

NAPATECH

4TH QUARTER 2018

INTERIM MANAGEMENT STATEMENT

DEAR SHAREHOLDERS

In the second half of 2018, the Napatech team has worked urgently to regain stability, focusing on our near-term sales development, our internal cost structure and efficiency, our cash position and building on our long-standing relationships with partners and customers to execute on our growth ambitions.

Coming from a weak start to the year, we saw signs of improvement in our second half of 2018, and during the final quarter of 2018 we took additional positive steps towards our goal of returning Napatech to stability and growth. In Q4, we secured sales of USD 7.4 million compared to reported sales of USD 4.8 million in Q3, representing a sequential improvement in our sales performance of 54%. As a result, our sales in the second half of 2018 came in at USD 12.2 million, an increase of 54% compared to the first half of 2018, with full year 2018 sales ending at USD 20 million, which is within the sales guidance presented in Q2 of USD 18 to 23 million.

This more normalized sales performance comes as a result of focused work to adapt to the ongoing transformation in the market and balance the situation of postponed customer projects and inventory reductions. We have come far, but we still have a lot to do, and we continue to work at full pace to improve our sales momentum into 2019.

In parallel, we are continuously working to improve our internal efficiency and operations. As previously reported, we have acted to improve our internal cost structure, and we see full effect of this improvement at the beginning of 2019. In Q4, Napatech was cash flow positive, and at the end of Q4 our total cash position including unused credit facilities was significantly improved compared to the end of Q3. Following the completed private placement referred to below, the company expects to be fully funded for 2019 and to become cash generating in 2020.

With the improved operating performance in the second half of 2018, our more positive momentum, exemplified by the recently reported design win with Axellio FabricXpress and the continued activation of strong partnerships with key industry players, we are looking forward to working towards our goal of building momentum with new product growth, leveraging our cost structure and maximizing shareholder profit.

Napatech has over 15 years of history in delivering FPGA-based technology to customers globally, with an unparalleled expertise in accelerating compute-intensive applications on standard open servers. In light of the significant transformation our markets have gone through over the past 24 months, we have made changes to our product-market strategy to align with the largest players in the FPGA market. Historically, a significant portion of our revenue has come from partners who have integrated our solution within their products, representing one of our primary paths to the market. As our partners and others have reported in various market sectors in 2018, many of these appliance companies have experienced volatility within their markets as their customers assess their internal strategies moving away from buying hardware centric solutions to buying software solutions that operate on commercial off-the-shelf servers.

Currently, we sit at the crossroads of two major market forces, as the SmartNIC is becoming the preferred solution to deliver faster computing on standard open servers, and more sophisticated and compute-intensive applications are

consuming and generating more data – which require more processing speed and power. Going forward, we will target the market through our application driven, software-centric and hardware independent approach, driving growth through our focus on three main product areas:

- Network Management: In the future, Network Management is expected to grow +10%.
- Cybersecurity: In the future, Cybersecurity is expected to grow +40%, and expected to eclipse Network Management in a few years.
- Virtualization Acceleration: In the future, Virtual Acceleration is expected to grow +80%.

To accomplish this, we will leverage our expertise in FPGA solutions to out-innovate our competition. The mega-market areas are gaining traction, and the key industry players now believe that the FPGA solution we deliver will solve the growing application acceleration opportunity.

At the end of 2018, the total cash position of the company, including unused credit facilities, was DKK 20.0 million. On February 22st, 2019 Napatech announced a private placement and a fully underwritten subsequent offering. Total amount to be raised within these transactions amounts to app. NOK 76.7 million.

With the new funding in place, we will stay closely focused on the FPGA software that differentiates Napatech, enhancing our offerings and accelerating our delivery of new products to the market in 2019 and 2020. In parallel, we will enhance our go-to-market strategy, sales and marketing to maximize the revenue impact from our new products and new unbundled service revenue, while the market for SmartNICs is expanding.

As stated above, we have come far, but still have a lot to do. Moving into 2019, we will continue to be focused on thorough execution of our growth strategy together with our valued partners and customers. Our long-term outlook is promising as Napatech's products and services become applicable to not only our current, but also new market segments. We see our long-term potential as significantly larger than our current business as we move to broader markets and support more applications, but we underline that the short-term visibility is limited and will be affected by quarter-to-quarter volatility and general business uncertainty.

However, as the recent actions and initiatives display, we are taking the right steps to build a solid foundation for our business going forward, and we are looking forward to seeing the positive effects of our implemented and ongoing initiatives in the coming quarters.

We thank our shareholders for their dedication to Napatech and we look forward to discussing the Q4 developments and outlook over the coming days and weeks.

Best regards,

Ray Smets, Chief Executive Officer

MANAGEMENT STATEMENT

Highlights:

- Sales in the fourth quarter 2018 of USD 7.4 million, compared to reported sales of USD 4.8 million in the third quarter of 2018. This provided sales for second half 2018 of USD 12.2 million, and with sales for first half of 2018 of USD 7.9 million total sales in 2018 amounts to USD 20 million¹. This is within the guidance of sales of USD 18 to 23 million presented in the Q2 report.
- Reported revenue in Q4 2018 amounted to DKK 54.0 million, an increase of 13% compared to Q4 2017. Revenue for the full year of 2018 were DKK 106.2 million, a decrease of 48% compared to 2017.
- Underlying product margin in the fourth quarter of 2018 was 67%. Reported cost of goods sold in Q4 is impacted by an extraordinary write down of inventories DKK 11.1 million aligned with the decision to end of life certain products, and by DKK 2.9 million related to the divestiture of the Pandion product line. Adjusted for these special items gross profit margin in Q4 was 67%, an increase of 13%-points compared to Q4 2017.
- Reported gross margin for full year of 2018 was 46%. Adjusted for the extraordinary inventory write downs in Q3 and special items in Q4 2018 gross margin in 2018 was 69% which is just above the guidance of around 68% presented in the Q2 report.
- Adjusted for the special items EBITDA in Q4 was DKK 4.1 million. Reported EBITDA for Q4 2018 amounted to negative DKK 10.0 million, compared to negative DKK 7.2 million in Q4 2017. EBITDA for the full year of 2018 was negative DKK 75.5 million, and negative DKK 38.4 million adjusted for special items.
- Depreciation, amortization and impairment for Q4 2018 was DKK 52.0 million, compared to DKK 9.4 million in Q4 2017. Q4 is impacted by the impairment of capitalized development projects by DKK 42.6 million. Depreciation, amortization and impairment for the full year of 2018 were DKK 107.6 million, compared to DKK 37.8 million for 2017.
- Cash flow from operating activities in Q4 2018 was DKK 18.0, compared to DKK 8.2 million in Q4 2017. Total cash flow from operating activities in 2018 was negative DKK 44.3, compared to DKK 12.7 million in Q4 2017.
- Investments in Q4 2018 were DKK 6.2 million all primarily related to new product development (capitalized development). In Q4 2017, total investments were DKK 13.5 million, of which DKK 12.2 million was related to internal product development.
- The total cash position of the Company including unused credit facilities at the end of Q4 2018 was DKK 20.0 million, compared to DKK 56.0 million at the end of Q4 2017.

(Figures in MDKK)	Q4 2018	Q4 2017	FY 2018
Revenue	54.0	47.9	106.2
Growth YoY	13%	-48%	-48%
Gross Margin adjusted for special items	67%	54%	69%
EBITDA adjusted for special items	4.1	-7.2	-38.4
Reported Gross Margin	41%	54%	46%
Reported EBITDA	-10.0	-7.2	-75.0
Cash flow from operating activities	18.0	8.2	-44.3
Cash and cash equivalents. end of period	17.2	40.0	17.2
Available funds. incl. unused credit facilities	20.0	56.0	20.0

This is Napatech

Napatech helps companies to reimagine their business by bringing Hyperscale computing benefits to IT organizations of every size. We enhance open and standard virtualized servers to boost innovation and release valuable computing resources that improve services and increase revenue. Our reconfigurable computing platform™ is based on a broad set of FPGA software for leading IT compute, network and security applications that are supported on a wide array of FPGA hardware designs.

Napatech operations.

The statements below are related to Napatech's development in the fourth of 2018 compared to the fourth quarter of 2017, unless as otherwise stated. Additional information is available at www.napatech.com/investor.

¹ "Sale" or "Sales" is defined as net invoiced sale in USD before accounting adjustments and commercial decision reported in Q3 to take returns.

Revenue and Gross Margin

Napatech reports revenue of DKK 54.0 million in the fourth quarter of 2018, an increase of 13% compared to the same period in 2017.

Revenue for 2018 were DKK 106.2 million, compared to DKK 206.0 million in 2017.

Reported gross margin for Q4 2018 was 41% compared to 54% in Q4 2017. Adjusted for an extraordinary inventory write down and cost related to the divestiture of the Pandion products line gross margin in Q4 2018 was 67%.

Reported gross margin for 2018 was 46%. Adjusted for special items gross margin in 2018 was 69% compared to 68% in 2017.

Costs

Operating expenses² in Q4 2018 were DKK 32.8 million, compared to DKK 33.0 million in Q4 2017.

Total operating expenses in 2018 were DKK 124.7 million, compared to DKK 125.6 million in 2017.

EBITDA

EBITDA in Q4 2018 was negative DKK 10.0 million, compared to negative DKK 7.2 million in Q4 2017. Adjusted for special items EBITDA was DKK 1.2 million in Q4 2018.

EBITDA in 2018 was negative DKK 75.5 million and adjusted for special items negative DKK 38.4 million, compared to DKK 13.9 million in 2017. The decrease in EBITDA is materially affected by special items in 2018 and by considerably lower revenue compared to 2017.

Depreciation, amortisation and impairment

Depreciation, amortization and impairment for Q4 2018 was DKK 52.0 million, compared to DKK 9.4 million in Q4 2017.

Q4 is impacted by the impairment of capitalized development projects by DKK 42.6 million. Impairments are primarily due to a revised assessment of timing of the expected acceleration of growth in the market for FPGA based solutions. Depreciation, amortization and impairment for the full year of 2018 were DKK 107.6 million, compared to DKK 37.8 million for 2017.

Financial Items

Financial items for Q4 2018 are negative DKK 2.9 million. The financial items are primarily affected by the hedging contracts entered in April 2018.

Financial items for 2018 were negative DKK 9.6 million, compared to an expense of DKK 6.0 million for 2017.

Taxes

Taxes for Q4 2018 were an income of DKK 19.0 million compared to an income of DKK 1.1 million in Q4 2017.

Total taxes for 2018 were an income of DKK 12.8 million, compared to an income of DKK 5.4 million 2017.

Investments

Investments in Q4 2018 were DKK 6.2 million related to new product development. In Q4 2017, total investments were DKK 13.5 million, of which DKK 12.2 million was related to internal product development.

Total Investments in 2018 were DKK 35.8 million, primarily related to new product development (capitalized development), representing DKK 35.4 million of total investments, compared to DKK 53.3 million in 2017, of which DKK 48.4 million was related to internal product development.

Cash Flow

Cash flow from operating activities in Q4 2018 was DKK 18.0, compared to DKK 8.2 million in Q4 2017. Total cash flow from operating activities in 2018 was negative DKK 44.3, compared to DKK 12.7 million in Q4 2017.

Net cash flow from investing activities in Q4 2018 was negative DKK 4.1 million, compared to negative DKK 13.5 million in Q4 2017. Total net cash flow from investing activities 2018 was DKK negative DKK 33.6 million compared to negative DKK 53.3 million in 2017.

Net cash from financing activities in Q4 2018 was negative DKK 3.6 million due to repayment of borrowings, compared to Q4 2017 were net cash from financing activities was DKK 22.9 million funds due to increase in borrowings. Net cash flow from financing activities for 2018 was DKK 58.8 million, compared to DKK 31.8 million in 2017.

The total cash position of the Company including unused credit facilities at the end of Q4 2018 was DKK 20.0 million, compared to DKK 57,0 million at the end of Q4 2017.

Significant events after the end of the period

After the end of the period, the company has as of February 22, 2018 conducted a private placement raising gross proceeds of NOK 50 million. Further, the company announce it will conduct a fully underwritten subsequent offering of NOK 25 million, and a separate offering tranche in favour of certain listed members of the company's board and management. Completion the Private Placement, the Subsequent Offering and the separate offering tranche is subject to approval by an Extraordinary General Meeting to be held on March 15th, 2019. After these transactions, the new share capital of the company is DKK 20,767,055 divided into 83,068,220 shares, each with a nominal value of DKK 0.25.

Outlook for 2019

2019 guidance is the following:

- Revenue in the range of DKK 150-180 million (USD 23-27,6 million)
- Gross margin around 68%
- Operating expenses² in the range of DKK 115-125 million
- Investments in development projects in the range DKK 20-25 million
- Depreciation and amortization in the range of DKK 20-25 million

With performance in the middle of the guided ranges EBITDA would be negative DKK 7.8 million and EBIT would be negative DKK 30.3 million.

Disclaimer:

This report contains statements regarding the future in connection with Napatech growth initiatives, profit figures, outlook, strategies and objectives. In particular, the section Outlook for 2019 contains forward-looking statements regarding the Group's expectations. All statements regarding the future are subject to inherent risks and uncertainties, and many factors can lead to actual profits and developments deviating substantially from what has been expressed or implied in such statements.

² "Operating expenses" include costs for Research and development, Selling and distribution expenses and Administrative expenses.

INCOME STATEMENT

For the period ended 31 December 2018

DKK'000	4th quarter		YTD December	
	2018	2017	2018	2017
Revenue	53.997	47.898	106.153	206.046
Cost of goods sold	(31.793)	(22.025)	(57.060)	(66.611)
Gross profit	22.204	25.873	49.093	139.435
Other operating income	599	-	599	-
Research and development costs	(6.603)	(6.451)	(18.460)	(17.907)
Selling and distribution expenses	(15.257)	(17.724)	(66.735)	(71.420)
Administrative expenses	(10.899)	(8.855)	(39.469)	(36.223)
Operating profit before depreciation, amortisation and impairment (EBITDA)	(9.956)	(7.157)	(74.972)	13.885
Depreciation, amortisation and impairment	(52.023)	(9.359)	(107.558)	(37.755)
Operating result (EBIT)	(61.979)	(16.516)	(182.530)	(23.870)
Finance costs	(2.857)	5.900	(9.576)	(5.956)
Result before tax	(64.836)	(10.616)	(192.106)	(29.826)
Income tax	19.025	1.169	12.808	5.395
Result for the period	(45.811)	(9.447)	(179.298)	(24.431)
Earnings / (loss) per share:				
Basic, DKK	(1,44)	(0,40)	(6,74)	(1,03)
Diluted, DKK	(1,39)	(0,39)	(6,48)	(1,00)

BALANCE SHEET

ASSETS	31 Dec.	30 Sep.	31 Dec.
DKK'000	2018	2018	2017
Development projects, completed	29.773	50.015	68.416
Development projects, in progress	8.194	32.867	46.342
Patents	4.972	5.149	5.412
Other intangible assets	-	9	50
Intangible assets	42.939	88.040	120.220
Plant and equipment	1.932	2.138	5.166
Leasehold improvements	605	702	1.079
Tangible assets	2.537	2.840	6.245
Leasehold deposits	2.407	2.423	2.283
Other non-current assets	2.407	2.423	2.283
Non-current assets	47.883	93.303	128.748
Inventories	17.485	37.194	36.124
Trade receivables	25.305	25.086	51.938
Other receivables	13.814	2.296	3.899
Income tax receivable	5.487	5.500	5.500
Cash and cash equivalents	17.159	620	39.967
Assets held for sale	-	9.662	-
Current assets	79.250	80.358	137.428
Total assets	127.133	173.661	266.176

EQUITY AND LIABILITIES

DKK'000	31 Dec. 2018	30 Sep. 2018	31 Dec. 2017
Share capital	7.981	7.981	5.969
Share premium	247.552	248.406	219.729
Foreign currency translation reserve	215	168	(9)
Other capital reserves	4.971	5.340	6.361
Retained earnings	(226.000)	(180.898)	(48.883)
Equity	34.719	80.997	183.167
Deferred tax liability	-	13.555	7.425
Other non-current financial liabilities	13.391	13.733	-
Non-current liabilities	13.391	27.288	7.425
Interest-bearing loans and borrowings	44.701	40.511	35.109
Other current financial liabilities	5.959	6.383	-
Trade payables	11.099	2.292	26.130
Other payables	13.720	12.789	13.855
Derivative financial instruments	-	2.933	-
Provisions	69	468	490
Deferred revenue	3.475	-	-
Current liabilities	79.023	65.376	75.584
Total liabilities	92.414	92.664	83.009
Total equity and liabilities	127.133	173.661	266.176

CASH FLOW STATEMENT
For the period ended 31 December 2018

DKK'000	4th quarter		YTD December	
	2018	2017	2018	2017
Operating activities				
Loss before tax	(64.836)	(10.616)	(192.106)	(29.826)
Adjustments to reconcile profit before tax to net cash flows:				
Finance costs	2.857	(5.900)	9.576	5.956
Depreciation, amortisation and impairment	52.023	9.359	107.558	37.755
Gain/loss on the sale of non-current assets	(599)	428	(599)	428
Non-cash changes in inventories	11.114	-	21.323	-
Share-based payment expense	340	243	1.101	978
Working capital adjustments:				
Change in inventories	8.595	3.598	(2.684)	(17.449)
Change in trade and other receivables	(4.254)	2	23.363	16.283
Change in trade and other payables, provisions and deferred revenue	12.779	11.076	(11.808)	(1.419)
Cash flows from operating activities	18.019	8.190	(44.276)	12.706
Cash flow hedges in financial items	(5.435)	3.637	(7.454)	2.505
Interest paid	(371)	(580)	(1.552)	(861)
Income tax received, net	5.470	1.950	5.383	730
Net cash flows from operating activities	17.683	13.197	(47.899)	15.080
Investing activities				
Proceeds from sale of tangible assets	126	-	126	-
Purchase of tangible assets	(34)	(1.336)	(461)	(4.864)
Proceeds from sale of intangible assets	1.979	-	1.979	-
Investments in intangible assets	(6.230)	(12.177)	(35.410)	(48.402)
Investments in leasehold deposits	(16)	(4)	124	(29)
Net cash used in investing activities	(4.175)	(13.517)	(33.642)	(53.295)
Financing activities				
Capital increase	-	-	31.505	1.705
Transaction costs on issue of shares	(480)	-	(1.606)	-
Increase of borrowings	-	20.035	28.942	30.109
Repayment of borrowings	(3.095)	-	-	-
Net cash flows (used in) / from financing activities	(3.575)	20.035	58.841	31.814
Net change in cash and cash equivalents	9.933	19.715	(22.700)	(6.401)
Net foreign exchange difference	87	(376)	(108)	(583)
Cash and cash equivalents at the beginning of the period	7.139	20.628	39.967	46.951
Cash and cash equivalents at the end of the period	17.159	39.967	17.159	39.967

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