ScanSource, Inc. **2016 Annual Report**

scansource®

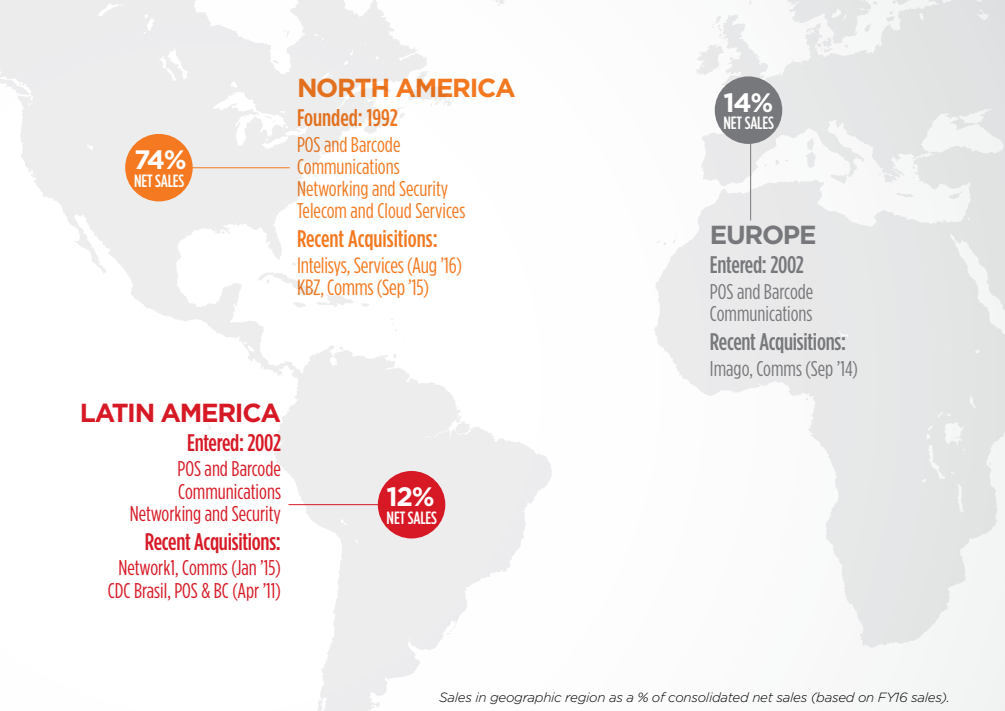**2016** ANNUAL REPORT

scansource®

ScanSource, Inc. (NASDAQ: SCSC) is a leading global provider of technology products and solutions, focusing on point-of-sale, barcode, physical security, video, voice, data networking, and technology services. ScanSource's teams provide value-added solutions and operate from two segments:

- Worldwide Barcode, Networking and Security
- Worldwide Communications and Services

ScanSource is committed to helping its resellers and sales partners choose, configure, and deliver the industry's best solutions across almost every vertical market in North America, Latin America, and Europe. In August 2016, ScanSource entered the recurring revenue telecom and cloud services market through its acquisition of Intelisys, the industry's leading technology services distributor.

Founded in 1992, ScanSource is headquartered in Greenville, South Carolina and ranks #685 on the Fortune 1000.

NORTH AMERICA
Founded: 1992
POS and Barcode
Communications
Networking and Security
Telecom and Cloud Services
Recent Acquisitions:
Intelisys, Services (Aug '16)
KBZ, Comms (Sep '15)

74% NET SALES

EUROPE
Entered: 2002
POS and Barcode
Communications
Recent Acquisitions:
Imago, Comms (Sep '14)

14% NET SALES

LATIN AMERICA
Entered: 2002
POS and Barcode
Communications
Networking and Security
Recent Acquisitions:
Network1, Comms (Jan '15)
CDC Brasil, POS & BC (Apr '11)

12% NET SALES

Sales in geographic region as a % of consolidated net sales (based on FY16 sales).

HEADQUARTERED
EST 1992
GREENVILLE, SC

NASDAQ
SCSC

45 OFFICES
WORLDWIDE

2300+ EMPLOYEES

imago
ScanSource

INTELISYS
Independence. No limits.

network1
a scansource company

scansource® catalyst

scansource® communications

scansource® networking and security

scansource® pos and barcode

TO OUR **SHAREHOLDERS:**

In fiscal 2016, we made important decisions that will continue to move ScanSource forward as a leading global provider of technology solutions. We remain committed to serving as a trusted advisor to our resellers and helping them drive growth with products and services that meet the evolving needs of their end-user customers. We continue to solidify our supplier partnerships by providing them with access to a broad range of customer channels. This approach gives us a strong competitive advantage as we operate our business in specialty technology markets around the world.

During the past 15 months, we continued to execute our strategic plan, including the implementation of our enterprise resource planning (ERP) system in North America, two strategic acquisitions, and a first step in developing a recurring revenue services strategy for our partners and ScanSource.

Global Platform for Growth. We began the fiscal year with the successful implementation of our SAP ERP system in North America in July 2015. Our scalable, flexible, robust system has the capacity to support organic growth and future acquisitions. Now, more than 80% of our business flows through our globally designed SAP ERP system. Additionally, the platform allows us to develop innovative digital tools for our partners' business growth.

Enhanced Profitable Growth Opportunities from Strategic Acquisitions. In evaluating M&A opportunities, we are excited to find target companies that will increase our capabilities in higher margin, higher growth areas.

been in enterprise wireless and security products. KBZ brought video conferencing expertise, new services capabilities, and a specialized public sector team. The ScanSource and KBZ teams coordinated their strengths to ensure a smooth integration for Cisco and our resellers. This combination and a strong balance sheet have led to accelerated growth and profitability in these markets.

In October 2015, we assembled an internal team to develop a services strategy to help our resellers and ScanSource build high margin, recurring revenues from services offerings. After the fiscal year end, on August 29, 2016, we completed the acquisition of Intelisys, the leading telecom and cloud services distributor whose services-based distribution model complements our products-based distribution model. The acquisition is another important step in our strategic plan, as it provides opportunities for resellers to generate new monthly recurring revenue streams with fully vetted, carefully selected, telecom and cloud services offerings. ScanSource resellers will have opportunities to sell connectivity along with products, and Intelisys sales partners will be able to sell products and solutions from the ScanSource vendor community. We are excited about these prospects for new business and recurring revenue for ScanSource.

Financial Strength and Flexibility. Our balance sheet remains very strong. It provides us with considerable flexibility to execute our capital allocation plan, which includes organic growth, strategic acquisitions, and share repurchases. For fiscal 2016, we generated operating cash of $52 million, invested $70 million in acquisitions, and

Mike Baur
CEO, ScanSource, Inc.

In September 2015, we completed our acquisition of KBZ, Cisco's leading collaboration growth distributor in the United States. The addition of KBZ complemented our existing Cisco business and added incremental resellers and markets, such as state, local, and federal government. ScanSource's Cisco business had primarily

returned $100 million to shareholders through share repurchases. As of June 30, 2016, our leverage totaled approximately 0.13 times trailing 12-month EBITDA.

We consider leverage of at least one times EBITDA to be a target for a more optimal capital structure. On August 29, 2016, we paid the $83.6 million

initial purchase price (representing 52% of the total purchase price) for our acquisition of Intelisys, which was funded with additional borrowings.

For fiscal 2016, we earned a return on invested capital (ROIC) of 13.3%.[1] We measure our performance using ROIC, and earning a mid-teens ROIC remains a key financial goal. Our financial objectives for fiscal 2017 include organic sales growth, margin expansion from services offerings including the Intelisys acquisition, and a significant improvement in ROIC from the prior year.

I want to thank our talented employees, whose passion, energy, and commitment to the Company make a difference every day, enabling ScanSource to remain a leader in the markets we serve. Our employees are critical to making us trusted advisors to our resellers and suppliers – which is the key to our success.

Thank you to our shareholders for your support and your investment in ScanSource. We look forward to the opportunities ahead as we strive to deliver value to all of our constituents.

Sincerely,

Michael L. Baur
CEO, ScanSource, Inc.

September 30, 2016

What is the strategic rationale for the acquisition?

Intelisys is the industry's leading technology services distributor of telecommunications and cloud services. Like ScanSource, Intelisys exclusively uses a two-tier model. By acquiring the market leader, ScanSource adds services capabilities and enters the high-growth, recurring revenue telecom and cloud services market. Today almost every device ScanSource delivers has a connectivity requirement. We see opportunities for resellers and sales partners to sell the total solution of hardware and software products along with the connectivity.

What is the market for telecom services?

In the United States, small- and medium-sized businesses spend an estimated $150 billion on telecom services. Approximately 10% of this market is currently served by the indirect channel. This is a large and growing addressable channel market for Intelisys and its sales partners. In addition, the market dynamics favor Intelisys' two-tier, services-based business model with an expected growth of business opportunities for the indirect channel.

Many vendors and distributors, including ScanSource, have been providing support for resellers to build a recurring revenue stream, but the acquisition of a master agent by a distributor is unprecedented. How was that decision made?

At ScanSource, we have been looking at ways for the reseller channel to benefit from the power of recurring revenues. During our research, it became clear that Intelisys, a master agent, provides an excellent entry point into the recurring revenue telecom and cloud services market. In addition, the Intelisys sales partner channel will benefit from having access to products and solutions from ScanSource vendors. We are creating a unique model with the convergence of a value-added distributor and a master agent – a win-win for both channels.

Q&A
Intelisys acquisition explained.

What will ensure the success of ScanSource and Intelisys partners?

We share a remarkable combination of strategies, views, and culture. We both use a two-tier business model and believe that we are only successful if our customers are successful. ScanSource and Intelisys partners will have access to training, sales, and marketing enablement programs, as well as the tools and platforms that help partners build recurring revenue streams.

[1] See pages 24 and 25 for additional information on this non-GAAP measure, including a reconciliation and our reasons for providing this measure and limitations on its use.

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