26 June 2020

**Ethernity Networks Ltd.**

(Ethernity or the "Company")

**Results for the Year Ended 31 December 2019**

Ethernity (AIM: ENET), a leading supplier of functional acceleration ethernet adapter cards on FPGA (field programmable gate array) for virtualised networking appliances, today announces its results for the year ended 31 December 2019.

**Financial Highlights**

- Revenues increased by 19.6% to $1.34m (2018: $1.12m)
- Gross margins increased by 41.6% to $1.15m (2018: $0.81m)
- Operating costs before amortisation of intangible assets, depreciation charges, changes in recognition of R&D costs and other non-operational charges decreased by 14.1% to $2.79m (2018: $3.25m)
- EBITDA Loss (adjusted for R&D capitalisation) improved by 35.3% to a loss of $1.52m (2018: loss of $2.35m)
- $2.7m net cash and short term cash deposits as at 31 December 2019. As at 16 June 2020 the Company had retained cash reserves of $0.54m (unaudited)
- Cessation of capitalisation of R&D expenditure from 1 July 2020

**Operational 2019 and Post-period highlights**

**Operational Highlights**

- First delivery of the ACE-NIC prototypes in early 2019
- Concluded the delivery associated with a licensing contract, signed in Q4 2018, with a U.S Tier 1 telecommunications OEM, that has subsequently resulted in a follow up contract at the end of April 2020
- ACE-NIC100 selected by FiberHome Telecommunication Technologies for vBNG (virtual broadband network gateway) offload; now refocused for 5G User Plane Functionality (UPF) to be delivered for testing by Chinese operators during Q4 2020
- Increased drive from Chinese markets, focused on building a 5G mobile network based on NFV (network function virtualisation), opening further ACE-NIC100 engagement opportunities

**Post-period highlight Highlights**

- Agreement in February 2020 with TietoEVRY to create a joint offering of open source concept based on VPP (vector packet processor) for 5G UPF to accelerate 5G packet processing at the network edge
- Ethernity named in Gartner's February 2020 Report *"Market Trends: Function Accelerator Cards Disrupting Traditional Ethernet Adapter Market"* as a *"Vendor to Watch"* for solutions within Functional Acceleration Cards
- Design win in March 2020 with Chinese OEM working on integrating their UPF control software to operate on top of Ethernity's ACE-NIC for UPF data plane offload

- ACE-NIC100 cards shipped to a large Chinese operator in April 2020 following an order received for implementation of 5G UPF

- Engaged in March 2020 with Tier 1 networking OEM vendor on the UEP-20, this engagement is on hold due to COVID-19.

- June 2020 - order from South Asian service provider planning to deliver their own UPF control and offload, with Ethernity's ACE-NIC, the UPF data plane

- Following conclusion in 2019 of the delivery associated with a licensing contract, signed in Q4 2018, with a U.S Tier 1 aviation/military supplier, a new project was originally planned to commence in Q2 2020. Due to the impact of COVID-19 the customer has estimated a delay in the programme development, for which we remain under consideration, to be between six to twelve months from now

- Direct relationship in place with three major telecom service providers in China - China Mobile, China Telecom and China Unicom - each either planning to use an FPGA SmartNIC offering for 5G UPF for integrating their own open UPF software to be offloaded by the ACE-NIC

- Staff safeguarding and cash conservation measures implemented in light of COVID-19

- Continued focus on delivering complete solutions for functional acceleration of virtualised platforms and programmable networking appliances, transitioning from a technology Intellectual Property licensing company to a complete solution offerings company

**David Levi, Chief Executive, said** *"I am encouraged by the fact that, finally, the telecom cloud and NFV market combined with the data usage requirements of 5G has been realised and, despite the uncertainty resulting from the COVID-19 pandemic, is now positioning towards mass deployment, allowing the Company to fulfil its goal. I am hopeful that the growing momentum around our 5G UPF acceleration solution will lead to the achievement of large scale growth in the coming years."*

The annual report and accounts for the year ended 31 December 2019 is being posted to shareholders shortly and is available on the Company's website at www.ethernitynet.com. The notice of annual general meeting, expected to be held during August 2020, will be despatched in due course.

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**About Ethernity** (www.ethernitynet.com)

Ethernity Networks Ltd. (AIM: ENET) provides innovative, comprehensive networking and security solutions on programmable hardware for accelerating telco/cloud networks performance. Ethernity's FPGA logic offers complete Carrier Ethernet Switch Router data plane processing and control software with a rich set of networking features, robust security, and a wide range of virtual function accelerations to optimise telecommunications networks. Ethernity's complete solutions quickly adapt to customers' changing needs, improving time-to-market and facilitating the deployment of 5G and edge computing.

The information contained within this announcement is deemed by the Company to constitute inside information stipulated under the Market Abuse Regulation (EU) No. 596/2014. Upon the publication of this announcement via a Regulatory Information Service, this inside information is now considered to be in the public domain.

# Chairman's Statement

During 2019 Ethernity continued to develop its technology so as to become a provider of complete network solutions to the market. At the outset of the year the Company anticipated receiving increased revenues during the year primarily from its proprietary technology licensing and services activities, and from first milestone sales of its Router-on-FPGA-NIC product.

Whilst customer engagement and solutions specification with customers developed steadily during the year, this did not translate into revenue levels as originally anticipated due to the delay in uptake by the Network Function Virtualisation (NFV) market and telco cloud markets, which the Company's customers supply.

However during the second half of the year, the Company received interest for its ACE-NIC100 product adapted with the offload 5G UPF virtualisation software, and therefore re-focussed the Company's R&D efforts to complete a product offering for the 5G UPF market, and gained design wins and increasing interest, particularly in China. The impact of and outlook for the market opportunities are set out in further detail in the Chief Executive's Statement and a summary of the Company's interface processes with customers is included in the Strategic and Financial Reviews, each set out below.

Revenues for 2019 were $1.34m (2018 $1.12m) with gross margin of $1.15m (2018 $0.81m) and operating loss of $4.54m (2018 $2.78m) respectively. The Company continued to invest significantly in planned Research and Development. However, the reported comparative operating loss for the year increased significantly. This was due to a change in accounting treatment for R&D expenditure from the second half of the year in line with the criteria as set out in the International Accounting Standard, IAS38, relating to the recognition of development costs as an intangible asset. The comparable loss for 2019 restated under the former basis of expenditure capitalisation would have been approximately $2.35m (2018 $2.78m). The Board will keep this policy under review for future reporting periods.

In accordance with IAS38 the Board undertook a review of the intangible assets valuation as at 31 December 2019, and accordingly instructed KPMG Somekh Chaikin to provide a third party professional evaluation. With the benefit of this report the Board has concluded that no impairment of value is appropriate. Further details relating to this matter are set out in the Financial Review below.

At the year end the Company's net cash and short term cash deposits was $2.7m (2018 $8.4m). Subsequent to the year end the Company updated that in light of the developing COVID-19 situation the Company had taken prudent steps to mitigate any impact through certain short-term cash conservation measures, and at 16 June 2020 the Company had retained cash reserves of $540,000 (unaudited).

As announced on 17 June 2020 the Company was not successful in receiving a grant applied for from the Innovation Authority in Israel and accordingly had taken prompt action to institute further cash conservation measures, which includes a reduction in certain R&D resources. The Board will be reviewing the Company's product developments to focus resources and solutions on its key markets and customers in the NFV and 5G markets.

In light of the change in status of the engagement with the Military/Aerospace T1 vendor as noted below in the Chief Executives Statement, the Company will need to secure additional short term funding in the latter half of H2 2020 either via short term finance arrangements or an additional issue of equity.

As previously reported the Company maintains close management of the use of cash resources and the rate of deployment of cash is monitored by management and the Board with a view to adjusting cash utilisation and maintaining cash resources to meet trading requirements.

At the Extraordinary General Meeting held on 22 June 2020, resolutions were approved, inter alia, granting the Directors share issuance authorities in line with other growth companies on the AIM market to provide the Company with greater flexibility and funding options.

### COVID-19

The Company has previously stated that in light of the continued uncertainty on the potential impact and duration of the COVID-19 pandemic, the Board had taken certain steps to both safeguard the well-being of staff and to position the Company for the future.

The Board remains conscious of the uncertainties over the timing of the securing of customer orders and receipt of revenues from product sales and licensing transactions both in relation to general market delays as well as delays from the impact of COVID-19 on customers and engagements. This remains a challenge for the executive management in predicting when substantive revenues and related profits will be earned, including for the current financial year.

The Board is very appreciative of the considerable efforts of our management and staff, who all work tirelessly towards the development, sales, and administrative goals of the Company. I thank them especially during these testing times for their continuing hard work and commitment to the Company.

### Outlook

The current year will be another period of particular challenges to continue developing customer engagements, and finance and grow the revenue delivery from current modest levels, into milestone new contracts. The Board is confident that, providing customers maintain their technology investment programs, progress will be made this year resulting in longer term value for shareholders.

**Graham Woolfman**

Chairman

25 June 2020

## Chief Executive's Statement

### Business and Market Overview

Ethernity Networks continues to operate in a market which is undergoing significant change. This includes the growing use of FPGA devices for networking appliances and the transition to 5G networks which will provide higher data throughput to users and will based on the NFV concept. The Company's ACE-NIC FPGA SmartNIC product is focussed on this market and is part of the strategy to of transitioning the Company's offering in the market from providing Intellectual Property to complete solutions to customers.

In 2019 we were further impacted by the delay in deployment of NFV infrastructure in the telecoms environment. This resulted in the Company not realising the anticipated revenues from our Router-on-FPGA-NIC products as previously expected. In order to diversify and create revenue opportunities for the Company during this period of market delay, the Company invested in the development of our all programmable Universal Edge Platform (UEP) offering including PON, OLT and ONU MAC as a solution for the existing markets, that has received significant interest from potential Tier 1 OEM customers during 2019 and 2020.

During the second half of 2019 we received growing interest for our Router-on-FPGA-NIC (the ACE-NIC) positioned to accelerate 5G User Plan Functionality (UPF), resulting in an increased number of engagement and design wins for our ACE-NIC100 5G UPF Functional Acceleration Cards (FAC). These deliver a breakpoint value of 1:20 saving on CPU cores and resultant 1:5 CAPEX saving for the telecom service provider in deployment of 5G UPF.

Furthermore, the Company is engaged in ongoing discussions on 5G Central Units data plan offload by utilising the ACE-NIC to support security, header compression, reordering, and protocol offloading with a number of software VNF vendors and service providers. An analysis performed with a vendor shows that by utilising the ACE-NIC on a server for acceleration of 5G CU networking and security functions, it resulted in an estimated 70% to 80% CAPEX saving for the service provider in deployment of 5G central units elements.

In February 2020 we were named in Gartner's Report "Market Trends: Function Accelerator Cards Disrupting Traditional Ethernet Adapter Market" as a "Vendor to Watch" for solutions within Functional Acceleration Cards. Gartner further noted in their report that *"by 2023, one in three network interface cards shipped will be a FAC"* and that *"as 5G adoption also starts to grow, FACs will also be handy at the edge for offloading NFV functions"*.

The industry's 5G mobile network deployment plans for 2021 will be constructed using the underlying principles of NFV, Software Defined Networks (SDN) and Edge Computing with the result that 5G will ultimately be a flexible, programmable, and distributed cloud network.

With 5G and NFV paving the way for deployment and with the breakpoint advantage offered with our ENET flow processor running on the ACE-NIC FPGA SmartNIC, the Company is now fully focused on obtaining market share in the 5G network, starting with the 5G UPF, and then moving deeper into other elements of the 5G infrastructure, being the 5G Cloud RAN (Radio Access Network) elements such as Central Unit (CU) and Distribution Unit (DU) which are all based on NFV technology and implemented on a computer server that requires ENET's FPGA SmartNIC with data processing offload functions.

The 5G Cloud RAN Network is depicted in the Annual Report.

Our estimated total addressable market for the next five years for NIC cards required for acceleration of 5G UPF is $1.2Bn, which the Ethernity ACE-NIC product family can address. This is based on the assumptions that a 100Gbps performance will serve 10,000 5G users, and with the market analysis (depicted in the Annual Report) that forecasts a total of 3 billion users by 2025. Within this we anticipate a market need for 300,000 FACs for 5G UPF over the next 5 years, commencing in 2021 with growth ramping up exponentially from 2022.

As a result of the market's intentions for 5G NFV based deployment, and the growing engagements with customers for our ACE-NIC family that embeds a Router-on-NIC implementation, the Company has continued and is now focussing its efforts on the ACE-NIC offering for acceleration of the 5G NFV based solution, deferring other activities, with the main goal being to capture a greater market share of the upcoming 5G market.

## Review of 2019 achievements

2019 began with the first delivery of the ACE-NIC prototypes to a Korean customer, though at this stage we do not anticipate further business with the customer due to a change to their internal priorities and focus.

Following conclusion in 2019 of the delivery associated with a licensing contract, signed in Q4 2018, with a U.S Tier 1 aviation/military supplier, a new project was originally planned to commence in Q2 2020. Due to the impact of COVID-19 the customer has estimated a delay in the programme development, for which we remain under consideration, to be between six to twelve months from now.

In June 2019 our ACE-NIC100 was selected by FiberHome Telecommunication Technologies for implementation within their Broadband Network Gateway (BNG) and promotion to FiberHome's core Chinese telecom customers. With the refocus of Chinese operators on 5G, the delivery of this project has been re-assigned to one of FibreHomes' group companies, with the Ethernity 5G UPF accelerated performance solution intended for lab testing by the largest Chinese operators during Q4 2020.

The increased drive from the Chinese markets, focused on building a 5G mobile network based on NFV, was the sign we have been waiting for over the last two years. It is based around the building of the edge compute virtualised network together with a need for extensive performance, for which Ethernity technology is the best fit, providing greater value added solutions that are appreciated and demanded by our customers. We have therefore taken the strategic decision to focus on porting the ENET flow processing features on the ACE-NIC100 to accelerate performance of the 5G UPF data plane. This has resulted in multiple engagements and design wins for our ACE-NIC100 during the first half of 2020 with the potential onward conversion to multiple delivery contracts during H2 2020 and into 2021.

## Current Trading

During H1 2020 we have continued with the momentum around the 5G UPF offering.

- In February 2020 we finalised our agreement with TietoEVRY to create a joint offering of an open source concept based on VPP for 5G User Plane Functionality (UPF) to accelerate 5G packet processing at the network edge. The intention is to deliver to customers an end-to-end open UPF platform that includes the UPF control utilising the VPP open source and the UPF data plane running and offloaded by the ACE-NIC100. Following completion of the enablement with the VPP we have delivered the offering for Lab testing to two operators and to two strategic partners. Furthermore major go-to-market activities are handled together with TietoEVRY in China.

- In March 2020 we achieved a further design win with another Chinese OEM that is working on integrating their UPF control software running over DPDK to operate on top of our ACE-NIC for UPF data plane offload with delivery of the complete offering for testing planned during Q4 2020.
- In April 2020 we shipped a number of ACE-NIC100 cards to a large Chinese operator following an order received.
- We have commenced a process with two strategic world technology industry leaders to support the introduction and dissemination in the open compute industry of our 5G UPF offload.
- In early June 2020 we received a further order directly from another Asian service provider planning to deliver their own UPF control and offload, with Ethernity's ACE-NIC, the UPF data plane. On a success case, with a deployment plan starting from second half of 2021, this may lead to 500-1000 ACE-NIC card sales in the two years following starting of deployment.

The Company now has a direct relationship with three major telecom service providers in China - China Mobile, China Telecom and China Unicom - all either planning to use an FPGA SmartNIC offering for 5G UPF, or already under development in their laboratories for integrating their own open UPF software to be offloaded by the ACE-NIC.

## COVID-19 Impact

The markets and industries Ethernity is mostly dependent on include telecommunications infrastructure. The Company is not overly exposed to areas of the market that are most immediately disrupted by COVID-19, such as transportation, shipping, tourism, and consumer electronics. Furthermore, worldwide telecom capex remains forecast to grow at a one percent CAGR until 2022.

In light of the continued uncertainty on the potential impact and duration of the COVID-19 pandemic, the Board has taken certain steps to both safeguard the well-being of staff and to position the Company for the future. However, given the continued high levels of uncertainty created by COVID-19 and the future global economic recovery, anticipated near to medium-term agreements may be the subject of temporary delays due to disruptions, as companies continue to impose their own safeguarding work policies, which would adversely affect our 2020 results.

## Outlook

As detailed, NFV deployment is now here to stay and will become the norm as 5G networks will be based on NFV and virtualisation technologies, with a need to support extensive performances. With the new virtualization concept that has finally been accepted and adopted by the market, 5G will supply 10 times more in throughput than 4G and alongside the virtualisation concept functionality acceleration card as provided by Ethernity, this will be a key element in the 5G network, as detailed in Gartner Market trend report.

As the Company continues to focus on delivering complete solutions for functional acceleration of virtualised platforms and programmable networking appliances, it is completing the move from a technology IP licensing company to a complete solution offerings company, as shown by the growing engagement and business based on our ACE-NIC100 product offering. Despite the change of status with the Military/Aerospace T1 vendor that where negotiations are on hold and the programme is being repositioned, we remain confident that the existing and new customer engagements and relationships in the forthcoming 12 months will provide approximately $2m in revenues from licensing and royalties without this anticipated contract. ACE-NIC

We have taken the decision to defer other technology developments, assigning our resources to focus on the ACE-NIC FPGA SmartNIC product. Once this has created the anticipated significant business and revenue streams, the Company will then revert to completing the developments of other value-add products. Furthermore, in order to ensure that our progress on the 5G offering is maintained and funded, the Company intends offering licensing deals on its IP of its PON and UEP technology.

Ethernity's large scale revenue target is the volume production and sale of cards directly to customers for integration with their virtualised networking function software, that then can run on any commercialised off the shelf (COTS) server.

The Company has and continues to derive modest revenue from customer relationships based on research and development investment alongside customer specifications, in advance of achieving volume production orders for its ACE-NIC product family from its OEM customers targeting onward delivery to the Communication Service Providers (CSP).

With the disaggregation framework (set out in more detail in the Strategic Review below) that is progressing within the CSPs, they create inhouse software development teams with the intention of delivering their own inhouse UPF software based on open source frameworks, or to purchase the UPF virtualised software from one vendor, and server

and FPGA SmartNICs from another vendor. In such a case delivery to the CSP will be dealt with by system integrators, such as TietoEVRY, server manufacturers, the company's OEM customers, or other channels that will supply and support the deployment at the CSP. In any event the Company does not plan to sell its products directly to the CSP for large scale deployment and intends to deliver to the market through the above channels.

I am encouraged by the fact that, finally, the telecom cloud and NFV market has been realised and is now positioning towards mass deployment, allowing the Company to fulfil its goal. I am hopeful that the growing momentum around our 5G UPF acceleration solution will lead to the achievement of large scale growth in the coming years.

We fully expect to see revenue growth during 2020, however in light of the disruptions resulting from COVID-19 there remains a significant element of uncertainty over the timing of near-term events.

**David Levi**

Chief Executive Officer

25 June 2020

# Strategic Review

We live in an age of massive demand for data. Today's devices and associated applications, whether Video on Demand, online gaming, online storage for data backup, remote surgery, or artificial intelligence demand far greater throughput than today's networks can provide, and they also require that the data be served with high availability, security, and reliability. To meet the ever-increasing application needs, operators have begun using Edge Computing to locate the content closer to the end users, and performing faster security authorisations with SDN/NFV technology that, when coupled with infrastructure improvements, allows delivery of 10 to 100 times more throughput.

NFV (network function virtualisation) is part of a larger trend known as disaggregation, which has enabled the industry to move toward agile networks. Whereas once the standard was for networks to rely on ASIC (application-specific integrated circuit)-based monolithic hardware appliances that bundled proprietary software into a vendor-locked device and integrated only with other offerings from that vendor, disaggregation has changed the paradigm to overcome such limitations.

Thanks to the use of X86 as a standard platform for server hardware, today's networks can disaggregate software applications from the underlying hardware bare metal server. Software-based functions run on top of CPUs inside standard servers from any of several different vendors, and open stacks that are used to communicate between virtual machines for application and service chaining dictate the overall appliance functionality that runs on the server.

Disaggregation within the data centre provides the flexibility to choose a software vendor separately from the choice of a hardware server platform, moving the industry away from monolithic ASIC-based appliances. It ensures that the resulting appliance is futureproof because the software can be upgraded or replaced without needing to replace the hardware that hosts it.

FPGAs are the natural hardware solution for NFV, as they are flexible, quick to market, efficient, scalable, and come with different size options to serve different markets and solutions. FPGA platforms are being widely deployed in automotive, aerospace, industrial, storage, and networking systems.

A similar disaggregation took place in streamlining the cloud. Cloud service providers addressed the performance gap associated with increased demand for sophisticated applications and therefore the amount of required data processing not by using more servers in the data centre, but rather by seeking ways to disaggregate the various components of the data delivery chain. Microsoft Azure has led the way on this front, and after investigating many different technologies to enable greater agility and efficiency, Microsoft determined that FPGAs demonstrated the best value for their cloud service. They have actively promoted their use of FPGA SmartNICs in their data centre, stating that FPGAs demonstrate the *"… performance characteristics of an ASIC, but the programmability and reconfigurability inherent in a software solution like a processor."*

*"We stopped burning CPU cores to run the network data path… Host cores show less than 1% utilization..."* after implementing FPGA SmartNICs. Other cloud service providers have also adopted FPGAs to enable disaggregation, including Alibaba, Tencent, and Baidu, and Amazon Web Services has built an FPGA farm to offer Acceleration-as-a-Service for applications within their cloud.

Telecommunications service providers have learned from the cloud service providers and are using disaggregation to add agility and efficiency at the network edge. The planned backbone of the 5G mobile infrastructure deployment is to use FPGAs for data plane processing, as the telecommunications industry has realised that standard compute platforms alone cannot deliver the required performance, especially when there is a need in telecom for data processing functions to support more sophisticated and complicated features compared to data processing for pure data centre and enterprise applications. After many years of being promised that NFV is coming, 5G is finally putting it to extensive use.

FPGAs are manufactured by major vendors like Xilinx and Intel. However, these FPGA vendors tend to focus on the silicon development of the FPGAs, the tools to program them, and a limited set of sample or reference software blocks. They do not have plans to provide a complete solution that couples with software that addresses the specific needs of the telecommunications industry, as provided by Ethernity.

Over the last 16 years, Ethernity has developed network processing technology that fits into low-cost FPGA silicon and serves as direct competition to ASIC-based packet processing and network processing vendors like Broadcom, Marvel, EZchip, PMC, and many others. With its patented technology, the company has succeeded in delivering the functionalities provided by such vendors, including Carrier Ethernet Switch/Router and traffic management, across FPGA, enabling these technologies to be packaged with additional features, such as compression, fragmentation and reassembly, bonding, reordering, packet header manipulation, and encryption. Other features, like search and counters on a large number of flows are implemented in the FPGA using low-cost DDRs. Ethernity has deployed its solutions in over 600,000 systems because it provides advanced programmable networking at a similar price point to an ASIC.

The same features that have been deployed on FPGA for various appliances in previous generations are now part of the requirement for 5G NFV performance acceleration, and the company has utilised its existing FPGA firmware to deliver an FPGA-based NIC acceleration solution for 5G and the telecom cloud.

Gartner's February 2020 research report entitled "Market Trends: Function Accelerator Cards Disrupting Traditional Ethernet Adapter Market" defines function accelerator cards (FACs) as "a class of network interface hardware that help improve and accelerate server availability, bandwidth performance and data transport efficiency in a network, besides enabling connectivity to a network. While all FACs are essentially NICs, not all NICs are FACs." The report also defines the size of the market, by claiming that "by 2023, we estimate that one in three NICs (network interface cards) shipped will be a FAC," and further adds that "as 5G adoption also starts to grow, FACs will also be handy at the edge for offloading NFV functions. Product leaders at semiconductor providers must, therefore, optimise their NIC hardware for capabilities to support such use cases and redraw their product roadmaps for traditional NICs to include FAC functionalities."

Ethernity's FAC delivers the FPGA SmartNIC hardware, the functional acceleration FPGA firmware code, DPDK APIs to allow connectivity to any virtual network function (VNF) for acceleration, and control software supporting the majority of today's L2/L3 network control protocols operating seamlessly on top of the FPGA data plane code.

FPGA SmartNICs are often considered as high-end and expensive compared to SmartNICs that are based on multicore programmable ASICs, but Ethernity's approach to the SmartNIC market enables the use of FPGA SmartNICs at the same price point of ASIC-based multicore devices such as those offered by Mellanox and Broadcom. The goal is to change the paradigm and to allow FPGA SmartNICs to capture larger market share compared to ASIC-based SmartNIC offerings.

While there are other FPGA SmartNIC providers, most only provide the physical hardware FPGA card coupled with a piece of FPGA reference design code. Others provide solutions specifically for data centres, focusing on flow classification and load balancing. Ethernity is actually the only vendor today that provides complete network processing for implementation of router and security engine on FPGA (versus an ASIC offering), as well as offering a complete Router-on-NIC for FPGA SmartNIC that can operate with control software. Such an offering is uniquely positioned far beyond the functionality provided by general-purpose multicore programmable ASIC-based SmartNICs by providing complete router data plane functionality coupled with other unique data processing elements on top of the general SmartNIC functions.

Ethernity delivers its ACE-NIC100 FPGA SmartNIC card equipped with the required FPGA code to implement a complete router data plane on a NIC while using a single FPGA on the card without the need for an external low-level NIC ASIC controller (such as the Intel XL710) on the board. As the adoption of FPGA increases, it is expected that FPGA-based SmartNIC hardware will be available from a wide range of vendors, and even that FPGA SmartNICs will be coupled with

servers as a hardware package by the major server providers as a general purpose server for cloud providers. In this case, Ethernity will be ready, taking advantage of its many years of experience programming FPGAs for the telecommunications industry to deliver the required software package for the FPGA and the servers, completely decoupling the hardware from the software.

To summarise, Ethernity Networks is a leading innovator of software-defined network processing and security solutions on programmable hardware. The Company is a supplier of functional acceleration ethernet adapter cards on FPGA for virtualised networking appliances accelerating commercialisation through the launch of its 5G UPF offering based on the Ethernity ACE-NIC100 FPGA SmartNIC, providing innovative networking and security solutions on programmable hardware for accelerating telecom and cloud networks.

Ported onto any FPGA, Ethernity offers complete data plane processing with a rich set of networking features and robust security, to enable improved performance of a wide range of virtual functions to optimise networks. The ACE-NIC SmartNICs, ENET Flow Processors, and turnkey network appliances offer best-in-class fully programmable platforms for the telecom, cloud service provider, and enterprise markets.

The Company offers complete solutions that enable customers to stop burning CPU cores and to quickly adapt to changing conditions, improving time-to-market, and facilitating the deployment of edge computing, 5G, and Network Function Virtualisation (NFV). The Company's core technology, which is populated on programmable logic, enables delivering data offload functionality at the pace of software development, improves performance and reduces power consumption and latency, therefore facilitating the deployment of virtualisation of networking functionality.

# Financial Review

### Financial Performance

As stated in our interim results to 30 June 2019, the adoption of the new networking virtualisation market in which we operate experienced continued delays, and our revenues, as a consequence, reflect this delay with our operating costs, including development costs which were maintained as we complete our transition from an IP technology Company to a solutions provider Company, being in line with expectations. We are now, however, beginning to experience the market entering engagement and deployment stages.

The Company continues to operate in line with its budgeted cost base and R&D expense allocation and is expecting to generate positive cash flows from operating activities during 2021. Whilst this continues to be reviewed and adjusted where appropriate, R&D activity and related expenditure remains focused on product developments aligned with our transition to a solutions provider, the market and customer requirements.

### Highlights

- Revenues increased by 19.6% to $1.34m
- Gross margins increased by 41.6% to $1.15m
- Operating costs before amortisation of intangible assets, depreciation charges, changes in recognition of R&D costs and other non-operational charges decreased by 14.1% to $2.79m
- EBITDA Loss (adjusted for R&D capitalisation) improved by 35.3% to a loss of $1.52m

### Key financial results

#### Recognition of Research and Development Costs.

The Company maintained the methodology of recognising as an intangible asset the costs arising from development of its solutions, specifically the directly associated costs of its Research and Development centre. In terms of the criteria laid out under IAS38, these costs may be recognised from the development stage as an intangible asset arising from development (or from the development phase of an internal project) may be recognised as an intangible asset.

Subsequent to 30 June 2019, the Company reviewed the principles and criteria of IAS 38 as outlined (as further described in Note 3.I. to the Financial statements) and believes that it meets all of the defined criteria. However with the uncertainty that existed as to timing of revenues and completing contractual arrangements as from 1 July 2019, and giving due regard to the subsequent worldwide COVD-19 situation that subsequently arose in the early part of 2020, the Company concluded that with effect from 1 July 2019 it would no longer continue recognising the costs as an intangible asset.

The resultant effect of this is that Research and Development expenditure of $2,193,408 incurred during the period from 1 July 2019 to 31 December 2019 has been recognised as an expense and charged against income. Once there is greater clarity on the financial resources as well as the worldwide COVID-19 situation with the economic impact relating thereto being able to be better assessed, and when revenues can be estimated with greater certainty, the Company may once again elect to recognise the Research and Development costs as an intangible asset in terms of the principles outlined under IAS 38.

Furthermore, an independent Fair Value report was commissioned by the management to support the management assertion that the underlying value of the intangible asset exceeded the carrying value on the balance sheet. This was undertaken by Somekh Chaikin KPMG (an Israeli member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative) and the report concluded and supported the management assertion that no impairment of the intangible asset on the Balance Sheet is required.

## EBITDA

EBITDA, albeit it not a recognised reportable accounting measure, provides a meaningful insight into the operations of a Company when removing the non-cash elements from trading results along with recognising actual costs versus some IFRS adjustments, in this case being the amortisation and non-cash items charges in operating income and the effects of IFRS 16 treatment of operational leases.

The EBITDA for the year under review for the financial year ended 31 December 2019 would be presented as follows:

| | **US Dollar** | |
|---|---|---|
| | **For the year ended 31 December** | |
| | **2019** | **2018** |
| **Revenues** | **1,343,844** | **1,123,707** |
| Gross Margin as presented | 1,150,832 | 812,513 |
| *Gross Margin %* | *85.64%* | *72.31%* |
| Operating (Loss) Profit as presented | (4,542,773) | (2,785,731) |
| Adjusted for: | | |
| *Add back Amortisation of Intangible Assets* | *743,752* | *322,724* |
| *Add back Share based compensation charges* | *69,654* | *5,031* |
| *Add back vacation accrual charges* | *(14,454)* | *3,408* |
| *Add back depreciation charges on fixed assets* | *151,977* | *100,918* |
| *Add IFRS operating leases depreciation* | *(122,729)* | - |
| **EBITDA** | **(3,714,573)** | **(2,353,650)** |
| Adjusted for R&D expenses not taken to intangible assets in H2 19 | 2,193,408 | - |
| **Comparable EBITDA** | **(1,521,165)** | **(2,353,650)** |

The EBITDA as above indicates a significant improvement in the operations of the Company with a decline of the EBITDA losses (before accounting for the change in treatment of the R&D capitalisation) of 35.37%

## Summarised trading results

| | **US Dollar** | |
|---|---|---|
| | **Audited** | |
| | **For the year ended 31 December** | |
| | **2019** | **2018** |
| **Revenues** | **1,343,844** | **1,123,707** |
| **Gross Margin** | **1,150,832** | **812,513** |
| *Gross Margin %* | *85.64%* | *72.31%* |
| **Operating (Loss) Profit** | **(4,542,773)** | **(2,785,731)** |
| Net Financing income (expenses) | (5,259) | 238,542 |
| (Loss) Profit before tax | (4,548,032) | (2,547,189) |

| | | |
|---|---|---|
| Tax benefit (reversal of previous deferred tax benefit) | (613,228) | - |
| **Net comprehensive (loss) income for the year** | **(5,161,260)** | **(2,547,189)** |
| **Basic earnings per ordinary share** | **(0.16)** | **(0.08)** |
| **Diluted earnings per ordinary share** | **(0.16)** | **(0.08)** |
| **Weighted average number of ordinary shares for basic earnings per share** | **32,556,686** | **32,526,149** |

### Revenue Analysis

Revenues for the twelve months ended 31 December 2019 increased by 19.6% to $1.344m (2018: $1.124m). This result is a positive reflection of the upward trend anticipated due to the increased customer engagements.

### Margins

Gross margins remained above the anticipated 50% level that the Company models its forecasts on, with the 2019 gross margin being 85.64% as compared to 72.31% in 2018. As always, the gross margin will vary according to the revenue mix as Royalty and Design Win revenues achieve an approximate 100% gross margin before any sales commissions are accounted for.

During the 2019 financial year, sales commissions of $39,419 (2018 $76,187) were paid and charged to cost of sales. Excluding these, the gross profit on revenues for 2019 would have been 88.6% compared to 79.1% for 2018.

### Operating Costs and Research & Development Costs

As noted above, during the latter half of 2019, the Company revised its treatment of capitalising its Research and Development costs to the intangible asset, the result being reflected in the material increase in Research and Development Expenses charged to income during the year. Had this change in accounting treatment not been undertaken, the resultant increases (decreases) in Operating costs, adjusted for the amortisation of the intangible asset for 2019 would have been:

| | **31 December 2019 US$** | **31 December 2018 US$** | **Increase (Decrease) US$** | **%** |
|---|---|---|---|---|
| Research and Development Costs net of amortisation | (72,172) | 150,765 | (222,938) | (147.87%) |
| General and Administrative expenses | 1,426,376 | 1,291,175 | 135,201 | 10.47% |
| Marketing expenses | 1,434,670 | 1,804,886 | (370,216) | (20.51)% |
| Total | 2,788,874 | 3,246,826 | (457,952) | (14.10)% |

Operating costs were in line with the Company targets and expectations as planned with increases in General and Administrative costs.

While there were increases in some of the Research and Development costs before amounts charged to income for the amortisation of the capitalised Research and Development intangible asset, the overall comparable costs against 2018 reduced by $222,938.

The increase in the General and Administrative costs were driven primarily by the addition of a financial director in January 2019 along with increased insurance costs for product liability insurance, together amounting to $132,898 of the net increases.

Sales and Marketing costs declined over the previous year primarily due to a reduction of personnel and their related costs of approximately $273,251 along with reductions in costs of overseas travel and conferences costs of approximately $97,350

### Operating Loss and Net Comprehensive Loss for the Year

After taking the above into account along with discontinuing the capitalisation of Research and Development costs, the Operating Loss for the year was in line with expectations, with the operating loss in 2019 of $4,542,773 not being comparable to that of $2,785,731 in 2018 due to this reason. However when adjusting for the effects of the change of

recognising the Research and Developments costs as a charge to income, the year on year figures become a more meaningfully comparable, with a reduction in the EBITDA loss of $832,485, and adjusting the capitalised costs of $2,193,316, the operating losses reduce by $436,274 to $2,349,457 as compared to the previous year, with the reduction in the loss of 15.6% being mainly attributable to the reasons outlined above along with the increase in the EBITDA level.

As a result of the continued delays in the NFV market that persisted throughout most of the year, revenue targets were not achieved as planned albeit the operating costs were in line with expectations. Based on revised expectations of revenues as the delayed market unfolded, the operating results were in line with our expectations for the year.

## Balance Sheet

The balance sheet quick and current ratios of the Company remains sound at 1.88 and 1.81 respectively (2018 6.46 and 6.38 respectively), with the reduction in the ratios being directly related to the cash consumption and consumptive nature of the operations.

The net cash utilised and cash reserves are carefully monitored by the Board, who continue to assess, that subject to action to reduce and carefully manage cash, cash resources remain sufficient to meet the current and future adjusted planned requirements. Cash utilised in operating activities for the year is $3,269,215 (2018 $2,155,378) related mainly to the increase in the Research and Development cash costs being directed in the main toward the R&D and customer developments. Gross cash reserves remained positive at $3,670,745 including financial instruments as of 31 December 2019, (2018 $8,557,524) and in line with forecast outcomes.

Short term borrowings of $1,012,731 (2018 $133,497) arose due to timing differences in relation to access to notice deposits, requiring a short term facility to meet immediate cash requirements. This was closed off on the 23rd of March 2020 when term deposits fell due. Taking this into account with the above, net cash reserves at 31 December 2019 were $2,658,014 compared with $8,424,027 at 31 December 2018.

The Intangible Asset on the Balance Sheet at a carrying value of $8,436,010 (2018 $6,869,815) is a result of the Company having adopted from 2015, the provisions of IAS38 relating to the recognition of Development Expenses, which methodology as noted in this report was ceased from 1 July 2019. The useful life and the amortisation method of each of the intangible assets with finite lives are reviewed at least at each financial year end. If the expected useful life of an asset differs from the previous estimate, the amortisation period is changed accordingly. Such change is accounted for as a change in accounting estimate in accordance with IAS 8. The Company undertook a third party assessment by Somekh Chaikin KPMG (an Israeli member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative) to assess the fair value of the Intangible Asset and based on this Management are in their view, satisfied with the continued practice of capitalising costs in terms of IAS38.

## COVID-19 impact and funding

In January 2020, the Company's forecast for the financial year showed a movement into positive operational cash flow from the end of the first half of 2021, having taken into account the effects of the cash flow enhancement measures announced. However, on 8 April 2020 and further on 6 May 2020, it announced that the rapid pace of developments in connection with COVID-19 had caused levels of uncertainty and that, in common with many other companies, it may need to seek alternative sources of funding, including having applied for a grant from the Israel Innovation Authority (previously the Office of the Chief Scientist). The Board announced in the market update of 6 May 2020 that given the continued high levels of uncertainty created by COVID-19, in the absence of receiving the Innovation Authority grant, it was likely the Company would need to seek access to alternative funding in order to trade to its then current plan and maximise its ability to secure contracts and conclude negotiations on terms favourable to the Company.

On 17 June 2020, the Company announced that its application for the Innovation Authority grant had been declined and as a result, the Company had taken prompt action to institute further cash conservation measures, which include a reduction in R&D resources that are not tightly coupled to the deliveries around Ethernity's 5G UPF-based ACE-NIC100 product offering in order to maintain the Company's momentum in this area. The auditors make reference to the existence of a material uncertainty in relation to going concern within the audit report, to which we draw your attention, and this is further described in Note 2 to these statements.

In light of the change in status of the engagement with the Military/Aerospace T1 vendor as noted above in the Chief Executives Statement, the Company will need to secure additional short term funding in the latter half of H2 2020 either via short term finance arrangements or an additional issue of equity.

Other than that as discussed above, there are no items on the Balance Sheet that warrant further discussion outside of the disclosures made in the Annual Financial statements of this Annual Report.

**Mark Reichenberg**

Chief Financial Officer

25 June 2020

# Board of Directors

### Graham Woolfman FCA (Non-Executive Chairman)

Graham Woolfman is as an Independent Non-executive Director and Chairman. Graham is a Fellow of the Institute of Chartered Accountants in England and Wales, and previously a Partner and head of Corporate Finance at Levy Gee. He has over 25 years' experience advising and supporting growth businesses and was a founder Director of Gateway VCT plc. Formerly, Graham was the Managing Director of Intrust Corporate Finance Limited, and is currently a non-executive director of Filta Group Holdings plc quoted on AIM, and Catalyst Housing Group, a substantial Public Interest Entity (PIE).

### David Levi (Chief Executive Officer)

David has over 25 years in the telecom industry, with vast technical and business experience in ATM, voice, TDM, SONET/SDH, Ethernet and PON. Prior to founding Ethernity, David was the founder of Broadlight, a semiconductor company that developed BPON and GPON components and was acquired by Broadcom (BRCM) for $230 million. David invented the GPON protocol with two US patents registered in his name. Prior to this, David worked as Director of Product Marketing at ECI Telecom in the Broadband Access division, and Senior Product Line Manager at RAD, responsible for $50 million product line sales, a product manager at Tadiran 36 Communication, sales manager at Dynamode Ltd, and served as a Systems Engineer and project manager in the Israeli Defense Forces.

### Mark Reichenberg CA(SA) (Chief Financial Officer)

Mark is a qualified Chartered Accountant from South Africa. Previously Mark held the position of VP Business Development and Corporate Affairs Officer of the Magnolia Silver Jewellery Group Limited, was the CFO of GLV International Ltd, and prior to that, held the position of Group Financial Director of Total Client Services Ltd, a company listed on the Johannesburg Stock Exchange. Mark has held various senior financial director positions in retail, wholesale and logistics. Mark holds a B. Acc degree from the University of the Witwatersrand (WITS) in South Africa

### Shavit Baruch (VP Research and Development)

Shavit has over 25 years of experience in the telecom and datacom industry, with vast technical experience in ATM, Ethernet and SONET/SDH, both at components and system level. Prior to Ethernity Networks, Shavit served as Chief Architect at Native Networks, a start-up company developing products for Metro Ethernet market. Prior to this, in 2002, Shavit established Crescendo Networks, a start-up company enhancing data centre applications performance. Prior to the venture at Crescendo, Shavit served as R&D Director at ECI Telecom, where he was in charge of development of all transmission cards for one of the world's most successful broadband systems. Earlier Shavit worked at Lannet Data Communication, acquired by AVAYA, designing, together with Galileo, Ethernet switch on silicon.

### Neil Rafferty (Independent Non-Executive Director)

Neil has over 30 years of experience in the telecoms and technology sectors holding a variety of senior executive positions with AT&T, Global One and Cisco Systems. He has run businesses in Switzerland and The Netherlands and was CEO of Easynet plc (listed on the London Stock Exchange until it was acquired). Latterly he has been advising companies across a variety of sectors helping them implement growth strategies as well as sitting on a number of Boards. Neil holds a BA (Hons) degree from Newcastle Polytechnic.

### Chen Saft-Feiglin (Independent Non-Executive Director)

Chen Saft-Feiglin is a lawyer and notary admitted in Israel with more than 25 years of experience in commercial law, insolvency and recovery procedures, as well as many years of experience as a business and family mediator and family business consultant. Chen is the founder and owner of Chen Saft, People, Processes and Enterprises, providing consulting services for family firms and enterprises, mediation in commercial disputes, and divorce mediation. Previously, Chen was a partner at Saft Walsh Law Offices, a niche law practice handling corporate, M&A, insolvency,

private client work and general representation of foreign clients (private and corporate) in Israel. Chen holds an LLB from Bar Ilan University and an MBA majoring in business and managerial psychology from the College of Management Academic Studies. Chen served as a Lieutenant in the Israel Defense Forces.

### Zohar Yinon (Independent Non-Executive Director)

Zohar is currently the CEO of Bar Ilan University in Israel. Prior to that Zohar held the position of CEO of Hagihon Company Ltd, a position he held from September 2011 to January 2018. Previously, Zohar was the Chief Financial Officer of Israel Military Industries, Ltd. and VP Business Development in Granite Hacarmel Ltd. Zohar has held other roles in Israel's private and public sectors, including with companies traded on the Tel Aviv Stock Exchange. Zohar holds a B.A. in Economics and an MBA in Business Administration, both from Bar-Ilan University (Israel) and he has graduated in managerial programs of M&A and Corporate Governance from the Interdisciplinary Center ("IDC") in Herzliya. He was a member of the CTG global panel of experts evaluating new start-ups in the field of Clean-tech and has served as a board member in a wide range of companies including governmental, private, publicly listed and start-up companies. Zohar served as a Major in the Israel Defense Forces.

# Corporate Governance Statement

### Introduction

The Board is responsible to shareholders for the effective direction and control of the Company, with the aim of generating long-term success for the Company.

The directors recognise the importance of high standards of corporate governance and in accordance with the AIM Rules for Companies and their requirement to adopt a recognised corporate governance code, the Board has adopted the Quoted Companies Alliance Corporate Governance Code (the "the Code"). The QCA Code was developed by the QCA as an alternative corporate governance code applicable to AIM companies

As a company incorporated in Israel the Company also complies with the corporate governance provisions of Israel's Companies Law, 5759-1999 (the "Companies Law") as may be applicable, the more relevant of which relates to the constitution of the Board of Directors, the Audit Committee and the Remuneration Committee. Whilst the Israeli Law requirements are more onerous, these have been incorporated into the requirements and guidance under the QCA.

The Board believes that good corporate governance reduces risks within the business, promotes confidence and trust amongst stakeholders and is important in ensuring the effectiveness and efficiency of the Company's management framework.

The Code is based around 10 broad principles of good corporate governance, aimed at delivering growth, maintaining a dynamic management framework, and building trust. The application of the Code requires the Company to apply these 10 principles and to publish certain related disclosures on its website and in its Annual Report. The Company addresses the key governance principles defined in the QCA Code as outlined on the Company website.

Further details of the Company's approach to the 10 principles of the Code, with the most recent Company update being 19 February 2020, and how it applies these principles, can be found on the Company`s Website section for Investors, specifically the corporate governance disclosures at https://ethernitynet.com/investors/#1454056723887-bab53599-82b7.

### The Directors and the Board

The Board is comprised of three executive directors, David Levi, Mark Reichenberg and Shavit Baruch, and of four non-executive directors, Graham Woolfman (Chairman), Neil Rafferty, Chen Saft-Feiglin and Zohar Yinon. The balance between executive and non-executive directors encourages a diversity of views, and ensures the independence of the directors, not allowing any group to dominate the Board's decision making.

In accordance with Israel Companies Law, the Board must always have at least two external directors who meet certain statutory requirements of independence (the "External Directors"). The Company's External Directors are currently Chen Saft-Feiglin and Zohar Yinon. The term of office of an External Director is three years, which can be extended for two additional three-year terms. Under the Companies Law, External Directors are elected by shareholders by a special majority and may be removed from office only in limited cases. Any committee of the Board must include at least one External Director and the Audit Committee and Remuneration Committee must each include all of the External Directors (including one External Director serving as the chair of the Audit Committee and Remuneration Committee),

and a majority of the members of each of the Audit Committee and Remuneration Committee must comply with the director independence requirements prescribed by the Companies Law.

The detailed composition of the board is as follows:

| | |
|---|---|
| Graham Woolfman | Independent Non-Executive Chairman (re-elected 22 June 2020)<br>Chairman of the Nomination Committee<br>*(Companies Law precludes the Chairman from being a member of the Audit and Remuneration Committees)* |
| David Levi | Chief Executive Officer (re-elected 22 June 2020)<br>Nomination Committee member |
| Mark Reichenberg | Chief Financial Officer and Company Secretary (re-elected 22 June 2020) |
| Shavit Baruch | Vice President R&D (re-elected 22 June 2020) |
| Neil Rafferty | Independent Non-Executive Director (re-elected 22 June 2020)<br>Audit Committee member<br>Remuneration Committee member<br>Nomination Committee member |
| Chen Saft Feiglin | External Director<br>Remuneration Committee Chairman<br>Audit Committee member |
| Zohar Yinon | External Director<br>Audit Committee Chairman<br>Remuneration Committee member |

Biographical details of all the Directors are set out on further above.

## Operation of the Board

The Board is responsible for the overall strategy and financial performance of the Company and has a formal schedule of matters reserved for its approval. In order to lead the development of the strategy of the Company and the progress of financial performance, the Board is provided with timely information that enables the Board to review and monitor the performance of the Company and to ensure it is in line with the Company's objectives in order to achieve its strategic goals.

The CFO and Company Secretary, Mark Reichenberg is responsible for ensuring that the Company complies with the statutory and regulatory requirements and maintains high standards of corporate governance. He supports and works closely with the Chairman of the Board, the Chief Executive Officer and the Board committee chairs in setting agendas for meetings of the Board and its committees and supports the transfer of timely and accurate information flow from and to the Board and the management of the Company.

During 2019, the Board met formally on nine occasions. Board members also hold ad hoc discussions amongst themselves between formal Board meetings to discuss governance, financial, operational, and other business matters. A majority of the Board members constitutes the legal quorum for a board meeting, and all but two Board members attended all of the board meetings. All Directors receive a board pack comprising of an agenda and all relevant operational information in advance of each meeting.

Attendance at Board and Committee meetings by members of the Board during the year ended 31 December 2019 was as follows:

| | **Board** | **Audit Committee** | **Remuneration Committee** | **Nominations Committee** (Note 1) |
|---|---|---|---|---|
| ***Number of meetings*** | ***9*** | ***4*** | ***2*** | ***0*** |

| | | | | |
|---|---|---|---|---|
| Graham Woolfman | 9 | 4 (as invitee) | 2 (as invitee) | - |
| David Levi | 9 | 1 (as invitee) | 1 (as invitee) | - |
| Mark Reichenberg | 9 | 4 (as invitee) | 2 (as invitee) | - |
| Shavit Baruch | 9 | - | - | - |
| Neil Rafferty | 9 | 4 | 2 | - |
| Chen Saft-Feiglin | 8 | 4 | 2 | - |
| Zohar Yinon | 6 | 4 | 2 | - |

**Notes:**
1. There were no formal requirements for any Nominations Committee meetings during the period under review.

## Re-election of Directors

In accordance with the Company's Articles the Directors are required to serve for a period of no less than three years from the date of appointment, or in the case of Admission, for 3 years from the date of Admission of the Company to AIM.

In terms of the General Meeting of the Company held on 22 June 2020, the term of David Levi and Shavit Baruch, in their capacity as directors, has been extended until 22 June 2023, the term of Mark Reichenberg, Graham Woolfman and Neil Rafferty, in their capacity as directors, has been extended until 28 June 2023. The term of Chen Saft-Feiglin and Zohar Yinon, in their capacity as external directors, remains unchanged until 14 November 2020.

## Board Committees

The Board has established properly constituted Audit, Remuneration and Nomination Committees of the Board with formally delegated duties and responsibilities.

### Audit Committee

The UK Corporate Governance Code recommends that an audit committee should comprise at least three members who are independent non-executive directors, and that at least one member should have recent and relevant financial experience. The Israel Companies Law requires that at least two the External Directors and one other non-executive director are members of the committee, and that the Chairman of the Company may not be a member of the Committee.

The Audit Committee, which comprises the Independent Non-Executive and External Directors (excluding the Chairman) and by invite the Internal Auditor of the Company (if one is appointed) is chaired by Zohar Yinon with the remaining members being Chen Saft-Feiglin and Neil Rafferty. The Committee invites other members of the Board and the Auditors to attend meetings as appropriate. The Audit Committee has responsibilities which include the review of:

- The Company's internal control environment;
- Financial risks;
- Financial statements, reports, and announcements, including the Board's responsibility to present an annual report that is fair, balanced, and understandable. The Audit Committee evidences this review in a report to the Board following its meeting with the auditors to discuss their Report to the Audit Committee and includes an assessment of the information provided in support of the Board's statement on going concern and on any significant issues and how those issues were addressed;
- Independence of auditors, including a review of the non-audit services provided and the level of such fees relative to the audit fee. In reviewing the Annual Financial Statements, discussions take place with the Auditor`s without executive management present and discussions are also held on the effectiveness of external audit;
- Ensuring the Company has a policy which allows any member of staff to raise, in confidence, any concern about possible impropriety in matters of financial reporting or other matters, and to ensure that suitable arrangements are in place for a proportionate independent investigation of such matters including any follow-up action required.

During the year ended 31 December 2019, the Audit Committee met on four occasions and the matters considered included the following:

- The discussion and approval of the audit work plan for the 2018 year end audit, treatment of Capitalisation of the Research and Development costs and an update on the cash flow status.
- Consideration of the Company`s annual audited financial statements for the year ended 31 December 2018 and recommendation to the Board for publication thereof.

- Review of and formal recommendation to the Board for the Issuance of the Interim Unaudited Financial Statements as at 30th June 2019.
- Appointment of the new Internal auditor for the Company.

### Remuneration Committee

The Israel Companies Law requires that at least two of the External Directors and one other non-executive director are members of the committee, and that the Chairman of the Company may not be a member of the Committee.

The Remuneration Committee comprising the Independent Non-Executive and External Directors (excluding the Chairman) is chaired by Ms. Chen Saft-Feiglin with the other members being Neil Rafferty and Zohar Yinon. The Committee invites other members of the Board to attend meetings as appropriate.

The Remuneration Committee has responsibility for reviewing and recommending to the Board the remuneration and incentive arrangements for the executive and non-executive directors, and delegated authorities to the chief executive relating to senior staff. The Remuneration Committee also has responsibility for:

- Recommending to the Board the adoption of or variations to a Compensation Policy for Office Holders and monitoring its implementation.
- Recommending to the Board any changes to the remuneration and incentive arrangements in accordance with the policy, for each executive and non-executive director (excluding the External directors), and senior executives.

The remuneration of all External Directors is fixed in terms of Israel Companies Law.

During the year ended 31 December 2019, the Remuneration Committee met formally on two occasions and confirmed the following.

- Options to be granted in terms of the Company's Employee Share Option Scheme were approved and recommended to the Board for ratification.
- Review of the proposed Compensation Policy for Office Holders and the recommendation to the Board for the adoption thereof (as amended) for approval by a General Meeting of the shareholders.
- Confirmation that the Compensation Policy for Office Holders, as approved at the Annual General Meeting of the Shareholders held on 13 August 2019, had been implemented.

### Nominations Committee

The Committee's responsibilities include ensuring that the size and composition of the Board is appropriate for the needs of the Company including an assessment of the diversity profile, selecting the most suitable candidate or candidates for the Board and to oversee succession planning aspects for the Board.

This Committee comprises Independent Non-Executive Directors and is chaired by Graham Woolfman with Neil Rafferty as the other member.

During the year ended 31 December 2019, there were no formal requirements for the Nomination Committee to meet.

### Internal Control

The Board considers on an ongoing basis the process for identifying, evaluating, and managing significant risks faced by the Company. This has been in place throughout the year and up to the date of approval of the Financial Statements. The process is regularly reviewed by the Board. The Directors are responsible for the Company's system of internal control and for reviewing its effectiveness. However, such a system can only provide reasonable, but not absolute, assurance against material misstatement or loss. The Company's system of internal control includes appropriate levels of authorisation and segregation of duties. Financial information is presented to the Board regularly comprising management accounts and other financial data which allows for regular reviews of performance.

The Company's key internal financial control procedures include:

- A review by the Board of actual results compared with budget and forecasts;
- Reviews by the Board of year end forecasts;
- The establishment of procedures for capital expenditure and expenditure incurred in the ordinary course of business.

The external auditors are engaged to express an opinion on the financial statements. They discuss with management the reporting of operational results and the financial condition of the Company, to the extent necessary to express their audit opinion.

### Internal Audit

During the first quarter of 2019, the Internal Audit position was vacated. A replacement independent Internal Auditor was appointed as ratified by the Audit Committee on 11 November 2019.

### Insurance

The Company maintains appropriate insurance cover in respect of litigation against the Directors and Officers of the Company.

## Directors' Report

The Directors present their Annual Report and audited Financial Statements for the financial year ended 31 December 2019.

### Principal Activities

Ethernity Networks is a technology solutions provider that develops and delivers data processing technology and solutions used in high-end Carrier Ethernet applications across the telecom, mobile, security and data center markets. The Company's core technology, which is populated on programmable logic, enables delivering data offload functionality at the pace of software development, improves performance and reduces power consumption and latency, therefore facilitating the deployment of virtualisation of networking functionality.

The Company is headquartered in Israel.

### Results and Dividends

The Consolidated Statement of Comprehensive Income for the year is set out on further below. No dividend is proposed for the year.

### Risk Management

The Company's policies for managing risk arising from activities are set out in Note 26 of the Financial Statements.

### Directors

The current Directors of the Company are:

Graham Woolfman *Independent Non-Executive Chairman**

David Levi *Chief Executive Officer**

Mark Reichenberg *Chief Financial Officer**

Shavit Baruch *VP R&D**

Neil Rafferty *Independent Non-Executive Director**

Chen Saft-Feiglin *External Director***

Zohar Yinon *External Director***

* Reappointed 22 June 2020

** An independent director appointed as an External Director in terms of Israel Companies Law

### Directors' Interests

The interests of current Directors in shares and options are disclosed in the Directors' Remuneration Report set out in Note 28 of the financial statements.

## STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS

### Directors' Responsibilities

The Directors are responsible for preparing the Annual Report (including Director's Report and Strategic Report) and the financial statements in accordance with applicable laws and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. The Directors are also required to prepare financial statements in accordance with the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market (AIM).

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the European Union, subject to any material departures disclosed and explained in the financial statements;
- recognise the possible impact of COVID-19 on the Company as a whole;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the requirements of the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### Website Publication

The Directors are responsible for ensuring the Annual Report and the financial statements are made available on a website. Financial statements are published on the Company's website in accordance with legislation in the Israel and the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the Company's website is the responsibility of the Directors. The Directors' responsibility also extends to the ongoing integrity of the financial statements contained therein.

### COVID-19 and Going Concern

In light of the continued duration of the COVID-19 pandemic, and the uncertainty on the potential ongoing and future impact, the Board took certain steps to both safeguard the well-being of staff and to position the Company for the future. Where possible a work-from-home policy was implemented and all non-discretionary expenditure was curtailed. The Company also took prudent steps to mitigate any impact through certain short-term cash conservation measures, including a reduction by all directors of up to 50% of their remuneration, with 20% of the reduction deferred.

The implementation of these cash management measures expected to allow the Company to meet its planned objectives in the absence of a prolonged uncertain outlook due to the effects of COVID-19. However, the Company recognises that revenues are likely to be delayed due to COVID-19 uncertainty, including where engaged customers' functions are affected through remote working arrangements. The Board continues to closely monitor the situation and will take further action, as appropriate, to manage its working capital position and strengthen the balance sheet to support the execution of the Company's plans.

On 8 April 2020 and further on 6 May 2020, the Company announced that the rapid pace of developments in connection with COVID-19 had caused levels of uncertainty and that, in common with many other companies, it may need to seek alternative sources of funding, including having applied for a grant from the Israel Innovation Authority. On 17 June 2020 the Company advised the market in an update that the application for the grant from the Israel Innovation Authority had been declined. The Company went on to state that it had taken prompt action to institute further cash conservation measures, which include a reduction in R&D resources that are not tightly coupled to the deliveries around Ethernity's 5G UPF-based ACE-NIC100 product offering in order to maintain the Company's momentum in this area.

Furthermore, in light of the situation regarding the Israel Innovation Authority grant the Board has reviewed the Company's product developments to focus resources and solutions on its key markets and customers. The revised

focus will delay further developments in products outside of Ethernity's key focus on NFV (network function virtualisation) and the 5G market.

Due to not receiving the Innovation Authority grant the Company will seek access to additional funding in order to trade to its revised plan, strengthen its position in the emerging 5G network market, maximise its ability to secure contracts and conclude negotiations on terms favourable to the Company.

## Independent auditor's report

**To the Shareholders of**
**Ethernity Networks Ltd.**

### Opinion

We have audited the financial statements of Ethernity Networks Ltd. (the "Company"), which comprise the Statement of financial position as of 31 December 2019 and the Statement of comprehensive loss, the Statement of changes in equity and the Statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as of 31 December 2019 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' International *Code of Ethics for Professional Accountants (Including International Independence Standards)* (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Israel, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Material uncertainty related to going concern

We draw attention to Note 2 in the financial statements, which indicates that the Company incurred a net comprehensive loss of 5.2 million US dollars and negative cash flows from operating activities of 3.3 million US dollars during the year ended December 31, 2019. As stated in Note 2, these events or conditions, along with other matters as set forth in Note 2, indicate that a material uncertainty exists that may cast significant doubt on the company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

### Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the year ended 31 December 2019. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the *Material Uncertainty Related to Going Concern* section, we have determined the matters described below to be key audit matters to be communicated in our report.

| | Description of Key Audit Matter and why a matter of most significance in the audit | Description of Auditor's Response and Key Observations |
|---|---|---|
| Intangible assets | The intangible assets include development costs that are directly attributable to a project's development phase, provided they met the recognition requirements in accordance with International Accounting Standard (IAS) 38 'Intangible Assets'. As such, | Our audit work included, but was not restricted to:<br><br>In 2019,we performed substantive audit procedures relating to the capitalization of the intangible assets. We specifically tested on a sample basis that those capitalized development costs met the required criteria as outlined by IAS 38, until 30 June, 2019, and |

| | | |
|---|---|---|
| | there is inherent risk that intangible assets may be improperly capitalized. Also, such intangible assets not yet available for use are required to be tested for impairment irrespective of whether there is any indication of impairment. Both the capitalization and impairment of intangible assets involve significant management judgement and therefore identified capitalization and impairment of intangible assets as a significant risk, which was one of the most significant assessed risks of material misstatement | tested that management assessment and policy were in accordance with IAS 38 as well, in respect of ceasing the capitalization of these costs commencing July 1, 2019, as further described in Note 3.I and Note 10 to the Company's financial statements.<br><br>We also assessed the recoverability of these assets by testing management's estimation of the value in use as part of the Intangible Asset Impairment Test that was performed by external valuation (as described in Note 10).<br><br>Such assessment included the evaluation of the competence and objectivity of management's expert in accordance with ISA 500 (Audit Evidence), and involved the assistance of an internal expert, in accordance with ISA 620 (Using the work of an Auditor's Expert). The assessment also included testing of evidence obtained from various areas of the audit including cash flows forecasts of revenue, expenses and profitability, the appropriateness of discount rates used related to the capitalized intangible assets, the most recent and updated business plans, Valuation model, working capital, useful life and the compliance with the requirements of IAS 36, impairment of assets.<br><br>Based on the audit work performed, we have not identified any material misstatement in the capitalization of development costs, the cessation of capitalization and the impairment of intangibles |

## Information other than the financial statements and auditor's report thereon

Management is responsible for the other information. The other information comprises of the information included in the Annual Report and Financial Statements but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Responsibilities of management and the board of directors for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

The Board of Directors is responsible for overseeing the Company's financial reporting process.

## Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with

ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Board of Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board of Directors, we determine those matters that were of most significance in the audit of the financial statements of the year ended 31 December 2019 and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Nir Yenni.

FAHN KANNE & CO. GRANT THORNTON ISRAEL

Tel-Aviv, Israel, 25 June 2020

**STATEMENTS OF FINANCIAL POSITION**

| | | US dollars | |
|---|---|---|---|
| | | 31 December | |
| | Notes | 2019 | 2018 |
| **ASSETS** | | | |
| **Current** | | | |
| Cash and cash equivalents | 5 | 1,116,922 | 473,815 |
| Other short-term financial assets | 6 | 2,553,823 | 8,083,709 |
| Trade receivables | 7 | 427,162 | 642,085 |

| | Note | | |
|---|---|---|---|
| Inventories | | 166,905 | 116,012 |
| Other current assets | 8 | 362,791 | 409,250 |
| **Current assets** | | **4,627,603** | **9,724,871** |
| | | | |
| **Non-Current** | | | |
| Property and equipment | 9 | 525,542 | 606,057 |
| Deferred tax assets | 24 | 186,772 | 800,000 |
| Intangible asset | 10 | 8,436,010 | 6,869,815 |
| Right -of -use asset | 11 | 448,081 | - |
| Other long term assets | | 5,167 | - |
| **Non-current assets** | | **9,601,572** | **8,275,872** |
| | | | |
| **Total assets** | | **14,229,175** | **18,000,743** |
| | | | |
| **LIABILITIES AND EQUITY** | | | |
| **Current** | | | |
| Short Term Borrowings | 12 | 1,012,731 | 133,497 |
| Trade payables | | 325,240 | 288,308 |
| Other current liabilities | 11,13 | 1,126,007 | 1,084,728 |
| **Current liabilities** | | **2,463,978** | **1,506,533** |
| | | | |
| **Non-Current** | | | |
| IIA royalty liability | 14 | - | 6,578 |
| Lease liability | 11 | 306,783 | - |
| **Non-current liabilities** | | **306,783** | **6,578** |
| | | | |
| **Total liabilities** | | **2,770,761** | **1,513,111** |
| | | | |
| **Equity** | 15 | | |
| Share capital | | 8,039 | 8,039 |
| Share premium | | 23,396,310 | 23,396,310 |
| Other components of equity | | 892,891 | 760,849 |
| Accumulated deficit | | (12,838,826) | (7,677,566) |
| **Total equity** | | **11,458,414** | **16,487,632** |
| | | | |
| **Total liabilities and equity** | | **14,229,175** | **18,000,743** |

**The accompanying notes are an integral part of the financial statements.**

## STATEMENTS OF COMPREHENSIVE LOSS

| | Notes | US dollars<br>For the year ended<br>31 December<br>2019 | 2018 |
|---|---|---|---|
| Revenue | 17, 27 | 1,343,844 | 1,123,707 |
| Cost of sales | | 193,012 | 311,194 |
| Gross profit | | 1,150,832 | 812,513 |
| Research and development expenses | 18 | 2,855,896 | 473,489 |
| General and administrative expenses | 19 | 1,426,376 | 1,291,175 |
| Impairment losses of financial assets | | - | 132,799 |
| Marketing expenses | 20 | 1,434,670 | 1,804,886 |
| Other income | 21 | (23,337) | (104,105) |
| **Operating loss** | | **(4,542,773)** | **(2,785,731)** |
| Financing costs | 22 | (93,584) | (15,450) |
| Financing income | 23 | 88,325 | 253,992 |
| **Loss before tax** | | **(4,548,032)** | **(2,547,189)** |
| Tax expense | 24 | (613,228) | - |
| **Net comprehensive loss for the year** | | **(5,161,260)** | **(2,547,189)** |
| **Basic and diluted loss per ordinary share** | 25 | **(0.16)** | **(0.08)** |
| Weighted average number of ordinary shares for basic loss per share | | 32,556,686 | 32,526,149 |

**The accompanying notes are an integral part of the financial statements.**

## STATEMENTS OF CHANGES IN EQUITY

| | Amounts in US dollars (except number of shares) | | | | | |
|---|---|---|---|---|---|---|
| | Number of shares | Share Capital | Share premium | Other components of equity | Accumulated deficit | Total equity |
| **Balance at 1 January 2018** | **32,518,186** | **8,028** | **23,356,078** | **615,322** | **(5,130,377)** | **18,849,051** |
| Employee share-based compensation | - | - | 36,393 | 145,527 | - | 181,920 |
| Exercise of employee options | 38,500 | 11 | 3,839 | - | - | 3,850 |
| Net comprehensive loss for the year | - | - | - | - | (2,547,189) | (2,547,189) |
| **Balance at 31 December 2018** | **32,556,686** | **8,039** | **23,396,310** | **760,849** | **(7,677,566)** | **16,487,632** |
| Employee share-based compensation | - | - | - | 132,042 | - | 132,042 |
| Net comprehensive loss for the year | - | - | - | - | (5,161,260) | (5,161,260) |
| **Balance at 31 December 2019** | **32,556,686** | **8,039** | **23,396,310** | **892,891** | **(12,838,826)** | **11,458,414** |

**The accompanying notes are an integral part of the financial statements.**

## STATEMENTS OF CASH FLOWS

| | US dollars | |
|---|---|---|
| | For the year ended 31 December | |
| | 2019 | 2018 |
| **Operating activities** | | |
| Net comprehensive loss for the year | (5,161,260) | (2,547,189) |
| **Non-cash adjustments** | | |
| Depreciation of property and equipment | 151,997 | 100,918 |
| Depreciation of operating lease right of use asset | 122,729 | - |
| Share-based compensation | 69,654 | 5,031 |
| Amortisation of intangible assets | 734,752 | 322,724 |
| Amortisation of liabilities | 3,499 | (13,255) |
| IPO related costs | - | (9,514) |
| Deferred tax expenses | 613,228 | - |
| Foreign exchange gains on cash balances | (7,878) | (24,517) |
| **Net changes in working capital** | | |
| Decrease (increase) in trade receivables | 214,923 | (128,120) |
| Increase in inventories | (50,893) | (116,012) |
| Decrease in other current assets | 46,459 | 29,015 |
| Increase in other long-term assets | (5,167) | - |
| Increase in trade payables | 36,932 | 63,221 |
| Increase (decrease) in other liabilities | (99,612) | 162,320 |
| **Net cash used in operating activities** | **(3,330,637)** | **(2,155,378)** |
| **Investing activities** | | |
| Withdrawals from other short-term financial assets | 11,529,886 | 5,985,763 |
| Deposits to other short-term financial assets | (6,000,000) | (3,000,000) |
| Purchase of property and equipment | (71,482) | (551,135) |
| Amounts carried to intangible assets | (2,238,559) | (3,835,583) |
| **Net cash provided by (used in) investing activities** | **3,219,845** | **(1,400,955)** |
| **Financing activities** | | |
| Proceeds from exercise of options | - | 3,850 |
| Repayment of IIA liability | (20,834) | (5,300) |
| Proceeds from short term borrowings | 1,012,731 | 133,497 |
| Repayment of long-term borrowings | (133,497) | (7,522) |
| Repayment of lease liability | (112,379) | - |
| **Net cash provided by financing activities** | **746,021** | **124,525** |
| Net change in cash and cash equivalents | 635,229 | (3,431,808) |
| Cash and cash equivalents, beginning of year | 473,815 | 3,881,106 |
| Exchange differences on cash and cash equivalents | 7,878 | 24,517 |
| **Cash and cash equivalents, end of year** | 1,116,922 | 473,815 |
| **Supplementary information:** | | |
| Interest paid during the year | 2,727 | 813 |
| Interest received during the year | 88,325 | 197,949 |
| **Supplementary information on non-cash activities:** | | |
| Share-based compensation capitalised to intangible assets | 62,388 | 186,403 |
| Recognition of right-of-use asset and lease liability | 570,810 | - |

**The accompanying notes are an integral part of the financial statements.**

## NOTES TO THE FINANCIAL STATEMENTS

### NOTE 1 - NATURE OF OPERATIONS

ETHERNITY NETWORKS LTD. (hereinafter: the "Company"), was incorporated in Israel on the 15th of December 2003 as Neracore Ltd. The Company changed its name to ETHERNITY NETWORKS LTD. on the 10th of August 2004.

The Company provides innovative, comprehensive networking and security solutions on programmable hardware for accelerating telco/cloud networks performance. Ethernity's FPGA logic offers complete Carrier Ethernet Switch Router data plane processing and control software with a rich set of networking features, robust security, and a wide range of virtual function accelerations to optimize telecommunications networks. Ethernity's complete solutions quickly adapt to customers' changing needs, improving time-to-market and facilitating the deployment of 5G, edge computing, and different NFV appliances including 5G UPF, SD-WAN, vCMTS and vBNG with the current focus on 5G emerging appliances.. The Company's customers are situated worldwide.

In June 2017 the Company completed an Initial Public Offering ("IPO") together with being admitted to trading on the AIM Stock Exchange and issued 10,714,286 ordinary shares at a price of GBP 1.40 per share, for a total consideration of approximately $19,444,000 (GBP 15,000,000) before underwriting and issuance expenses. Total net proceeds from the issuance amounted to approximately $17,800,000.

### NOTE 2 - GOING CONCERN

The financial statements have been prepared assuming that the Company will continue as a going concern. Under this assumption, an entity is ordinarily viewed as continuing in business for the foreseeable future unless management intends or has no realistic alternative other than to liquidate the entity or to stop trading for at least, but not limited to, 12 months from the reporting date. The assessment has been made of the Company's prospects, considering all available information about the future, which have been included in the financial budget, from managing working capital and among other factors such as debt repayment schedules. Consideration has been given inter alia, to the current stage of the Company's life cycle, its losses and cash outflows, including with respect to the development of the Company's products, the expected timing and amounts of future revenues and the ability of the Directors to raise further funds either through debt, equity, or asset sales, or deferral of liabilities, their current assessment of financial and operational risk and their best estimate of the potential impact of COVID-19 on operations and the material uncertainties arising therefrom. As of 31 December 2019, the Company incurred an accumulated deficit of 12.8 million dollars and reported net comprehensive loss of 5.2 million dollars and negative cash flows from operating activities of 3.3 million dollars during the year ended December 31, 2019. The Company also has not yet generated material revenues from its operations to fund its activities and is therefore dependent upon external sources for financing its operations. The cash balances as of June 16, 2020 was approximately 540,000$.

In January 2020, the Company's forecast for the financial year showed a movement into positive operational cash flow from the end of the first half of 2021, having taken into account the effects of the cash flow enhancement measures announced. However, on 8 April 2020 and further on 6 May 2020, it announced that the rapid pace of developments in connection with COVID-19 had caused levels of uncertainty that, it may need to seek alternative sources of funding, including having applied for a grant from the Israel Innovation Authority. The Board announced in the market update of 17 June 2020 that the application for a grant from the Innovation Authority in Israel (previously the Office of the Chief Scientist) had been declined. As a result, the Company has taken prompt action to institute further cash conservation measures, which include a reduction in R&D resources that are not tightly coupled to the Company's key deliverables.

Furthermore, in light of the situation regarding the Innovation Authority grant, the Board will be reviewing the Company's product developments to focus resources and solutions on its key markets and customers.

The Company has renegotiated its short term banking facilities with its bankers, with the resultant new facility being a change from 550,000 NIS short term facility to a NIS 1,600,000 facility consisting of NIS 100,000 short term facilities and a NIS 1,500,000 revolving invoice financing facility.

Current internal forecasts based on information available at the date of the approval of these financial statements and using a variety of scenarios indicate that the Company may need to secure further funds and external sources in order to meet its current plans and liabilities as they fall due in the next 12 months. In the light of enquiries made, as well as bearing in mind the ability of the Company to raise funds previously, the Directors have a reasonable expectation that the Company has or will have access to adequate resources to continue in operational existence for the foreseeable future and therefore have adopted the going concern basis of preparation in the financial statements.

Notwithstanding, as described above, there is material uncertainty that may cast doubt on the Company's ability to continue as a going concern and fulfil its obligations and liabilities in the normal course of business in the near future. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

## NOTE 3 - SUMMARY OF ACCOUNTING POLICIES

The following accounting policies have been consistently applied in the preparation and presentation of these financial statements for all of the periods presented, unless otherwise stated. In 2019, new standards become effective as at 1 January 2019 – see note 3.X below.

### A. Basis of presentation of the financial statements and statement of compliance with IFRS

These financial statements have been prepared in accordance with International Financial Reporting Standards (hereinafter – “IFRS”), as issued by the International Accounting Standards Board ("IASB").

The financial information has been prepared on the historical cost basis.

The Company has elected to present profit or loss items using the function of expense method. Additional information regarding the nature of the expenses is included in the notes to the financial statements.

The financial statements for the year ended 31 December 2019 (including comparative amounts) were approved and authorised for issue by the board of directors on 25 June 2020.

### B. Use of significant accounting estimates and assumptions and judgements

The preparation of financial statements in conformity with IFRS requires management to make accounting estimates and assessments that involve use of judgment and that affect the amounts of assets and liabilities presented in the financial statements, the disclosure of contingent assets and liabilities at the dates of the financial statements, the amounts of revenues and expenses during the reporting periods and the accounting policies adopted by the Company. Actual results could differ from those estimates.

Estimates and judgements are continually evaluated and are based on prior experiences, various facts, external items and reasonable assumptions in accordance with the circumstances related to each assumption.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Regarding significant judgements and estimate uncertainties, see Note 4.

### C. Functional and presentation currency

The Company prepares its financial statements on the basis of the principal currency and economic environment in which it operates (hereinafter - the "functional currency").

The Company's financial statements are presented in US dollars ("US$") which constitutes the functional currency of the Company and the presentation currency of the Company.

### D. Foreign currency transactions and balances

Specifically identifiable transactions denominated in foreign currency are recorded upon initial recognition at the exchange rates prevailing on the date of the transaction. Exchange rate differences deriving from the settlement of monetary items, at exchange rates that are different than those used in the initial recording during the period, or than those reported in previous financial statements, are recognised in the statement of comprehensive income in the year of settlement of the monetary item. Other profit or loss items are translated at average exchange rates for the relevant financial year.

Assets and liabilities denominated in or linked to foreign currency are presented on the basis of the representative rate of exchange as of the date of the statement of financial position (spot exchange rate as published by the Bank of Israel).

Exchange rate differentials are recognised in the financial statements when incurred, as part of financing expenses or financing income, as applicable.

The exchange rates as at the 31st of December, of one unit of foreign currency to each US dollar, were:

| | **2019** | **2018** |
|---|---|---|
| New Israeli Shekel (“NIS”) | 0.289 | 0.267 |
| EURO | 1.319 | 1.279 |
| Sterling | 1.122 | 1.145 |

### E. Cash and cash equivalents

Cash and cash equivalents include cash on hand, call deposits and highly liquid investments, including short-term bank deposits (with original maturity dates of up to three months from the date of deposit), that are subject to an insignificant risk of changes in their fair value and which do not have restrictions as to what it may be used for.

### F. Property and equipment

Property and equipment items are presented at cost, less accumulated depreciation and net of accrued impairment losses. Cost includes, in addition to the acquisition cost, all of the costs that can be directly attributed to the bringing of the item to the location and condition necessary for the item to operate in accordance with the intentions of management.

The residual value, useful life span and depreciation method of fixed asset items are tested at least at the end of the fiscal year and any changes are treated as changes in accounting estimate.

Depreciation is calculated on the straight-line method, based on the estimated useful life of the fixed asset item or of the distinguishable component, at annual depreciation rates as follows:

| | % |
|---|---|
| Computers | 33 |
| Testing equipment | 10-33 |

| | |
|---|---|
| Furniture and equipment | 6-15 |
| Leasehold improvements | 33 |

Leasehold improvements are depreciated on a straight-line basis over the shorter of the lease term (including any extension option held by the Company and intended to be exercised) and the expected life of the improvement.

Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognised. An asset is derecognised on disposal or when no further economic benefits are expected from its use.

**G. Basic and diluted earnings (loss) per share**

Basic and diluted earnings (loss) per share is computed by dividing the income for the period applicable to Ordinary Shares by the weighted average number of shares of Ordinary Shares outstanding during the period.

In computing diluted earnings per share, basic earnings per share are adjusted to reflect the potential dilution that could occur upon the exercise of options or warrants issued or granted using the “treasury stock method”.

**H. Severance pay liability**

The Company's liability for severance pay pursuant Israel's Severance Pay Law is based on the last monthly salary of the employee multiplied by the number of years of employment, as of the date of severance.

Pursuant to section 14 of Severance Pay Law, which covers the Company's employees, monthly deposits with insurance companies release the Company from any future severance obligations in respect of those employees (defined contribution). Deposits under section 14 are recorded as an expense in the Company's statement of comprehensive income.

**I. Research and development expenses**

Expenditures on the research phase of projects to develop new products and processes are recognised as an expense as incurred.

Development activities involve a plan or a design for the production of new or substantially improved products and processes. Development costs that are directly attributable to a project’s development phase are recognised as intangible assets, provided they meet all of the following recognition requirements:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale.
- its intention to complete the intangible asset and use or sell it.
- its ability to use or sell the intangible asset.
- how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.
- its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Development costs not meeting these criteria for capitalisation are expensed as incurred.

Directly attributable costs include (if relevant) employee costs incurred on software development along with an appropriate portion of relevant overheads and borrowing costs.

The Company maintained the policy of recognising as an intangible asset the costs arising from development of its solutions, specifically the directly associated costs of its Research and Development centre.

Subsequent to 30 June 2019, the Company reviewed the principles and criteria of IAS 38 as outlined above and giving due regard to the uncertainty that exists as to the timing of revenues and the completion of contractual arrangements, effective as from 1 July 2019 the Company concluded that it would no longer continue recognising these costs as an intangible asset.

An intangible asset that was capitalized but not available for use, is not amortised and is subject to impairment testing once a year or more frequently if indications exist that there may be a decline in the value of the asset until the date on which it becomes available for use. (see also note 10).

The amortisation of an intangible asset begins when the asset is available for use, i.e., it is in the location and condition needed for it to operate in the manner intended by management. The development asset is amortised on the straight-line method, over its estimated useful life, which is estimated to be ten years.

The useful life and the amortisation method of each of the intangible assets with finite lives are reviewed at least at each financial year end. If the expected useful life of an asset differs from the previous estimate, the amortisation period is changed accordingly. Such change is accounted for as a change in accounting estimate in accordance with IAS 8.

Commencing 1 July 2019, the Company ceased to capitalize development expenses (see Note 10).

**J. Government grants**

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item (such as research and development of an intangible asset), it is recognised as 'other income' on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

Where the grant relates to an asset (such as development expenses that were recognised as an intangible asset), it is recognised a deduction of the related asset.

Grants from the Israeli Innovation Authority of the Ministry of Economy (hereinafter – the "IIA") in respect of research and development projects are accounted for as forgivable loans according to IAS 20 Accounting for Government Grants and Disclosure of Government Assistance.

Grants received from the IIA are recognised as a liability according to their fair value on the date of their receipt, unless on that there is reasonable assurance in that the amount received will not be refunded. The fair value is calculated using a discount rate that reflects a market rate of interest at the date of initial recognition. The difference between the amount received and the fair value on the date of receiving the grant is recognised as a deduction from the cost of the related asset or as other income, as applicable.

The amount of the liability is re-examined each period, and any changes in the present value of the cash flows discounted at the original interest rate of the grant are recognised in profit or loss.

The difference between the amount received and the fair value on the date of receiving the grant is recognised as a deduction of research and development expenses.

Grants which do not include an obligation to pay royalties are recognised as a deduction of the related asset or as other income, as applicable (See Note 21).

### K. Financial instruments

#### 1. Classification and measurement of financial assets and financial liabilities

**Initial recognition and measurement**

The Company initially recognizes trade receivables on the date that they are originated. All other financial assets and financial liabilities are initially recognized on the date on which the Company becomes a party to the contractual provisions of the instrument. As a rule, a financial asset or a financial liability are initially measured at fair value with the addition, for a financial asset or a financial liability that are not presented at fair value through profit or loss, of transaction costs that can be directly attributed to the acquisition or the issuance of the financial asset or the financial liability. Trade receivables that do not contain a significant financing component are initially measured at the price of the related transaction.

**Financial assets - subsequent classification and measurement**

On initial recognition, financial assets are classified to measurement at amortized cost.

Financial assets are not reclassified in subsequent periods, unless, and only to the extent that the Company changes its business model for the management of financial debt assets, in which case the affected financial debt assets are reclassified at the beginning of the reporting period following the change in the business model.

A financial asset is measured at amortized cost if it meets the two following cumulative conditions and is not designated for measurement at fair value through profit or loss:

- The objective of the entity's business model is to hold the financial asset to collect the contractual cash flows; and

- The contractual terms of the financial asset create entitlement on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The Company has balances of trade and other receivables and deposits that are held under a business model the objective of which is collection of the contractual cash flows. The contractual cash flows in respect of such financial assets comprise solely payments of principal and interest that reflects consideration for the time-value of the money and the credit risk. Accordingly, such financial assets are measured at amortized cost.

**Financial assets at amortized cost**

In subsequent periods, these assets are measured at amortized cost, using the effective interest method and net of impairment losses. Interest income, currency exchange gains or losses and impairment are recognized in profit or loss. Any gains or losses on derecognition are also carried to profit or loss.

#### 2. Financial assets at fair value through profit or loss

**Financial liabilities - classification, subsequent measurement and gains and losses**

Financial liabilities are classified to measurement at amortized cost or at fair value through profit or loss. Financial liabilities at fair value through profit or loss are measured at fair value, and any net gains and losses, including any interest expenses, are recognized in profit or loss. Other financial liabilities are measured at amortized cost in subsequent periods, using the

effective interest method. Interest expenses and currency exchange gains and losses are recognized in profit or loss. Any gains or losses on derecognition are also carried to profit or loss.

**Derecognition of financial liabilities**

Financial liabilities are derecognized when the contractual obligation of the Company expires or when it is discharged or cancelled. Additionally, a significant amendment of the terms of an existing financial liability, or an exchange of debt instruments having substantially different terms, between an existing borrower and lender, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability at fair value.

The difference between the carrying amount of the extinguished financial liability and the consideration paid (including any other non-cash assets transferred or liabilities assumed), is recognized in profit or loss. In the event of a non-material modification of terms (or exchange of debt instruments), the new cash flows are discounted at the original effective interest rate and the difference between the present value of financial liability under the new terms and the present value of the original financial liability is recognized in profit or loss.

**3. Impairment**

**Financial assets and contract assets**

The Company creates a provision for expected credit losses in respect of:

- Contract assets (as defined in IFRS 15).
- Financial assets measured at amortized cost.

The Company has elected to measure, if relevant, the provision for expected credit losses in respect of trade receivables, contract assets at an amount that is equal to the credit losses expected over the life of the instrument.

In assessing whether the credit risk of a financial asset has significantly increased since initial recognition and in assessing expected credit losses, the Company takes into consideration information that is reasonable and verifiable, relevant and attainable at no excessive cost or effort. Such information comprises quantitative and qualitative information, as well as an analysis, based on the past experience of the Company and the reported credit assessment, and contains forward-looking information.

**Measurement of expected credit losses**

Expected credit losses represent a probability-weighted estimate of credit losses. Credit losses are measured at the present value of the difference between the cash flows to which the Company is entitled under the contract and the cash flows that the Company expects to receive.

Expected credit losses are discounted at the effective interest rate of the financial asset.

**L. Off-set of financial instruments**

Financial instruments and financial liabilities are presented in the statements of financial position at their net value if the Company has a legal and enforceable right of offset and the Company intends on settling the asset and the liability on a net basis or simultaneously.

## M. Share-based compensation

Share-based compensation transactions that are settled by equity instruments that were executed with employees or others who render similar services, are measured at the date of the grant, based on the fair value of the granted equity instrument. This amount is recorded as an expense in profit or loss with a corresponding credit to equity, over the period during which the entitlement to exercise or to receive the equity instruments vests.

For purposes of estimating the fair value of the granted equity instruments, the Company takes into consideration conditions which are not vesting conditions (or vesting conditions that are performance conditions which constitute market conditions). Non-market performance and service conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting period, an estimate is made of the number of instruments expected to vest. Grants that are contingent upon vesting conditions (including performance conditions that are not market conditions) which are not ultimately met are not recognised as an expense. A change in estimate regarding prior periods is recognised in the statement of comprehensive income over the vesting period.

Share-based payment transactions settled by equity instruments executed with other service providers are measured at the date the services were received, based on the estimated fair value of the services or goods received, unless their value cannot be reliably estimated. In such a case, the transaction is measured by estimating the fair value of the granted equity instruments. This amount is carried as an expense or is capitalized to the cost of an asset (if relevant), based on the nature of the transaction. Share based compensation amounts related to grants that were forfeited, are reclassified to Share Premium.

## N. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value measurement is based on the assumption that the transaction will take place in the asset's or the liability's principal market, or in the absence of a principal market in the most advantageous market.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its best use or by selling it to another market participant that would use the asset in its best use.

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value. Maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities measured at fair value or for which fair value is disclosed are categorized into levels within the fair value hierarchy based on the lowest level input that is significant to the entire fair value measurement:

- Level 1 - unadjusted quoted prices are available in active markets for identical assets or liabilities that the Company has the ability to access as of the measurement date.

- Level 2 – pricing inputs are other than quoted prices in active markets that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data.
- Level 3 – pricing inputs are unobservable for the non-financial asset or liability and only used when there is little, if any, market activity for the non-financial asset or liability at the measurement date. The inputs into the determination of fair value require significant management judgment or estimation. Level 3 inputs are considered as the lowest priority within the fair value hierarchy.

**O. Transactions with controlling shareholders**

Transactions with controlling shareholders are recognised at fair value. Any difference between the fair value and the original terms of the transaction, represent capital contribution or dividend, as applicable and accordingly, carried to equity.

**P. Revenue recognition**

The Company generates revenues mainly from sales of programmable devices ("FPGA") that embed intellectual property ("IP") developed by the Company, or IP developed by the Company together with software application tools, to assist its customers to design their own systems based on the Company IP.

The Company recognises revenue when the customer obtains control over the promised goods or services. The revenue is measured according to the amount of the consideration to which the Company expects to be entitled in exchange for the goods or services promised to the customer.

**<u>Identification of the contract</u>**

The Company treats a contract with a customer only where all of the following conditions are fulfilled:

1. The parties to the contract have approved the contract (in writing, orally or according to other customary business practices) and they are committed to satisfying their obligations thereunder;
2. The Company is able to identify the rights of each party in relation to the goods or services that are to be transferred;
3. The Company is able to identify the payment terms for the goods or services that are to be transferred;
4. The contract has commercial substance (i.e., the entity's risk, timing and amount of future cash flows are expected to change as result of the contract); and
5. It is probable that the consideration to which the Company is entitled to in exchange for the goods or services transferred to the customer will be collected.

**<u>Identification of performance obligations</u>**

On the contract's inception date the Company assesses the goods or services promised in the contract with the customer and identifies as a performance obligation any promise to transfer to the customer one of the following:

1. Goods or services that are distinct; or
2. A series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer.

The Company identifies goods or services promised to the customer as being distinct when the customer can benefit from the goods or services on their own or in conjunction with other readily available resources and the Company's promise to transfer the goods or services to the customer

separately identifiable from other promises in the contract. In order to examine whether a promise to transfer goods or services is separately identifiable, the Company examines whether it is providing a significant service of integrating the goods or services with other goods or services promised in the contract into one integrated outcome that is the purpose of the contract.

**Determination of the transaction price**

The transaction price is the amount of the consideration to which the Company expects to be entitled in exchange for the goods or services promised to the customer, other than amounts collected for third parties. The Company takes into account the effects of all the following elements when determining the transaction price; variable consideration, the existence of a significant financing component, non-cash consideration, and consideration payable to the customer.

**Variable consideration**

The transaction price includes fixed amounts and amounts that may change as a result of discounts, credits, price concessions, incentives, penalties, claims and disputes and contract modifications where the consideration in their respect has not yet been agreed to by the parties.

The Company includes the amount of the variable consideration, or part of it, in the transaction price only when it is considered highly probable that its inclusion will not result in a significant revenue reversal in the future when the uncertainty has been subsequently resolved. At the end of each reporting period and if necessary, the Company revises the amount of the variable consideration included in the transaction price.

**Satisfaction of performance obligations**

Revenue is recognised when the Company satisfies a performance obligation by transferring control over promised goods or services to the customer, as applicable.

**Contract costs**

Incremental costs of obtaining a contract with a customer, such as sales fees to agents, are recognised as an asset when the Company is likely to recover these costs. Costs to obtain a contract that would have been incurred regardless of the contract are recognised as an expense as incurred unless the customer can be billed for those costs.

Costs incurred to fulfill a contract with a customer and that are not covered by another standard are recognised as an asset when they: relate directly to a contract the Company can specifically identify; they generate or enhance resources of the Company that will be used in satisfying performance obligations in the future; and they are expected to be recovered. In any other case the costs are recognised as an expense as incurred.

Capitalized costs are amortised in the statement of income on a systematic basis that is consistent with the pattern of transfer of the goods or services to which the asset relates.

In every reporting period, the Company examines whether the carrying amount of the asset recognised as aforesaid exceeds the consideration the entity expects to receive in exchange for the goods or services to which the asset relates, less the costs directly attributable to the provision of these goods or services that were not recognised as expenses, and if necessary an impairment loss is recognised in the statement of income.

**Contract modification**

A contract modification is a change in the scope or price (or both) of a contract that was approved by the parties to the contract. A contract modification can be approved in writing, orally or be implied by customary business practices.

When a contract modification has not yet been approved by the parties, the Company continues to recognise revenues according to the existing contract, while disregarding the contract modification, until the date the contract modification is approved or the contract modification is legally enforceable.

The Company accounts for a contract modification as an adjustment of the existing contract since the remaining goods or services after the contract modification are not distinct and therefore constitute a part of one performance obligation that is partially satisfied on the goods that are expected to be returned, instead of revenue, the Company recognises a refund liability. A right of return asset (and corresponding adjustment to cost of sales) is also recognised for the right to recover products from a customer, date of the contract modification. The effect of the modification on the transaction price and on the rate of progress towards full satisfaction of the performance obligation is recognised as an adjustment to revenues (increase or decrease) on the date of the contract modification, meaning on a catch-up basis.

Sales of goods

Revenues from sale of programmable devices are recognised at the point in time when control of the asset is transferred to the customer, generally on delivery of the devices.

Certain contracts provide a customer with a right to return the goods within a specified period. The Company uses the expected value method to estimate the goods that will not be returned because this method best predicts the amount of variable consideration to which the Company will be entitled. The requirements in IFRS 15 on constraining estimates of variable consideration are applied with respect to arrangements that provides such right of return, in order to determine the amount of variable consideration that can be included in the transaction price. Accordingly, the Company recognize amounts subject to right of return only if it is highly probable that there will not be a significant reversal of revenues if the estimate of expected returns changes. As of December 31, 2018 and 2019, there was no significant amount of goods that were subject to right of return.

Contracts with milestone payments

Certain contracts with major customers are structured to provide the Company with payment upon the achievements of certain predefined milestones which might include development of new product offerings ore new features of existing products such as programmable devices ("design tools").

Management has determined that the performance obligations under such arrangements are recognized at the point in time when control of the design tools is transferred to the customer, generally on delivery of the design tools.

As payments under the contract are dependent upon the Company's achievement of certain milestones, and as the payments are generally designed to depict the Company's performance under the arrangements, the Company measures progress toward satisfying the performance obligation based on the results actually achieved (i.e. the achievements of milestones) using the output method. Amounts received (including up-front payments), which relate to milestones that were non achieved yet, are deferred and presented as deferred revenues.

Multiple element transactions

Some of the Company's contracts with customers contain multiple performance obligations. For these contracts, the Company account for individual performance obligations separately if they

are distinct. The transaction price is allocated to the separate performance obligations on a relative standalone selling price basis. The Company determine the standalone selling prices based on our overall pricing objectives, taking into consideration market conditions and other factors.
Revenues are then recognized for each separate performance obligations - sales of goods or designed tools, based on the criteria described in the above paragraph.

Revenue from royalties

The Company is entitled to royalties based on sales by third parties, of products which consist IP developed by the Company.

For arrangements that include such sales-based royalties, including milestone payments based on the level of sales, and the license of the IP developed by the company is deemed to be the predominant item to which the royalties relate, the Company recognizes revenue at the later of (i) when the performance obligation to which some or all of the royalty has been allocated has been satisfied (or partially satisfied), or (ii) when the related sales occur.
Accordingly, revenues from royalties are recognized based on the actual sales of products as reported to the Company on a quarterly basis.

**Q. Income taxes**

Taxes on income in the statement of comprehensive loss comprise deferred taxes. Deferred taxes are recognised in the statement of comprehensive income, except to the extent that the tax arises from items which are recognised directly in other comprehensive income or in equity. In such cases, the tax effect is also recognised in the relevant item.

Deferred tax assets are recognised to the extent that it is probable that the underlying tax loss or deductible temporary difference will be utilised against future taxable income. This is assessed based on the Company's forecast of future operating results, adjusted for significant non-taxable income and expenses and specific limits on the use of any unused tax loss or credit. See also Note 24.

Deferred tax assets are presented in the statement of financial position as non-current assets.

**R. Operating cycle**

The normal operating cycle of the Company is a twelve-month period ending in December of each year.

**S. Impairment testing of other intangible assets and property and equipment**

For impairment assessment purposes, assets are grouped at the lowest levels for which there are largely independent cash inflows (cash-generating units). As a result, some assets are tested individually for impairment and some are tested at cash-generating unit level.

An impairment loss is recognised for the amount by which the asset's (or cash-generating unit's) carrying amount exceeds its recoverable amount, which is the higher of fair value less costs of disposal and value-in-use. To determine the value-in-use, management estimates expected future cash flows from each asset or cash-generating unit and determines a suitable discount rate in order to calculate the present value of those cash flows. The data used for impairment testing procedures are directly linked to the Company's latest approved budget, adjusted as necessary to exclude the effects of future reorganisations and asset enhancements. Discount factors are determined individually for each cash-generating unit assets and reflect current market assessments of the time value of money and asset-specific risk factors, see also Note 10.

**T. Ordinary shares**

Ordinary shares issued by the Company which do not meet the definition of financial liability or financial asset, were recognised as part of equity on the basis of the consideration received in respect thereof, net of costs attributed directly to the issue.

**U. Equity and reserves**

Share capital represents the nominal par value of shares that have been issued.

Share premium includes any premiums received on issue of share capital. Any transaction costs associated with the issuing of shares are deducted from share premium, net of any related income tax benefits.

**V. Provisions, contingent assets and contingent liabilities**

Provisions for legal disputes, onerous contracts or other claims are recognised when the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic resources will be required and amounts can be estimated reliably. Timing or amount of the outflow may still be uncertain.

No liability is recognised if an outflow of economic resources as a result of present obligations is not probable. Such situations are disclosed as contingent liabilities unless the outflow of resources is remote.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Provisions are discounted to their present values, where the time value of money is material.

Any reimbursement that the Company is virtually certain to collect from a third party with respect to the obligation is recognised as a separate asset. However, this asset may not exceed the amount of the related provision.

**W. Leased assets**

As described in Note 3.X. the Company has applied IFRS 16 from 1 January 2019 using the modified retrospective approach. Under this approach the cumulative effect of initially applying IFRS 16 is recognised as an adjustment to equity at the date of initial application. Comparative information is not restated.

**Accounting policy applicable from 1 January 2019 - the Company as a lessee**

For any new contracts entered into on or after 1 January 2019, the Company considers whether a contract is, or contains a lease. A lease is defined as 'a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration'. To apply this definition the Company assesses whether the contract meets three key evaluations which are whether:

- the contract contains an identified asset, which is either explicitly identified in the contract or implicitly specified by being identified at the time the asset is made available to the Company
- the Company has the right to obtain substantially all of the economic benefits from use of the identified asset throughout the period of use, considering its rights within the defined scope of the contract

- the Company has the right to direct the use of the identified asset throughout the period of use. The Company assesses whether it has the right to direct 'how and for what purpose' the asset is used throughout the period of use.

**Measurement and recognition of leases as a lessee**

At lease commencement date, the Company recognises a right-of-use asset and a lease liability on the balance sheet. The right-of-use asset is measured at cost, which is made up of the initial measurement of the lease liability, any initial direct costs incurred by the Company, an estimate of any costs to dismantle and remove the asset at the end of the lease, and any lease payments made in advance of the lease commencement date (net of any incentives received).

The Company depreciates the right-of-use assets on a straight-line basis from the lease commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The Company also assesses the right-of-use asset for impairment when such indicators exist.

At the commencement date, the Company measures the lease liability at the present value of the lease payments unpaid at that date, discounted using the interest rate implicit in the lease if that rate is readily available or the Company's incremental borrowing rate.

Lease payments included in the measurement of the lease liability are made up of fixed payments (including in substance fixed), variable payments based on an index or rate, amounts expected to be payable under a residual value guarantee and payments arising from options reasonably certain to be exercised.

Subsequent to initial measurement, the liability will be reduced for payments made and increased for interest. It is re-measured to reflect any reassessment or modification, or if there are changes in in-substance fixed payments.

When the lease liability is re-measured, the corresponding adjustment is reflected in the right-of-use asset, or profit and loss if the right-of-use asset is already reduced to zero.

The Company has elected to account for short-term leases and leases of low-value assets using the practical expedients. Instead of recognising a right-of-use asset and lease liability, the payments in relation to these are recognised as an expense in profit or loss on a straight-line basis over the lease term.

On the statement of financial position, right-of-use assets have been included under non-current assets and the current portion of lease liabilities have been included in other current liabilities.

**Accounting policy applicable before 1 January 2019 - the Company as a lessee**

**Finance leases**
Management applies judgment in considering the substance of a lease agreement and whether it transfers substantially all the risks and rewards incidental to ownership of the leased asset. Key factors considered include the length of the lease term in relation to the economic life of the asset, the present value of the minimum lease payments in relation to the asset's fair value, and whether the Company obtains ownership of the asset at the end of the lease term.

These assets are depreciated over the useful lives of the assets held under finance leases. The interest element of lease payments is charged to profit or loss as finance costs, over the period of the lease.

**Operating leases**

All other leases are treated as operating leases. Where the Company is a lessee, payments on operating lease agreements are recognised as an expense on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

**X. New Standard adopted as at 1 January 2019**

The Company has adopted the new accounting pronouncement for Leases which has become effective this year.

**IFRS 16 'Leases'**
IFRS 16 'Leases' replaces IAS 17 'Leases' along with its three related Interpretations.

The adoption of this new Standard has resulted in the Company recognising a right-of-use asset and related lease liability in connection with all former operating leases except for those identified as low-value or having a remaining lease term of less than 12 months from the date of initial application, which are accounted for as in the past - recognising the lease expense on a straight line basis over the remaining lease term.

The new Standard has been applied using the modified retrospective approach, with the cumulative effect of adopting IFRS 16 being recognised in equity as an adjustment to the opening balance of retained earnings for the current period. There was no such adjustment to the Company's retained earnings as the initial value of the right-of-use asset equalled the lease liability recorded. Prior periods have not been restated.

The Company has elected not to include initial direct costs in the measurement of the right-of-use asset for operating leases in existence at the date of initial application of IFRS 16, being 1 January 2019. At this date, the Company has also elected to measure the right-of-use assets at an amount equal to the lease liability adjusted for any prepaid or accrued lease payments that existed at the date of transition.

Instead of performing an impairment review on the right-of-use assets at the date of initial application, the Company has relied on its historic assessment as to whether leases were onerous immediately before the date of initial application of IFRS 16.

On transition to IFRS 16 the weighted average incremental borrowing rate applied to lease liabilities recognised under IFRS 16 was 4.2%.

The Company has benefited from the use of hindsight for determining the lease term when considering options to extend and terminate leases.

The following is a reconciliation of the financial statement line items from IAS 17 to IFRS 16 at 1 January 2019:

| | Carrying amount at 31 December 2018 | Remeasure-ment | IFRS 16 carrying amount at 1 January 2019 |
|---|---|---|---|
| Operating lease right of use asset | - | 441,068 | 441,068 |
| Lease liabilities | - | (441,068) | (441,068) |
| **Total** | - | - | - |

The following is a reconciliation of total operating lease commitments at 31 December 2018 (as disclosed in the financial statements to 31 December 2018) to the lease liabilities recognised at 1 January 2019:

| | US dollars |
|---|---|
| **Total operating lease commitments disclosed at 31 December 2018** | **579,000** |
| Recognition exemptions – lease of low value assets | (99,512) |
| **Operating lease liabilities before discounting** | **479,488** |
| Discounted using incremental borrowing rate | (38,420) |
| **Total lease liabilities recognised under IFRS 16 at 1 January 2019** | **441,068** |

## NOTE 4 - SIGNIFICANT MANAGEMENT JUDGEMENT IN APPLYING ACCOUNTING POLICIES AND ESTIMATION UNCERTAINTY

When preparing the financial statements, management makes a number of judgements, estimates and assumptions about the recognition and measurement of assets, liabilities, income and expenses.

**Significant management judgement**

- Capitalisation of internally developed intangible assets

  Distinguishing the research and development phases of a new or substantially improved customised research and development project and determining whether the recognition requirements for the capitalisation of development costs are met, requires judgement. After capitalization (if relevant), management monitors whether the recognition requirements continue to be met and whether there are any indicators that capitalized costs may be impaired (see Note 10).

**Estimation uncertainty**

- Impairment of non-financial assets

  In assessing impairment of non-financial assets (primarily, internally developed intangible assets – see Note 10), management estimates the recoverable amount of each asset or cash generating units (if relevant) based on expected future cash flows and uses an interest rate to discount them. Estimation uncertainty relates to assumptions about future operating results and the determination of a suitable discount rate.

- Useful lives of depreciable assets

  Management reviews its estimate of the useful lives of depreciable assets (including capitalized development expenses recognised as an intangible asset) at each reporting date, based on the expected utility of the assets. Uncertainties in these estimates relate to technological obsolescence that may change the utility of certain intangible assets (see Notes 9 and 10).

- Fair value measurement of employees' options

  Management uses valuation techniques to determine the fair value of employees' options. This involves developing estimates and assumptions consistent with how market participants would price the instrument. Management bases its assumptions on observable data as far as possible but this is not always available. In that case management uses the best information available. Estimated fair values may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date (see Note 16).

## NOTE 5 - CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

| | US dollars | |
|---|---|---|
| | 31 December | |
| | 2019 | 2018 |

| | | |
|---|---|---|
| In Sterling | 36,780 | 23,717 |
| In U.S. Dollar | 41,491 | 212,209 |
| In Euro | 3,862 | 12,260 |
| In New Israeli Shekel | 1,034,789 | 225,629 |
| | 1,116,922 | 473,815 |

**NOTE 6 - OTHER SHORT-TERM FINANCIAL ASSETS**

As at 31 December 2019, this consisted of one short term 12 month deposit of $2,500,000 earning an annual interest rate of 2.68%.

As at 31 December 2018, this consisted of one short term 12 month deposit of $8,000,000 earning an annual interest rate of 2.48%.

**NOTE 7 - TRADE RECEIVABLES**

Trade and other receivables consist of the following:

| | US dollars | |
|---|---|---|
| | 31 December | |
| | 2019 | 2018 |
| Trade receivables | 399,404 | 633,366 |
| Unbilled revenue | 102,758 | 83,719 |
| Less: provision for expected credit losses | (75,000) | (75,000) |
| **Total receivables** | 427,162 | 642,085 |

All amounts are short-term. The net carrying value of these receivables is considered a reasonable approximation of fair value. All of the Company's trade and other receivables have been reviewed for the possibility of loss (an allowance for impairment losses). See also Note 26A.

**NOTE 8 - OTHER CURRENT ASSETS**

Other current assets consist of the following:

| | US dollars | |
|---|---|---|
| | 31 December | |
| | 2019 | 2018 |
| Prepaid Expenses | 244,553 | 206,513 |
| Deposits to suppliers | 9,108 | 19,512 |
| Government institutions | 100,350 | 83,329 |
| Grant receivable | - | 99,896 |
| Other current assets | 8,780 | - |
| **Total other current assets** | 362,791 | 409,250 |

**NOTE 9 - PROPERTY AND EQUIPMENT**

Details of the Company's property and equipment are as follows:

**US dollars**

| | Testing equipment | Computers | Furniture and equipment | Leasehold improve-ments | Total |
|---|---|---|---|---|---|
| **Gross carrying amount** | | | | | |
| Balance 1 January 2019 | 486,709 | 237,826 | 74,284 | 60,102 | 858,921 |
| Additions | 65,633 | 4,287 | 1,562 | - | 71,482 |
| Balance 31 December 2019 | 552,342 | 242,113 | 75,846 | 60,102 | 930,403 |
| **Depreciation** | | | | | |
| Balance 1 January 2019 | (58,126) | (149,798) | (26,522) | (18,418) | (252,864) |
| Depreciation | (78,614) | (45,579) | (6,618) | (21,186) | (151,997) |
| Balance 31 December 2019 | (136,740) | (195,377) | (33,140) | (39,604) | (404,861) |
| **Carrying amount 31 December 2019** | **415,602** | **46,736** | **42,706** | **20,498** | **525,542** |

| | US dollars | | | | |
|---|---|---|---|---|---|
| | Testing equipment | Computers | Furniture and equipment | Leasehold improve-ments | Total |
| **Gross carrying amount** | | | | | |
| Balance 1 January 2018 | 43,844 | 202,845 | 47,649 | 13,448 | 307,786 |
| Additions | 442,865 | 34,981 | 26,635 | 46,654 | 551,135 |
| Balance 31 December 2018 | 486,709 | 237,826 | 74,284 | 60,102 | 858,921 |
| **Depreciation** | | | | | |
| Balance 1 January 2018 | (24,404) | (106,529) | (20,853) | (160) | (151,946) |
| Depreciation | (33,722) | (43,269) | (5,669) | (18,258) | (100,918) |
| Balance 31 December 2018 | (58,126) | (149,798) | (26,522) | (18,418) | (252,864) |
| **Carrying amount 31 December 2018** | **428,583** | **88,028** | **47,762** | **41,684** | **606,057** |

## NOTE 10 - INTANGIBLE ASSET

Details of the Company's intangible asset is as follows:

| | US dollars |
|---|---|
| | **Total** |
| **Gross carrying amount** | |
| Balance 1 January 2019 | 7,347,554 |
| Additions (*) (**) | 2,300,947 |
| Balance 31 December 2019 | 9,648,501 |
| **Amortisation** | |

| | |
|---|---|
| Balance 1 January 2019 | 477,739 |
| Amortisation | 734,752 |
| Balance 31 December 2019 | 1,212,491 |
| | |
| **Carrying amount 31 December 2019** | **8,436,010** |

(*) The additions include $62,388 of share based compensation.

(**) As described in Note 3.I. applicable development costs were capitalized and were recognized as intangible assets. However, as the Company did not meet all the measurement criteria of IAS 38 specifically with regard to being confident of sufficient financial resources for the 12 months following the date of this report, the Company ceased to capitalize development costs commencing the second half of 2019.

The Company commissioned an impairment test of the capitalized intangible assets as of 31 December 2019, by a top-tier independent international firm with expertise in valuation procedures. According to such independent report, the value in use of these intangible assets is approximately USD 27 million - more than three times the book value and accordingly there has been no need to record an impairment to such capitalized assets.

The valuation method determined, to best reflect the fair value of the intangible assets, was the discounted future cash flows expected to be generated from such assets between 2020 through 2029.

The primary assumptions used in determining the fair value of these intangible assets are as follows:

- Corporate tax rate for the Company remains at 23%.
- The pre-tax discount rate used to value future cash flows is 30.6% (post-tax 25%).

| | **US dollars** |
|---|---|
| | **Total** |
| **Gross carrying amount** | |
| Balance 1 January 2018 | 3,325,568 |
| Additions (*) | 4,021,986 |
| Balance 31 December 2018 | 7,347,554 |
| **Amortisation** | |
| Balance 1 January 2018 | 155,015 |
| Amortisation | 322,724 |
| Balance 31 December 2018 | 477,739 |
| | |
| **Carrying amount 31 December 2018** | **6,869,815** |

(*) The additions include $186,403 of share based compensation.

## NOTE 11 - LEASES

**A.** Details of the Company's operating lease right of use assets are as follows:

| | **US dollars** | | |
|---|---|---|---|
| | **Buildings** | **Vehicles** | **Total** |
| **Gross carrying amount** | | | |
| Balance 1 January 2019 | - | - | - |
| IFRS 16 adoption | 441,068 | - | 441,068 |

| | | | |
|---|---|---|---|
| Additions | - | 129,742 | 129,742 |
| Balance 31 December 2019 | 441,068 | 129,742 | 570,810 |
| | | | |
| **Accumulated depreciation** | | | |
| Balance 1 January 2019 | - | - | - |
| Depreciation expense | (112,614) | (10,115) | (122,729) |
| Balance 31 December 2019 | (112,614) | (10,115) | (122,729) |
| | | | |
| **Total right-of-use assets as at 31 December 2019** | **328,454** | **119,627** | **448,081** |

The vehicle right-of-use assets comprises 4 vehicles used by employees, all of which lease terms extend until the second half of 2022.

**B.** Lease liabilities are presented in the statement of financial position as follows:

| | US dollars |
|---|---|
| | 31 December |
| | 2019 |
| Current | 151,648 |
| Non-current | 306,783 |
| | **458,431** |

**C.** In December 2017, the Company committed to a three year lease agreement for its primary offices in the Industrial area of Lod, Israel. At the termination of the lease, the Company has an option to renew it for a further two years. In addition, the Company signed two other one year lease agreements for a total of 26 parking bays, with an option to extend them for another year. With the exception of short-term leases and leases of low-value underlying assets (the parking bay leases), each lease is reflected on the balance sheet as a right-of-use asset and a lease liability.

Each lease generally imposes a restriction that, unless there is a contractual right for the Company to sublet the asset to another party, the right-of-use asset can only be used by the Company. Leases are either non-cancellable or may only be cancelled by incurring a substantive termination fee. Some leases contain an option to purchase the underlying leased asset outright at the end of the lease, or to extend the lease for a further term. The Company is prohibited from selling or pledging the underlying leased assets as security. For leases over office buildings and factory premises the Company must keep those properties in a good state of repair and return the properties in their original condition at the end of the lease. Further, the Company must insure items of property, plant and equipment and incur maintenance fees on such items in accordance with the lease contracts.

**D.** The lease liabilities are secured by the related underlying assets. Future minimum lease payments at 31 December 2019 were as follows:

| | Minimum lease payments due | | | |
|---|---|---|---|---|
| | US dollars | | | |
| | **2020** | **2021** | **2022** | **Total** |
| Lease payments | 167,283 | 170,049 | 149,013 | 486,345 |
| Finance charges | (15,634) | (9,396) | (2,884) | (27,914) |
| **Net present values** | **151,649** | **160,653** | **146,129** | **458,431** |

**E.** Lease payments not recognised as a liability.

The Company has elected not to recognise lease liabilities for leases of low value assets (parking bays). Payments made under such leases are expensed on a straight-line basis. The expense for the year ended 31 December 2019, relating to payments not included in the measurement of the lease liability is $25,514.

**NOTE 12 - SHORT- TERM BORROWINGS**

Borrowings include the following financial liabilities:

| | Annual % Interest rate[1] | US dollars | |
|---|---|---|---|
| | | 31 December | |
| | 2019 | 2019 | 2018 |
| Bank borrowings [2] | 3.3% | 1,012,731 | 133,497 |
| **Total short- term borrowings** | | 1,012,731 | 133,497 |

[1] The loans bore variable interest of 3.3% (4.2% in 2018). The above interest rate is the weighted average rate as of 31 December 2019. The loan was fully repaid in March 2020.

[2] The Company has an unused credit facility of 550,000 NIS (approx. $159,000).

**NOTE 13 - OTHER CURRENT LIABILITIES**

Other short-term liabilities consist of:

| | US dollars | |
|---|---|---|
| | 31 December | |
| | 2019 | 2018 |
| Salaries, wages and related costs (see Note 28.B.) | 318,235 | 295,790 |
| Provision for vacation | 159,898 | 131,148 |
| Current portion of IIA royalty liability (see Note 14) | - | 10,757 |
| Accrued expenses and other | 70,472 | 235,965 |
| Deferred revenue [*] | 23,334 | 40,000 |
| Short term lease liability | 151,648 | - |
| Related parties (see Note 28.A.) | 402,420 | 371,068 |
| **Total other short-term liabilities** | 1,126,007 | 1,084,728 |

[*] These deferred revenues are recognized over 12 months starting from August 2019.

**NOTE 14 - IIA ROYALTY LIABILITY**

As described in Note 3.J., the Company received research and development grants from the Israel Innovation Authority ("IIA") of approximately $3,050,000 and undertook to pay royalties of approximately 3.5% of revenues derived from research and development projects that were financed by these grants up to 100% of the amounts received. As at 31 December 2019, the Company has repaid approximately $521,000 of these grants, in the form of royalties. The maximum amount of royalties that would be payable, if the Company had unlimited revenue attracting royalty obligations, would be approximately $2,700,000 as at 31 December 2019.

During the years 2005 through 2012, the Company received grants from the IIA (Israel Innovation Authority) totaling approximately $3.05 million, to support the Company's various research and development programs. The Company is required to pay royalties to the IIA at a rate of 3.5%, of the Company revenue up to an amount equal to the grants received, plus interest from the date of the

grant. The total amount including interest is approximately $2.7 million. Such contingent obligation has no expiration date.

## NOTE 15 - EQUITY

**A. Details regarding share capital and number of shares at 31 December 2019 and at 31 December 2018 are:**

**Share capital:**

| | US dollars | |
|---|---|---|
| | 31 December | |
| | **2019** | **2018** |
| Ordinary shares of NIS 0.001 par value | 8,039 | 8,039 |
| **Total share capital** | 8,039 | 8,039 |

**Number of shares:**

| | **Authorized** | **Issued and paid-in** |
|---|---|---|
| Ordinary shares of NIS 0.001 par value | 50,000,000 | 32,556,686 |

In the first half of 2017, prior to the IPO, the Company effected a 10:1 share split of all its authorized and issued, ordinary and preferred shares. The par value of the Company's shares reduced from NIS 0.01 to NIS 0.001. In addition, the number of all options and warrants granted prior to the share split, increased tenfold and the exercise price reduced by 90%. All share amounts in these financial statements have been adjusted to reflect this 10:1 share split.

**B. Description of the rights attached to the Ordinary Shares**

All ordinary shares have equal rights including voting rights, rights to dividends and to distributions upon liquidation. They confer their holder the rights to receive notices, attend and vote at general meetings.

**C. Other components of equity include the following:**

- Share premium includes any premiums received on the issue of share capital Including costs in respect of share-based payments to consultants for the issuance of equity instruments. Any transaction costs associated with the issuance of shares are deducted from the share premium, net of any related income tax benefit.
- Capital reserve includes the value of equity-settled share and option based payments provided to employees, consultants and third parties.

**D. IPO - Admission to the AIM exchange in London**

On 29 June 2017 the Company completed an IPO together with being admitted to trading on the AIM Stock Exchange and issued 10,714,286 ordinary shares at a price of GBP 1.40 per share, for a total consideration of approximately $19,444,000 (GBP 15,000,000) before underwriting and issuance expenses. Total net proceeds from the issuance amounted to approximately $17,800,000. Concurrent with the IPO, all the preferred shares were mandatorily converted into ordinary shares on a 1:1 basis, as mentioned in Note 15.D. The Company trades on the AIM Stock Exchange under the symbol "ENET".

Immediately after the IPO the Company issued certain prior shareholders, one year warrants to purchase up to 148,778 shares of the Company at an exercise price of GBP 1.40. These warrants expired in June 2018. In June 2017, the Company also issued five-year options to the IPO broker

to purchase up to 162,591 shares of the Company at an exercise price of GBP 1.40 (see Note 16.C.) The Company's last share price as at 31 December 2019 was GBP 0.435 (2018: GBP 0.325).

**NOTE 16 - SHARE-BASED COMPENSATION**

**A.** In 2013 the Company's Board of Directors approved a share option plan for the grant of options without consideration, to employees, consultants, service providers, officers and directors of the Company. The options are exercisable into the Company's ordinary shares of NIS 0.01 par value. The exercise price and vesting period (generally four years) for each grantee of options, is determined by the Company's Board of Directors and specified in such grantee's option agreement. In accordance with Section 102 of the Israel tax code, the Israeli resident grantees' options, are held by a trustee. The options are not cashless (they need to be paid for) and expire upon the expiration date determined by the Board of Directors (generally ten years from the date of the grant). The expiration date may be brought forward, upon the termination of grantee's employment or services to the Company. Options do not vest after the termination of employment or services to the Company. Options are not entitled to dividends.

The following table summarises the salient details and values regarding the options granted (all amounts are in US Dollars unless otherwise indicated):

The following table summarises the salient details and values regarding the options granted:

| | Option grant dates | | |
|---|---|---|---|
| | 17 Jul 2018 | 17 Jul 2018 | 25 Jul 2019 |
| Number of options granted | 160,000 | 280,000 | 180,000 |
| Recipients of the options | employees | consultants | employees |
| Approximate fair value at grant date: | | | |
| Total benefit | 16,632 | 29,106 | 32,621 |
| Per option benefit | 0.10 | 0.10 | 0.18 |
| Assumptions used in computing value: | | | |
| Risk-free interest rate | 2.85% | 2.85% | 2.05% |
| Dividend yield | 0.00% | 0.00% | 0.00% |
| Expected volatility | 40% | 40% | 40% |
| Expected term (in years) | 10 | 10 | 10 |
| Expensed amount recorded for year ended: | | | |
| 31 December 2018 | 1,515 | 11,075 | - |
| 31 December 2019 | 3,004 | 6,231 | 15,622 |
| Capitalised amount recorded for year ended: | | | |
| 31 December 2018 | 4,463 | - | - |
| 31 December 2019 | 2,572 | - | - |

The value of these options at 31 December 2019 which have yet to be recorded as expenses, amount to $91,698.

**A.** The following table presents a summary of the status of the option grants by the Company as of 31 December, 2019 and 2018:

| | **Number** | **Weighted average exercise price (US$)** |
|---|---|---|

| | Number | Weighted average exercise price (US$) |
|---|---|---|
| **Year ended 31 December 2019** | | |
| Balance outstanding at beginning of year | 3,145,920 | 0.42 |
| Granted | 180,000 | 1.25 |
| Exercised | - | - |
| Forfeited | (230,000) | 1.01 |
| Balance outstanding at end of the year | 3,095,920 | 0.43 |
| Balance exercisable at the end of the year | 2,521,420 | |

| | Number | Weighted average exercise price (US$) |
|---|---|---|
| **Year ended 31 December 2018** | | |
| Balance outstanding at beginning of year | 3,155,920 | 0.30 |
| Granted | 460,000 | 1.32 |
| Exercised | (38,500) | 0.10 |
| Forfeited | (431,500) | 0.16 |
| Balance outstanding at end of the year | 3,145,920 | 0.42 |
| Balance exercisable at the end of the year | 2,349,670 | |

**B.** The following table summarises information about options outstanding at 31 December 2019:

| Exercise price | Outstanding at 31 December 2019 | Weighted average remaining contractual life (years) | Weighted average exercise price (US$) | Exercisable at 31 December 2019 | Weighted average remaining contractual life (years) |
|---|---|---|---|---|---|
| $0.10 | 2,166,920 | 3.8 | 0.10 | 2,166,920 | 3.8 |
| $0.20 | 129,000 | 7.2 | 0.20 | 69,500 | 7.2 |
| £1.05 | 40,000 | 7.2 | 1.28 | 20,000 | 7.2 |
| £1.05 | 210,000 | 7.5 | 1.36 | 105,000 | 7.5 |
| £1.43 | 30,000 | 7.5 | 1.84 | 15,000 | 7.5 |
| £1.40 | 30,000 | 7.7 | 1.83 | 15,000 | 7.7 |
| £1.00 | 340,000 | 8.6 | 1.32 | 85,000 | 8.6 |
| £1.00 | 150,000 | 9.6 | 1.25 | 45,000 | 9.6 |
| | 3,095,920 | | | 2,521,420 | |

The following table summarises information about options outstanding at 31 December 2018:

| Exercise price | Outstanding at 31 December 2018 | Weighted average remaining contractual life (years) | Weighted average exercise price (US$) | Exercisable at 31 December 2018 | Weighted average remaining contractual life (years) |
|---|---|---|---|---|---|
| $0.10 | 2,236,920 | 4.9 | 0.10 | 2,202,420 | 4.8 |
| $0.20 | 129,000 | 8.2 | 0.20 | 37,250 | 8.2 |
| £1.05 | 40,000 | 8.2 | 1.28 | 10,000 | 8.2 |
| £1.05 | 210,000 | 8.5 | 1.36 | 52,500 | 8.5 |
| £1.43 | 30,000 | 8.5 | 1.84 | 7,500 | 8.5 |
| £1.40 | 30,000 | 8.7 | 1.83 | 7,500 | 8.7 |
| £1.40 | 30,000 | 8.7 | 1.89 | 7,500 | 8.7 |

| | | | | | |
|---|---|---|---|---|---|
| £1.00 | 440,000 | 9.6 | 1.32 | 25,000 | 9.6 |
| | 3,145,920 | | | 2,349,670 | |

The fair value of options granted to employees was determined at of the date of each grant. The fair value of the options granted are expensed in the profit and loss, except for those that were allocated to capitalised research and development costs (up to and including 30 June, 2019)

**C.** Options issued to the IPO broker

Upon the IPO consummation the Company issued five-year options to the IPO broker to purchase up to 162,591 shares of the Company at an exercise price of GBP 1.40. These options were valued at approximately $121,000 with the Black Scholes option model, using the assumptions of a risk-free rate of 1.82% and volatility of 46%. The options may only be exercised after 28 June 2018. As described in Note 3.U., costs incurred in raising equity finance is applied as a reduction from those equity sale proceeds and is recorded in Other Components of Equity.

## NOTE 17 - REVENUE

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Sales | 972,196 | 805,647 |
| Royalties | 371,648 | 318,060 |
| **Total revenue** | 1,343,844 | 1,123,707 |

## NOTE 18 - RESEARCH AND DEVELOPMENT EXPENSES

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Employee remuneration, related costs and subcontractors (*) | 2,049,839 | 122,004 |
| Maintenance of software and computers | 51,472 | 13,145 |
| Insurance and other expenses | 19,833 | 15,616 |
| Amortisation | 734,752 | 322,724 |
| **Total research and development expenses** | 2,855,896 | 473,489 |
| (*) Including share based compensation of: | 40,858 | - |

## NOTE 19 - GENERAL AND ADMINISTRATIVE EXPENSES

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Employee remuneration and related costs (*) | 478,908 | 339,566 |
| Professional fees | 388,290 | 505,540 |
| Rentals and maintenance | 266,808 | 342,185 |
| Depreciation | 274,726 | 100,918 |
| Travel expenses | 17,644 | 2,966 |
| **Total general and administrative expenses** | 1,426,376 | 1,291,175 |

| | | |
|---|---|---|
| (*) Including share based compensation of: | 17,861 | 33,540 |

## NOTE 20 - MARKETING EXPENSES

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Employee remuneration and related costs (*) | 643,526 | 545,129 |
| Marketing expenses | 758,580 | 1,139,669 |
| Travel expenses | 32,564 | 120,088 |
| **Total marketing expenses** | 1,434,670 | 1,804,886 |
| (*) Including share based compensation of: | 10,935 | (28,509) |

## NOTE 21 - OTHER INCOME

As described in Note 3.J, when the grant is related to an expense item, it is recognised as other income.

## NOTE 22 - FINANCING COSTS

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Bank fees and interest | 16,144 | 15,450 |
| Lease liability financial expenses | 17,584 | - |
| Exchange rate differences | 59,856 | - |
| **Total financing costs** | 93,584 | 15,450 |

## NOTE 23 - FINANCING INCOME

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Interest and revaluation of embedded derivative on shareholder loans | - | 20,417 |
| Interest received | 88,325 | 197,949 |
| Exchange rate differences | - | 35,626 |
| **Total financing income** | 88,325 | 253,992 |

## NOTE 24 - TAX EXPENSE

**A.** The Company is assessed for income tax in Israel - its country of incorporation. The Israeli corporate tax rates for the relevant years are:

| | % |
|---|---|
| 2018 | 23.0 |
| 2019 | 23.0 |

**B.** As of 31 December 2019, the Company has carry-forward losses for Israeli income tax purposes of approximately $14 million. According to the revised management's estimation of the Company's future taxable profits, it is no longer probable in the foreseeable future, that future taxable profits would be utilise all the tax losses.

**C. Deferred taxes**

| | US dollars | | |
|---|---|---|---|
| | Year ended 31 December | | |
| | **Origination and reversal of temporary differences** | **Utilisation of previously recognised tax loss carry-forwards** | **Total Deferred tax expense** |
| **Balance at 1 January 2018** | 186,772 | 613,228 | 800,000 |
| **Balance at 31 December 2018** | 186,772 | 613,228 | 800,000 |
| Deductions (*) | - | (613,228) | (613,228) |
| **Balance at 31 December 2019** | 186,772 | - | 186,772 |

(*) For the year ended 31 December 2019, the Company reduced the carrying amount of the deferred tax assets, for carry-forward tax losses, to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of all of that deferred tax asset to be utilized.

**D. Theoretical tax reconciliation**

For the years ended 31 December 2019 and 2018, the following table reconciles the expected tax expense (benefit) per the statutory income tax rate to the reported tax expense in profit or loss as follows:

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | **2019** | **2018** |
| Tax expense (benefit) at statutory rate | 23% | 23% |
| Expected tax expense (benefit) at statutory rate | (1,046,047) | (585,853) |
| Increase in taxes from permanent differences in share-based compensation | 16,020 | 44,030 |
| Increase in loss carryforwards - not affecting the deferred tax asset | 1,030,027 | 541,824 |
| Deferred tax expense - reversal of temporary differences | 613,228 | - |
| Income tax expense | 613,228 | - |

**NOTE 25 - BASIC AND DILUTED LOSS PER ORDINARY SHARE**

**A.** The earnings and the weighted average number of shares used in computing basic loss per ordinary share, are as follows:

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | **2019** | **2018** |
| Loss for the year attributable to ordinary shareholders | (5,161,260) | (2,547,189) |

**Number of shares**

| | Year ended 31 December | |
|---|---|---|
| | 2019 | 2018 |
| Weighted average number of ordinary shares used in the computation of basic loss per ordinary share | 32,556,686 | 32,526,149 |

**B.** The earnings and the weighted average number of shares used in computing diluted loss per ordinary share, are as follows:

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Loss for the year attributable to ordinary shareholders | (5,161,260) | (2,547,189) |

| | Number of shares | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Weighted average number of ordinary shares | 32,556,686 | 32,526,149 |
| Weighted average number of free shares from share options | 1,900,421 | 1,734,348 |
| Weighted average number of ordinary shares used in the computation of diluted loss per ordinary share | 34,457,107 | 34,260,497 |

## NOTE 26 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### A. Financial risk management risk

The activity of the Company exposes it to a variety of financial risks and market risks. The Company re-assesses the financial risks in each period and makes appropriate decisions regarding such risks. The risks are managed by Company management which identifies, assesses and hedges against the risks.

- **Exposure to changes in exchange rates**

  The Company is exposed to risks relating to changes in the exchange rate of the NIS and other currencies versus the U.S. dollar (which constitutes the Company's functional currency). Most of the revenues of the Company are expected to be denominated in US dollars, while the substantial majority of its expenses are in shekels (mainly payroll expenses). Therefore, a change in the exchange rates may have an impact on the results of operations of the Company.

**Currency basis of monetary balances**

| | US dollars | | | | |
|---|---|---|---|---|---|
| | 31 December 2019 | | | | |
| | NIS | GBP | Euro | US $ | Total |
| **Assets** | | | | | |
| Cash and cash equivalents | 1,034,789 | 36,780 | 3,862 | 41,491 | 1,116,922 |
| Other short-term financial assets | - | - | - | 2,553,823 | 2,553,823 |
| Trade receivables | - | - | - | 427,162 | 427,162 |
| Other current assets | 362,791 | - | - | - | 362,791 |
| | 1,397,580 | 36,780 | 3,862 | 3,022,476 | 4,460,698 |
| **Liabilities** | | | | | |
| Short term borrowings | 1,012,731 | - | - | - | 1,012,731 |

| | | | | | |
|---|---|---|---|---|---|
| Trade payables | 223,817 | 32,638 | - | 68,785 | 325,240 |
| Other liabilities | 1,055,690 | - | - | 70,317 | 1,126,007 |
| Non-current lease liabilities | 306,783 | | | | 306,783 |
| | 2,599,021 | 32,638 | - | 139,102 | 2,770,761 |
| | | | | | |
| | (1,201,441) | 4,142 | 3,862 | 2,883,374 | 1,689,937 |

**Currency basis of monetary balances**

| | US dollars | | | | |
|---|---|---|---|---|---|
| | 31 December 2018 | | | | |
| | **NIS** | **GBP** | **Euro** | **US $** | **Total** |
| **Assets** | | | | | |
| Cash and cash equivalents | 225,629 | 23,717 | 12,260 | 212,209 | 473,815 |
| Other short-term financial assets | - | - | - | 8,083,709 | 8,083,709 |
| Trade receivables | 43,085 | - | - | 599,000 | 642,085 |
| Other current assets | 267,405 | 39,002 | - | 102,843 | 409,250 |
| | 536,119 | 62,719 | 12,260 | 8,997,761 | 9,608,859 |
| **Liabilities** | | | | | |
| Short term borrowings | 133,497 | - | - | - | 133,497 |
| Trade payables | 198,416 | 3,517 | - | 86,375 | 288,308 |
| Other liabilities | 823,971 | - | - | 260,757 | 1,084,728 |
| | 1,155,884 | 3,517 | - | 347,132 | 1,506,533 |
| | | | | | |
| | (619,765) | 59,202 | 12,260 | 8,650,629 | 8,102,326 |

- **Sensitivity to changes in exchange rates of the NIS and other currencies to the US dollar**

  A change in the exchange rate of the NIS and other currencies to the USD as of the dates of the relevant statement of financial position, at the rates set out below, which according to Management are reasonably possible, would increase (decrease) the profit and loss by the amounts set out below. The analysis below was performed under the assumption that the rest of the variables remained unchanged.

| | US dollars | | | | |
|---|---|---|---|---|---|
| | Sensitivity to changes in exchange rates of the non US dollar currencies to the US dollar | | | | |
| | Effect on profit (loss)/equity (before tax) from the changes caused by the market factor | | Book value | Effect on profit (loss)/equity (before tax) from the changes caused by the market factor | |
| | Increase at the rate of | | 31 December | Decrease at the rate of | |
| | **10%** | **5%** | **2019** | **5%** | **10%** |
| Cash and cash equivalents | (107,543) | (53,772) | 1,075,431 | 53,772 | 107,543 |
| Other current assets | (36,279) | (18,140) | 362,791 | 18,140 | 36,279 |
| Short Term Borrowings | 101,273 | 50,637 | (1,012,731) | (50,637) | (101,273) |
| Trade payables | 25,646 | 12,823 | (256,455) | (12,823) | (25,646) |
| Other liabilities | 105,569 | 52,785 | (1,055,690) | (52,785) | (105,569) |
| Non-current lease liability | 30,678 | 15,339 | (306,783) | (15,339) | (30,678) |
| **Total** | **119,344** | **59,672** | **(1,193,437)** | **(59,672)** | **(119,344)** |

| | US dollars | | | | |
|---|---|---|---|---|---|
| | Sensitivity to changes in exchange rates of the non US dollar currencies to the US dollar | | | | |
| | Effect on profit (loss)/equity (before tax) from the changes caused by the market factor | | Book value | Effect on profit (loss)/equity (before tax) from the changes caused by the market factor | |
| | Increase at the rate of | | 31 December | Decrease at the rate of | |
| | 10% | 5% | 2018 | 5% | 10% |
| Cash and cash equivalents | (26,161) | (13,080) | 261,606 | 13,080 | 26,161 |
| Trade receivables | (4,309) | (2,154) | 43,085 | 2,154 | 4,309 |
| Other current assets | (30,641) | (15,320) | 306,407 | 15,320 | 30,641 |
| Short Term Borrowings | 13,350 | 6,675 | (133,497) | (6,675) | (13,350) |
| Trade payables | 20,193 | 10,097 | (201,933) | (10,097) | (20,193) |
| Other liabilities | 82,397 | 41,199 | (823,971) | (41,199) | (82,397) |
| **Total** | **54,829** | **27,417** | **(548,303)** | **(27,417)** | **(54,829)** |

- **Credit risk**

  All of the cash and cash equivalents and other short-term financial assets as of 31 December, 2019 and 2018 were deposited with one of the major banks in Israel.

  Trade receivables as of 31 December, 2019 and 2018 were from customers in Israel, the U.S., Asia and countries of the European Union, which included the major customers as detailed in Note 27. The Company performs ongoing reviews of the credit worthiness of customers, the amount of credit granted to customers and the possibility of loss therefrom. The Company includes an adequate allowance for impairment losses. As at 31 December 2019, the provision for expected credit losses was $75,000 (2018: $75,000).

  As of 31 December 2019 the trade receivables, after deducting the provision for expected credit losses, amounted to 3.8 months of 2019 annual revenue (2018: 6.9 months of 2018 annual revenue). See Note 7 for more details.

- **Trade receivables**

  IFRS 9 provides a simplified model of recognising lifetime expected credit losses for all trade receivables as these items do not have a significant financing component.

  In measuring the expected credit losses, the trade receivables have been assessed by management on a collective basis as well as on a case by case basis. Trade receivables are written off when there is no reasonable expectation of recovery. Management have indicated a concern regarding the receivable from one customer, for which a provision has been made.

  Management have concluded that there is no material risk of non-collection, regarding the balance of these receivables and therefore no further provision is necessary

- **Liquidity risk**

  The Company financed its activities from its operations, Shareholders' loans and short and long-term borrowings from the bank. Subsequent to the IPO, the Company has large cash resources to finance and expand its operations. All the non-current liabilities at 31 December 2018 were repaid in 2019. The short-term borrowings at 31 December 2019 were repaid in 2020 and the trade payables and other current liabilities are expected to be paid within 1 year.

## B. Fair value of financial instruments

**General**

The financial instruments of the Company include mainly trade receivables and debit balances, credit from banking institutions and others, trade payables and credit balances, IIA liability, and balances from transactions with shareholders.

The principal methods and assumptions used in calculating the estimated fair value of the financial instruments are as follows (fair value for disclosure purposes):

**Financial instruments included in current asset items**
These instruments (cash and cash equivalents, other short-term financial assets, trade receivables and debit balances) are of a current nature and, therefore, the balances as of 31 December, 2019 and 2018, approximate their fair value.

**Financial instruments included in current liability items**
These instruments (credit from banking institutions and others, trade payables and credit balances, suppliers and service providers and balances from transactions with shareholders) - in view of the current nature of such instruments, the balances as of 31 December, 2019 and 2018 approximate their fair value.

**C. Capital management**

The objectives of the Company's policy are to maintain its ability to continue operating as a going concern with a goal of providing the shareholders with a return on their investment and to maintain a beneficial equity structure with a goal of reducing the costs of capital. The Company may take different steps toward the goal of preserving or adapting its equity structure, including a return of equity to the shareholders and/or the issuance of new shares for purposes of paying debts and for purposes of continuing the research and development activity conducted by the Company. For the purpose of the Company's capital management, capital includes the issued capital, preference shares, share premium and all other equity reserves attributable to the equity holders of the Company.

## NOTE 27 - SEGMENT REPORTING

The Company has implemented the principles of IFRS 8 ('Operating Segments'), in respect of reporting segmented activities. In terms of IFRS 8, the management has determined that the Company has a single area of business, being the development and delivery of high end network processing technology.

The Company's revenues from customers are divided into the following geographical areas:

| | US dollars | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Asia | 60,840 | 203,000 |
| Europe | - | 117,888 |
| Israel | 437,479 | 324,220 |
| United States | 845,525 | 478,600 |
| | 1,343,844 | 1,123,708 |

| | % | |
|---|---|---|
| | Year ended 31 December | |
| | 2019 | 2018 |
| Asia | 4.5% | 18.1% |

| | | |
|---|---|---|
| Europe | 0.0% | 10.5% |
| Israel | 32.6% | 28.9% |
| United States | 62.9% | 42.6% |
| | 100.0% | 100.0% |

Revenue from customers in the Company's domicile, Israel, as well as its major market, the Unites States, Asia and Europe, have been identified on the basis of the customer's geographical locations.

The Company's revenues from major customers as a percentage of total revenue was:

| | % | |
|---|---|---|
| | Year ended 31 December | |
| | **2019** | **2018** |
| Customer A | 28% | 28% |
| Customer B | 28% | 22% |
| Customer C | 21% | 18% |
| Customer D | 8% | 11% |
| Customer E | 8% | 10% |
| | 93% | 89% |

## NOTE 28 - RELATED PARTIES

### A. Founders

In accordance with the employment agreements of the two founders of the Company, Mr. David Levi and Mr. Baruch Shavit, both were entitled to an annual bonus of 5% of the Company's revenue for the years 2012-2015 if the Company had positive cash flow from operations. This was in addition to their salaries and share based compensation.

In April 2017, the employment agreement of the two founders of the Company was amended, in terms of which each of them is entitled to a performance bonus of 5% of the Company's annual profit before tax. For each year, the bonus shall be capped at $250,000 each.

### B. Chief Financial Officer

Mr. Reichenberg also received 109,000 ESOP options on his appointment in March 2017, vesting over four years, exercisable at $0.20 per option and with an expiration date in March 2027. Mr. Reichenberg was reappointed as a director on 22 June 2020.

### C. Remuneration of key management personal including directors for the year ended 31 December 2019

In terms of Israeli Companies Law, the following needs to be disclosed:

| | | US dollars | | |
|---|---|---|---|---|
| **Name** | **Position** | **Salary and benefits** | **Share based compe-nsation** | **Total** |

| | | | | |
|---|---|---|---|---|
| Graham Woolfman [(1)(3)] | Non-Executive Chairman | 47,905 | - | 47,905 |
| David Levi | Chief Executive Officer [(4)] | 213,994 | - | 213,994 |
| Mark Reichenberg [(1)] | Chief Financial Officer [(4)] | 141,735 | 17,125 | 158,860 |
| Shavit Baruch | VP Research & Development [(4)] | 214,030 | - | 214,030 |
| Neil Rafferty [(1) (3)] | Non Executive Director | 38,324 | - | 38,324 |
| Chen Saft-Feiglin [(2) (3)] | Non Executive Director | 14,981 | - | 14,981 |
| Zohar Yinon [(2) (3)] | Non Executive Director | 14,532 | - | 14,532 |
| | | 685,501 | 17,125 | 702,626 |

**Remuneration of key management personal including directors for the year ended 31 December 2018**

In terms of Israeli Companies Law, the following needs to be disclosed:

| | | US dollars | | |
|---|---|---|---|---|
| Name | Position | Salary and benefits | Share based compe-nsation | Total |
| Graham Woolfman [(1)(3)] | Non-Executive Chairman | 50,030 | - | 50,030 |
| David Levi | Chief Executive Officer [(4)] | 206,340 | - | 206,340 |
| Mark Reichenberg [(1)] | Chief Financial Officer [(4)] | 109,442 | 32,130 | 141,572 |
| Shavit Baruch | VP Research & Development [(4)] | 206,340 | - | 206,340 |
| Neil Rafferty [(1) (3)] | Non Executive Director | 40,024 | - | 40,024 |
| Chen Saft-Feiglin [(2) (3)] | Non Executive Director | 17,517 | - | 17,517 |
| Zohar Yinon [(2) (3)] | Non Executive Director | 19,185 | - | 19,185 |
| | | 648,878 | 32,130 | 681,008 |

(1) Reappointed 22 June 2020.
(2) Appointed 15 November 2017.
(3) Independent director.
(4) Key management personnel as well as director

**D. Directors' equity interests in the Company as at 31 December 2019**

| | Shares | | | Options | | |
|---|---|---|---|---|---|---|
| Name | Direct holdings | Beneficial holdings | Total shares held | Unexercised vested options | Unvested options | Total options |
| Graham Woolfman | - | 10,715 | 10,715 | - | - | - |
| David Levi | 6,767,900 | - | 6,767,900 | 60,710 | - | 60,710 |
| Shavit Baruch | 4,500,000 | - | 4,500,000 | 60,710 | - | 60,710 |
| Mark Reichenberg | - | - | - | 54,500 | 54,500 | 109,000 |
| Neil Rafferty | 7,143 | - | 7,143 | - | - | - |
| Chen Saft-Feiglin | - | - | - | - | - | - |
| Zohar Yinon | - | - | - | - | - | - |
| | 11,275,043 | 10,715 | 11,285,758 | 175,920 | 54,500 | 230,420 |

**Directors' equity interests in the Company as at 31 December 2018**

| Name | Shares | | | Options | | |
|---|---|---|---|---|---|---|
| | Direct holdings | Beneficial holdings | Total shares held | Unexercised vested options | Unvested options | Total options |
| Graham Woolfman | - | 10,715 | 10,715 | - | - | - |
| David Levi | 6,767,900 | - | 6,767,900 | 60,710 | - | 60,710 |
| Shavit Baruch | 4,500,000 | - | 4,500,000 | 60,710 | - | 60,710 |
| Mark Reichenberg | - | - | - | 27,250 | 81,750 | 109,000 |
| Neil Rafferty | 7,143 | - | 7,143 | - | - | - |
| Chen Saft-Feiglin | - | - | - | - | - | - |
| Zohar Yinon | - | - | - | - | - | - |
| | 11,275,043 | 10,715 | 11,285,758 | 148,670 | 81,750 | 230,420 |

**NOTE 29 - Reconciliation of liabilities arising from financing activities**

| | Lease Liabilities | Short Term Borrowings | Total |
|---|---|---|---|
| 1 January 2019 | - | 133,497 | 133,497 |
| IFRS 16 adoption as of 1 January 2019 (see Notes 3.X and 11) (*) | 441,068 | - | 441,068 |
| New leases during the year | 129,742 | - | 129,742 |
| Cashflow | | | |
| - Repayments | (112,379) | (133,497) | (245,876) |
| - Proceeds | - | 1,012,731 | 1,012,731 |
| 31 December 2019 (**) | 458,431 | 1,012,731 | 1,471,162 |

(*) Including current maturities of $102,731
(**) Including current maturities of $151,649

| | Long Term Borrowings | Short Term Borrowings | Total |
|---|---|---|---|
| 1 January 2018 | 7,522 | - | 7,522 |
| Cashflow | | | |
| - Repayments | (7,522) | - | (7,522) |
| - Proceeds | - | 133,497 | 133,497 |
| 31 December 2018 | - | 133,497 | 133,497 |

**NOTE 30 - Subsequent events**

**1. Innovation Authority Grant**

On 17 June 2020, the Company announced that its application for the Innovation Authority grant had been declined and as a result, the Company had taken prompt action to institute further cash conservation measures, which include a reduction in R&D resources that are not tightly coupled to the deliveries around Ethernity's 5G UPF-based ACE-NIC product offering in order to maintain the Company's momentum in this area. It is likely the Company will need to seek access to additional funding in order to trade to its revised plan and to maintain its focus on the current markets

**2. COVID-19**

On March 11, 2020, the World Health Organization recognized the novel strain of coronavirus, COVID-19, as a pandemic. This coronavirus outbreak has severely restricted the level of economic activity around the world. In response to this coronavirus outbreak, the governments of many countries, states, cities, and other geographic regions have taken preventive or protective actions, such as imposing restrictions on travel and business operations and advising or requiring individuals to limit or forego their time outside of their homes.

In light of the continued duration of the COVID-19 pandemic, and the uncertainty on the potential ongoing and future impact, the Board took certain steps to both safeguard the well-being of staff and to position the Company for the future. Where possible a work-from-home policy was implemented and all non-discretionary expenditure was curtailed. The Company also took prudent steps to mitigate any impact through certain short-term cash conservation measures, including a reduction by all directors of up to 50% of their remuneration, with 20% of the reduction deferred.

In addition, the Company recognises that revenues are likely to be delayed due to COVID-19 uncertainty, including where engaged customers' functions are affected through remote working arrangements. The Board continues to closely monitor the situation and will take further action, as appropriate, to manage its working capital position and strengthen the balance sheet to support the execution of the Company's plans.

On 8 April 2020 and further on 6 May 2020, the Company announced that the rapid pace of developments in connection with COVID-19 had caused levels of uncertainty and that, in common with many other companies, it may need to seek alternative sources of funding.