



Interim Report  
Effnet Group AB (publ.)  
*January-June 2000*



## **Effnet Group AB (publ.)**

### **Interim Report for January-June 2000**

- Net sales totalled KSEK 3 716 (589).
- An operating deficit of KSEK -57 441 (-22 065) was recorded.
- A deficit of KSEK -49 186 (-22 027) after financial items was reported.
- The company had 79 employees at the end of June, an increase of 34.
- To fully capitalize on the global market opportunities a new US-based CEO, CTO and Chairman of the Board have been appointed. Tony Svensson, currently CEO of Effnet, Inc., has been appointed CEO of Effnet Group AB. Svensson will keep his position as CEO of Effnet, Inc., and will remain in Silicon Valley. Norman Rasmussen, member of the Board for over two years, has been elected Chairman of the Board. Dr. Stephen Pink, Professor in Computer Science and one of the Company founders has been appointed CTO for Effnet Group AB. Dr. Pink is based in Tucson, Arizona.
- The acquisition of Wkit Online AB (company name changed in June to Wkit Security AB) has been finalised. The final purchase price is 330,000 shares in Effnet. Wkit's business is based on data security-related services and products. The company has 17 employees in two divisions, one for services and one for products. Wkit anticipates total sales of KSEK 30 million for the 2000/2001 (ending 30 June 2001) according to the acquisition agreement.
- Effnet announced during second quarter a partnership with the global independent semiconductor supplier STMicroelectronics. The agreement allows STMicroelectronics to provide high performance network technology with Effnet's award winning IP packet-processing technology integrated with their own products. The partnership should be considered as the starting point of a long-term relationship within the framework for the Effnet Technology Partner Program, TPP.
- In May, a split was implemented, involving the issue of five new shares for each original share.

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Effnet operates in four locations: Stockholm, Luleå, Håverud and Mountain View, California. Shares in Effnet Group AB are quoted on the "New Market" List, Stockholm.

To find out more about Effnet, please visit our Web site at: <http://www.effnet.com/>

## **The Network Market**

The Internet, as a network of networks, has changed the rules of the game for manufacturers of network equipment. Prior to 1994, manufacturers of servers, routers, switches, processor chips and related equipment met the needs of the market by designing and building products that offered varying levels of speed. In fact, the need for speed varied widely among groups of PC users. In that market, which was dominated by LAN (local area networks) and WAN (wide area networks), manufacturers could offer levels of security that were "good enough" for the needs of these isolated groups of computers.

In 1994, however, with the first commercial Internet browser and the birth of the World Wide Web, millions of new users instantly became virtually "connected" to each other.

Additionally, the ability to view graphics on the formerly text-only Internet created a deep demand for bandwidth. The result has been the gradual awareness of the need for both efficient speed and optimal data security without sacrifice on either side of the equation. This accelerated bandwidth, combined with the growth in broadband computing, exponentially multiplies the demand for fast and secure Internet access.

## **Effnet in the Network Market**

Until recently, manufacturers of networking components focused either on speed or on security. Today, the industry is seeing a convergence of these two requirements.

With the tag line "You can never be too fast, or too secure", Effnet brings to the market network products, technologies and services that resolve bottlenecks and enhance security in Internet communications. The long-term goal is to become a leading provider of security and core technologies for the Internet economy.

Effnet offers patented and award winning technologies through its own branded products, licensing and security services. During the last twelve months, Effnet evolved from a development company into a commercial operator shipping product and signing technology-licensing contracts. Today, Effnet operates in four locations: Stockholm, Luleå, Håverud and Mountain View, California.

Effnet's purpose is clear, to maximize shareholder value through its unique value proposition and superior customer value.

## **Effnet's Approach**

Effnet markets its technology through several entry points in the Internet economy.

For example, during the first and second quarters, the Company signed its first round of licensing agreements with leading independent network processor and communication chip vendors in North America and Europe. Two steps are normally involved in a licensing arrangement. In the first step, Effnet's technology is adapted to the customer's product. In the second, which takes place after the adaptations have been tested and accepted, the solution is implemented into the finished product. Effnet receives payment in the form of licensing fees and royalties.

Eventually, these chips will find their way into products that drive the Internet, and quite possibly back into Effnet's own future products.

Effnet provides its technologies and services to vendors of networking equipment that use network processor and communication chips in their products. Furthermore, Effnet provides its solutions to customers using Broadband connections, Mobile Internet and E-commerce.

In order to strengthen Effnet's security focus, the Company has acquired the data security company Wkit Security AB. The acquisition provides Effnet with:

- An increased customer base
- A broader product portfolio
- A strategically complementary service to the Company's technology and product offerings

In short, the Company is becoming well positioned to build a brand name that equates with Internet speed and security.

## **Sales**

Effnet's net sales during the period totalled KSEK 3 716 (589).

## **Second Quarter 2000**

During the second quarter, Effnet's sales amounted to KSEK 1 776 (326).

In North America, the Company launched the Technology Partner Program (TPP) and signed its first licensing agreement with a leading independent network processor and communication chip vendor. The Company is currently in dialog with several additional potential technology licensees. Effnet also consolidated its North American presence to the U.S. West Coast. By moving into modern offices and recruiting key talent in the heart of Silicon Valley, Effnet strengthened its position as a global high-tech player.

We signed our first European licensing agreement with STMicroelectronics, a world leading semiconductor company. The agreement allows STMicroelectronics to provide high performance network technology with Effnet's award winning IP packet-processing technology integrated with their own products. In line with our objectives this year, channel partners have been added. The sales and marketing organization has been strengthened with the addition of four new positions. Marketing has been focused on campaigns supporting the sales force and generating leads, as well as corporate branding.

## **Financial Results**

The Group reports an operating deficit of KSEK -57 441 (-22 065). The Group's result after financial items was a deficit of KSEK -49 186 (-22 027).

The strengthening of the sales and marketing organization in Europe and North America continued according to plan. Expenses has increased by KSEK 3 495 compared to first quarter 2000 reflecting mainly the personnel reinforcement and extended marketing/PR activities. Selling and marketing expenses amounted to KSEK 20 023 (7 232).

The costs of product and technology development, reported on a current basis, amounted to KSEK 16 366 (11 672). The development of Effnet's technology platform continues, but with an increased focus on data security after the acquisition of Wkit Security AB. A more aggressive patent strategy to promote Effnet's technology has resulted in higher expenses compared to January-June 1999.

Administrative expenses have risen compared with the same period last year. The change very much reflects the build-up of the finance organization. The administrative expenses include a non-recurring cost of KSEK 2 995 due to reservation for change in management.

The Wkit acquisition resulted in goodwill of KSEK 184 759, which is depreciated over ten years. Goodwill depreciation for the second quarter amounted to KSEK -4 651 and is reported under other operating income/expenses.

## **Financial Position**

Effnet's equity-to-assets ratio at 30 June 2000 was 96.4% (88.4%). Liquid assets, including current investments, totalled KSEK 340 597 (49 824).

## **Capital Expenditures**

Capital expenditure during the period totalled KSEK 2 009 (651) and consisted mainly of expenditure on computer equipment.

## **Personnel**

The number of employees at the close of the period totalled 79 (45). The average number of full time employees at the close of the period totalled 68 (33).

## **Events Following the Close of the Second Quarter**

Roger Undhagen, the CEO of the Swedish subsidiary Effnet AB, resigned.

Mats Olsson, board member since January 1999, has just resigned from the board citing the increased emphasis on internationalizing the company and the board. The company is currently in discussions with several Silicon Valley high technology veterans about joining the board.

## **Outlook for 2000/2001**

The outlook can best be assessed by looking at the major deals under active consideration or development in our three lines of business.

- In the firewall/router business, our largest single contract is with Ericsson Radio Systems AB, which involves supplying firewalls; that deal was signed in late 1999, with high expectations for increased revenue this year. We have had to push our revenue expectations out at least six months because of software problems at our end, but these problems were fixed with a new software release in late May.
- We have a half dozen licensing deals under active discussion. Our goal is that two will materialize as contracts in this fiscal year.
- In the security business, there are several large projects being actively pursued by senior management of Wkit and Effnet Group AB. We have high hopes that at least one of these will be placed under contract this fiscal year.

## **Financial Calendar**

Interim Report, January - September      2 November    2000

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

Stockholm, 17 August 2000

Effnet Group AB (publ.)

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<b>Consolidated Profit and Loss Account</b>	<b>2000</b>	<b>1999</b>	<b>1999</b>
<b>(Summary) (KSEK '000)</b>	<b>January – June</b>	<b>January - June</b>	<b>January - December</b>
Net sales	3 716	589	2 272
Cost of goods sold	- 1 689	- 266	- 714
<b>Gross profit</b>	<b>2 027</b>	<b>323</b>	<b>1 558</b>
Selling expenses	- 20 023	- 7 232	- 23 395
Administrative expenses	- 18 456	- 3 483	- 8 944
Research and development costs	- 16 366	- 11 672	- 21 309
Other operating income/expenses	- 4 623	0	2 285
<b>Operating result</b>	<b>- 57 441</b>	<b>- 22 065</b>	<b>- 49 805</b>
Financial items, net	8 302	38	1 312
<b>Result after financial items</b>	<b>- 49 138</b>	<b>- 22 027</b>	<b>- 48 493</b>
Tax	- 48	0	93
Minority interest in result for the period	0	0	11
<b>Result for the period</b>	<b>- 49 186</b>	<b>- 22 027</b>	<b>- 48 389</b>

<b>Consolidated Balance Sheet (Summary) (KSEK '000)</b>	<b>2000</b>	<b>1999</b>	<b>1999</b>
	<b>30 June</b>	<b>30 June</b>	<b>31 December</b>
<b>Assets</b>			
Intangible fixed assets	180 139	0	0
Tangible fixed assets	6 374	1 238	1 798
Current assets	16 474	4 367	5 414
Cash & bank balances	340 597	49 824	386 979
<b>Total assets</b>	<b>543 584</b>	<b>55 429</b>	<b>394 191</b>
<b>Shareholders' equity &amp; liabilities</b>			
Shareholders' equity	524 061	49 018	385 922
Minority interest	0	0	58
Provisions	95	95	95
Current liabilities	19 428	6 316	8 116
<b>Total shareholders' equity &amp; liabilities</b>	<b>543 584</b>	<b>55 429</b>	<b>394 191</b>

<b>Consolidated Cash Flow Statement (KSEK '000)</b>	<b>2000</b>	<b>1999</b>	<b>1999</b>
	<b>January – June</b>	<b>January – June</b>	<b>January - December</b>
Cash flow from day-to-day operations	- 43 784	- 21 549	- 48 191
Changes in working capital	- 3 765	1 884	2 645
Investments	- 2 322	- 681	- 1 170
Financing	3 489	70 127	428 037
Change in liquid assets	- 46 382	49 781	381 321

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<b>Per-share data (adjusted to reflect new share issues) 2000</b>		<b>1999</b>	<b>1999</b>
<b>Amounts in KSEK</b>	<b>30 June</b>	<b>30 June</b>	<b>31 December</b>
Number of shares at close of period	52 679 525	46 054 525	52 054 525
Average number of shares	52 181 585	38 994 350	42 096 370
Earnings per share	- 0.94	- 0.56	- 1.15
Earnings per share after full dilution	- 0.84	- 0.54	- 1.08
Shareholders' equity per share	10.04	1.26	9.17
Shareholders' equity per share after full dilution	8.97	1.20	8.58

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