



Final Report (unaudited)
Effnet Group AB (publ)
Fiscal Year 1999



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Final Report January-December 1999

- **Net sales totalled KSEK 2,272 (KSEK 75).**
- **An operating deficit of KSEK - 49,805 (KSEK - 17,822) was recorded.**
- **A deficit of KSEK - 48,493 (KSEK - 17,633) after financial items is reported.**
- **The Group had 52 employees, an increase of 25.**
- **Effnet's ROC PCI-Card product was the winner of the prestigious European Information Societies Technology Grand Prize, amounting to 200,000 Euros.**
- **In November, a five-for-one share split was carried out.**
- **In the fourth quarter, a VAR (Value Added Reseller) agreement was signed with HSD Consult GmbH, one of the leading system integrators and Internet Service Providers in the German market.**
- **In December, a directed share issue aimed at several Swedish and international institutional investors was carried out. The issue, which was heavily over-subscribed, resulted in a capital infusion of KSEK 364,000 net, after costs.**
- **At year-end the Technology Partner Program (TPP) for licensing of Effnet's technology in the USA was launched.**

Effnet develops, markets, sells and distributes network products and network technology designed to resolve bottlenecks in Internet communication, thereby creating maximum benefit to the customer. Effnet markets its technology in three ways: as own-brand products, under OEM agreements and via licensing the Company's technology to other operators in the network industry. During 1999, Effnet changed from being a specialist development company into a commercial operator in the network market. The Company is now entering a phase in which the focus is on marketing and sales. Effnet's long-term goal is to become one of the world's leading operators in resolving present and future bottlenecks in Internet communication. Today, Effnet is represented in four locations; Stockholm and Luleå in Sweden, and Boston and Mountain View, California, in the USA. Effnet Group AB's shares are listed on the *Nya Marknaden* (New Market) list of the OM Stockholm Stock Exchange. The Company has 52 employees.

Major events during the financial year

- On 6 April, Effnet shares were launched on the *Nya Marknaden* (New Market) list of the OM Stockholm Stock Exchange following a new share issue totalling KSEK 72,600. The launch price for the shares was SEK 165. At year-end, the share price had risen to SEK 1,525 before the five-for-one split, an increase of 824 percent.
- An OEM (Original Equipment Manufacturers) agreement was signed with Ericsson Radio Systems AB. Under the agreement, Effnet will deliver firewall solutions for Ericsson Radio's IP-based local area network systems.
- An independent test nominated the Effnet FTC500FR firewall as the fastest firewall in the market. The test was conducted by the institute KeyLabs, in Utah, USA.
- A VAR (Value Added Reseller) agreement was signed with Cygate AB. As a result, Effnet has sales channels in Sweden, Finland, Denmark, Poland and the Baltic Region.

Major events after the financial year-end

- In January 2000, Effnet opened a new office in Mountain View, California. With this, Effnet has offices in the two most attractive regions in the USA for IT and network technology - the Boston area and California.
- In January 2000, Effnet received a favourable final report from the Swedish Patents and Registration Office with regard to Effnet's patent application for its first-generation firewall technology. This indicates that a national patent for Sweden is to be granted shortly.
- Effnet AB will be the main supplier of firewalls to Figuration AB for that company's development of broadband networks in Sweden. The agreement also covers collaboration in defining and evaluating new technical solutions and new products for the new broadband market. The founders and personnel of Figuration AB have been involved in the design, building, commissioning and maintenance of the new generation of broadband networks. This recently established company has leading-edge expertise in speech, telecommunication, data communications and network technologies. Figuration AB's customers include Framfab and Bredbandsbolaget.

The network market

In 2001, sales in the global network market are expected to be at least 500 SEK billion, according to the research firm Forrester Research. This dynamic growth follows from the explosive expansion of the Internet, and from the extensive - in some cases global - networks being built up by many companies. There is also strong demand for systems designed for application within a particular network, for example inside a company or between a company and its external partners.

Over the next few years, electronic commerce, mobile Internet and expansion in broadband will drive up the rate of increase in the number of users and the volume of information on the Internet. As this expansion progresses, new bottlenecks will be discovered, ones that will be very difficult to resolve using traditional technology. These bottlenecks identify Effnet's opportunities for business.

The router market

Total sales in the router market in 1999 are estimated at USD 8.4 billion, according to the International Data Corporation, IDC. In 2000, sales are expected to reach around USD 9 billion. North America is the biggest market, but Europe and Asia are steadily reducing in the USA's lead.

Traditionally, the router market is divided into three segments: high-end, mid-range and low-end. As far as the cheapest products in the low-end segment are concerned, high potential for growth is anticipated for the next five years. One reason for this is that many small businesses are demanding cost-efficient solutions for connecting to the Internet. As the complexity of applications grows, as electronic commerce becomes more widespread and as broadband expansion gathers pace, the demand for performance in the low-end segment will expand sharply.

With this development, demand for Effnet's technology and products will grow in pace with the expansion of electronic commerce, mobility, broadband and increasingly complex applications.

The firewall market

In 1999, total sales of software for firewalls are estimated at MUSD 663 million throughout the world, according to the research firm IDC. In 2000, sales are expected to total around MUSD 861 million. Average annual growth is forecast at around 30 percent over the next five years. It is estimated that in 2000 Western Europe will account for roughly 26 percent of world sales, corresponding to approximately MUSD 224. Western Europe and Asia are the markets in which strongest growth is anticipated over the next two years.

Market trends

The overall trend evident is that all types of communication will be conducted via the Internet. This applies to speech, video, pictures, text and other forms of information, whether via fixed or mobile communication devices. As a result, the pace of growth - already explosive - will further quicken - in terms of both the number of connected units and the complexity of the applications. In addition, the need for systems of security will expand sharply.

Convergence between datacom and telecom

To most companies in both datacom and telecom, the ability to offer systems in both telephony and data is becoming increasingly important. This is one explanation for the many mergers and strategic joint ventures in the past year between data communication and telecommunication companies.

In the near future, there will be no distinction between speech and other forms of communication. Every kind of communication will be possible via the Internet.

Mobile Internet

In Sweden, several companies are already offering wireless connection to the Internet. Systems are also available for wireless connection to internal networks. Moreover, the trend is increasingly towards mobility: users should always be able to be connected, wherever they may be. WAP technology and other technologies serving mobile Internet applications will dramatically change everyday life, for both businesses and private individuals.

Electronic commerce

As both fixed and mobile use of the Internet expands, electronic commerce will become more and more common between businesses and between businesses and private individuals. In that situation, adequate security will be vital, without performance having to be sacrificed.

Broadband systems

Sweden is a leader in broadband systems, especially for the home. Over the next few years, the tempo of expansion in broadband will further accelerate. This will enable all communication to and from the home to be carried via the Internet, whether in the form of video, speech, pictures, text or other modes of communication. This will bring greater demands on security and so on the level of performance delivered by security solutions.

Implications to Effnet

Because Effnet's technologies and products are designed to resolve bottlenecks in the Internet, demand for the Company's products will show continuous growth. The expansion of electronic commerce, mobile Internet and broadband systems will generate further bottlenecks in the Net, which will fuel the demand for Effnet's products. This will apply to products sold under the Company's own brand, as well as via OEM systems and licensing.

Fourth quarter 1999

Net sales by Effnet during the fourth quarter totalled KSEK 1,090, an increase of 84 % over sales in the third quarter. The Company recorded an operating deficit of KSEK -15,194, compared to KSEK -12,546 in the preceding quarter. The change essentially reflects the continued expansion of Effnet's sales and market organization in Europe and the USA.

During the fourth quarter, management resources were strengthened. Recruited were two key people from Cisco Systems: Roger Undhagen, as Managing Director at Effnet AB, and Karin

Bjurel, as Director of Sales and Market at Effnet AB. In addition, Jan Holmgren was recruited from Ericsson Radio Systems AB, as Director of Support and Logistics with a global remit.

During the fourth quarter, Effnet focused its efforts on building broadband capabilities. It engaged in negotiations with, among others, Figuration AB, a company started by the people who commissioned and were responsible for Bredbandsbolaget's network. Figuration AB's customers include Framfab and Bredbandsbolaget. These negotiations became protracted. This resulted in agreement not being able to be concluded until February 2000. A further consequence of the delay was that the revenue forecast originally for this business in quarter 4 has been carried over to the year 2000.

In the North American market, the Company during the fourth quarter intensified commercial discussions with potential licensees for its technology. These discussions are expected to lead to signed agreements during the first half of the year 2000.

Total sales

Effnet markets its technology platform in three ways: as products under the Company's own brand, by allowing our products to be used in more extensive system solutions and via licensing our technology to other operators in the network market.

In 1999, the Group's net sales increased by KSEK 2,197 to KSEK 2,272. Of net sales, products sold under the Company's own brand represented KSEK 1,699. Sales of our products to major system customers accounted for the remainder, KSEK 573. All sales were to customers in Europe.

Financial result

The Group reports an operating result of of KSEK - 49,805 (KSEK - 17,822). The Group's result after financial items was KSEK - 48,493 (KSEK - 17,633).

Sales and marketing costs increased steeply during 1999 and amount to KSEK 23,395 (KSEK 2,402), as a result of the build-up of a sales and market organization in the USA as well as in Europe. The expansion developed according to plan.

The costs of product and technology development, written off on an ongoing basis, amounted to KSEK 21,309 (KSEK 9,768). Major areas of investments were further development of Effnet's technology platform and customer-driven development on behalf of strategically important customers.

Under other income/expenses is carried the value of the prize, 200 000 Euros, which Effnet was awarded in the prestigious competition "European Information Societies Technology Grand Prize".

Financial position

Effnet's equity/assets ratio on 31 December 1999 was 97.9 % (67.4 %). The Group's liquid assets total KSEK 386,979 (KSEK 5,658).

Investments

Investments during the period amounted to KSEK 1,510 (KSEK 1,094), comprising above all computer equipment.

Dividend

Because Effnet is in a phase of rapid expansion which is expected to continue over the next few years, the Board proposes to the Annual General Meeting that no dividend be paid in respect of the 1999 financial year.

Personnel

The number of employees at the close of the period totalled 52 (27). The average number of full-year employees at the close of the period was 37 (15), including 4 (1) in the USA.

Outlook

Effnet's strategy for becoming a leading global supplier of technology to resolve bottlenecks in Internet-based communication is:

- to develop its Technology Partner Program (TPP), aimed at strategic global partners in order to, through them, reach out on a broad front with our technology
- to establish a global reseller network for products sold under the Company's own brand with initial focus on Europe
- to continue the development of the technology and reinforce our leading position.

Effnet's long-term financial objectives are to increase sales faster than our competitors and to reach a positive operating margin in excess of 20 percent.

During the next financial year, Effnets goals are:

- to sign up at least three global partners to its TPP
- to establish reseller and distribution channels in strategic markets in Europe. Initially, Effnet will establish its own local representation in the United Kingdom, the Benelux Countries and France. In addition, further sales channels are planned in Sweden and Germany
- to double the number of personnel in the Europe and North America market organizations
- to file at least three patent applications
- to build up a global support organization
- to obtain listing on the Stockholm Stock Exchange O-list
- to obtain listing on Nasdaq

Financial calendar

Effnet Group AB's full annual report will be available on 21 March at Effnet's office at Gustavslundsvägen 151G, Alviks Strand, Bromma, Greater Stockholm. At the same time, it will be distributed to all shareholders.

Annual General Meeting	13 April	2000
Interim Report, January - March	4 May	2000
Interim Report, January - June	17 August	2000
Interim Report, January - September	2 November	2000

This Final Report has not been audited by the Company's auditor.

Stockholm, 15 February 2000

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Consolidated Profit and Loss Account (KSEK) (Summary)	1999 January – December	1998 January - December	1997 September - December
Net sales	2,272	75	0
Cost of goods sold	-714	-53	0
Gross profit	1,558	22	0
Selling expenses	- 23,395	- 2,402	0
Administrative expenses	- 8,944	- 5,674	- 251
Research and development costs	- 21,309	- 9,768	- 1,700
Other operating income/expenses	2,285	0	13
Operating result	- 49,805	- 17,822	- 1,938
Financial items, net	1,312	189	2
Result after financial items	- 48,493	- 17,633	- 1,936
Tax	93	- 12	0
Minority interest in result for the year	11	0	0
Result for the year	- 48,389	- 17,645	- 1,936

Consolidated Balance Sheet (KSEK) (Summary)	1999 31 December	1998 31 December	1997 31 December
Assets			
Fixed assets	1,798	793	0
Current assets	392,393	8,684	4,560
Total assets	394,191	9,477	4,560
Shareholders' equity and liabilities			
Shareholders' equity	385,922	6,392	3,416
Minority interest	58	0	0
Provisions	95	2	0
Current liabilities	8,116	3,083	1,144
Total shareholders' equity and liabilities	394,191	9,477	4,560

Consolidated Cash Flow Statement (KSEK)	1999	1998	1997
	January-December	January-December	September-December
Cash flow from day-to-day operations	- 48,184	- 17,427	- 1,936
Changes in working capital	2,645	- 356	412
Investments	- 1,177	- 1,013	0
Financing	428,037	20,625	5,351
Change in liquid assets	381,321	1,829	3,827

Per-share data (adjusted to reflect new share issues)¹ (Amounts in SEK)	1999	1998	1997
	31 December	31 December	31 December
Number of shares at close of period	10,410,905	7,010,905	5,882,000
Average number of shares	8,419,274	6,334,325	5,073,500
Earnings per share	- 5.75	- 2.78	- 0.38
Earnings per share after full dilution	- 5.38	- 2.63	- 0.38
Shareholders' equity per share	45.84	1.01	0.67
Shareholders' equity per share after full dilution	42.91	0.95	0.67

¹ Per-share data for 1998 and 1997 refers to the Effnet Holding AB-Group.