

Dialog Semiconductor
Annual Report 2004

Innovative Silicon for a Mobile World



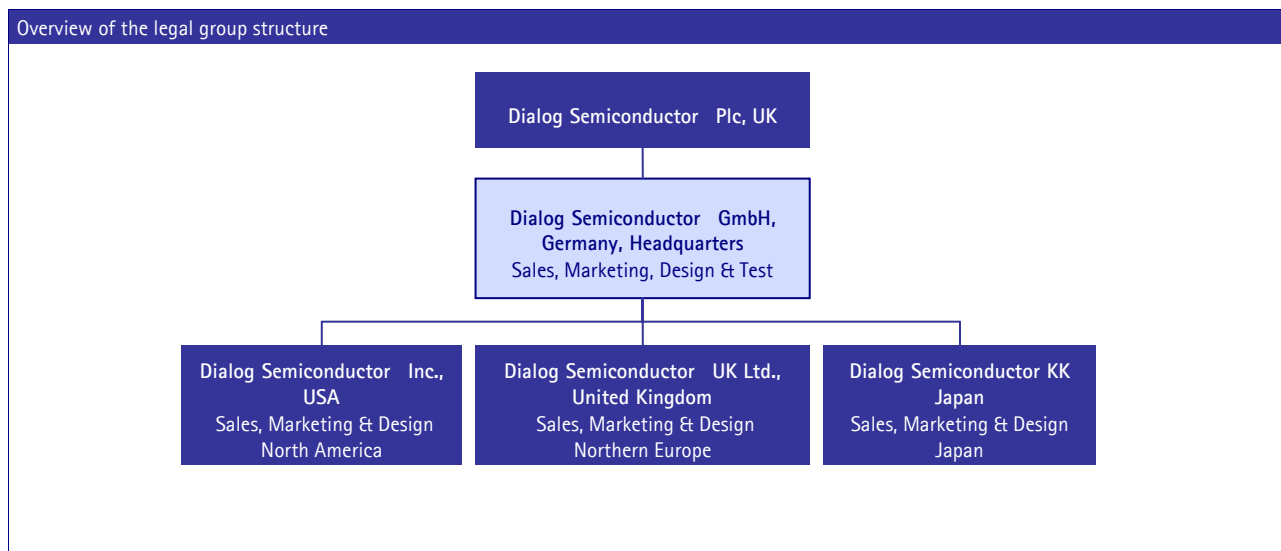
Dialog
Semiconductor

Dialog Semiconductor Plc – Five-Year Financial Summary Selected Financial Data

(in thousands of €, except per share, equity ratio and employee data)	2004	2003	2002	2001	2000
Earnings data					
Revenues	116,044	92,893	77,104	100,519	214,459
Research and development expenses	(29,071)	(30,590)	(34,530)	(31,256)	(22,898)
Operating profit (loss)	(6,088)	(13,224)	(27,406)	(24,136)	38,387
Net income (loss)	(5,743)	(20,420)	(10,208)	(41,386)	26,650
Cash flow from operations 1)	(8,601)	7,588	(7,596)	15,139	18,072
Balance Sheet data					
Cash and cash equivalents	13,977	8,109	31,005	32,626	29,879
Marketable securities	17,542	44,900	-	-	-
Liquid assets	31,519	53,009	31,005	32,626	29,879
Shareholders' equity	121,135	126,843	147,495	158,092	199,287
Equity ratio in %	85.3	90.3	88.8	88.3	80.5
Total assets	141,959	140,471	166,073	179,062	247,572
Capital expenditures	12,321	5,901	3,872	3,157	39,024
Share data					
Basic earnings (loss) per share	(0.13)	(0.46)	(0.23)	(0.94)	0.62
Weighted average number of shares (in thousands) - basic	44,025	43,951	43,888	43,788	42,669
Other data					
Employees (at December 31)	296	273	284	287	268

1) In 2000 excluding advance payments to secure silicon capacity of € 23,201.

Overview of the legal group structure



Unaudited Quarterly Financial Information

2004	Q1	Q2	Q3	Q4	Total
Revenues	23,000	30,402	31,584	31,058	116,044
Gross margin	7,974	10,229	10,373	7,685	36,261
Selling, general and administrative expenses	(2,668)	(2,799)	(2,794)	(3,438)	(11,699)
Research and development	(7,387)	(6,923)	(7,166)	(7,595)	(29,071)
Amortization of intangible assets	(486)	(474)	(289)	(271)	(1,520)
Restructuring and related impairment charges	(59)	-	-	-	(59)
Operating profit (loss)	(2,626)	33	124	(3,619)	(6,088)
Financial income (expense), net	248	161	210	(264)	355
Recovery of investment	54	-	-	-	54
Result before income taxes	(2,324)	194	334	(3,883)	(5,679)
Income taxes	836	(69)	(120)	(711)	(64)
Net income (loss)	(1,488)	125	214	(4,594)	(5,743)
Basic earnings (loss) per share	(0.03)	0.00	0.00	(0.10)	(0.13)

2003	Q1	Q2	Q3	Q4	Total
Revenues	21,015	21,086	23,247	27,545	92,893
Gross margin	6,221	6,472	8,008	9,818	30,519
Selling, general and administrative expenses	(2,335)	(2,344)	(2,347)	(2,215)	(9,241)
Research and development	(8,767)	(7,455)	(7,296)	(7,072)	(30,590)
Amortization of intangible assets	(551)	(553)	(485)	(484)	(2,073)
Restructuring and related impairment charges	(1,465)	(315)	(59)	-	(1,839)
Operating profit (loss)	(6,897)	(4,195)	(2,179)	47	(13,224)
Financial income (expense), net	2	205	71	25	303
Recovery of investment	166	-	149	-	315
Result before income taxes	(6,729)	(3,990)	(1,959)	72	(12,606)
Income taxes	1,864	1,352	457	(11,487)	(7,814)
Net income (loss)	(4,865)	(2,638)	(1,502)	(11,415)	(20,420)
Basic earnings (loss) per share	(0.11)	(0.06)	(0.03)	(0.26)	(0.46)

2002	Q1	Q2	Q3	Q4	Total
Revenues	19,063	17,051	17,903	23,087	77,104
Gross margin	5,516	4,648	4,993	4,538	19,695
Selling, general and administrative expenses	(2,297)	(2,603)	(2,696)	(3,000)	(10,596)
Research and development	(7,996)	(8,617)	(8,574)	(9,343)	(34,530)
Amortization of intangible assets	(447)	(444)	(540)	(544)	(1,975)
Operating profit (loss)	(5,224)	(7,016)	(6,817)	(8,349)	(27,406)
Financial income (expense), net	362	(1,422)	491	(228)	(797)
Recovery of investment	6,457	755	2,675	2,082	11,969
Result before income taxes	1,595	(7,683)	(3,651)	(6,495)	(16,234)
Income taxes	(588)	2,773	1,299	2,542	6,026
Net income (loss)	1,007	(4,910)	(2,352)	(3,953)	(10,208)
Basic earnings (loss) per share	0.02	(0.11)	(0.05)	(0.09)	(0.23)

Meeting the silicon needs of a new digital age

For the first time in the history of electronics, the world is experiencing very fast moving demand for everything digital. There seems to be a rapidly growing global appetite for always-connected lifestyles, with the ability to talk, take photos, listen to music, watch movies, play games and connect to the internet at any time.

Many products and services enabling this lifestyle have only come to reality within the last 12 months or so – such as mobile phones with multiple megapixel resolution cameras and advanced color displays enabling an all-in-one device with additional video download capability; and digital music players capable of playing back hours of downloaded music.

As operators and service providers drive market acceptance of this new digital age,

electronics equipment manufacturers are having to keep up the pace of new product development to meet consumer demand for the latest must-have gadgets. At Dialog Semiconductor, we work closely with industry leaders in wireless, optics and imaging to deliver mixed signal semiconductor solutions that enable these sophisticated electronics products.

With over 20 years experience in research, development and manufacture of power management, audio and imaging technology behind several generations of mobile handsets, our technical knowledge and expertise is also enabling solutions for automotive and industrial electronics markets.

Our chip and system-level solutions address two key market areas:

Wireless



We provide the industry's most highly integrated power management and audio ICs that improve standby times and therefore extend battery life in wireless and other hand-held consumer electronics

products. On top of this, our CMOS technology image sensors, camera modules, and liquid crystal display drivers add sophisticated high-resolution imaging capabilities to these mobile and consumer gadgets.

Automotive / Industrial



Our application specific ICs are providing the leading automotive manufacturers with engine management and comfort electronics systems, based on our expertise in power management and analog and digital

circuit system integration. Extending this technology to high voltages, we also provide industrial lighting control system ICs for fluorescent lamps.

Table of Contents

Shareholder Information	2
Letter to our Shareholders	2
Management	4
The Dialog Semiconductor Share in 2004	5
Corporate Profile	10
Business Overview	10
Our Mission and Strategy	12
Our Solution	13
Our Principal Products	14
Our Principal Customers	16
Our Product Cycle	16
Management Report	19
Executive Summary	19
Operating and Financial Review	20
Results of Operations	21
Trend Information	23
Liquidity and Capital Resources	25
Critical Accounting Policies and Related Uncertainties	27
Risk Factors	29
Outlook	30
Report of Independent Registered Public Accounting Firm	31
Consolidated Financial Statements	33
Consolidated Statements of Operations	34
Consolidated Balance Sheets	35
Consolidated Statements of Cash Flows	36
Consolidated Statements of Changes in Shareholders' Equity	37
Notes to the Consolidated Financial Statements	38
Corporate Governance	52
Report of the Board of Directors	52
Accounting under International Financial Reporting Standards (IFRSs)	52
Corporate Governance Principles	53
Members of the Board of Directors	56

Shareholder Information

Letter to our Shareholders

Dear Shareholders,



I am able to report revenue growth of 25 percent in 2004 compared to 2003. Our 2004 revenue grew to €116 million, and we reduced operating losses for the full year by more than 50 percent. With the increased opportunities created by our new products and implementation of an operational review to manage costs appropriate to our revenue levels, we remain positive for steady growth through 2005.

Key developments during the year

Dialog Semiconductor had significant developments during 2004 on many fronts – new products, partnerships, and further penetration of key markets and customers. We are especially encouraged by the significant progress represented by the inclusion of our audio and power management products in 3G handsets. In 2004 20 million 3G handsets were shipped worldwide. This market is expected to grow to almost 50 million in 2005.

During the first three quarters of 2004, revenue increased 30 percent over the first

nine months of 2003. However, in the fourth quarter, like others in the industry we were affected by the weak US dollar exchange rate against the Euro. Combined with lower than expected uptake from key customers, this impacted our business, slowing down revenue growth for the full year to 25 percent.

Overall, shipments of our ICs for wireless and automotive applications were up in value terms compared to 2003. This is a result of two developments for the Company: one is the addition of new products such as our liquid crystal display (LCD) drivers for wireless handsets, and the second is continued success in winning design slots within the growing number of handsets and other consumer electronic products being designed and manufactured in Asia.

Products & partnerships

We announced new products and partnerships in two key areas during 2004 – in display drivers and imaging, and in integrated power management ICs. Both are extremely important as we enter an age in which multimedia and communications are reaching unprecedented levels of convergence.

In displays and imaging, our entry into color LCD driver ICs, announced in February 2004, has proved to be a success. We introduced the first products in this family, the DA8912A and DA8913A, in June and started shipping in volume to customers during the second half of the year.

We also announced a long-term collaboration with Carl Zeiss, a world leader in the optical and optoelectronics industry, to develop and market modules for high quality camera phones. The combination of Carl

Zeiss' optical expertise and our high quality image sensor capability promises to be exciting as we look to jointly shape the market for next generation camera phones.

In power management, we launched the DA9030 in May, the first integrated power management IC (PMIC) to support the Wireless Intel SpeedStep® technology. The IC, targeted at entry-level, mid-range and premium smartphones, personal digital assistants (PDAs) and communicators with highly sophisticated multimedia and internet capabilities, provides significant power consumption and system cost savings compared to equivalent discrete solutions.

Outlook

During 2004, we established a very good platform from which to exploit many more opportunities in both the wireless handset market and the automotive electronic industry. The ability to build on our strengths in mixed signal IC design, applications knowledge and experience in the wireless market have resulted in Dialog Semiconductor being able to develop and deliver a range of products and solutions to meet our customers' needs.

The Company is therefore continuing to evolve as we establish ourselves as a supplier of both application specific standard products (ASSPs) and solutions for wireless and automotive electronic markets, as well as application specific integrated circuits (ASICs).

We expect to build further market share in imaging through partnerships with other blue-chip names in opto-mechanical and imaging. In addition, we are working with the leading mobile phone manufacturers to position ourselves as a key supplier of mixed signal devices in a number of different design sockets within the handset – not just power management or audio. Our product portfolio includes embedded cameras and display drivers.

With these multiple component design-in prospects, we are positive about the Company's growth potential in 2005. This would not be possible without the continued commitment of all our stakeholders, so I would like to once again thank all our employees, customers, partners and all others who have helped Dialog Semiconductor maintain a growth path in 2004.

Kirchheim/Nabern, February 2005



Roland Pudelko

CEO & President

Management

Roland Pudelko

Chief Executive Officer and President (52)

With Dialog Semiconductor since 1989 and served as Executive Director, CEO and President from 1998. He has over 20 years experience in management, design and engineering in electronics, including with the Daimler-Benz Group, and TEMIC.

Gary Duncan

Vice-President, Engineering – Imaging (49)

With the company since 1987 and is responsible for the design and development of imaging products. Prior experience includes various senior engineering and management positions at Plessey and ES2.

Peter Hall

Vice-President, Quality and Technical Support (53)

Joined in 1987 and is responsible for technical support, IT and quality. Previous management and engineering positions were at STC Semiconductors and MEM in Switzerland.

Erwin Hopf

Vice-President, Operations (50)

Joined in 2002, after over 20 years experience in various process engineering as well as research and development and production management positions at Siemens Components and Infineon Technologies.

Yoshihiko Kido

Vice-President, Japan (52)

Joined in 2001, after various management positions at General Electric, Act Japan and Seagate. He was also a founding employee of Nippon Ericsson, as procurement director for mobile phones and base station components.

Martin Klöble

Vice-President, Finance and Controlling (45)

With the company since 1999 and previously a partner with KPMG. An MBA graduate and qualified tax consultant and certified public accountant in Germany (Wirtschaftsprüfer) and in the United States (CPA).

Martin Sallenhag

Director of Product Marketing (36)

Joined Dialog Semiconductor in 2001, after roles in management and engineering at Ericsson Mobile Communications and Axis Communications. He is responsible for the technical marketing of Dialog's product groups.

Richard Schmitz

Vice-President, Engineering – Mixed Signal ICs (48)

Joined in 1989 and is responsible for mixed signal semiconductors for power management & audio, RF, and automotive & industrial products. Previously at Hewlett Packard's instruments division and the Institute for Microelectronics, Stuttgart.

The Dialog Semiconductor Share in 2004

The International Stock Markets in 2004

Following three years ending in losses from 2000 to 2002, and the bull market of 2003, the momentum of the international stock markets slowed a little in 2004. While the most important leading stock exchanges in Europe, the US and Japan were up at the end of the trading year, growth was significantly slower than in the previous year. In addition to factors such as the development of the dollar-euro exchange rate and the interest rate increase implemented by the Federal Reserve Bank in the summer, the high price of oil was a key negative impact on the continuation of the bull market.

The Dow Jones Index of the most important US industrials rose by 3.6 percent over the trading year as a whole. The Nasdaq Com-

posite ended 2004 up by 8.7 percent. However, both figures disguise the fact that the price level in the US fell considerably at times in late summer. It was not until the last quarter of 2004 that price developments were again increasingly positive, being driven primarily by sustained increases in corporate profits and sound economic data.

The DAX also shared this development. Following a relatively highly volatile performance in the first half-year, prices rallied strongly from August, allowing the DAX to rise by 7.3 percent at year-end. At the very end of the year, the DAX reached its annual high of 4256 points. In contrast, the TecDAX turned in a negative performance, falling 3.9 percent over the year.

Leading German indices mixed

The Dialog Semiconductor Share Performance

The very strong performance of the 2003 trading year continued at the beginning of 2004. Dialog Semiconductor's share began 2004 with a Xetra closing price of €3.55. Buoyed by, among other things, its inclusion in the TecDAX effective from March 22, 2004, Dialog Semiconductor's share developed positively in the opening weeks of the year, reaching its annual high of €4.49 (NASDAQ \$5.66) on February 18. While maintaining stable trading volumes, the share remained at around this level until the end of the first quarter.

At the start of the second quarter, the performance of Dialog Semiconductor's share was initially weaker, though this was in line with the performance of the TecDAX as a whole, which was also down. The share started the second quarter at €4.01 with a quarterly high of €4.09 (NASDAQ \$5.00) and a quarterly low of €2.69 (NASDAQ \$3.06). As at June 30 – following a temporary recovery from around mid-May to mid-June – the Xetra closing price was €3.08.

Largely parallel to the somewhat weaker performance of the TecDAX and international stock markets as a whole, the price of Dialog Semiconductor's share tracked largely sideways in the third quarter and subsequently also in the fourth quarter, while displaying relatively low volatility and below-average trading volumes. The quarterly high for the third quarter was €3.09 (NASDAQ \$3.75) and €2.94 for the fourth quarter (NASDAQ \$3.57).

The share's development in the final quarter of 2004 was largely defined by the announcement of a negative business outlook for the fourth quarter on December 15. With the weakness of the dollar and revenue falling short of forecasts in the Mobile Communications sector, Dialog Semiconductor was forced to adjust its revenue and earnings targets for the fourth quarter and fiscal 2004 downwards. Following this announcement, the share price dropped significantly by 28 percent to its annual low of €1.63 (NASDAQ \$2.29).

Finally, as a result of this drastic price slide in the final days of trading in 2004, Dialog Semiconductor's share fell 49.7 percent in total as against its closing price on December 31, 2003.

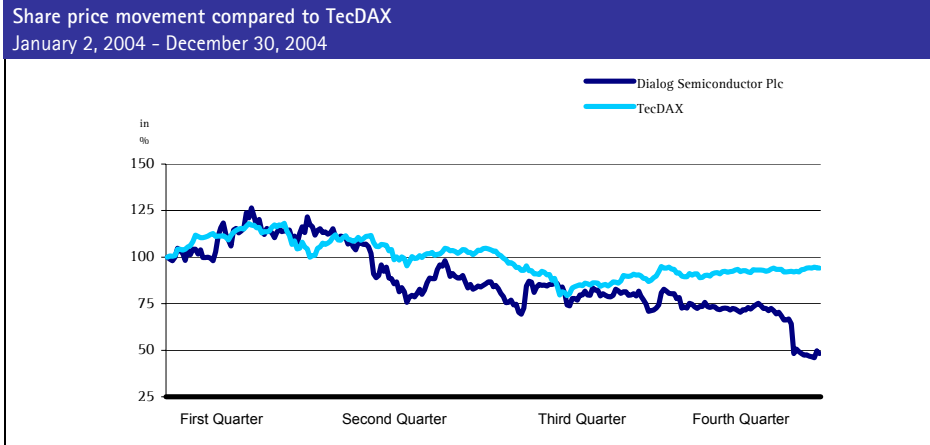
Looking back over the year, one highlight was the inclusion of Dialog Semiconductor in the TecDAX. Thus, since March 22, 2004, Dialog Semiconductor's share has been listed in the blue chip index for the 30 largest technology stocks in the Prime Standard. The share's listing in this index came as a result of the improved performance of Dialog Semiconductor's share in 2003 and market and investor confidence in the progressive change in the company's business orientation and its impact on the trend towards profitability. As at December 31, 2004, in the TecDAX league table, Dialog Semiconductor was placed at 21 for the criterion of trading volume and at 40 for market capitalization. In the preceding

months, the share was rated significantly below 35, the threshold used in semi-annual reviews. Against this backdrop, the possibility that Deutsche Börse will remove the share from the TecDAX in its forthcoming review cannot be ruled out. However, it has been made clear in the past that consistency is often weighted more heavily as a review factor than short-term shortfalls. Taken over the year as a whole, Dialog Semiconductor has good results in this context, which would support its remaining in the TecDAX.

Capital Increase

On September 24, 2004, the company issued 2,000,000 new ordinary shares from authorized capital at a price of £0.10 per share for the employee stock option plan, so as to have shares to serve option rights granted to employees.

Inclusion in the TecDAX



Market prices

The following table shows, for the periods indicated, the highest and lowest closing market prices for our shares on the TecDAX (Xetra) and the NASDAQ:

		2004		2003	
		High	Low	High	Low
Frankfurt (DLG)	First Quarter	€ 4.49	€ 3.48	€ 1.31	€ 0.82
	Second Quarter	€ 4.09	€ 2.69	€ 1.64	€ 0.85
	Third Quarter	€ 3.09	€ 2.46	€ 3.28	€ 1.56
	Fourth Quarter	€ 2.94	€ 1.63	€ 4.39	€ 2.90
NASDAQ (DLGS)	First Quarter	\$ 5.66	\$ 4.40	\$ 1.68	\$ 0.95
	Second Quarter	\$ 5.00	\$ 3.06	\$ 1.93	\$ 0.95
	Third Quarter	\$ 3.75	\$ 3.01	\$ 3.80	\$ 1.80
	Fourth Quarter	\$ 3.57	\$ 2.29	\$ 5.52	\$ 3.45
Average trading volume per day		237,200		253,640	

Investor Relations:

Successful Continuation of Dialog with the Financial Community

Creating and maintaining transparency for capital market participants – this principle that all TecDAX companies are required to follow was again the maxim of Dialog Semiconductor's financial communication in fiscal 2004.

On roadshows in London, Frankfurt, Cologne and Vienna and at numerous technology conferences, the Dialog Semiconductor management team addressed and answered questions put by investors, analysts and journalists. As is traditional when publishing annual results, we held a DVFA analysts' conference, as well as telephone conferences on the publication of our quarterly results. Furthermore, some 30 individual meetings were held with investors,

analysts and the press worldwide in fiscal 2004.

We continued to intensively maintain and extend our investor relations offering on our home page www.dialog-semiconductor.com. In addition to the comprehensive offering of share price overviews, financial reports and other information, of particular note here are, for example, disclosures on all Dialog Semiconductor Plc directors' dealings in line with Section 15a of the *Wertpapierhandelsgesetz* (WpHG – German Securities Trading Act) under the German Corporate Governance Code and all disclosures published as ad hoc publicity.

Intensive exchange of information with investors, analysts and the press

Investor Relations Activities in 2004

Date	Location	Event
February 18	Frankfurt	Press and Analyst Conference of 2003 result
March 15 - 16	London	Roadshow Kepler Equities
March 25 - 26	Frankfurt/Cologne	Roadshow Kepler Equities
April 27	Frankfurt	DZ Bank Conference
April 28	Conference Call	Release of first quarter results
May 12	London	Annual shareholders' meeting
July 21	Conference Call	Release of second quarter results
July 27	Frankfurt	Roadshow Berenberg Bank
September 16	Vienna	Roadshow Dresdner Kleinwort Wasserstein
September 21	Frankfurt	Roadshow WestLB
October 20	Conference Call	Release of third quarter results
November 2	London	Roadshow WestLB

Reporting by Financial Analysts

In the past fiscal year, we continued to maintain the intensive and ongoing exchange of opinions and information with financial analysts.

The following table shows a selection of institutes and analysts that published reports on Dialog Semiconductor or covered our company as part of a peer group analysis for the semiconductor industry in 2004.

Institution	Analyst
Areté Research	Brett Simpson
Berenberg Bank	Dr. Oliver Wojahn
BW Bank	Helmut Bartsch
DZ Bank	Harald Schnitzer
ING BHF-Bank	Manuel Deimel
Kepler Equities	Ingo Queiser
LBBW	Stephan Wittwer
MM Warburg	Michael Bahlmann
SES Research	Oliver Drebing
WestLB Panmure	Dr. Karsten Iltgen

Share Data (share prices refer to Xetra, Frankfurt Stock Exchange)

Stock Exchanges and Symbols	Frankfurt Stock Exchange (Prime Standard) : DLG NASDAQ, USA : DLGS
Security Identification Number (SIN)	927 200
Number of shares as of Dec. 31, 2004	46,068,930
Share price as of Dec. 31, 2004 (in €)	1.71
2004 High (in €)	4.49
2004 Low (in €)	1.63
Performance since offering	(82%)
Trading volume per day (average 2004)	237,200
Market capitalization (in millions of €)	79
Basic loss per share 2004 (in €)	(0.13)

Principal Shareholders

Information regarding entities known by the company to be beneficial owners of more than 3 percent of outstanding shares in the company is shown in the table below:

Name	Number	Percent
Apax Partners	8,460,793	18.4
Adtran, Inc.	2,520,960	5.5
Ericsson Radio Systems AB	2,101,554	4.5
Free float ⁽¹⁾	32,985,623	71.6
Total	46,068,930	100.0

(1) Of which 4,688,171 shares (10.2%) are held by the Capital Group Companies Inc as notified on January 13, 2005 on behalf of discretionary clients. 2,001,559 shares (4.3%) are held by the Dialog Semiconductor Plc Benefit Trust.

Disclosure of Interests

The provisions of the UK Companies Act of 1985 require that any person acquiring a direct or indirect interest of 3 percent or more of a class of shares issued by the company (including shares held in the form of ADSs) with voting rights at the company's general meetings

must inform the company of its interest within two working days. If the 3 percent interest is exceeded, the shareholder must inform the company of any increase or decrease of one percentage point in its interest.

Corporate Profile

Business Overview

Innovative IC solutions for wireless, automotive and industrial electronics

Dialog Semiconductor develops and supplies a range of innovative integrated circuit (IC) product solutions for wireless, automotive and industrial electronics systems. Our background and strengths are in specific design skills such as mixed signal circuits, image sensing and processing. Our business model is a 'fabless' one whereby we design ICs, outsource production of silicon wafers, and then deliver final chips to our customers.

Dialog's customers are designers and manufacturers of mobile handsets and portable electronics products, as well as automotive suppliers. Our chip solutions for their products range from comprehensive and highly integrated power management and audio functions, to image sensors, image processing and multimedia display drivers.

History and Development of the Company

Our roots are firmly established in the design of complex analog and digital circuits. Dialog Semiconductor originated from the European activities of a US semiconductor company, International Micro-electronic Products, Inc. ("IMP"), founded in 1981 in Silicon Valley, specializing in mixed signal CMOS semiconductor tech-

nology. After being acquired by Daimler-Benz AG and becoming a part of its subsidiary Temic Telefunken Microelectronic, Dialog Semiconductor Plc was created as a result of a subsequent management buy-out financed by Apax Partners, Adtran and Ericsson. Then in 1999 we made an initial public offering on the Frankfurt Stock Exchange and in 2000 listed on NASDAQ.

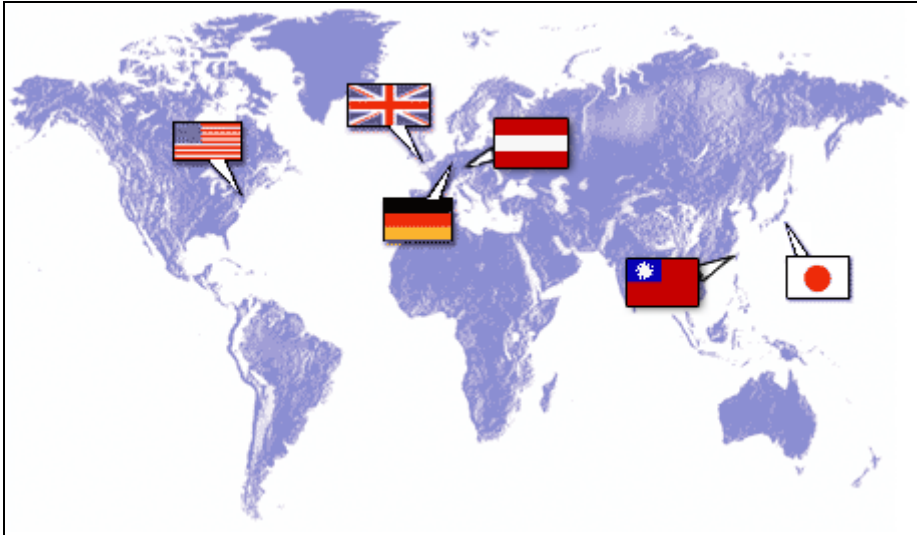
In 2002 we acquired the CMOS imaging business and associated Active Pixel Sensor (APS) patent portfolio from Sarnoff Corporation.

Throughout our history we have delivered several technology firsts. For example, in 1996 we introduced the first system level CMOS power management device, and four years later the first combined power management and audio device for 3G. In imaging, we developed the first digital camera accessory module in 2001 for a leading mobile phone manufacturer, and in 2002 we launched a full VGA resolution camera module as a standard product for high quality photo imaging and video in mobile phones and personal digital assistants (PDAs).

Global Presence

Our corporate headquarters office is located near Stuttgart, Germany. To support our growing customer base in greater China we recently, in the first quarter of 2005,

opened a new office based in Taipei, Taiwan. We have additional offices in Germany as well as Austria, Japan, United Kingdom and the USA.



New office opened in Taipei

Our Expertise

Dialog Semiconductor's competitive advantage comes from a strong track record in designing, manufacturing, testing and delivering mixed signal circuits produced entirely in complimentary metal oxide semiconductor ("CMOS") technology. Our core technology expertise is applied across different target markets, enabling maximum return on investment from our research and development while delivering the latest technology products for each of these chosen markets.

For example, the technology that helps us optimize power usage, processes audio

signals, and convert analog or digital data for wireless handsets also provides us with the ability to deliver competitive solutions in automotive, industrial and imaging applications.

Our Employees

In the year ended December 31, 2004 our global workforce grew to 296 employees in eight locations worldwide, the majority of whom are employed in R&D functions. This represents an 8% headcount increase compared with 273 employees at the end of the preceding year.



Our Mission and Strategy

Dialog Semiconductor's mission is:

“To be the leading global supplier of lowest power, highest quality, mixed signal components and system level solutions to the wireless and automotive markets”

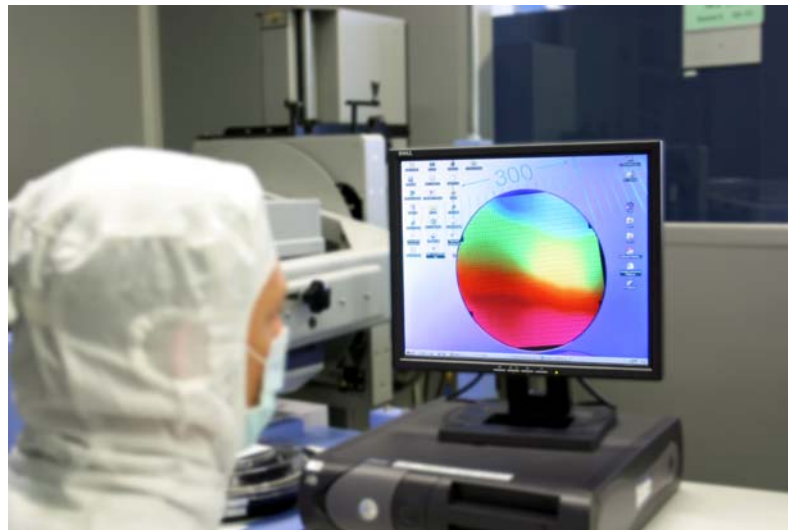
Achieving this mission requires a clearly focused strategy that we have developed based on:

- Expanding relationships with key industry leaders
- Building on a common technology platform
- Marketing standard product solutions
- Proactively refining customers' system architecture
- Expanding engineering expertise
- Selectively expanding global capabilities

- Remaining focused on our existing business model
- Delivering the highest quality products

The success of this strategy is demonstrated by the strong and growing relationships developed with some of our high profile, high volume customers. They see Dialog Semiconductor as a flexible partner and integral part of their overall supply chain.

We work with our customers to rapidly develop appropriate responses, both technically and commercially, to changing market trends and requirements. Through our relationships with partners and manufacturers, we then ensure rapid delivery of quality-approved products to the customer.



Our Solution

Dialog Semiconductor's products address the needs of original equipment manufacturers (OEMs) requiring either standard products or customer-specific silicon. We design, develop and deliver mixed signal components and system level solutions based on our technology expertise in key areas such as power management, audio-CODECS, imaging and system-on-a-chip integration.

Our solutions address two major market requirements in:

- Wireless communication electronics
- Automotive and industrial electronics

In wireless applications, key factors driving the pace of development of our product solutions are the rapid evolution of smaller and more sophisticated devices packed with advanced capabilities such as wireless communications, digital camera, video and audio.

This places huge demands on the power management and requires excellent imaging and displays. Dialog Semiconductor's strength in developing highly integrated power management and audio chips enable optimum use of the battery to prolong usage time, and provide high performance audio playback at the same time. In addition, our excellent image sensors, image processing and display drivers enhance the user experience with the camera and graphical user interface.

In automotive and industrial, our products address the safety, management and control of electronics systems in the car; and highly integrated smart power electronics management systems such as electronic ballasts for lighting.

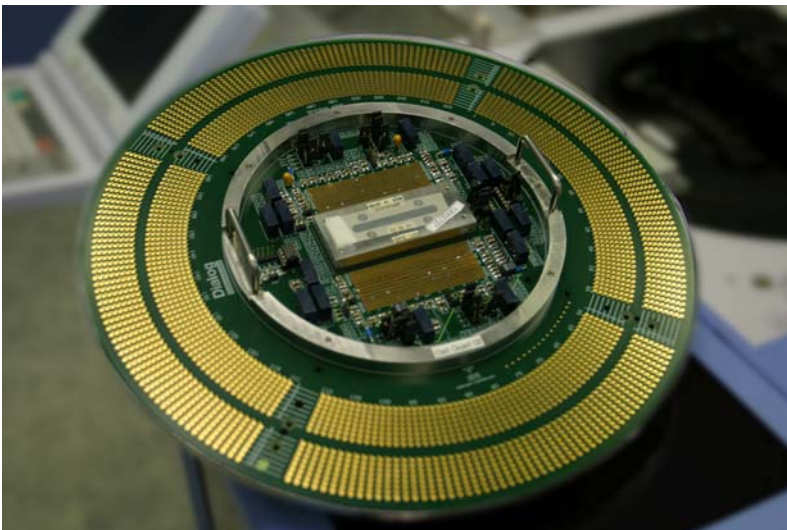
With all our products, our customers acknowledge our leadership in creating innovative silicon solutions in 100% CMOS technology - fully tested and delivered quickly to achieve competitive time-to-market objectives.

We address two major markets:

Wireless



Automotive / Industrial



Our Principal Products

Dialog Semiconductor's products utilize common technology platforms to deliver unique, highly integrated and high performance capabilities for selected target applications.

Our main product categories are:

- Power management and audio ICs
- Camera modules
- Liquid crystal display drivers
- Application specific ICs

Power Management and audio ICs

The drive towards smaller and more sophisticated portable consumer electronics products puts the challenge to designers and manufacturers to achieve maximum battery life. Effective power management is therefore an increasingly vital part of the system – an area in which Dialog Semiconductor has considerable experience as a result of designing chips for hundreds of millions of cellular handsets. We continue to develop new power management products such as the DA9030 and DA9011 introduced during 2004.

Combined with our expertise in integrating both low voltage and high voltage circuits for car electronics and lighting control systems, we also deliver custom and intelligent power management solutions for automotive and industrial electronics systems.

Our chips for cellphones take advantage of the benefits of integrating high performance audio CODEC functions with power management circuits. The two are complementary functions that can be designed onto a single chip, enabling one chip to both improve battery life and provide digital audio playback or hi-fi quality voice.

This results in unique power management and audio chips which are highly integrated and can contain over 30 different functions, all in a single chip. Typical functions include:

- Smart mirror™ LDO (low dropout voltage) regulators – minimizing current consumption and simplifying circuit design
- High efficiency buck and boost converters – designed for efficiencies over 90% with currents up to 500mA
- Programmable multiple chemistry battery chargers – handling all common battery technologies, NiMH, LiIon and polymer
- Audio CODECs with up to 24-bit capability for digital audio player algorithms and based on Dialog's own digital signal processing (DSP) designs optimized for minimum power consumption and silicon area

Camera modules

Since developing the first digital camera accessory module for a leading mobile handset manufacturer in 2001, and acquiring the CMOS imaging business and associated patent portfolio from Sarnoff Corporation in 2002, Dialog Semiconductor has developed a range of standalone CMOS image sensors and complete modules consisting of sensor, image DSP, lens, housing and connector.

In 2004 we announced our collaboration with Carl Zeiss Corporation to initiate a program of camera module development utilizing the best of our image sensor and processing technology, and combining it with a high quality lens in an extremely small package using optics from Carl Zeiss. The relationship between our companies is a powerful one that we expect to shape a growing market for high quality camera phones.

Our high-resolution, high performance sensors and modules are ideal for embedding into wireless handsets and hand-held electronics. In addition the high sensitivity of the pixels and processing capability down to each pixel makes our image sensor technology the ideal choice for automotive systems, where near real-time response is required.

New power management IC:
DA9030



Key features of our CMOS image sensors include:

- Superior video in outdoor uncontrolled lighting
- High confidence image capture
- Fast response
- Very low power and low voltage requirements
- High resolution still and streaming video modes

Liquid Crystal Display Drivers

In 2004 we announced availability of a brand new range of color liquid crystal display (LCD) drivers providing real innovation for the mobile phone display market. Delivered as standard parts ready for production, the DA89xx family delivers superior color performance and low power consumption, while providing mobile phone handset makers the flexibility to customize display parameters for creating differentiation.

Our family of color display drivers is specially developed for the growing number of wireless handsets with high-resolution color displays and also with dual displays. The color STN (super-twisted nematic) liquid crystal display (LCD) drivers provide excellent resolution of up to 65,000 colors, and address a demand for higher performance full color, high speed moving images using MLA (multi-line addressing) LCD technology. This ensures faster response time compared to conventional passive matrix displays, and high-speed moving images are supported while maintaining very low power consumption.

Products include the new DA8912A and DA8913A, which incorporate fully integrated graphic display memory with high speed interfaces and various power management functions to enable a single, low power chip for managing the display in next generation mobile phone handsets and portable electronic products. The devices offer fast display graphic transfer rates, supporting moving images.

Application Specific ICs (ASICs)

Although we are increasingly seeing standard product solutions addressing a vast majority of customer requirements in our target markets, there is still a demand from some customers for custom solutions. These ASIC solutions are based on our in-house expertise in mixed signal design, and in integrating complex analog high voltage (up to 40V) and other low voltage circuits, all produced in mainstream CMOS technology.

Our expertise is based on many years of experience, proven in-house technology, and the latest CAD tools to rapidly develop leading-edge application specific ICs. This experience is gained from delivering custom solutions for cellular phone handsets, in automotive electronics systems, and in industrial systems.

In cellular phones for example, we have developed over 50 different power management designs for the world's leading cellphone manufacturers. Our ASICs are becoming ever more integrated with many power management functions on the chip – such as high performance LDOs (low drop out voltage regulators), high efficiency AC-DC converters, complete battery charging circuits, programmable LED drivers and USB interfaces. For sophisticated audio capability, we have also successfully integrated audio functions on to the same chip – exploiting the complementary nature of power and audio sub-systems.

In automotive electronics, our ASICs control safety, engine management, and comfort electronics for the top automobile manufacturers. This exploits Dialog's competence in power management systems and mixed signal design, together with knowledge of integrating high performance analog circuits and high-density digital logic and high voltage circuits on a single chip in a standard CMOS process. Our partnership with leading automotive equipment suppliers has also resulted in developing chips able to connect directly to high voltage circuits of up to 40V.

In industrial systems, our single chip solutions integrate high voltage low power

Color LCD driver: DA8912A



circuits for electronic ballasts used to control fluorescent lamps. Our customers are using ASICs that integrate, for example, the functionality of power factor correction circuits, lamp management circuits, and half bridge driver. Our expertise in the integration of these circuits forms the basis of highly integrated control chips for smart power electronic systems in other applications such as computer and mobile communications systems. Dialog's solution is ideal for instances where the chip must be highly integrated yet have the ability to

control high voltages intelligently using digital circuits on the same chip.

Our ASIC solutions are manufactured by leading foundry partners, with which we work in true partnership to ensure our customers can access both the latest CMOS processes, as well as foundry capacity. This enables our customers to meet both costs and time-to-market objectives for their products. We also have our own process engineers in-house to ensure our customers benefit from extracting the optimum capability from a process.

Our Principal Customers

Our principal customers are recognized wireless communications, consumer electronics, and automotive equipment manufacturers. These customers are for both our standard products introduced over the last two years, as well as application specific (ASIC) products.

expertise, while the close working relationship provides us with an opportunity to continually develop and fine-tune market leading technological expertise with recognized industry leaders.

The rapidly evolving technology in all our target market sectors means that a partnership approach with our customers is essential – whether it is for standard products or for custom solutions. Hence our customers look to Dialog as an outside source of

Long-term relationships with our customers include those with Ericsson, Motorola and Siemens for wireless communications; Adtran for wireline communications applications; Bosch and Conti Temic for automotive applications; and Tridonic for industrial applications.

Our Product Cycle

As a fabless semiconductor manufacturer, our focus is on developing the products and technology, and then delivering quality-approved products to our customers. Hence we design, develop and supply mixed signal ASICs and ASSPs, outsource the actual manufacture of wafers and assembly to selected foundries and assemblers, and then test the products in-house, before final delivery to customers. The product cycle is as follows:

- Design and development
- Manufacture of wafers
- Assembly and testing
- Quality and environment control

Design and development

Our customers gain significant advantage from our ability to rapidly develop mixed signal ASIC and ASSP designs, fostered through many years of design experience and a highly skilled engineering staff of over 150 professionals. Evolving designs are constantly monitored through our design library database, and we achieve rapid design cycles through our strategy of modifying and reusing previously designed building blocks.

We use industry standard design tools from suppliers such as Cadence Design Systems, Inc. to increase design automation and top-level simulation to identify system design incompatibilities at an early stage.

Our focus is on furthering our technology expertise in power management, audio-CODECs, image sensors and systems, and display driver technology. We also ensure that our process teams are up to date with the latest commercially available CMOS manufacturing technologies.

Our total spend on research and development in 2004 was €29 million. This resource was focused on enhancing our software development, state-of-the-art digital system design, leading edge analog design, as well as test systems.

Manufacture of wafers

We outsource our wafer production to selected foundries with a demonstrated ability to provide high quality products on tight deadlines. Foundries we use include Chartered Semiconductor Manufacturing Pte., Ltd. in Singapore and Taiwan Semiconductors Manufacturing Co., Ltd. ("TSMC").

Our choice of technology is CMOS rather than bipolar, primarily because CMOS devices consume less power and permit more transistors to be integrated on a single chip, essential for the target markets we address.

We always aim to ensure that all steps in the manufacturing process can be provided by at least two suppliers, in order to prevent shortage or loss of chip production due to market conditions or disasters such as foundry fires.

Since the successful manufacture of silicon wafers is critical to our reputation and profitability, we work carefully to identify suitable foundries in order to maintain continuity and security of supply for our customers. We also place, where possible, our own process engineers directly at the fab premises to resolve any potential engineering issues and to ensure both the quality and timely delivery of the finished product.

Assembly and testing

We outsource final assembly of the chips from the wafers to various sub-contractors in the Far East and Europe. Completely

assembled chips are then returned to Dialog Semiconductor for final testing before delivery to the customer. All our chips are tested in-house, and no product is delivered to a customer unless it has been tested and approved.

Our rigorous testing approach allows us to ensure overall quality control of our manufactured products. The test programs developed by our test engineers are based upon specifications determined by individual customers as well as our own standard product specifications, and are developed in parallel with the design. Our test equipment is regularly calibrated to ensure the accuracy of test parameters.

Quality and environment control

Dialog Semiconductor's policy is to supply products and services in full compliance with relevant specifications to ensure customer requirements are met. Hence our quality management system has been established and is maintained to provide customers with the assurance that our products and services fulfil both their contractual requirements as well as future needs. Our main target is to achieve 'Zero Fails'.

An uncompromising approach to quality assurance in every area of our operations, through active participation from every employee within the company, produces a highly structured quality environment that has resulted in Dialog Semiconductor being approved by all our major blue-chip customers.

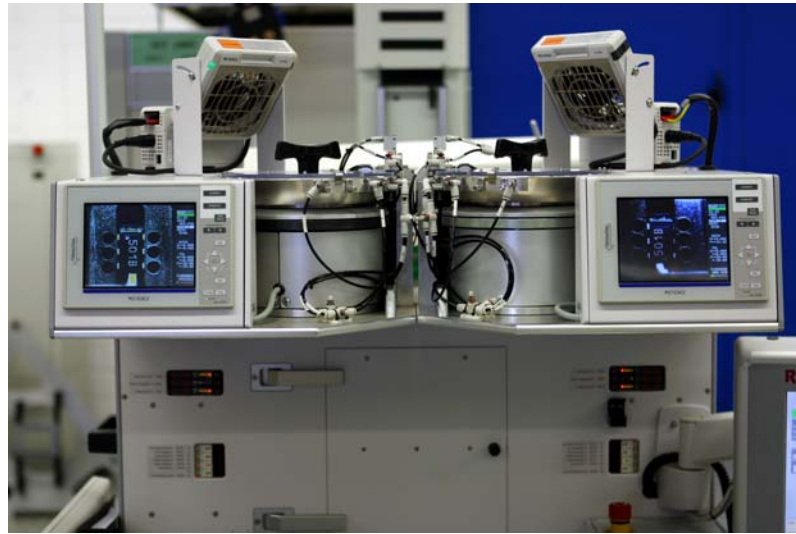
In addition to ensuring the highest levels of product quality and operational efficiency, we also believe in a commitment to environmentally friendly products. Responsibility for nature and the environment have been an important part of our company philosophy and activities since 1999. Our aim is to minimize adverse environmental impacts by advancing environmentally compatible product design and environmentally friendly activities.

As part of this commitment, we maintain a certified environmental management system in accordance with international stan-

dards (ISO14001). Awareness and knowledge of environmental issues is promoted throughout the organization so that it becomes a natural part of the decision making process.

As a fabless semiconductor company, Dialog Semiconductor's business model is based on strategic outsourcing. In order to achieve the highest quality we must de-

mand world-class quality standards from both our fabrication and assembly partners as well as our own internal processes to increase our customers' confidence in our products. Dialog Semiconductor is accredited to QS9000/ISO9001:2000/ISO14001 and as an extension of this practice it is our policy to build partnerships with suppliers that are also qualified to the same international quality standards.



Management Report

The following discussion of our financial condition and results of operations should be read in conjunction with the

audited financial statements included in this annual report, which have been prepared in accordance with US GAAP.

Executive Summary

We are a global supplier of power management, audio and imaging technology, delivering innovative mixed signal standard products as well as application specific integrated circuits for wireless, automotive and industrial applications. To date, we have shipped over 500 million integrated circuits for cellular phones. We operate in intense competitive markets and our customers select us based upon numerous factors including price, design cycle time, reliability and performance. Our customers purchase our products through periodic orders made throughout the year. The prices paid for each type of product or design are generally agreed with customers on an annual basis for specified volumes of each design ordered by the customer during the year. Potential price reductions in subsequent years are typically offset by lower production costs as a result of improved yields, lower wafer costs or smaller chip sizes.

Critical success factors for us include the continued growth in the worldwide market for cellular handsets, the completion of our new designs on a timely basis, customers acceptance and implementation of our designs in large-scale production, and continued demand from our key customers for the development of new products. Partnerships with companies at all levels of business are important for our success in a market dominated by major international semiconductor companies. We rely on our fabless business model that enables us to focus our research and development activities, which are essential for us to respond to our customers' cutting edge silicon solutions requirements and also maintain our competitiveness in our market. Consequently, it is critical for us to make significant and ongoing cash expenditures to

fund our research and development activities. We have also made significant investments in long-lived assets, primarily for our in-house test equipment.

We have a significant amount of liquid assets on hand, primarily from the remaining sales proceeds from the issuance of our ordinary shares in 1999 and 2000, cash generated from operations in previous years and recoveries of certain of our investments and deposits. Substantially all of our near term future cash inflows are expected to come from the sale of our products. We generally collect cash from our customers within 58 days after product delivery. However, we derive a substantial portion of our revenues from a relatively small number of wireless communications manufacturers. Sales to two customers individually accounted for 65% of total revenues in 2004. Therefore, the main action we are taking to minimize the risk of this dependency is developing new products for new customers; such new products include a range of color liquid crystal display drivers, image sensors and camera modules. Material opportunities we envision include growth in our main market, cellular handsets, based on the expected transition to 3G, and a further worldwide growth in semiconductor sales, especially in Asia. However, our revenues, profitability and growth could decline if the growth in these markets slows.

We believe that our key performance indicators are revenues, gross margin and research and development costs, thereby being the main driver of our operating profit or loss. Accordingly, our Board of Directors and management use operating profit as a measure of performance.

More than 500 million ICs shipped

New products reduce dependency on few customers

Operating profit is a key performance indicator

Operating and Financial Review

Forward-looking statements.

This annual report contains “forward-looking statements”. All statements regarding our future financial condition, results of operations and businesses, strategy, plans and objectives are forward-looking. Statements containing the words “believes”, “intends”, “expects” and words of similar meaning are also forward-looking. Such statements involve unknown risks, uncertainties and other factors that may cause our results, performance or achievements or conditions in the markets in which we operate to differ from those expressed or implied in such statements. These factors include, among others, product demand, the effect of economic conditions and conditions in the semiconductor and telecommunications markets, exchange rate and interest rate movements, capital and credit market developments, the timing of customer orders and manufacturing lead

times, the changes in customer order and payment patterns, the financial condition and strategic plans of our major customers, insufficient, excess or obsolete inventory, and the impact of competing products and their pricing, product development, commercialization and technological difficulties, political risks in the countries in which we operate or sale and supply constraints. It is not possible to predict or identify all such factors. Consequently, any such list should not be considered to be a complete statement of all potential risks or uncertainties. We do not assume the obligations to update forward-looking statements.

The following table sets forth historical consolidated statements of operations of Dialog for the fiscal years ended December 31, 2004, 2003 and 2002 in thousands of Euros and as a percentage of revenues:

(in thousands of €)	2004	% of revenues	2003	% of revenues	2002	% of revenues
Revenues	116,044	100.0	92,893	100.0	77,104	100.0
Cost of sales	(79,783)	(68.8)	(62,374)	(67.2)	(57,409)	(74.4)
Gross margin	36,261	31.2	30,519	32.8	19,695	25.6
Selling and marketing expenses	(6,237)	(5.3)	(4,197)	(4.5)	(4,149)	(5.4)
General and administrative expenses	(5,462)	(4.7)	(5,044)	(5.4)	(6,447)	(8.4)
Research and development expenses	(29,071)	(25.0)	(30,590)	(32.9)	(34,530)	(44.8)
Amortization of intangible assets	(1,520)	(1.3)	(2,073)	(2.2)	(1,975)	(2.5)
Restructuring and related impairment charges	(59)	(0.1)	(1,839)	(2.0)	-	-
Operating loss	(6,088)	(5.2)	(13,224)	(14.2)	(27,406)	(35.5)
Interest income, net	1,081	0.9	757	0.8	1,121	1.5
Foreign currency exchange gains and losses, net	(726)	(0.6)	(454)	(0.5)	(1,918)	(2.5)
Recovery of investment	54	-	315	0.3	11,969	15.5
Result before income taxes	(5,679)	(4.9)	(12,606)	(13.6)	(16,234)	(21.0)
Income tax (expense) benefit	(64)	(0.1)	(7,814)	(8.4)	6,026	7.8
Net loss	(5,743)	(5.0)	(20,420)	(22.0)	(10,208)	(13.2)

Results of Operations

Revenues

Revenues were €116.0 million for the year ended December 31, 2004 compared with €92.9 million for year ended December 31, 2003. The increase of 25% in revenues primarily results from higher sales volumes in our wireless communication and automotive markets which more than offset a decline in revenues in our industrial applications sector during the period. Revenues in the wireless communications sector were €90.6 million for the year ended December 31, 2004 compared with €69.9 in 2003, comprising 78% and 75% of our total revenues in the years ended December 31, 2004 and 2003, respectively. Revenues from our automotive applications sector were €11.9 million and €7.9 million, representing 10% and 9% of our total revenues in 2004 and 2003, respectively. Revenues from our industrial applications sector were €13.5 million or 12% of total revenues in 2004 and €15.1 million or 16% of total revenues in 2003.

Regional growth was particularly strong in Asia where revenue increased from €24.9 million (China €18.2 million, other Asian countries €6.7 million) to €42.1 million (China €19.7 million, other Asian countries €22.4 million) for year ended December 31, 2003 and 2004, respectively.

Due to the shipments of new products in volume production to the market we expect revenues for the year ended December 31, 2005 to be higher than those for the year ended December 31, 2004. However, our forward visibility with respect to customer demand is limited and a successful introduction of new products depends on the completion of new designs on a timely basis. Our revenues for 2005 will also be highly dependent on continued growth in the worldwide market for cellular handsets. We cannot give any assurance that this growth trend will continue throughout 2005.

Cost of Sales

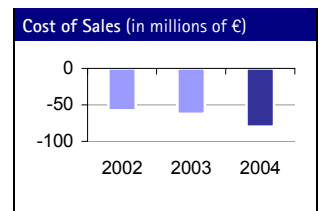
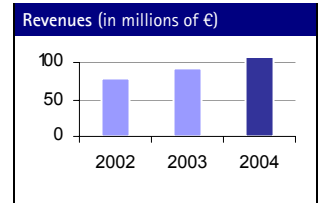
Cost of sales consists of the costs of outsourcing production and assembly, related personnel costs and applicable overhead and depreciation of test and other equipment. Cost of sales increased by 28% from €62.4 million (67.2% of our total revenues) for the year ended December 31, 2003 to €79.8 million (68.8% of our total revenues) for year ended December 31, 2004, in line with increased production volumes. In addition, as a result of introducing new products to volume production in 2004, per unit production costs increased during their ramp-up phase and also increased cost of sales as a percentage of total revenues.

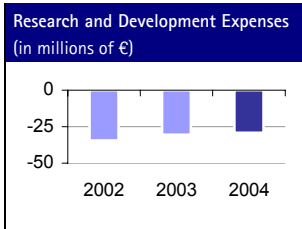
Selling and Marketing Expenses

Selling and marketing expenses consist primarily of salaries, travel expenses, sales commissions and costs associated with advertising and other marketing activities. Selling and marketing expenses increased from €4.2 million for year ended December 31, 2003 to €6.2 million for year ended December 31, 2004 due primarily to an increase in sales commissions incurred in connection with higher sales volumes. As a percentage of total revenues, selling and marketing expenses increased from 4.5% to 5.3%.

General and Administrative Expenses

General and administrative expenses consist primarily of personnel and support costs for our finance, human resources, information systems and other management departments. General and administrative expenses increased from €5.0 million for the year ended December 31, 2003 to €5.5 million for the year ended December 31, 2004, due primarily to legal fees and other costs incurred in connection with the filing of patent applications. General and administrative expenses decreased from 5.4% of total revenues to 4.7% of total revenues resulting from the proportionally higher revenue base.





Research and Development Expenses

Research and development expenses principally consist of design and engineering related costs associated with the development of new application specific integrated circuits (“ASICs”) and application specific standard products (“ASSPs”). Research and development expenses decreased 5% from €30.6 million for the year ended December 31, 2003 to €29.1 million for the year ended December 31, 2004. The decrease in research and development expenses primarily results from continued cost savings following the closure of our Swedish subsidiary. Research and development expenses decreased from 32.9% to 25.0% as a percentage of total revenues resulting both from the absolute decrease and the proportionately higher revenue base.

Amortization of Intangible Assets

Intangible assets subject to amortization include ASIC design software, a 16-bit microcontroller, licenses and certain imaging patents. Amortization expense for the year ended December 31, 2004 was €1.5 million as compared to €2.1 million for the year ended December 31, 2003, a decrease of 27%. Amortization expense decreased as certain intangible assets reached the end of their useful lives.

Restructuring and Related Impairment Charges

In the second quarter of 2003 we closed our Swedish subsidiary. In connection with the closure of the facility, we recorded restructuring charges of €1.5 million and impairment charges of €0.3 million, totaling €1.8 million for the year ended December 31, 2003. In 2004 we settled a lease obligation in connection with the closure and incurred additional costs of €0.1 million. See Note 3 to the consolidated financial statements for further information.

Operating Loss

We reported an operating loss of €6.1 million for the year ended December 31, 2004 and €13.2 million for the year ended December 31, 2003, a decrease of 54%. This decrease in operating loss was primarily due to a higher gross margin and lower

restructuring and impairment charges in the year ended December 31, 2004.

Interest Income, net

Interest income, net from the Company’s investments (primarily short-term deposits and exchange-traded funds) increased from €0.8 million for the year ended December 31, 2003 to €1.1 million for the year ended December 31, 2004 reflecting higher cash equivalents and marketable securities balances during 2004.

Foreign Currency Exchange Gains and Losses, net

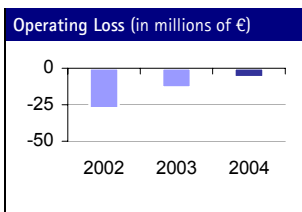
Foreign currency transaction gains and losses result from amounts ultimately realized upon settlement of foreign currency transactions and from the period end re-measurement of foreign currency denominated receivables, prepaid expenses and payables into Euro. Foreign currency exchange losses, net were €0.7 million for the year ended December 31, 2004 and €0.5 million for the year ended December 31, 2003.

Recovery of Investment

In the fourth quarter of 2001, we determined that our ability to recover the full amount of our investments in silicon supplier ESM Holding Limited (“ESM”) was impaired. Accordingly we wrote off our investments in ESM. In March 2002, International Rectifier acquired ESM. As a result we were able to recover €0.1 million and €0.3 million for the years ended December 31, 2004 and 2003, respectively.

Income Taxes

Income tax expense was €0.1 million for the year ended December 31, 2004 compared with €7.8 million income tax expense for the year ended December 31, 2003. The change in income taxes mainly reflects a valuation allowance on deferred tax assets recognized in 2003 of €11.8 million primarily related to the uncertainty about the future realizability of our German tax-loss carryforwards. See Note 6 to the consolidated financial statements for further information.



Trend Information

General

The semiconductor industry in general is highly cyclical and has been subject to significant economic downturns which, at various times, have resulted in production overcapacity, reduced product demand and an accelerated erosion of average selling prices.

Revenues from our wireless communications applications accounted for 78% of our total revenues for the year ended December 31, 2004, 75% of our total revenues for the year ended December 31, 2003 and 71% of our total revenues for the year ended December 31, 2002.

According to the Semiconductor Industry Association (SIA), strong growth in sales of personal computers and wireless handsets were among the major drivers of record chip sales in 2004, evidenced by a 28% growth rate in 2004 for the total market for semiconductors (source: SIA press release, 31 January 2005, "Global semiconductor sales hit record \$213 billion in 2004"). The wireless handset market saw its first real growth in 3G/WCDMA (Wideband code-division multiple access) phones, with 20 million shipped worldwide in 2004, representing 3% of total handset sales in 2004 (source: Strategy Analytics press release, 14 February 2005, "20 Million 3G Phones Sold Worldwide in 2004"). This growth was driven by aggressive mobile operator marketing in Japan and Western Europe to encourage millions of early adopters to upgrade from their existing 2.5G devices. The top handset manufacturers in this space expect the market to more than double in size in 2005 as usability and styling is improved.

Overall wireless handset shipment growth was up last year, as a result of technological advanced features such as color screens, cameras and clamshell designs. The markets saw more clamshell handsets with dual displays, larger main displays to display content, more sophisticated and higher resolution cameras, and high quality audio. These developments were accompanied by

manufacturers increasingly using additional applications and graphics processors, and continually demanding even lower power consumption in the same form factor despite incorporating more sophisticated features.

Market Trends

The biggest market trend in the industry that Dialog Semiconductor addresses is the convergence of multimedia and mobile communications. This means we will see not just camera phones or smart phones, but devices such as PDAs with integrated phone and multimedia capability. There will most likely be an explosion in other mobile gaming and entertainment possibilities in the next three years, resulting from the rapid evolution of the mobile handset as we currently know it.

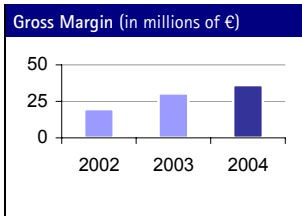
Camera phones alone will build on the growth of 200% in 2004 (source: In-Stat/MDR press release, 14 December 2004, "Camera Phone Market Continues to Boom - 200% Growth in Annual Shipments"). Mobile gaming services are expected to generate significant additional revenue in future years, accounting for over 4% of total wireless data revenue in the USA by 2009 (source: In-Stat/MDR press release, 7 September 2004, "Gaming to be Key Contributor to Wireless Data Usage and Revenues").

Traditional mobile phone handsets will also continue to grow, although not at as great a rate as in the boom years leading up to 2001. Gartner predicts 763 million handsets to be shipped in 2008, compared to 629 million in 2004 (source: Gartner Market Focus Report: "Semiconductors in Mobile Phones, Worldwide, 2004-2008", 24 December 2004).

More than 20 million 3G phones shipped in 2004

WCDMA technology ready for commercial launch as networks improve and handsets become generally available

In the broader consumer electronics sector, there has also been a burst of consumer interest in devices for playing back downloaded digital music. This trend is likely to fuel interest and also significant growth in portable digital music players, even with the different music download standards such as MP3, AC3 or WMA.



In automotive, complex electronics systems were in the past a feature of only the most prestigious cars. However, the growing trend among the manufacturers of lower cost cars is to add more value to their cars, making the electronics systems almost as complex as those of the top end cars. The result will be a mass market rather than niche market for complex electronics systems built in to the car.

One other key trend will be the growing use of imaging electronics for driver safety features such as geographic positioning, navigation systems, blind spot detection and white lane departure systems.

Geographic Market Trends

We allocate our revenues to countries based on the location of the shipment destination. Changes in revenues from period to period have differed among geographical regions. As our customers have continued to increase their production in the greater China region and by adding new Asian customers, regional growth was particularly strong in Asia in 2004, where revenue increased by 69% from €24.9 million for the year ended December 31, 2003 to €42.1 million for the year ended December 31, 2003, respectively. Particularly in France, we experienced decline in demand for our ASIC products where revenue decreased by 58% from €4.5 million for the year ended December 31, 2003 to €1.9 million for the year ended December 31, 2004, due primarily to the fact that our contract with one customer based in France was not renewed upon expiration. In 2003, regional growth was particularly strong in Germany and China where revenue increased from €31.5 million for the year ended December 31, 2002 to €45.4 million for the year ended December 31, 2003 and from €13.0 million for the year ended December 31, 2002 to €18.2 million for the year ended December

31, 2003, respectively. In 2003, particularly in France, we experienced decline in demand for our ASIC products where revenue decreased from €9.3 million for the year ended December 31, 2002 to €4.5 million for the year ended December 31, 2003.

Gross Margin Trends

Our gross margin decreased from 32.8% of revenues for the year ended December 31, 2003 to 31.2% of revenues for the year ended December 31, 2004. The weakening of the US dollar against the Euro and the reduction in price of wireless communication ICs were the primary factors contributing to this decrease in our gross margin.

Research and Development Expenditure Trends

Research and development costs amounted to €29.1 million in 2004, €30.6 million in 2003 and €34.5 million in 2002. We expect to incur research and development costs below the current level based on certain cost savings measures. Our ability to generate revenues in the long term depends on achieving technical feasibility from our research and development programs, and on customers accepting our designs and implementing them in large-scale production.

Foreign Currency Exchange Rate Trends

The reporting currency for our consolidated financial statements is the Euro. The functional currency for our operations is generally the applicable local currency. Accordingly, the assets and liabilities, the equity accounts and the statements of income and cash flow of companies whose functional currency is not the Euro must be translated into the reporting currency (the Euro). See Note 2 to the consolidated financial statements for further information. Changes in exchange rates also influence our results of operations. Our sales are primarily denominated in US Dollars and Euro, whereas our purchases of raw materials and manufacturing services are primarily denominated in US Dollars.

In order to hedge our foreign currency exposure, primarily the US Dollar, we attempt to match cash inflows and outflows in the same currency.

Since its introduction on January 1, 1999, the Euro has fluctuated in value against the US Dollar. From the date of its introduction through December 31, 2001, the Euro declined approximately 25% against the US Dollar. Through February 04, 2005 the Euro had recovered to 110% of its original value. Changes in the exchange rate between the Euro and other non-Euro currencies, principally the US Dollar, will affect the translation of our consolidated financial results into Euro, and will also affect the value of any amounts that our subsidiaries distribute to us. Exchange rate changes may also affect our balance sheet. Changes in the Euro values of our assets and liabilities resulting from exchange-rate movements may cause us to record foreign currency gains and losses. We do not currently enter into forward or other derivative transactions to hedge against exchange rate fluctuations.

For the year ended December 31, 2004, 55% of our revenues were denominated in Euro and 45% were denominated in US Dollars, and 18% of our cost of sales was denominated in Euro and 82% was denominated in US Dollars. Due to the weak-

ening of the US Dollar in the fourth quarter and a higher proportion of US Dollar-denominated revenue compared with previous quarters combined with lower than expected uptake from key customers, our revenue growth was lower in the fourth quarter compared with the first three quarters of the year.

For the year ended December 31, 2003 78% of our revenues were denominated in Euro and 22% were denominated in US Dollars, and 25% of our cost of sales was denominated in Euro and 75% was denominated in US Dollars. For the year ended December 31, 2002, 76% of our revenues were denominated in Euro, 23% were denominated in US Dollars and 1% were denominated in Pound Sterling, and 25% of our cost of sales was denominated in Euro and 75% was denominated in US Dollars.

We also have foreign currency risk with respect to our net investments in foreign subsidiaries in Japan, the United Kingdom and the United States. Foreign currency translation gains and losses with respect to these subsidiaries are included in other comprehensive income.

Liquidity and Capital Resources

Cash flows

Cash used for operating activities was €8.6 million for year ended December 31, 2004 compared with cash provided by operating activities of €7.6 million for the year ended December 31, 2003. In the year ended December 31, 2004 we used cash mainly to increase our inventory to meet previously projected forecasts of our customers. We expect this level to be reduced in the first half 2005. In the year ended December 31, 2003, our working capital (excluding cash and cash equivalents and marketable securities) had decreased primarily due to contractually required refunds of advance payments from a silicon supplier which resulted in a related operating cash inflow.

Cash provided by investing activities was €14.5 for year ended December 31, 2004 compared with cash used for investing

activities of €30.3 million for year ended December 31, 2003. Cash provided by investing activities for the year ended December 31, 2004 consisted mostly of a net sale of marketable securities of €27.4 million offset in part by the purchase of test equipment, tooling (masks), laboratory and EDP equipment of €12.3 million, and the purchase of software, licenses and patents of €0.7 million. Cash used for investing activities for the year ended December 31, 2003 consisted mostly of the purchase of marketable securities of €45.0 million, the purchase of test equipment, tooling (masks), laboratory and EDP equipment of €5.9 million, and the purchase of software, licenses and patents of €1.4 million. In October 2003, we also received an early repayment of our deposit of €21.7 million (USD 20 million) from Chartered.

Liquidity

At December 31, 2004 we had €14.0 million in cash and cash equivalents and €17.5 million in marketable securities. The working capital was €67.1 million.

Our primary sources of liquidity have historically been cash from operations, cash from the issuance of ordinary shares in 1999 and 2000, short-term borrowings, the recovery of the investment in ESM Limited and in 2003 the early repayment of a deposit from Chartered. As of December 31, 2004 we had no long-term debt. We expect to reduce our working capital in 2005, thereby increasing our cash and cash equivalents and marketable securities in 2005. A decrease in customer demand for our products caused by unfavorable industry conditions or an inability to develop new products in response to technological changes could materially reduce the amount of cash generated from operations.

If necessary, we have available for use a short-term credit facility of €12.5 million that bears interest at a rate of EURIBOR + 0.75% per annum. At December 31, 2004 we had no amounts outstanding under this facility. Accordingly, we believe the funding available from these and other sources will be sufficient to satisfy our working capital requirements in the near to medium term.

Capital Expenditures and Investments

Purchases of property, plant and equipment were €12.3 million for the year ended December 31, 2004 compared to €5.9 million for the year ended December 31, 2003 and €3.9 million for the year ended December 31, 2002. Our capital expenditures in 2004, 2003 and 2002 consisted primarily of purchasing new or replacement test systems, tooling equipment, handling systems and other equipment in the ordinary course of our business. Capital expenditures in 2004 increased over that of prior years as we upgraded eight test systems enabling us to test four ICs in a single test step, and added certain test equipment to test color display and image sensor ICs. In 2004, 2003 and 2002 we paid install-

ments of €0.3, €0.8 and €1.5 million, respectively, for the CMOS imaging technology and associated CMOS Active Pixel Sensor (APS) patents which we acquired in 2002. We expect capital expenditures in 2005 to be below the 2004 level.

In future periods, we may make strategic investments or acquisitions in connection with our plans to expand our business internationally.

Off-Balance Sheet Arrangements and Other Commitments

We have no off-balance sheet arrangements involving variable interest entities. We lease design software, all of our office facilities, office and test equipment, and vehicles under operating leases. Future minimum lease payments under rental and lease agreements, which have initial or remaining terms in excess of one year at December 31, 2004 are as follows (€ thousands)

(in thousands of €)	Operating leases
2005	8,148
2006	6,629
2007	6,399
2008	6,429
2009	3,297
Thereafter	316

We have no long-term debt, capital lease obligations, unconditional purchase obligations or any other long-term obligations that would have a material impact on our liquidity or financial condition. We have supply agreements with various suppliers and maintain an outstanding balance of advance payment of €1.2 million with one supplier, which will be refunded in proportion to our purchases of wafers. See Note 11 to the consolidated financial statements.

Dividends

We did not pay dividends in the years ended December 31, 2004, 2003 and 2002. We do not currently plan to pay dividends in the foreseeable future.

Critical Accounting Policies and Related Uncertainties

We have identified the following accounting policies and related uncertainties with the accounting measures used in preparing our consolidated financial statements that we believe are essential to understanding the financial reporting risks present in the current economic environment.

Recoverability of Long-Lived Assets

Goodwill

At December 31, 2004, the carrying value of our goodwill is €11.8 million. Since 2002, goodwill is no longer amortized, but we have, and will continue to evaluate the recoverability of our goodwill at least annually or when significant events occur or circumstances arise which indicate that the fair value of the Company may be less than its net shareholders' equity. The fair value of the Company is determined by estimating the present value of future cash flows, which we believe is a more appropriate measure to determine fair value than the Company's current market capitalization (which is based on the quoted market price of the Company's ordinary shares). For purposes of performing step 1 of the impairments test, the fair value of the entire company is determined based on expected cash flows which are derived from the Company's strategic plan and forecasts. The discount rate applied considered marketplace participant assumptions including a risk-free rate, market risk premium and a beta factor that is consistent with the Company's market peers. If it becomes necessary to change assumptions used to determine the fair value of the company, we may conclude that our ability to recover the carrying value of our goodwill is impaired. Such an impairment charge could have a material adverse impact on our future result of operations.

Other Long-Lived Assets

Our business is capital intensive and has required, and will continue to require, significant investments in long-lived

assets, including property, plant, equipment and intangible assets (other than goodwill). At December 31, 2004, the carrying amount of our property, plant and equipment was €21.2 million. As discussed in Note 2 to the consolidated financial statements, recoverability of these long-lived assets that will continue to be held and used is evaluated whenever an indication of impairment exists. Then we will compare the carrying amount of the asset or group of assets to the net undiscounted cash flows expected to be generated by the asset or group of assets. If the asset or group of assets is considered impaired, the impairment recognized is measured as the amount by which the carrying amount of the impaired asset or group of assets exceeds its fair value.

We do not believe that our ability to recover the carrying value of our other long-lived assets has been impaired and no significant impairment charges have been recognized in any of the past three years. However, a general economic downturn and, specifically, a continued downturn in the semiconductor industry would intensify competitive pricing pressure because of overcapacity in the industry, and we could be forced to decrease production and reduce capacity. Such events could adversely affect our estimates of future net cash flows expected to be generated by our long-lived assets. It is reasonably possible that our future operating results could be materially and adversely affected by an impairment charge related to the recoverability of our long-lived assets.

Realizable Value of Inventories

We value inventory at the lower of cost or market. We review the recoverability of inventory based on regular monitoring of the size and composition of the inventory positions, market conditions, current economic events, the pricing environment and projected future demand. This evaluation is inherently judgmental and requires material esti-

mates, including both forecasted product demand and pricing environment, both of which may be susceptible to significant change.

Changes in estimates regarding the realizability of the carrying value of our inventory has resulted in excess inventory provision of €1.9 million being charged to costs of sales in 2002. No excess inventory provision was required in 2004 and 2003. At December 31, 2004, our total inventory was €29.8 million. We believe that the carrying value of our inventory will be recovered through customer consumption of goods based on their forecasts and related contractual agreements. However, the demand for our products can fluctuate significantly in response to rapid technological changes in the semiconductor and wireless communications industries. It is reasonably possible that future operating results could be materially and adversely affected if any excess inventory charges are needed.

Realization of Deferred Tax Assets

Total deferred tax assets, before the recognition of valuation allowances, were €31.2 million at December 31, 2004, which include deferred tax assets of €25.2 million on tax loss carryforwards. While the majority of these losses may be carried forward indefinitely, their realization is dependent on generating sufficient taxable income to utilize the losses. In December 2003, the German government enacted new tax legislation, which among other things, limits the use of German tax-loss carryforwards to 60% of the taxable income for fiscal years starting from 2004 and thereafter. We have evaluated our deferred tax asset position and the need for a valuation allowance as a result of this change in tax law. The assessment requires the exercise of judgment on the part of our management, with respect to, among other things, benefits that could be realized from available tax strategies and future taxable income, as well as other positive and negative factors. Our assessment considered the weight given to cumulative tax losses incurred in

Germany, as well as detailed forecasts of taxable income in the foreseeable future. Although we forecasted generating future taxable income, the change in tax law increased the forecasted number of additional years we had to generate such future taxable income in order to fully realize these loss carryforward benefits. Pursuant to SFAS 109 and the inherent uncertainties in projecting future taxable income, we concluded that it is more likely than not that a portion of our tax losses could not ultimately be realized. Consequently, we recognized an additional valuation allowance of €1.9 million and €11.8 million as of December 31, 2004 and 2003, respectively, to reduce the carrying value of our net deferred tax assets to an amount that we believed was more likely than not expected to be ultimately realized.

Risk Factors

The market in which we compete is characterized by continuous development and technological improvement. As a result, our success depends on our ability to develop new designs and products on a cost effective, timely basis. Our future success also depends on our ability to anticipate and respond to new market trends, to rapidly implement new designs which satisfy customers' desires, and to keep abreast of technological changes within the semiconductor industry generally. It is not possible to predict or identify all relevant risk factors and, therefore, the following list should not be considered to be a complete statement of all potential risks or uncertainties.

- We have not been profitable for the last four fiscal years, and there is no guarantee that we will return to profitability
- We currently depend on a few customers for a substantial portion of our revenues, and the loss of one or more of these customers may result in a material decline in our revenues
- Our revenues, profitability and growth could decline if the growth of the wireless communications market slows
- If we are unable to adapt rapidly to changing markets and technology, we may lose customers and be unable to develop new business
- The semiconductor industry is highly cyclical in nature and this results in periodic overcapacity
- We face intense competition, and if we are unable to compete effectively or if we are unable to adapt rapidly to changing markets and technology, we could lose customers and be unable to develop new business
- The loss of one of our principal foundry relationships or assembly services or a delay in foundry or assembly production may result in a material loss of production and revenues
- Obtaining access to manufacturing capacity at semiconductor manufacturing plants may become increasingly difficult and could result in higher costs and a material loss of revenues
- Perceived health risks relating to cellular handsets could lead to decreased demand for ASICs
- Our business, financial condition and reputation may be materially adversely affected if our ASICs, or the electronic systems of which they are a part, contain defects that cause damage or injury
- Our products are difficult to manufacture and manufacturing defects can adversely affect our results
- We may not be able to remain competitive if we lose any of our key executives or if we cannot hire and retain qualified engineers and sales and marketing personnel
- If we are unable to protect our intellectual property and knowhow from being copied or used by others, our competitors may gain access to its content and technology
- The profitability of our business may be adversely affected by currency fluctuations and by the economic and legal developments in the countries where we conduct our business
- We may become a passive foreign investment company
- US-resident shareholders may find it more difficult to protect their interests than they would as shareholders of a US-based corporation
- Our future operating results could be materially affected if judgments underlying any of our accounting policies were to significantly change

Outlook

In recent years, convergence of mobile communications and multimedia has been talked about as a key driver for growth in the electronics industry. Dialog Semiconductor expects 2005 to be the first year when this is expected to have a major impact on our business.

Convergence will drive growth in shipments of our integrated circuits (ICs) for power management and color LCD displays as well as camera modules featuring advanced optics for wireless and consumer electronics products. In addition, we expect to see further advances in the use of image sensors in automotive and industrial electronics on top of our established market in safety and comfort electronics in cars.

While mobile phone handset growth is expected to rise progressively to 763 million handsets in 2008 (from 629 million in 2004, source: Gartner Market Focus Report: "Semiconductors in Mobile Phones, Worldwide, 2004-2008", 24 December 2004), we are now supplying more than just the power management and audio IC that represented the traditional slot for Dialog Semiconductor in the handset. Expansion of our product range over the last three years not only addresses more elements of the handset and smartphone, but also extends to other portable consumer electronics devices like PDAs (personal digital assistants) and personal audio players (such as MP3).

Asia plays a strong part in this growth of wireless and consumer electronics, which is why we have also strengthened our operations in the region with our new southeast Asia office for local sales, marketing and technical support to a growing customer base.

In the wireless sector, some of the market indicators illustrate where greater demand is likely to emerge for our diversified range of ICs and modules for the mobile phone.

Worldwide annual shipments of camera phones was up more than 200% in 2004 (source: In-Stat/MDR press release, 14

December 2004, "Camera Phone Market Continues to Boom - 200% Growth in Annual Shipments"), and CMOS image sensor shipments will grow at roughly seven times the rate of CCDs (charge coupled devices) through 2008 (source: In-Stat/MDR press release, 18 October 2004, "Camera Phones and Digital Still Cameras Driving Market for CMOS and CCDs"). CMOS sensors offer lower prices, lower power consumption, and the ability to integrate other functions on chips, making them ideal for camera phones. We have introduced camera modules that improve picture quality due to world-class optics from Carl Zeiss, and provide excellent image sensor performance.

As operators look to increase ARPU (average revenue per user), mobile gaming services are expected to generate 4.4% of total wireless data revenues of US\$1.8 billion in the USA by 2009; gaming downloads will also increase 10-fold from 2003 levels (source: In-Stat/MDR press release, 7 September 2004, "Gaming to be Key Contributor to Wireless Data Usage and Revenues"). The implication in the US and worldwide is that handsets will need both advanced color graphic display capability and extremely efficient power management systems.

In the automotive sector, we are expecting more interest in our imaging systems addressing applications such as lane departure warning and blind spot detection.

Overall, Dialog Semiconductor believes the prospects for growth during 2005 are positive as a result of our transition to both developing more application specific standard products (ASSPs) for emerging 'convergence' applications in wireless and consumer electronics, as well as addressing the needs of our application specific IC (ASIC) customers in the more traditional but advancing automotive and industrial electronics markets.

Report of Independent Registered Public Accounting Firm

To the Board of Directors of Dialog Semi-conductor Plc:

We have audited the accompanying consolidated balance sheets of Dialog Semiconductor Plc and subsidiaries (the "Company") as of December 31, 2004 and 2003 and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with standards established by the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Dialog Semiconductor Plc and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

Stuttgart, Germany

February 21, 2005

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Consolidated Financial Statements

Consolidated Financial Statements	33
Consolidated Statements of Operations	34
Consolidated Balance Sheets	35
Consolidated Statements of Cash Flows	36
Consolidated Statements of Changes in Shareholders' Equity	37
Notes to the Consolidated Financial Statements	38
1. General	38
2. Summary of Significant Accounting Policies	39
3. Restructuring and Related Impairment Charges	42
4. Recovery of Investment	42
5. Other Disclosures to the Statements of Operation	43
6. Income Taxes	43
7. Additional Cash Flow Information	45
8. Trade Accounts Receivable, net	45
9. Inventories	45
10. Marketable Securities	45
11. Deposits and Prepaid Expenses	46
12. Property, Plant and Equipment, net	46
13. Intangible Assets and Goodwill	46
14. Accrued Expenses	47
15. Shareholders' Equity and Comprehensive Income	47
16. Pension Scheme	47
17. Stock-based Compensation	48
18. Commitments	49
19. Financial Instruments and Hedging Activities	49
20. Segment Reporting	50
21. Transactions with Related Parties	51
Corporate Governance	52
Report of the Board of Directors	52
Accounting under International Financial Reporting Standards (IFRSs)	52
Corporate Governance Principles	53
Members of the Board of Directors	56

Consolidated Statements of Operations

(in thousands, except per share data)	Notes	2004	2004	2003	2002
Revenues	20	\$ 157,100	€ 116,044	€ 92,893	€ 77,104
Cost of sales	5	(108,010)	(79,783)	(62,374)	(57,409)
Gross margin		49,090	36,261	30,519	19,695
Selling and marketing expenses		(8,444)	(6,237)	(4,197)	(4,149)
General and administrative expense		(7,394)	(5,462)	(5,044)	(6,447)
Research and development expenses		(39,356)	(29,071)	(30,590)	(34,530)
Amortization and intangible assets		(2,058)	(1,520)	(2,073)	(1,975)
Restructuring and related impairment charges	3	(80)	(59)	(1,839)	-
Operating loss		(8,242)	(6,088)	(13,224)	(27,406)
Interest income, net		1,463	1,081	757	1,121
Foreign currency exchange gains and losses, net		(983)	(726)	(454)	(1,918)
Recovery of investment	4	73	54	315	11,969
Result before income taxes		(7,689)	(5,679)	(12,606)	(16,234)
Income tax (expense) benefit	6	(86)	(64)	(7,814)	6,026
Net loss		(7,775)	(5,743)	(20,420)	(10,208)
Loss per share:					
Basic and diluted		(0.18)	(0.13)	(0.46)	(0.23)
Weighted average number of shares (in thousands):					
Basic and diluted		44,025	44,025	43,951	43,888

The accompanying notes are an integral part of these Consolidated Financial Statements

Consolidated Balance Sheets

(in thousands)	Notes	Dec 31, 2004	Dec 31, 2004	Dec 31, 2003
ASSETS				
Cash and cash equivalents		\$ 18,922	€ 13,977	€ 8,109
Trade accounts receivable, net	8	32,540	24,036	14,338
Inventories	9	40,335	29,794	13,242
Marketable securities	10	23,749	17,542	44,900
Deferred taxes	6	950	702	103
Prepaid expenses	11	834	616	2,131
Other current assets		380	281	993
Total current assets		117,710	86,948	83,816
Property, plant and equipment, net	12	28,752	21,238	20,590
Intangible assets	13	5,775	4,266	5,440
Goodwill	13	15,956	11,786	11,786
Deposits	11	263	194	183
Deferred taxes	6	22,270	16,450	17,729
Prepaid expenses	11	1,458	1,077	927
TOTAL ASSETS		192,184	141,959	140,471
LIABILITIES AND SHAREHOLDERS' EQUITY				
Trade accounts payable		20,888	15,429	7,157
Accrued expenses	14	4,175	3,084	3,165
Income taxes payable		12	9	18
Deferred taxes	6	9	7	4
Other current liabilities		1,726	1,275	1,615
Total current liabilities		26,810	19,804	11,959
Deferred taxes	6	1,381	1,020	1,669
Total liabilities		28,191	20,824	13,628
Ordinary Shares	15	9,515	7,028	6,737
Additional paid-in capital		228,497	168,782	168,795
Accumulated deficit		(72,323)	(53,422)	(47,679)
Accumulated other comprehensive loss		(1,294)	(956)	(984)
Employee stock purchase plan shares		(402)	(297)	(26)
Shareholders' equity		163,993	121,135	126,843
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		192,184	141,959	140,471

The accompanying notes are an integral part of these Consolidated Financial Statements

Consolidated Statements of Cash Flows

(in thousands)	2004	2004	2003	2002
Cash flows from operating activities:				
Net loss	\$ (7,775)	€ (5,743)	€ (20,420)	€ (10,208)
Adjustments to reconcile net loss to net cash provided by (used for) operating activities:				
Recovery of investment	(73)	(54)	(315)	(11,969)
Provision for excess inventory	-	-	-	1,930
Restructuring and related impairment charges	(444)	(328)	613	-
Depreciation of property, plant and equipment	15,570	11,501	12,545	12,834
Amortization intangible assets	2,058	1,520	2,073	1,975
Losses on disposals of fixed assets	199	147	253	-
Increase in deferred tax asset valuation allowance	-	-	10,237	-
Other changes in deferred taxes	24	18	(1,984)	(4,167)
Changes in current assets and liabilities:				
Trade accounts receivable	(13,128)	(9,697)	1,691	450
Inventories	(22,408)	(16,552)	1,265	715
Prepaid expenses	1,844	1,362	5,382	1,663
Trade accounts payable	11,204	8,276	(2,846)	1,760
Accrued expenses	(104)	(77)	(258)	(1,381)
Income taxes payable	(12)	(9)	(107)	(1,224)
Other assets and liabilities	1,401	1,035	(541)	26
Cash provided by (used for) operating activities	(11,644)	(8,601)	7,588	(7,596)
Cash flows from investing activities:				
Recovery of investment	73	54	315	11,969
Purchases of property, plant and equipment	(16,680)	(12,321)	(5,901)	(3,872)
Purchases of intangible assets	(914)	(675)	(1,410)	(2,101)
Investments and deposits received (made)	(27)	(20)	21,670	94
Purchases of marketable securities	(67,243)	(49,670)	(44,998)	-
Sale of marketable securities	104,360	77,087	-	-
Cash provided by (used for) investing activities	19,569	14,455	(30,324)	6,090
Cash flows from financing activities:				
Costs for issuance of shares	(28)	(21)	-	-
Sale of employee stock purchase plan shares	40	30	37	58
Other	-	-	-	(44)
Cash provided by financing activities	12	9	37	14
Cash provided by (used for) operating, investing and financing activities	7,937	5,863	(22,699)	(1,492)
Effect of foreign exchange rate changes on cash and cash equivalents	7	5	(197)	(129)
Net increase (decrease) in cash and cash equivalents	7,944	5,868	(22,896)	(1,621)
Cash and cash equivalents at beginning of period	10,978	8,109	31,005	32,626
Cash and cash equivalents at end of period	18,922	13,977	8,109	31,005

The accompanying notes are an integral part of these Consolidated Financial Statements

Consolidated Statements of Changes in Shareholders' Equity

(in thousands of €)	Accumulated other comprehensive loss							Total
	Ordinary Shares	Additional paid-in capital	Accumulated deficit	Currency translation adjustment	Available for sale securities	Derivative financial instruments	Employee stock purchase plan shares	
Balance at December 31, 2001	6,737	168,788	(17,051)	(270)	-	(42)	(70)	158,092
Net loss	-	-	(10,208)	-	-	-	-	(10,208)
Other comprehensive loss	-	-	-	(287)	-	(116)	-	(403)
Total comprehensive loss								(10,611)
Cost of issuance of shares in 2000	-	(44)	-	-	-	-	-	(44)
Sale of employee stock purchase plan shares	-	37	-	-	-	-	21	58
Balance at December 31, 2002	6,737	168,781	(27,259)	(557)	-	(158)	(49)	147,495
Net loss	-	-	(20,420)	-	-	-	-	(20,420)
Other comprehensive income (loss)	-	-	-	(366)	(61)	158	-	(269)
Total comprehensive loss								(20,689)
Sale of employee stock purchase plan shares	-	14	-	-	-	-	23	37
Balance at December 31, 2003	6,737	168,795	(47,679)	(923)	(61)	-	(26)	126,843
Net loss	-	-	(5,743)	-	-	-	-	(5,743)
Other comprehensive income (loss)	-	-	-	(5)	33	-	-	28
Total comprehensive loss								(5,715)
New issuance of shares	291	(22)	-	-	-	-	(291)	(22)
Sale of employee stock purchase plan shares	-	9	-	-	-	-	20	29
Balance at December 31, 2004	7,028	168,782	(53,422)	(928)	(28)	-	(297)	121,135

The accompanying notes are an integral part of these Consolidated Financial Statements.

Notes to the Consolidated Financial Statements

1. General

a) Description of Business

Dialog Semiconductor Plc and subsidiaries ("Dialog" or the "Company") is a fabless semiconductor company that develops and supplies power management, audio and imaging technology, delivering innovative mixed signal standard products as well as application specific IC solutions for wireless, automotive and industrial applications. The company's expertise in mixed signal design, with products manufactured entirely in CMOS technology, enhances the performance and features of wireless, hand-held and portable electronic products. Its technology is also used in intelligent control circuits in automotive and industrial applications. Production of these designs is then outsourced, and the final products are returned to Dialog for approval and testing before delivery to the customers.

b) Vulnerability Due to Certain Significant Concentrations

The Company's future results of operations involve a number of risks and uncertainties. Factors that could affect the Company's future operating results and cause actual results to vary materially from historical results include, but are not limited to, the highly cyclical nature of both the semiconductor and wireless communications industries, dependence on certain customers and the ability to obtain adequate supply of sub-micron wafers.

The Company's products are generally utilized in the cellular communications and automotive industries. The Company generates a substantial portion of its revenue from the wireless communications market, which accounted for 78%, 75% and 71% of the Company's total revenue for the years ended December 31, 2004, 2003 and 2002, respectively.

The Company's revenue base is diversified by geographic region and by individual customer. Changes in foreign currency exchange rates influence the Company's results of operations. The Company's sales are primarily denominated

in Euros and US dollars whereas purchases of raw materials and manufacturing services are primarily denominated in US dollars (see Note 19 for a description of the Company's hedging activities). The Company also has foreign currency exchange risks with respect to its net investments in foreign subsidiaries in Japan, the United Kingdom and the United States. Fluctuations in these currencies could significantly impact the Company's reported results from operations.

The Company depends on a relatively small number of customers for a substantial portion of its revenues, and the loss of one or more of these customers may result in a significant decline in future revenue. During 2004 and 2002, two customers individually accounted for more than 10% of the Company's revenues. Total revenues from these two customers were €75,651 and €46,746 or 65% and 61% in 2004 and 2002, respectively. Net receivables from these two customers were €15,724 at December 31, 2004. During 2003, one customer individually accounted for more than 10% of the Company's revenue. Total revenue from this customer was €60,192 or 65%. Net receivables from this customer were €9,414 at December 31, 2003. The Company performs ongoing credit evaluations of its customers' financial condition and, generally, requires no collateral from its customers.

c) Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). All amounts herein are shown in thousands of Euro ("€") and for the year 2004 are also presented in U.S. Dollars ("\$"), the latter being unaudited and presented solely for convenience of the reader at the rate of €1 = \$1.3538, the Noon Buying Rate of the Federal Reserve Bank of New York on December 31, 2004.

2. Summary of Significant Accounting Policies

Principles of Consolidation and Investments in Affiliated Companies

The consolidated financial statements include Dialog Semiconductor Plc and all of its owned subsidiaries:

Name	Registered Office	Participation
Dialog Semiconductor GmbH	Kirchheim/Teck - Nabern, Germany	100%
Dialog Semiconductor (UK) Limited	Swindon, UK	100%
Dialog Semiconductor Inc	Clinton, New Jersey, USA	100%
Dialog Semiconductor KK	Tokyo, Japan	100%

All intercompany accounts and transactions are eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with original maturity dates of three months or less.

Marketable Securities

Marketable securities at December 31, 2004 and 2003 consist of exchange traded funds and at December 31, 2003 also debt securities that are classified as available-for-sale and are accounted for on the basis of the settlement date and recorded at fair value as determined by the most recently quoted market price of each security at the balance sheet date. Unrealized gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a component of other comprehensive income (loss) until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. A decline in the market value of any available-for-sale security below cost that is deemed to be other than temporary will result in an impairment, which is charged to earnings. Interest income is recognized when earned.

Inventories

Inventories are valued at the lower of cost or market. Cost, which includes direct materials, labor and overhead plus indirect overhead, is determined using the first-in, first-out (FIFO) or weighted average cost methods.

Trade Accounts Receivable

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company reviews its allowance for doubtful accounts quarterly. Management, considering current information and events regarding the customers' ability to repay their obligations, considers the collectibility of a trade account receivable to be impaired when it is probable that the Company will be unable to collect all amounts due according to the sales terms. When a trade receivable is considered to be impaired, the amount of the impairment is measured based on the present value of expected future cash flows.

Any credit losses are included in the allowance for doubtful accounts through a charge to bad debt expense. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. In the profit and loss account, impairment losses are included in sales and marketing expenses. Recoveries of trade receivables previously written-off are recorded when received. Reversals of impairment losses, if any, would be included in other operating income. The Company does not have any off-balance-sheet credit exposure related to its customers.

Other Current Assets

Other current assets include tax refunds receivable at December 31, 2004 and 2003. It also included interest receivable at December 31, 2003.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation is charged on a straight-line basis over the estimated useful lives of the assets as follows:

Equipment	Useful life
Test equipment	3 to 8 years
Leasehold improvements	Shorter of useful life or lease term
Office and other equipment	3 to 13 years

Goodwill and other Intangible Assets

Goodwill represents the excess of purchase price over fair value of net assets of businesses acquired. Purchased intangible assets with estimable useful lives primarily consist of licenses, software, customer lists and patents and are recorded at acquisition cost less accumulated amortization. Intangible assets other than goodwill are amortized on a straight-line basis over the estimated useful lives of the assets ranging from 3 to 17 years.

Goodwill is tested annually for impairment and more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent the carrying amount exceeds the asset's fair value.

Prior to the adoption of SFAS 142 in 2002, goodwill and assembled workforce were amortized over their estimated useful life.

Impairment of Long-Lived Assets

In accordance with SFAS 144, long-lived assets, such as property, plant and equipment, and purchased intangibles subject to amortization, are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset or group of assets to future undiscounted net cash flows expected to be generated by the asset or group of assets. If the carrying amount of an asset or group of asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

Foreign Currencies

The functional currency for the Company's operations is generally the applicable local currency. Accordingly, the assets and liabilities of companies whose functional currency is other than the Euro are included in the consolidation by translating the assets and liabilities into the reporting currency (the Euro) at the exchange rates applicable at the end of the reporting year. Equity accounts are measured at historical rates. The statements of income and cash flows are translated at the average exchange rates during the year. Translation gains or losses are accumulated as a separate component of shareholders' equity. Foreign currency transaction gains and losses are included in financial income, net at each reporting period. They result from amounts ultimately realized upon settlement of foreign currency transactions and from the period end re-measurement of foreign currency denominated monetary assets and liabilities into the functional currency of the respective entity.

The exchange rates of the more important currencies against the Euro used in preparation of the consolidated financial statements were as follows:

Currency	Exchange rate at			Annual average exchange rate		
	Dec 31, 2004	Dec 31, 2003	2004	2003	2002	
	€ 1 =	€ 1 =	€ 1 =	€ 1 =	€ 1 =	
Great Britain	0.71	0.70	0.68	0.69	0.63	
Japan	139.83	133.68	134.46	130.93	118.05	
United States	1.36	1.25	1.24	1.13	0.94	

Revenue Recognition

Substantially all of the Company's revenue is derived from the sale of its products. Product revenue, net of discounts, is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price of the transaction is fixed and determinable, and collectibility is reasonably assured.

Product-Related Expenses

Cost of sales consist of the costs of outsourcing production and assembly, personnel costs and applicable overhead and depreciation of test and other equipment. Provisions for estimated product warranty are recorded in cost of sales at the time the related sale is recognized. Expenditures for advertising and sales promotion and for other sales-related expenses are charged to marketing expenses as incurred. Shipping and handling costs amounting to €313 (2003: €251; 2002: €221) are recorded within selling expenses.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years, in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company records deferred tax valuation allowances, if any, to reduce the deferred tax assets to amounts, which will more likely than not be realized.

Stock-Based Compensation

The Company has a stock-based employee compensation plan that is accounted for using the intrinsic-value-based method prescribed by APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Under this method, no stock-based compensation cost is reflected in net income (loss), as all options granted by the plan had an

exercise price equal to market value of the underlying common stock on the date of grant. SFAS 123, Accounting for Stock-Based Compensation, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation. As allowed by SFAS 123, the Company has elected to continue to apply the intrinsic-value-based method of accounting described above, and has adopted only the disclosure requirements of SFAS 123, as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure. The following table illustrates the effect on net loss if the fair-value-based method had been applied to all outstanding and unvested awards in each period.

	2004	2003	2002
Net loss, as reported:	(5,743)	(20,420)	(10,208)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(847)	(601)	(1,166)
Pro forma net loss	(6,590)	(21,021)	(11,374)
Earnings (loss) per share			
Basic – as reported	(0.13)	(0.46)	(0.23)
Basic – pro forma	(0.15)	(0.48)	(0.26)
Diluted – as reported	(0.13)	(0.46)	(0.23)
Diluted – pro forma	(0.15)	(0.48)	(0.26)

Derivative Instruments and Hedging Activities

The Company operates internationally, giving rise to exposure to changes in foreign currency exchange rates. The Company applies SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended by SFAS No. 137, SFAS No. 138 and SFAS No. 149, which provides guidance on accounting for all derivative instruments, and for hedging activities. Derivative financial instruments are recorded at their fair value and included in other current assets or other current liabilities.

Earnings (Loss) per Share

Earnings (loss) per share has been computed using the weighted average number of outstanding ordinary shares for each year. Because the Company reported a net loss in each of the years in the three-year period ended December 31, 2004, only basic per share amounts have been presented for those years. Had the Company reported net income in 2004, 2003 and 2002, the weighted average number of shares outstanding would have potentially been diluted by 1,309,406 and 962,184 and 2,634,382 stock options, respectively (not assuming the effects of applying the treasury stock method).

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, as well as disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and ex-

penses during the reporting period. Significant items subject to such estimates and judgments include the recoverability of the carrying value of goodwill and other long-lived assets, the realizability of deferred income tax assets and inventories, and the fair value of stock-based employee compensation awards. Actual results may differ from those estimates.

In the fourth quarter of 2004, the company determined that the useful life of its test equipment is eight years. Previously the useful life had been determined to be five years. The effect of this change in accounting estimates resulted in a lower depreciation of €1,349 (€842, net of tax, or €0.02 per share).

Recently Issued Accounting Standards

In June 2004, EITF No. 03-1, The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investment, was issued which includes new guidance for evaluating and recording other than temporary impairment losses on debt and equity securities accounted for under SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities and cost method investments, as well as new disclosure requirements for investments that are deemed to be temporarily impaired. While the disclosure requirements for specified debt and equity securities and cost method investments are effective for annual periods ending after December 15, 2003, the FASB Board has directed the FASB staff to delay the effective date for the measurement and recognition guidance contained in EITF No. 03-1. This delay does not suspend the requirement to recognize other-than-temporary impairments as required by existing authoritative literature. The Company does not expect the adoption of EITF No. 03-1 to have a material impact on its consolidated financial statements.

In November 2004, the FASB issued Statement No. 151, Inventory Costs, to amend the guidance in Chapter 4, "Inventory Pricing," of FASB Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins. Statement 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). The Statement requires that those items be recognized as current-period charges. Additionally, Statement 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The company does not believe the adoption of SFAS No. 151 will have a material impact on its consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123(R), Share-Based Payment, which establishes standards for transactions in which an entity exchanges its equity instruments for goods or services. This standard requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date

fair value of the award based upon an option-pricing model and an estimate of the number of awards expected to vest. Compensation cost will be recognized as they vest, including related tax effects. SFAS No. 123(R) will be effective for interim or annual reporting periods beginning on or after June 15, 2005. The statement provides for three alternate transition methods, each having a different reporting implication. The company previously accounted for its stock based

compensation plan using the intrinsic-value-based method based on APB Opinion No 25. Under this method, no stock-based compensation is reflected in net income (loss) (see also "Stock based compensation" in this note 2 to the consolidated financial statements). The Company is in the process of determining the transition method it is going to adopt and the potential impact on the financial statements.

3. Restructuring and Related Impairment Charges

Restructuring and related asset impairment charges are comprised of €59 restructuring charges for the year ended December 31, 2004 and of €1,554 restructuring charges and €285 impairment charges totaling €1,839 for the year ended December 31, 2003.

Restructuring Charges

In the first quarter of 2003 the Company decided to close the Swedish subsidiary. Restructuring charges incurred in 2003, include termination benefits that were paid to all employees affected by the closing of €1,076 and a provision for estimated costs that will continue to be incurred under an operating lease for the building for its remaining term without economic benefit to the Company of €478. In the first quarter of 2004 the Company settled its building lease obligation in connection with the closure and recognized an additional charge of €59. The contractual termination benefits were accounted for in accordance with SFAS 88. The provision for the operating lease was recorded at its estimated fair value in accordance with SFAS 146.

The pretax amounts for the restructuring charges are comprised of the following:

(in thousands of €)	Employee termination costs	Contract termination costs	Total
Liability balance at January 1, 2003	-	-	-
Initial charges	834	346	1,180
Additional charges	242	132	374
Payments made	(1,076)	(150)	(1,226)
Liability balance at December 31, 2003	-	328	328
Additional charges	-	59	59
Payments made	-	(387)	(387)
Liability balance at December 31, 2004	-	-	-

Asset Impairment Charges

As a result of the closure of the Swedish facility, certain long-lived assets with a net carrying value of €158 have been abandoned and certain prepaid expenses of €127 no longer provided any future benefit to the Company. Accordingly, impairment charges totaling €285 were recognized for the year ended December 31, 2003, to write-off these assets.

4. Recovery of Investment

In the fourth quarter of 2001, the Company determined that its ability to recover the full amount of its investments in silicon supplier ESM was impaired. Accordingly the Company wrote off the investments in ESM. In March 2002, ESM was

acquired by International Rectifier. As a result, the Company was able to subsequently recover €12.0 million, €0.3 million and €0.1 million of its total investment in ESM in 2002, 2003 and 2004.

5. Other Disclosures to the Statements of Operation

Result before income taxes is stated after charging:

(in thousands of €)	2004	2003	2002
Depreciation of property, plant and equipment	11,501	12,545	12,834
Amortization of intangible assets	1,520	2,073	1,975
Personnel costs	21,622	21,197	20,193
Cost of sales: provision for excess inventory	-	-	1,930

6. Income Taxes

Loss before income taxes consists of the following:

(in thousands of €)	2004	2003	2002
Germany	(3,079)	(6,323)	(11,376)
Foreign	(2,600)	(6,283)	(4,858)
	(5,679)	(12,606)	(16,234)

Benefit (provision) for income taxes are as follows:

(in thousands of €)	2004	2003	2002
Current taxes:			
Germany	-	250	43
Foreign	(38)	(91)	1,685
Deferred taxes:			
Germany	-	(8,287)	3,941
Foreign	(26)	314	357
	(64)	(7,814)	6,026

Although Dialog is a UK company, its principal operations are located in Germany and all of its operating subsidiaries are owned by its German subsidiary. Accordingly, the following information is based on German corporate tax law. The Company's statutory tax rate for its German subsidiary is 25%. Including the impact of the solidarity surcharge of 5.5%, the federal corporate tax rate amounts to 26,375%.

A reconciliation of income taxes determined using the German corporate tax rate of 26,375% plus the after federal tax benefit rate for trade taxes of 11,225%, for a combined statutory rate of 37.6%, is as follows:

	2004	2003	2002
Expected benefit for income taxes	2,135	4,740	6,104
Foreign tax rate differential	(200)	(505)	(387)
Amortization of non-deductible intangible assets	(41)	(41)	(41)
Valuation allowance on deferred tax assets	(1,947)	(11,804)	(118)
Others	(11)	(204)	468
Actual benefit (expense) for income taxes	(64)	(7,814)	6,026

Deferred income tax assets and liabilities are summarized as follows:

	Dec 31, 2004	Dec 31, 2003
Property, plant and equipment	374	196
Net operating loss and tax credit carryforwards	25,158	24,284
Liabilities	5,654	5,640
Other	12	41
	31,198	30,161
Valuation allowance	(14,046)	(12,329)
Deferred tax assets	17,152	17,832
Property, plant and equipment	(1,020)	(1,669)
Receivables	(7)	(4)
Deferred tax liabilities	(1,027)	(1,673)
Net deferred tax assets	16,125	16,159

Tax loss carryforwards and established valuation allowances are summarized as follows:

	December 31, 2004			December 31, 2003		
	Tax loss carryforward	Tax loss carryforwards subject to valuation allowance	Valuation allowance	Tax loss carryforward	Tax loss carryforwards subject to valuation allowance	Valuation allowance
Germany	63,124	28,648	11,392	61,696	27,220	10,235
UK	6,384	6,286	2,026	4,391	4,293	1,288
US						
Federal	1,571	1,571	498	1,520	1,520	493
State	1,442	1,442	131	1,514	1,514	131
Sweden	-	-	-	543	543	182
Total			14,046			12,329

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods, in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. In December 2003, the German government enacted new tax legislation, which among other things, limits the use of German tax-loss carryforwards to 60% of the taxable income for fiscal years starting from 2004 and thereafter. As a result of this change in tax law, at December 31, 2003 the Company has re-evaluated its deferred tax asset position and the need for a valuation allowance for the German tax losses. The assessment requires the exercise of judgment on the part of management, with respect to, among other things, benefits that could be realized from available tax strategies and future taxable income, as well as other positive and negative factors. The assessment in 2003 considered the weight given to cumulative losses incurred in Germany over the three-year period ended December 31, 2003, as well as detailed forecasts

of taxable income in the foreseeable future. Although the Company forecasted generating future taxable income to approximate available tax-loss carryforwards, the change in tax law increased the forecasted number of additional years that future taxable income must be generated in order to fully realize these loss carryforward benefits. Pursuant to SFAS 109 and the inherent uncertainties in projecting future taxable income, management had concluded that it is more likely than not that a portion of our tax losses could not ultimately be realized. Consequently, in 2003 the Company recognized a valuation allowance of €10,235, to reduce the carrying value of its net deferred tax assets on tax loss carryforwards in Germany to an amount that was more likely than not expected to be ultimately realized. Furthermore, based on management's assessment, at December 31, 2003 the company established valuation allowances of €1,288, €624 and €182 on tax losses in the UK, the US and Sweden, respectively, since it was more likely than not, that the deferred tax assets will not be realized through future taxable earnings.

Due to losses incurred in 2004, the company has not recognized any additional deferred tax assets and established an additional valuation allowance of €1,947 on the tax-loss

carryforwards generated mainly in Germany in 2004. However, management has evaluated whether it is more likely than not that the Company can recover the carrying amount of deferred tax assets and determined that an additional valuation allowance with respect to the deferred tax assets is not required at December 31, 2004.

The tax loss carryforwards in the US are expiring in 2005 through 2017, the other tax loss carryforwards have no expiration date.

7. Additional Cash Flow Information

The following represents supplemental information with respect to cash flows:

(in thousands of €)	2004	2003	2002
Interest paid, net	5	14	9
Income taxes paid, net	49	372	911

8. Trade Accounts Receivable, net

The recorded trade accounts receivable for which an impairment has been recognized and the related allowance for doubtful accounts at December 31, 2004 and 2003 were €34 and €17, and €270 and €197, respectively.

The allowance for doubtful accounts developed as follows:

(in thousands of €)	2004	2003	2002
Allowance for doubtful accounts at beginning of year	197	397	439
Additions charged to bad debt expense	16	230	222
Write-offs charged against the allowance	(186)	(210)	(139)
Reductions charged to bad debt expense	(10)	(220)	(125)
Allowance for doubtful accounts at end of year	17	197	397

9. Inventories

Inventories are comprised of the following:

(in thousands of €)	2004	2003
Raw materials	9,893	2,738
Work-in-process	13,906	5,026
Finished goods	5,995	5,478
	29,794	13,242

10. Marketable Securities

The Company has invested in "investment grade" rated debt securities with a maturity up to six months, and exchange traded funds, which invest in debt-securities. All marketable

securities are classified as available for sale. The aggregate costs, fair values and unrealized losses per security class are as follows:

(in thousands of €)	Dec 31, 2004			Dec 31, 2003		
	Cost	Fair value	Unrealized loss	Cost	Fair value	Unrealized loss
Corporate debt securities	-	-	-	43,029	42,947	(82)
Debt based funds	17,581	17,542	(39)	1,969	1,953	(16)
	17,581	17,542	(39)	44,998	44,900	(98)

11. Deposits and Prepaid Expenses

At December 31, 2002, the Company maintained deposits of \$20 million with Chartered Semiconductor Manufacturing Pte., Ltd. ("Chartered"). These deposits were refunded to the Company in October 2003. In addition, the Company paid Chartered a total of \$10 million in 2000 as an advance payment for future wafer deliveries and \$2.5 million to another supplier. Such advance payments are classified in the balance sheet line items "Prepaid expenses". In 2004 all remaining advance payments paid to Chartered were refunded to the company. The outstanding balance of the advance payments

is refunded in proportion to the Company's purchases of wafers from the other supplier, and at this time, the Company expects to have the entire advance payments refunded. The amount of advance payments classified in prepaid expenses on the consolidated balance sheet as current assets represents that amount of advance payments expected to be refunded in the next twelve months.

12. Property, Plant and Equipment, net

A summary of activity for property, plant and equipment for the year ended December 31, 2004 is as follows:

(in thousands of €)	Cost						Accumulated depreciation	Net book value as of Dec 31, 2004	Accumulated depreciation	Net book value as of Dec 31, 2003	Depreciation
	Jan 1, 2004	Currency change	Additions	Reclassifications	Disposals	Dec 31, 2004					
Test equipment	53.050	(2)	8.028	300	(863)	60.513	(45.227)	15.286	(36.956)	16.094	(9.076)
Leasehold improvements	903	(19)	158	-	(145)	897	(596)	301	(550)	353	(121)
Office and other equipment	14.303	(112)	2.412	(33)	(860)	15.710	(11.782)	3.928	(10.427)	3.876	(2.304)
Advance payment relating to test equipment	267	-	1.723	(267)	-	1.723	-	1.723	-	267	-
Property, plant and equipment	68.523	(133)	12.321	-	(1.868)	78.843	(57.605)	21.238	(47.933)	20.590	(11.501)

13. Intangible Assets and Goodwill

A summary of activity for intangible assets and Goodwill for the year ended December 31, 2004 is as follows:

(in thousands of €)	Cost						Accumulated depreciation	Net book value as of Dec 31, 2004	Accumulated depreciation	Net book value as of Dec 31, 2003	Depreciation
	Jan 1, 2004	Currency change	Additions	Reclassifications	Disposals	Dec 31, 2004					
Software, licenses and other	10.930	(26)	348	-	(199)	11.053	(8.952)	2.101	(7.992)	2.938	(1.183)
Patents	3.008	-	-	-	-	3.008	(843)	2.165	(506)	2.502	(337)
Intangible assets	13.938	(26)	348	-	(199)	14.061	(9.795)	4.266	(8.498)	5.440	(1.520)
Goodwill	15.736	-	-	-	-	15.736	(3.950)	11.786	(3.950)	11.786	-

During the year ended December 31, 2004 and 2003, the Company acquired software and licenses for a total purchase price of €348 and €618 respectively. The expected weighted average useful life of these assets is 3 years. During the year 2002, the Company acquired the CMOS imaging technology and associated CMOS Active Pixel Sensor (APS) patent portfolio from Sarnoff Corporation, a research and development

institute, for a total purchase price of €3,008. The expected weighted average useful life of these patents is 9 years. In addition, Sarnoff may be paid additional contingent consideration which will be determined as a percentage of the revenues received from sales of imagers used for camera applications and as an agreed sum for each imager used for cellular phone applications. Such contingent consideration is

limited in absolute terms and has a fixed expiration date as specified in the purchase agreement.

The aggregate amortization expense for the years ended December 31, 2004, 2003 and 2002 was €1,520, €2,073 and

€1,975, respectively. Amortization expense of the gross carrying amount of intangible assets at December 31, 2004 is estimated to be €1,015 in 2005, €631 in 2006, €542 in 2007, €518 in 2008 and €483 in 2009.

14. Accrued Expenses

The Company issues various types of contractual product warranties under which it guarantees the performance of products delivered for a certain period or term. The changes in the provision for those product warranties are summarized as follows:

(in thousands of €)	2004	2003
Balance at beginning of year	135	115
Utilizations	(8)	(115)
Additions	28	135
Balance at end of year	155	135

15. Shareholders' Equity and Comprehensive Income

At December 31, 2003, Dialog had authorized 104,311,860 ordinary shares with a par value of €0.10 per share, of which 44,068,930 were issued and outstanding. All shares are fully paid.

On September 24, 2004, the Company completed an offering of 2,000,000 previously unissued ordinary shares at €0.10 per share to its employee benefit trust, to make such shares available for the exercise of stock option rights that had

previously been granted to employees. These shares are legally issued and outstanding, but are not considered issued and outstanding for accounting purposes and accordingly have been reported in the caption "employee stock purchase plan shares" as a reduction of shareholders' equity.

The related tax effects allocated to each component of other comprehensive income (loss) for the years ended December 31, 2004, 2003 and 2002 are as follows:

(in thousands of €)	2004			2003			2002		
	Pretax	Tax effect	Net	Pretax	Tax effect	Net	Pretax	Tax effect	Net
Unrealized (losses) gains on available for sale securities	59	(26)	33	(98)	37	(61)	-	-	-
Unrealized (losses) gains on derivative financial instruments	-	-	-	253	(95)	158	(185)	69	(116)
Currency translation adjustment	12	(17)	(5)	(508)	142	(366)	(437)	150	(287)
Other Comprehensive Income (loss)	71	(43)	28	(353)	84	(269)	(622)	219	(403)

In 2003, realized losses of €44 (net of €27 tax benefits) on the settlement of a derivative financial instrument were reclassified into net loss (see Note 19)

16. Pension Scheme

The group operates defined contribution pension schemes. The pension cost charge for the year represents contributions payable by the group to the funds and amounted to €484

(2003: €565; 2002: €640). At December 31, 2004, contributions amounting to €59 (2003: €5) were payable to the funds and are included in creditors.

17. Stock-based Compensation

a) Stock option plan

On August 7, 1998, the Company adopted a stock option plan ("Plan") under which employees and directors may be granted from time-to-time, at the discretion of the Board, stock options to acquire up to 3,840,990 shares of the Company's authorized but unissued ordinary shares. On May 16, 2002 the shareholders of the Company approved a resolution increasing the maximum amount of stock options which may be granted by the company to 15%, after issue, of the Company's issued share capital. At December 31, 2004, 15%, after issue, of the Company's issued share capital amounted to 8,129,811 shares. Stock options are granted with an exercise price not less than the quoted price at the date of grant. Stock options have terms of ten years and vest over periods of one to five years from the date of grant.

The fair value of all grants in the three-year period ended December 31, 2004 is estimated using the Black-Scholes

option pricing model. Expectations of early exercise are accounted for within the average life of the options. The following weighted-average assumptions were used for stock option grants for the years ended December 31, 2004, 2003 and 2002.

	2004	2003	2002
Expected dividend yield	0%	0%	0%
Expected volatility	80%	74%	106%
Risk free interest rate	3.4%	3.4%	3.7%
Expected life (in years)	5.0	3.8	5.0
Weighted average share price	3.70	3.37	2.33
Weighted average exercise price	3.70	3.37	2.33
Weighted-average fair value of options granted (in €)	2.44	2.21	1.83

Stock option plan activity for the years ended December 31, 2004, 2003 and 2002 was as follows:

(prices in €)	2004		2003		2002	
	Options	Weighted average exercise price	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding at beginning of year	3,412,270	2.32	2,634,382	3.62	2,672,506	3.78
Granted	108,960	3.70	2,050,180	3.37	124,060	2.33
Exercised	(64,648)	0.44	(76,828)	0.52	(79,174)	0.79
Forfeited	(157,176)	3.48	(204,004)	6.21	(83,010)	9.78
Cancelled	-	-	(991,460)	7.29	-	-
Outstanding at end of year	3,299,406	2.34	3,412,270	2.32	2,634,382	3.62
Options exercisable at year end	1,827,076	1.53	1,013,356	0.70	1,217,402	3.07

The weighted average share price at the date of exercise of options was €3.23 in the year ended December 31, 2004.

In April 2003, the Company's board of directors approved a resolution giving employees the right to cancel their options

granted in 2000, 2001 and 2002. Employees elected to cancel a total of 991,460 options with a weighted average exercise of €7.29. In November 2003, approximately 2.0 million options were granted at an exercise price equal to fair value (at that date) of €3.45 per share.

The following table summarizes information about stock options outstanding at December 31, 2004:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding at December 31, 2004	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price	Number Exercisable at December 31, 2004	Weighted-Average Exercise Price
€0.32 - 2.15	1,345,086	5.0	0.70	1,254,622	0.64
€3.00 - 8.00	1,954,320	8.7	3.47	572,454	3.48
€0.32 - 8.00	3,299,406	7.2	2.34	1,827,076	1.53

b) Employee Stock Purchase Plan

On March 26, 1998, in connection with the acquisition of the Company, the Company and its then majority owner, Apax Partners, adopted a Subscription and Shareholders Agreement under which employees and directors were invited at the discretion of the Board, to purchase up to 3,456,890 ordinary shares of the Company from Apax Partners or an established Employee Benefit Trust. The purchase price of the shares was equal to their estimated fair value on the date the employee or director subscribes for those shares. During the first quarter of 1999, the Trust acquired the remaining 668,800 ordinary shares from Apax Partners, which had not been sold to employees or directors, for purposes of distributing them to employees under the Employee Stock Purchase

Plan or for distribution in connection with the exercise of employee stock options.

On September 24, 2004, the Company completed an offering of 2,000,000 previously unissued ordinary shares at €0.10 per share to its employee benefit trust, to make such shares available for the exercise of stock option rights that had previously been granted to employees.

At December 31, 2004, the Trust continued to hold 2,001,559 shares, equaling the remaining balance of the acquired 668,800 shares and the 2,000,000 shares acquired in 2004 (see note 15).

18. Commitments

The Company leases design software, all of its office facilities, office and test equipment, and vehicles under operating leases. Total rentals under operating leases, charged as an expense in the statement of operations, amounted to €7,780, €7,581 and €7,229 for the years ended December 31, 2004, 2003 and 2002, respectively.

Future minimum lease payments under rental and lease agreements, which have initial or remaining terms in excess of one year at December 31, 2004 are as follows:

(in thousands of €)	Operating leases
2005	8,148
2006	6,629
2007	6,399
2008	6,429
2009	3,297
Thereafter	316
Total	31,218

At December 31, 2004, the Company had an unused short-term credit line of €12,500. There are no amounts outstanding under this credit line at December 31, 2004.

19. Financial Instruments and Hedging Activities

a) Use of Derivative Financial Instruments

The Company's sales are primarily denominated in Euros and US dollars whereas purchases of raw materials, manufacturing services and the use of design software are primarily denominated in US dollars, whereas other costs and expenses such as salaries and other overhead costs are denominated in Euro, GBP and US dollars. In order to manage these foreign currency exchange risks, the Company attempts to match

cash inflows and outflows (sales with supply costs) in the same currency, primarily the US dollar. In situations where the Company is not able to effectively match cash inflows and outflows in the same currency, management considers the use of derivative financial instruments. As a matter of policy, the Company does not engage in derivatives trading, derivatives market-making or other speculative activities.

To hedge existing foreign currency exposure related to a \$20 million deposit (see Note 11), the Company purchased foreign currency forward contracts in 2000 to effectively change the US Dollar deposits into Euro (€21,680) upon the expected return of the deposit as of December 31, 2003. These deposits were refunded to the Company in October 2003. Upon receipt of the deposit, the Company settled its currency hedging position related to this deposit and recognized a loss of €71 in the consolidated statement of operations.

In the fourth quarter of 2003, the Company entered into derivative financial arrangements with a bank (the "counterparty") that obligates the Company, if directed to do so by the counterparty, to purchase a total of \$3,611 during the

first half of 2004 at euro-dollar exchange rates ranging from 1.22 to 1.24. These arrangements do not qualify for hedge accounting treatment. Accordingly, the fair value of these derivative financial instruments, which are based on a Black-Scholes pricing model, are recognized on the balance sheet and the changes in fair value are recognized in earnings. At December 31, 2003, these transactions resulted in a net unrealized loss of €78 recognized in earnings.

b) Fair value of financial instruments

The fair value of a financial instrument is the price at which one party would assume the rights and /or duties of another party.

The carrying amounts and fair values of the Group's financial instruments are as follows:

(in thousands of €)	Dec 31, 2004		Dec 31, 2003	
	Carrying amount	Fair Value	Carrying amount	Fair Value
Financial instruments (other than derivative instruments)				
Cash and cash equivalents	13,977	13,977	8,109	8,109
Marketable securities	17,542	17,542	44,900	44,900
Deposits	194	194	183	183
Derivative instruments (currency contracts)				
Current liabilities	-	-	78	78

20. Segment Reporting

The Company has one operating segment, which is the design and supply of semiconductor chips. The Company delivers its products to various market sectors and generates a substantial portion of its revenue from the wireless communications market; 78%, 75% and 71% of total revenues in the years ended December 31, 2004, 2003 and 2002, respectively.

Revenues by market sector consisted of the following:

	2004	2003	2002
Wireless communication	90,617	69,849	54,715
Automotive	11,898	7,896	6,074
Industrial	13,529	15,148	16,315
	116,044	92,893	77,104

Revenues are allocated to countries based on the location of the shipment destination:

	2004	2003	2002
Germany	47,719	45,395	31,478
France	1,936	4,532	9,348
Other European countries	14,931	10,438	11,698
China	19,738	18,198	13,006
Other Asian countries	22,351	6,695	5,154
Other countries	9,369	7,635	6,420
	116,044	92,893	77,104

Following are the net carrying values of investments in property, plant and equipment by geographic location:

	Dec 31, 2004	Dec 31, 2003
Property, plant and equipment		
Germany	20,675	19,634
Japan	92	176
United Kingdom	189	358
USA	282	422
	21,238	20,590

21. Transactions with Related Parties

Timothy Anderson, a member of the Company's Board of Directors, is also a partner in the law firm Reynolds Porter Chamberlain, which frequently acts as the Company's legal adviser. Fees to Reynolds Porter Chamberlain for legal ser-

vices rendered were €212, €162 and €268 in 2004, 2003 and 2002, respectively.

Corporate Governance

Report of the Board of Directors

As reported in this document, 2004 was a year of consolidation and preparation for new opportunities from a broadening product and technology portfolio. Collaboration with partners and customers ensured that we made progress in the development of products for a more diverse customer base.

During the year the Board oversaw the functioning of executive management of the Company at the quarterly Board Meetings of February 4, April 21, July 13, October 13, 2004 and assured itself of the proper conduct of executive management during that year. At such Board Meetings the Board received and analyzed reports from the chief executive as to the achievements of the Company as compared to budget and progress made in achieving the commercial goals for the year.

The Compensation Committee, comprising Jan Tufvesson, Michael Glover and Greg Reyes met in October 2004 to discuss the achievements of the Management during that year and to establish the individual objectives of the Management for 2005. The Audit Committee, comprising of Jan Tufvesson, Michael Glover and since October 1st 2004 Aidan Hughes, met on a quarterly basis. These meetings concentrated on a review of the financial information to be reported on for the relevant prior financial period and on the internationally accepted standards for fair and responsible financial reporting and corporate governance.

The Company's audited financial statements, for the year ended December 31, 2003, and the reports from the Directors and Auditors thereon were presented to, and approved by, the shareholders at the annual general meeting of the Company, held on May 12, 2004, at which KPMG, the Company's independent auditor was reappointed until the following annual general meeting of the Company.

The Board extends its thanks and appreciation to the Executive Management and all employees for their hard work and considerable achievements in 2004.

Accounting under International Financial Reporting Standards (IFRSs)

In compliance with the European Parliament and Council Regulation on the application of International Financial Reporting Standards (IFRSs) adopted in July 2002, all listed European Union companies, including banks and insurance companies, are required to prepare their consolidated financial statements in accordance with IFRS for fiscal years commencing on or after January 1, 2005.

IFRS 1, First-Time Adoption of International Financial Reporting Standards, requires disclosures that explain how the transition from previous GAAP to IFRSs affected the entity's reported financial position, financial performance and cash flows and to comply with each IFRS effective at the reporting date for its first IFRS financial statements. An entity shall prepare an opening IFRS balance sheet at the date of transition and present at least one year of comparative information under IFRSs. Accordingly our date of transition to IFRSs is the beginning of business on 1 January 2004 (opening IFRS balance sheet date). As a UK company, Dialog has to use its UK GAAP financial statements (previous GAAP) which are filed at Companies House for purposes of conversion from previous GAAP to IFRSs. We expect to prepare and publish IFRS financial statements in the first quarter 2005.

Convergence of IFRSs and U.S. GAAP

Dialog strongly supports further alignments between IFRSs and U.S. GAAP to increase international comparability and transparency in financial reporting. In preparation for our adoption of IFRSs, we closely track developments and activities at both standard setting bodies, the IASB and the U.S. Financial Accounting Standards Board—FASB, and expressly welcome the joint initiatives that have already and will further significantly increase the speed and extent of convergence of IFRSs and U.S. GAAP. Following a formal commitment to the common goal of convergence in September 2002, both Boards have added a joint short-term convergence project to their agendas, which is aimed at removing a number of individual differences in the short-term. That is in consideration of the 2005 IFRSs adoption date in Europe, usually by selecting current practice either under existing IFRSs or U.S. GAAP. A long-term objective for the IASB and the FASB is to work together to reduce or eliminate remaining differences on an ongoing basis, through a series of joint projects and through coordination of future work programs. In addition, the Boards have agreed to work together through

their respective interpretive bodies in converging interpretation and application issues.

Dialog expects the adoption of IFRSs to have the following impact on its Consolidated Financial Statements:

Research and development costs

U.S. GAAP generally requires R&D costs to be expensed as incurred. Separate rules apply to software development costs, which may qualify for capitalization under certain circumstances. Under IFRSs, a distinction is to be made between research and development. All costs identified as research costs are to be expensed as incurred, whereas development costs are to be capitalized and amortized if specified criteria are met.

Accounting for Goodwill

Goodwill represents the excess of purchase price over fair value of net assets of businesses acquired. Under U.S. GAAP, beginning January 1, 2002, goodwill is no longer amortized, but instead tested for impairment. In accordance with IFRS 1, we expect not to apply IFRS 3, Business Combinations, retrospectively to past business combinations. Therefore the carrying amount of goodwill in the opening IFRS balance sheet shall be the carrying amount under previous GAAP at the date of transition to IFRSs. We previously have amortized goodwill over a five year period resulting in a zero balance as of December 31, 2003 in our UK GAAP financial statements. Accordingly, goodwill is no longer recorded as an asset in our IFRS financial statements.

Corporate Governance Principles

High corporate governance standards

Dialog Semiconductor Plc is committed to comply with German, US and internationally accepted standards for fair and responsible corporate governance. Accordingly, Dialog Semiconductor (as a foreign Company listed on the German stock exchange) has established and published its own Corporate

Governance Principles corresponding in substance to the provision of the "German Declaration on Corporate Governance". Also, in accordance with the Sarbanes-Oxley Act of 2002, Dialog has adopted a Code of Business Conduct and Ethics and maintains an Audit Committee. Furthermore, as Dialog is listed on NASDAQ, the Code of Business Conduct and Ethics complies with NASDAQ's corporate governance rules. Dialog has adopted and will follow these principles and codes in order to further enhance the confidence of shareholders, customers, employees and the general public in the Company.

Full details of the Corporate Governance Principles and the Code of Business Conduct and Ethics are published on Dialog Semiconductor's internet site (www.dialog-semiconductor.com). In summary the Corporate Governance Principles cover the following key areas

Shareholders rights and the Annual General Meeting (AGM)

Each share carries one vote, and there are no multiple voting rights or preferential voting rights (golden shares). All financial and independent audit reports are presented to the AGM. The AGM is where the directors will obtain authorization to approve and pass resolutions related to Company business, such as auditor's remuneration, and issue of new shares. The Company will also facilitate the personal exercising of shareholders' voting rights. The company shall publish key information relating to the AGM on its web site on the day of the annual meeting.

Board of Directors' responsibilities, composition and compensation

Dialog has seven non-executive directors and one executive director on the Board, to supervise the general management and develop the Company's strategy. The non-executive directors do not play an active role in day-to-day operations providing an independence and objectivity in the making of key decisions. During 2004, directors received the remuneration listed below and their shareholdings in Dialog Semiconductor are as follows.

Name	Position	Compensation (in €)		Directors Holdings	
		Base salary	Bonus / Long-term incentives	Shares	Options
Roland Pudelko	Executive Director, CEO and President	279.105	33.334	320.405	517.450
Tim Anderson ¹⁾	Non-executive Director	7.366	-	75.166	-
Michael Glover	Non-executive Chairman of the Audit Committee	51.565	-	195.000	-
Aidan Hughes	Non-executive Director (since October 1, 2004)	11.050	-	-	-
John McMonigall	Non-executive Director	29.466	-	-	-
Gregorio Reyes	Non-executive Director	44.198	-	35.000	-
Michael Risman	Non-executive Director	29.466	-	1.172	-
Jan Tufvesson	Non-executive Chairman	51.565	-	175.062	-
		503.781	33.334	801.805	517.450

1) Tim Anderson is also a partner in the law firm Reynolds Porter Chamberlain, which frequently acts as our legal adviser. Fees to Reynolds Porter Chamberlain for legal services rendered during the 2004 fiscal year amounted to €212.

Variable compensation of the Chief Executive Officer is measured based on the profitability of the Company as well as success in reaching specific strategic goals.

Audit Committee and Compensation Committee

Dialog has established an Audit Committee of the Board of Directors consisting of independent directors: Messrs. Glover (chairman of the Audit Committee), Tufvesson and Hughes. To maintain independence, members of the Committee are not to receive payment from the Company for consulting, advisory, or other services other than for board service and are not to be affiliated with the Company. The Compensation Committee determines the salaries and incentive compensation of Dialog's officers and the officers of the Company's subsidiaries and provides recommendations for the salaries and incentive compensation of other employees and consultants. Our Compensation Committee consists of Messrs. Tufvesson (chairman of the Compensation Committee), Glover and Reyes. None of the members of this Committee should serve as an employee of the Company.

Transparency, including director's dealing, insider dealing and loans

Dialog promptly discloses price sensitive information to the stock exchanges and then publishes the information electronically. Significant shareholder interests should be reported to the Company according to the UK Companies Act 1985. Transactions in securities of the Company's own shares carried out by members of the Board of Directors and of their family members will be reported and published without delay pursuant to section 15a of the German Securities Trading Act (Wertpapierhandelsgesetz). With regard to insider dealing Dialog has adopted a Code of Dealing, in which we comply with stringent guidelines to ensure against suspicion of abusing the possession of price sensitive information, by prohibiting dealing in any of the company's financial instruments during defined periods. In addition, the Company will not provide or guarantee any loans to directors or senior executives.

Business conduct and ethics

The Company shall comply with all governmental laws, rules and regulations that are applicable to the Company's activities, and expects that all directors, officers and employees acting on behalf of the Company will obey the law. Directors, officers and employees should not be involved in any activity, which creates or gives the appearance of a conflict of interest between their personal interests and the Company's interests. The Company is committed to promoting the values of honesty, integrity and fairness in the conduct of its business and sustaining a work environment that fosters mutual respect, openness and individual integrity. Directors, officers and employees are expected to deal honestly and fairly with the Company's customers, suppliers, competitors and other third parties.

Auditor's independence

The aggregate fees billed for each of the last two fiscal years for professional services rendered by the principal accountant for the audit of annual financial statements or services by the principal accountant, KPMG, were as follows:

(in thousands of €)	2004	2003
Audit fees	174	169
Tax fees	110	65
	284	234

Tax services rendered in 2004 were pre-approved by the audit committee in accordance with § 401(i) of the Sarbanes – Oxley Act of 2002.

Our Auditor, KPMG, confirmed their independence at each quarterly audit committee meeting and declared the following:

“We hereby confirm, that as of February 21, 2005, we are independent accountants with respect to the Company within in the meaning of the Securities Acts administered by the Securities and Exchange Commission of the United States and the requirements of the Independence Standards Board, Auditing Standard No. 2 of the Public Company Accounting Oversight Board (United States), German law, the German Corporate Governance Code and professional standards in Germany and the United States. In particular

- We verified that no professional relationships to the Company exist that may reasonably be thought to bear on our independence. This relates especially to board membership and employee relationships with the Company.
- We verified that no financial relationships exist that may reasonably be thought to bear on our independence. This relates especially to direct investments such as stocks, bonds and similar investments. We are also independent in respect to the requirements of § 319 paragraph 2 no. 8 HGB (unamended version). For each of the last five years our annual revenues generated from services to the Company and other entities for, which the Company holds more than 20% ownership amounted to less than 30% in fact, less than 1% of our total revenues. This is also expected to be the case for the current fiscal year (§ 319 paragraph 3 no. 5 HGB (amended version)).
- We will also ensure that anything, which may reasonably be thought to bear on our independence with regard to the self review threat will be avoided. In particular, apart from the audit we have not taken part in the maintenance of any books or records or the preparation of financial statements and will not do so in future.
- We will comply with the requirements regarding internal rotation (§ 319 paragraph 3 no. 6 HGB).
- We are not aware of any other relationships or matters, which may reasonably be thought to bear on our independence such as close family or personal relationships with the board members or management of the Company.

Our internal organization complies with the requirements of the “Gemeinsamen Stellungnahme der Wirtschaftsprüferkammer und des Instituts der Wirtschaftsprüfer in Deutschland: Zur Qualitätssicherung in der Wirtschaftsprüferpraxis“ (VO 1/1995). Our partners are prohibited to have any financial investment in a KPMG audit client. All other professional staff is prohibited to have any financial investment in an audit client he or she delivers services to. The affected persons have to declare that they comply with these regulations on a regular basis.”

Declaration of conformity with regard to the German corporate governance code

“Dialog Semiconductor Plc has established and published its own corporate governance principles corresponding in substance to the provisions of the German “Declaration on Corporate Governance” as published on November 13, 2002 thereby adopting in substance the recommendations of the Government Commission on the German Corporate Governance Code”.

This declaration is available on the Internet at: www.dialog-semiconductor.com/Investor Relations/Corporate Governance.

London, February 2005

Jan Tufvesson, Chairman

Members of the Board of Directors

Jan Olof Ingemar Tufvesson, Chairman (66)

joined the board of our then-holding company in 1990 and has served as chairman of the board since March 1998. Between 1972 and 1980 he held senior appointments on the Royal Swedish Air Force Board. In 1980 he joined Ericsson where he had a number of executive roles, the last being a vice president at LM Ericsson corporate, responsible for all procurement in Ericsson and for developing relations with key suppliers. Mr. Tufvesson graduated from the Royal University of Technology in Stockholm with a masters degree in electronic engineering in 1962. Mr. Tufvesson retired from Ericsson in 1998 and is now based in Stockholm.

Roland Pudelko, Chief Executive Officer and President (52)

joined us in 1989 as managing director and has served as Executive Director, CEO and President since March 1998. He has over 20 years experience in electronics and microelectronics, primarily in management positions within the Daimler-Benz Group. During that time, he was on the board of a joint venture with ACER of Taiwan, and in the TEMIC Group he was responsible for worldwide design and engineering. Mr. Pudelko has a diploma in communication technologies. He is also the managing director of Dialog Semiconductor GmbH and other consolidated subsidiaries of Dialog Semiconductor Plc.

Timothy Richard Black Anderson (43)

joined the board of our then-holding company in 1990 and has served as a director since February 1998. Mr. Anderson has been a partner with the London law firm Reynolds Porter Chamberlain since 1989, where he specializes in business law for media and technology companies. He holds a law degree from Southampton University and is qualified as a solicitor in England and Wales.

Michael John Glover (66)

joined the board of our then-holding company in 1990 and has served as a director since March 1998. Mr. Glover was a senior executive with technology based companies in the United Kingdom, Europe, the Far East and North America prior to becoming involved in private equity fund management in 1985. He has a degree in economics from the University of Birmingham. Mr. Glover is currently Managing Director of Aylestone Strategic Management Limited and serves as a director of other companies.

Aidan Hughes (44)

joined us as a director in October 2004. He qualified as a chartered accountant with Price Waterhouse in the 1980s before taking senior accountant roles at Lex Service Plc and Carlton Communications Plc. He served the Sage Group Plc as finance director from 1993 until 2000. Between December 2001 and August 2004 Hughes was a director of Communisis Plc.

John McMonigall (61)

has served as one of our directors since March 1998. He joined Apax Partners as a director in 1990 and is currently the director responsible for investments in telecommunications, software and related fields. Between 1986 and 1990, Mr. McMonigall held a variety of senior positions at British Telecom, including managing director of the customer service division. He was also a member of the management board of British Telecom. He is currently on the board of five other public and private companies, including Crane Telecommunications Ltd, Autonomy plc and Amphion Ltd.

Gregorio Reyes (63)

joined us as a director in December 2003, and has been a private investor and management consultant since 1994 with current board positions at companies including LSI Logic Corp., Appshop, Amphion Semiconductor, Astute Networks, Future Trade Technologies, and Nuera Communications. He has held various executive positions with National Semiconductor (1962-1967), Motorola (1967-1968) and Fairchild Semiconductor (1968-1978). He was also president and CEO of National Micronetics (1981-1984), and chairman and CEO of American Semiconductor Equipment Technologies (1986-1990), and of Sunward Technologies (1990-1994).

Michael Risman (36)

joined us as a director in August 1999, having been closely involved with our company since March 1998. He is a director of Apax Partners where he has responsibility for their European IT investment activities and is a member of their International Approval Committee. Before joining Apax Partners in 1995, Mr. Risman worked for Cap Gemini as a consultant and for Jaguar Cars as an R&D engineer. He earned an MBA from Harvard Business School and an MA (Hons) degree in Electrical Engineering and Management from Cambridge University. He is also a director of Frontier Silicon (Holdings) Ltd, Red-M (Communications) Limited and Streamserve Inc.

Investor Information

■ Annual Meeting

The annual meeting of Dialog Semiconductor Plc will be held on May 11, 2005
9 a.m. local time
278/282 High Holborn
London WC1V 7HA
United Kingdom

■ Corporate Calendar

April 20, 2005
Release of first quarter results
May 11, 2005
Annual shareholders' meeting
July 20, 2005
Release of second quarter results
October 19, 2005
Release of third quarter results

■ Corporate Counsel

Reynolds Porter Chamberlain
London, United Kingdom

■ Certified Public Accountants

KPMG Deutsche Treuhand-Gesellschaft
Stuttgart, Germany

■ US Listing

Our Shares are listed on Nasdaq in the form of American Depositary Shares (ADS). Each ADS represents one ordinary share.
Dialog Semiconductor is subject to the regulations of the Securities and Exchange Commission (SEC) in the USA as they apply to foreign companies and files with the SEC its Annual Report on Form 20-F and other information as required.

■ ADS Administrator

ADS holders may instruct The Bank of New York, which administers our ADS program, as to the exercise of voting rights pertaining thereto:
The Bank of New York
101 Barclay Street, 22W
New York, NY 10286
Telephone: +1 (888) 269-2377
Facsimile: +1 (212) 571-3050

■ Please direct inquiries to:

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E-mail: birgit.hummel@diasemi.com

■ www.dialog-semiconductor.com

All our recent press releases are accessible together with the latest Annual and Interim Reports.
Publications of interest to current and potential investors (Form 20-F, Annual and Interim Reports) are available without charge upon request.
Please order within the investor relations section of our homepage.

Technical Glossary

Analog A type of signal in an electronic circuit that takes on a continuous range of values rather than only a few discrete values.

APS Advanced Pixel Sensor technology used in Dialog Semiconductor's CMOS image sensors.

ASIC Application Specific Integrated Circuit; an integrated chip custom designed for a specific application.

ASSP Application Specific Standard Product; a semiconductor device integrated circuit (IC) dedicated to a specific application and sold to more than one user.

Audio CODEC The interface between analog signals (such as the human voice) and the digital data processing inside a mobile phone, determining voice quality.

CAD Computer Aided Design, usually refers to a software tool used for designing electronics hardware or software systems.

CDMA (Code Division Multiple Access) An alternative to GSM technology for mobile wireless networks.

Chips Electronic integrated circuits.

CMOS Complimentary Metal Oxide Semiconductor, the most popular class of semiconductor manufacturing technology.

DC-DC A DC-to-DC converter accepts a direct current input voltage and produces a direct current output voltage. The output is typically at a different voltage level than the input, and often the component provides power bus regulation.

Digital A type of signal used to transmit information that has only discrete levels of some parameter (usually voltage).

Fabless A term describing a company that designs and delivers semiconductors by outsourcing the fabrication (manufacturing) process.

Foundry A manufacturing plant where silicon wafers are produced.

GPS Global Positioning System. A worldwide satellite navigation system used in electronics systems for positional information.

GPRS General Packet Radio Service, a step between GSM and 3G (third generation) mobile networks, offering fast data transmission via the GSM network

GSM Global System for Mobile Communications, the world's most widely used mobile system.

IC Integrated Circuit; an electronic device with numerous components on a single chip.

Imaging The capture and processing of images via an image sensor for use by an electronic device to send to a display for viewing by a user.

Liquid Crystal Display (LCD) A display technology found in many portable electronics products, including personal organizers, cellular handsets and notebook computers.

LDO Low Dropout voltage regulators are used in battery operated systems, where the output voltage

is typically lower than the input voltage.

LED Light Emitting Diode. A semiconductor device that emits light when charged with electricity, often used for LCD display backlights.

Mixed signal Describes a combination of analog and digital signals being generated, controlled or modified on the same chip.

MLA Multi-Line Addressing is a technology used in color LCDs to enable full color, high quality display of moving images with fast response time, high brightness, lower cost and low power consumption.

MP3 (MPEG-1 Audio Layer-3) A standard technology format for compression of sound sequences into very small files, while preserving the original level of sound quality.

Multimedia messaging services (MMS) A standardized messaging service for the mobile environment, delivering user-created content from phone to phone, and containing any combination of graphics, images and audio.

NiMH, L Ion and polymer Various battery technologies.

Personal digital assistant (PDA) A hand-held computer designed for use as a personal organizer with communications capabilities.

Power management The management of the power requirements of various subsystems, important in hand-held and portable electronics equipment.

PMIC Power Management IC.

Semiconductor A base material halfway between a conductor and an insulator, which can be physically altered by mixing in certain atoms. Semiconductors form the basis for present-day electronics.

Silicon A semi-metallic element used to create a wafer, and the most common semiconductor material - in about 95% of all manufactured chips.

Smart Mirror™ A technology patented by Dialog Semiconductor which simplifies circuit design and provides very low current consumption in power management circuits.

STN Super-Twisted Nematic, refers to the direction of rotation of the liquid crystals in an LCD to enable excellent brightness and a wide angle at which the display can be viewed before losing much contrast.

System on chip (SOC) Advanced semiconductor device embedding custom circuits and intellectual property (IP) elements into single chip solutions.

USB Universal Serial Bus. A universal interface standard to connect different electronics devices

VGA Video Graphics Array. A standard size/resolution of 640 pixels by 480 pixels for digital cameras, images, and displays.

Wafer A slice of silicon from a 4, 5, 6 or 8 inch diameter silicon bar and used as the foundation on which to build semiconductor products.

WCDMA Wideband CDMA, a 3G (third generation) wireless standard, also referred to as UMTS.

Financial Glossary

Cash Flow The primary purpose of a statement of cash flows is to provide relevant information about the cash receipts and cash payments of an enterprise during a period. It helps to assess the enterprise's ability to generate positive future net cash flows. A statement of cash flows shall explain the change in cash and cash equivalents during the period by classifying cash receipts and payments according to whether they stem from operating, investing, or financing activities.

Cash flow from operating activities Cash flow from operating activities includes all transactions and other events that are not defined as investing or financing activities in paragraphs. Operating activities generally involve producing and delivering goods and providing services. Cash flows from operating activities are generally the cash effects of transactions and other events that enter into the determination of net income.

Comprehensive Income The purpose of reporting comprehensive income is to report a measure of all changes in equity of an enterprise that result from recognized transactions and other economic events of the period other than transactions with owners such as capital increases or dividends. An example of items effecting comprehensive income is foreign currency translation adjustments resulting from the process of translating an entity's financial statements in a foreign currency into the reporting currency.

Corporate Governance Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.

Deferred taxes Deferred tax assets or liabilities are temporary differences between the tax basis of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible amounts in future years when the reported amount of the asset or liability is recovered or settled, respectively.

Derivative financial instruments A financial instrument that derives its value from the price or expected price of an underlying asset (e.g. a security, currency or bond).

Goodwill Goodwill is to be recorded in a purchase business combination for an excess of the cost of the acquired enterprise over the total amount assigned to the identifiable assets acquired less liabilities assumed.

Gross Margin Gross Margin equals the difference between revenues and cost of sales as presented in the statement of operations.

Hedging A strategy used to minimize exposure to changes in prices, interest rates or exchange rates by means of derivative financial instruments (options, swaps, forward contracts, etc.).

Impairment Impairment is the condition that exists when the carrying amount of a long-lived asset exceeds its fair value (the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset).

IFRS (International Financial Reporting Standards) Accounting standards generally to be used for fiscal years commencing on or after January 1, 2005 by all publicly listed European Union companies in compliance with the European Parliament and Council Regulation adopted in July 2002.

Prime Standard The new segmentation of the equity market of the German Stock Exchange comprises a Prime Standard segment in addition to the General Standard segment that applies the statutory minimum requirements. The Prime Standard segment addresses companies that wish to target international investors. These companies are required to meet high international transparency criteria, over and above those set out by the General Standard.

Restructuring Charges Costs associated with an exit or disposal activity, e.g. termination benefits provided to employees that are involuntarily terminated.

Securities Debt securities are instruments representing a creditor relationship with an enterprise and include government securities, corporate bonds, commercial paper, and all securitized debt instruments. Available-for-sale securities are debt securities not classified as held-to-maturity or trading securities.

Shareholders' equity Shareholders' equity reflects the investment of shareholders in a company. Shareholders' equity is comprised of ordinary shares, additional paid-in capital, retained earnings and accumulated other comprehensive income.

Stock option plans Stock option plans include all agreements by an entity to issue shares of stock or other equity instruments to employees. Stock option plans provide employees the opportunity to receive stock resulting in an additional compensation based on the future share price performance. The purpose of stock option plans is to motivate employees to increase shareholder value on a long-term basis.

Total Assets Total assets include all current and non-current assets. Total assets equal total liabilities and shareholders' equity.

Working Capital Working capital is represented by the excess of current assets over current liabilities and identifies the relatively liquid portion of total enterprise capital that constitutes a margin or buffer for meeting obligations within the ordinary operating cycle of the business



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