



Year End Report  
Effnet Group AB (publ)  
Fiscal Year 2000



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

### **Year End Report January-December 2000**

- A new strategy focusing on licensing the company's core asset, the Effnet Edge IP packet processing software was implemented in September
- Effnet's Technology Partner Program (TPP) acquired two partners under its three-phase (retainer, integration services and licensing fee) model for EffnetEdge™ technology
- The Swedish data security company, Wkit Security AB was acquired in April 2000. Wkit is a company specialized in IT security audit services and Compact Disk copy protection programs
- Wkit received important orders on disc copy protection from SDC DanDisc and on data security audits from Dubai Internet City during the second half of 2000
- Net sales KSEK 5,091 (2,272)
- An operating result of KSEK -142,804 (-49,805) was recorded excluding items effecting comparability which consist of a write-down of goodwill related to the Wkit acquisition amounting to KSEK -153,129
- Liquid assets of KSEK 274,956

#### **Events after the Financial Year-end**

- Effnet is currently in the process of negotiating two licensing contracts, one to a major chip supplier for wireless Internet technology. During the first period of 2001 we have seen a major increase in the number of potential customers both in the US and in Europe.
- Marika Philipson appointed new CFO. Marika has been working as acting CFO since the end of October. Prior to Effnet she was employed by the regional airline Skyways as VP of Finance and Administration.
- To be able to focus on developing the company's operations, management has decided to postpone the listing stock on the OM Stockholm Stock Exchanges O-list.
- Several month ahead of scheduled on development related to existing licensing contracts

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*Effnet innovates and licenses award-winning key technologies that resolve data speed, efficiency and security challenges in Internet Protocol (IP) networking and IT security. Effnet's modular IP packets processing technology -- the EffnetEdge™ Toolkit -- as well as its complete firewall and router technology for hardware manufacturers enable optimized performance. The wholly owned subsidiary, Wkit, offers data encryption and copy protection technologies, and security audit services for public and private sector companies. With more than 70 employees, the company operates in Stockholm, Luleå and Håverud, Sweden, and in Silicon Valley, California. Effnet Group AB shares are traded on Sweden's Nya Marknaden (symbol: EFFN). Read more about Effnet at [www.effnet.com](http://www.effnet.com). Read about Wkit at [www.wkit.com](http://www.wkit.com).*

## Operations

### Effnet Edge

In September, a change in business strategy was announced and implemented following a comprehensive review of the company's strengths and weaknesses. The new strategy focuses the company's efforts and resources on licensing the company's core asset, the Effnet Edge IP packet processing software.

In the new strategy, Effnet licenses its technology in two ways:

1. EffnetEdge™ technology integration — through Technology Partner Programs (TPP) licensing agreements — into chips, boards and systems manufactured by suppliers of both physical and wireless network components; and
2. Licensing of hardware-design instructions and the Effnet Firewall/Router Software Stack to manufacturers of OEM-branded routers and firewalls.

In short, the Company is building a brand name that equates with Internet speed, security and efficient design.

Effnet's licensed technology is the superior choice for developers facing a "make or buy" decision for their IP packet processing implementations. Effnet aims to become a recognized world leader in embedded technology solutions for networking, targeting component and equipment manufacturers who build the Internet and data communications infrastructure.

The growing need for faster network backbones and higher bandwidth will continue, along with the need for increasingly sophisticated packet processing. Market drivers are e-commerce, quality of service (QOS) and wireless communication.

Effnet entered into license agreements with three new partners during the year. Two are Technology Partner Program members (TPP) under the three-phase retainer, integration services and royalties licensing model for EffnetEdge™ technology. These two customers, including ST Microelectronics, are global suppliers of semiconductor products and/or network components. The third is the SDC DanDisc contract for Wkit's CD-ROM copy protection software.

Effnet was awarded a patent for its firewall technology and the underlying packet classification method from the Swedish patent office. The company also indicated its intent to pursue patenting of this technology in other countries.

One of Effnet's founders, Mikael Degermark, was awarded the Chester Carlsson Research Prize for 2000 for pioneering work in Internet development by inventing algorithms and IP header compression technologies.

The IP header compression technologies resulted in the establishment of international standards that enable efficient wireless Internet communications. Effnet announced its intention to incorporate the IP packet header compression standard in its Effnet Edge toolkit.

### Market situation

Effnet brings to market network products, technologies and services that resolve bottlenecks and enhance security in Internet communications. The goal is to become a *leading provider of core technologies* for the Internet infrastructure.

Effnet offers patented and award winning technologies. During the last quarter, Effnet has started aligning operations to support the new business strategy, and is pursuing extensive discussions with technology and software licensing prospects.

Effnet has identified four initial areas for its IP networking technology:

1. The network processor market (estimated at \$2.8 billion in 2004).
2. The rest of the total programmable communications processor market (estimated at \$16 billion in 2004).
3. The mobile communication market, with Ericsson, Motorola, Nokia, Samsung, Siemens and others.
4. The router and firewall markets, conservatively estimated at \$14 billion in 2004.

### **Wkit Securities**

Wkit Security AB was acquired in April 2000 through a stock swap. Wkit is a company specialized in IT security audit services and compact disk copy protection programs. The consideration was 1,650,000 newly issued Effnet shares.

Wkit Security signed a new five-year agreement for copy protection with the Danish CD manufacturers SDC, strengthening the existing partnership. The agreement is estimated to be worth MSEK10 per year, for a total of MSEK 50 over the contract period.

In December, Wkit Security AB obtained a substantial contract from Dubai Internet City (DIC) to perform security audits, including vulnerability analysis and penetrations on DIC's systems.

### **New Chairman and CEO, and new board members**

Norman Rasmussen, member of the Board for over two years, was elected Chairman of the Board. Tony Svensson, formerly CEO of Effnet, Inc., was appointed CEO of Effnet Group AB. Stephen Pink, Ph.D., Professor of Computer Communications at the University of Arizona, and one of the Company founders, was appointed Chief Technology Officer for Effnet Group AB.

At a special stockholders meeting in November two microelectronics executives from silicon valley were elected to the board. They are Magnus Ryde And Scott Macomber.

### **Fourth Quarter 2000**

Contrary to announced expectations no licensing contract were definitively consummated in the fourth quarter. The business has not disappeared; there are simply delays at play.

Net sales amounted to KSEK 1,062 during the fourth quarter. The company reported an operating result of KSEK -43,843 compared with -41,520 during the third quarter, excluding items effecting comparability of to KSEK -153,129 related to a write-down of goodwill in Wkit.

The acquisition of Wkit was financed by a share swap. At the time of the acquisition, the Effnet share price was SEK 112. The write down of goodwill was made to reflect the changed valuation of companies within the IT sector during the second half of the year. After the write down remaining goodwill amounts to KSEK 19,470.

## **Total Sales**

Effnet's revenue derives mainly from licensing the Effnet technology to other operators and hardware producing companies. The subsidiary Wkit sales consist of consulting fees and licensing income.

In 2000 the Group's net sales amounted to KSEK 5,091, an increase compared with year 1999 of KSEK 2,819. License fees amounted to KSEK 1,834. Of total sales KSEK 1,835 went to customers outside Europe. Products sold under the Company's own brand amounted to KSEK 2,286.

## **Financial Result**

The Group reports an operating loss of KSEK 295,933 (KSEK -49,805) including items effecting comparability of KSEK -153,129. The Group's result after financial items was KSEK -281,913 (-48,493).

Selling expenses amounted to KSEK -51,166 which is an increase of KSEK 27,771 compared with last year. The increase in selling expenses is mainly due to a build-up of the Mountain View office. .

Research and development (R&D), which is written off on an ongoing basis, amounted to KSEK 41,571 (-21,309). The increased cost of R&D is mainly due to an organized and planned build-up phase both in the US and in Sweden.

Administrative expenses increased during the period and amounts to KSEK -37,067 (-8,944). Besides a planned increase due to higher costs for administrating a larger organisation the increase consists of costs from changes in the Management during 2nd and 3<sup>rd</sup> quarter.

A goodwill write-down related to the Wkit acquisition was made to reflect the changed valuation of the companies within the IT sector during the second half of the year. After the write down, remaining goodwill amounts to KSEK 19,470.

## **Financial Position**

Effnet's equity/assets ratio was 95.3% (97.9%) on 31 December 2000. The Group's liquid assets totaled KSEK 274,956 (386,979).

## **Investments**

Total investments in property, plant and equipment during the year amounted to KSEK 7,316 (1,510). Of this amount, KSEK 3,206 was fixed assets acquired through the purchase of Wkit Security AB. Other investments comprised mainly of computer and office equipment.

Wkit was acquired in April 2000. The total consideration consisted of 1,650,000 Effnet shares (post split 5:1). At the acquisition goodwill was recorded with KSEK 186,855. After a write down at year-end KSEK 19,470 remains.

## **Dividend**

The Board of Directors proposes to the Annual General Meeting that no dividend will be paid in respect of the financial year 2000.

## **Personnel**

The average number of employees during the period have been 72 (37), including 5 (4) in the USA and 1 (0) in the Netherlands. The average number of employees increased by 20 compared to last year. A new incentive program for employees has been accepted by an Extra General meeting in November comprising 2,1 million share options.

## **Outlook**

The Company's long-term objective is to become a recognized world leader in embedded enabling technology solutions for IP networking, targeting component manufacturers who build the Internet and data communications infrastructure. We aim to achieve this objective by licensing core technology and hardware design to network component and system manufacturers.

Effnet's objectives for 2001 are:

- To focus on opportunities where Effnet's IP packet processing strengths give us the greatest leverage, such as in the wireless sector with robust header compression, and in the wired sector with packet classification and forwarding technologies
- To be recognized in these target markets as the leading provider of IP packet processing technology
- Continue to build the Engineering, Sales, Marketing and Support organizations to be able to execute on the new strategy and meet the financial objectives
- To increase Wkit sales in both operational areas

To be able to focus on developing the company's operations, management has decided to place postpone on listing the stock on the OM Stockholm Stock Exchanges O-list. However The Board of Directors at Effnet does now meet requirements stated by the Company committee of the Stockholm Stock exchange

## **Financial calendar**

Effnet Group AB's full audited report will be distributed to all registered shareholders beginning of April and available on our homepage at [www.effnet.se](http://www.effnet.se).

Annual General Meeting	25	April	2001
Interim report January - March	25	April	2001
Interim report January - June	27	August	2001
Interim report January - September	12	November	2001

14 February 2001

Tony Svensson  
CEO

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<b>Consolidated Profit and Loss Statement (KSEK)</b> <b>(Summary)</b>	<b>2000</b> <b>Jan. - December</b>	<b>1999</b> <b>Jan. - December</b>	<b>1998</b> <b>Jan. - December</b>
Net Sales	5 091	2 272	75
Cost of goods sold	-4 365	-714	-53
<b>Gross profit</b>	<b>726</b>	<b>1 558</b>	<b>22</b>
Selling expenses	-51 166	-23 395	-2 402
Administrative expenses	-37 067	-8 944	-5 674
Research & Development costs	-41 571	-21 309	-9 768
Items effecting comparability	-153 129	-	-
Other operating income/expenses	-13 726	2 285	-
<b>Operating result</b>	<b>-295 933</b>	<b>-49 805</b>	<b>-17 822</b>
Financial items, net	14 020	1 312	189
<b>Result after financial items</b>	<b>-281 913</b>	<b>-48 493</b>	<b>-17 633</b>
Tax	-	93	-12
Minority interest in result for the year	-	11	-
<b>Result for the year</b>	<b>-281 913</b>	<b>-48 389</b>	<b>-17 645</b>

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<b>Consolidated Balance Sheet (KSEK)</b> <b>(Summary)</b>	<b>2000</b> <b>31 December</b>	<b>1999</b> <b>31 December</b>	<b>1998</b> <b>31 December</b>
<b>Assets</b>			
Intangible fixed assets	19 470	-	-
Tangible fixed assets	9 580	1 798	793
Current assets	10 934	5 414	3 027
Cash & bank balances	274 956	386 979	5 658
<b>Total assets</b>	<b>314 940</b>	<b>394 191</b>	<b>9 478</b>
<b>Shareholders' equity &amp; liabilities</b>			
Shareholders' equity	300 046	385 922	6 392
Minority interest	-	58	-
Provisions	95	95	2
Current liabilities	14 799	8 116	3 084
<b>Total shareholders' equity &amp; liabilities</b>	<b>314 940</b>	<b>394 191</b>	<b>9 478</b>

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<b>Consolidated Cash Flow Statement (KSEK)</b>	<b>2000</b>	<b>1999</b>	<b>1998</b>
	<b>Jan. - December</b>	<b>Jan. - December</b>	<b>Jan. - December</b>
Cash flow from:			
Operating activities	- 111 486	- 48 184	- 17 427
Changes in working capital	-2 105	2 645	-356
Investing activities	- 7 562	- 1 177	-1 013
Financing activities	9 130	428 037	20 625
<b>Change in liquid assets</b>	<b>-112 023</b>	<b>381 321</b>	<b>1 829</b>

Liquid asset include investments in bonds with maturity up to 1,25 years.

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<b>Per-share data (adjusted to reflect new share issues) 2000</b>	<b>1999</b>	<b>1998</b>
<b>(Amounts in SEK)</b>	<b>31 December</b>	<b>31 December</b>
Number of shares at close of period	54 942 650	52 054 525
Average number of shares	53 021 135	42 096 370
Earnings per share	- 5,17	- 1,15
Earnings per share after full dilution	- 5,17	-1,08
Shareholders' equity per share	5,46	9,17
Shareholders' equity per share after full dilution	5,46	8,58
Share price	11,80	61,00

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<b>Stock options granted</b>			
<b>Date of issue</b>	<b>Number of options</b>	<b>Exercise period</b>	<b>Strike price</b>
November 4, 1999	1 000 000	July 2, 2001 – Dec. 31, 2001	56 SEK
April 13, 2000	418 370	Jan. 1, 2002 – June 30, 2002	216 SEK
June 9, 2000	2 182 777	July 1, 2000 – Dec. 31, 2009	54 SEK

Issued stock options are not dilutive as of 2000-12-31

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