicated banks for US$1,200 million, comprising US$800 million as short term, on December 18, 2013. As at June 30, 2016, the facility was utilized to the extent of US$800 million (March 31, 2016: US$800 million), comprising US$400 million (March 31, 2016: US$400 million) short-term.

In addition, on May 26, 2015, the Group entered into a 5-Year loan facility agreement with a bank for US$300 million. The facility was fully utilized as at June 30, 2016 (March 31, 2016: fully utilized).

On May 8, 2014, the Group completed the issuance of 5-Year US$1.5 billion notes bearing annual interest at 4.7% due in May 2019; and on June 10, 2015, the Group completed the issuance of 5-Year RMB4 billion notes bearing annual interest at 4.95% due in June 2020. The proceeds have been used for general corporate purposes including working capital, and acquisition activities.

The Group has also arranged other short-term credit facilities. At June 30, 2016, the Group's total available credit facilities amounted to US$10,503 million (March 31, 2016: US$10,661 million), of which US$1,181 million (March 31, 2016: US$1,277 million) was in trade lines, US$366 million (March 31, 2016: US$366 million) in short-term and revolving money market facilities and US$8,956 million (March 31, 2016: US$9,018 million) in forward foreign exchange contracts. At June 30, 2016, the amounts drawn down were US$565 million (March 31, 2016: US$540 million) in trade lines, US$7,122 million (March 31, 2016: US$6,872 million) being used for the forward foreign exchange contracts, and US$48 million (March 31, 2016: US$46 million) in short-term bank loans.

At June 30, 2016, the Group's outstanding borrowings represented by the term bank loan of US$397 million (March 31, 2016: US$396 million), short-term bank loans of US$741 million (March 31, 2016: US$746 million) and long term notes of US$2,093 million (March 31, 2016: US$2,109 million). When compared with total equity of US$3,311 million (March 31, 2016: US$3,026 million), the Group's gearing ratio was 0.98 (March 31, 2016: 1.07). The net debt position of the Group at June 30, 2016 is US$1,167 million (March 31, 2016: US$1,172 million).

The Group is confident that all the facilities on hand can meet the funding requirements of the Group's operations and business development.

The Group adopts a consistent hedging policy for business transactions to reduce the risk of currency fluctuation arising from daily operations. At June 30, 2016, the Group had commitments in respect of outstanding forward foreign exchange contracts amounting to US$7,122 million (March 31, 2016: US$6,872 million). The Group's forward foreign exchange contracts are either used to hedge a percentage of future transactions which are highly probable, or used as fair value hedges for identified assets and liabilities.

**Contingent Liabilities**

The Group, in the ordinary course of its business, is involved in various claims, suits, investigations, and legal proceedings that arise from time to time. Although the Group does not expect that the outcome in any of these legal proceedings, individually or collectively, will have a material adverse effect on its financial position or results of operations, litigation is inherently unpredictable. Therefore, the Group could incur judgments or enter into settlements of claims that could adversely affect its operating results or cash flows in a particular period.

## CONSOLIDATED INCOME STATEMENT

| | Note | **3 months ended June 30, 2016 (unaudited)** ***US$'000*** | 3 months ended June 30, 2015 (unaudited) *US$'000* |
|---|---|---|---|
| Revenue | *2* | **10,056,086** | 10,715,839 |
| Cost of sales | | **(8,521,603)** | (9,069,364) |
| Gross profit | | **1,534,483** | 1,646,475 |
| Other income – net | *3* | **-** | 1,653 |
| Selling and distribution expenses | | **(589,021)** | (565,577) |
| Administrative expenses | | **(458,591)** | (565,655) |
| Research and development expenses | | **(355,743)** | (389,547) |
| Other operating income/(expenses) - net | | **113,973** | (31,929) |
| Operating profit | *4* | **245,101** | 95,420 |
| Finance income | *5(a)* | **6,140** | 9,010 |
| Finance costs | *5(b)* | **(55,477)** | (51,041) |
| Share of profits/(losses) of associates and joint ventures | | **9,837** | (1,558) |
| Profit before taxation | | **205,601** | 51,831 |
| Taxation | *6* | **(37,966)** | 50,045 |
| Profit for the period | | **167,635** | 101,876 |
| Profit/(loss) attributable to: | | | |
| Equity holders of the Company | | **172,947** | 105,152 |
| Non-controlling interests | | **(5,312)** | (3,276) |
| | | **167,635** | 101,876 |
| Earnings per share attributable to equity holders of the Company | | | |
| Basic | *7(a)* | **US1.57 cents** | US 0.95 cents |
| Diluted | *7(b)* | **US1.56 cents** | US 0.94 cents |

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | **3 months ended June 30, 2016 (unaudited)** ***US$'000*** | 3 months ended June 30, 2015 (unaudited) *US$'000* |
|---|---|---|
| Profit for the period | **167,635** | 101,876 |
| Other comprehensive (loss)/income: | | |
| Items that have been reclassified or may be subsequently reclassified to profit or loss | | |
| Fair value change on available-for-sale financial assets, net of taxes | **(2,166)** | 5,999 |
| Investment revaluation reserve reclassified to consolidated income statement on disposal of available-for-sale financial assets | **-** | 154 |
| Fair value change on cash flow hedges from forward foreign exchange contracts, net of taxes | | |
| - Fair value gain/(loss), net of taxes | **6,012** | (108,570) |
| - Reclassified to consolidated income statement | **68,453** | (19,888) |
| Currency translation differences | **53,038** | 31,944 |
| Other comprehensive income/(loss) for the period | **125,337** | (90,361) |
| Total comprehensive income for the period | **292,972** | 11,515 |
| Total comprehensive income/(loss) attributable to: | | |
| Equity holders of the Company | **298,284** | 14,791 |
| Non-controlling interests | **(5,312)** | (3,276) |
| | **292,972** | 11,515 |

## CONSOLIDATED BALANCE SHEET

| | Note | **June 30, 2016 (unaudited)** *US$'000* | March 31, 2016 (audited) *US$'000* |
|---|---|---|---|
| Non-current assets | | | |
| Property, plant and equipment | | **1,344,189** | 1,391,494 |
| Prepaid lease payments | | **324,203** | 337,929 |
| Construction-in-progress | | **252,460** | 231,110 |
| Intangible assets | | **8,630,797** | 8,661,087 |
| Interests in associates and joint ventures | | **50,276** | 40,439 |
| Deferred income tax assets | | **1,045,515** | 1,000,572 |
| Available-for-sale financial assets | | **151,252** | 139,572 |
| Other non-current assets | | **177,117** | 164,410 |
| | | **11,975,809** | 11,966,613 |
| Current assets | | | |
| Inventories | | **2,577,472** | 2,637,317 |
| Trade receivables | *8(a)* | **4,560,679** | 4,403,507 |
| Notes receivable | | **171,306** | 130,718 |
| Derivative financial assets | | **78,413** | 27,021 |
| Deposits, prepayments and other receivables | *9* | **3,642,359** | 3,548,760 |
| Income tax recoverable | | **149,315** | 140,237 |
| Bank deposits | | **157,444** | 152,336 |
| Cash and cash equivalents | | **1,906,191** | 1,926,880 |
| | | **13,243,179** | 12,966,776 |
| Total assets | | **25,218,988** | 24,933,389 |

## CONSOLIDATED BALANCE SHEET (CONTINUED)

| | Note | **June 30, 2016 (unaudited)** ***US$'000*** | March 31, 2016 (audited) *US$'000* |
|---|---|---|---|
| Share capital | *13* | **2,689,882** | 2,689,882 |
| Reserves | | **600,514** | 310,318 |
| Equity attributable to owners of the Company | | **3,290,396** | 3,000,200 |
| Non-controlling interests | | **233,637** | 238,949 |
| Put option written on non-controlling interest | *11(c)* | **(212,900)** | (212,900) |
| Total equity | | **3,311,133** | 3,026,249 |
| Non-current liabilities | | | |
| Borrowings | *12* | **2,489,253** | 2,505,112 |
| Warranty provision | *10(b)* | **289,956** | 290,857 |
| Deferred revenue | | **527,821** | 532,780 |
| Retirement benefit obligations | | **450,871** | 442,874 |
| Deferred income tax liabilities | | **220,985** | 222,679 |
| Other non-current liabilities | *11* | **2,178,985** | 2,152,578 |
| | | **6,157,871** | 6,146,880 |
| Current liabilities | | | |
| Trade payables | *8(b)* | **4,713,765** | 4,266,687 |
| Notes payable | | **268,874** | 234,661 |
| Derivative financial liabilities | | **111,109** | 150,864 |
| Other payables and accruals | *10(a)* | **8,035,505** | 8,305,844 |
| Provisions | *10(b)* | **1,036,565** | 1,157,257 |
| Deferred revenue | | **655,798** | 710,164 |
| Income tax payable | | **187,009** | 188,968 |
| Borrowings | *12* | **741,359** | 745,815 |
| | | **15,749,984** | 15,760,260 |
| Total liabilities | | **21,907,855** | 21,907,140 |
| Total equity and liabilities | | **25,218,988** | 24,933,389 |

## CONSOLIDATED CASH FLOW STATEMENT

| | Note | **3 months ended June 30, 2016 (unaudited)** *US$'000* | 3 months ended June 30, 2015 (unaudited) *US$'000* |
|---|---|---|---|
| Cash flows from operating activities | | | |
| Net cash generated from/(used in) operations | *14* | **178,219** | (147,107) |
| Interest paid | | **(69,690)** | (55,855) |
| Tax paid | | **(100,486)** | (107,038) |
| Net cash generated from/(used in) operating activities | | **8,043** | (310,000) |
| Cash flows from investing activities | | | |
| Purchase of property, plant and equipment | | **(34,627)** | (56,585) |
| Purchase of prepaid lease payments | | **(171)** | - |
| Sale of property, plant and equipment and prepaid lease payments | | **160,728** | 23,258 |
| Interests acquired in associates | | **-** | (1,051) |
| Payment for construction-in-progress | | **(48,307)** | (69,336) |
| Payment for intangible assets | | **(31,282)** | (26,890) |
| Purchase of available-for-sale financial assets | | **(13,387)** | (26,261) |
| Net proceeds from disposal of available-for-sale financial assets | | **-** | 2,835 |
| Increase in bank deposits | | **(5,108)** | (2,038) |
| Interest received | | **6,140** | 9,010 |
| Net cash generated from/(used in) investing activities | | **33,986** | (147,058) |
| Cash flows from financing activities | | | |
| Contribution to employee share trusts | | **(36,673)** | (66,314) |
| Proceeds from borrowings | | **400,901** | 226,255 |
| Repayments of borrowings | | **(404,877)** | (483,950) |
| Issue of long term notes | | **-** | 640,895 |
| Net cash (used in)/generated from financing activities | | **(40,649)** | 316,886 |
| Increase/(decrease) in cash and cash equivalents | | **1,380** | (140,172) |
| Effect of foreign exchange rate changes | | **(22,069)** | 4,377 |
| Cash and cash equivalents at the beginning of the period | | **1,926,880** | 2,855,223 |
| Cash and cash equivalents at the end of the period | | **1,906,191** | 2,719,428 |

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | Attributable to equity holders of the Company | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital (unaudited) *US$'000* | Investment revaluation reserve (unaudited) *US$'000* | Employee share trusts (unaudited) *US$'000* | Share-based compensation reserve (unaudited) *US$'000* | Hedging reserve (unaudited) *US$'000* | Exchange reserve (unaudited) *US$'000* | Other reserve (unaudited) *US$'000* | Retained earnings (unaudited) *US$'000* | Non-controlling interests (unaudited) *US$'000* | Put option written on non-controlling interest (unaudited) *US$'000* | Total (unaudited) *US$'000* |
| At April 1, 2016 | **2,689,882** | **962** | **(52,897)** | **13,161** | **(88,328)** | **(1,141,195)** | **83,363** | **1,495,252** | **238,949** | **(212,900)** | **3,026,249** |
| Profit/(loss) for the period | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **172,947** | **(5,312)** | **–** | **167,635** |
| Other comprehensive (loss)/income | **–** | **(2,166)** | **–** | **–** | **74,465** | **53,038** | **–** | **–** | **–** | **–** | **125,337** |
| Total comprehensive (loss)/income for the period | **–** | **(2,166)** | **–** | **–** | **74,465** | **53,038** | **–** | **172,947** | **(5,312)** | **–** | **292,972** |
| Vesting of shares under long-term incentive program | **–** | **–** | **41,998** | **(48,137)** | **–** | **–** | **–** | **–** | **–** | **–** | **(6,139)** |
| Share-based compensation | **–** | **–** | **–** | **34,724** | **–** | **–** | **–** | **–** | **–** | **–** | **34,724** |
| Contribution to employee share trusts | **–** | **–** | **(36,673)** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(36,673)** |
| At June 30, 2016 | **2,689,882** | **(1,204)** | **(47,572)** | **(252)** | **(13,863)** | **(1,088,157)** | **83,363** | **1,668,199** | **233,637** | **(212,900)** | **3,311,133** |
| At April 1, 2015 | 2,689,882 | 592 | (11,441) | 9,852 | 118,082 | (834,114) | 75,712 | 2,035,078 | 235,378 | (212,900) | 4,106,121 |
| Profit/(loss) for the period | – | – | – | – | – | – | – | 105,152 | (3,276) | – | 101,876 |
| Other comprehensive income/(loss) | – | 6,153 | – | – | (128,458) | 31,944 | – | – | – | – | (90,361) |
| Total comprehensive income/(loss) for the period | – | 6,153 | – | – | (128,458) | 31,944 | – | 105,152 | (3,276) | – | 11,515 |
| Transfer to statutory reserve | – | – | – | – | – | – | 7,651 | (7,651) | – | – | – |
| Vesting of shares under long-term incentive program | – | – | 68,101 | (97,715) | – | – | – | – | – | – | (29,614) |
| Deferred tax credit in relation to long-term incentive program | – | – | – | 17,363 | – | – | – | – | – | – | 17,363 |
| Share-based compensation | – | – | – | 39,107 | – | – | – | – | – | – | 39,107 |
| Contribution to employee share trusts | – | – | (66,314) | – | – | – | – | – | – | – | (66,314) |
| At June 30, 2015 | 2,689,882 | 6,745 | (9,654) | (31,393) | (10,376) | (802,170) | 83,363 | 2,132,579 | 232,102 | (212,900) | 4,078,178 |

Notes

## 1 General information and basis of preparation

The financial information relating to the year ended March 31, 2016 that is included in the FY2016/17 first quarter results announcement as comparative information does not constitute the Company's statutory annual consolidated financial statements for that year but is derived from those financial statements. Further information relating to these statutory financial statements required to be disclosed in accordance with section 436 of the Hong Kong Companies Ordinance is as follows:

The Company will deliver the financial statements for the year ended March 31, 2016 to the Registrar of Companies as required by section 662(3) of, and Part 3 of Schedule 6 to, the Hong Kong Companies Ordinance.

The Company's auditor has reported on those financial statements. The auditor's report was unqualified; did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying its report; and did not contain a statement under sections 406(2), 407(2) or (3) of the Hong Kong Companies Ordinance.

Basis of preparation

The financial information presented above and notes thereto are extracted from the Group’s consolidated financial statements and presented in accordance with Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The Board is responsible for the preparation of the Group’s financial statements. The financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards. The financial statements have been prepared under the historical cost convention except that certain financial assets and financial liabilities are stated at fair values.

The Group has adopted the following new amendments to existing standards that are mandatory for the year ending March 31, 2017 which the Group considers are appropriate and relevant to its operations:

- Amendments to HKAS 1, Disclosure initiative
- Amendments to HKAS 16 and HKAS 38, Clarification of acceptable methods of depreciation and amortization
- Amendments to HKAS 27, Equity method in separate financial statements
- Amendments to HKFRS 10, HKFRS 12 and HKAS 28, Investment entities: applying the consolidation exception
- Amendments to HKFRS 11, Accounting for acquisitions of interests in joint operations

The adoption of these newly effective amendments to existing standards does not result in substantial changes to the Group’s accounting policies or financial results.

The following new standards and amendments to existing standards, which are considered appropriate and relevant to the Group’s operations, have been issued but are not effective for the year ending March 31, 2017 and have not been early adopted:

| | Effective for annual periods beginning on or after |
|---|---|
| HKFRS 9, Financial instruments | January 1, 2018 |
| HKFRS 15, Revenue from contracts with customers | January 1, 2018 |
| HKFRS 16, Leases | January 1, 2019 |
| Amendments to HKAS 7, Disclosure initiative | January 1, 2017 |
| Amendments to HKAS 12, Recognition of deferred tax assets for unrealised losses | January 1, 2017 |
| Amendments to HKFRS 10 and HKAS 28, Sale or contribution of assets between an investor and its associate or joint venture | Date to be determined |

The Group is in the process of making an assessment of the impact of these new standards and amendments to existing standards upon initial application.

## 2 Segment information

Management has determined the operating segments based on the reports reviewed by the Lenovo Executive Committee (the "LEC"), the chief operating decision-maker, that are used to make strategic decisions.

The LEC considers business from a geographical perspective. The Group has four geographical segments, China, AP, EMEA and AG, which are also the Group's reportable operating segments.

The LEC assesses the performance of the operating segments based on a measure of adjusted pre-tax income/(loss). This measurement basis excludes the effects of non-recurring expenditure such as restructuring costs from the operating segments. The measurement basis also excludes the effects of unrealized gains/(losses) on financial instruments. Certain interest income and expenditure are not allocated to segments, as this type of activity is driven by the central treasury function, which manages the cash position of the Group.

Supplementary information on segment assets and liabilities presented below is primarily based on the geographical location of the entities or operations which carry the assets and liabilities, except for entities performing centralized functions for the Group the assets and liabilities of which are not allocated to any segment.

(a) Segment revenue and adjusted pre-tax income/(loss) for reportable segments

| | **3 months ended June 30, 2016** | | 3 months ended June 30, 2015 | |
|---|---|---|---|---|
| | **Revenue from external customers** | **Adjusted pre-tax income/ (loss)** | Revenue from external customers | Adjusted pre-tax income/ (loss) |
| | ***US$'000*** | ***US$'000*** | *US$'000* | *US$'000* |
| China | **2,854,788** | **137,861** | 3,165,253 | 153,334 |
| AP | **1,679,890** | **16,532** | 1,619,726 | 34,885 |
| EMEA | **2,466,575** | **(49,366)** | 2,661,878 | 39,799 |
| AG | **3,054,833** | **38,190** | 3,268,982 | (130,929) |
| Segment total | **10,056,086** | **143,217** | 10,715,839 | 97,089 |
| Unallocated: | | | | |
| Headquarters and corporate income/(expenses) | | **96,010** | | (8,023) |
| Finance income | | **5,345** | | 6,996 |
| Finance costs | | **(48,808)** | | (44,326) |
| Net gain on disposal of available-for-sale financial assets | | **-** | | 1,653 |
| Share of profits/(losses) of associates and joint ventures | | **9,837** | | (1,558) |
| Consolidated profit before taxation | | **205,601** | | 51,831 |

(b) Segment assets for reportable segments

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| China | **7,585,896** | 7,064,692 |
| AP | **3,127,547** | 3,229,634 |
| EMEA | **3,380,443** | 3,445,913 |
| AG | **6,666,808** | 6,535,732 |
| Segment assets for reportable segments | **20,760,694** | 20,275,971 |
| Unallocated: | | |
| Deferred income tax assets | **1,045,515** | 1,000,572 |
| Derivative financial assets | **78,413** | 27,021 |
| Available-for-sale financial assets | **151,252** | 139,572 |
| Interests in associates and joint ventures | **50,276** | 40,439 |
| Unallocated bank deposits and cash and cash equivalents | **517,146** | 898,577 |
| Unallocated inventories | **726,640** | 755,799 |
| Unallocated deposits, prepayments and other receivables | **1,454,838** | 1,355,219 |
| Income tax recoverable | **149,315** | 140,237 |
| Other unallocated assets | **284,899** | 299,982 |
| Total assets per consolidated balance sheet | **25,218,988** | 24,933,389 |

(c) Segment liabilities for reportable segments

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| China | **4,830,662** | 4,332,504 |
| AP | **1,834,275** | 1,924,875 |
| EMEA | **1,590,727** | 1,762,689 |
| AG | **3,292,590** | 3,559,616 |
| Segment liabilities for reportable segments | **11,548,254** | 11,579,684 |
| Unallocated: | | |
| Income tax payable | **187,009** | 188,968 |
| Deferred income tax liabilities | **220,985** | 222,679 |
| Derivative financial liabilities | **111,109** | 150,864 |
| Unallocated borrowings | **3,182,411** | 3,198,749 |
| Unallocated trade payables | **2,723,930** | 2,506,235 |
| Unallocated other payables and accruals | **2,414,654** | 2,522,636 |
| Unallocated provisions | **106,654** | 174,534 |
| Unallocated other non-current liabilities | **1,331,019** | 1,293,625 |
| Other unallocated liabilities | **81,830** | 69,166 |
| Total liabilities per consolidated balance sheet | **21,907,855** | 21,907,140 |

(d) Analysis of revenue by significant category

Revenue from external customers are mainly derived from the sale of personal technology products and services. Breakdown of revenue by business group is as follows:

| | **3 months ended June 30, 2016** *US$'000* | 3 months ended June 30, 2015 *US$'000* |
|---|---|---|
| PC and Smart Device Business Group ("PCSD") | **6,991,583** | 7,556,680 |
| Mobile Business Group ("MBG") | **1,705,821** | 1,814,805 |
| Data Center Group ("DCG") | **1,086,531** | 1,077,046 |
| Others | **272,151** | 267,308 |
| | **10,056,086** | 10,715,839 |

Note: PCSD consists of core PC business as well as slate tablets, detachables, gaming and other smart devices.

(e) Other segment information

| | **China** | | **AP** | | **EMEA** | | **AG** | | **Total** | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **2016** *US$'000* | 2015 *US$'000* | **2016** *US$'000* | 2015 *US$'000* | **2016** *US$'000* | 2015 *US$'000* | **2016** *US$'000* | 2015 *US$'000* | **2016** *US$'000* | 2015 *US$'000* |
| For the three months ended June 30 | | | | | | | | | | |
| Depreciation and amortization | **65,115** | 49,624 | **30,188** | 34,983 | **44,242** | 51,032 | **53,460** | 53,121 | **193,005** | 188,760 |
| Finance income | **37** | 631 | **339** | 276 | **67** | 64 | **352** | 1,043 | **795** | 2,014 |
| Finance costs | **432** | 955 | **1,843** | 1,831 | **1,303** | 2,494 | **3,091** | 1,435 | **6,669** | 6,715 |
| Additions to non-current assets (Note) | **28,180** | 19,543 | **2,609** | 2,024 | **4,245** | 6,284 | **14,747** | 17,036 | **49,781** | 44,887 |

Note: Other than financial instruments and deferred income tax assets; and excluding other non-current assets.

(f) Included in segment assets for reportable segments are goodwill and trademarks and trade names with indefinite useful lives with an aggregate amount of US$6,216 million (March 31, 2016: US$6,171 million). The carrying amounts of goodwill and trademarks and trade names with indefinite useful lives are presented below:

At June 30, 2016

| | **China** *US$ million* | **AP** *US$ million* | **EMEA** *US$ million* | **AG** *US$ million* | **Total** *US$ million* |
|---|---|---|---|---|---|
| Goodwill | | | | | |
| - PCSD | **1,057** | **589** | **221** | **335** | **2,202** |
| - MBG | **-** | **322** | **372** | **950** | **1,644** |
| - DCG | **481** | **161** | **91** | **364** | **1,097** |
| Trademarks and trade names | | | | | |
| - PCSD | **211** | **59** | **104** | **69** | **443** |
| - MBG | **-** | **90** | **104** | **266** | **460** |
| - DCG | **162** | **54** | **31** | **123** | **370** |

At March 31, 2016

| | China<br>*US$ million* | AP<br>*US$ million* | EMEA<br>*US$ million* | AG<br>*US$ million* | Total<br>*US$ million* |
|---|---|---|---|---|---|
| Goodwill | | | | | |
| - PCSD | 1,085 | 549 | 233 | 326 | 2,193 |
| - MBG | - | 314 | 362 | 926 | 1,602 |
| - DCG | 484 | 162 | 92 | 366 | 1,104 |
| Trademarks and trade names | | | | | |
| - PCSD | 211 | 59 | 103 | 69 | 442 |
| - MBG | - | 90 | 104 | 266 | 460 |
| - DCG | 162 | 54 | 31 | 123 | 370 |

The directors are of the view that there was no indication of impairment of goodwill and trademarks and trade names as at June 30, 2016 (March 31, 2016: Nil).

## 3 Other income – net

| | **3 months ended June 30, 2016**<br>***US$'000*** | 3 months ended June 30, 2015<br>*US$'000* |
|---|---|---|
| Net gain on disposal of available-for-sale financial assets | **-** | 1,653 |

## 4 Operating profit

Operating profit is stated after charging the following:

| | **3 months ended June 30, 2016**<br>***US$'000*** | 3 months ended June 30, 2015<br>*US$'000* |
|---|---|---|
| Depreciation of property, plant and equipment and amortization of prepaid lease payments | **69,361** | 60,202 |
| Amortization of intangible assets | **123,644** | 128,558 |
| Employee benefit costs, including | **849,764** | 937,526 |
| *- long-term incentive awards* | ***33,070*** | *28,430* |
| Rental expenses under operating leases | **22,577** | 26,352 |

## 5 Finance income and costs

(a) Finance income

| | **3 months ended June 30, 2016**<br>***US$'000*** | 3 months ended June 30, 2015<br>*US$'000* |
|---|---|---|
| Interest on bank deposits | **5,312** | 8,823 |
| Interest on money market funds | **828** | 183 |
| Others | **-** | 4 |
| | **6,140** | 9,010 |

(b) Finance costs

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Interest on bank loans and overdrafts | **10,271** | 7,896 |
| Interest on long term notes | **25,752** | 20,723 |
| Interest on promissory note | **9,965** | 9,447 |
| Factoring costs | **7,072** | 9,248 |
| Commitment fee | **24** | 1,069 |
| Interest on contingent considerations and put option liability | **1,771** | 1,782 |
| Others | **622** | 876 |
| | **55,477** | 51,041 |

## 6 Taxation

The amount of taxation in the consolidated income statement represents:

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Current tax | | |
| Hong Kong profits tax | **1,666** | 9,217 |
| Taxation outside Hong Kong | **89,379** | 44,486 |
| Deferred tax | **(53,079)** | (103,748) |
| | **37,966** | (50,045) |

Hong Kong profits tax has been provided for at the rate of 16.5% (2015/16: 16.5%) on the estimated assessable profit for the period. Taxation outside Hong Kong represents income and irrecoverable withholding taxes of subsidiaries operating in the Chinese Mainland and overseas, calculated at rates applicable in the respective jurisdictions.

## 7 Earnings per share

(a) Basic

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the period after adjusting shares held by employee share trusts for the purposes of awarding shares to eligible employees under the long term incentive program.

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| Weighted average number of ordinary shares in issue | **11,108,654,724** | 11,108,654,724 |
| Adjustment for shares held by employee share trusts | **(58,062,423)** | (21,702,196) |
| Weighted average number of ordinary shares in issue for calculation of basic earnings per share | **11,050,592,301** | 11,086,952,528 |
| | ***US$'000*** | *US$'000* |
| Profit attributable to equity holders of the Company | **172,947** | 105,152 |

(b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding due to the effect of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares, namely long-term incentive awards.

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| Weighted average number of ordinary shares in issue for calculation of basic earnings per share | **11,050,592,301** | 11,086,952,528 |
| Adjustment for long-term incentive awards | **13,003,485** | 132,188,826 |
| Weighted average number of ordinary shares in issue for calculation of diluted earnings per share | **11,063,595,786** | 11,219,141,354 |
| | ***US$'000*** | *US$'000* |
| Profit attributable to equity holders of the Company used to determine diluted earnings per share | **172,947** | 105,152 |

For the adjustment for dilutive potential ordinary shares of long-term incentive awards, a calculation is performed to determine whether the long-term incentive awards are dilutive, and the number of shares that are deemed to be issued.

There is no adjustment to profit attributable to equity holders of the Company used for the calculation of diluted earnings per share.

## 8 Ageing analysis

(a) Customers are generally granted credit term ranging from 0 to 120 days. Ageing analysis of trade receivables of the Group at the balance sheet date, based on invoice date, is as follows:

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| 0 – 30 days | **3,176,313** | 3,246,600 |
| 31 – 60 days | **673,625** | 617,199 |
| 61 – 90 days | **243,939** | 240,470 |
| Over 90 days | **577,299** | 405,410 |
| | **4,671,176** | 4,509,679 |
| Less: provision for impairment | **(110,497)** | (106,172) |
| Trade receivables – net | **4,560,679** | 4,403,507 |

(b) Ageing analysis of trade payables of the Group at the balance sheet date, based on invoice date, is as follows:

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| 0 – 30 days | **3,275,574** | 3,013,430 |
| 31 – 60 days | **901,209** | 789,183 |
| 61 – 90 days | **412,876** | 347,257 |
| Over 90 days | **124,106** | 116,817 |
| | **4,713,765** | 4,266,687 |

## 9 Deposits, prepayments and other receivables

Details of deposits, prepayments and other receivables are as follows:

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Deposits | **16,020** | 13,207 |
| Other receivables | **2,848,711** | 2,811,260 |
| Prepayments | **777,628** | 724,293 |
| | **3,642,359** | 3,548,760 |

Majority of other receivables are amounts due from subcontractors for part components sold in the ordinary course of business.

## 10 Provisions, other payables and accruals

(a) Details of other payables and accruals are as follows:

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Accruals | **1,829,572** | 2,048,551 |
| Allowance for billing adjustments (i) | **1,806,852** | 1,904,076 |
| Other payables (ii) | **4,399,081** | 4,353,217 |
| | **8,035,505** | 8,305,844 |

Notes:

(i) Allowance for billing adjustments relates primarily to allowances for future volume discounts, price protection, rebates, and customer sales returns.

(ii) Majority of other payables are obligations to pay for finished goods that have been acquired in the ordinary course of business from subcontractors.

(iii) The carrying amounts of other payables and accruals approximate their fair values.

(b) The components of provisions are as follows:

| | Warranty<br>*US$'000* | Environmental restoration<br>*US$'000* | Restructuring<br>*US$'000* | Total<br>*US$'000* |
|---|---|---|---|---|
| Year ended March 31, 2016 | | | | |
| At the beginning of the year | 1,559,795 | 16,475 | - | 1,576,270 |
| Exchange adjustment | (19,051) | 382 | 1,501 | (17,168) |
| Provisions made | 945,709 | 9,104 | 342,103 | 1,296,916 |
| Amounts utilized | (1,164,186) | (8,477) | (220,501) | (1,393,164) |
| Unused amounts reversed | - | (8,667) | - | (8,667) |
| | 1,322,267 | 8,817 | 123,103 | 1,454,187 |
| Long-term portion classified as non-current liabilities | (290,857) | (6,073) | - | (296,930) |
| At the end of the year | 1,031,410 | 2,744 | 123,103 | 1,157,257 |
| Period ended June 30, 2016 | | | | |
| At the beginning of the period | **1,322,267** | **8,817** | **123,103** | **1,454,187** |
| Exchange adjustment | **(3,595)** | **508** | **1,981** | **(1,106)** |
| Provisions made | **170,349** | **3,188** | **-** | **173,537** |
| Amounts utilized | **(247,414)** | **(3,098)** | **(42,935)** | **(293,447)** |
| | **1,241,607** | **9,415** | **82,149** | **1,333,171** |
| Long-term portion classified as non-current liabilities | **(289,956)** | **(6,650)** | **-** | **(296,606)** |
| At the end of the period | **951,651** | **2,765** | **82,149** | **1,036,565** |

The Group records its warranty liability at the time of sales based on estimated costs. Warranty claims are reasonably predictable based on historical failure rate information. The warranty accrual is reviewed quarterly to verify it properly reflects the outstanding obligation over the warranty period. Certain of these costs are reimbursable from the suppliers in accordance with the terms of relevant arrangements with them.

The Group records its environmental restoration provision at the time of sales based on estimated costs of environmentally-sound disposal of waste electrical and electronic equipment upon return from end-customers and with reference to the historical or projected future return rate. The environmental restoration provision is reviewed at least annually to assess its adequacy to meet the Group's obligation.

Restructuring costs provision mainly comprises lease termination obligations and employee termination payments, arising from a series of restructuring actions to reduce costs and enhance operational efficiency. The Group records its restructuring costs provision when it has a present legal or constructive obligation as a result of restructuring actions.

## 11 Other non-current liabilities

Details of other non-current liabilities are as follows:

| | **June 30, 2016** *US$'000* | March 31, 2016 *US$'000* |
|---|---|---|
| Deferred considerations (a) | **1,418,592** | 1,383,555 |
| Guaranteed dividend to non-controlling shareholders of a subsidiary (b) | **8,055** | 8,195 |
| Environmental restoration (Note 10 (b)) | **6,650** | 6,073 |
| Written put option liability (c) | **222,048** | 221,499 |
| Government incentives and grants received in advance (d) | **145,793** | 144,919 |
| Deferred rent liabilities | **110,735** | 112,934 |
| Others | **267,112** | 275,403 |
| | **2,178,985** | 2,152,578 |

(a) Pursuant to the completion of business combinations, the Group is required to pay in cash to the then respective shareholders/sellers deferred consideration. Accordingly, current and non-current liabilities in respect of the present values of deferred considerations have been recognized. Deferred consideration is subsequently measured at amortized cost.

As at June 30, 2016, the potential undiscounted amounts of future payments in respect of the deferred considerations that the Group could be required to make to the then respective shareholders/sellers under the arrangements are as follows:

| | |
|---|---|
| Joint venture with NEC Corporation | US$251 million |
| Google Inc. | US$1,448 million |

(b) Following the acquisition of Medion AG ("Medion") on July 29, 2011, Lenovo Germany Holding GmbH ("Lenovo Germany"), an indirect wholly-owned subsidiary of the Company and the immediate holding company of Medion entered into a domination and profit and loss transfer agreement (the "Domination Agreement") with Medion on October 25, 2011. Pursuant to the Domination Agreement, Lenovo Germany has guaranteed to the non-controlling shareholders of Medion an annual guaranteed pre-tax dividend amounting to EUR0.82 per share for each fiscal year. The Domination Agreement became effective on January 3, 2012 and is terminable by either Lenovo Germany or Medion after March 31, 2017. Accordingly, a non-current liability in respect of future guaranteed dividend has been recognized. The corresponding amount stated at its discounted value on the date of acquisition of Medion was charged to retained earnings in equity.

(c) Pursuant to the joint venture agreement entered into between the Company and Compal Electronics, Inc. (“Compal”) to establish a joint venture company (“JV Co”) to manufacture notebook computer products and related parts, the Company and Compal are respectively granted call and put options which entitle the Company to purchase from Compal and Compal to sell to the Company the 49% Compal’s interests in the JV Co. The call and put options will be exercisable at any time after October 1, 2019 and October 1, 2017 respectively. The exercise price for the call and put options will be determined in accordance with the joint venture agreement, and up to a maximum of US$750 million.

The financial liability that may become payable under the put option is initially recognized at fair value within other non-current liabilities with a corresponding charge directly to equity, as a put option written on non-controlling interest.

The put option liability shall be re-measured at its fair value resulting from the change in the expected performance of the JV Co at each balance sheet date, with any resulting gain or loss recognized in the consolidated income statement. In the event that the put option lapses unexercised, the liability will be derecognized with a corresponding adjustment to equity.

(d) Government incentives and grants received in advance by certain group companies included in other non-current liabilities mainly relate to research and development projects and construction of property, plant and equipment. These group companies are obliged to fulfill certain conditions under the terms of the government incentives and grants. The government incentives and grants are credited to the consolidated income statement upon fulfillment of those conditions.

## 12 Borrowings

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Current liabilities | | |
| Short-term loans (i) | **741,359** | 745,815 |
| Non-current liabilities | | |
| Term loan (ii) | **396,695** | 396,365 |
| Long term notes (iii) | **2,092,558** | 2,108,747 |
| | **2,489,253** | 2,505,112 |
| | **3,230,612** | 3,250,927 |

(i) Short-term loans primarily comprised a US$1,200 million 5-Year loan facility (comprising US$800 million short term) entered into in December 2013 which has been utilized to the extent of US$400 million as at June 30, 2016 (March 31, 2016: US$400 million), and a US$300 million 5-Year loan facility entered into in May 2015 which has been utilized to the extent of US$300 million as at June 30, 2016 (March 31, 2016: US$300 million). The majority of the short-term bank loans are denominated in United States dollar.

(ii) Term loan primarily comprised a US$1,200 million 5-Year loan facility (comprising US$800 million short term) entered into in December 2013, and has been drawn down to the extent of US$400 million as at June 30, 2016 (March 31, 2016: US$400 million).

(iii) On May 8, 2014, the Group completed the issuance of 5-Year US$1.5 billion notes bearing annual interest at 4.7% due in May 2019; and on June 10, 2015, the Group completed the issuance of 5-Year RMB4 billion notes bearing annual interest at 4.95% due in June 2020. The proceeds have been used for general corporate purposes including working capital, and acquisition activities.

The exposure of all the borrowings of the Group to interest rate changes and the contractual repricing dates as at June 30, 2016 and March 31, 2016 are as follows:

| | **June 30, 2016** | March 31, 2016 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Within 1 year | **741,359** | 745,815 |
| Over 1 to 3 years | **1,890,125** | 396,365 |
| Over 3 to 5 years | **599,128** | 2,108,747 |
| | **3,230,612** | 3,250,927 |

## 13 Share capital

| | **June 30, 2016** | | March 31, 2016 | |
|---|---|---|---|---|
| | ***Number of shares*** | ***US$'000*** | *Number of shares* | *US$'000* |
| *Issued and fully paid:* | | | | |
| Voting ordinary shares: | | | | |
| At the beginning and end of the period/year | **11,108,654,724** | **2,689,882** | 11,108,654,724 | 2,689,882 |

## 14 Reconciliation of profit before taxation to net cash generated from/(used in) operations

| | **3 months ended June 30, 2016** | 3 months ended June 30, 2015 |
|---|---|---|
| | ***US$'000*** | *US$'000* |
| Profit before taxation | **205,601** | 51,831 |
| Share of (profits)/losses of associates and joint ventures | **(9,837)** | 1,558 |
| Finance income | **(6,140)** | (9,010) |
| Finance costs | **55,477** | 51,041 |
| Depreciation of property, plant and equipment and amortization of prepaid lease payments | **69,361** | 60,202 |
| Amortization of intangible assets | **123,644** | 128,558 |
| Share-based compensation | **33,070** | 28,430 |
| Gain on disposal of property, plant and equipment and prepaid lease payments | **(131,712)** | (2,922) |
| Net gain on disposal of available-for-sale financial assets | **-** | (1,653) |
| Loss on disposal of intangible assets | **217** | - |
| Fair value change on financial instruments | **(16,682)** | (9,510) |
| Decrease in inventories | **59,845** | 128,242 |
| (Increase)/decrease in trade receivables, notes receivable, deposits, prepayments and other receivables | **(301,816)** | 142,574 |
| Increase/(decrease) in trade payables, notes payable, provisions, other payables and accruals | **57,827** | (726,289) |
| Effect of foreign exchange rate changes | **39,364** | 9,841 |
| Net cash generated from/(used in) operations | **178,219** | (147,107) |

## PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the three months ended June 30, 2016, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities, except that the trustee of the long-term incentive program of the Company purchased 51,432,738 shares from the market for award to employees upon vesting. Details of the program are set out in the 2015/16 annual report of the Company.

## REVIEW BY AUDIT COMMITTEE

The Audit Committee of the Company has been established since 1999 with the responsibility to assist the Board in providing an independent review of the financial statements, risk management and internal control systems. It acts in accordance with its terms of reference which clearly deal with its membership, authority, duties and frequency of meetings. Currently, the Audit Committee is chaired by an independent non-executive director, Mr. Nicholas C. Allen, and comprises three members including Mr. Allen and the other two independent non-executive directors, Ms. Ma Xuezheng and Mr. William Tudor Brown.

The Audit Committee of the Company has reviewed the unaudited financial results of the Group for the three months ended June 30, 2016. It meets regularly with the management, the external auditor and the internal audit personnel to discuss the accounting principles and practices adopted by the Group and internal control and financial reporting matters.

## COMPLIANCE WITH CORPORATE GOVERNANCE CODE

None of the directors of the Company is aware of any information that would reasonably indicate that the Company is not, or was not during the three months ended June 30, 2016, in compliance with the code provisions of the Corporate Governance Code and Corporate Governance Report (the "**CG Code**") as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, with the exception that the roles of the chairman of the Board (the "**Chairman**") and the chief executive officer of the Company (the "**CEO**") have not been segregated as required by code provision A.2.1 of the CG Code.

The Board is of the opinion that it is appropriate and in the best interests of the Company at the present stage for Mr. Yang Yuanqing ("**Mr. Yang**") to continue to hold both the positions as it would help to maintain the continuity of the strategy execution and stability of the operations of the Company. The Board comprising a vast majority of independent non-executive directors meets regularly on a quarterly basis to review the operations of the Company led by Mr. Yang.

The Board also appointed Mr. William O. Grabe as the lead independent director ("**Lead Independent Director**") with broad authority and responsibility. Among other responsibilities, the Lead Independent Director will chair the Nomination and Governance Committee meeting and/or the Board meeting when considering (i) the combined roles of Chairman and CEO; and (ii) assessment of the performance of Chairman and/or CEO. The Lead Independent Director will also call and chair meeting(s) with all independent non-executive directors without management and executive director present at least once a year on such matters as are deemed appropriate. Accordingly, the Board believes that the current Board structure with combined roles of Chairman and CEO, the appointment of Lead Independent Director and a vast majority of independent non-executive directors will provide an effective balance on power and authorizations between the Board and the management of the Company.

By Order of the Board
**Yang Yuanqing**
*Chairman and*
*Chief Executive Officer*

August 17, 2016

*As at the date of this announcement, the executive director is Mr. Yang Yuanqing; the non-executive directors are Mr. Zhu Linan, Mr. Zhao John Huan and Mr. Gordon Robert Halyburton Orr; and the independent non-executive directors are Dr. Tian Suning, Mr. Nicholas C. Allen, Mr. Nobuyuki Idei, Mr. William O. Grabe, Mr. William Tudor Brown, Ms. Ma Xuezheng and Mr. Yang Chih-Yuan Jerry.*