Making the difference in power management

Annual report and accounts 2007

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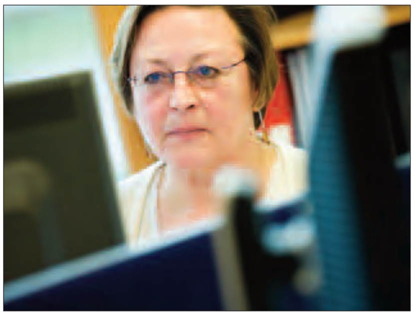
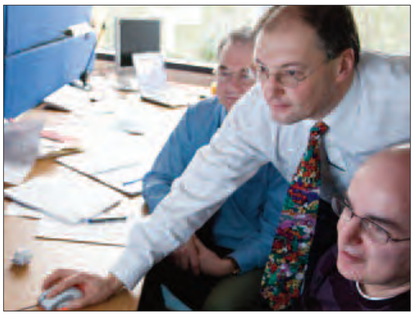






Dialog Semiconductor develops innovative mixed signal and system-level integrated circuit solutions for wireless, automotive and industrial applications. We supply standard and customer-specific products to a wide range of the world's leading original equipment manufacturers.

Our chips and system-level solutions improve the performance and features of wireless, hand-held and portable electronic devices. They facilitate advanced applications – such as multi-media messaging, video, gaming and digital audio players – on mobile phones, while our mixed signal technology enables intelligent solutions – such as comfort, safety and lighting control – to be incorporated into automotive and industrial systems.

Our headquarters are near Stuttgart, Germany; we also have design centres in other parts of Germany and Austria, design and marketing facilities in the UK and Japan, and sales offices in the USA and Greater China.

Dialog at a glance

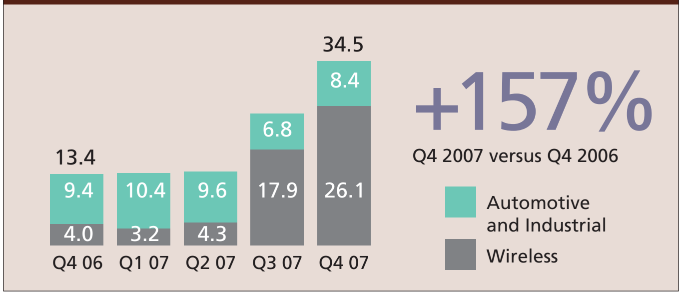
Financial highlights

- Four consecutive quarterly increases in revenue and gross margin
- Full-year 2007 net losses reduced by 53% to US$19.0 million
- In Q4 2007 Dialog generated positive cash flow from operations and returned to quarterly profitability
- More than 70% of Q4 2007 revenues derived from new, higher margin products
- In 2007, Dialog Semiconductor share price outperformed all sector benchmark indices (TecDAX, SOX, Prime Semicon IG)
- Dialog remains debt free

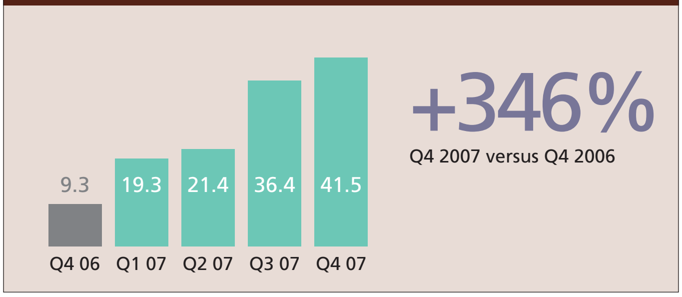
Operational highlights

- New standard products launched
- Edinburgh design centre, focusing on audio and power management products, opened in March
- Growing customer diversification
- Offshore test and support model fully integrated

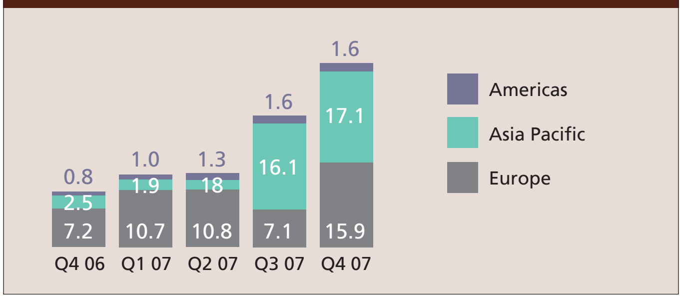
Revenue: Q4 2006 and 2007 (US$m)



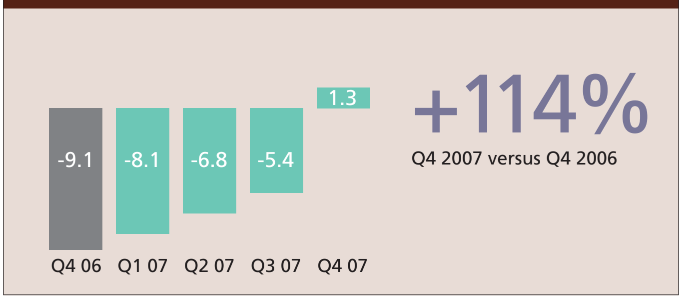
Gross margin: Q4 2006 and 2007 (%)



Geographic revenue: Q4 2006 and 2007 (US$m)



Net loss/profit: Q4 2006 and 2007 (US$m)



"Cell phone technology changes so quickly, how can Dialog stay ahead of the game?"

"Through experience and an understanding of market needs. Our design methodology enables us to incorporate improved performance quickly – and at minimum risk."

Our markets

Dialog has a successful record of delivering qualified and tested chips to the world's leading Original Equipment Manufacturers ("OEMs").

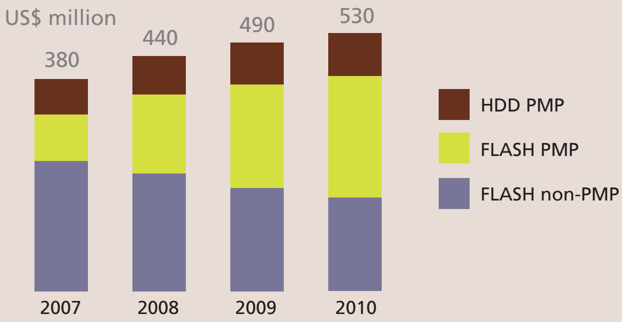
We supply these customers with standard or Application-Specific IC ("ASIC") products through a combination of direct sales and specialist independent sales representatives.

Our power management, audio and display semiconductor solutions are designed to meet the needs of the wireless, automotive and industrial systems markets.

Wireless communications

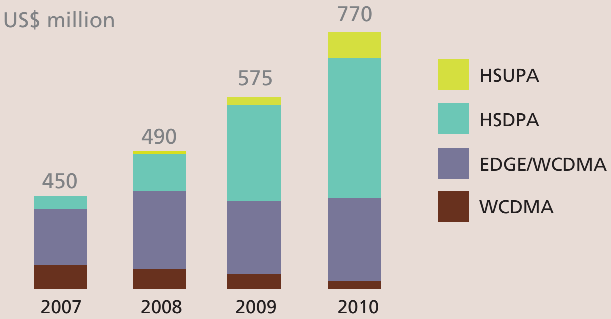
Our knowledge of designing for the wireless communications market is one of our major strengths, and the basis of a significant proportion of our business: more than 500 million mobile phone handsets incorporate our power management and audio processing chip designs. Our expertise in low-power, mixed signal circuit design helps manufacturers to deliver a range of highly integrated chip and system-level solutions for mobile and cellular handsets, and to satisfy the requirements of 2.5G, 3G, GPRS and CDMA wireless systems. Our products employ leading-edge silicon and packaging technologies.
We design, manufacture and test our products to enable complex devices and features to be developed rapidly and at low-risk.

Personal media players – power management and audio CODEC TAM



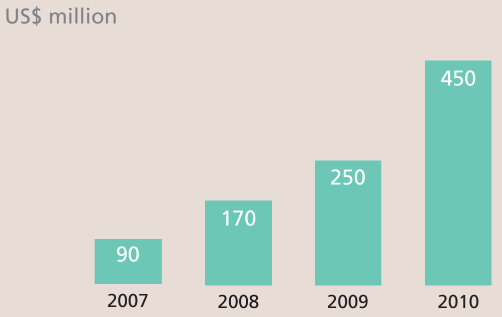
Source: Dialog marketing

3G & High-speed data mobile phones – power management and audio CODEC TAM



Source: Dialog marketing

Mobile terminal – OLED display driver TAM



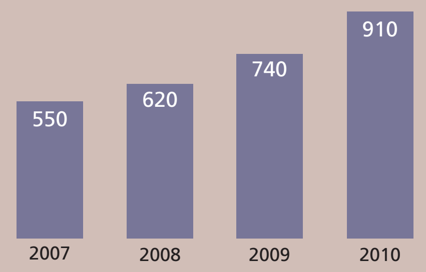
Source: Dialog marketing

Our power management, audio and display semiconductor solutions are designed to meet the needs of the wireless, automotive and industrial systems markets.

We focus our semiconductor solutions for the automotive industry on safety and comfort electronics. Working closely with our customers, we develop Application-Specific Integrated Circuit ("ASIC") or custom chips for systems which support safety and comfort for the car driver and passengers such as windscreen wiper motor controller, seatbelt adjusters and intelligent battery management. We also work in partnership with automotive manufacturers on the development of high-voltage (40V) System-on-Chips ("SoC") which, on the same silicon, include a microcontroller, embedded flash memory, high-voltage devices, and high-performance analog components.

Automotive safety and comfort electronics – integrated motor controllers TAM

US$ million



Source: Dialog marketing

Industrial systems

We offer a range of established mixed signal components for industrial systems, including dimming, control, sensor and power management ASICs for use in lighting systems, and single-chip solutions for intelligent control of fluorescent lamps.

We supply these customers with standard or Application-Specific IC ("ASIC") products through a combination of direct sales and specialist independent sales representatives.

Chairman's statement

Dear Shareholders,
In the 2006 Annual Report, I wrote that 2007 would be a year of further transition for the Company. This has proved to be the case: the management team has made terrific progress in positioning the Company for sustainable growth and, of course, in increasing Shareholder value.

For the Board, the most pleasing aspect has been the steady increase in gross margin throughout 2007, from just under 20% in the first quarter of the year to just over 40% in the fourth quarter. While there is still much to do, the Board is much more confident that the business is on the right course. As a result, it not only thanks the management team for its efforts but, in a drive to maintain the current momentum in the business, is also looking at ways to align the team members' rewards more closely to the interests of Shareholders. A proposal to this effect will be made at the Annual General Meeting (AGM) and will, I hope, receive the support of our Shareholders. More information will be included in the Notice of Meeting, which will be published on our Website in due course.

As we report in the Corporate Governance section of this report, we have created a new Nominations and Remuneration Committee. We formerly dealt with these matters separately, but the Board considered that there were many issues that were common to both, and quality and efficiency of reporting would be improved by bringing the disciplines together. By regularly questioning the composition and processes of the Board and its committees, we ensure they provide apposite guidance and support to the management team, as well as effective Corporate Governance for the Company.

Indeed, in relation to the composition of the Board and its committees, the Non-executive Directors – Peter Tan, Russ Shaw and Chris Burke – who joined Dialog recently have become increasingly active participants in Board meetings, and each also is a member of one of our committees. This is very pleasing to me and is, I know, much appreciated by our Chief Executive Officer, Dr Jalal Bagherli, and his team.

As you will read in Jalal's review that follows, the Board sees 2008 as a year of opportunity for Dialog to demonstrate sustainable growth and attain profitability. His confidence in the Company's ability to achieve this, of course subject to the wider uncertainties in the world economy, is very encouraging.

Greg Reyes
Chairman

The most pleasing aspect has been the steady increase in gross margin throughout 2007, from just under 20% in the first quarter of the year to just over 40% in the fourth quarter.

Dialog Semiconductor shares in 2007

Investment case

Dialog Semiconductor has a strong record in the development and supply of state-of-the-art power management, audio and display driver technology, and has built a worldwide reputation as a supplier of superior products to the wireless and automotive industries. The Company's core competence is its focus on innovative, mixed signal standard products, as well as application-specific IC solutions manufactured entirely in CMOS technology.

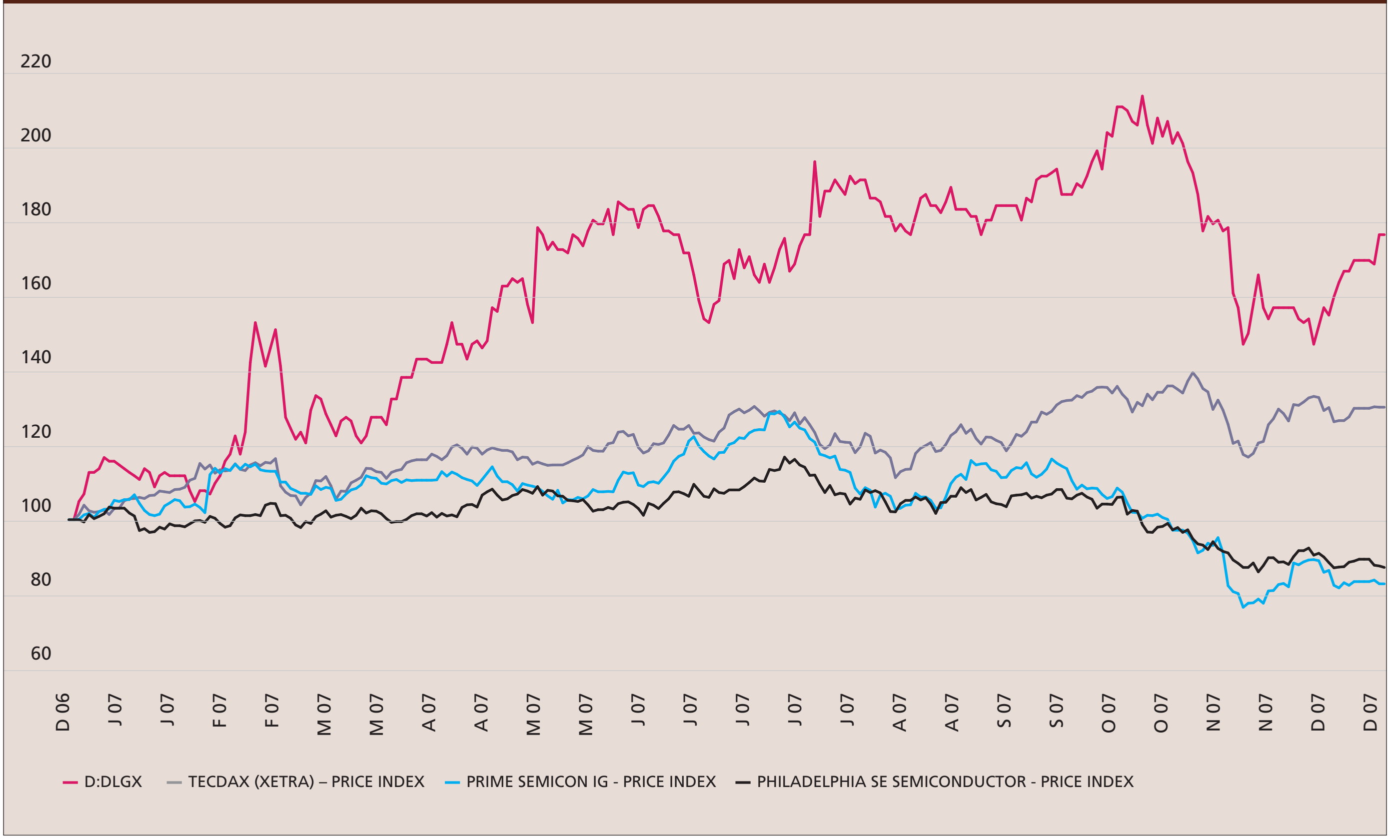
Dialog's products enhance the performance and features of wireless, hand-held and portable electronic devices, in addition to providing the technology used in intelligent control circuits in automotive and industrial applications. This broad spread of applications enables it to derive value from a number of established, and new and exciting high growth, markets.

Dialog Semiconductor's share price development

The following graphs chart the cumulative Shareholder return of the Company for the past three years and for the past 12 months, compared with Germany's TECdax index and Prime Semiconductor index ("SemiC"), and the Philadelphia SE Semiconductor index ("SOX").

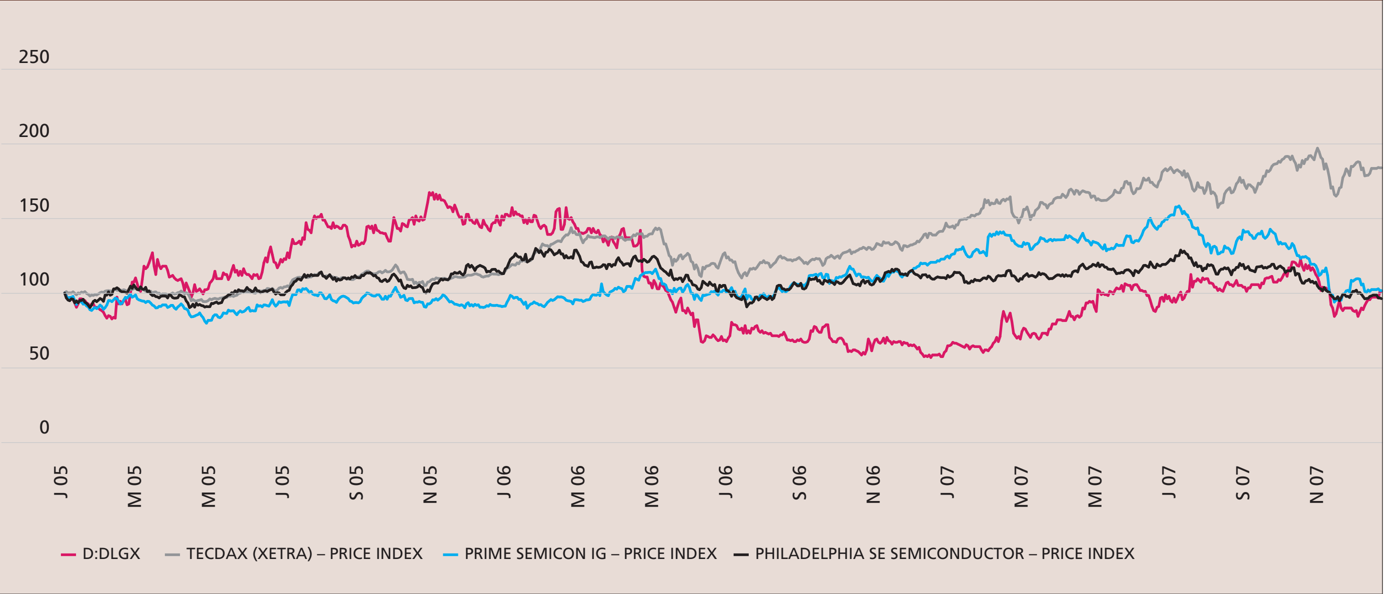
In 2007, Dialog Semiconductor's share price increased by 77%, from €1.02 at the beginning of the year to €1.80 at the end of the year. It outperformed all selected benchmark indices.

2007 12-month Dialog Semiconductor stock analysis



Dialog Semiconductor shares in 2007

2005-2007 Dialog Semiconductor stock analysis



Share fundamentals for the financial year 2007

Total number of shares outstanding and registered as of 31 December 2007	46,068,930
Weighted average number of shares during 2007 (basic and diluted)	44,937,631
Type	Ordinary
Par value (in £)	0.1
Bloomberg Symbol	DLG
Reuters Symbol	DLGS.DE
ISIN	GB0059822006

Key figures for the financial year 2007 based on weighted average number of shares (basic)

Sales per share (from continuing operations in US$)	1.93
Operating loss per share (from continuing operations in US$)	(0.38)
Net loss per share (in US$)	(0.42)
Book value per share as of 31 December 2007 (in US$)	1.19
Accounting standards	IAS/IFRS

Market data 2007

Exchange segment Germany	Midcap, Prime All Share, Prime Technology, Technology All Share
Designated sponsor	West LB
Market capitalisation as of 31 December 2007 (in millions of €)	82.9
Turnover of shares during 2007	89,583 shares/day

Trading in Dialog shares

Dialog shares are traded in Germany on the XETRA and Frankfurt regulated official markets and on all other German regional exchanges on the open market.

The Company has made a strategic commitment to creating a lower-cost platform in order to take full advantage of key growth opportunities. In line with this commitment, the decision was taken in the fourth quarter of 2006 to terminate the Company's American Depositary Receipt programme ("ADRs") and de-list from the Nasdaq National Market in the USA. ADRs in Dialog Semiconductor were de-listed from Nasdaq at the close of business on 28 December 2006. In accordance with SEC regulations governing deregistration from a US exchange, the Company filed notice of its intention to deregister with the SEC (Form 15) on 31 January 2007. The deregistration became effective 90 days later. In June 2007, new SEC rules on deregistration gave the Company the opportunity to terminate its SEC registration permanently by filing Form 15F with the SEC. The original Form 15 filing only granted the Company the right to suspend its SEC reporting obligation temporarily for any years in which it had fewer than 300 US Shareholders. In July 2007, Dialog filed a Form 15F making the deregistration permanent.

Dividend policy

Dialog Semiconductor participates in industries that are considered to be global growth engines and provides its services and products to the major players in these industries.

Dialog's Board of Directors is committed to re-investing all profits into laying the framework for future growth and continues to believe that – in line with the strategic changes underway – this policy is in the best interests of all its Shareholders.

Investor relations

Dialog Semiconductor understands the importance of clear communication with investors and analysts, particularly during a period of strategic change. During 2007, the management team continued its efforts to ensure that the market was kept up to date with the important and exciting changes underway at the Company.

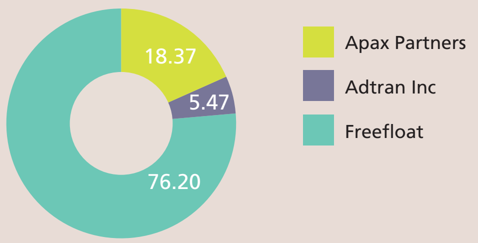
Dialog Semiconductor's shares are followed by a number of analysts representing major banks and research institutions in Europe. During 2007, we held our annual analyst conference and, in addition, kept in regular contact with our investors and analysts.

All information provided, including presentations, press releases and reports of the Company, as well as the recommendations of analysts covering the Company, can be downloaded from the corporate Website: www.dialog-semiconductor.com.

Shareholder structure

Information about the main Shareholders of the Company is shown in the following graph.

Dialog main Shareholders



Freefloat

Freefloat includes 4,621,593 shares (10.0%) held by the Capital Group International, Inc. as notified on 14 December 2007 on behalf of discretionary clients, 2,227,700 shares (4.8%) held by Pictet Asset Management Ltd as notified on 4 October 2007 on behalf of discretionary clients, 2,148,204 shares (4.7%) held by Union Investment Privatfonds GmbH as notified on 7 February 2008 on behalf of discretionary clients and 1,046,387 shares (2.3%) held by the Dialog Semiconductor Plc Benefit Trust.

Disclosure of interests

The provisions of the UK Companies Act 2006 require that any person acquiring a direct interest of 3% or more of a class of shares issued by the Company – with voting rights at the Company's general meeting – must inform the Company of its interest within two working days. If the 3% interest is exceeded, the Shareholder must inform the Company of any increase or decrease of one percentage point in its interest.

Business review



The strategic decisions we made in 2006 enabled us to begin 2007 with low inventory, no debt and more cash than we had at the beginning of the previous year.

In 2006's Annual Report, we set out a number of objectives designed to enable us to build, and improve, on that position during 2007. Since the creation of sustainable shareholder value lies at the heart of our strategy, profitable growth continues to be our principal objective.

We stated that we would continue our efforts to fine-tune our strategy and to develop the Company to ensure that we achieve our objectives. Our financial KPIs are set out on page 2, our operational KPIs are set out on this page.

Strategy: to improve our cost platform

Progress: **Transition of final-test operations** to sub-contractors in Asia completed
Financial reporting process simplified by delisting from Nasdaq

Strategy: to diversify our revenue

Progress: **New market area developed** through production of highly-integrated power management devices for a leading consumer electronics company
Began shipping highly-integrated audio and power management devices for 3G/HPSDA mobile and smart phones

Strategy: to focus our products and sales on higher-growth markets

Progress: **R&D focused on a broad base of products**
invested in low-power audio technology by setting up a new design centre in Scotland
Developed new products for automotive and industrial markets, ready to launch in 2008
Applied SoC technology for smart motor controllers to new end-applications

Strategy: to strengthen our management and skill base

Progress: **Brought new Non-executive Directors on to the Board**
Continued to recruit highly-qualified employees for marketing, manufacturing and R&D

"Why are the big MP3 companies interested in working with Dialog? Aren't we pretty small fry?"

"Well, we're good at what we do! Our circuits work, they're cost-effective, we really understand power management and our engineers love technical challenges."

"Great! But doesn't everyone say that?"

"Sure, but we deliver. We develop products quickly, they work and we can produce high volumes without missing a beat. So, we've got a loyal A-list customer base – and you can't argue with that."

"You certainly can't!"

Chief Executive's review

During 2007, Dialog's board and executive team worked diligently to position the Company for future profitable growth. While there is still room for improvement, I am pleased to report that we have made significant progress.

In last year's Annual Report, I indicated my belief in Dialog's potential and ability to pursue a number of higher-growth opportunities in the mobile phone, consumer electronics and automotive systems markets. During 2007 we made considerable progress in this endeavour, and established relationships with a number of world-class customers. Clearly this is still a "work in progress", but the early results can be seen in increased revenue and improved gross margins over the four quarters of 2007.

We also maintained our focus on tackling the key challenges that I indicated last year, and that are facing Dialog in the years ahead:

- improving our cost platform;
- diversifying our revenue;
- focusing our products and sales on higher-growth markets; and
- strengthening our management and skill base.

We made significant progress in the year in addressing each of these challenges.

Improving our cost platform

We completed the transition of our final-test operations from Germany to off-shore subcontractors in Asia. We now have a truly scalable business platform to build further growth without having incurred major capital expenditure for manufacturing equipment. The transition was carried out with the utmost care and without disrupting our excellent product delivery record to our customers.

We implemented our decision to de-list from Nasdaq in January 2007 and that has already helped to simplify our financial reporting process and reduce our administrative costs.

Diversifying our revenue

In 2007, we developed a completely new market area for the Company when we began volume production of highly-integrated power management devices for one of the world's leading consumer electronics companies. We made steady gains of new customer designs in Asia, Europe and North America, and started shipping our highly-integrated audio and power management devices for third-generation 3G/HSDPA mobile phones and smart multimedia phones. This business had a significant, and increasing, impact on our revenue in the second half of the year.

We also continue to focus on innovative differentiated, "always-on" display drivers, targeted at the emerging thin, low-power displays for mobile, and personal handheld applications, using technologies such as e-paper, MEMS and OLED. From the second half of 2008, this range of new products in established, and emerging, sectors will provide the Company with new opportunities for revenue generation in growth markets for a number of years.

Focusing our products and sales on higher-growth markets

During the year we focused our research and development (R&D) effort on producing world-class technology in the shape of an increasingly broad base of products, from which to generate future solutions for customers and returns for our Shareholders. We made a further investment in advanced low-power audio technology when we set up a new design centre in Scotland.

Our portfolio of automotive and industrial products, which covers highly-integrated smart motor controllers and electronic lamp ballast products, continued to produce dependable revenue in 2007 while we completed the development of a number of new products, ready to launch in 2008.

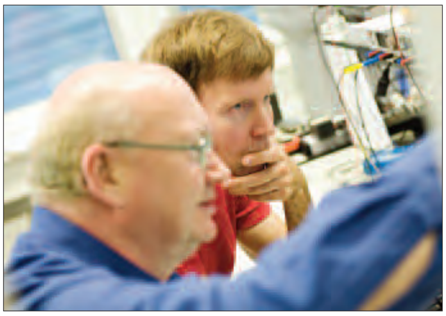
We had notable success in applying our System-on-Chip ("SoC") technology for smart motor controllers for new end-applications – such as seatbelt control and cooling fan equipment – with new tier1 automotive customers. In addition, we are pursuing the integration of advanced 32-bit microprocessors on chips that require sophisticated signal processing for intelligent car batteries.

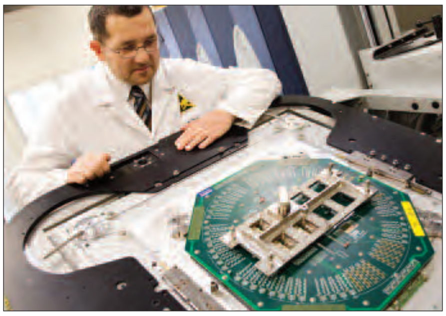
In addition, we are developing an increasing family of highly-integrated power management and audio companion IC products for a number of our partners' popular Application and Baseband processors. Our products address market sub-segments, such as smart phones, PND and other handheld multimedia devices.

"How can we help address the challenges of automotive in today's environmentally conscious world?"

"You know, Dialog has 20 years' experience in automotive and industrial IC development. Our design teams bring an international dimension to problem solving and with our combined high voltage and high performance CMOS technology we can give our customers true system integration and save power."

Chief Executive's review





Strengthening our management and skill base

The Non-executive Directors who joined our Board brought valuable new perspectives from mobile phone operators, world-class manufacturing and Silicon Valley culture. These, together with the additional members of the executive team, who have brought further semiconductor industry management expertise since early 2006, have made a significant contribution to the Company's knowledge base and, through that, to its strategy.

We continued to attract significant industry talent and expertise in 2007, particularly in our Design, Application engineering, Product Marketing, Sales, and Global Manufacturing teams, and our new design centre in Scotland has already attracted a highly-qualified team of international R&D engineers. The restructuring of our manufacturing has, inevitably, resulted in a degree of turnover in our staff, but it has enabled us to augment and upgrade our technical and marketing skills without increasing our total headcount. Most importantly, this will increase our ability to deliver our mid-term strategy.

A year of recovery

The year was – as we forecast – one of recovery and improving financial performance. During the first half, we gradually began to recover from the unforeseen insolvency of our major wireless customer – BenQ Mobile GmbH – in Q3 2006, while maintaining a tight control over expenditure and cash management.

Also as we forecast, in the second half of the year, we began to see a resurgence in revenue from our Wireless products. This was fuelled by the shipment of our new 3G phones and portable consumer multimedia products. By the end of the year, our focus on higher-growth opportunities was already manifesting itself in quarterly improvements in revenue and gross margin: we ended Q4 2007 with a normalised quarterly gross margin approaching 40%.

Gross margin for the full year reached 33.4% – a significant improvement over 2006 (18.6%) and 2005 (28.3%). This is a clear indication that our strategy of selecting opportunities in higher-growth higher-margin segments, while exiting lower-margin commoditised LCD products, is proving to be a success.

The future

Going forward, we will continue our efforts to fine-tune our strategy to ensure that the Company is well positioned to deliver sustainable growth, in revenue and profits, for the benefit of all our Shareholders.

In 2008 we will focus on developing and accelerating the implementation of our strategy. We will:

- continue building our our portfolio of Application Specific Standard Products for power management, audio, display and automotive applications. These will enable us to broaden our customer base by using specialist distributors channels;
- enhance our competitive advantage in power management, advanced audio, and high voltage mixed-signal SoC through focused R&D;
- increase our sales, marketing and technical support to clients, worldwide, with particular focus on expansion in the North America and Asia markets;
- optimise our operating platform by migrating to an advanced Information Management Systems to enable further scalable growth; and
- position and communicate Dialog's brand, strategy and unique values coherently to the broader markets as well as to investors.

2007 was a year of recovery, execution and a return to a growth path, and I am grateful to all Dialog's employees, who showed great professionalism and dedication throughout a very challenging year.

At the heart of our strategy, we continue to be committed to creating sustainable Shareholder value, and we view sustainable profitable growth as our prime objective. Subject to wider economic uncertainties, your Board sees the current year as one of opportunity for Dialog to demonstrate that sustainable growth, and attain profitability.

I have every confidence in our future.

Dr Jalal Bagherli
Chief Executive Officer

Solutions, products and key customers

Our products and solutions meet the needs of Original Equipment Manufacturers (“OEMs”). We design, develop and deliver mixed signal components and system-level solutions in areas such as power management, audio CODECs, and System-on-Chip (“SoC”) integration.

Our solutions
Our solutions address two major markets: mobile handset and portable electronic devices, and automotive and industrial electronics.

The continuing decrease in size – and increase in capabilities – of electronic devices, is a major driver in the development of our solutions. High-speed data, video and high-quality audio on mobile telephones and other handheld products, make huge demands on battery energy management, as well as on the technology which controls the quality of images and displays. Our skill in developing highly-integrated silicon solutions enables our customers to design products which deliver excellent performance as well as market-leading talk and standby times.

In the automotive market customers use our products in the comfort and safety systems, as well as in the management and control of the electronic systems they design for cars; and in the industrial market customers use our products in highly-integrated smart-power management systems, such as intelligent electronic ballasts for fluorescent lighting.

Design, development and production
We are justifiably recognised for the quality and feature-rich functionality of our mixed signal standard Integrated Circuit (“IC”) and Application Specific Integrated Circuit (“ASIC”) solutions. We nevertheless continually work to increase our digital and analog design expertise, and to develop our software. During 2007, we invested US$31 million in research and development.

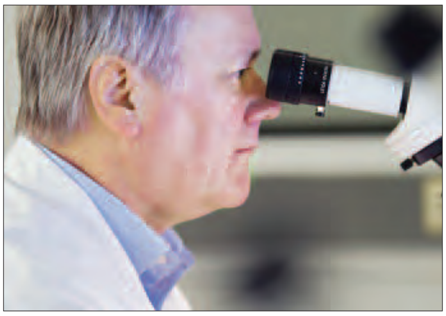
Our ability to develop mixed signal ASIC and Application Specific Standard Product (“ASSP”) designs rapidly, enables us to respond to customers’ needs for new solutions that increase performance while, at the same time, reducing cost. Our strategy of modifying and re-using a wide set of specialised analog building blocks speeds up the design process; in addition, our use of industry-standard design tools increases the level of automation and the quality of verification in our products. Our commitment to continuously deepening our expertise has resulted in increased levels of integration and product innovation in all business sectors. We continue to focus our research and development on state-of-the-art technology to meet the demands of next-generation products.

Our products
Broadly speaking, we produce two ranges of products which are both built around similar technology “building blocks”. For high-volume customers, we engineer and fine-tune system solutions to their precise specifications; for those market segments which consist of lower-volume customers, we provide a range of flexible standard products designed to cover a broader set of requirements. This approach gives a diverse set of customers access to the highly-integrated power management, audio and display technologies developed by Dialog.

Now that the majority of semiconductor manufacturers are “fabless” (they outsource the fabrication, or manufacture, of their chips to silicon foundries) the electronics industry is becoming more specialised. For example, our system platform partners often enter into agreements with us to design exclusive custom chips to form part of their systems and, in turn, license their system platform to a number of manufacturers of end-user equipment. Those OEM manufacturers complete the circle by buying the chips from us.

Power management and audio ICs. Effective power management – in which the design of chips used in hundreds of millions of mobile phones and other portable devices has given us a great deal of experience – is increasingly one of the fundamentals of system design.

Solutions, products and key customers



We have developed more than 50 different power management designs for the world's leading mobile phone manufacturers. These designs offer unprecedented integration with multiple power management functions on the chip, including programmable high-performance LDOs (low drop-out voltage regulators), high-efficiency DC-DC voltage converters, intelligent battery charging circuits, LED drivers, sensor ADCs, USB interfaces, and sophisticated audio capabilities.

By capitalising on our experience in integrating high and low voltage circuits on CMOS – the most widely-used semiconductor technology – and combining it with our experience in developing and integrating high-performance CODECs and other analog functions, we are able to offer a selection of unique power management and audio solutions. The integration of more than 30 different functions on a single chip delivers significant space, power and cost savings to our customers.

Display drivers and related-system ICs. LCD displays have a significant effect on battery life: when they are left on permanently they can consume as much as 70% of a device's power. To address this market opportunity, we focus on developing innovative drivers for "always-on" display technologies, such as e-paper, MEMS and OLED-based technologies. In May 2007 we launched a number of new standard products supporting E-Ink Corporation's electronic paper displays for the production of consumer devices in 2008.

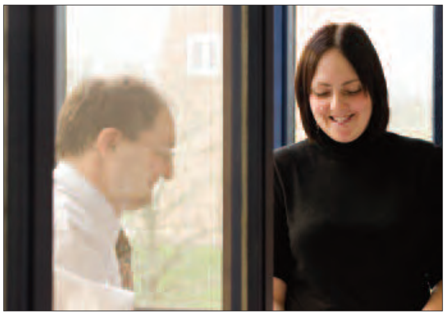
We recently completed the development of our new SmartXtend™ technology, which uses a number of innovative design techniques, including a unique multi-line addressing scheme, accurate dynamic current matching, and state-of-the-art power management. This will form the basis of a new family of display drivers which we will develop for passive matrix OLEDs.

Automotive and industrial system ICs. The ICs we supply to many leading car manufacturers capitalise on our expertise and knowledge of technology, ranging from power management systems and mixed signal design, to high-voltage circuits and embedded microprocessors on a single chip in a standard CMOS process. We provide technology for windscreen wipers, electric windows and motorised seat belts, and our partnership with leading manufacturers has resulted in chips which can be connected direct to a car battery without external protection circuits. In addition, we are pursuing the Systems-on-Chip integration of advanced 32-bit microprocessors for products that require sophisticated signal processing for automotive sensing applications.

Our single-chip solutions for industrial systems integrate microprocessors with high-voltage, low-power circuits which allow dimming and power factor correction used for fluorescent and high intensity lamps.

Application Specific Integrated Circuits ("ASICs"). Our ASICs form the basis for highly-integrated control chips for smart power electronic systems, in applications such as computer and mobile communications systems. They are ideal for situations in which chips have to be highly integrated and also have the ability to control high voltages intelligently using digital circuits on the same chip.

We work in partnership with the silicon foundries which manufacture our ASIC solutions, to ensure that our customers have access to the latest CMOS processes, as well as to the foundries' capacity. This, combined with our own in-house engineering capability, ensures that our customers are able to meet their cost and time-to-market objectives.



Manufacture, assembly and testing

Wafer manufacture. We outsource our wafer production to selected foundries, principally in Singapore and Taiwan, which provide high-quality products and have the ability to meet tight deadlines. Our choice of CMOS, rather than bipolar, technology enables more transistors to be integrated on a single chip – a necessary requirement for our target markets – and the end products are less power hungry.

Assembly and testing. The final assembly of our chips is outsourced to a number of sub-contractors. Our test programmes, based on our own and individual customers' specifications, are developed by our test engineers in parallel with the design process. In 2007, we concluded our transformation into a truly "fabless" company when we completed the transfer of our test, final test and "tape and reel" manufacturing activity to sub-contractors in the Far East.

We have also created a specialist off-shore support centre in Taiwan. We have our own manufacturing and technical engineers close to foundries, and assembly and test sub-contractors in Asia. By being "on the spot" to resolve any potential engineering issues quickly, they can forestall potential delays in production.

Quality and environment control

We have an uncompromising approach to quality assurance in every area of our operations: the participation of each of our employees, results in a highly-structured quality environment that wins the approval of all our major customers. The objective of our quality management system is to provide customers with the assurance that our products and services not only fulfil their contractual requirements, but will also meet their future needs. We have a "zero-fails" target.

We are committed to minimising our impact on the environment by developing and promoting environmentally-compatible products, and operate in accordance with the international quality standard, ISO 14001. We promote awareness and knowledge of environmental issues throughout the organisation to ensure that they become a natural part of the decision-making process.

We demand the same standards from our suppliers and form partnerships with those who are accredited to the same international quality standards.

For more detailed information on specific products, please see our Website, www.dialog-semiconductor.com.

Our principal customers

Our principal customers are recognised wireless communications, consumer electronics, and automotive equipment manufacturers. These include customers for both our standard products introduced over recent years and for application specific (ASIC) products.

The rapidly-evolving technology in all our target market sectors means that a partnership approach with our customers is essential – whether for standard products or for custom solutions. As a result, our customers look to Dialog as an outside source of expertise, while the close working relationship provides us with an opportunity continually to develop and fine-tune market leading technological expertise with recognised industry leaders.

We strive to form long-term relationships with all our major customers. In 2007, major revenue contributions came from customers such as Sony Ericsson Mobile Communication, Sharp, Motorola, Apple, Bosch, ContiTemic, Tridonic, Siemens, Adtran and Qualcomm.

Financial review

"I am pleased with the way we managed our cash flow and costs to provide the Company with a platform to fuel its ambition."

Jean-Michel Richard, CFO, Vice-President, Finance

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 International Financial Reporting Standards ("IFRS").

The following table details the historical consolidated statements of the operations of Dialog for the financial years ended 31 December 2007 and 2006 in US dollars and as a percentage of revenues:

	2007		2006		Change
	US$000	**% of revenues**	US$000	% of revenues	%
Revenues					
Wireless	**51,505**	**59.4**	57,934	61.7	(11.1)
Automotive/industrial	**35,268**	**40.6**	36,004	38.3	(2.0)
Revenues	**86,773**	**100.0**	93,938	100.0	(7.6)
Cost of sales	**(57,812)**	**(66.6)**	(76,435)	(81.4)	(24.4)
Gross profit	**28,961**	**33.4**	17,503	18.6	65.5
Selling and marketing expenses	**(7,253)**	**(8.4)**	(7,190)	(7.6)	0.9
General and administrative expenses	**(7,945)**	**(9.2)**	(17,644)	(18.8)	(55.0)
Research and development expenses	**(31,105)**	**(35.8)**	(27,529)	(29.3)	13.0
Other operating income	**1,190**	**1.4**	–	–	(87.1)
Net restructuring and related impairment charges	**(1,120)**	**(1.3)**	(6,115)	(6.5)	–
Operating loss	**(17,272)**	**(19.9)**	(40,975)	(43.6)	(57.8)
Impairment of investments	**(2,662)**	**(3.1)**	–	–	–
Interest income	**1,053**	**1.2**	1,356	1.4	(22.3)
Interest expense	**(84)**	**(0.1)**	(204)	(0.2)	(58.8)
Foreign currency exchange gains and losses	**519**	**0.6**	(2,084)	(2.2)	124.9
Other financial income	**44**	**0.1**	–	–	–
Other financial expenses	**(447)**	**(0.5)**	–	–	–
Result before income taxes	**(18,849)**	**(21.7)**	(41,907)	(44.6)	(55.0)
Income tax benefit (expense)	**(136)**	**(0.2)**	158	0.2	(186.1)
Net loss from continuing operations	**(18,985)**	**(21.9)**	(41,749)	(44.4)	(54.5)
Loss from discontinued operations	**–**	**–**	(2,267)	(2.4)	100.0
Net loss	**(18,985)**	**(21.9)**	(44,016)	(46.8)	(56.9)

Results of operations

Segmental reporting

Wireless communications. Revenues in this segment were US$51.5 million for the year ended 31 December 2007 (2006: US$57.9 million) comprising 59.4% (2006: 61.7%) of our total revenues. The 11% decrease in revenue was a result of anticipated lower sales as certain products were phased out following the planned transition from 2G to 3G, and successor products began to contribute to revenue only in the second half of 2007. When comparing the second half of 2007 with that of 2006, the Company increased revenues by 186% to US$44.0 million in 2007 (2006: US$15.5 million), as a direct result of successfully introducing new consumer entertainment products and 3G cell phones.

The operating loss decreased in 2007 by 58.4% to US$13.0 million (2006: US$31.1 million). This was achieved through increased revenue in the second half of 2007, coupled with a richer product mix and higher margins derived from new products introduced during the period. In the second half of 2007 we achieved an operating profit of US$1.1 million (2006: operating loss of US$25.7 million).

Automotive/industrial applications. Revenues decreased slightly to US$35.3 million (2006: US$36.0 million), or 40.6% (2006: 38.3%) of total revenues for the year ended 31 December 2007. In this sector, as a result of the investments we made to fuel our anticipated growth, we made an operating loss of US$1.6 million (2006: US$0.9 million).

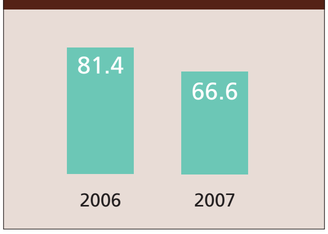
Revenues

Revenues for the year ended 31 December 2007 were US$86.8 million (2006: US$93.9 million). Excluding those revenues generated in 2006 from discontinued products (low-margin commodity STN liquid crystal displays were no longer marketed in 2007), baseline revenues increased by 11%. This more than compensated for the revenue lost in 2006 as a result of the insolvency of BenQ Mobile GmbH. In the second half of 2007, revenues of US$59.3 million (2006: US$33.5 million) represented an increase of 77%.

Cost of sales

Cost of sales consists of materials, outsourced production and assembly, related personnel costs, and applicable overhead and depreciation of test and other equipment.

Cost of sales as % of revenue



For the year ended 31 December 2007, cost of sales decreased by 24.4% to US$57.8 million (2006: US$76.4 million), 66.6% of total earnings (2006: 81.4% of total earnings). This demonstrated the gains made possible by our ongoing efforts to improve the Company's product mix and the efficiency of the restructuring measures undertaken over the past 18 months.

Sales and marketing expenses

Sales and marketing expenses primarily consist of salaries, travel expenses, sales commission, and advertising and other marketing costs. In 2007, sales and marketing expenses, at US$7.3 million (2006: US$7.2 million) or 8.4% (2006: 7.6%) were at the same level as in 2006. It might be expected that a decrease in sales commission, resulting from lower revenue, would have resulted in a decrease in overall costs, but we invested in creating value by increasing staff in strategic marketing functions.

General and administrative expenses

General and administrative expenses consist primarily of personnel and support costs for our finance, human resources and other management departments. General and administrative expenses decreased to US$7.9 million in 2007 (2006: US$17.6 million). The amount in 2006 included costs incurred as a write-down of accounts receivable of US$2.6 million, and inventory and materials at suppliers of US$5.8 million, dedicated to BenQ Mobile GmbH, a former customer, which became insolvent in the third quarter of 2006. Excluding these one-off charges, general and administrative expenses would have totalled US$9.2 million in 2006. As a percentage of total revenues, general and administrative expenses (excluding the one-off effects) decreased to 9.2% in 2007 (2006: 9.8%). When comparing the second half of 2007 with the first half, general and administrative expenses increased by 5%, while revenues increased by more than 115%.

Research and development expenses

Research and development expenses consist principally 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 increased to US$31.1 million in 2007 (2006: US$27.5 million). The Company continues to invest in audio, emerging display technologies and automotive intelligent sensors to position itself for further growth and diversification. As a result of working from a lower revenue base, research and development expenses as a percentage of total revenues increased to 35.8% (2006: 29.3%) over these periods.

Financial review

Other operating income

Other operating income includes an unexpected settlement of US$0.9 million, received in November 2007, against a receivable which had been written down in 2006 as a result of the insolvency of BenQ Mobile GmbH.

Restructuring and related impairment charges

Restructuring and related impairment charges in 2007 are mainly comprised of US$0.4 million of employee termination costs, impairment charges, other losses and gains relating to assets that became redundant of US$0.3 as well as other costs, especially for transportation, of US$0.4 million, resulting from the transfer of the Company's Wafer Test, Final Test and Tape & Reel operations, from Nabern, Germany, to dedicated outsourced assembly and test organisations in Asia. As a result of the transfer, the Company reduced its workforce by 33 employees in the third quarter of 2006 and a further six employees in the fourth quarter of 2007.

In 2006 restructuring and related impairment charges mainly comprised US$1.6 million employee termination costs and US$4.1 million of asset impairment charges.

For further information see note 4 to the consolidated financial statements (page 52).

Operating loss

We reported an operating loss of US$17.3 million for 2007 (2006: US$41.0 million). The improvement primarily resulted from higher gross profits recognised in the year and lower restructuring charges, as described above. In addition, 2006 included the write-down of BenQ Mobile GmbH receivables, inventory and materials at suppliers.

Write-down of investment

In the third quarter, we recorded a one-off charge of US$2.7 million. This related to a write-down in the value of our investment in Digital Imaging Systems (a former division of the Company which became a spin-off woth venture capital funding in February 2006), as a result of the reduced visibility of revenue break-even in this business and an increase in long-term funding requirements. Of the amount written down, US$1.6 million relates to payments made before 31 December 2006 and US$1.1 million relates to further payments the Company was committed to in 2007.

Interest income, net

Interest and similar income, net, from the Company's investments (primarily short-term deposits and securities) was US$1.0 million for the year ended 31 December 2007 (2006: US$1.2 million). The reduction was primarily as a result of the decrease in liquidity.

Foreign currency exchange gains and losses, net

Foreign currency transaction gains and losses result from amounts ultimately realised on the settlement of foreign currency transactions, and from the period-end remeasurement of foreign currency-denominated receivables, payables and cash into US dollars (2006: into euros). Foreign currency gains, net, were US$0.5 million for 2007 (2006: losses of US$2.1 million). As described in note 1 to the consolidated financial statements, on 1 January 2007, the Company changed its functional currency from the euro to the US dollar. For this reason, although the dollar lost in value against the euro in both periods, we show a foreign currency gain in 2007 and a foreign currency loss in 2006.

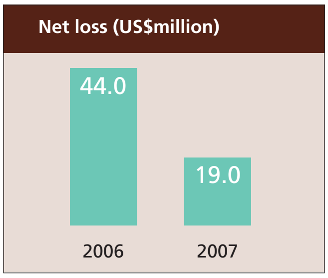
Income tax benefit (expense)

Income tax expense was US$136,000 in 2007 (2006: benefit of US$158,000). The tax benefit recorded in 2006 principally relates to a refund of a corporation tax credit in Germany which we were able to recognise after a change in tax legislation during that year.

Loss from discontinued operations

There were no losses from discontinued operations. Losses from discontinued operations in 2006 of US$2.3 million were incurred through the disposal of our Imaging division in February 2006, as well as legal and transaction fees related to the transaction. For further information see note 3 to the consolidated financial statements (page 51).

Net loss



For the reasons described above, we reported a net loss of US$19.0 million in 2007 (2006: US$44.0). Loss per share (basic) was US$0.42 in 2007 (2006: US$0.99).

Liquidity and capital resources

Cash flows

Cash used for operating activities was US$10.2 million for the year ended 31 December 2007 (2006: US$16.2 million cash provided by operating activities).

The cash outflow in 2007 relates primarily to the financing of working capital, principally trade accounts receivable and inventory in the second half of 2007. The cash inflow in 2006 mainly resulted from the collection of trade accounts receivable and lower inventory balances.

Cash used for investing activities was US$6.1 million for the year ended 31 December 2007 (2006: US$6.6 million). Cash used for investing activities during 2007 principally consisted of the purchase of tooling (masks), laboratory equipment, probe cards, load boards and, to a lesser extent, test equipment, for a total of US$4.1 million (2006: US$3.7 million); a further payment of US$1.0 million for our committed investment in Digital Imaging Systems; US$1.1 million (2006: US$1.3 million) for the purchase of software and licences; and payment related to capitalised development costs of US$0.7 million (2006: US$nil). This cash outflow was partially offset by cash in-flows of US$1.1 million from the sale of excess assets resulting from our restructuring activities. For further information see note 4 to the consolidated financial statements (page 52).

Liquidity

At 31 December 2007 we had cash and cash equivalents of US$15.9 million (2006: US$32.0 million) and marketable securities of US$19.9 million (2006: US$19.4 million). The working capital (defined as current assets minus current liabilities) was US$36.1 million (2006: US$54.4 million). As at 31 December 2007 we had no long-term debt.

A reduction in customer demand for our products, caused by unfavourable 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 short-term credit facilities of US$9.4 million (€6.4 million) available that bear interest at a rate of EURIBOR +0.75% per annum. At 31 December 2007 we had no amounts outstanding under this facility. As a result of entering into a factoring agreement, as stated in note 25 to the consolidated financial statements (page 72), which provides the Company with up to €10.0 million (or US$ equivalent) of readily-available cash, the Company decided to reduce the credit line from its lead bank from previously €12.5 million to €6.4 million (US$9.4 million). 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 if required.

Balance sheet

	2007 US$000	2006 US$000	Change US$000	%
Assets				
Cash and cash equivalents and available-for-sale securities	**31,844**	51,383	(19,539)	(38.0)
All other current assets	**21,822**	14,063	7,759	55.2
Total current assets	**53,666**	65,446	(11,780)	(18.0)
Non-current assets held for sale	**–**	1,393	(1,393)	(100.0)
Property, plant and equipment, net	**10,452**	12.417	(1,965)	(15.8)
Intangible assets	**2,443**	1.579	864	54.7
Held-to-maturity securities	**4,000**	–	4,000	–
All other non-current assets	**662**	2,294	(1,632)	(71.1)
Total non-current assets	**17,557**	16,290	1,267	7.8
Total assets	**71,223**	83,129	(11,906)	(14.3)
Liabilities and Shareholders' equity				
Current liabilities	**17,531**	12,460	5,071	40.7
Net Shareholders' equity	**53,692**	70,669	(16,977)	(24.0)
Total liabilities and Shareholders' equity	**71,223**	83,129	(11,906)	(14.3)

Financial review

The balance sheet total was US$71.2 million at 31 December 2007 (2006: US$83.1 million). Cash and cash equivalents and securities (held as available for sale and held to maturity) decreased by 30.2% to US$35.8 million (2006: US$51.4 million). This was mainly the result of an operating cash outflow to finance increasing working capital needs, particularly in the second half of 2007 as described above.

Non-current assets held for sale were reduced to zero by 31 December 2007 as a result of assets being sold, written down or reclassified to property plan and equipment. For further information see note 4 to the consolidated financial statements (page 52).

Total non-current assets, as at 31 December 2007, increased to US$17.6 million (2006: US$16.3 million) or 24.7% (2006: 19.6%) of the balance sheet total. The increase mainly results from capital expenditure and investments in 2007 of US$7.0 million and the acquisition of new securities, classified as "held to-maturity", of US$4.0 million. It was partly offset by the depreciation and amortisation of property, plant and equipment and intangible assets of US$6.4 million, the write-down of the investment in Digital Imaging Systems of US$2.6 million (see above), disposals of assets with a net book value of US$0.6 million and the asset write-down related to the restructuring of US$0.3 million.

Current liabilities in 2007 were US$5.1 million above the previous year's level. They relate primarily to higher trade accounts payable in the course of our increased business volume in the second half of 2007.

We had no non-current liabilities at 31 December 2007.

Shareholders' equity decreased to US$53.7 million at 31 December 2007 (2006: US$70.7 million) as a result of the net loss which occurred during the year. The equity ratio, while decreasing from 85% to 75%, remains healthy, however.

Off-balance sheet arrangements and other commitments

We have no off-balance sheet arrangements involving variable interest entities. We lease all our office facilities, office equipment and vehicles under operating leases. In addition we have contracted consulting services related to CAD (computer aided design) until 29 December 2009. Future minimum payments under these agreements, which have initial or remaining terms in excess of one year at 31 December 2007, are as follows:

Operating leases

	2007 US$000	2006 US$000
within one year	**4,473**	4,621
between one and two years	**2,895**	3,718
between two and three years	**1,228**	1,746
between three and four years	**270**	275
between four and five years	**5**	208
thereafter	**–**	–
Total	**8,871**	10,568

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.

Dividends

We did not pay dividends in the years ended 31 December 2007 and 2006 and do not plan to pay dividends in the foreseeable future. Dialog's Board of Directors is committed to re-investing all profits into creating a framework for future growth and continues to believe that – in line with the strategic changes underway – this policy is in the best interest of Dialog's Shareholders.

Jean-Michel Richard
CFO, Vice President Finance

Risks and their management

The market
The market in which we compete is intensely competitive and highly cyclical, and is characterised by continuous development and technological improvement. Our future success depends on our ability to anticipate and respond to new market trends, to implement new designs rapidly to meet customers' needs, and to keep abreast of the technological changes. As a result, we invest in research and development to enable us to create innovative designs and products on a cost-effective, timely basis.

Revenue and profitability
While we have not been profitable for the past seven financial years, and cannot guarantee that we will become so, we constantly seek to improve profitability by launching new products and acquiring new customers. Since we continue to rely on a relatively small number of customers for a substantial proportion of our revenue, the loss of one or more of these customers would be likely to have a material affect. Our goal is to spread this risk by acquiring more customers. In the past year, we have made considerable progress in this objective.

We are attempting to reduce the risk of our revenues, profitability and growth being affected by a slow-down in the wireless communications market by winning customers in other sectors.

Third-party costs
During 2007, we outsourced our manufacturing and testing to lower-cost environments, where there is excellent capacity, to overcome the potential problem of an inability to access manufacturing capacity which would result in increased costs and, therefore, decreased revenue.

Intellectual property
We make strenuous efforts to protect our intellectual property from being copied or used by others.

Interest rate risk
The Company earns interest from bank deposits, uses money market deposits and invests in non-current interest-bearing held-to-maturity investments. It has also invested in highly-liquid "investment-grade" rated debt-based funds – classified as held-to-maturity – which are contracted to mature in 2010 and which incorporate a floating interest rate linked to market rates.

It is our policy to manage our interest income using a mix of fixed and variable interest rate debts. To achieve this, we invest in highly-liquid funds which have a matching investment strategy. Funds not needed for financing operations in the near future are invested in floating interest rate securities. Only short-term deposits bear fixed interest rates.

Currency risk
The Company's functional – and presentational – currency is the US dollar, and the majority of its revenue and expenses are in that currency.

There are, however, foreign exchange risks associated with transactions, and recognised assets and liabilities in other currencies, primarily the euro and the pound sterling.

Transaction currency exposures arise from sales or purchases in currencies other than the US dollar. We use forward currency contracts to eliminate our exposure associated with the payment of salaries and wages in other currencies. We maximise the effectiveness of our hedge derivatives by matching the terms and conditions of the hedge to those of the underlying obligation. (See Note 25 on page 73 for further information.)

Other price risks
IFRS 7 requires us to disclose how hypothetical changes in risk variables, such as stock exchange prices, would affect the price of financial instruments.

As part of our cash management, we invest in available-for-sale securities with defined maturities and repayments of 100% of their nominal amounts. Fluctuations could occur during their maturity, however, and have an impact on the Company's profit or loss. (See Note 25 on page 74 for further information.)

Credit risk
The Company is exposed to credit risk from its operating activities and certain of its financing activities. We ensure that our exposure to bad debt is minimised by constantly monitoring all customers who trade on credit terms, and receivable balances.

In August 2007, we entered into a factoring agreement with a reputable German financial institution for a total of €10 million to finance our growth. Since the financial institution assumes all risks associated with the collection of receivables from selected customers, the agreement significantly reduces our risks associated with their collection.

We, in turn, have pledged US$6.5 million of our securities to the financial institution concerned. These will be drawn on only if an action of ours partially or completely invalidates the claim on a receivable that had been financed through the factoring programme.

Our exposure to credit risks arising from other financial assets, such as cash and cash equivalents, available-for-sale and held-to-maturity financial investments, would arise from the default of a counterparty and is limited to the carrying amount of the particular instruments.

Liquidity risk
We monitor our liquidity on a quarterly basis with the objective of avoiding interest on short-term bank liabilities or overdrafts. Our policy is to structure the maturity of our current financial assets in the Group to meet 100% of the respective maturities and liabilities.

Corporate social responsibility

Corporate social responsibility
Dialog is committed to the adoption of the Electronics Industry Code of Conduct (EICC) standard as the model for ensuring that working conditions for internal and external suppliers are safe and that all workers are treated with respect and dignity. In addition, the company complies with the ISO 14001 environmental standard – and expects its suppliers to do the same – in order to ensure that all manufacturing processes are environmentally responsible.

Management systems
Dialog's management system complies with the EICC code. It is certified to the TS16949 international standard as a formal implementation of the code and is committed to implementing and facilitating continuous improvements, and to mitigating operations-related risks. To enable us to comply with all applicable laws, regulations and customer requirements, as required by the code, we also ensure that all our major supply-chain partners are accredited to the same standard. To ensure that we constantly improve our management systems, we regularly review and audit internal and supply-chain management systems.

The environment and environmental protection
Our commitment to the environment is evidenced by our ISO14001 certification. Since we firmly believe that sustainable development can be secured only if we safeguard our valuable resources, we deal only with suppliers which have similar environmental goals and are also accredited to the ISO14001 standard.

Within our supply chain, we continually emphasise that environmental issues should be an instinctive part of any decision-making process, and that suppliers should use environmentally-friendly technology to:
- reduce and eliminate emissions of ozone-depleting, and other, chemicals;
- manage, reduce and dispose of hazardous substances safely;
- monitor and control waste water and solid waste emissions;
- reduce and eliminate all types of waste, including water and energy;
- reduce waste by maximising product yields; and
- ensure all environmental permits are obtained, maintained and kept current.

Health and safety
Dialog considers a safe and healthy working environment to be essential in the maintenance of employees' morale and in the production of high-quality and innovative products. As a result, we require our major suppliers also to be committed to ensuring the creation of healthy and safe working conditions. We expect them to provide evidence of suitable controls, safe working procedures, preventative maintenance and general protective measures in their working environments.

When hazards cannot be adequately controlled by these means alone, suitable protective clothing or equipment is supplied, and evacuation procedures and facilities are in place at Dialog's and suppliers' premises.

Connecting with employees
Dialog aims to attract and retain the best people by ensuring that all employees receive comprehensive on-the-job formal training, coaching and mentoring. Clear and regular communication is achieved through regular company-wide information sessions, led by the CEO, and every effort is made to keep employees fully aware of Company matters that affect them.

We encourage employee feedback at all levels for new ideas to improve business efficiency and performance. We support initiatives and fund raising in the local communities in which we work. In 2007, for example, we made a contribution to a cancer hospice charity.

Ethics
Dialog believes that continued success in the semiconductor market can be achieved only by adopting continuously high standards of ethical behaviour when dealing with customers, suppliers and workers. It is particularly important to protect Intellectual Property ("IP"), which is the key to ensuring the development of innovative solutions to complex problems. Any transfer of technology or know-how is always done in a manner that protects IP rights; effective protection also means that products can be discussed openly with our business partners.

The disclosure of information which is related to business activities, structure, our financial situation and performance is always carried out in accordance with applicable regulations and prevailing industry practices. We expect the highest standards of integrity from all Dialog stakeholders; any malpractice is strictly prohibited and may result in immediate termination and legal action.

Neither we nor our suppliers offer or accept inducements or any other means of obtaining undue or improper advantage. We have a "whistleblower" policy in place to protect employees' confidentiality and encourage our suppliers to do the same.

Human rights
Dialog's suppliers must demonstrate a commitment to upholding workers' human rights and to treating them with dignity and respect. Standards such as the Universal Declaration of Human Rights, Social Accountability International and the Ethical Trading Initiative have been used as a basis for these requirements.

All labour must be given voluntarily and workers must be free to leave their employment on reasonable notice. Child labour must not be used at any stage of manufacturing. Working hours must not exceed the maximum set by local laws, and wages must comply with all applicable laws.

Suppliers must ensure that workers are not threatened or subjected to inhumane or harsh treatment, harassment or any form of unlawful discrimination. Communication and direct engagement between workers and management is encouraged, even in those countries where there is no meaningful legal protection.

Executive management

Dr Jalal Bagherli (51)
Chief Executive Officer
Jalal joined Dialog, as CEO, in September 2005. He was previously Vice President & General Manager of the Mobile Multimedia business unit for Broadcom Corporation and the CEO of Alphamosaic. He has extensive experience of the semiconductor industry, through his previous professional and executive positions at Texas Instruments and Sony, and a wealth of knowledge about the Far Eastern, European and North American markets. He is a non-executive director of Lime Microsystems Ltd.

Gary Duncan (52)
Vice President, Engineering
Gary, who joined the Company in 1987, is responsible for the design and development of our semiconductor products. Before joining Dialog, he held senior engineering and management roles at Plessey and ES2.

Peter Hall (56)
Vice President, Operations and Quality
Peter joined Dialog in 1987 and is responsible for operations and quality. His previous experience includes management and engineering positions at STC Semiconductors and MEM, in Switzerland. Peter holds a BSc in electrical and electronic engineering from Newcastle University and an MSc in digital design techniques from Herriot Watt University, Edinburgh.

Udo Kratz (45)
Vice President, General Manager Audio and Power Management Business Unit
Udo joined Dialog in May 2006. He is responsible for the Audio and Power Management Business Unit which makes products for the mobile phone and portable consumer markets. His 18 years' experience in the semiconductor industry were gained in general management, senior marketing and engineering at Robert Bosch GmbH, Sony Semiconductor and Infineon Technologies. Udo holds an electronic engineering degree from the University for Appiled Sciences, Mannheim.

Jürgen Friedel (59)
Vice President, General Manager Automotive and Industrial Business Unit
Jürgen joined Dialog in 1999 and is responsible for the Automotive and Industrial Business Unit. He previously held senior management positions at SEL/ITT and National Semiconductor, in Germany. Jürgen holds a diploma in communications engineering from the University for Applied Sciences, Esslingen.

Manoj Thanigasalam (44)
Vice President, General Manager Display Systems Business Unit
Manoj joined the Company in March 2006. Responsible for the Display Systems Business Unit, he was previously VP Business Development at ZBD Displays and, before that, was General Manager of marketing for the Digital TV and wireless communications market at Sony Semiconductor. He has also worked for Texas Instruments, Philips, ARM and LSI Logic. Manoj holds a degree in physics and electronics from Bradford University.

Jean-Michel Richard (44)
CFO, Vice President Finance
Jean-Michel joined the Company in 2006 to head up its finance department. He was previously Finance Director for the Global Manufacturing and Technology Division of ON Semiconductor, in Phoenix, Arizona, and before that held senior finance and treasury positions at ON and Motorola, in Europe and the US. Jean-Michel holds a Masters in Economics from the University of Geneva, Switzerland.

From left to right: Peter Hall, Jürgen Friedel, Gary Duncan, Udo Kratz, Jean-Michel Richard, Manoj Thanigasalam, Jalal Bagherli.

Board of Directors

Gregorio Reyes (65)
Chairman
Gregorio joined the Board in December 2003. His experience is primarily in data storage and magnetic recording, semiconductors, and telecommunications. He was President and CEO of National Micronetics from 1981 to 1984, and Chairman and CEO of American Semiconductor Equipment Technologies from 1986 to 1990. He co-founded Sunward Technologies in 1985 and was Chairman and CEO until 1994. He is currently on the board of Seagate Technology and is also a director of a number of privately-held companies, including LSI Logic, Nuera Communications, Future Trade Technology, Appshop and Astute Networks.

Dr Jalal Bagherli (51)
Chief Executive Officer
Jalal joined Dialog, as CEO, in September 2005. He was previously Vice President & General Manager of the Mobile Multimedia business unit for Broadcom Corporation and the CEO of Alphamosaic. He has extensive experience of the semiconductor industry, through his previous professional and executive positions at Texas Instruments and Sony, and a wealth of knowledge about the Far Eastern, European and North American markets. He is a non-executive director of Lime Microsystems Ltd.

Michael John Glover (69)
Non-executive Director
Michael joined the Board of Dialog's then holding company in 1990 and has been a Director of Dialog since March 1998. He was previously an executive and director of technology-based companies in the UK, Europe, South-east Asia and North America and he is a Senior Fellow specialising in Entrepreneurial Business Development at the University of Surrey's School of Management. He holds a degree in economics from the University of Birmingham.

Aidan Hughes (46)
Non-executive Director
Aidan joined the Board 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 was Finance Director of the Sage Group plc from 1993 until 2000 and, from December 2001 to August 2004 was a director of Communisis Plc. He is a director of, and investor in, a number of UK private technology companies.

John McMonigall (64)
Non-executive Director
John joined the Board in March 1998. He has been a director at Apax Partners since 1990 and, between 1986 and 1990, held a variety of senior positions at British Telecommunications plc and was also a member of the management board. He is currently on the board of several other public and private companies including Autonomy Plc.

Peter Weber (61)
Non-executive Director
Peter joined Dialog on 1 February 2006. He brought with him 35 years' experience, gained at a broad range of companies in the semiconductor sector, including Texas Instruments, Intel, Siliconix, the Temic Group and Netro Corporation. Since 1998 he has been an investor and management consultant, and is a director of a number of companies in Europe and the US. Peter holds an MSEE degree in communications engineering.

Peter Tan (58)
Non-executive Director
Peter joined the Board in July 2006. He has held senior management roles across a wide range of technology companies, including Apple Computer, Molex and Flextronics. During more than 30 years' experience of operating in the Far East he has built up expertise in world-class manufacturing and technology companies.

Russ Shaw (44)
Non-executive Director
Russ joined the Board in July 2006. He is currently Director of Innovation at Telefonica. He was previously Innovation Director at O_2, which he joined as Marketing Director in 2005. The strong brand and product range he established resulted in significant customer growth. His more-than 20 years' senior marketing and brand management experience in the telecoms and financial services area has enabled him to bring an excellent level of knowledge to Dialog.

Chris Burke (47)
Non-executive Director
Chris joined the Board in July 2006. Until the end of 2004, he was CTO at Vodafone UK Limited and was previously CTO at Energis, after spending 15 years in Research & Development at Northern Telecom. He holds appointments at Connectivity Ltd (an Esprit, and 3i Portfolio Company); Tatara Systems; One Access; INUK Networks; and March Networks. He currently invests from his own fund and provides strategic advice to a wide range of investors and technology companies, including HP Communications & Media, and VantagePoint Venture Partners.

From left to right: Jalal Bagherli, Chris Burke, Michael John Glover, Russ Shaw, Peter Weber, Gregorio Reyes, John McMonigall, Aidan Hughes, Peter Tan.

Directors' report

The Directors of Dialog Semiconductor Plc ("Dialog" or "the Company") present their Annual Report and audited financial statements for the year ended 31 December 2007. These accounts have been prepared for UK reporting purposes; separate accounts which comply with the rules governing the Company's Germany listing are available on the Company's Website, www.dialog-semiconductor.com.

Principal activities and review of the business

Dialog Semiconductor develops and supplies a range of innovative integrated circuit (IC) solutions for wireless, automotive and industrial electronic systems. The Company's background and strengths are in designing low-power mixed signal circuits for sensing, processing and conversion, high-quality audio, and expert handling of high voltages on CMOS technology. It operates a "fabless" business model, under which it designs ICs, outsources the production of silicon wafers, packaging, and testing, then delivers final chips to its customers, which are designers and manufacturers of mobile handsets and portable electronic products, and industrial and automotive suppliers.

The Company's corporate headquarters are located near Stuttgart, Germany. It has product development facilities in Kirchheim, Heidelberg and Munich in Germany; Graz in Austria; Swindon and Edinburgh in the UK; and Tokyo in Japan.

More information about the business is set out in the Chairman's statement, on page 6, and in the Business review, on pages 10 to 24.

Future developments

The Group's stated objective 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.

Research and development (R&D)

The Group believes that its future competitive position will depend on its ability to respond to the rapidly-changing needs of its customers by developing new designs in a timely and cost-effective manner. To this end, the Company's management is committed to investing in researching and developing new products and customising existing products.

To date, R&D projects have been in response to key customers' requests to assist in the development of new products, and for the development of application-specific standard products (ASSPs). The Company does not expect any material change to this approach in the foreseeable future.

Going concern

After reviewing the 2008 budget and longer-term plans, the directors are satisfied that, at the time of approving the financial statements, it is appropriate to adopt the going-concern basis in preparing the financial statements of the Company.

Dividends

The directors do not recommend the payment of a dividend (2007: nil). They are committed to re-investing all profits into the business and believe that this policy is in the best interests of its Shareholders.

Purchase of own shares

The Company operates an Employee Share Option Trust which purchases shares in the Company for the benefit of employees under the Company's share option scheme. Since the Company has control of the assets and liabilities of the Trust, they are included in the Company and Group balance sheets. At 31 December 2007, the Trust held 1,046,387 shares, which represented 2.3% of the total called-up share capital, at a nominal value of £104,639.

Share capital

Details of the share capital are set out in note 19 to the consolidated financial statements.

Substantial shareholdings

Details of substantial shareholdings are on page 9 of this Annual Report.

Directors

The directors, together with their biographies, are listed on page 26 of this report.

Directors' remuneration and interests

Directors' remuneration and interests are detailed in the Directors' remuneration report on pages 31 to 34 of this annual report.
No director had a material interest during the year ended 31 December 2007 in any contract of significance with any Group company.

Directors' report

Directors' third-party indemnity provisions

The Company has granted an indemnity to its directors against proceedings brought against them by third parties, by reason of their being directors of the Company, to the extent permitted by the Companies Act 1985. Such indemnity remains in force as at the date of approving the directors' report.

Election and re-election of directors

In accordance with the Company's Articles of Association, one third of the Non-executive directors have to stand for re-election at the Annual General Meeting. The next Annual General Meeting will be held on 30 April 2008 at 9am.

Corporate governance

The Company's corporate governance statement is set out on pages 29 and 30 of this report.

Supplier payment policy

It is the Group's policy to pay creditors in accordance with the terms and conditions agreed with them, and in accordance with contractual and other legal obligations. Days payable outstanding for the Group at 31 December 2007 was 56 days (2006: 43 days).

Financial instruments

The Group's financial risk management and policies, and exposure to risks, are set out on page 23.

Political and charitable contributions

The Group made no political contributions during the period. We made charitable contributions of US$1,200 to local community projects.

Employee policies

It is our policy to support our people through training, career development and opportunities for promotion. We operate an open-management approach and consult with our staff on matters which are of concern to them. We share information with them on the performance of the Company which, together with related bonuses, encourages staff involvement.

Disabled persons

Our policy provides for disabled persons, whether registered or not, to be considered for employment, training and career development in accordance with their aptitudes and abilities.

Statement on disclosure of information to auditors

The directors who were members of the Board at the time of approving the directors' report are listed on page 26. Having made enquiries of fellow directors and of the Company's auditors, each of the directors affirms that:

- to the best of their knowledge and belief, there is no information relevant to the preparation of their report of which the Company's auditors are unaware; and
- they have taken all reasonable steps to be aware of relevant audit information and to establish that the Company's auditors are aware of that information.

Annual General Meeting

The notice convening the Annual General Meeting will be published separately and posted on the Company's website. The meeting will be held at Tower Bridge House, St Katherine's Way, London E1W 1AA on 30 April 2008 at 9am.

Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of Ernst & Young LLP as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.

By order of the Board

Dr Jalal Bagherli
Director

28 February 2008

Corporate Governance

Governance standards
Dialog Semiconductor Plc is committed to implementing high levels of 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".

Dialog's Corporate Governance principles are published on its Website (www.dialog-semiconductor.com). The Website also contains a full version of the Company's Code of Business Conduct and Ethics. This details Dialog's expectations regarding the ethical standards that each Director, officer and employee should follow while acting on the Company's behalf.

Corporate Governance information relating to the past financial year is set out below.

Shareholders and the Annual General Meeting ("AGM")
The AGM, at which the annual financial statements and audit reports are presented, is the main forum for Shareholders to exercise their voting rights. Directors appointed by the Board during any given year are subject to Shareholder approval at the AGM. In addition, one-third of the Directors must resign each year and may put themselves forward for re-election. Changes to the constitution of the Company are decided by Shareholders' resolution. Similarly, the AGM is the forum at which Shareholders can authorise the Directors to issue new shares.

Dialog does not have any shares in issue which have multiple voting rights, preferential voting rights or maximum voting rights.

Board of Directors
The Board is responsible for determining Dialog's business strategy and ensuring that an executive is appointed to implement it. It is also responsible for overseeing the financial aspects of the business.

The Board, which met five times during the year, currently consists of eight Non-executive Directors and one executive Director. The compensation provided to each Director is detailed in the Directors' remuneration report on pages 32 and 33. The executive Director's remuneration is performance related and is connected to a set of goals and Dialog's profitability.

Audit Committee, and Nomination and Remuneration Committee
During the year, Dialog's Audit Committee comprised the following Directors: Aidan Hughes (Chairman), Michael Glover, Peter Weber and Peter Tan. The Committee is responsible for monitoring financial statements and reviewing the performance of the external Auditors. It also assesses the efficiency of the audit process and (among other things) considers compliance with accounting standards. The Chief Executive Officer, Chief Financial Officer, the Company Secretary and representatives of the external Auditors usually attend Audit Committee meetings.

During the year, the Audit, and Nomination and Remuneration Committees met frequently to analyse issues under their jurisdiction, usually on the day before each Board meeting.

The roles of the Compensation Committee, and of the Governance and Nomination Committee have been changed since the year end. The Board reviewed the Committees' responsibilities and concluded that, because their work often overlapped, the existence of two Committees did not represent the most efficient format for Dialog. The following changes have resulted:

- the Compensation Committee, and the Governance and Nomination Committee have been merged to form the Nomination and Remuneration Committee. The members of the new Committee are Russ Shaw (Chairman), Michael Glover and Chris Burke. With the exception of Corporate Governance, the new Nomination and Remuneration Committee takes over the responsibilities of the previous Committees. These include determining, subject to Board approval, the salaries and incentives of Dialog's senior executives and deciding on the size and composition of the Board; and
- Corporate Governance is now monitored at Board level – a reflection of the importance it is given by the Board.

Corporate Governance

Transparency
Under UK Disclosure and Transparency Rules, significant Shareholders are required to notify Dialog of a shareholding of 3% or more. Dialog must then notify BaFin and the Stock Exchange. Under s.15a of the German Securities Trading Act (Wertpapierhandelsgesetz) transactions in the Company's shares carried out by members of the Board of Directors and their family members are reported and published without delay.

The Company operates a Code of Dealing in its shares which is designed to prevent insider trading and the abuse of price sensitive information.

The Board appreciates the value of keeping Shareholders informed of Dialog's performance throughout the year. As a result it publishes quarterly financial reports, together with key information on the AGM, on its Website.

Business conduct and ethics
Dialog seeks to comply with all laws and regulations that have an impact on its business. In addition, the Company expects its employees and Directors to act with honesty, integrity and fairness in the conduct of its business. Dialog's Code of Business Conduct and Ethics is published on the Company's Website.

Dialog is committed to taking account of interests outside the Company, including those of employees, business partners, the environment and the local communities on which it has an impact. The Board values, and has developed, a culture of corporate social responsibility that takes the above factors into consideration.

Audit and auditors
The consolidated financial statements have been audited by Dialog's Auditors, Ernst and Young ("E&Y"). E&Y were appointed in October 2006 following a tender process.

The remuneration given to the Auditors over the past two financial years is detailed in note 30 to the consolidated financial statements on page 80.

The Company's audited financial statements for the year ended 31 December 2006, and the reports from the Directors and Auditors thereon, were presented to, and approved by, the Shareholders at the AGM of the Company held on 10 May 2007. E&Y, the Company's independent Auditor, was reappointed until the following AGM.

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 "Corporate Governance Code" as amended on 14 June 2007 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.

Gregorio Reyes
Chairman

28 February 2008

Directors' remuneration report

Policy on Directors' remuneration

The Board is responsible for setting the Company's policy on Directors' remuneration; the Compensation Committee agrees the remuneration for each executive Director.

The primary objectives of the Company's policy on executive Directors' remuneration are first, that it should be structured so as to attract and retain executives of a high calibre, with the skills and experience necessary to develop the Company successfully and, second, to reward them in a way which encourages the creation of value for the Company's Shareholders.

The performance measurement of each executive Director and the determination of his annual remuneration package are undertaken by the Nomination and Remuneration Committee.

No Director is involved in deciding his or her own remuneration. The Nomination and Remuneration Committee comprises Non-executive Directors and its role is, to apply the Board's policy on remuneration. The current members of the committee are Russ Shaw (Chairman), Michael Glover and Chris Burke.

The Company has one executive Director, Dr Jalal Bagherli, who was appointed on 12 September 2005. The executive Director's remuneration consists of three components:
1. Salary – reflects the executive's experience, responsibilities and market value;
2. Bonus – as part of his remuneration Dr Bagherli received a supplementary bonus, which was payable quarterly until 31 September 2007 and relates to benefits associated with an early exit from his previous employment contract. Further bonuses are based on objectives set by the Nomination and Remuneration Committee relative to the performance of the Group, as an incentive to Dr Bagherli to achieve relevant and demanding targets, such as revenue growth, operating profit, design wins; and
3. Share options – details are set out in note 21 to the consolidated financial statements (page 65).

Compensation of Non-executive Directors

Non-executive Directors, who are not associated with any of our principal Shareholders, are paid quarterly for their roles as Directors. Additional fees are paid for their participation in the Company's Board committees, the Audit Committee, the Nomination and Remuneration Committee.

Our Directors are all reimbursed for any reasonable travel expenses incurred in connection with their attendance at Board meetings or Board committees, they are also eligible to receive share options.

Further information concerning the remuneration of Directors is set out in note 21 to the consolidated financial statements, on page 66.

Directors' contracts

The service agreement with Dr Jalal Bagherli, executive Director, dated 19 July 2005, is of unlimited duration. The agreement may be terminated by either party on six months' notice.

Performance graph

Details are set out on page 7 of this report.

Share options

Details are set out in note 21 to the consolidated financial statements, on page 65.

Directors' share interests

Directors' beneficial interests (as defined by the Companies Act 1985) in 10 pence Ordinary shares of the Company are set out in note 21c, on page 66, in the notes to the consolidated financial statements.

Directors' remuneration report

Directors' pension arrangements

The Company contributes 9% of the executive Director's basic salary to a pension scheme. There are no pension arrangements for Non-executive Directors.

The compensation of the members of the Board of Directors is as follows:

Name and position	Base salary US$	Buy out US$	Other US$	**Total 2007 US$**	Total 2006 US$	**Directors' holdings at 31 December 2007**	
						Shares	**Options[2]**
Dr Jalal Bagherli[1]	320,192	252,694	57,961	**630,847**	626,324	**454,900**	**434,731**
Chris Burke	40,024		–	**40,024**	19,632	**8,000**	**70,000**
Michael Glover	40,024		–	**40,024**	46,135	**220,000**	**70,000**
Aidan Hughes	50,030		–	**50,030**	58,897	**25,000**	**70,000**
John McMonigall r	45,027		–	**45,027**	41,228	**100,000**	**70,000**
Roland Pudelko	–		–	**–**	370,716	**n/a**	**–**
Gregorio Reyes	55,033		–	**55,033**	56,442	**160,000**	**70,000**
Michael Risman	–		–	**–**	24,540	**n/a**	**–**
Russ Shaw	40,024		–	**40,024**	19,632	**19,891**	**70,000**
Peter Tan	40,024		–	**40,024**	19,632	**30,000**	**70,000**
Jan Tuvfesson	–		–	**–**	34,356	**n/a**	**–**
Peter Weber	40,024		–	**40,024**	41,718	**25,000**	**70,000**
	670,402	**252,694**	**57,961**	**981,057**	**1,359,252**	**1,042,791**	**994,731**

1) Of the amount shown under "other" US$28.817 relates to pension contributions under a defined pension contribution plan. The amount shown under "buy out" relates to a payment in connection with a buy out provision for Dr Bagherli's previous employment. Final payment was made in Q3 2007.

2) For further information see note 21 to the consolidated financial statements on page 65.

Non-executive Directors' terms

All Non-executive Directors are appointed for up to three years by the Board of Directors, subject to any earlier requirements to stand for re-election as required by the Articles of Associations (one-third of the Non-executive Directors must stand for re-election at each AGM). This applies regardless of any terms prescribed in their Directors' contracts.

Share options granted to the executive Director

As of 31 December 2007, Jalal Bagherli, executive Director, held 434,731 options over Ordinary shares which entitle him to acquire the same amount of shares:

Exercise price €	Date of grant	Expiry date	Vesting period	At 31 December 2006	Number of options cancelled	**At 31 December 2007**
2.00	12.09.2005	11.09.2015	4 years	60,000		**60,000**
3.50	12.09.2005	11.09.2015	4 years	60,000		**60,000**
5.00	12.09.2005	11.09.2015	4 years	60,000		**60,000**
6.50	12.09.2005	11.09.2015	4 years	60,000		**60,000**
8.00	12.09.2005	11.09.2015	4 years	60,000		**60,000**
0.10	01.02.2006	18.07.2015	1-44 months	94,063	(10,625)	**83,438**
0.10	01.02.2006	18.07.2015	1-44 months	57,825	(6,532)	**51,293**
				451,888	**(17,157)**	**434,731**

25% of the shares granted with a four-year vesting period may be exercised on 30 September 2006 and in the subsequent three years. There is no performance criteria linked to the exercise of these options.

The shares granted in February 2006 are subject to the achievement of performance and market targets to vest in eight equal semi-annual tranches between 31 March 2006 and 30 September 2009.

Directors' remuneration report

Share options granted to the Non-executive Directors

Each Non-executive Director is entitled to an initial grant of 50,000 options vesting monthly in 48 equal tranches. As soon as possible after the AGM, Non-executive Directors will receive a further 20,000 options vesting over 12 months. Options may be exercised at the market price prevailing at the date of grant. The Non-executive Directors are not subject to performance criteria related to remuneration, including Board membership fees, attendance fees and stock option grants. The stock options granted to Non-executive Directors are not, therefore, subject to the achievement of performance targets.

The share option grants to Non-executive Directors are as follows:

Director	Exercise price €	Date of grant	Expiry date	Vesting period	At 31 December 2006	Number of options granted	**At 31 December 2007**
Chris Burke	1.40	12.07.2006	11.07.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Michael Glover	1.27	19.06.2006	18.06.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Aidan Hughes	1.27	19.06.2006	18.06.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
John McMonigall	1.27	19.06.2006	18.06.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Gregorio Reyes	1.27	19.06.2006	18.06.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Russ Shaw	1.40	12.07.2006	11.07.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Peter Tan	1.40	12.07.2006	11.07.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Peter Weber	1.27	19.06.2006	18.06.2013	48 months	50,000	–	**50,000**
	1.80	10.05.2007	09.05.2014	12 months	–	20,000	**20,000**
Total					**400,000**	**160,000**	**560,000**

Approved by the Board of Directors and signed on its behalf by:

Tim Anderson
Secretary

28 February 2008

Statement of Directors' responsibilities

Statement of Directors' responsibilities

The Directors are responsible for preparing the IFRS Report and Accounts 2006 and the Group and parent company financial statements in accordance with the applicable law and regulations.

Company law requires the Directors to prepare Group and parent company financial statements for each financial year. Under the law the Directors are required to prepare the Group financial statements in accordance with IFRS as adopted by the EU and have elected to prepare the parent company financial statements on the same basis.

The Group and parent company financial statements are required by law and IFRS as adopted by the EU to present fairly the financial position of the Group and the parent company and the performance for that period; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of the Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' report and Directors' remuneration report that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's Website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislations in other jurisdictions.

Responsibility statement

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit and loss of the Group, and the Group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group.

Dr Jalal Bagherli
Chief Executive Officer

Jean-Michel Richard
CFO, Vice President Finance

28 February 2008

Independent Auditors' report

Independent auditors' report to the members of the Board of Directors of Dialog Semiconductor Plc:
We have audited the Group and parent company financial statements (the "financial statements") of Dialog Semiconductor Plc for the year ended 31 December 2007 which comprise the Group income statement, the Group and parent company balance sheets, the Group company cash flow statement, the Group and parent company statement of changes in equity and the related notes 1 to 33. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' remuneration report that is described as having been audited. This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors
The Directors' responsibilities for preparing the Annual Report, the Directors' remuneration report and the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRS) as adopted by the European Union are set out in the statement of Directors' responsibilities. Our responsibility is to audit the financial statements and the part of the Directors' remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the Group financial information, Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' report is consistent with the financial statements. The information given in the Director's report includes that specific information presented in the operating and financial review that is cross referred from the business review section of the Directors' report. In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions are not disclosed. We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the unaudited part of the Directors' remuneration report, the Chairman's statement, the operating and financial review and the Corporate Governance statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' remuneration report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' remuneration report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' remuneration report to be audited.

Opinion
In our opinion:
- the Group financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the Group's affairs as at 31 December 2007 and of its loss for the year then ended;
- the parent company financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2007;
- the financial statements and the part of the Directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Directors' report is consistent with the financial statements.

Ernst & Young LLP
Registered auditor
Reading

12 March 2008

Consolidated income statement

For the year ended 31 December 2007

	Notes	2007 US$000	2006 US$000
Revenues	24	**86,773**	93,938
Cost of sales		**(57,812)**	(76,435)
Gross profit		**28,961**	17,503
Sales and marketing expenses		**(7,253)**	(7,190)
General and administrative expenses		**(7,945)**	(17,644)
Research and development expenses	24	**(31,105)**	(27,529)
Other operating income		**1,190**	–
Net restructuring and related impairment charges	4	**(1,120)**	(6,115)
Operating loss	24	**(17,272)**	(40,975)
Impairment of investments	15	**(2,662)**	–
Interest income	5	**1,053**	1,356
Interest expense	5	**(84)**	(204)
Foreign currency exchange gains and losses		**519**	(2,084)
Other financial income	5	**44**	–
Other financial expenses	5	**(447)**	–
Result before income taxes		**(18,849)**	(41,907)
Income tax benefit (expense)	6	**(136)**	158
Net loss from continuing operations		**(18,985)**	(41,749)
Loss from discontinued operations	3	**–**	(2,267)
Net loss		**(18,985)**	(44,016)

		2007	2006
Net loss per share			
Basic and diluted		**(0.42)**	(0.99)
Net loss per share from continuing operations			
Basic and diluted		**(0.42)**	(0.94)
Weighted average number of shares (in US$000)			
Basic and diluted	2	**44,938**	44,549

Consolidated balance sheet

As at 31 December 2007

	Notes	At 31 December 2007 US$000	At 31 December 2006 US$000
Assets			
Cash and cash equivalents	7	**15,923**	32,032
Available-for-sale financial assets	8	**15,921**	19,351
Trade accounts receivable and other receivables	9	**2,569**	4,666
Inventories	10	**17,051**	7,459
Other financial assets	11	**336**	–
Other current assets		**1,866**	1,938
		53,666	65,446
Non-current assets classified as held for sale	4	**–**	1,393
Total current assets		**53,666**	66,839
Property, plant and equipment, net	12	**10,452**	12,417
Intangible assets	13	**2,443**	1,579
Held to maturity securities	14	**4,000**	–
Investments	15	**–**	1,620
Deposits		**209**	231
Assets for current tax	6	**453**	443
Total non-current assets		**17,557**	16,290
Total assets		**71,223**	83,129
Liabilities and Shareholders' equity			
Trade and other payables	16	**14,735**	9,109
Provisions	17	**978**	1,430
Income taxes payable		**40**	28
Other current liabilities	18	**1,778**	1,893
Total current liabilities		**17,531**	12,460
Ordinary shares		**9,328**	9,328
Additional paid-in capital		**222,914**	222,781
Accumulated deficit		**(177,844)**	(159,764)
Other reserves		**(501)**	(1,444)
Employee stock purchase plan shares		**(205)**	(232)
Net Shareholders' equity	19	**53,692**	70,669
Total liabilities and Shareholders' equity		**71,223**	83,129

Consolidated statements of cash flows

For the year ended 31 December 2007

	Notes	2007 US$000	2006 US$000
Cash flows from operating activities:			
Net loss		**(18,985)**	(44,015)
Adjustments to reconcile net loss to net cash provided by (used for) operating activities:			
Interest income, net		**(969)**	(1,152)
Other income tax expense	6	**136**	(158)
Impairment of inventories		**937**	7,899
Impairment of trade accounts receivable		**–**	2,644
Impairment of investment	15	**2,662**	–
Depreciation of property, plant and equipment	12	**5,486**	7,087
Amortisation of intangible assets	13	**900**	3,883
Losses on disposals of fixed assets and impairment of fixed and financial assets		**743**	1,472
Expense related to share-based payments	21	**905**	1,157
Restructuring and related impairment charges	4	**332**	5,473
Changes in working capital:			
Trade accounts receivable and other receivables	9	**(6,816)**	30,042
Factoring	25	**8,913**	–
Inventories		**(10,529)**	7,254
Prepaid expenses		**(321)**	154
Trade accounts payable		**6,290**	(5,814)
Provisions		**(461)**	(175)
Other assets and liabilities		**(496)**	(874)
Cash generated from (used for) operations		**(11,273)**	14,877
Interest paid		**(76)**	(8)
Interest received		**1,153**	1,410
Income taxes paid		**(53)**	(48)
Cash flow from (used for) operating activities		**(10,249)**	16,231
Cash flows from investing activities:			
Sale of property, plant and equipment		**1,081**	–
Purchases of property, plant and equipment	12	**(4,146)**	(3,733)
Purchases of intangible assets	13	**(1,100)**	(1,333)
Payments for capitalised development costs	13	**(724)**	–
Investments and deposits made		**(1,021)**	(1,564)
Purchase of securities	8, 11, 14	**(26,621)**	–
Sale of securities	8	**26,471**	–
Cash used for investing activities		**(6,060)**	(6,630)
Cash flows from financing activities:			
Sale of employee stock purchase plan shares		**159**	279
Cash flow from financing activities		**159**	279
Cash flow from (used for) operating, investing and financing activities		**(16,150)**	9,880
Effect of foreign exchange rate changes on cash and cash equivalents		**41**	(150)
Net increase (decrease) in cash and cash equivalents		**(16,109)**	9,730
Cash and cash equivalents at beginning of period		**32,032**	22,302
Cash and cash equivalents at end of period		**15,923**	32,032

Consolidated statement of changes in Shareholders' equity

For the year ended 31 December 2007

	Ordinary shares US$000	Additional paid-in capital US$000	Accumulated deficit US$000	Other reserves: Currency translation adjustment US$000	Other reserves: Derivative financial instruments US$000	Other reserves: Available-for-sale securities US$000	Employee stock purchase plan shares US$000	Total US$000
Balance at 1 January 2006	9,328	222,600	(116,906)	(1,075)	–	(394)	(331)	113,222
Net loss	–	–	(44,015)	–	–	–	–	(44,015)
Other comprehensive income (loss)	–	–	–	53	–	(28)	–	25
Total comprehensive loss	–	–	(44,015)	53	–	(28)	–	(43,990)
Sale of employee stock purchase plan shares	–	181	–	–	–	–	99	280
Equity settled transactions, net of tax	–	–	1,157	–	–	–	–	1,157
Changes in equity total	–	181	(42,858)	53	–	(28)	99	(42,553)
Balance at 31 December 2006/ 1 January 2007	9,328	222,781	(159,764)	(1,022)	–	(422)	(232)	70,669
Net loss	–	–	(18,985)	–	–	–	–	(18,985)
Other comprehensive income (loss)	–	–	–	120	89	734	–	943
Total comprehensive loss	–	–	(18,985)	120	89	734	–	(18,042)
Sale of employee stock purchase plan shares	–	133	–	–	–	–	27	160
Equity settled transactions, net of tax	–	–	905	–	–	–	–	905
Changes in equity total	–	133	(18,080)	120	89	734	27	(16,977)
Balance at 31 December 2007	**9,328**	**222,914**	**(177,844)**	**(902)**	**89**	**312**	**(205)**	**53,692**

Notes to the consolidated financial statements

For the year ended 31 December 2007

1. General

Basis of presentation

The accompanying consolidated financial statements have been prepared on the basis of the recognition and measurement requirements of IFRS and its interpretation adopted by the EU. Based on these standards, management has applied the accounting policies as set out below.

After completing the transfer of the Wafer Test, Final Test and Tape & Reel operations from the largest company within the Group in Kirchheim/Teck, Germany, to subcontractors in the Far East, all the manufacturing costs of the producing companies within the Group became US dollar denominated. The transfer of these activities was also considered a trigger for changing the functional currency of the largest company within the Group from euros to US dollars. With all significant companies within the Group having the US dollar as their functional currency, the Group changed its presentation currency from euros to US dollars effective from 1 January 2007.

The financial statements are now presented in US dollars ("US$") except when otherwise stated. All prior period numbers, including amounts presented in the balance sheet, the income statement, the cash flow statement, the statement of changes in Shareholders' equity and all notes were translated at the year-end exchange rate as of 31 December 2006 (1€ = US$1.3181). The resulting translated amounts for non-monetary items are treated at their historical cost.

The financial statements are prepared on the historical cost basis except that financial instruments classified as available-for-sale and derivative financial instruments are stated at their fair value.

A summary of significant accounting policies is provided in note 2.

The consolidated financial statements for the year ended 31 December 2007 were authorised for issue in accordance with a resolution of the Directors on 28 February 2008.

2. Summary of significant accounting policies

Principles of consolidation and investments in affiliated companies

The consolidated financial statements include Dialog Semiconductor Plc and its subsidiaries as at 31 December each year:

Name	Registered office	Participation
Dialog Semiconductor GmbH	Kirchheim/Teck, Germany	100%
Dialog Semiconductor (UK) Limited	Swindon, UK	100%
Dialog Semiconductor, Inc.	Wilmington, Delaware, USA	100%
Dialog Semiconductor KK	Tokyo, Japan	100%
Dialog Semiconductor GmbH, Taiwan Branch	Taipei, Taiwan	100%

Subsidiaries are fully consolidated from the date of acquisition, being the date on which Dialog Semiconductor Plc obtains control, and continues to be consolidated until the date such control ceases.

The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intra-group balances, income and expenses, and unrealised gains and losses resulting from intra-Group transactions are fully eliminated.

Foreign exchange

The functional currency for the Company's operations is generally the currency in which it primarily generates and expends cash. Each entity in the Group determines its own functional currency. Accordingly, the assets and liabilities of companies whose functional currency is other than the US dollar are included in the consolidation by translating the assets and liabilities into the reporting currency (US$) 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.

Notes to the consolidated financial statements

For the year ended 31 December 2007

2. Summary of significant accounting policies continued

Transactions in a foreign currency are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to profit and loss with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal of the net investment at which time they are recognised in profit or loss. Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. Foreign currency transaction gains and losses are disclosed separately in the income statement, at each reporting period. Regarding the change in the functional currency please see note 1. Key exchange rates against US dollars used in preparing the consolidated financial statements were:

	Exchange rate at		Annual average exchange rate	
Currency	**31 December 2007 US$1 =**	31 December 2006 US$1 =	**2007 US$1 =**	2006 US$1 =
Great Britain	**0.50**	0.50	**0.50**	0.51
Japan	**112.12**	118.84	**117.78**	110.78
Euro	**0.68**	0.76	**0.73**	0.79

Financial instruments

A financial instrument is any contract that gives rise to a financial asset in one entity and a financial liability or equity instrument in another. Financial assets include, in particular, cash and cash equivalents, trade receivables and other originated loans and receivables, held-to-maturity investments and derivative and non-derivative financial assets held for trading, as well as investments available for sale. Financial liabilities generally substantiate claims for repayment in cash or another financial asset. In particular, this includes trade payables, liabilities to banks and derivative financial liabilities. In general, financial assets and financial liabilities are offset and the net amount presented in the balance sheet when, and only when, the entity currently has a right to set off the recognised amounts and intends to settle on a net basis.

Investments and other financial assets

Financial assets within the scope of IAS 39 are classified as being at fair value through profit or loss, loans and receivables, held-to-maturity investments or available-for-sale financial assets, as appropriate. When financial assets are first recognised, they are measured at fair value, plus, in case of investments not at fair value through profit or loss, directly attributable transaction costs.

The Company determines the classification of its financial assets on first recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

All regular purchases and sales of financial assets are recognised on the settlement date, which is the date that the Group receives the asset. Regular purchases or sales are classified as purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention of the market place.

At each balance sheet date, the Group assesses whether a financial asset or group of financial assets is impaired.

Cash and cash equivalents

Cash and cash equivalents include highly-liquid investments with original maturity dates of three months or less and are subject to an insignificant risk of changes in value.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as loans and receivables, held-to-maturity investments or as financial assets at fair value through profit or loss. These financial assets are generally measured at fair value.

After initial measurement available-for-sale financial assets are measured at fair value. Unrealised gains and losses, net of the related tax effect, on available-for-sale financial assets are excluded from earnings and are reported as a component of other reserves until realised, or the investment is determined as being impaired.

2. Summary of significant accounting policies continued

At each reporting date, the carrying amounts of available-for-sale assets are assessed to determine whether there is objective, significant evidence of impairment as outlined in IAS 39.59. Any impairment losses on available-for-sale financial assets are charged to earnings. The Group does not use allowance accounts in order to record the impairment in the balance sheet but credits the impairment loss directly against the book value of the financial assets. If this impairment relates to losses previously recognised in equity then the impairment loss is transferred from equity to the income statement. Reversals of impairment losses in respect of equity instruments or investment funds that are classified as available for sale and are not recognised in profit or loss. Reversals of impairment losses on debt instruments are reversed through profit or loss if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

The fair value of available-for-sale financial assets actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments in which there is no active market, fair value is determined using valuation techniques, including recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; discounted cash flow analysis; or other valuation models. If the fair value of unquoted equity instruments cannot be measured with sufficient reliability, these instruments are measured at cost (less any impairment losses, if applicable).

Financial assets held-to-maturity

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Company has the positive intention and ability to do so. After initial measurement, held-to-maturity investments are measured at amortised cost using the effective interest method. The effective interest method takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Gains and losses are recognised in profit or loss when the investments are de-recognised or impaired, as well as through the amortisation process.

The carrying amount of financial assets held-to-maturity are tested at each reporting date to determine whether there is objective, material evidence of impairment as outlined in IAS 39.59. Any impairment losses caused by the fair value being lower than the carrying amount are recognised in profit or loss. The Group does not use allowance accounts in order to record the impairment in the balance sheet but credits the impairment loss directly against the book value of the financial assets. If in a subsequent period the fair value increases and this increase can be related objectively to events occurring after the impairment was recognised, the impairment loss is reversed to income in the appropriate amount. The fair value which is required for impairment testing corresponds to the present value of the estimated future cash flows discounted using the original effective interest rate.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market, such as trade account receivables. Loans and receivables are recorded at fair value. As of 31 December 2007 as well as 31 December 2006, loans and receivables comprise mostly trade accounts receivables from customers. After initial recognition, loans and receivables are subsequently carried at amortised cost using the effective interest method, less any allowance for impairment, if necessary.

Gains and losses are recognised in the income statement when the loans and receivables are de-recognised or impaired. Interest effects on the application of the effective interest method are also recognised in profit or loss.

The Company continuously reviews its allowance for doubtful accounts. Management considers the collectability 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, based on current information and events regarding the customers' ability to meet their obligations. The amount of the impairment loss on loans and receivables is measured as the difference between the carrying amount of the asset and the present value of estimated future cash flows, discounted at the original effective interest rate of the financial asset. The amount of the impairment loss is recognised in profit or loss.

If, in a subsequent reporting period, the amount of the impairment loss decreases, and the decrease can objectively be related to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed and recognised in profit or loss.

When a trade receivable is considered to be impaired, any credit losses are included in the allowance for doubtful accounts through a charge to bad debt expense. Account balances are set off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Recoveries of trade receivables previously written-off are recorded when received. Reversals of impairment losses are recognised in profit and loss. The Company does not have any off-balance sheet credit exposure related to its customers.

Receivables from work in process for customer specific development projects according to IAS 11 are recorded in the balance sheet line "trade account receivables and other receivables" and are disclosed in the notes respectively.

Notes to the consolidated financial statements

For the year ended 31 December 2007

2. Summary of significant accounting policies continued

De-recognition of financial assets

A financial asset is de-recognised when:

- the right to receive cash flows from the asset have expired;
- the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass through agreement"; or
- the Company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Company has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset, nor transferred control of the asset, the asset is recognised to the extent of the Company's continuing involvement in it.

Inventories

Inventories include assets held for sale in the ordinary course of business (finished goods), in the process of production (work in process) or in the form of materials to be consumed in the production process (raw materials). Inventories are valued at the lower of cost and net realisable value. Cost, which includes direct materials, labour and overhead, plus indirect overhead, is determined using the first-in, first-out (FIFO) method. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and estimated costs to make the sale.

Non-current assets held for sale

Assets that meet the criteria of IFRS 5 are classified as held for sale if the carrying amount will be recovered principally through a sale transaction rather than through continuing use. The assets are available for immediate sale and the sale is highly probable. The assets have been accounted for at the lower of the carrying amount and the estimated fair value, less costs to sell.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. These include the cost of replacing part of the plant and equipment when that cost is incurred, if the recognition criteria are met. Depreciation is charged on a straight-line basis over the estimated useful lives of the assets as follows:

Equipment	Useful life
Test equipment	Three to eight years
Leasehold improvements	Shorter of useful life or lease term
Office and other equipment	18 months to 13 years

The asset's residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end.

Intangible assets

Purchased intangible assets with definite useful lives primarily consist of licences, software and patents, and are recorded at acquisition cost less accumulated amortisation and accumulated impairment losses. Intangible assets are amortised on a straight-line basis over the estimated useful lives of three to five years. For a particular software licence a useful life of ten years was estimated. Amortisation expenses are allocated to the cost of goods sold, selling expenses, research and development expenses, or general administration expenses. The Company has no intangible assets with an indefinite useful life.

Self-developed intangible assets are recorded on a cost basis. They are amortised on a straight-line basis over the estimated usefulness of 18-24 months. Please also refer to the research and development costs section.

Impairment of non-monetary assets

In accordance with IAS 36, at each reporting date an assessment is made as to whether there is an indication that a non-monetary asset, such as property, plant and equipment or purchased intangibles, may be impaired. If any such indication exists, an estimate is made of the asset's recoverable amount: the higher of an asset's fair value, less cost to sell and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value, using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining the fair value less costs to sell, an appropriate valuation model is used.

2. Summary of significant accounting policies continued

For assets, an assessment is made at each reporting date as to whether any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, an estimation of the recoverable amount is made. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount, however, cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in profit or loss unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. As of 31 December 2007 and 2006 no non-monetary assets have been accounted for using a fair value model.

Financial liabilities

Financial liabilities primarily include trade accounts payable, liabilities due to banks, derivative financial liabilities and other liabilities.

Financial liabilities measured at amortised costs

After initial recognition at fair value, less directly attributable transaction costs, financial liabilities are subsequently measured at amortised cost using the effective interest method.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss. Derivatives, including separated embedded derivatives are also classified as held for trading and, therefore, accounted for at fair value through profit or loss unless they are designated as effective hedging instruments. Gains and losses on liabilities held for trading are recognised in profit or loss.

During the financial years 2007 and 2006 the Company did not classify any financial liabilities as financial liabilities at fair value through profit or loss.

De-recognition of financial liabilities

A financial liability is de-recognised when the obligation under the liability is discharged, cancelled or expires.

Derivative financial instruments and hedge accounting

The Company uses derivative financial instruments, such as forward contracts, mainly for the purposes of hedging currency risks that arise from its operating activities. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value on each subsequent reporting date. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains and losses arising from changes in the fair value on derivatives during the year that do not qualify for hedge accounting are taken directly to profit or loss.

The fair value of quoted derivatives is equal to their positive or negative market value. The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group first becomes party to the contract. Reassessment occurs only if there is a change in the terms of the contract that significantly modify the cash flows that would otherwise be required.

If the requirements for hedge accounting set out in IAS 39 are met, the Company designates and documents the hedge relationship from the date a derivative contract is entered into, either as a fair value hedge or a cash flow hedge.

The Company did not enter into fair value hedges in 2007 and 2006.

In a cash flow hedge, the variability of cash flows to be received or paid related to a recognised asset or liability, or a highly probable forecast transaction, or a firm commitment (in case of currency risks) is hedged. To hedge a currency risk of an unrecognised firm commitment, the Company makes use of the option to recognise this as a cash flow hedge rather than a fair value hedge. The documentation of the hedge relationship includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in cash flows, and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Notes to the consolidated financial statements

For the year ended 31 December 2007

2. Summary of significant accounting policies continued

For cash flow hedges, fair value changes of the effective portion of the hedging instrument are recognised in other reserves, net of applicable taxes, while any ineffective portion of the fair value changes are recognised immediately in profit or loss. Amounts taken to equity are transferred to the income statement when the hedged transaction affects the income statement, such as when the forecast or committed expenses occur. If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognised in equity are transferred to profit or loss.

If the derivative instrument does not, or no longer, qualifies for hedge accounting because the qualifying criteria for hedge accounting are not, or are no longer, met the derivative financial instruments are classified as held for trading. Amounts previously recognised in equity are transferred to profit or loss.

If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction or the firm commitment occurs.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

For arrangements entered into before 1 January 2005, the date of inception is deemed to be 1 January 2005 in accordance with the transitional requirements of IFRIC 4.

Where the Group is lessee, finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are reflected in profit and loss. As of 31 December 2007 and 2006 the Group had no finance lease arrangements. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

Where the Group is lessor and the Group does not transfer substantially all the risks and benefits of ownership of the asset to the lessee, the lease is classified as an operating lease. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised over the leased term on the same bases as rental income. Contingent rents are recognised as revenue in the period in which they are earned. As of 31 December 2007 and 2006 the Group had no lease arrangements as lessor.

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and other sales taxes or duty. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods

Revenue from the sale of goods is derived from the sale of products, application specific integrated circuit ("ASIC") and application specific standard product ("ASSP") to end customers. These products are manufactured and tested in accordance with customers' technical specifications prior to delivery. Revenue is recognised when title passes, the risks and rewards of ownership have been transferred to the customer, the fee is fixed or determinable, and collection of the related receivable is probable. Revenues are recorded net of sales taxes and customer discounts, if any.

The Company has insurance for product claims and also records a provision for warranty costs as a charge in cost of sales, based on historical trends of warranty costs incurred as a percentage of sales, which management has determined to be a reasonable estimate of the probable costs to be incurred for warranty claims in a period. Customer returns are permitted only for quality-related reasons within the applicable warranty period and any potential warranty claims are subject to the Company's determination that it is at fault for damages. Such claims must usually be submitted within a short period of the date of sale.

Research and development

Revenue from customer-specific research and development contracts involving the development of new customer-specific technology is recognised on the percentage of completion basis when the outcome of the contract can be estimated reliably. A contract's outcome can be estimated reliably when total contract revenue can equally be estimated, it is probable that economic benefits associated with the contract will flow to the Company, and the stage of contract completion can be measured reliably. When the Company is not able to meet those conditions, the policy is to recognise revenues only to costs incurred to date, to the extent that such costs are expected to be recovered. Completion is measured by reference to costs incurred to date as a percentage of estimated total project costs. The percentage of completion method relies on estimates of total expected contract revenue and costs, as well as the dependable measurement of the progress made towards completing the particular project. Losses on projects in progress are recognised in the period they become likely and can be estimated.

2. Summary of significant accounting policies continued

Cost of sales

Cost of sales consists of the costs of outsourcing production, assembly and test, personnel costs and applicable overheads and depreciation of equipment. Provisions for estimated product warranties are recorded in cost of sales at the time the related sale is recognised.

Sales and marketing expenses

Sales and marketing expenses consist primarily of salaries, travel expenses, sales commissions, bad debt expenses and costs associated with advertising and other marketing activities.

General and administrative expenses

General and administrative expenses consist primarily of personnel and support costs for finance, human resources, information systems and other management departments which are not attributable to development, production or sales functions. In 2006, the impairment of accounts receivable and inventories related to the insolvency of BenQ Mobile GmbH ("BenQ") was also recorded in general and administrative expenses.

Research and development costs

Costs identified as research costs are expensed as incurred, whereas development costs are capitalised as an intangible asset and amortised if the Company can demonstrate the following:

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

Interest income/expense

Interest income is recognised as interest accrues. Interest income includes interest income from investments in securities, cash and cash equivalents. Income and expense resulting from the allocation of premiums and discounts is also included. Interest expense is expensed as incurred.

Foreign currency exchange gains and losses

The foreign currency exchange gains and losses mainly result from foreign currency cash transactions and period end revaluation of foreign currency denominated cash into US dollars (2006: into euros). It is the Company's view that these gains and losses are driven by the financing activities of the Company and are therefore shown in the financial result.

Other financial income/expense

Other financial income/expense includes all remaining miscellaneous income and expense from financial transactions which are not included in interest income/expense.

Employee benefits – defined contribution plans

Obligations for contributions to defined contribution and state-funded pension plans are recognised in the income statement as expense as incurred.

Income taxes

Current income taxes for current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

Deferred tax assets and liabilities are accounted for using the liability method and are recognised for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities, and their respective tax bases, as well as on the carry-forward of unused tax losses that can be utilised.

Notes to the consolidated financial statements

For the year ended 31 December 2007

2. Summary of significant accounting policies continued

Deferred tax assets and liabilities are measured using tax rates that have been enacted, or substantially enacted, by the balance sheet date expected to apply to taxable income in the years, in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognised in income in the period that includes the enactment date.

A deferred tax asset is recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Unrecognised deferred income tax assets are reassessed at each balance sheet date and are recognised to the extent, that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists, to set off current tax assets against current tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Share-based payments

The Company has established an equity-settled share option scheme under which employees and Directors may be granted stock options to acquire shares of the Company.

The fair value of options granted is recognised as a compensation expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the service period during which the employees become unconditionally entitled to the options.

The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date, reflects the extent to which the vesting period has expired and the best estimate of the number of equity instruments that will ultimately vest. The income statement charge or credit for a period represents the movement in cumulative expense in the period.

The fair value of the options granted is measured using the Black-Scholes option pricing model, taking into account the terms and conditions on which the options were granted. Expectations of early exercise are accounted for within the average life of the options. The Company applies IFRS 2 to all options granted after 7 November 2002 that had not been vested as of 1 January 2005.

Employee share trust

The Company has established an employee share trust. The share trust is separately administrated and is funded by the Company, which consolidates the assets, liabilities, income and expenses in its own accounts. The shares held by the trust are recorded at cost and are shown under "Employee stock purchase plan shares" in the statement of changes in Shareholders' equity.

Loss per share

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 two periods presented, only basic per share amounts have been presented for those periods. Had the Company reported net income in 2007 and 2006, the weighted average number of shares outstanding would have been as follows:

	2007	2006
Basic number of shares	**44,938**	44,549
Effect of dilutive options outstanding	**2,015**	1,512
Dilutive number of shares	**46,953**	46,061

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 expenses during the reporting period.

2. Summary of significant accounting policies continued

Subject to such estimates and judgements is the following:

Impairment of non-financial assets

The Group assesses whether there are any indicators of impairment for all non-financial assets at each reporting date. In case of such an indicator, an impairment test is made. This requires the determination of the value in use and the fair value less costs to sell respectively of the assets. Estimating the value in use requires management to make an estimate of the expected future cash flows from the asset and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of such assets including assets held for sale at 31 December 2007 was US$12,895,000 (2006: US$17,009,000). Further information regarding impairment charges is provided in notes 4 and 12.

Impairment of available-for-sale financial assets and investments

The Group classifies certain assets as available-for-sale and recognises movements in the fair value in equity. When the fair value declines, management makes assumptions about the decline in value to determine whether it is an impairment that should be recognised in profit or loss.

Impairment losses on investments amounting to US$2,662,000 have been charged to profit and loss in 2007 (2006: US$nil). The carrying amount of these unquoted equity instruments at 31 December 2007 was US$nil (2006: US$1,620,000). Please see note 15.

Deferred tax assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing of future taxable profits, together with future tax planning strategies. At year end 2007 and 2006, no deferred tax assets were recognised. The unrecognised deferred tax assets at 31 December 2007 were US$58,675,000 (2006: US$63,090,000). Further information regarding the assessment of future taxable income is disclosed in note 6.

Share-based employee compensation awards

Share-based payment transactions are measured by reference to the fair value at the date on which they are granted. The fair value of share-based payments is determined using the Black-Scholes model, which involves making assumptions about interest rates, volatilities, market conditions and fluctuation. Due to the nature of these assumptions, such estimates are subject to significant uncertainty. In 2007, the expense related to stock options was US$905,000 (2006: US$1,157,000).

Customer-specific research and development

For the determination of revenue and costs for customer specific research and development contracts, management judgement is required. It is, therefore, necessary to determine the stage of completion based on the progress made towards completing the particular project, as well as the contract revenue and the contract costs. At 31 December 2007 no receivables from constructions contracts were outstanding (2006: US$nil).

Self-developed intangible assets

Development costs are capitalised in accordance with the accounting policy mentioned above. Initial capitalisation of costs is based on management's judgement that technological and economical feasibility is confirmed, usually when a product development project has reached a defined milestone according to an established project management model. In determining the probable future economic benefits of the self-developed intangible asset, management makes assumptions regarding the expected future cash generation of the assets, discount rates to be applied and the expected period of benefits. At 31 December 2007, the best estimate of the carrying amount of capitalised development costs was US$597,000 (2006: US$nil).

Actual results may differ from those estimates.

Changes in accounting policies

The accounting policies are consistent with those of the previous financial year except as follows:

The Company has adopted the following new and amended IFRS and IFRIC interpretations during the year.

IFRS 7 Financial Instruments Disclosures

In August 2005, the IASB issued IFRS 7 "Financial Instruments: Disclosures". IFRS 7 introduces new requirements to improve the information on financial instruments that is given in entities' financial statements, and changes or amends certain disclosure requirements. It replaces IAS 30 "Disclosures in the Financial Statements of Banks and Similar Financial Institutions" and some of the requirements in IAS 32, "Financial Instruments: Disclosure and Presentation". IFRS 7 is effective for annual periods beginning on or after 1 January 2007. As a result of the first-time adoption of IFRS 7, additional disclosure within the notes to the consolidated financial statements has been prepared.

Notes to the consolidated financial statements

For the year ended 31 December 2007

2. Summary of significant accounting policies continued

IAS 1 Presentation of Financial Statements

In August 2005, the IASB issued a complementary amendment to IAS 1 "Presentation of Financial Statements – Capital Disclosures". The amendment to IAS 1 adds requirements for all entities to disclose the entity's objectives, policies and processes for managing capital and is effective for annual periods beginning on or after 1 January 2007. As a result of the first-time adoption of this amendment to IAS 1, additional disclosure within the notes to the consolidated financial statements has been prepared.

IFRIC 7 Applying the Restatement Approach Under IAS 29

IFRIC 7 is effective for annual periods beginning on or after 1 March 2006 and provides guidance on how to apply the requirements of IAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional currency, when that economy was not hyperinflationary in the prior period, and the entity therefore restates its financial statements in accordance with IAS 29. The interpretation had no impact on the financial position or performance of the Company as none of its Group companies is located in an economy with hyperinflation.

IFRIC 8 Scope of IFRS 2

This interpretation is effective for the annual period beginning on or after 1 May 2006, and requires IFRS 2 to be applied to any arrangements in which the entity cannot identify specifically some or all of the goods received, in particular where equity instruments are issued for consideration which appears to be less than fair value. As equity instruments are issued only to employees in accordance with the employee share scheme, the interpretation had no impact on the financial position or performance of the Company.

IFRIC 9 Reassessment of Embedded Derivatives

IFRIC 9 is effective for financial years beginning on or after 1 June 2006, and establishes that the date to assess the existence of an embedded derivative is the date on which an entity first becomes party to the contract, with reassessment only if there is a change that significantly modifies the cash flow. The adoption of this interpretation did not have any effect on the financial statements of the Company.

IFRIC 10 Interim Financial Reporting and Impairment

IFRIC Interpretation 10 is effective for annual periods beginning on or after 1 November 2006. The interpretation addresses the apparent conflict between the requirements of IAS 34 Interim Financial Reporting and those in other standards on the recognition and reversal in financial statements of impairment losses on goodwill and certain financial assets. The adoption of this interpretation did not have any effect on the financial statements of the Company.

Recently issued accounting standards not yet adopted

IFRS 2 Share-Based Payments

The amended IFRS 2 was issued in January 2008 and is effective for financial years beginning on or after 1 January 2009. The amendment deals with two matters. It clarifies that vesting conditions are service conditions and performance conditions only. Other features of a share-based payment are not vesting conditions. It also specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The amended standard has not yet been endorsed by the EU. The Company does not expect material changes in its accounting due to this amended IFRS.

IFRS 3 Business Combinations (revised) and IAS 27 Consolidated and Separate Financial Statements (amended)

The revised IFRS 3 and the amended IAS 27 were issued in January 2008 and are effective for annual periods beginning on or after 1 July 2009. The changes made to the existing standards are comprehensive and mainly address the accounting for acquisition costs, contingent considerations, goodwill and non-controlling interests, step acquisitions, partial disposal of an investment while a controlling interest is retained or control is lost, and acquisition of additional shares after control is obtained. The revised and amended standards have not yet been endorsed by the EU.

IFRS 8 Operating Segments

IFRS 8 Operating Segments which replaces IAS 14 Segment Reporting was issued in November 2006 and is effective for annual periods beginning on or after 1 January 2009. The IFRS requires an entity to adopt the "management approach" to reporting on the financial performance of its operating segments. Generally, the information to be reported would be what management uses internally for evaluating segmental performance and deciding how to allocate resources to operating segments. The Company does not expect that the operating segments would significantly differ from the business segments identified under IAS 14 Segment Reporting. Additional disclosures about each of these segments are expected. The Company has not yet, however, finally assessed the impact of the adoption of IFRS 8 on its segmental reporting.

2. Summary of significant accounting policies continued

IAS 1 Presentation of Financial Statements – Revised

The revised IAS 1 was issued in September 2007 and is effective for periods beginning on or after 1 January 2009. The changes made are to require information in financial statements to be aggregated on the basis of shared characteristics and to introduce a statement of comprehensive income. The revised standard gives preparers of financial statements the option of presenting items of income and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements. The Company has not yet finally assessed the impact of the adoption of the revised IAS 1 on its financial statements presentation. The revised standard has not yet been endorsed by the EU.

IAS 23 Borrowing Costs

The revised IAS 23 Borrowing Costs was issued in March 2007 and is effective for periods beginning on or after 1 January 2009. The revised standard removes the option of immediately recognising borrowing costs, that relate to assets that take a substantial period of time to get ready for use or sale, as an expense. Following this revised standard, the Company will change its currently adopted policy of immediately expensing borrowing costs. The revised standard has not yet been endorsed by the EU.

In addition, the following interpretations have been issued:

Interpretation	Title	Effective date
IFRIC 11	Group and Treasury Share Transactions	1 March 2007
IFRIC 12	Service Concession Agreements	1 January 2008
IFRIC 13	Customer Loyalty Programmes	1 July 2008
IFRIC 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	1 January 2008

Only IFRIC 11 has, so far, been endorsed by the EU.

The above-listed interpretations did not, and will not, have an effect on the financial statements as they do not currently apply to the Company. We do not intend to make early application and interpretation of the above, not yet effective standards.

Reclassification

In order to fulfil the requirements of IFRS 7, particularly the separation of financial instruments into classes, some financial assets and liabilities have been reclassified. Prior year numbers have been adjusted accordingly.

3. Discontinued operations

On 14 February 2006 the Company concluded the disposal of its Imaging Division. The business of this division included the development, design, manufacture, assembly, marketing and delivering of image sensor semiconductors and camera modules. Dialog transferred the assets of the Division to a newly-created entity, Dialog Imaging Systems GmbH (“DIS”), subsequently renamed Digital Imaging Systems GmbH. For further information regarding DIS, please see note 15.

The losses from discontinued operations of US$2,267,000 in 2006 solely comprise of operating losses incurred before control was legally transferred on 14 February 2006 and include transaction and legal costs. In the statements of cash flows, the relating cash flow of US$2,267,000 is classified as cash used for operations. In February 2007 DIS officially changed its company name to Digital Imaging Systems.

Notes to the consolidated financial statements

For the year ended 31 December 2007

4. Restructuring and related impairment charges

In the third quarter of 2006 the Company decided to transfer its "Wafer Test", "Final Test" and "Tape & Reel" operations from Kirchheim/Teck, Germany to dedicated outsourced assembly and test organisations in Asia. This transfer was completed in the second quarter of 2007 and, as a result, in the fourth quarter of 2007, the Company announced a further reduction of its workforce in Germany.

The 2006 restructuring and related impairment charges in connection with the transfer of the test operation mainly comprise employee termination costs (US$1,568,000) and impairment charges (US$4,105,000). The 2007 restructuring charges mainly comprise further employee termination costs (net of US$421,000), impairment charges and other losses (US$687,000) in relation to obsolete assets resulting from the transfer and gains from the sale of excess assets (US$355,000).

By 31 December 2007, any assets previously classified as "held for sale" were either sold, disposed of or returned to production when new information was received that these assets could be used. Therefore, at 31 December 2007, non-current assets classified as "held for sale" amount to zero.

When assets were returned to production, the Company ceased to classify the asset as "held for sale". Assets were valued at the lower of:

a) their carrying amount before the asset (or disposal group) was classified as held for sale, adjusted for any depreciation, amortisation or revaluations that would have been recognised had the asset (or disposal group) not been classified as held for sale; and
b) their recoverable amount at the date of the subsequent decision not to sell.

The following table shows the composition of the restructuring reserve, restructuring expenses and gains and related cash flows.

	Workforce reduction US$000	Fixed assets US$000	Other costs US$000	Total US$000
Reserve balance at 1 January 2006	–	–	–	–
Restructuring expenses				
Initial charges	1,568	4,370	1	5,939
Additional charges	152	538	289	979
Reversal of impairment	–	(803)	–	(803)
Total restructuring expenses	1,720	4,105	290	6,115
Payments made	(356)	–	(290)	(646)
Amount charged against current and non-current assets	–	(4,105)	–	(4,105)
Reserve balance at 31 December 2006/1 January 2007	1,364	–	–	1,364
Restructuring expenses				
Additional charges	587	687	367	1,641
Gains from sale of assets	–	(355)	–	(355)
Release of accrual	(166)	–	–	(166)
Total restructuring expenses	421	332	367	1,120
Depreciation catch up		146	–	146
Payments received	–	887	–	887
Payments made	(1,198)	–	(367)	(1,565)
Amount charged against assets held for sale	–	(1,393)	–	(1,393)
Reclassification to property, plant and equipment	–	219	–	219
Amount charged against fixed assets	–	(191)	–	(191)
Currency change	51	–	–	51
Reserve balance at 31 December 2007	**638**	**–**	**–**	**638**

5. Other disclosures to the income statements

a) Operating expenses and revenues

The operating result before income taxes is stated after charging:

	2007 US$000	2006 US$000
Auditors' remuneration for the audit	**(468)**	(224)
Depreciation of property, plant and equipment	**(5,486)**	(7,087)
Amortisation of intangible assets	**(900)**	(3,883)
Personnel costs		
Wages and salaries	**(22,320)**	(23,895)
Social and security costs	**(4,427)**	(3,730)
Share-based payment	**(905)**	(1,157)
Pension costs	**(958)**	(805)
	(28,610)	(29,587)
Included in revenues		
Revenue from the sale of goods	**84,545**	92,731
Revenue from customer specific research and development contracts	**2,228**	1,207
Included in cost of sales:		
Costs in relation to customer specific research and development contracts	**(2,228)**	(1,207)
Amount of inventory recognised as expense	**(47,807)**	(55,500)
Impairment of inventories recognised as an expense	**(937)**	(728)
Included in general and administration expenses		
Impairment of inventories recognised as an expense	**–**	(7,171)
Impairment of trade accounts receivable	**–**	(2,644)
Included in other operating income		
Income from recoveries on trade accounts receivable impaired in prior periods	**903**	–

b) Interest income and interest expense

Interest, income and expenses comprise the following items:

	2007 US$000	2006 US$000
Interest income	**1,053**	1,356
Interest expense	**(84)**	(204)
	969	1,152
Of which: from financial instruments relating to categories in accordance with IAS 39		
Loans and receivables	**1,397**	911
Held-to-maturity investments	**(14)**	–
Available-for-sale financial assets	**(414)**	445
Financial liabilities measured at amortised costs	**–**	(204)
	969	1,152

Notes to the consolidated financial statements

For the year ended 31 December 2007

5. Other disclosures to the income statements continued

c) Other financial income and other financial expenses

Other financial income and expenses comprise the following items:

	2007 US$000	2006 US$000
Other financial income	**44**	–
Other financial expenses	**(447)**	–
	(403)	–
Composition and categories in accordance with IAS 39:		
Gain from the sale of available-for-sale financial assets	**44**	–
Loss from the sale of available-for-sale financial assets	**(377)**	–
Revaluation of financial assets held for trading	**(70)**	–
	(403)	–

d) Headcount

The average number of persons employed by the Group (including the Executive Director) during the year, analysed by category, was as follows:

	2007 US$000	2006 US$000
Research and development	**128**	118
Production	**47**	74
Sales and marketing	**22**	21
Administration	**21**	18
IT	**10**	10
	228	241

6. Income taxes

Loss before income taxes (including loss from discontinued operations) consists of the following:

	2007 US$000	2006 US$000
Germany	**(20,905)**	(38,881)
Foreign	**2,056**	(5,293)
	(18,849)	(44,174)

Income tax income (expense) is comprised of the following components:

	2007 US$000	2006 US$000
Current taxes:		
Germany	**–**	443
Foreign	**(63)**	(50)
Deferred taxes:		
Germany	**–**	–
Foreign	**(73)**	(235)
Income tax benefit (expense)	**(136)**	158

The deferred tax expenses in 2007 and 2006 relate to items that are charged or credited to equity.

Although Dialog is a UK company, its principal operations are located in Germany and its operating subsidiaries are all 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%. When 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:

	2007 US$000	2006 US$000
Expected benefit for income taxes	**7,087**	16,609
Effect of change in German tax rate	**(1,878)**	–
Other tax rate differential	**302**	(286)
Tax effect resulting from differences between functional currency and local currency used for taxation purposes	**(269)**	–
Repayment of German corporation tax credit	**–**	443
Non-deductible portion of share-based payments	**(325)**	(252)
Non-deductible expenses	**(92)**	(91)
Unrecognised deferred tax assets	**(4,939)**	(17,341)
Adjustments recognised for tax of prior periods	**–**	1,048
Other	**(22)**	28
Actual income (expense) for income taxes	**(136)**	158

On 14 August 2007 in Germany the Company tax reform 2008 (Unternehmensteuerreform 2008) was enacted. Among other things, this new legislation reduces the Company's statutory tax rate for its German subsidiary from 25% to 15%, effective 1 January 2008. When including the impact of the solidarity surcharge of 5.5%, the federal corporate tax rate amounts to 15.825%. Including the federal tax benefit rate for trade taxes of 9.387%, the combined statutory tax rate of the Company will be 25.212%. In the UK, the statutory tax rate was reduced from 30% to 28%. The Company's deferred income tax assets and liabilities have to be reduced to reflect the impact of the decreased tax rates. The effect on the net deferred tax asset carried forward from 2006 is US$14,116,000.

Notes to the consolidated financial statements

For the year ended 31 December 2007

6. Income taxes continued

Deferred income tax assets and liabilities are summarised as follows:

	31 December 2007 US$000	31 December 2006 US$000
Property, plant and equipment	**620**	618
Net operating loss and tax credit carryforwards	**52,955**	56,309
Liabilities	**4,036**	5,101
Deferred taxes in relation to tax credits	**1,443**	1,514
Other	**53**	153
Deferred tax assets	**59,107**	63,695
Property, plant and equipment	**(255)**	(602)
Intangible assets	**(174)**	–
Other	**(3)**	(3)
Deferred tax liabilities	**(432)**	(605)
Net deferred tax assets	**58,675**	63,090
Recognised net deferred tax assets	**–**	–
Unrecognised deferred tax assets	**58,675**	63,090

Tax loss carry-forwards and unrecognised deferred tax assets are summarised as follows:

	31 December 2007				31 December 2006			
	Tax loss carry-forwards US$000	Temporary differences US$000	Tax credits US$000	Unrecognised deferred tax asset US$000	Tax loss carry-forwards US$000	Temporary differences US$000	Tax credits US$000	Unrecognised deferred tax asset US$000
Germany	**177,463**	**12,608**	**–**	**52,643**	140,992	12,074	–	56,021
UK	**7,036**	**2,311**	**5,154**	**4,060**	10,681	2,126	5,047	5,359
US								
Federal	**4,398**	**–**	**–**	**1,495**	3,814	–	–	1,325
State	**3,954**	**–**	**–**	**356**	3,792	–	–	348
Other	**274**	**130**	**–**	**121**	–	88	–	37
Total				**58,675**				63,090

In assessing whether the deferred tax assets can be used, management considers the likelihood that some, or all, of the deferred tax assets will not be realised. The ultimate realisation 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, benefits that could be realised from available tax planning strategies and other positive and negative factors in making this assessment. Considering the weight given to cumulative losses incurred in Germany over the seven-year period ended 31 December 2007, as well as the inherent uncertainties in projecting future taxable income, pursuant to IAS 12, management concluded that tax losses may not ultimately be realised. Consequently, the Company did not recognise deferred tax assets of US$58,675,000 as of 31 December 2007 (US$63,090,000 as of 31 December 2006).

The tax loss carry-forwards in the US will expire between 2008 and 2021; other tax loss carry-forwards have no expiration date.

Included in unrecognised deferred tax assets is an amount of US$1,443,000 (2006: US$1,514,000) (the increase results from foreign currency adjustments) in relation to tax credits in the UK. This asset may be recovered against future taxable profits derived from certain overseas dividends for the company concerned.

6. Income taxes continued

The amount shown under "assets for current tax" in the balance sheet includes a corporation tax refund claim of the Company's German subsidiary. The total amount the Company is entitled to receive amounts to US$610,000 to be paid out in ten equal amounts during 2008 to 2017. The amount shown under "assets for current tax" represents the discounted part of the claim that is due after 2008. The amount that will be paid in 2008 is shown under "other current assets".

7. Cash and cash equivalents

Cash and cash equivalents comprise cash at bank (2007: US$15,187,000; 2006: US$15,507,000) and short-term deposits (2007: US$736,000; 2006: US$16,525,000). Short-term deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Company. Cash and cash equivalents earn interest at the respective short-term deposit rates. The fair value of the cash and cash equivalents approximates its book value. As prescribed in note 25, in 2007 the Company entered into a selective factoring agreement. Included in cash at bank is an amount of U$8,913,000 (2006: nil) held at the factoring bank which represents the cash value of selected receivables sold to the factoring bank. This amount is non-interest bearing until the related receivables have been entirely settled. The factoring bank charges interest on amounts drawn from the account.

8. Available-for-sale financial assets

The Company has invested in highly liquid "investment grade" rated debt, equity and currency-based funds, classified as available for sale. The principal of these securities is guaranteed to be 100% of the acquisition costs at maturity. The aggregate costs, fair values and unrealised gains (losses) per security class are shown in the table below.

	At 31 December 2007				At 31 December 2006			
	Cost US$000	**Fair value US$000**	**Unrealised gain US$000**	**Carrying value US$000**	Cost US$000	Fair value US$000	Unrealised loss US$000	Carrying value US$000
Available-for-sale securities	**15,609**	**15,921**	**312**	**15,921**	20,036	19,351	(685)	19,351

In 2007, net realised losses of US$333,000 from the sale of available-for-sale securities that had been previously recognised directly in equity were recycled into profit and loss.

Reclassifications

The Company reclassified available-for-sale financial assets amounting to US$4 million into held-to-maturity financial assets. The reclassification was made as a result of a change in the Company's intention which is now to hold those securities to maturity.

Contracted maturities of financial instruments

The majority of the above available-for-sale financial instruments is contracted to mature within one year or less and/or incorporate a floating interest rate that is reset as market rates change. One security with a carrying amount of US$2,776,000, contracted to mature in June 2010, was sold in February 2008.

Pledging

In connection with the agreement as prescribed in note 25, the Company has pledged US$6.5 million worth of its securities to the factoring bank. For further information please see note 25.

Notes to the consolidated financial statements

For the year ended 31 December 2007

9. Trade accounts receivable and other receivables

	2007 US$000	2006 US$000
Trade account receivables	**1,034**	4,666
Receivables from factoring agreement	**1,535**	–
	2,569	4,666

Trade receivables are non-interest bearing and are generally on 30-60-day terms.

As described in note 25, in 2007 the Company entered into a selective factoring agreement. The amount shown as receivables from the factoring agreement represents a 15% retainer kept by the factoring bank against sold receivables. The retainer is released only once the receivable is fully paid by the customer, at the latest, 120 days after the receivable becomes due or if the insurance event occurs. The amounts are non-interest bearing and are generally on 30-60-day terms.

The recorded trade accounts receivable for which an impairment has been recognised, was US$1,624,000 and US$2,814,000 at 31 December 2007 and 2006, respectively. The related allowance for doubtful accounts was US$1,624,000 and US$2,556,000 at 31 December 2007 and 2006, respectively. The decrease of the allowance for doubtful accounts mainly results from a recovery of accounts receivable of US$903,000 related to BenQ Mobile GmbH, which were written off in 2006.

The allowance for doubtful accounts developed as follows:

	2007 US$000	2006 US$000
Allowance for doubtful accounts at beginning of year	**2,556**	11
Additions charged to bad debt expense	**–**	2,666
Write-offs charged against the allowance	**–**	–
Reductions credited to income	**(903)**	(8)
Effect of movements in foreign currency	**(29)**	(113)
Allowance for doubtful accounts at end of year	**1,624**	2,556

As at 31 December, the aged analysis of trade account receivables is as follows:

	2007 US$000	2006 US$000
Receivables neither past due nor impaired	**576**	4,073
Receivables past due, not impaired individually		
Less than 30 days	**256**	213
30 to 59 days	**202**	122
Total	**1,034**	4,408
Receivables impaired individually	**–**	258
Carrying amount	**1,034**	4,666

With respect to the receivables that are neither past due nor impaired, there are no indications as at the reporting date that the debtors will not meet their payment obligations.

Receivables from construction contracts

As at 31 December 2007 and 2006, all incurred external costs for customer related research and development projects had been charged to the customers in accordance with agreed milestones. Consequently, as at 31 December 2007 and 2006, the Company had no receivables from construction contracts.

10. Inventories

Inventories are comprised of the following:

	At 31 December 2007 US$000	At 31 December 2006 US$000
Raw materials	**1,490**	822
Work in process	**5,321**	3,948
Finished goods	**10,240**	2,689
	17,051	7,459

The carrying amount of inventories carried at fair value less costs to sell at 31 December 2007 is US$nil (2006: US$1,323,000).

11. Other financial assets

Other financial assets comprise:

	At 31 December 2007 US$000	At 31 December 2006 US$000
Embedded derivatives	**247**	–
Hedging instruments	**89**	–
	336	–

Embedded derivatives represent the book value of the Company's investment in a currency index-linked derivative instrument which has been separated from its host contract. For further details regarding the risk associated to this investment please see note 25.

The hedging instruments include the fair value of derivative financial instruments used for cash flow hedges. The Company is exposed to currency risks in the course of its operating activities. These risks are reduced by the use of forward currency exchange contracts.

The Company has clear guidelines as to the use of those derivatives, and compliance is constantly monitored. For further information on the Company's hedging policy please see note 25.

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12. Property, plant and equipment, net

A summary of activity for property, plant and equipment for the years ended 31 December 2007 and 2006 is as follows:

	Test equipment US$000	Leasehold improvements US$000	Office and other equipment US$000	Advance payments US$000	Total US$000
Cost					
Balance at 1 January 2006	82,710	1,246	22,919	2,087	108,962
Effect of movements in foreign currency	4	8	(1)	–	11
Acquisitions	2,122	7	1,604	–	3,733
Reclassifications	2,087	–	–	(2,087)	–
Reclassifications to assets held for sale[1]	(12,275)	–	–	–	(12,275)
Disposals	(5,514)	(219)	(6,145)	–	(11,878)
Balance at 31 December 2006/1 January 2007	69,134	1,042	18,377	–	88,553
Effect of movements in foreign currency	3	13	66	–	82
Acquisitions	2,050	99	1,991	6	4,146
Reclassifications	–	–	–	–	–
Reclassifications from assets held for sale[1]	1,007	–	–	–	1,007
Disposals	(1,395)	–	(719)	–	(2,114)
Balance at 31 December 2007	**70,799**	**1,154**	**19,715**	**6**	**91,674**
Depreciation and impairment losses					
Balance at 1 January 2006	(67,414)	(901)	(19,940)	–	(88,255)
Effect of movements in foreign currency	(4)	(14)	(7)	–	(25)
Depreciation charge for the year	(5,537)	(38)	(1,512)	–	(7,087)
Reclassifications to assets held for sale[1]	8,541	–	–	–	8,541
Disposals	5,042	108	5,540	–	10,690
Balance at 31 December 2006/1 January 2007	(59,372)	(845)	(15,919)	–	(76,136)
Effect of movements in foreign currency	(2)	(14)	(55)	–	(71)
Depreciation charge for the year	(4,262)	(41)	(1,183)	–	(5,486)
Impairment charges	(191)	–	(108)	–	(299)
Reclassifications from assets held for sale[1]	(788)	–	–	–	(788)
Disposals	1,281	–	277	–	1,558
Balance at 31 December 2007	**(63,334)**	**(900)**	**(16,988)**	**–**	**(81,222)**
Net book value					
At 1 January 2006	15,296	345	2,979	2,087	20,707
At 31 December 2006/1 January 2007	9,762	197	2,458	–	12,417
At 31 December 2007	**7,465**	**254**	**2,727**	**6**	**10,452**

1) For further information see note 4 – Restructuring and related impairment charges.

13. Intangible assets

A summary of activity for intangible assets for the years ended 31 December 2007 and 2006 is as follows:

	Purchased software, licences and other US$000	Purchased patents US$000	Intangible assets from internal development US$000	Total US$000
Cost				
Balance at 1 January 2006	22,800	3,965	–	26,765
Effect of movements in foreign currency	14	–	–	14
Acquisitions	543	–	–	543
Disposals	(10,742)	(3,965)	–	(14,707)
Balance at 31 December 2006/1 January 2007	12,615	–	–	12,615
Effect of movements in foreign currency	23	–	–	23
Acquisitions/additions	1,100	–	724	1,824
Disposals	(66)	–	–	(66)
Balance at 31 December 2007	**13,672**	**–**	**724**	**14,396**
Amortisation and impairment losses				
Balance at 1 January 2006	(13,343)	(3,965)	–	(17,308)
Effect of movements in foreign currency	(16)	–	–	(16)
Amortisation charge for the year	(3,883)	–	–	(3,883)
Disposals	6,206	3,965	–	10,171
Balance at 31 December 2006/1 January 2007	(11,036)	–	–	(11,036)
Effect of movements in foreign currency	(23)	–	–	(23)
Amortisation charge for the year	(773)	–	(127)	(900)
Disposals	6	–	–	6
Balance at 31 December 2007	**(11,826)**	**–**	**(127)**	**(11,953)**
Net book value				
At 1 January 2006	9,457	–	–	9,457
At 31 December 2006/1 January 2007	1,579	–	–	1,579
At 31 December 2007	**1,846**	**–**	**597**	**2,443**

During the years ended 31 December 2007 and 2006, the Company acquired software and licences for a total purchase price of US$1,100,000 and US$543,000 respectively. The acquisitions in 2007 and 2006 are principally software.

The expected weighted average useful life of the acquired intangible assets is three years. The aggregate amortisation expense for the years ended 31 December 2007 and 2006 was US$900,000 and US$3,883,000 respectively.

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14. Held-to-maturity securities

In the third quarter 2007, financial instruments at an amount of US$4.0 million previously classified as available for sale had been reclassified to held-to-maturity. The reclassification was made as a result of a change in the Company's intention which is now to hold those securities to maturity.

The investments in held-to-maturity securities comprise securities which mature on 12 August 2010. The securities are interest bearing with a variable interest rate, not less that 0.7%. Repayment on maturity will amount to 100% of the nominal value.

15. Investments

Investments comprise the Company's 9.5% interest in DIS, which is classified as an available-for-sale financial asset.

DIS is a private entity that is not listed on a public stock exchange. As the fair value cannot be reliably determined the investment in DIS is therefore accounted for at acquisition cost less accumulated impairment charges.

As prescribed in note 3, in connection with the Company's disposition of its imaging division, the Company created a new entity ("DIS"). A total of US$29,320,000 was invested in DIS by private equity investors, the management team of DIS, and the Company. Of this the Company invested US$2,662,000 which was paid in two tranches of US$1,620,000 and US$1,042,000 in 2006 and 2007 respectively.

In the third quarter of 2007, based on current business and cash flow projections, the Company recognised an impairment of US$2,662,000 for the investment in DIS. This impairment is disclosed separately in the income statement under impairment of investments.

The impairment test requires management to make estimates about the expected future cash flows of the unquoted equity instruments which are discounted at adequate interest rates. Management has determined that the potential effect of using reasonably possible alternatives as inputs to the valuation model would not result in materially different amounts.

For further information regarding the Company's investment in DIS please see note 3.

16. Trade and other payables

Trade and other payables comprise:

	At 31 December 2007 US$000	At 31 December 2006 US$000
Trade accounts payable	**12,319**	6,024
Other payables	**2,416**	3,085
	14,735	9,109

Terms and conditions of the above trade and other payables:

- trade payables are non-interest bearing and are normally settled on 30-60-day terms; and
- other payables are non-interest bearing and have an average term of five months.

17. Provisions

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 estimated provision is based on historical warranty data. Regarding the provision for restructuring please see note 4. The Company expects all provisions to mature within the next 12 months.

The changes in the provision are summarised as follows:

	Balance at 1 January 2007 US$000	Currency change US$000	Additions US$000	Used US$000	Released US$000	**At 31 December 2007 US$000**
Obligations for product warranties	66	–	330	(56)	–	**340**
Restructuring	1,364	51	483	(1,094)	(166)	**638**
Total	1,430	51	813	(1,150)	(166)	**978**

	Balance at 1 January 2006 US$000	Currency change US$000	Additions US$000	Used US$000	Released US$000	At 31 December 2006 US$000
Obligations for product warranties	256	–	–	(190)	–	66
Restructuring	–	–	1,720	(356)	–	1,364
Total	256	–	1,720	(546)	–	1,430

18. Other current liabilities

Other current liabilities comprise:

	At 31 December 2007 US$000	At 31 December 2006 US$000
Obligations for personnel and social expenses	**1,110**	1,501
Other	**668**	392
	1,778	1,893

Terms and conditions of the above other current liabilities:

- obligations for personnel and social expenses have an average term of three months (2006: five months); and
- other payables are non-interest bearing and are normally settled on 30 day terms.

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19. Shareholders' equity and other reserves

Ordinary shares

At 31 December 2007 and 2006, Dialog had authorised 104,311,860 Ordinary shares with a par value of £0.10 per share, of which 46,068,930 shares were issued and outstanding. The Company's stock is all issued in the form of bearer shares, and all shares are fully paid.

On 24 September 2004, the Company completed an offering of 2,000,000 previously unissued Ordinary shares at £0.10 per share to its employee share option trust ("Trust"), to make such shares available for the exercise of stock option rights that had previously been granted to employees. At 31 December 2007 and 31 December 2006 the Trust continued to hold 1,046,387 and 1,178,957 shares respectively. These shares are legally issued and outstanding, but are not considered issued and outstanding for accounting purposes and accordingly have been reported under "employee stock purchase plan shares" as a reduction of Shareholders' equity.

Share premium

The account comprises additional paid-in capital in connection with the issue of shares.

Accumulated deficit

The accumulated deficit comprises losses and non-distributed earnings of consolidated Group companies. Because of the accumulated deficit, the Company cannot pay a dividend and does not plan to pay dividends in the foreseeable future.

Nature and purpose of other reserves

Currency translation reserve

The currency translation reserve is used to record exchange differences arising from the translation of the financial statements of subsidiaries whose functional currency is not the US$.

Derivative financial instruments reserve

The reserve records the portion of the gain or loss on a hedging instrument that is determined to be an effective cash flow hedge.

Available-for-sale securities reserve

This reserve records fair value changes on available-for-sale investments.

Accumulated other comprehensive income

The related tax effects allocated to each component of other comprehensive income (loss) for the years ended 31 December 2007 and 2006 are as follows:

		2007			2006	
	Pretax US$000	**Tax effect US$000**	**Net US$000**	Pretax US$000	Tax effect US$000	Net US$000
Unrealised (losses) gains on available-for-sale securities	**734**	**–**	**734**	(12)	(16)	(28)
Currency translation adjustment	**47**	**73**	**120**	(198)	251	53
Derivative financial instruments	**89**	**–**	**89**	–	–	–
Other comprehensive income (loss)	**870**	**73**	**943**	(210)	235	25

20. 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 US$958,000 (2006: US$805,000). At 31 December 2007, contributions amounting to US$80,000 (2006: US$152,000) were payable to the funds and are included in creditors.

21. Share-based payments

a) Stock option plan

On 7 August 1998, the Company adopted a stock option plan (the "Plan") under which employees and Executive 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 authorised but unissued Ordinary shares. On 16 May 2002 the Shareholders of the Company approved a resolution increasing the maximum amount of stock options which may be granted by the Company at any time, to 15% of the Company's issued share capital on a diluted basis. At 31 December 2007, 8,129,811 shares could be issued.

Except in relation to the Chief Executive Officer, stock options granted to employees are granted with an exercise price not less than the quoted price at the date of grant, and vest during the service period of the employee without any further vesting conditions. Stock options granted before 31 October 2006 have terms of ten years and vest over periods of one to five years from the grant date. On 19 June 2006 the Company adopted a revised stock option plan under which stock options now have a seven-year life and vest monthly over a period of one to 48 months. The new stock options may not be exercised until they have been held for one calendar year from the grant date. The new rules were implemented on grants made on or after 31 October 2006.

The fair value of all grants in the two-year period ended 31 December 2007 was estimated using the Black-Scholes option pricing model. Expectations of early exercise are considered in the determination of the expected life of the options. The Company does not have adequate historical development of the share price, particularly as a result of material unusual effects in the stock market in recent years. Furthermore, implicit volatility cannot be determined since none of the Company's options are actively traded. The Company has therefore based its calculation of expected volatility on an average of its own volatility and the historical development of other companies in its business segment.

The following assumptions were used for stock option grants for the years ended 31 December 2007 and 2006:

	2007	2006
Expected dividend yield	**0%**	0%
Expected volatility	**33% – 54%**	21% – 49%
Risk-free interest rate	**4.0%**	4.1%
Expected life (in years)	**2.0 – 6.0**	2.0 – 6.0
Weighted average share price (US$)	**3.58**	1.85
Weighted average exercise price (in US$)	**2.22**	1.67
Weighted average fair value (in US$)	**0.84**	0.67

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21. Share-based payments continued

Stock option plan activity for the years ended 31 December 2007 and 2006 was as follows:

	2007		2006	
	Options	Weighted average exercise price US$	Options	Weighted average exercise price US$
Outstanding at beginning of year	**5,501,781**	**2.56**	3,850,008	3.23
Granted	**905,968**	**2.22**	3,012,080	1.67
Exercised	**(132,570)**	**1.17**	(512,198)	0.54
Forfeited	**(903,173)**	**3.02**	(848,109)	3.76
Outstanding at end of year	**5,372,006**	**2.77**	5,501,781	2.56
Options exercisable at year end	**2,534,781**	**3.14**	2,051,796	2.97

The weighted average share price at the date of exercise of options was US$2.56 and US$2.01 in the years ended 31 December 2007 and 2006 respectively.

The following table summarises information on stock options outstanding at 31 December 2007:

	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding at 31 December 2007	Weighted average remaining contractual life (in years)	Weighted average exercise price US$	Number exercisable at 31 December 2007	Weighted average exercise price US$
€0.00-2.98	**4,046,074**	**5.5**	**1.81**	**1,469,803**	**1.44**
€3.00-8.00	**1,325,932**	**6.2**	**5.71**	**1,064,978**	**5.48**
€0.00-8.00	**5,372,006**	**5.7**	**2.77**	**2,534,781**	**3.14**

b) ESOP Trust

The Company established an employee share option trust (the "Trust"). The Trust purchases shares in the Company for the benefit of employees under the Company's share option scheme. At 31 December 2007 the Trust held 1,046,387 shares.

c) Non-executive Directors' stock option plan

At the 2006 Annual General Meeting, Shareholders approved a stock option plan for Non-executive Directors. Each Non-executive Director is entitled to an initial grant of 50,000 options vesting over four years and each year thereafter. As soon as possible after each Annual Shareholder Meeting a further 20,000 options vesting over 12 months are granted. Options are exercisable at the market price prevailing at the date of grant.

22. Additional disclosures on financial instruments

Carrying amounts, amounts recognised and fair values by classes of financial assets and liabilities as well as by category:

		Amounts recognised in balance sheet according to IAS 39					
	Category in accordance with IAS 39 US$000	**Carrying amount 31 December 2007 US$000**	Amortised cost US$000	Cost US$000	Fair value recognised in equity US$000	Fair value recognised in profit or loss US$000	Fair value 31 December 2007 US$000
Assets							
Cash and cash equivalents	LaR	**15,923**	15,923	–	–	–	15,923
Trade accounts receivables	LaR	**2,569**	2,569	–	–	–	2,569
Other non-derivative financial instruments							
Available-for-sale financial assets (current)	AfS	**15,921**	–	–	15,921	–	15,921
Held-to-maturity investments	HtM	**4,000**	4,000	–	–	–	3,795
Investments (non-current)	AfS	**–**	–	–	–	–	n/a
Derivative financial assets							
Derivatives without hedging relationship	n/a	**247**	–	–	–	247	247
Derivatives with hedging relationship	n/a	**89**	–	–	89	–	89
Liabilities							
Trade account payables	FLAC	**12,319**	12,319	–	–	–	12,319
Other payables	FLAC	**2,416**	2,416	–	–	–	2,416
Derivative financial liabilities							
Derivatives without hedging relationship	n/a	**n/a**	–	–	–	–	n/a
Derivatives with hedging relationship	n/a	**n/a**	–	–	–	–	n/a
Of which aggregated by category in accordance with IAS 39:							
Loans and receivables (LaR)		**18,492**	18,492	–	–	–	18,492
Held-to-maturity investments (HtM)		**4,000**	4,000	–	–	–	3,795
Available-for-sale financial assets (AfS)		**15,921**	–	–	15,921	–	15,921
Derivatives without hedging relationship		**247**	–	–	–	247	247
Derivatives with hedging relationship		**89**	–	–	89	–	89
Financial liabilities at amortised cost (FLAC)		**14,735**	12,319	–	–	–	12,319

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22. Additional disclosures on financial instruments continued

	Amounts recognised in balance sheet according to IAS 39						
	Category in accordance with IAS 39 US$000	Carrying amount 31 December 2006 US$000	Amortised cost US$000	Cost US$000	Fair value recognised in equity US$000	Fair value recognised in profit or loss US$000	Fair value 31 December 2006 US$000
Assets							
Cash and cash equivalents	LaR	32,032	32,032	–	–	–	32,032
Trade accounts receivables	LaR	4,666	4,666	–	–	–	4,666
Other non-derivative financial instruments							
Available-for-sale financial assets (current)	AfS	19,351	–	–	19,351	–	19,351
Investments (non-current)	AfS	1,620	–	1,620	–	–	n/a
Derivative financial assets							
Derivatives without hedging relationship	n/a	n/a	–	–	–	–	–
Derivatives with hedging relationship	n/a	n/a	–	–	–	–	–
Liabilities							
Trade accounts payable	FLAC	6,024	6,024	–	–	–	6,024
Other payables	FLAC	3,085	3,085	–	–	–	3,085
Derivative financial liabilities							
Derivatives without hedging relationship	n/a	n/a	–	–	–	–	n/a
Derivatives with hedging relationship	n/a	n/a	–	–	–	–	n/a
Of which aggregated by category in accordance with IAS 39:							
Loans and receivables (LaR)		36,698	36,698	–	–	–	36,698
Held-to-maturity investments (HtM)		n/a	n/a	n/a	n/a	n/a	n/a
Available-for-sale financial assets (AfS)		20,971	–	1,620	19,351	–	19,351
Financial liabilities at amortised cost (FLAC)		9,109	6,024	–	–	–	6,024

The fair values of investments that are actively traded in organised financial markets are determined by reference to quoted market bid prices at the close of business on the balance sheet date. Market values have therefore, been used to determine the fair value of listed available-for-sale and held-to-maturity financial assets. The fair value of derivatives has been determined with reference to available market information. For the valuation of unlisted equity instruments see note 15. The carrying amounts of the loans and receivables and financial liabilities approximate their fair values due to short-term maturities.

23. Commitments

The Company leases all its office facilities and vehicles, and some of its office and test equipment, under operating leases. In addition, the Company has contracted consulting services and software licences related to Computer Aided Design ("CAD") until 29 December 2009. Total rentals under these agreements (excluding the software licence agreement explained below), charged as an expense in the income statement, amounted to US$2,178,000 and US$2,545,000 for the years ended 31 December 2007 and 2006 respectively.

Future minimum lease payments under rental and lease agreements, which have initial or remaining terms in excess of one year at 31 December 2007, are as follows:

	Operating leases	
	2007	2006
	US$000	US$000
Within one year	**4,473**	4,621
Between one and two years	**2,895**	3,718
Between two and three years	**1,228**	1,746
Between three and four years	**270**	275
Between four and five years	**5**	208
Thereafter	**–**	–
Total	**8,871**	10,568

From 30 December 2006 the Company has entered into a software licence agreement amounting to US$7,200,000. The contract period is three years, and quarterly payments of US$600,000 have been agreed. If the total volume of the contract term is used before the end of the contract period, the remaining contract fee becomes due.

The Company has contractual commitments for the acquisition of property, plant and equipment in 2008 of US$597,000 and for the acquisition of intangible assets of US$110,000.

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24. Segmental reporting

Segmental information is presented according to Dialog's business and geographic segments. The primary format, business segments, is based on the Company's principal sales markets.

a) Business segments

The Company's business segments are:

Wireless

The wireless segment includes our Power Management and Audio ICs and the Display Drivers which are used in portable electronic products, such as mobile phones and other hand-held devices.

Automotive and industrial

In the automotive and industrial market our products address the safety, management and control of electronics systems in cars and for industrial applications.

Imaging

Before being discontinued, the business of this division included the development, design, manufacture and assembly of image sensor semiconductors and camera modules.

	2007					2006					
	Wireless US$000	**Automotive/ industrial US$000**	**Corporate general US$000**	**Corporate imaging[1] US$000**	**Total US$000**	Wireless US$000	Automotive/ industrial US$000	Corporate US$000	Total continued operations US$000	Imaging (discontinued operations) US$000	Total US$000
Revenues[2]	**51,505**	**35,268**	**–**	**–**	**86,773**	57,934	36,004	–	93,938	–	93,938
R&D expenses	**23,172**	**7,933**	**–**	**–**	**31,105**	20,391	7,138	–	27,529	–	27,529
Operating profit (loss)	**(12,952)**	**(1,572)**	**(2,748)**	**–**	**(17,272)**	(31,103)	(879)	(8,993)	(40,975)	(2,267)	(43,242)
Depreciation/amortisation	**4,740**	**1,646**	**–**	**–**	**6,386**	7,910	3,060	–	10,970	–	10,970
Reversal of impairment losses	**–**	**–**	**–**	**–**	–	–	–	–	–	–	–
Impairment losses	**617**	**574**	**687**	**2,662**	**4,540**	10,543	–	4,105	14,648	–	14,648
Investments	**4,431**	**1,539**	**–**	**1,021[3]**	**6,991**	3,113	1,163	1,564[3]	5,840	–	5,840
	31 December 2007					31 December 2006					
Total assets	**25,687**	**9,692**	**35,844**	**–**	**71,223**	16,307	13,244	51,958	81,509	1,620	83,129
Liabilities	**12,584**	**4,371**	**576**	**–**	**17,531**	9,214	3,246	–	12,460	–	12,460

1) The imaging business was discontinued in 2006.
2) All revenues are from sales to external customers.
3) Investment in DIS.

Corporate expenses and gains include the holding company, the restructuring expenses and gains and other expenses, and gains not specifically attributable to the business segments. Corporate assets include certain financial assets such as cash and cash equivalents, marketable securities and, in 2006, the assets held for sale. Corporate liabilities include liabilities of the holding company and other liabilities not specifically attributable to business segments.

Segment assets and liabilities comprise all assets and liabilities employed by the relevant business segment to generate the operating segment's profit or loss.

Investments comprise additions to property, plant and equipment, and intangible assets.

In 2007 and 2006 the Company had no inter-segment sales, income, expenses, receivables, payables or provisions.

24. Segmental reporting continued

b) Geographic segments

	2007 US$000	2006 US$000
Revenues		
Germany	**6,887**	12,112
Austria	**14,015**	13,666
Hungary	**12,846**	13,224
Sweden	**6,847**	
Other European countries	**3,843**	3,055
Japan	**1,735**	14,585
China	**31,055**	12,004
Other Asian countries	**4,106**	12,380
Other countries	**5,439**	12,912
Total revenues	**86,773**	93,938
Investments		
Germany	**6,583**	4,114
Japan	**10**	26
United Kingdom	**330**	133
Other	**68**	3
Total investments	**6,991**	4,276

	At 31 December 2007 US$000	At 31 December 2006 US$000
Assets		
Germany	**68,884**	81,355
Japan	**580**	622
United Kingdom	**1,665**	556
USA	**94**	596
Total assets	**71,223**	83,129

Revenues are allocated to countries based on the location of the shipment destination. Segmental investments and assets are allocated based on the geographic location of the asset.

Notes to the consolidated financial statements

For the year ended 31 December 2007

25. Financial risk management objectives and policies

Vulnerability due to certain significant risk 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 utilised in the cellular communications and automotive industries. The Company generates a substantial portion of its revenue from the wireless communications market, which accounted for 59% and 62% of its total revenue for the years ended 31 December 2007 and 2006, 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, purchases of raw materials and manufacturing services are primarily denominated in US$. The Company also has foreign currency exchange risks with respect to its net investments in foreign subsidiaries in Japan, Taiwan and the United Kingdom. Fluctuations in these currencies could have a significant impact on 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 2007 four customers individually accounted for more than 10% of the Company's revenues. Total revenues from these four customers were US$65,620,000 or 76%. Net receivables from these four customers were US$562,000 at 31 December 2007. During 2006 four customers individually accounted for more than 10% of the Company's revenues. Total revenues from these four customers were US$64,004,000 or 68%. Net receivables from these four customers were US$2,829,000 at 31 December 2006. The Company performs ongoing credit evaluations of its customers' financial condition.

Financial risk management objectives and policies

The Company's principal financial instruments, other than derivatives, comprise cash and cash equivalents, short-term deposits and securities. The main purpose of these financial instruments is to raise finance for the Company's operations. The Company has other financial instruments which mainly comprise trade receivables and trade payables which arise directly from its operations.

During the year 2007 the Company also entered into derivative transactions (forward currency contracts). The purpose is to manage the currency risks arising from the Company's operations.

It is, and has been throughout 2007 and 2006, the Company's policy that no trading in derivatives shall be undertaken.

Exposure to currency, interest rate and credit risk arises in the normal course of the Company's business. The Board of Directors reviews and agrees policies for managing each of these risks which are summarised below:

Interest risk

The Company earns interest from bank deposits and uses money market deposits with highly rated financial institutions. Furthermore the Company invests in non-current interest bearing held-to-maturity investments. During the year, the Company has held cash on deposit with a range of maturities from one week to one month. This can vary in view of changes in the underlying currency's interest rates and the Company's cash requirements.

The Company has invested in liquid "investment grade" rated debt-based funds classified as available for sale. These funds are highly liquid and are contracted to mature within three years or less and/or incorporate a floating interest rate that is reset as market rates change.

The Company has invested in liquid "investment grade" rated debt-based funds classified as held-to-maturity. These funds are contracted to mature in 2010 and incorporate a floating interest rate that is reset as market rates change.

The Company has no long-term debt and no amounts outstanding under short-term credit facilities as at 31 December 2007 (2006: US$nil).

The Company's policy is to manage its interest income using a mix of fixed and variable interest rate debts. In order to achieve this policy, the Company invests in highly liquid funds having a matching investment strategy. Once the operating business has been financed, short-term excess funds are invested in floating interest rate securities. Only short-term deposits bear fixed interest rates.

25. Financial risk management objectives and policies continued

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Company's profit before tax as well as the Company's equity:

	Increase/decrease in basis points US$000	Effect on profit US$000	Effect on equity US$000
2007			
	12	**91**	**91**
	(12)	**(91)**	**(91)**
2006			
	12	67	67
	(12)	(67)	(67)

Currency risk

The main functional currency within the Group and the presentation currency for the consolidated financial statements is the US$. For the change in the functional currency resulting from the transfer from some production activities to subcontractors please see note 1. Accordingly, foreign exchange risks arise from transactions, and recognised assets and liabilities, the functional currency of which is not the US$. The currencies giving rise to these exposure risks are primarily the euro and pound sterling. The majority of the Company's revenue and material expenses are denominated in US$. The majority of other operating expenses are denominated in euros and pounds sterling. The Company has transactional currency exposures. Such exposure arises from the sales or purchases by an operating unit in currencies other than the unit's functional currency. In 2007 nearly all the Company's sales were denominated in US$. The Company uses forward currency contracts to eliminate the currency exposure of recurring expected payments, such as salaries, wages and office rents non-US$ denominated. The forward currency contracts must be the same currency as the hedged item. It is the Company's policy not to enter into forward contracts until a firm commitment is in place.

It is the Company's policy to maximise hedge effectiveness by negotiating the terms of hedge derivatives to match the terms of the hedged item.

The Company did not use foreign exchange instruments in prior years to hedge its currency risk. In prior years the Company ensured that the net exposure was kept to an acceptable level by selling or buying foreign currencies (primarily US$ and pounds sterling) spot when required.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of the Company's profit before tax (resulting from changes in the fair value of monetary assets, excluding securities, and liabilities) and the Company's equity (resulting from changes in the fair value of forward exchange contracts).

	Increase/decrease against US$	Effect on profit US$000	Effect on equity US$000
2007			
Euro	**12%**	**(39)**	**1,082**
Pounds sterling	**2%**	**16**	**161**
Euro	**(12)%**	**39**	**(1,082)**
Pounds sterling	**(2)%**	**(16)**	**(161)**
2006			
Euro	14%	3,465	3,465
Pounds sterling	11%	91	91
Euro	(14)%	(3,465)	(3,465)
Pounds sterling	(11)%	(91)	(91)

The analysis shows the Company's significantly-reduced foreign currency exposure resulting from the change of its functional currency. The above analysis does not include the available-for-sale securities. A risk analysis for the Company's securities was done separately, based on the inherent historic volatility of the specific securities, see below.

Notes to the consolidated financial statements

For the year ended 31 December 2007

25. Financial risk management objectives and policies continued

Other price risks

IFRS 7 also requires disclosures on how hypothetical changes in risk variables affect the price of financial instruments. Important risk variables are stock exchange prices.

As part of its cash management the Company invests in available-for-sale securities. Price fluctuations would have an impact on the equity of the Company. The following table summarises the impact of hypothetical changes of the market price of the respective securities based on the inherent historic volatility of the specific securities:

	Increase/decrease in %	Effect on profit US$000	Effect on equity US$000
2007			
Available-for-sale financial assets	**0.2%**	**–**	**24**
Available-for-sale financial assets	**(0.2)%**	**–**	**(24)**
2006			
Available-for-sale financial assets	3.4%	–	665
Available-for-sale financial assets	(3.4)%	–	(665)

Not included in this risk analysis is an investment made in 2007 into a structured US dollar note linked to a Currency Harvest Index. This investment which includes an embedded derivative was sold in February 2008. The carrying amount of the investment at 31 December 2007 (including the host contract, the embedded derivative and accrued interest) amounted to US$3,023,000. The net cash proceeds from the sale were US$3,047,000. For further information regarding this investment please see below, "Embedded derivatives".

All securities held at 31 December 2006, which were subject to the 2006 analysis above, were sold in 2007.

Credit risk

The Company is exposed to credit risk from its operating activities and certain financing activities. The Company trades only with recognised, creditworthy third parties. It is the Company's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis, with the result that the Company's exposure to bad debts is not significant. The maximum exposure is the carrying amount as disclosed in note 9. Regarding the risk concentration please see above,"vulnerability due to certain significant considerations".

In order to finance its growth, in August 2007 the Company entered into a factoring agreement with a reputable German financial institution. The maximum amount of cash that can be received under this agreement is €10 million (or US$ equivalent). The agreement, which comprises receivables from selective customers, significantly reduces the underlying credit risk because the financial institution assumes all credit risks associated with the collection of the receivables financed under the programme.

As part of the factoring agreements, the Company has pledged US$6.5 million of securities to the financial institution. The institution would draw down on these only if a commercial action by Dialog were to invalidate – partly or completely – the claim on a receivable financed through the factoring programme. The pledge can be released after 1 October 2008, providing the Company returns to profitability.

The Company's exposure to credit risk arising from other financial assets of the Company, which comprise cash and cash equivalents, available-for-sale and held-to-maturity financial investments would arise from default by a counterparty. The maximum exposure is equal to the carrying amount of the instruments.

25. Financial risk management objectives and policies continued

Liquidity risk

The Company uses quarterly cash flow forecasts to monitor its liquidity risk. It takes financial investments and financial assets (e.g. trade accounts receivables and other financial assets) into consideration, as well as projected cash flows from operations. The Company's objective is to minimise interest expense by avoiding the use of short-term bank liabilities or bank overdrafts within the Group.

At 31 December 2007, the Company had cash and cash equivalents of US$15,923,000 (2006: US$32,032,000) and marketable securities of US$15,921,000 (2006: US$19,351,000). Furthermore as of 31 December 2007, the Company held held-to-maturity investments, disclosed as non-current, in the amount of US$4,000,000 (2006: US$nil). Even though these investments are non-current, they are liquid.

The Company's policy is to structure its maturities of current financial assets within the Group to meet 100% of the respective maturities of the liabilities. As of 31 December 2007, and 31 December 2006, all liabilities are current and due within one year.

The table below summarises the maturity profile of the Company's financial liabilities at 31 December 2007, based on contractual undiscounted payments:

	Less than three months US$000	Three to 12 months US$000	One to five years US$000	Total US$000
Financial year ended 2007				
Trade accounts payable	**12,289**	**15**	**15**	**12,319**
Other payables	**1,229**	**1,173**	**14**	**2,416**
	13,518	**1,188**	**29**	**14,735**
Financial year ended 2006				
Trade accounts payable	6,024	–	–	6,024
Other payables	1,696	1,342	47	3,085
	7,720	1,342	47	9,109

At 31 December 2007, the Company had unused short-term credit lines of US$9,418,000. There were no amounts outstanding under these credit lines at 31 December 2007.

Capital management

The primary objective of the Company's capital management is to ensure that it maintains healthy capital ratios in order to support its business and strategies for growth.

The Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions. To maintain or adjust its capital structure, the Company may generally issue new shares. No changes were made in the objectives, policies or processes during the years ending 31 December 2007 and 31 December 2006.

The Company monitors capital using an equity ratio (total equity divided by total assets). The equity ratio as of 31 December 2007 was 75.4% (2006: 84.9%). Capital includes net Shareholders' equity. The Company's policy is to finance business development and growth with equity rather than long-term liabilities. It is, therefore, also its policy to keep a strong equity ratio. This policy will be reconsidered as soon as sustainable profits are earned in order to achieve leverage.

Notes to the consolidated financial statements

For the year ended 31 December 2007

25. Financial risk management objectives and policies continued

Hedging activities

At 31 December 2007, the Company held several forward exchange contracts designated as hedges of firm commitments and forecast transactions in euros and pounds sterling. The forward exchange contracts are being used to hedge the foreign currency risk of contractual cash flows, principally resulting from wages and salaries, and rental payments with the aim of eliminating the currency risk by transforming these cash flows from euros or pounds sterling into US dollars. The fair values which equal the book values are as follows:

	At 31 December 2007		At 31 December 2006	
	Assets US$000	**Liabilities US$000**	Assets US$000	Liabilities US$000
Forward exchange contracts				
Fair values	**336**	**–**	–	–

The critical terms of the forward currency contracts have been negotiated to match the terms of the hedged cash flows.

The cash flow hedges of the expected future cash flows in each month from January 2008 to May 2008 were assessed to be highly effective and, at 31 December 2007, a net unrealised gain of US$89,000 was included in equity in respect of these cash flows. During the financial year 2007 an amount of US$313,0000 (2006: US$nil) was recognised in equity and an amount of US$224,000 (2006: US$nil) was removed from equity and recognised in profit and loss. The months of occurrence of the cash flows are the same as the month when the income statement is affected.

The following tables show the contractual maturities of the payments, i.e., when the hedged item will be recognised in profit or loss:

Maturity	Nominal amount €000
January 2008	300
February 2008	1,400
March 2008	1,400
April 2008	1,650
May 2008	1,610

Maturity	Nominal amount £000
January 2008	811
February 2008	650
March 2008	766
April 2008	650
May 2008	755

Embedded derivatives

In 2007, the Group acquired a structured US$ note linked to a Currency Harvest Index. This 100% capital repayment-guaranteed structured note was issued by Deutsche Bank AG. This note was separated into an available-for-sale financial instrument with a fair value of US$2,711,000 and an embedded derivative with a fair value of US$247,000 at 31 December 2007, which is recognised under other financial assets. In February 2008 the Company decided to sell this structured US$ note. The net cash proceeds from this transaction were US$3,047,000.

26. Transactions with related parties

For the relationship between the parent company, Dialog Semiconductor Plc, and its subsidiaries please see note 2.

Related parties are comprised of eight Non-executive members of the Board of Directors and seven members of the executive management which are named in the management and governance section. These are the only related parties of the Group.

Compensation of key management personnel of the Company

For the composition of our key management please see management and governance beginning on page 25. Compensation of key management personnel of the Company is as follows:

	2007 US$000	2006 US$0000
Short-term employee benefits	**2,511**	2,730
Buy out[1]	**253**	266
Post-employment benefits[2]	**165**	119
Termination benefits	**454**	120
Share-based payments	**420**	867
	3,803	4,102

1) The amount shown under "buy out" relates to a payment in connection with a buy out provision for Dr Bagherli's previous employment.
2) The amounts include payments for defined contribution plans.

Compensation of Non-executive Directors

The compensation of Non-executive Directors was US$350,000 (2006: US$733,000). As at 31 December 2007 the amount of US$54,000 for Board member fees was outstanding (2006: US$58,000). For further information please see the directors' remuneration report within the management and governance section on page 32.

Other related-party transactions

In 2007 and 2006 there were no transactions with other related parties.

27. Subsequent event

No subsequent events occurred after the balance sheet date.

Company financial statements

On the following pages information regarding the holding company Dialog Semiconductor Plc is given.

Company balance sheet

For the year ended 31 December 2007

	Notes	At 31 December 2007 US$000	At 31 December 2006 US$000
Assets			
Cash and cash equivalents		**708**	1,618
Available-for-sale financial assets	8	**15,921**	19,351
Amounts owed by Group undertakings		**29,361**	25,371
Prepaid expenses		**57**	21
Other financial assets		**247**	–
Other current assets		**321**	446
Total current assets		**46,615**	46,807
Investments	28	**97,521**	97,521
Held-to-maturity securities		**4,000**	–
Amounts owed by Group undertakings (due after more than one year)		**3,104**	3,557
Total non-current assets		**104,625**	101,078
Total assets		**151,240**	147,885
Liabilities and Shareholders' equity			
Trade accounts payables		**151**	95
Other payables		**426**	856
Total current liabilities		**577**	951
Ordinary shares		**9,328**	9,328
Share premium		**222,914**	222,781
Retained deficit		**(81,686)**	(84,521)
Other reserves		**312**	(422)
Employee stock purchase plan shares		**(205)**	(232)
Total Shareholders' equity	31	**150,663**	146,934
Total liabilities and Shareholders' equity		**151,240**	147,885

Profit for the financial year

As permitted by Section 230 of the Companies Act 1985, the parent company's profit and loss account has not been included in these financial statements. The parent company's profit after taxation was US$ 2,835,000 (2006: (3,842,000)).

These financial statements were approved by the Board of Directors on 28 February 2008 and were signed on its behalf by:

Dr Jalal Bagherli
Director

Company statement of changes in equity

For the year ended 31 December 2007

	Ordinary shares US$000	Additional paid-in capital US$000	Accumulated deficit US$000	Available-for-sale securities US$000	Employee stock purchase plan shares US$000	Total US$000
Balance at 31 December 2005	9,328	222,600	(80,679)	(394)	(331)	150,524
Net loss	–	–	(3,842)	–	–	(3,842)
Other comprehensive income (loss)	–	–	–	(28)	–	(28)
Total comprehensive loss	–	–	(3,842)	(28)	–	(3,870)
Sale of employee stock purchase plan shares	–	181	–	–	99	280
Balance at 31 December 2006	9,328	222,781	(84,521)	(422)	(232)	146,934
Net loss	–	–	2,835	–	–	2,835
Other comprehensive income (loss)	–	–		734	–	734
Total comprehensive loss	–	–	2,835	734		3,569
Sale of employee stock purchase plan shares	–	133	–	–	27	160
Balance at 31 December 2007	**9,328**	**222,914**	**(81,686)**	**312**	**(205)**	**150,663**

Company financial statements

Notes to the company financial statements

For the year ended 31 December 2007

28. Investments

This represents the investment of the Company in Dialog Semiconductor GmbH. On 29 December 2006 the Board of Directors concluded a capital contribution into Dialog Semiconductor GmbH in the amount of US$21.1 million to prevent a negative equity situation at this subsidiary. Investments in subsidiaries are stated at cost less any provision for impairment in value.

29. Deferred tax

	At 31 December 2007 US$000	At 31 December 2006 US$000
Net operating loss and tax credit carryforwards	**1,320**	2,326
Deferred taxes in relation to tax credits	**1,443**	1,514
Other	**26**	129
Net deferred tax assets	**2,789**	3,969
Recognised net deferred tax assets	**–**	–
Unrecognised deferred tax assets	**2,789**	3,969

For further information on deferred taxes see note 6.

30. Auditors' remuneration

	2007 US$000	2006 US$000
Auditors' remuneration for the audit	**370**	96

31. Share capital and share options

Details of the Company's share capital and share options are set out in notes 19 and 21.

32. Headcount and costs

The Company does not have any employees.

33. Events since the balance sheet date

No subsequent events occurred after the balance sheet date.

Glossary

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.
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 company that designs and delivers semiconductors by outsourcing the fabrication (manufacturing) process.
Foundry A manufacturing plant where silicon wafers are produced.
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 organisers, 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 A combination of analog and digital signals being generated, controlled or modified on the same chip.
MLA Multi-Line Addressing: a technology used in colour LCDs to enable full-colour, 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.
NiMH, L Ion and polymer Various battery technologies.
OEM Original Equipment Manufacturer: a company that builds products or components that are used in products sold by another company.
OLED Organic Light Emitting Diode.
PDA Personal Digital Assistants: handheld devices that were originally designed as personal organisers, but became much more versatile over the years. A basic PDA usually includes date book, address book, task list, memo pad, clock, and calculator software.
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.
SmartXtend™ A technology patented by Dialog Semiconductor that extends the life and reduces power consumption of high-resolution, passive matrix OLED displays.
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.
Subcontractor A business that signs a contract to perform part or all of the obligations of another's contract.
TAM Total addressable market TAM measures the potential market for your product – and your product only – assuming you could reach 100% of your customers.
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.

Glossary

Financial glossary

AGM Annual General Meeting

CAGR Compound Annual Growth Rate: a method of assessing the average growth of a value over time.

Cash flow The primary purpose of a statement of cash flow 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 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 recognised 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 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's 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).

Dividends are payments made by a company to its Shareholders. When a company earns a profit, that money can be put to two uses: it can either be re-invested in the business (called retained earnings), or it can be paid to the shareholders of the company as a dividend.

EURIBOR (Euro Interbank Offered Rate) is the rate at which euro interbank term deposits within the euro zone are offered by one prime bank to another prime bank.

Freefloat the proportion of an issuer's share capital that is available for purchase in the public equity markets by investors.

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

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 financial years commencing on or after 1 January 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 securitised debt instruments. Available-for-sale securities are debt securities not classified as held to maturity or trading securities.

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

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

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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Shares
Information on the Company's shares and on significant shareholdings canbe found on pages 7 to 9.

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Registered number
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Financial calendar

Annual General Meeting	30 April 2008
Q1 2008 Results	6 May 2008
Q2 2008 Results	22 July 2008
Q3 2008 Results	21 October 2008
Preliminary results for 2008	February 2009

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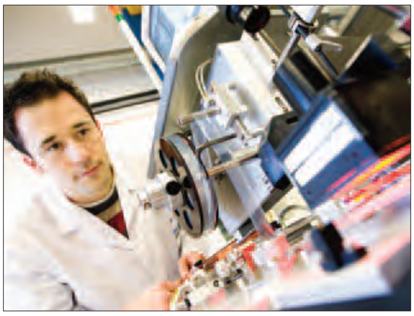



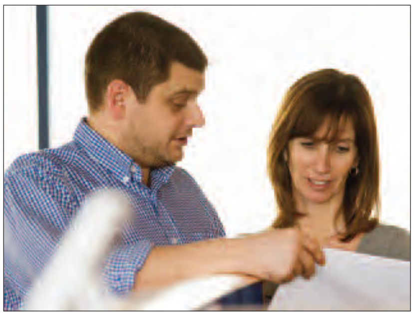
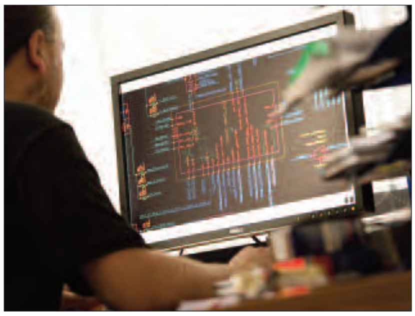


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