

# INTERIM REPORT

2<sup>nd</sup> Quarter 2007



August 30<sup>th</sup>, 2007

## Quarterly Highlights

*All figures NOK*

- ❑ New CEO appointed to lead sales and marketing expansion
- ❑ Dolphin Express products target Enterprise Cluster market
- ❑ Dolphin Express hardware upgrade ready for Q3 launch
- ❑ MySQL collaboration drives new enterprise customer engagements
- ❑ PCI Express Expansion products announced
- ❑ Positive growth in StarFabric with new design-wins announced
- ❑ NumaChip on track for Q3 2008 prototype, IBM selected as chip manufacturer

Dolphin is executing its strategy to reposition its products toward the enterprise cluster market. It is making the strategic investments appropriate for capitalizing on this large market opportunity. Dolphin's proven leadership in computer interconnect technology, originally developed for the embedded market, is demonstrating compelling customer value in enterprise clusters. Dolphin's acquisition of StarGen early this year is an important piece of this strategy. This acquisition is bearing fruit by enabling new enterprise cluster products to be launched later this year. Additionally a significant initiative to expand sales and marketing capability has started.

## New CEO Appointed to Lead Sales and Marketing Expansion

As part of its new enterprise computing focus, Dolphin has undertaken several organizational initiatives with the goal of strengthening the company's sales and marketing effectiveness. Tim Miller was appointed as the CEO of Dolphin as of 1 July 2007. Tim was formerly the

CEO of StarGen and previously had spent over 20 years as a sales and marketing executive in the high tech industry. He will lead a major expansion of Dolphin's sales and marketing capabilities specifically aimed at success in the enterprise cluster market.

## Dolphin Express for Enterprise Cluster Market

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Dolphin Express, launched in April, is a complete hardware and software interconnect solution for enterprise clusters.

- utilizes company's core competencies in high performance computer-to-computer interconnect technology
- accelerates database performance for applications like web infrastructure, telecom services, business intelligence, and data warehousing
- enables powerful clusters built from standard off-the-shelf servers
- 100% software compatible to popular clustered database platforms like Oracle and MySQL
- enterprise cluster market > 10 times larger than Dolphin's historical markets.

### **New Generation of hardware on track for Q3 Launch**

Dolphin Express will be enhanced with a new generation of hardware based on the industry standard PCI Express interconnect this fall. The new hardware will provide over 2x improvement in latency and over 5x improvement in bandwidth versus the currently shipping hardware. These products will sample to customers in Q4 and begin to contribute revenue in the beginning of 2008.

### **MySQL Collaboration Spearheads Market Penetration**

Dolphin has established a strategic relationship with MySQL. MySQL is the fastest growing database application, with an especially strong position for web infrastructure and advanced telecom service deployments. During Q2 Dolphin and MySQL collaborated on both joint customer engagements as well as benchmarking and characterization projects. These initiatives are validating the customer advantages realized with the Dolphin Express and are resulting in early customer successes. A growing number of customer pilot projects have been completed or are underway with leading web services providers, telecom companies and several major server OEMs.

## Other markets and customers

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In addition the company continues to support ongoing business in its traditional embedded markets.

### PCI Express Expansion

Dolphin announced its PCI Express IO Expansion product line in early August at the LinuxWorld conference in San Francisco. The products are targeted at applications that can benefit from locating a system's IO devices remotely from the host processing complex. The products will be sold to traditional users in the embedded marketplace.



### StarFabric

The StarFabric PCI Switch and Bridge products were acquired as part of the StarGen acquisition earlier this year. StarFabric revenue increased by 20% over Q1 with continued strength from major US and Japanese OEMs. Additionally, several new design wins were announced for the products, including a new communication product from Furukawa Network Solutions Corporation, an aerospace control system from Sony Manufacturing Systems Corporation and an application in automated manufacturing developed by Seiko Epson Corporation.

### NumaChip

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The NumaChip is being developed by Dolphin to revolutionize the high end server market. Using the NumaChip customers will be able to build mainframe class enterprise systems out of standard low cost servers at less than a tenth of the cost. The NumaChip will complement the Dolphin Express products by providing further penetration into the high end enterprise market.

Dolphin has selected IBM as the chip vendor for the NumaChip. Dolphin and IBM will collaborate closely on preparing the chip for manufacture in IBM's semiconductor foundry. All other important licenses and resources for the project are in place and all partners are working on the project. The collaboration now includes Dolphin, AMD, Siemens I&S, IBM, Synopsis and the University of Mannheim. Dolphin has dedicated resources in Oslo as well as in the US for completion of the NumaChip. Prototype availability is planned for Q3 2008.

## Summary of 2<sup>nd</sup> Quarter Results (Figures for 2nd Quarter 2006 in parenthesis)

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Total operating revenues reached 7.8 million in the Quarter, a decrease of 26.4% from the 2<sup>nd</sup> Quarter last year (10.6 million). The main reason for the decline is the wind up of a large

OEM contract on SCI products in September last year. The activities of StarGen Inc has been consolidated as of January 1, 2007 and compared to the first Quarter of 2007, total revenues declined 9.3%. Sales of Star Fabric increased 11% compared to the second Quarter 2006 and grew 20% compared to the first Quarter 2007. Temporary low orders from a major customer in June 2007 accounts for the decline in SCI based products from Q1. Gross margin was at 63% in the 2<sup>nd</sup> Quarter 2007, well above the 55% level seen in the 2<sup>nd</sup> Quarter last year. The increase is mainly explained by higher margins in the sales of the StarFabric products.

Payroll expenses for the Quarter were 4.9 million (2.2 million), and the increase is mainly contributable to the consolidation of the former StarGen organization as from January 1<sup>st</sup> 2007. 0.6 million is a non-payable cost due to the warrants-program implemented in connection with the merger. According to IFRS, labour cost in product development shall be capitalized and reported payroll figures therefore fluctuate with the level of capitalized development activities in a given period.

EBITDA ended at -4.2 million in the 2<sup>nd</sup> Quarter (1.2 million). Depreciation for the Quarter totalled 0.6 million (0.1).

Operating profit (EBIT) ended at -4.7 million in the Quarter (1.1 million). Net financial profit was 0.3 million in the 2<sup>nd</sup> Quarter (0.2 million) and profit before taxes ended at -4.4 million (1.4 million). Net profit ended at -3.2 million compared to 2.6 million in the 2<sup>nd</sup> Quarter last year.

## Equity, balance sheet and cash flow items

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Deferred income tax assets increased to 14.2 million in the Quarter. The US subsidiary has a historic deficit to carry forward from former StarGen. Deferred tax assets related to this deficit amounts to approximately 11.8 million (USD 2 million), and the tax assets have not been booked in the balance sheet. Total equity in the Group was 110.6 million, or 92.9% at the end of the 2<sup>nd</sup> Quarter (93.7%).

In the 2<sup>nd</sup> Quarter, total development cost of 5.2 million has been capitalized. Total immaterial assets in the form of capitalized development cost thus increased to 56.7 million. Of the total figure, 37.2 million has been allocated to intangible assets as a result of the acquisition of StarGen in the beginning of 2007. In the second Quarter 2006 capitalized development amounted to 11.2 million. Cash and cash equivalents was at 25.8 million at the end of the 2<sup>nd</sup> Quarter (56.7 million). During the Quarter, there was a net decrease in cash and equivalents of 10.4 million whereof 5 million as a result of operating activities and 5.2 million as a result of investments in product development (intangible assets).

## Financing and shareholders

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As of August 24<sup>th</sup>, the total number of shareholders in the company was 462, of which the 20 largest are included in the table below.

	<b>Shareholder</b>	<b>No of shares</b>	<b>%</b>
1	MORGAN STANLEY & CO. INC.	1 251 345	11 %
2	CITIGROUP GLOBAL MARKETS INC.	1 100 586	10 %
3	SELVAAG INVEST	1 023 783	9 %
4	DEN NORSKE KRIGSFORSIKRING FOR	749 881	7 %
5	VERDIPAPIRFONDET DANSKE FUND NOR	432 048	4 %
6	GRANADA FORVALTNING AS	325 082	3 %
7	VERDIPAPIRFONDET KLP AKSJENORGE	254 196	2 %
8	MP PENSJON	228 702	2 %
9	DRAGE INDUSTRIES AS V/ARNE STEEN	200 000	2 %
10	BAMO AS	175 000	2 %
11	GRANADA MANAGEMENT AS	152 544	1 %
12	SANDVOLD	140 000	1 %
13	FIXDAL	135 930	1 %
14	CONSORT INVEST A/S	135 483	1 %
15	RASMUSSEN	132 102	1 %
16	ALFHEIM	130 000	1 %
17	INTEL CAPITAL (CAYMAN) CORPORATION	129 112	1 %
18	LEGIO A/S	127 598	1 %
19	FALKUM INVEST	124 000	1 %
20	AROSA INVEST AS	119 006	1 %
	Total 20 largest shareholders	7 066 398	62 %
	Other shareholders	4 416 712	38 %
	Total outstanding shares	11 483 110	100 %

## Accounting principles

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Dolphin Interconnect Solutions ASA follows the principles of IFRS in this report. The figures are reported in accordance with the regulations for interim reporting in IAS 34. For further reference on accounting principles, see the annual report for 2006.

## Corporate priority and outlook

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Dolphin is focused on building a strong sales and marketing infrastructure to drive its technology into the enterprise markets. Near term hardware product introductions will significantly improve the product offerings. Work will continue to secure strategic partnerships for both Dolphin Express and NumaChip. The Board believes robust growth in revenue will return in 2008.

The Board of Directors, Dolphin Interconnect Solutions ASA  
Oslo, August 29<sup>th</sup>, 2007

# Dolphin Interconnect Solutions Group

## Income Statement

	Q2 / 07	Q2 / 06	YTD 07	YTD 06	Full year 2006
<b>OPERATING REVENUES</b>					
Sales	7 775 535	10 441 885	16 389 090	20 762 048	32 091 691
Other operating revenue	0	131 300	0	348 587	3 949 841
<b>TOTAL OPERATING REVENUE</b>	<b>7 775 535</b>	<b>10 573 185</b>	<b>16 389 090</b>	<b>21 110 635</b>	<b>36 041 532</b>
<b>OPERATING EXPENSES</b>					
Cost of goods sold	2 908 438	4 755 390	5 763 304	9 478 593	14 662 028
Payroll expenses	4 934 008	2 191 773	12 041 485	3 171 345	11 884 495
Other operating expenses	4 084 566	2 399 312	8 323 485	4 969 727	12 168 929
<b>TOTAL OPERATING EXPENSES</b>	<b>11 927 012</b>	<b>9 346 475</b>	<b>26 128 274</b>	<b>17 619 665</b>	<b>38 715 452</b>
<b>EBITDA</b>	<b>-4 151 477</b>	<b>1 226 710</b>	<b>-9 739 184</b>	<b>3 490 970</b>	<b>-2 673 920</b>
Depreciation	563 818	81 660	1 434 143	162 050	348 419
Write off	0	0	0	0	6 038 104
<b>OPERATING PROFIT (EBIT)</b>	<b>-4 715 295</b>	<b>1 145 050</b>	<b>-11 173 327</b>	<b>3 328 920</b>	<b>-9 060 443</b>
<b>NET FINANCIAL PROFIT</b>	<b>302 939</b>	<b>220 476</b>	<b>549 178</b>	<b>258 881</b>	<b>1 195 397</b>
<b>PROFIT BEFORE TAXES</b>	<b>-4 412 356</b>	<b>1 365 526</b>	<b>-10 624 149</b>	<b>3 587 801</b>	<b>-7 865 046</b>
Income taxes	-1 239 958	-1 250 788	-4 469 140	-606 774	-3 989 793
<b>NET PROFIT</b>	<b>-3 172 398</b>	<b>2 616 314</b>	<b>-6 155 009</b>	<b>4 194 575</b>	<b>-3 875 253</b>
Avg.no. of shares outstanding	11 483 110	8 325 967	10 644 181	7 220 297	8 093 437
Net profit per share	-0,28	0,31	-0,58	0,58	-0,48

# Dolphin Interconnect Solutions Group

## Balance Sheet

ASSETS	30.06.2007	30.06.2006	31.12.2006
<b>NON-CURRENT ASSETS</b>			
Capitalized development cost	56 701 810	11 239 135	8 911 664
Deferred income tax assets	14 184 372	6 319 349	9 710 424
Operating equipment	1 605 211	66 711	179 344
Other long term receivables	952 230	2 182	2 189
<b>TOTAL NON-CURRENT ASSETS</b>	<b><u>73 443 623</u></b>	<b><u>17 627 377</u></b>	<b><u>18 803 621</u></b>
<b>CURRENT ASSETS</b>			
Inventories	11 016 150	6 843 017	11 296 088
Trade receivables	3 601 896	3 921 810	1 764 659
Other short term receivables	5 142 217	4 309 508	3 908 499
Cash and cash equivalents	25 758 049	56 707 412	48 553 242
<b>TOTAL CURRENT ASSETS</b>	<b><u>45 518 311</u></b>	<b><u>71 781 747</u></b>	<b><u>65 522 488</u></b>
<b>TOTAL ASSETS</b>	<b><u>118 961 934</u></b>	<b><u>89 409 124</u></b>	<b><u>84 326 109</u></b>
<b>EQUITY AND LIABILITIES</b>			
<b>EQUITY</b>			
<b>Subscribed equity</b>			
Share capital	2 296 622	1 790 468	1 790 468
Share premium fund	84 028 101	44 041 951	44 041 951
<b>Total subscribed equity</b>	<b><u>86 324 723</u></b>	<b><u>45 832 419</u></b>	<b><u>45 832 419</u></b>
<b>Retained equity</b>			
Retained earnings	24 228 194	37 949 401	29 881 606
<b>Total retained equity</b>	<b><u>24 228 194</u></b>	<b><u>37 949 401</u></b>	<b><u>29 881 606</u></b>
<b>TOTAL EQUITY</b>	<b><u>110 552 917</u></b>	<b><u>83 781 820</u></b>	<b><u>75 714 025</u></b>
<b>NON CURRENT LIABILITIES</b>			
Other long-term liabilities	577 828	996 493	883 751
<b>TOTAL NON CURRENT LIABILITIES</b>	<b><u>577 828</u></b>	<b><u>996 493</u></b>	<b><u>883 751</u></b>
<b>CURRENT LIABILITIES</b>			
Trade payables	5 647 132	2 479 384	4 814 349
Public duties payable	499 893	740 947	1 248 197
Other current liabilities	1 684 165	1 410 480	1 665 787
<b>TOTAL CURRENT LIABILITIES</b>	<b><u>7 831 190</u></b>	<b><u>4 630 811</u></b>	<b><u>7 728 333</u></b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b><u>118 961 934</u></b>	<b><u>89 409 124</u></b>	<b><u>84 326 109</u></b>

# Dolphin Interconnect Solutions Group

## Cash Flow Statement / Change in Equity

CASH FLOW STATEMENT	Q2 / 07	Q2 / 06	YTD 07	YTD 06	Full year 2006
<b>Cash Flow from Operations</b>					
Operating result before tax	-4 412 356	1 365 526	-10 624 149	3 587 801	-7 865 046
Depreciation & write off	563 818	81 660	1 434 143	162 050	6 386 523
Changes in inventories	1 280 227	565 518	279 938	673 436	-3 779 635
Changes in receivables	664 429	177 734	-1 837 237	-1 486 411	670 740
Changes in trade payables	-852 027	460 359	832 783	-1 626 689	708 276
Changes in other current assets/debt items	-2 263 144	184 428	-2 579 097	-3 610 114	-2 460 116
<b>Net Cash Flow from Operations</b>	<b>-5 019 053</b>	<b>2 835 225</b>	<b>-12 493 619</b>	<b>-2 299 927</b>	<b>-6 339 258</b>
<b>Cash Flow from Investments</b>					
Purchase of operating equipment	-73 127	-22 212	-1 786 432	-43 997	-187 474
Purchase of intangible assets	-5 195 991	-1 471 632	-48 403 256	-4 002 552	-7 868 310
<b>Net Cash Flow from Investments</b>	<b>-5 269 118</b>	<b>-1 493 844</b>	<b>-50 189 688</b>	<b>-4 046 549</b>	<b>-8 055 784</b>
<b>Cash Flow from Financial Activities</b>					
Payment of long term liabilities	-151 204	-195 765	-305 923	-230 887	-343 629
Issue of shares	0	44 293 634	40 492 304	44 293 634	44 293 634
<b>Net Cash Flow from Financial Activities</b>	<b>-151 204</b>	<b>44 097 869</b>	<b>40 186 381</b>	<b>44 062 747</b>	<b>43 950 005</b>
Net change in cash and equivalents	-10 439 375	45 439 250	-22 496 926	37 716 271	29 554 963
Foreign currency effect on cash	-56 739	-16 768	-298 267	-24 438	-17 300
Opening balance, cash and equivalents	36 254 163	11 284 930	48 553 242	19 015 579	19 015 579
<b>Closing balance, cash and equivalents</b>	<b>25 758 049</b>	<b>56 707 412</b>	<b>25 758 049</b>	<b>56 707 412</b>	<b>48 553 242</b>
<b>CHANGE IN EQUITY</b>					
Equity opening balance	113 330 459	36 876 573	75 714 025	35 301 932	35 301 932
Issue of shares	0	49 875 000	40 492 304	49 875 000	49 875 000
Cost of issue of shares	0	-5 581 366	0	-5 581 366	-5 581 366
Option granted to employees	619 753	0	929 630	0	0
Currency converting effect	-224 898	-4 701	-428 034	-8 321	-6 288
Net profit	-3 172 398	2 616 314	-6 155 009	4 194 575	-3 875 253
<b>Equity closing balance</b>	<b>110 552 916</b>	<b>83 781 820</b>	<b>110 552 916</b>	<b>83 781 820</b>	<b>75 714 025</b>