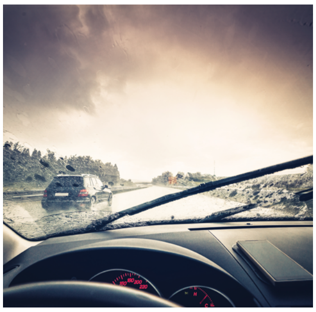
Dialog Semiconductor Plc
Interim report – 9M 2019

Powering the smart connected future

Contents

Interim report – 9M 2019



Section 1

Section 2

Section 3

Press release – 6 November 2019

Dialog Semiconductor reports results for the third quarter ended 27 September 2019

Q3 2019 Revenue up 7% year-on-year to US$409 million slightly above the high-end of the guidance range, earnings acceleration and strong cash flow generation.

London, UK, 6 November 2019 – Dialog Semiconductor Plc (XETRA: DLG) today reports unaudited results for the third quarter ended 27 September 2019.

	IFRS basis (unaudited)		Underlying[1] (unaudited)		
US$ millions	**Q3 2019**	Q3 2018	**Q3 2019**	Q3 2018	Change
Revenue	**408.8**	383.6	**408.8**	383.6	+7%
Gross margin	**49.2%**	48.5%	**49.5%**	48.6%	+90bps
Operating expenses[2]	**122.5**	125.1	**103.7**	104.4	-1%
Operating profit	**83.9**	63.5	**103.8**	83.7	+24%
Operating margin	**20.5%**	16.6%	**25.4%**	21.8%	+360bps
Diluted EPS	**0.91**	0.60	**1.13**	0.85	+33%
Free cash flow			**86.8**	79.1	+10%

1 Underlying measures and free cash flow quoted in this Press Release are non-IFRS measures (see page 39).
2 Comprising SG&A and R&D expenses.

Q3 2019 Financial highlights

- Revenue of US$409 million slightly above the high end of the guidance range and 7% above Q3 2018.
- Gross margin at 49.2% (Q3 2018: 48.5%) and underlying gross margin at 49.5% (Q3 2018: 48.6%) in line with the July guidance.
- Operating profit of US$83.9 million, 32% higher than in Q3 2018. Underlying operating profit of US$103.8 million, 24% above Q3 2018.
- Diluted EPS of US$0.91 (Q3 2018: US$0.60) and underlying diluted EPS of US$1.13 (Q3 2018: US$0.85).
- US$37 million returned to shareholders in Q3 2019 through the 2019 Buyback Programme.
- At the end of Q3 2019, we held cash and cash equivalents of US$1,171 million.
- On 7 October 2019, the Company announced it had signed a definitive agreement to acquire Creative Chips GmbH, a supplier of Integrated Circuits (ICs) to the Industrial Internet of Things (IIoT) market. The transaction was closed on 31 October 2019.

Q3 2019 Operational highlights

- Continued design-in momentum at our largest customer for the development and supply of a number of mixed-signal integrated circuits. Revenue from recently awarded high-volume contracts is expected to begin with new smartphones for the second half of 2021.
- Revenue from our largest customer in Custom Mixed Signal not covered by the license agreement doubled year-on-year.
- Extended product portfolio with the launch of new configurable, high-frequency sub-PMICs, powering advanced multi-core processors in a wide range of applications.
- Launched the first automotive Configurable Mixed-Signal IC (CMIC), the SLG46620-A, providing lower project costs, shorter time to market and unified development flows.
- Q3 2019 revenue from our AC/DC charging products was up 8% year-on-year, led by growth in rapid charge products.
- Increased our footprint in IoT with our Bluetooth® low energy (BLE) products, which delivered 51% year-on-year revenue growth.
- Samsung adopted our BLE SoC, DA14697, for seamless connectivity and enhanced battery life in its latest wearable Galaxy Fit.

Commenting on the results, Dialog Chief Executive, Dr Jalal Bagherli, said:

"We have reported another excellent quarter, delivering record Q3 revenue slightly above the high-end of the guidance range alongside increased operating profit and strong cash flow generation. This strong performance is the result of our strategic focus in high-growth segments of our target end markets coupled with operational excellence. Since the beginning of the year we have been awarded new designs for mixed-signal custom products, in a wide range of applications, including power management, charging, display and backlighting LED drivers which we estimate will generate a lifetime revenue of approximately one billion dollars."

"The recently announced acquisition of Creative Chips, gives us a strong foothold in the growing industrial IoT market, broadening our customer base and opening up new potential opportunities for our existing product portfolio. Our solid financial position enables us to make targeted investments to expand our product portfolio and leverage our technology into new markets. These investments support our growth strategy and help to rebalance the end-market exposure of our business, creating long-term and sustainable value for shareholders."

Press release – 6 November 2019 continued

Outlook

In Q4 2019, we anticipate revenue to be in the range of US$350 million to US$390 million. At the mid-point, this will result in full year 2019 IFRS revenue of US$1,556 million and underlying revenue of US$1,410 million.

FY 2019 underlying gross margin is expected to be broadly in line with that achieved in 9M 2019.

Q3 2019 Financial overview

Revenue was 7% above Q3 2018 at US$409 million driven by year-on-year growth in all business segments. License revenue of US$6 million related to the Apple agreement was reported in Corporate.

Gross margin was 49.2%, 70bps above Q3 2018 due to the positive contribution from the license revenue (Q3 2019: US$6 million; Q3 2018: nil).

Q3 2019 underlying[1] gross margin was 49.5%, 90bps above Q3 2018, due to the positive contribution from the ongoing license revenue as well as favourable product mix and lower manufacturing costs.

Operating expenses (OPEX) comprising SG&A and R&D expenses, in Q3 2019 were 2% below Q3 2018 representing 30.0% of revenue (Q3 2018: 32.6%). Underlying OPEX was down 1% year-on-year at 25.4% of revenue (Q3 2018: 27.2%) due to lower R&D expenses offsetting the acquisition of FCI.

R&D expenses in Q3 2019 were 4% below Q3 2018 representing 19.3% of revenue (Q3 2018: 21.4%). Underlying R&D expenses were down 4% year-on-year representing 17.6% of revenue (Q3 2018: 19.5%). The decrease in R&D expenses was mainly due to the transfer of over 300 employees to Apple on 8 April 2019.

SG&A expenses in Q3 2019 were up 2% from Q3 2018, representing 10.7% of revenue (Q3 2018: 11.2%). Underlying SG&A in Q3 2019 was 6% above Q3 2018 representing 7.7% of revenue (Q3 2018: 7.7%). The increase in SG&A expenses was mainly due to the acquisition of FCI.

Other operating income in Q3 2019 was US$5.2 million (Q3 2018: US$2.6 million), which comprised income from engineering contracts.

Underlying other operating income in Q3 2019 was also US$5.2 million, significantly above Q3 2018 (Q3 2018: US$1.5 million) due to higher income from engineering development work contracts for specific customers.

Operating profit in Q3 2019 was US$83.9 million, 32% above Q3 2018, mainly reflecting the higher revenue and gross margin, together with lower operating expenses. Underlying[1] operating profit was US$103.8 million, 24% above Q3 2018.

The effective tax rate in Q3 2019 was 21.3% (Q3 2018: 24.9%). The relatively high effective tax rate for Q3 2018 was principally due to the distorting effect on our income tax expense of the tax and accounting treatments of share-based compensation, business combinations and certain of our strategic investments. The underlying effective tax rate in Q3 2019 was 20.5%, down 50bps on the Q3 2018 underlying effective tax rate of 21.0%.

Net income was 47% above Q3 2018 at US$68.2 million (Q3 2018: US$46.4 million). This increase was mostly due to the increase in operating profit.

Underlying net income was up 28% year-on-year. The year-on-year increase in underlying net income was mainly driven by the underlying operating profit movement.

Diluted EPS in Q3 2019 was up 52% year-on-year at US$0.91 (Q3 2018: US$0.60). Underlying diluted EPS in Q3 2019 was up 33% year-on-year to US$1.13 (Q3 2018: US$0.85).

At the end of Q3 2019, our total inventory level was US$125 million (or ~54 days), which is 20% below the previous quarter, representing a 29-day decrease in our days of inventory from Q2 2019. During Q4 2019, we expect inventory value to be broadly in line with Q3 2019 and days of inventory to be slightly above Q3 2019.

On 19 September 2019, the first interim settlement of the first tranche of the 2019 Buyback Programme took place. The Company purchased 800,000 ordinary shares for €33.1 million at an initial average price of €41.40. Under this tranche the company committed to purchase shares for an amount between €125 million and €150 million and a latest maturity date of 5 December 2019. Subsequent to quarter end, on 31 October 2019, we completed the second interim settlement of this tranche, purchasing 865,000 ordinary shares for €37.1 million at an initial average price of €42.87.

At the end of Q3 2019, we held cash and cash equivalents of US$1,171 million. Cash inflow from operating activities in Q3 2019 was US$97.3 million, up 12% over Q3 2018 (Q3 2018: US$86.9 million) mainly as a result of higher cash generated from operations partially offset by higher income tax paid. Free cash flow in Q3 2019 was US$86.8 million, 10% above Q3 2018 (Q3 2018: US$79.1 million) mostly due to the higher cash flow from operating activities. Free cash flow margin (as a percentage of revenue) in Q3 2019 was above Q3 2018 at 21.2% (Q3 2018: 20.6%).

In support of our growth strategy and the expansion of our product portfolio, on 7 October 2019, the Company announced it had signed a definitive agreement to acquire Creative Chips GmbH, a Germany based fabless semiconductor company supplying a broad portfolio of industrial Ethernet and other mixed-signal products to top-tier, blue-chip manufacturers of industrial automation systems. Creative Chips is expected to generate revenues of approximately US$20 million in calendar year 2019 with revenue growth of over 25% per annum anticipated over the next few years. The transaction was completed on 31 October 2019. We purchased Creative Chips for consideration of US$80 million on a cash and debt-free basis. Additional contingent consideration of up to US$23 million in cash, may be payable based on future revenue targets in 2020 and 2021.

Q3 2019 Segmental overview

Dialog is a fabless semiconductor company primarily focused on the development of highly integrated mixed-signal products for consumer electronics and other high-growth markets. Our highly skilled engineers, partnership approach, operational flexibility and the quality of our products are sources of competitive advantage. Our primary end markets are consumer markets such as the Internet of Things (IoT) and Mobile. The increasing adoption of standard technologies, such as Bluetooth® low energy or LED lighting, and the expansion of high-performance processors into infotainment systems, has contributed to the expansion of our presence in the automotive segment. In line with our strategic goals, we intend to continue the expansion of our product portfolio through a combination of organic and inorganic initiatives. Our ambition is to build a vibrant mixed-signal business, with a balanced end market exposure, on innovative low power products which enable our customers to get fast to market.

Underlying results by segment

	Revenue			Operating profit/(loss)			Operating margin	
US$ millions – unless stated otherwise	**Q3 2019**	Restated[3] Q3 2018	Change	**Q3 2019**	Restated[3] Q3 2018	Change	**Q3 2019**	Restated[3] Q3 2018
Custom Mixed Signal	**278.2**	274.6	+1%	**88.7**	72.0	+23%	**31.9%**	26.2%
Advanced Mixed Signal	**70.0**	66.3	+6%	**6.2**	9.1	-32%	**8.8%**	13.6%
Connectivity & Audio	**54.3**	42.7	+27%	**5.4**	5.6	-3%	**10.0%**	13.1%
Total Segments	**402.5**	383.6	+5%	**100.3**	86.7	+16%	**24.9%**	22.6%
Corporate and other unallocated items	**6.3**	–	nm	**3.5**	(3.0)	nm	**55.7%**	nm
Total Group	**408.8**	383.6	+7%	**103.8**	83.7	+24%	**25.4%**	21.8%

Custom Mixed Signal (CMS)

In Q3 2019 revenue was US$278 million, up 1% over Q3 2018 due to higher volumes and content per device across multiple platforms, partially offset by lower volumes from smartphone main PMICs. Revenue in CMS from our largest customer's products not covered by the licensing agreement doubled year-on-year to US$92 million (Q3 2018: US$46 million). Underlying operating profit for CMS increased 23% year-on-year to US$88.7 million. This improvement was mainly due to the slightly higher revenue and lower operating expenses.

We continue to receive requests for quotations for new custom designs for 2021 and beyond in diverse areas of power, charging, display and audio technologies.

Dialog has recently been awarded high-volume new contracts from our largest customer for the development and supply of a range of mixed-signal integrated circuits. Revenue from recently awarded high-volume contracts is expected to begin with new smartphones in the second half of 2021.

During the quarter we expanded our power management product portfolio with the introduction of four new sub-PMICs that offer best-in-class transient response and in-circuit digital programmability, in a smaller form factor than current market solutions. The devices are ideal for ARM® Cortex™ based multi-core application processors and high-performance SoCs, FPGAs and GPUs. The four new sub-PMICs drive higher efficiency without sacrificing functionality, simplifying complex system sequencing with digital programmability and configurability, for a seamless interface to the system microcontroller depending on the system requirements.

In parallel, we continue to leverage our power management technology into new markets and geographies through the expansion of our platform reference designs. The collaborations with Renesas and Xilinx strengthen Dialog's presence in the IVI[4] and ADAS[4] applications automotive segment. There are currently over 45 automotive customer engagements in place most of which are expected to go into production over the next three years.

3 Restated to reflect the segment reorganisation and measurement changes.
4 Intelligent In-Vehicle Infotainment and Advanced Driver-Assistance Systems.

Press release – 6 November 2019 continued

Advanced Mixed Signal (AMS)

During Q3 2019, AMS revenue was 6% above Q3 2018. Revenue from AC/DC charging products was up 17% sequentially and 8% above Q3 2018, led by growth in rapid charge. Revenue from LED drivers ICs and CMICs was also up year-on-year. During the quarter we continued to invest in our AMS business, resulting in lower underlying operating profit year-on-year.

Dialog has successfully maintained a commanding market share in the rapid charge market through a combination of differentiated technology, speed of execution and wide support of rapid charge protocols.

Our broad product portfolio, which includes LED backlighting and Solid-State Lighting (SSL) LED driver ICs, and proprietary digital control technology for power conversion, enable high quality solutions at a low cost. LED backlighting performed strongly during Q3 2019, contributing to the expansion of our customer base in the high-end TV market, as well as targeting the mobile and automotive display markets over the medium term.

With over 4.0 billion CMICs having been shipped since launch, Dialog's configurable technology, including the highly successful GreenPAK™ product family, has become established as the leading choice in the market. Low power consumption and in-system programming enables customers to rapidly customise and integrate multiple analog, logic and discrete components into a single chip. In Q3 2019, we launched our first automotive grade CMIC device bringing Dialog's GreenPAK™ platform to the automotive space, providing lower project costs, an accelerated time to market and unified development flows. This CMIC, along with other members of the GreenPAK family, replace dozens of components in automotive applications to optimize flexibility, footprint and a reduction of the bill of materials. During the quarter, our CMIC incorporating Dialog's industry-leading LDO regulator was adopted by three tier 1 mobile customers and is being evaluated by various other customers.

Connectivity and Audio (C&A)

During Q3 2019, revenue was 27% above Q3 2018 as a result of the strong performance of Bluetooth® low energy and the new audio products, alongside the revenue contribution from the acquisition of FCI. Underlying operating profit in C&A was broadly in line with Q3 2018 at US$5.4 million mainly due to the acquisition of FCI.

Revenue from our SmartBond™ System-on-Chip (SoC) was 51% above Q3 2018, due to the ramp of new products from customers in Korea and China. The DA1469x family, the latest addition to Dialog's SmartBond™ line, was adopted by Samsung's Galaxy Fit fitness tracker. Our most advanced SmartBond™ product enables the Galaxy Fit seamless smartphone connectivity while conserving energy to extend battery life. The Bluetooth® low energy market is estimated to grow over 20% CAGR over the 2019-2022 period[5], a reflection of the continuing adoption of the technology across a wide range of applications. Our strategy remains focused on targeted verticals, like wearables, proximity tags, smart home, gaming accessories and connected health. On 4th November we launched SmartBond™ TINY, the latest addition to our Bluetooth® low energy offering. SmartBond TINY has been designed to power the next billion IoT devices, lowering the cost of adding Bluetooth® low energy functionality to a system without compromising performance or size.

New audio technology performed strongly during Q3 2019, up 65% over Q3 2018. The C&A Segment is targeting the rapidly-growing consumer wireless headset market with our SmartBeat™ wireless Audio IC. This technology enables a new immersive headset experience and supports both wired USB 3.0 Type-C™ and Bluetooth® based consumer headsets. Our product portfolio targeting the headset market also includes a family of highly-integrated audio codec chips that deliver best-in-class active noise cancellation (ANC), providing optimal audio performance in any environment.

5 Source: IHS Technology October 2019 and Company estimates.

Dialog Semiconductor invites you today at 07.30 am (London) / 08.30 am (Frankfurt) to take part in a live conference call and to listen to management's discussion of the Company's Q3 2019 performance, as well as guidance for Q4 2019. Participants will need to register using the link below. A full list of dial in numbers will also be available. To register for the webcast and receive dial in numbers, the conference PIN and a unique User ID please click on the link below:

https://www.incommglobalevents.com/registration/client/2298/dialog-semiconductor-2019-q3-results/

In parallel to the call, the presentation will be available at:

https://webcast.openbriefing.com/dialog-Q3results/

The presentation will also be available under the investor relations section of the Company's website at:

https://www.dialog-semiconductor.com/investor-relations/results-center

A replay will be posted on the Dialog website four hours after the conclusion of the presentation and will be available at:

https://www.dialog-semiconductor.com/investor-relations/results-center

The full release including the Company's unaudited consolidated financial statements for the quarter ended 27 September 2019 is available under the investor relations section of the Company's website at:

https://www.dialog-semiconductor.com/investor-relations/results-center

For further information please contact:

Dialog Semiconductor
Jose Cano
Head of Investor Relations
T: +44 (0)1793 756 961
jose.cano@diasemi.com

FTI Consulting London
Matt Dixon
T: +44 (0)2037 271 137
matt.dixon@fticonsulting.com

FTI Consulting Frankfurt
Anja Meusel
T: +49 (0)69 9203 7120
anja.meusel@fticonsulting.com

Press release – 6 November 2019 continued

About Dialog Semiconductor

Dialog Semiconductor provides highly integrated standard (ASSP) and custom (ASIC) mixed-signal integrated circuits (ICs), optimised for smartphone, tablet, IoT, LED Solid-State Lighting (SSL), and Smart Home applications. Dialog brings decades of experience to the rapid development of ICs while providing flexible and dynamic support, world-class innovation and the assurance of dealing with an established business partner. With world-class manufacturing partners, Dialog operates a fabless business model and is a socially responsible employer pursuing many programs to benefit employees, the community, other stakeholders and the environment we operate in.

Dialog's power saving technologies including DC-DC configurable system power management deliver high efficiency and enhance the consumer's user experience by extending battery lifetime and enabling faster charging of their portable devices. Its technology portfolio also includes audio, Bluetooth® Low Energy, Rapid Charge™ AC/DC power conversion and multi-touch.

Dialog Semiconductor Plc is headquartered in London with a global sales, R&D and marketing organisation. It currently has approximately 2,000 employees worldwide. In 2018, it had approximately US$ 1.44 billion in revenue. The company is listed on the Frankfurt (XETRA: DLG) stock exchange (Regulated Market, Prime Standard, ISIN GB0059822006) and is a member of the German TecDax and MDAX indices.

Forward Looking Statements

This press release contains "forward-looking statements" that reflect management's current views with respect to future events. The words "anticipate," "believe," "estimate", "expect," "intend," "may," "plan," "project" and "should" and similar expressions identify forward-looking statements. Such statements are subject to risks and uncertainties, including, but not limited to: an economic downturn in the semiconductor and telecommunications markets; changes in currency exchange rates and interest rates, the timing of customer orders and manufacturing lead times, insufficient, excess or obsolete inventory, the impact of competing products and their pricing, political risks in the countries in which we operate or sale and supply constraints. If any of these or other risks and uncertainties occur (some of which are described under the heading "Managing risk and uncertainty" in Dialog Semiconductor's most recent Annual Report) or if the assumptions underlying any of these statements prove incorrect, then actual results may be materially different from those expressed or implied by such statements. We do not intend or assume any obligation to update any forward-looking statement which speaks only as of the date on which it is made, however, any subsequent statement will supersede any previous statement.

Financial review

Basis of preparation

Interim financial statements

The interim financial statements of Dialog Semiconductor Plc ("the Company") and its subsidiaries (together "Dialog" or "the Group") for the three- and nine-month periods ended 27 September 2019 are set out in Section 2 of this Interim Report.

The interim financial statements are unaudited but have been reviewed by the Company's auditor, Deloitte LLP, whose review report is set out on page 14.

The Group's significant accounting policies are unchanged compared with the year ended 31 December 2018 (see pages 101 to 107 of our Annual Report and Accounts 2018), except for the adoption of IFRS 16 *Leases* with effect from 1 January 2019.

Recent accounting pronouncements that have not yet been adopted by the Group are set out in note 1 to the interim financial statements.

Adoption of IFRS 16

IFRS 16 *Leases* provides a single lessee accounting model, requiring lessees to recognise a right-of-use asset and a lease liability for all leases, except those with a short lease term and/or involving an underlying asset of low value. In summary, for lessees, the distinction between an operating lease and a finance lease has disappeared and most operating leases are accounted for similarly to the way in which finance leases were accounted for under the predecessor accounting standard, IAS 17 *Leases*.

We adopted IFRS 16 using a modified retrospective approach whereby prior periods were not restated but cumulative effect adjustments were made to the opening consolidated balance sheet on the transition date, 1 January 2019. We recognised lease liabilities totalling US$67.6 million on adoption of IFRS 16 and corresponding right-of-use assets totalling US$66.4 million (after deducting existing net accrued lease rentals of US$1.2 million).

During 9M 2019, the effect of IFRS 16 was to increase operating profit by US$1.1 million but to reduce net income by US$0.2 million.

Details of the adoption of IFRS 16 and its financial effect are set out in note 18 to the interim financial statements.

Non-IFRS measures

Underlying measures of revenue, profitability and free cash flow quoted in the Financial Review are non-IFRS measures.

Reconciliations of these measures to the nearest equivalent IFRS measures on a consolidated basis are presented in Section 3 of this Interim Report.

Recent corporate transactions

Acquisition of Creative Chips

On 7 October 2019, we announced that we had agreed to acquire a 100% equity interest in Creative Chips, a supplier of integrated circuits ("ICs") to the Industrial Internet of Things ("IIoT") market.

We completed the acquisition on 31 October 2019.

We acquired Creative Chips for US$80.0 million on a cash- and debt-free basis. Additional consideration of up to US$23.0 million in cash may be payable contingent on Creative Chips' performance against revenue targets for 2020 and 2021.

On completion, we paid initial consideration of US$83.7 million in cash, including US$3.7 million in respect of Creative Chip's estimated cash, debt and working capital levels on completion that may be subject to adjustment once those amounts have been finalised.

During Q3 2019, we incurred transaction costs of US$0.5 million in relation to the acquisition of Creative Chips (within general and administrative expenses).

Completion of agreements with Apple

Licensing and asset transfer agreement

On 11 October 2018, we announced that we had entered into an agreement with Apple Inc. ("Apple") to license our power management technologies and to transfer to Apple certain assets and over 300 employees from our design centres in the UK, Germany and Italy.

Following the receipt of the necessary regulatory approvals and satisfaction of the other closing conditions, the transaction closed on 8 April 2019. Apple paid Dialog US$300.0 million in respect of the licensing arrangements and asset transfers.

Pursuant to the agreement, Dialog granted to Apple:

- a perpetual licence over Dialog's Power Management IP as it existed at the closing date; and
- an effective licence over certain of Dialog's IP as it existed at the closing date and is developed for a period of at least four years thereafter.

On closing of the licensing and asset transfer agreement, Apple made an interest-free prepayment to Dialog of US$300.0 million. On initial recognition, we measured the prepayment at its fair value of US$288.6 million. We considered that the resulting "below market element" of the prepayment of US$11.4 million represented additional consideration in respect of the licensing arrangements and asset transfers.

We allocated the total consideration of US$311.4 million in respect of the licensing arrangements and asset transfers as follows:

- US$145.8 million to the perpetual IP licence;
- US$136.4 million to the effective IP licence; and
- US$29.2 million to the design centre businesses transferred.

We consider that the perpetual licence granted Apple a "right to use" the related IP and therefore recognised the related consideration as revenue on the closing date.

We consider that the effective licence granted Apple a "right to access" the related IP and are therefore recognising the related consideration as revenue over the four-year period following the closing date. We recognised revenue of US$12.2 million in relation to the effective licence in 9M 2019.

We recognised a gain of US$15.9 million on the transfer of the design centre businesses in Q2 2019 (within other operating income).

We incurred transaction costs totalling US$18.7 million in relation to the agreement with Apple, of which US$10.9 million was incurred during 9M 2019 (within general and administrative expenses).

Further details of the transaction are set out in note 6 to the interim financial statements.

Prepayment from Apple

It is intended that the US$300.0 million prepayment will be recouped by Apple against amounts payable to Dialog for the purchase of certain of our products over the three-year period ending on 31 March 2022.

Settlement of the prepayment is scheduled to take place in quarterly instalments in arrears such that US$200.0 million is settled in the first year and US$50.0 million is settled in each of the second and third years. During each quarter, Apple will settle our invoices on its normal payment terms. If there are insufficient invoices outstanding on a recoupment date, Apple may require us to settle the shortfall against the scheduled recoupment in cash.

We account for the prepayment as a financial liability measured at amortised cost. At the end of Q3 2019, the carrying amount of the liability was US$242.6 million.

Financial review continued

Acquisition of FCI

On 31 May 2019, we completed the acquisition of Silicon Motion Technology Corporation's Mobile Communications product group, branded as FCI.

We acquired FCI for US$45.0 million on a cash and debt-free basis. We paid consideration of US$54.2 million in cash, including US$9.2 million in respect of FCI's estimated cash and working capital on completion that may be subject to adjustment once those amounts have been agreed with the seller.

FCI is included in our Connectivity & Audio segment where we will use its technology to enhance our IoT offerings.

We have recognised provisional goodwill of US$13.7 million on the acquisition of FCI. Details are set out in note 7 to the interim financial statements.

During 9M 2019, we incurred transaction costs of US$2.2 million in relation to the acquisition of FCI (within general and administrative expenses).

Acquisition of Silego

We completed the acquisition of Silego Technology Inc. ("Silego") on 1 November 2017.

Contingent consideration of up to US$30.4 million was payable for the acquisition of Silego dependent on Silego's revenue in 2017 and 2018.

Silego's revenue for 2018 was such that US$17.9 million of the second instalment of up to US$20.4 million was payable. In February 2019, we paid US$16.7 million in settlement of the element of the second instalment that was attributable to the shares and vested options acquired and attributed the balance to deferred cash rights that are payable over the period to March 2021.

During 9M 2019, we also paid deferred consideration of US$1.7 million in relation to the purchase of Silego.

Disposal of Dyna Image

On 7 December 2018, we agreed to sell our shareholding in Dyna Image Corporation ("Dyna Image") for consideration of between US$2.4 million and US$5.0 million. We obtained the necessary regulatory approvals but the purchaser was unable to complete the transaction. As a result, the sale agreement was terminated on 2 September 2019 and we entered into a new agreement to sell our shareholding to another purchaser for a nominal amount.

Since the end of 2018, the carrying amount of the Group's investment in Dyna Image has been nil, so no additional loss will be recognised on the sale.

The transaction is expected to close in the fourth quarter of 2019.

Results of operations

Segment reorganisation and measurement changes

With effect from the beginning of Q2 2019, the Group made a number of organisational changes. Details of the changes are set out in note 3 to the interim financial statements.

Following the changes, the Group has three reportable segments: Custom Mixed Signal; Advanced Mixed Signal; and Connectivity & Audio.

At the same time as effecting the organisational changes, the Management Team changed its focus from IFRS measures to underlying measures as the principal basis for allocating resources to and assessing the financial performance of the Group's businesses. Underlying revenue is therefore the measure of segment revenue and underlying operating profit/loss the measure of segment profit/loss that is now presented in the Group's segment disclosures.

In the analysis of the Group's results by reportable segment presented below, comparative information for 9M 2018 has been restated to reflect these organisational and measurement changes.

Analysis by reportable segment

Custom Mixed Signal's underlying revenue was US$709.1 million in 9M 2019 compared with US$714.5 million in 9M 2018, a decrease of 1%. Revenue declined principally due to the effect of our reduced share of volume for the main PMIC on our largest customer's 2018 smartphone platform, though this was largely offset by higher demand for our custom PMICs on other products.

Revenue from our largest customer for products not covered by the perpetual IP licence increased to US$201.7 million in 9M 2019 compared with US$90.5 million in 9M 2018.

Custom Mixed Signal's underlying operating profit was US$200.2 million compared with US$170.1 million in 9M 2018. Underlying operating profit increased principally due to income of US$12.5 million received from Apple for product development work and the reduction in R&D expenses following the transfer of design centre businesses to Apple at the beginning of Q2 2019. Underlying operating margin was 28.2% compared with 23.8% in 9M 2018.

Advanced Mixed Signal's underlying revenue was US$185.0 million in 9M 2019 compared with US$183.8 million in 9M 2018, an increase of 1%. Revenue increased principally due to growth in sales of backlighting ICs and CMICs, though this was largely offset by lower sales of rapid charge ICs and AC/DC charger ICs for smartphone power adaptors.

Advanced Mixed Signal's underlying operating profit was US$12.5 million compared with US$20.2 million in 9M 2018. While underlying operating profit benefited from favourable product mix, this was outweighed by the effect of higher R&D expenses. Underlying operating margin declined to 6.8% compared with 11.0% in 9M 2018.

Results by reportable segment

	Underlying revenue			Underlying operating profit/(loss)	
US$ millions	**9M 2019**	Restated* 9M 2018	Change	**9M 2019**	Restated* 9M 2018
9M 2019 compared with 9M 2018					
Custom Mixed Signal	**709.1**	714.5	(1)%	**200.2**	170.1
Advanced Mixed Signal	**185.0**	183.8	1%	**12.5**	20.2
Connectivity & Audio	**133.6**	113.0	18%	**17.3**	9.1
Total segments	**1,027.7**	1,011.3	2%	**230.0**	199.4
Corporate and other unallocated items	**12.2**	0.1	nm	**3.1**	(21.2)
Total Group	**1,039.9**	1,011.4	3%	**233.1**	178.2

* Restated to reflect the segment reorganisation and measurement changes.

Connectivity & Audio's underlying revenue was US$133.6 million in 9M 2019 compared with US$113.0 million in 9M 2018, an increase of 18%. Connectivity & Audio's revenue increased principally due to strong growth in demand for Bluetooth® low energy and new audio products.

Connectivity & Audio's underlying operating profit was higher at US$17.3 million compared with US$9.1 million in 9M 2018, principally due to increased sales volumes with beneficial product mix. Underlying operating margin was significantly higher at 12.9% compared with 8.0% in 9M 2018.

Corporate and other unallocated items comprise the costs of operating central corporate functions, the Group's share-based compensation expense and certain other unallocated items including, from Q2 2019, the revenue recognised in relation to the effective IP licence granted to Apple.

Corporate and other unallocated items represented an underlying operating profit of US$3.1 million compared with a loss of US$21.2 million in 9M 2018, with the improvement being principally due to the recognition of effective IP licence revenue of US$12.2 million in 9M 2019 and lower unallocated R&D expenses.

Analysis of the Group's results

Revenue was US$1,185.7 million in 9M 2019 compared with US$1,011.4 million in 9M 2018, with the substantial increase being principally due to the recognition of revenue of US$158.0 million in relation to the licensing arrangements with Apple.

Excluding the perpetual IP licence fee of US$145.8 million, underlying revenue was US$1,039.9 million in 9M 2019 compared with US$1,011.4 million in 9M 2018, an increase of 3%.

Underlying revenue increased principally due to the strong growth in volumes in Connectivity & Audio and the recognition of revenue of US$12.2 million in relation to the effective IP licence granted to Apple.

Cost of sales was US$527.3 million in 9M 2019 compared with US$529.8 million in 9M 2018, broadly unchanged because the benefit of manufacturing cost savings was largely offset by higher inventory provisions.

Gross profit was US$658.4 million in 9M 2019 compared with US$481.6 million in 9M 2018, with the substantial increase being principally due to the recognition of the Apple licence fees in Q2 2019.

Gross margin was 55.5% compared with 47.6% in 9M 2018. Gross margin was higher principally due to the recognition of the Apple licence fees.

Underlying gross profit was US$515.6 million compared with US$486.2 million in 9M 2018, an increase of 6%. Underlying gross margin was 150 basis points higher at 49.6% compared with 48.1% in 9M 2018.

Underlying gross profit excludes the perpetual IP licence fee of US$145.8 million, share-based compensation expenses and related payroll taxes of US$2.1 million (9M 2018: US$1.5 million) and the consumption of the fair value uplift on acquired inventory of US$0.9 million (9M 2018: US$3.1 million).

Selling and marketing expenses increased to US$67.3 million in 9M 2019 compared with US$62.7 million in 9M 2018.

Underlying selling and marketing expenses were also higher at US$51.7 million compared with US$48.9 million in 9M 2018 and represented 5.0% of the Group's underlying revenue compared with 4.8% in 9M 2018.

Underlying selling and marketing expenses exclude share-based compensation expenses and related payroll taxes totalling US$3.9 million (9M 2018: US$2.9 million), amortisation of US$11.4 million (9M 2018: US$10.5 million) on the fair value uplift of acquired intangible assets and deferred consideration payable for Silego treated as compensation expense of US$0.3 million (9M 2018: US$0.4 million).

General and administrative expenses were US$68.7 million in 9M 2019 compared with US$58.7 million in 9M 2018, with the increase being largely due to acquisition-related and corporate transaction costs incurred in 9M 2019.

Underlying general and administrative expenses decreased slightly to US$41.8 million compared with US$42.3 million in 9M 2018 and represented 4.0% of the Group's underlying revenue compared with 4.2% in 9M 2018.

Underlying general and administrative expenses exclude share-based compensation and related payroll taxes totalling US$12.7 million (9M 2018: US$9.7 million), acquisition-related and corporate transaction costs of US$13.6 million (9M 2018: US$4.7 million), integration costs of US$0.5 million (9M 2018: US$1.9 million) and deferred consideration payable for Silego treated as compensation expense of US$0.1 million (9M 2018: US$0.1 million).

R&D expenses were US$235.0 million in 9M 2019 compared with US$241.4 million in 9M 2018.

R&D costs totalled US$250.3 million (9M 2018: US$264.2 million), of which US$11.2 million (9M 2018: US$18.9 million) was capitalised and US$4.1 million (9M 2018: US$3.9 million) was offset by R&D expenditure credits. R&D costs were lower compared with 9M 2018 principally due to the transfer of design centre businesses to Apple at the beginning of Q2 2019.

Underlying R&D expenses were US$211.9 million in 9M 2019 compared with US$219.1 million in 9M 2018 and represented 20.4% of the Group's underlying revenue compared with 21.7% in 9M 2018.

Summary of the Group's results

	IFRS basis (unaudited)		Underlying (unaudited)*		
US$ millions unless stated otherwise	**9M 2019**	9M 2018	**9M 2019**	9M 2018	Change
Revenue	**1,185.7**	1,011.4	**1,039.9**	1,011.4	+3%
Gross margin	**55.5%**	47.6%	**49.6%**	48.1%	+150bps
Operating expenses	**371.0**	362.8	**305.4**	310.3	-2%
Operating profit	**326.2**	122.6	**233.1**	178.2	+31%
Operating margin	**27.5%**	12.1%	**22.4%**	17.6%	+480bps
Diluted EPS	**$3.33**	$1.05	**$2.46**	$1.83	+34%
Free cash flow			**405.1**	147.4	+175%

* Non-IFRS measures (see section 3 of this Interim Report)

Financial review continued

Underlying R&D expenses exclude share-based compensation expenses and related payroll taxes totalling US$15.5 million (9M 2018: US$15.2 million), amortisation of US$7.3 million (9M 2018: US$6.5 million) on the fair value uplift of acquired technology, deferred consideration payable for Silego treated as compensation expense of US$0.3 million (9M 2018: US$0.4 million) and, in 9M 2018, integration costs of US$0.2 million.

Other operating income was substantially higher at US$38.8 million in 9M 2019 compared with US$3.8 million in 9M 2018, principally due to the recognition in Q2 2019 of the gain of US$15.9 million on the transfer of design centre businesses to Apple and higher income from R&D contracts, in particular, US$12.5 million received from Apple for product development costs incurred between October 2018 and April 2019.

Excluding the gain on the transfer of the design centre businesses, underlying other operating income was US$22.9 million in 9M 2019 compared with US$2.3 million in 9M 2018.

Operating profit was US$326.2 million in 9M 2019 compared with US$122.6 million in 9M 2018.

Underlying operating profit was US$233.1 million compared with US$178.2 million in 9M 2018, an increase of 31%. Underlying operating profit increased principally due to the improvement in underlying gross profit, lower underlying R&D expenses and the income receivable from Apple for development work recognised in Q2 2019.

Underlying operating margin was consequently higher at 22.4% compared with 17.6% in 9M 2018.

Interest income was US$16.9 million in 9M 2019 compared with US$6.6 million in 9M 2018, with the increase reflecting the higher average cash balance during 9M 2019.

Interest expense was US$8.1 million in 9M 2019 compared with US$2.3 million in 9M 2018, with the increase reflecting the recognition of interest expense of US$4.0 million on the prepayment from Apple and US$2.3 million on lease liabilities following the adoption of IFRS 16.

Other finance expense was US$4.0 million in 9M 2019 compared with US$8.0 million in 9M 2018.

We recognised a net currency translation loss on monetary assets and liabilities of US$3.8 million compared with a loss of US$0.6 million in 9M 2018.

We recognised a fair value loss of US$1.4 million (9M 2018: loss of US$8.6 million) on the warrants that we hold over shares in Energous and a credit arising from the amortisation of the gain on initial recognition of the second tranche of warrants amounting to US$1.2 million (9M 2018: US$1.2 million).

Income tax expense was US$74.3 million (9M 2018: US$35.8 million) on profit before tax of US$331.0 million (9M 2018: US$118.9 million), an effective tax rate for the period of 22.4% (9M 2018: 30.1%).

Our income tax expense for the first nine months of the year is calculated by applying the estimated effective tax rate for the full year to the profit before tax for the period excluding specific items that distort the tax rate and then by taking into account the tax effect of those specific items.

Our relatively high effective tax rate for 9M 2018 was principally due to the distorting effect on our income tax expense of the tax and accounting treatments of share-based compensation and business combinations.

Our underlying income tax expense was US$48.8 million (9M 2018: US$40.0 million) on underlying profit before tax of US$238.5 million (9M 2018: US$183.6 million). Our underlying effective tax rate for 9M 2019 was therefore 20.5%, which compares with 21.8% for 9M 2018.

Net income was US$256.7 million in 9M 2019 compared with US$81.9 million in 9M 2018. Underlying net income was US$189.6 million compared with US$142.5 million in 9M 2018, an increase of 33%.

Basic earnings per share were US$3.53 (9M 2018: US$1.11) based on the weighted average of 72.6 million shares (9M 2018: 73.8 million shares) that were in issue during the period excluding the weighted average of 2.0 million shares (9M 2018: 2.5 million shares) held by employee benefit trusts and, in 9M 2019, the weighted average of 1.8 million shares that were held in treasury. Underlying basic earnings per share were US$2.61 (9M 2018: US$1.93).

Diluted earnings per share were US$3.33 (9M 2018: US$1.05). Diluted earnings per share additionally reflect the weighted average of 4.4 million (9M 2018: 3.9 million) dilutive employee share options. Underlying diluted earnings per share were US$2.46 (9M 2018: US$1.83).

Summary cash flow statement

US$ millions	9M 2019	9M 2018
Cash generated from operations	**473.0**	214.4
Interest received, net	**13.0**	5.3
Income taxes paid	**(47.0)**	(27.5)
Cash inflow from operating activities	**439.0**	192.2
Purchase of property, plant and equipment	**(10.1)**	(20.2)
Purchase of intangible assets	**(4.0)**	(3.9)
Capitalised development expenditure	**(11.2)**	(19.0)
Capital element of lease payments	**(8.6)**	(1.7)
Free cash flow	**405.1**	147.4
Purchase of FCI, net of acquired cash	**(44.6)**	–
Payment of consideration for Silego	**(18.4)**	(12.1)
Proceeds from transfer of design centres, net of cash disposed	**27.8**	–
Receipt of prepayment from Apple	**288.6**	–
Cash settlement of prepayment from Apple	**(20.3)**	–
Sale of Dialog shares by EBTs	**3.2**	2.1
Purchase of own shares	**(148.9)**	–
Other cash flows, net	**(0.2)**	0.1
Net cash inflow during the period	**492.3**	137.5
Currency translation differences	**0.7**	(0.2)
Increase in cash and cash equivalents	**493.0**	137.3

Cash flows

Cash inflow from operating activities was US$439.0 million in 9M 2019 compared with US$192.2 million in 9M 2018.

Cash generated from operations before changes in working capital was US$539.9 million compared with US$212.8 million in 9M 2018, the increase being principally due to the receipt of consideration totalling US$282.2 million in relation to the IP licensing arrangements with Apple. Excluding the cash inflow from the Apple licences, cash generated from operations before changes in working capital was US$257.7 million compared with US$212.8 million in 9M 2018.

Net working capital increased by US$66.9 million in 9M 2019 compared with a decrease of US$1.6 million in 9M 2018.

Demand for our products has historically been higher in the fourth quarter of the year and lower in the first and second quarters.

Inventory decreased during 9M 2019, releasing cash of US$18.9 million, principally reflecting higher than expected demand for our products during Q3 2019. At the end of Q3 2019, inventories represented 54 days' cost of sales in the preceding quarter (end of 2018: 61 days' cost of sales).

Trade and other receivables increased during 9M 2019, absorbing cash of US$37.0 million and cash flow from operations was further reduced by US$29.7 million due to the partial settlement of the first quarterly instalment of the prepayment from Apple by recoupment against receivables. At the end of Q3 2019, trade and other receivables represented 32 days' sales in the preceding quarter (end of 2018: 24 days' sales) and reflected our use of receivables financing facilities.

Trade and other payables declined during 9M 2019, absorbing cash of US$9.8 million. At the end of Q3 2019, trade and other payables represented 50 days' cost of sales in the preceding quarter (end of 2018: 50 days' cost of sales).

Movements on other working capital items had the effect of absorbing cash of US$9.3 million during 9M 2019.

Net interest received was US$13.0 million in 9M 2019 compared with US$5.3 million in 9M 2018.

Net income tax payments were US$47.0 million in 9M 2019 compared with US$27.5 million in 9M 2018. Income tax cash flows comprise payments on account in respect of current year taxable profits and adjusting payments or receipts in respect of earlier years.

Cash outflow from investing activities was US$60.5 million in 9M 2019 compared with US$55.2 million in 9M 2018.

Capital expenditure comprising cash outflows in relation to the purchase of property, plant and equipment and intangible assets and capitalised development expenditure totalled US$25.3 million compared with US$43.1 million in 9M 2018. Capital expenditure declined due to the transfer of design centre businesses to Apple in April 2019.

During 9M 2019, there was a cash outflow of US$44.6 million on the acquisition of FCI (net of cash of US$9.6 million held by the business on the acquisition date).

During 9M 2019, we paid US$16.7 million (9M 2018: US$9.1 million) in settlement of contingent consideration and US$1.7 million (9M 2018: US$2.3 million) in respect of deferred consideration payable for Silego. During 9M 2018, we also paid a purchase price adjustment of US$0.7 million following agreement with the vendors of Silego's cash, debt and working capital levels on completion.

During 9M 2019, we received proceeds of US$27.8 million on the transfer of design centre businesses to Apple (net of cash of US$1.5 million held by the businesses on the transfer date).

Cash flow from financing activities was an inflow of US$113.8 million in 9M 2019 compared with an inflow of US$0.5 million in 9M 2018.

Balance sheet

Summary balance sheet

US$ millions	As at 27 September 2019	As at 31 December 2018
Assets		
Cash and cash equivalents	**1,170.9**	677.8
Other current assets	**301.9**	296.2
Total current assets	**1,472.8**	974.0
Goodwill	**453.0**	439.5
Other intangible assets	**224.8**	217.4
Property, plant and equipment – owned	**52.3**	66.4
Property, plant and equipment – leased	**53.9**	–
Deferred tax assets	**7.6**	6.0
Other non-current assets	**8.4**	13.8
Total non-current assets	**800.0**	743.1
Total assets	**2,272.8**	1,717.1
Liabilities and equity		
Current liabilities	**550.8**	393.9
Deferred tax liabilities	**13.2**	8.0
Other non-current liabilities	**229.6**	12.7
Total liabilities	**793.6**	414.6
Total equity	**1,479.2**	1,302.5
Total liabilities and equity	**2,272.8**	1,717.1

During 9M 2019, we recognised the receipt of the prepayment from Apple at its fair value of US$288.6 million and paid US$20.3 million in cash in partial settlement of the first quarterly instalment of US$50.0 million.

During 9M 2019, there was a cash outflow of US$148.9 million on the purchase of shares under the Company's share buyback programme.

During 9M 2019, the cash outflow on the capital element of lease payments was $8.6 million, higher compared with US$1.7 million in 9M 2018 due to the recognition of additional lease liabilities following the adoption of IFRS 16.

During 9M 2019, employee benefit trusts received proceeds of US$3.2 million (9M 2018: US$2.1 million) on the exercise of share options.

Liquidity and capital resources

Cash and cash equivalents

At the end of Q3 2019, cash and cash equivalents amounted to US$1,170.9 million (end of 2018: US$677.8 million), which principally comprised investments in money market funds and bank deposits with a maturity of three months or less.

Prepayment from Apple

At the end of Q3 2019, the principal amount of the prepayment outstanding was US$250.0 million, of which US$162.5 million is expected to be settled by recoupment against invoices outstanding or in cash within 12 months.

We settled the second quarterly instalment of US$50.0 million in October 2019 wholly by recoupment against invoices outstanding.

Revolving credit facility

Since July 2017, we have had a US$150 million revolving credit facility provided by four financial institutions. The facility is committed and available for general corporate purposes. In June 2019, the full amount of the facility was extended for a further year and will now mature on 28 July 2022.

We retain the option to increase the amount of the facility by US$75 million subject to certain conditions.

We have not made any drawings under the facility.

Receivables financing facilities

We utilise non-recourse receivables financing facilities provided by two financial institutions in an aggregate amount of US$240 million. In July 2019, the principal facility of US$220 million was extended for a further two years and will now mature on 31 October 2021.

Gross receivables sold under the facilities decreased by US$26.5 million to US$87.0 million at the end of Q3 2019 compared with US$113.5 million at the end of 2018.

At the end of Q3 2019, cash and cash equivalents included US$74.5 million (end of 2018: US$96.1 million) in relation to receivables sold under these facilities.

Financial review continued

Share buyback programme

Since initiating the share buyback programme in May 2016, the Company has purchased 10,090,668 of its own ordinary shares and returned €338.9 million (US$374.1 million) to shareholders.

On 6 November 2018, we announced details of the first tranche of the share buyback programme pursuant to an authority granted by shareholders at the Company's 2018 AGM, under which the Company committed to purchase shares with a minimum cost of €100.0 million and a maximum cost of €150.0 million.

We completed the first and final settlement of this tranche on 31 May 2019, purchasing 3,941,852 shares at a cost of €100.0 million (US$111.5 million). We also incurred transaction costs of US$0.6 million.

At the Company's AGM on 2 May 2019, the Directors were granted a new authority to purchase up to 11,457,321 of the Company's ordinary shares, representing approximately 15% of the issued ordinary share capital of the Company as at 27 March 2019. Such authority shall (unless previously renewed, varied or revoked) expire on the day before the next AGM of the Company or on 30 June 2020, whichever is the earlier.

On 5 June 2019, we announced details of the first tranche of purchases under the 2019 AGM authority, under which the Company committed to purchase shares with a minimum cost of €125.0 million and a maximum cost of €150.0 million.

On 19 September 2019, we completed the first intermediate settlement of this tranche, purchasing 800,000 shares at an initial cost of €33.1 million (US$36.6 million). We also incurred transaction costs of US$0.2 million.

Subsequent to the balance sheet date, we completed the second intermediate settlement of this tranche, purchasing 865,000 shares at an initial cost of €37.1 million (US$41.3 million).

We have a remaining maximum obligation to purchase shares under this tranche of €79.8 million. The broker may continue to purchase shares under this tranche until 5 December 2019.

Balance sheet

Non-current assets totalled US$800.0 million at the end of Q3 2019 compared with US$743.1 million at the end of 2018, an increase of US$56.9 million. During 9M 2019, we recognised provisional goodwill and other intangible assets totalling US$48.1 million on the acquisition of FCI and right-of-use assets totalling US$66.4 million on the adoption of IFRS 16, the effect of which was partially offset by depreciation and amortisation totalling US$68.8 million.

Current assets totalled US$1,472.8 million at the end of Q3 2019 compared with US$974.0 million at the end of 2018, an increase of US$498.8 million.

Cash and cash equivalents increased by US$493.0 million to US$1,170.9 million. Other current assets increased slightly by US$5.7 million to US$301.9 million.

Current liabilities totalled US$550.8 million at the end of Q3 2019 compared with US$393.9 million at the end of 2018, an increase of US$156.9 million.

Trade and other payables decreased by US$6.1 million to US$116.0 million. Current financial liabilities increased by US$114.3 million to US$311.2 million, principally due to the addition of the current element of the prepayment from Apple of US$157.5 million and current lease liabilities of US$12.0 million following the adoption of IFRS 16.

Income taxes payable increased by US$22.9 million to US$31.1 million, reflecting higher taxable profits and the timing of tax payments.

Other current liabilities increased by US$29.2 million to US$87.4 million, reflecting the addition of the current element of the deferred revenue relating to the effective IP licence granted to Apple of US$33.0 million.

Non-current liabilities totalled US$242.8 million at the end of Q3 2019 compared with US$20.7 million at the end of 2018, an increase of US$222.1 million.

Non-current financial liabilities increased from US$0.8 million to US$128.2 million, principally due to the addition of the non-current element of the prepayment from Apple of US$85.1 million and non-current lease liabilities of US$43.1 million following the adoption of IFRS 16.

Deferred tax liabilities increased by US$5.2 million to US$13.2 million principally due to the recognition of deferred tax liabilities on the identifiable intangible assets acquired with FCI.

Other non-current liabilities increased from US$8.9 million to US$98.5 million, reflecting the addition of the non-current element of the deferred revenue relating to the effective IP licence granted to Apple of US$91.1 million.

Total equity was US$1,479.3 million at the end of Q3 2019 compared with US$1,302.5 million at the end of 2018. At the end of Q3 2019, Dialog shares held in treasury amounted to US$148.9 million (end of 2018: $nil) and Dialog shares held by employee benefit trusts amounted to US$22.4 million (end of 2018: US$22.5 million).

Consequences of Brexit

Considerable uncertainty exists as to whether and, if so, when the UK will leave the EU, the terms of any withdrawal agreement between the UK and the EU and the effect of Brexit on the UK's future relationships with the EU, other multilateral organisations and individual countries outside the EU.

We continue to believe that Brexit will not have a significant impact on Dialog in the short term because only a small amount of our revenue is derived from customers in the UK. However, since approximately half of our workforce is based in the EU and our teams are typically comprised of several nationalities, we will monitor very closely any proposed changes to the current regulations in respect of the rights of EU and other nationals to work in the UK, and vice versa.

The longer-term effects of Brexit on our operating environment are difficult to predict and subject to wider global macroeconomic trends and events, but may impact ourselves, our customers and other counterparties.

While the withdrawal negotiations are ongoing and during any subsequent transition period, we will operate on a business as usual basis within applicable regulations and our continuing focus will be on growing our business.

Wissam Jabre
Chief Financial Officer,
Senior Vice President Finance

Other information

Directors and Management Team

Board of Directors

Rich Beyer, Chairman

Dr Jalal Bagherli

Alan Campbell

Mike Cannon

Mary Chan

Joanne Curin*

Nick Jeffery

Eamonn O'Hare

* Joined the Board on 1 August 2019

Management Team

Dr Jalal Bagherli, *Chief Executive Officer*

Vivek Bhan, *Senior Vice President, General Manager, Custom Mixed Signal*

Wissam Jabre, *Chief Financial Officer, Senior Vice President, Finance*

Davin Lee, *Senior Vice President, General Manager, Advanced Mixed Signal*

Alex McCann, *Senior Vice President, Global Operations*

Sean McGrath, *Senior Vice President, General Manager, Connectivity & Audio*

Julie Pope, *Senior Vice President, Human Resources*

Tom Sandoval, *Senior Vice President, Automotive*

Colin Sturt, *Senior Vice President, General Counsel*

John Teegan, *Senior Vice President, Worldwide Sales*

Mark Tyndall, *Senior Vice President, Corporate Development and Strategy*

Going concern

After making enquiries, the Directors consider that the Group has adequate resources to continue in operation for the foreseeable future. As at 27 September 2019, the Group held cash and cash equivalents amounting to US$1,170.9 million and had an undrawn committed US$150.0 million revolving credit facility that, when taken together, significantly exceeded the Group's obligations expected to fall due within the following 12 months. Accordingly, the Directors have adopted the going concern basis in preparing the interim financial statements for the three- and nine-month periods ended 27 September 2019.

Principal risks and uncertainties

We describe the principal risks and uncertainties that could adversely impact the Group's ability to execute its strategic objectives on pages 52 to 56 of our Annual Report and Accounts 2018. In the opinion of the Directors, there has been no fundamental change in the principal risks and uncertainties affecting Dialog since the approval of the Annual Report and Accounts 2018.

Responsibility statement

We confirm that, to the best of our knowledge, the interim financial statements for the three- and nine-month periods ended 27 September 2019 have been prepared in accordance with IAS 34 *Interim Financial Reporting* and the interim management report includes a fair review of the development and performance of the Group during the period, a fair review of material transactions with related parties and changes during the period, and fairly describes the principal risks and uncertainties affecting the Group for the remainder of the year ending 31 December 2019.

Dr Jalal Bagherli
Chief Executive Officer

Wissam Jabre
Chief Financial Officer, Senior Vice President, Finance

6 November 2019

Independent review report to Dialog Semiconductor Plc

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the interim report for the three- and nine-month periods ended 27 September 2019 which comprises the condensed consolidated statement of income, the condensed consolidated statement of comprehensive income, the condensed consolidated balance sheet, the condensed consolidated statement of cash flows, the condensed consolidated statement of changes in equity and the related notes 1 to 19. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the Financial Reporting Council. Our work has been undertaken so that we might state to the Company those matters we are required to state to it in an independent review 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, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The interim report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the interim report in accordance with the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority and the disclosure requirements of the German Securities Trading Act (WpHG).

As disclosed in note 1, the annual financial statements of the Company and its subsidiaries are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this interim report has been prepared in accordance with IAS 34 *Interim Financial Reporting* as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the interim report based on our review.

Scope of review

We conducted our review in accordance with the International Standard on Review Engagements (UK and Ireland) 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements for the three- and nine-month periods ended 27 September 2019 is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting* as adopted by the European Union and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority and the disclosure requirements of the German Securities Trading Act (WpHG).

Deloitte LLP
Statutory Auditor

Reading, UK

6 November 2019

Condensed consolidated statement of income

For the three- and nine-month periods ended 27 September 2019

	Note	Third quarter		First nine months	
		Three months ended 27 September 2019 US$000 (Unaudited)	Three months ended 28 September 2018 US$000 (Unaudited)	**Nine months ended 27 September 2019 US$000 (Unaudited)**	Nine months ended 28 September 2018 US$000 (Unaudited)
Revenue	2, 3	**408,803**	383,574	**1,185,657**	1,011,393
Cost of sales		**(207,645)**	(197,599)	**(527,263)**	(529,794)
Gross profit		**201,158**	185,975	**658,394**	481,599
Selling and marketing expenses		**(23,835)**	(20,432)	**(67,328)**	(62,739)
General and administrative expenses		**(19,776)**	(22,494)	**(68,678)**	(58,680)
Research and development expenses		**(78,846)**	(82,180)	**(235,035)**	(241,358)
Other operating income	4	**5,156**	2,619	**38,807**	3,776
Operating profit	3	**83,857**	63,488	**326,160**	122,598
Interest income		**6,428**	2,654	**16,889**	6,565
Interest expense		**(3,510)**	(664)	**(8,087)**	(2,322)
Other finance expense		**(140)**	(3,186)	**(3,989)**	(7,980)
Profit before income taxes		**86,635**	62,292	**330,973**	118,861
Income tax expense		**(18,439)**	(15,504)	**(74,315)**	(35,832)
Profit after income taxes		**68,196**	46,788	**256,658**	83,029
Share of loss of associate		**–**	(367)	**–**	(1,116)
Net income		**68,196**	46,421	**256,658**	81,913

Earnings per share (US$)	5				
Basic		**0.96**	0.63	**3.53**	1.11
Diluted		**0.91**	0.60	**3.33**	1.05
Weighted average number of shares (in thousands)	5				
Basic		**70,780**	73,966	**72,605**	73,850
Diluted		**74,777**	77,971	**77,043**	77,754

Condensed consolidated statement of comprehensive income

For the three- and nine-month periods ended 27 September 2019

	Third quarter		First nine months	
	Three months ended 27 September 2019 US$000 (Unaudited)	Three months ended 28 September 2018 US$000 (Unaudited)	**Nine months ended 27 September 2019 US$000 (Unaudited)**	Nine months ended 28 September 2018 US$000 (Unaudited)
Net income	**68,196**	46,421	**256,658**	81,913
Other comprehensive income				
Items that may be reclassified to profit or loss in subsequent periods				
Currency translation differences on foreign operations				
– Loss recognised in the period	**(1,771)**	(255)	**(287)**	(444)
– Loss transferred to profit or loss on disposal of a subsidiary	**–**	–	**309**	–
Income tax relating to currency translation differences on foreign operations	**(86)**	(49)	**(123)**	(111)
Cash flow hedges:				
– Fair value loss recognised on effective hedges in the period	**(5,490)**	(2,469)	**(8,096)**	(6,897)
– Fair value loss/(gain) transferred to profit or loss	**2,196**	1,780	**8,635**	(5,183)
Income tax relating to cash flow hedges	**626**	131	**(102)**	2,312
	(4,525)	(862)	**336**	(10,323)
Items that will not be reclassified to profit or loss				
Fair value loss on equity investments	**(1,827)**	(8,194)	**(4,297)**	(16,249)
Income tax relating to equity investments	**–**	–	**–**	1,015
	(1,827)	(8,194)	**(4,297)**	(15,234)
Other comprehensive loss for the period	**(6,352)**	(9,056)	**(3,961)**	(25,557)
Total comprehensive income for the period	**61,844**	37,365	**252,697**	56,356

Condensed consolidated balance sheet

As at 27 September 2019

	Note	**As at 27 September 2019 US$000 (Unaudited)**	As at 31 December 2018* US$000 (Audited)
Assets			
Cash and cash equivalents	8	**1,170,888**	677,848
Trade and other receivables		**153,369**	114,514
Other current financial assets		**581**	202
Inventories	9	**124,685**	149,736
Income tax receivables		**–**	2,146
Other current assets		**23,266**	18,306
		1,472,789	962,752
Assets classified as held for sale	13	**–**	11,295
Total current assets		**1,472,789**	974,047
Goodwill	10	**453,035**	439,508
Other intangible assets	10	**224,844**	217,445
Property, plant and equipment – owned	11	**52,260**	66,359
Property, plant and equipment – leased	11	**53,897**	–
Other investments	12	**5,823**	11,538
Other non-current financial assets		**2,177**	1,807
Other non-current assets		**426**	398
Deferred tax assets		**7,587**	6,034
Total non-current assets		**800,049**	743,089
Total assets		**2,272,838**	1,717,136
Liabilities and equity			
Trade and other payables		**115,993**	122,140
Lease liabilities		**12,027**	–
Other current financial liabilities		**299,160**	196,890
Provisions		**5,109**	5,253
Income taxes payable		**31,094**	8,193
Other current liabilities		**87,378**	58,237
		550,761	390,713
Liabilities directly associated with assets held for sale	13	**–**	3,167
Total current liabilities		**550,761**	393,880
Lease liabilities		**43,118**	–
Other non-current financial liabilities		**85,089**	841
Provisions		**2,879**	3,078
Deferred tax liabilities		**13,180**	7,958
Other non-current liabilities		**98,528**	8,872
Total non-current liabilities		**242,794**	20,749
Ordinary shares		**14,204**	14,204
Share premium account		**403,660**	403,660
Retained earnings		**1,260,100**	930,576
Other reserves	16	**(176,328)**	(23,419)
Dialog shares held by employee benefit trusts		**(22,353)**	(22,514)
Total equity		**1,479,283**	1,302,507
Total liabilities and equity		**2,272,838**	1,717,136

* Extracted from the Company's audited consolidated financial statements for the year ended 31 December 2018.

Condensed consolidated statement of cash flows

For the three- and nine-month periods ended 27 September 2019

		Third quarter		First nine months	
	Note	**Three months ended 27 September 2019 US$000 (Unaudited)**	Three months ended 28 September 2018 US$000 (Unaudited)	**Nine months ended 27 September 2019 US$000 (Unaudited)**	Nine months ended 28 September 2018 US$000 (Unaudited)
Cash flows from operating activities					
Net income		**68,196**	46,421	**256,658**	81,913
Non-cash items within net income:					
– Depreciation of property, plant and equipment		**10,189**	8,138	**30,672**	24,074
– Amortisation of intangible assets		**13,774**	12,538	**38,127**	36,563
– Addition to inventory reserve, net		**2,073**	1,222	**9,523**	3,390
– Share-based compensation expense		**9,435**	9,131	**30,938**	29,749
– Deferred licence revenue		**(6,252)**	–	**(12,232)**	–
– Other non-cash items		**3,766**	1,730	**202**	5,526
Effective IP licence fee received	6	**–**	–	**136,400**	–
Gain on transfer of design centre businesses	6	**–**	–	**(15,898)**	–
Interest income, net		**(2,918)**	(1,990)	**(8,802)**	(4,243)
Income tax expense		**18,439**	15,504	**74,315**	35,832
Cash generated from operations before changes in working capital		**116,702**	92,694	**539,903**	212,804
Changes in working capital:					
– Increase in trade and other receivables		**(58,157)**	(23,186)	**(66,666)**	(19,966)
– Decrease/(increase) in inventories		**28,748**	(8,522)	**18,902**	24,173
– (Increase)/decrease in prepaid expenses		**(444)**	790	**(1,950)**	(4,964)
– Increase/(decrease) in trade and other payables		**19,913**	28,342	**(9,814)**	5,454
– Increase/(decrease) in provisions		**123**	173	**(1,034)**	(586)
– Change in other assets and liabilities		**5,307**	3,985	**(6,303)**	(2,536)
Cash generated from operations		**112,192**	94,276	**473,038**	214,379
Interest paid		**(1,082)**	(117)	**(3,078)**	(398)
Interest received		**6,831**	2,623	**16,105**	5,725
Income taxes paid		**(20,625)**	(9,886)	**(47,048)**	(27,523)
Cash inflow from operating activities		**97,316**	86,896	**439,017**	192,183
Cash flows from investing activities					
Purchase of property, plant and equipment		**(3,157)**	(3,462)	**(10,142)**	(20,245)
Purchase of intangible assets		**(1,770)**	(653)	**(3,957)**	(3,891)
Payments for capitalised development costs		**(2,618)**	(3,731)	**(11,189)**	(18,950)
Purchase of FCI, net of acquired cash	7	**(271)**	–	**(44,593)**	–
Payment of consideration for Silego	7	**(413)**	(508)	**(18,445)**	(12,119)
Proceeds from transfer of design centres, net of cash disposed	6	**–**	–	**27,814**	–
Increase in other long-term assets		**–**	87	**–**	4
Cash outflow from investing activities		**(8,229)**	(8,267)	**(60,512)**	(55,201)
Cash flows from financing activities					
Receipt of prepayment from Apple	6	**–**	–	**288,583**	–
Cash settlement of prepayment from Apple	6	**(20,345)**	–	**(20,345)**	–
Capital element of lease payments		**(2,981)**	–	**(8,662)**	(1,650)
Sale of shares by employee benefit trusts		**719**	639	**3,201**	2,125
Purchase of own shares into treasury		**(36,838)**	–	**(148,933)**	–
Cash (outflow)/inflow from financing activities		**(59,445)**	639	**113,844**	475
Net cash inflow during the period		**29,642**	79,268	**492,349**	137,457
Cash and cash equivalents at beginning of period		**1,141,185**	537,473	**677,848**	479,295
Currency translation differences		**61**	(220)	**691**	(231)
Cash and cash equivalents at end of period	8	**1,170,888**	616,521	**1,170,888**	616,521

Condensed consolidated statement of changes in equity

For the nine-month period ended 27 September 2019

	Ordinary shares US$000	Share premium account US$000	Retained earnings US$000	Other reserves (note 16) US$000	Dialog shares held by employee benefit trusts US$000	Total US$000
Nine months ended 27 September 2019 (Unaudited)						
As at 31 December 2018	**14,204**	**403,660**	**930,576**	**(23,419)**	**(22,514)**	**1,302,507**
Adjustment on initial application of IFRS 16 (note 18)	**–**	**–**	**40**	**–**	**–**	**40**
Adjusted balance as at 1 January 2019	**14,204**	**403,660**	**930,616**	**(23,419)**	**(22,514)**	**1,302,547**
Net income	**–**	**–**	**256,658**	**–**	**–**	**256,658**
Other comprehensive loss	**–**	**–**	**–**	**(3,961)**	**–**	**(3,961)**
Total comprehensive income/(loss)	**–**	**–**	**256,658**	**(3,961)**	**–**	**252,697**
Other changes in equity:						
– Purchase of own shares into treasury	**–**	**–**	**(3,290)**	**(148,948)**	**–**	**(152,238)**
– Share buyback obligation	**–**	**–**	**38,357**	**–**	**–**	**38,357**
– Sale of shares by employee benefit trusts	**–**	**–**	**3,040**	**–**	**161**	**3,201**
– Share-based compensation, net of tax	**–**	**–**	**34,719**	**–**	**–**	**34,719**
As at 27 September 2019	**14,204**	**403,660**	**1,260,100**	**(176,328)**	**(22,353)**	**1,479,283**
Nine months ended 28 September 2018 (Unaudited)						
As at 31 December 2017	14,204	403,660	915,482	9,977	(902)	1,342,421
Adjustment on initial application of IFRS 15	–	–	1,541	–	–	1,541
Adjusted balance as at 1 January 2018	14,204	403,660	917,023	9,977	(902)	1,343,962
Net income	–	–	81,913	–	–	81,913
Other comprehensive loss	–	–	–	(25,557)	–	(25,557)
Total comprehensive income/(loss)	–	–	35,492	(16,501)	–	56,356
Other changes in equity:						
– Sale of shares by employee benefit trusts	–	–	2,025	–	100	2,125
– Share-based compensation, net of tax	–	–	29,674	–	–	29,674
As at 28 September 2018	14,204	403,660	1,030,635	(15,580)	(802)	1,432,117

Notes to the condensed consolidated financial statements

For the three- and nine-month periods ended 27 September 2019

1. Background

Description of business

Dialog Semiconductor Plc ('the Company') is a public limited company that is incorporated in England and Wales and domiciled in the United Kingdom. The Company's ordinary shares are listed on the Frankfurt Stock Exchange.

Dialog creates and markets highly integrated, mixed signal integrated circuits, optimised for personal, portable, hand-held devices, low energy short-range wireless, LED solid-state lighting and automotive applications. Following a segment reorganisation that became effective at the beginning of Q2 2019, Dialog has three reportable segments: Custom Mixed Signal; Connectivity & Audio; and Advanced Mixed Signal. Segment information is presented in note 3.

Registered office

The Company's registered office is at Tower Bridge House, St Katharine's Way, London E1W 1AA, United Kingdom.

Statement of compliance

The interim financial statements of the Company and its subsidiaries (together, "Dialog" or the "Group") on pages 15 to 38 have been prepared in accordance with IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") and adopted for use in the European Union, the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority and the disclosure requirements of the German Securities Trading Act (WpHG).

Basis of preparation

The interim financial statements are for the three- and nine-month periods ended 27 September 2019 ("Q3 2019" and "9M 2019") with comparative information for the three- and nine-month periods ended 28 September 2018 ("Q3 2018" and "9M 2018").

The interim financial statements have been prepared using the same principles for recognising assets, liabilities, income and expenses as are used in preparing the Group's annual financial statements, except that, as required by IAS 34, the income tax expense is calculated by applying the estimated effective income tax rate for the current financial year to the year-to-date profit before income taxes excluding specific items that distort the effective income tax rate and then by taking into account the tax effect of those specific items.

Measurements for each interim reporting period are made on a year-to-date basis, which may involve changes in estimates of amounts reported in prior interim periods of the current financial year.

Presentation currency

The interim financial statements are presented in US dollars ("US$"), which is the functional currency of the Company. All US dollar amounts are rounded to the nearest thousand US dollars ("US$000"), except where otherwise stated.

Significant accounting policies

The interim financial statements have been prepared on a going concern basis and in accordance with the historical cost convention, except that certain investments and derivative financial instruments are stated at their fair value.

The Group's significant accounting policies are unchanged compared with the year ended 31 December 2018 (see pages 101 to 107 of our Annual Report and Accounts 2018), except for the adoption of IFRS 16 *Leases.* Information about the adoption of IFRS 16 and its impact on the Group's results and financial position is set out in note 18.

We also adopted IFRIC 23 *Uncertainty over Income Tax Treatments* and *Plan Amendment, Curtailment or Settlement* (Amendments to IAS 19) with effect from 1 January 2019. Neither of these pronouncements had any immediate impact on the Group's results or financial position.

1. Background continued

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. Actual outcomes could differ from those estimates and assumptions and affect the Group's results in future periods.

Seasonality of operations

Our business is not highly seasonal but our revenue, particularly in our Custom Mixed Signal operating segment, is dependent on the spending patterns in the consumer markets in which our major customers operate. As a result, our revenue tends to be higher in the second half of the year when those customers prepare for the major holiday selling seasons around the turn of the calendar year.

Accounting standards issued but not yet adopted

We outlined in note 1 to our consolidated financial statements for the year ended 31 December 2018 the following relevant accounting pronouncements that have been issued by the IASB but have not yet been adopted by Dialog:

→ *Definition of a Business (Amendments to IFRS 3)*

→ *Definition of Material (Amendments to IAS 1 and IAS 8)*

Subject to their endorsement for use in the European Union, the amendments will be effective from 1 January 2020. We do not expect that the amendments will have an immediate impact on the Group's results or financial position.

Review and approval of the interim financial statements

The interim financial statements are unaudited, but have been reviewed by the Company's auditor, Deloitte LLP, whose report can be found on page 14. The interim financial statements do not constitute statutory accounts within the meaning of section 434(3) of the Companies Act 2006. The Company's audited statutory accounts for the year ended 31 December 2018 have been delivered to the Registrar of Companies in England and Wales. The auditor's report on those accounts was unqualified, did not draw attention to any matters by way of emphasis and did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

The interim financial statements were approved by the Board of Directors on 6 November 2019.

2. Revenue

Revenue may be analysed as follows:

	Third quarter		First nine months	
	Three months ended 27 September 2019 US$000	Three months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Nine months ended 28 September 2018 US$000
Sale of goods:				
– Sales direct to end customers	**308,819**	303,472	**786,587**	789,572
– Sales to distributors	**93,556**	79,779	**240,390**	220,991
Total sale of goods	**402,375**	383,251	**1,026,977**	1,010,563
Licensing agreements with Apple:				
– Perpetual licence fee	**–**	–	**145,750**	–
– Effective licence fee	**6,252**	–	**12,232**	–
Royalties	**176**	323	**698**	830
Total revenue	**408,803**	383,574	**1,185,657**	1,011,393

Revenue from research and development contracts of US$4,851 in Q3 2019 (Q3 2018: US$ 1,506) and US$21,742 in 9M 2019 (9M 2018: US$ 2,298) is included in other operating income.

Notes to the condensed consolidated financial statements continued

3. Segment information

Background

Segment information is presented in the financial statements on a basis consistent with the information presented to the Management Team (the "chief operating decision maker") for the purposes of allocating resources within the Group and assessing the financial performance of the Group's businesses. Members of the Management Team are identified on page 13.

The Group's reportable segments are determined based on the nature of the products that they provide to our customers.

Organisational and measurement changes

With effect from the beginning of Q2 2019, the Group made a number of organisational changes. Prior to the changes, the Group had four operating segments: Mobile Systems; Connectivity; Automotive & Industrial; and Advanced Mixed Signal.

The following organisational changes were made:

- Mobile Systems' standard PMICs and charging products were transferred to Advanced Mixed Signal and its standard audio products were transferred to Connectivity;
- Mobile Systems was re-named Custom Mixed Signal to reflect its new focus on custom products and Connectivity was re-named Connectivity & Audio;
- Automotive & Industrial ceased to exist as a segment as its custom automotive motor control ICs were transferred to Custom Mixed Signal and its industrial lighting products were transferred to Advanced Mixed Signal.

Following the changes, the Group has three reportable segments: Custom Mixed Signal; Advanced Mixed Signal; and Connectivity & Audio.

- Custom Mixed Signal provides custom ICs designed to meet the needs of our customers in the mobile, automotive, computing and storage markets.
- Advanced Mixed Signal provides standard products including CMICs, AC/DC converter solutions for smaller, fast charging power adaptors for portable devices as well as LED drivers for backlighting and solid-state lighting products.
- Connectivity & Audio provides standard products incorporating short-range wireless, digital cordless, Bluetooth®, VoIP and low-power Wi-Fi technologies.

Each of the Group's operating segments has a manager who is responsible for its performance and is accountable to the Chief Executive Officer. Custom Mixed Signal comprises our Custom Mixed Signal business group and our Automotive business unit, each of which meets the definition of an operating segment but have been aggregated because they have similar economic characteristics and both provide custom products to similar types of customers through similar distribution channels. Otherwise, we have not aggregated any operating segments in determining our reportable segments.

At the same time as effecting the organisational changes, the Management Team changed its focus from IFRS measures to underlying measures as the principal basis for allocating resources to and assessing the financial performance of the Group's businesses. Underlying revenue is therefore the measure of segment revenue and underlying operating profit/loss the measure of segment profit/loss that is now presented in the Group's segment disclosures.

Comparative information for Q3 2018 and 9M 2018 has been restated to reflect these organisational and measurement changes.

Underlying performance measures

Underlying performance measures exclude specific items of income or expense that are recognised in profit or loss reported in accordance with IFRS that we consider hinder comparison of the financial performance of our businesses from one period to another, with each other or with other similar businesses.

Details of the items excluded from profit or loss reported under IFRS in arriving at the Group's underlying profit or loss for each of the periods presented are set out in Section 3 of this Interim Report.

Segment revenue and results

Underlying revenue and underlying operating profit by reportable segment were as follows:

Third quarter

	Underlying revenue[1]		Underlying operating profit/(loss)	
	Three months ended 27 September 2019 US$000	Restated Three months ended 28 September 2018 US$000	**Three months ended 27 September 2019 US$000**	Restated Three months ended 28 September 2018 US$000
Custom Mixed Signal	**278,200**	274,535	**88,709**	72,027
Advanced Mixed Signal	**70,033**	66,265	**6,184**	9,040
Connectivity & Audio	**54,318**	42,734	**5,443**	5,590
Total segments	**402,551**	383,534	**100,336**	86,657
Corporate and other unallocated items	**6,252**	40	**3,483**	(2,977)
Total Group	**408,803**	383,574	**103,819**	83,680

3. Segment information continued

First nine months

	Underlying revenue[1]		Underlying operating profit/(loss)	
	Nine months ended 27 September 2019 US$000	Restated Nine months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Restated Nine months ended 28 September 2018 US$000
Custom Mixed Signal	**709,069**	714,475	**200,216**	170,100
Advanced Mixed Signal	**184,972**	183,842	**12,489**	20,243
Connectivity & Audio	**133,627**	113,020	**17,258**	9,053
Total segments	**1,027,668**	1,011,337	**229,963**	199,396
Corporate and other unallocated items	**12,239**	56	**3,118**	(21,192)
Total Group	**1,039,907**	1,011,393	**233,081**	178,204

1 Revenue is from sales to external customers (there were no inter-segment sales).

Reconciliation of underlying revenue to revenue reported under IFRS

	Third quarter		First nine months	
	Three months ended 27 September 2019 US$000	Three months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Nine months ended 28 September 2018 US$000
Underlying revenue	**408,803**	383,574	**1,039,907**	1,011,393
Perpetual licence fee	**–**	–	**145,750**	–
Revenue reported under IFRS	**408,803**	383,574	**1,185,657**	1,011,393

Reconciliation of underlying operating profit to profit before income taxes reported under IFRS

	Third quarter		First nine months	
	Three months ended 27 September 2019 US$000	Three months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Nine months ended 28 September 2018 US$000
Underlying operating profit	**103,819**	83,680	**233,081**	178,204
Licence and asset transfers to Apple:				
– Perpetual licence fee	**–**	–	**145,750**	–
– Gain on transfer of design centre businesses	**–**	–	**15,898**	–
Share-based compensation and related payroll taxes	**(10,718)**	(10,205)	**(34,105)**	(29,299)
Accounting for business combinations:				
– Acquisition-related costs	**(1,021)**	–	**(2,696)**	–
– Amortisation of acquired intangible assets	**(6,964)**	(5,658)	**(18,724)**	(16,972)
– Consumption of the fair value uplift of acquired inventory	**(483)**	(335)	**(886)**	(3,129)
– Consideration accounted for as compensation expense	**(285)**	(342)	**(910)**	(1,146)
– Forfeiture of deferred consideration	**50**	14	**148**	177
– Remeasurement of contingent consideration	**–**	1,154	**–**	1,519
Integration costs	**(306)**	(940)	**(502)**	(2,103)
Corporate transaction costs	**(235)**	(3,880)	**(10,894)**	(4,653)
Operating profit reported under IFRS	**83,857**	63,488	**326,160**	122,598
Interest income	**6,428**	2,654	**16,889**	6,565
Interest expense	**(3,510)**	(664)	**(8,087)**	(2,322)
Other finance expense	**(140)**	(3,186)	**(3,989)**	(7,980)
Profit before income taxes	**86,635**	62,292	**330,973**	118,861

Notes to the condensed consolidated financial statements continued

4. Other operating income

Other operating income comprised:

	Third quarter		First nine months	
	Three months ended 27 September 2019 US$000	Three months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Nine months ended 28 September 2018 US$000
Revenue from research and development contracts	**4,851**	1,506	**21,742**	2,298
Gain on transfer of design centre businesses (note 6)	**–**	–	**15,898**	–
Change in estimate of contingent consideration	**–**	1,113	**–**	1,478
Other items	**305**	–	**1,167**	–
Total	**5,156**	2,619	**38,807**	3,776

During 9M 2019, revenue from research and development contracts included US$12,490 received from Apple for product development costs incurred between October 2018 and April 2019.

5. Earnings per share

Basic earnings per share amounts are calculated by dividing the profit for the period attributable to holders of ordinary shares in the Company by the weighted average number of ordinary shares outstanding during the period.

Diluted earnings per share amounts are calculated by dividing the profit attributable to holders of ordinary shares in the Company by the weighted average number of ordinary shares outstanding during the period plus the weighted average number of ordinary shares that would be issued if all the securities or other contracts to issue ordinary shares were exercised.

Profit attributable to shareholders in the Company and the weighted average number of ordinary shares for calculating basic and diluted earnings per share were calculated as follows:

		Third quarter		First nine months	
		Three months ended 27 September 2019 US$000	Three months ended 28 September 2018 US$000	**Nine months ended 27 September 2019 US$000**	Nine months ended 28 September 2018 US$000
Profit attributable to shareholders in the Company					
For calculating basic and diluted earnings per share	a	**68,196**	46,421	**256,658**	81,913
Weighted average number of ordinary shares					
Average number of shares in issue during the period		**76,382,139**	76,382,139	**76,382,139**	76,382,139
Deduct:					
– Average number of shares held by employee benefit trusts		**(1,562,836)**	(2,415,909)	**(1,992,762)**	(2,532,433)
– Average number of treasury shares		**(4,039,630)**	–	**(1,784,169)**	–
For calculating basic earnings per share	b	**70,779,673**	73,966,230	**72,605,208**	73,849,706
Add:					
– Average number of dilutive share options and awards		**3,997,598**	4,005,121	**4,438,158**	3,904,278
For calculating diluted earnings per share	c	**74,777,271**	77,971,351	**77,043,366**	77,753,984
Earnings per share (US$)					
Basic	a/b	**0.96**	0.63	**3.53**	1.11
Diluted	a/c	**0.91**	0.60	**3.33**	1.05

6. Licensing and asset transfer agreement with Apple

Summary of the transaction

On 11 October 2018, we announced that we had entered into an agreement with Apple Inc. ("Apple") to license our power management technologies and to transfer to Apple certain assets and over 300 employees from our design centres in the UK, Germany and Italy.

Following the receipt of the necessary regulatory approvals and satisfaction of the other closing conditions, the transaction closed on 8 April 2019. Apple paid us US$300 million in respect of the licensing arrangements and asset transfers.

Pursuant to the agreement, Dialog granted to Apple:

- a perpetual licence over Dialog's Power Management IP as it existed at the closing date; and
- an effective licence over certain of Dialog's IP as it existed at the closing date and is developed for a period of at least four years thereafter.

Continuation of the effective licence beyond the initial four-year period is contingent on Apple's purchases from Dialog exceeding a specified level in successive preceding twelve-month periods.

While there was no transfer of legal ownership of the licensed IP rights, a relatively small number of patents were included in the business assets transferred to Apple.

Contingent on closing of the licensing and asset transfer agreement, Apple made an interest-free prepayment to Dialog of US$300 million. On initial recognition, we measured the prepayment at its fair value of US$288,584. We considered that the resulting "below market element" of the prepayment of US$11,416 represented additional consideration in respect of the licensing arrangements and asset transfers.

We allocated the consideration received in respect of the licensing and asset transfer arrangements as follows:

	US$000
Fair value at closing date	
Licensing arrangements:	
– Perpetual IP licence	**145,750**
– Effective IP licence	**136,400**
Design centre businesses	**29,266**
Total fair value	**311,416**
Consideration	
Cash received	**300,000**
Below market element of prepayment	**11,416**
Total consideration	**311,416**

We incurred transaction costs totalling US$18,681 in relation to the agreement with Apple, of which US$10,894 was incurred during 9M 2019 (within general and administrative expenses).

Notes to the condensed consolidated financial statements continued

6. Licensing and asset transfer agreement with Apple continued

Subsequent accounting for the transaction

Licensing arrangements

We consider that the perpetual IP licence granted Apple a "right to use" the related IP. We therefore recognised the consideration of US$145,750 allocated to the perpetual licence as revenue on the closing date.

We consider that the effective IP licence granted Apple a "right to access" the related IP. We are therefore recognising the consideration of US$136,400 allocated to the effective licence as revenue over the four-year period following the closing date. We are amortising the deferred revenue in proportion to the present value of the cash flows that supported the fair value of the effective licence at the closing date. During 9M 2019, we recognised revenue of US$12,232 in relation to the effective licence.

Transfer of design centre businesses

We recognised a gain of US$15,898 on the transfer of the design centre businesses (within other operating income) that was calculated as follows:

	US$000
Carrying amount of assets transferred	
Cash and cash equivalents	**1,452**
Other current assets	**292**
Property, plant and equipment – owned	**13,824**
Property, plant and equipment – leased	**4,287**
Patents	**224**
Other non-current assets	**77**
Total assets transferred	**20,156**
Carrying amount of associated liabilities	
Trade and other payables	**161**
Income tax payables	**119**
Current lease liabilities	**790**
Other current liabilities	**1,051**
Non-current lease liabilities	**3,650**
Provisions	**1,326**
Total liabilities transferred	**7,097**
Net assets transferred	**13,059**
Currency translation loss transferred from equity	**309**
Gain on transfer of design centre businesses	**15,898**
Consideration received	**29,266**

Prepayment from Apple

It is intended that the US$300 million prepayment will be recouped by Apple against amounts payable to Dialog for the purchase of certain of our products over the three-year period ending on 31 March 2022. Settlement of the prepayment is scheduled to take place in quarterly instalments in arrears such that US$200 million is settled in the first year and US$50 million is settled in each of the second and third years. During each quarter, Apple will settle our invoices on its normal payment terms. If, on a recoupment date, there is a shortfall of invoices outstanding against the scheduled recoupment amount, Apple may require us to settle the shortfall in cash or may permit us to carry forward the shortfall for recoupment in the subsequent quarter.

In July 2019, the first quarterly instalment of US$50,000 was settled by recoupment by Apple against invoices outstanding totalling US$29,655 and a balancing cash payment by Dialog of US$20,345.

We account for the prepayment as a financial liability measured at amortised cost. At the end of Q3 2019, the carrying amount of the liability was US$242,628. During 9M 2019, we recognised an interest expense of US$4,045 in relation to the prepayment.

As a condition of the prepayment, we put in place a reducing letter of credit in favour of Apple for the outstanding principal amount. During 9M 2019, we incurred related commitment fees of US$773 (within interest expense).

7. Business combinations

Acquisition of FCI

On 31 May 2019, we completed the acquisition of 100% of the equity interests in Silicon Motion Technology Corporation's Mobile Communications product group, branded as FCI.

FCI is based near Seoul, South Korea and is a leading supplier of Mobile TV SoCs and Low Power Wi-Fi SoCs. During the fourth quarter of 2018, FCI began ramping production of its first Ultra-Low- Power Wi-Fi SoC that is designed to meet the demands of battery powered IoT devices, providing direct internet connectivity. FCI is being integrated into our Connectivity & Audio operating segment where we plan to combine its Ultra-Low-Power WiFi technology with our own Bluetooth® low-energy chips and modules, principally to enhance our IoT offerings.

We acquired FCI for US$45,000 on a cash and debt-free basis. On completion, we paid consideration of US$53,884 in cash, including US$8,884 (net of US$271 transaction tax withheld) in respect of FCI's estimated cash and working capital on completion. We paid the withheld transaction tax to the Korean tax authority during Q3 2019.

We paid US$5,400 of the consideration into an escrow fund that is available to settle any valid claims that we may make in relation to the representations, warranties and indemnities that were provided to us by the seller.

Our provisional allocation of the purchase price to the identifiable assets and liabilities of FCI and goodwill is as follows:

	US$000
Assets acquired	
Cash and cash equivalents	**9,562**
Trade and other receivables	**1,791**
Inventories	**4,347**
Other current assets	**705**
Intangible assets	**34,396**
Property, plant and equipment – owned	**872**
Property, plant and equipment – leased	**762**
Other non-current assets	**395**
Total assets acquired	**52,830**
Liabilities assumed	
Trade and other payables	**2,385**
Current lease liabilities	**415**
Other current liabilities	**983**
Non-current lease liabilities	**284**
Net defined benefit liability	**771**
Deferred tax liabilities	**7,429**
Other non-current liabilities	**83**
Total liabilities	**12,350**
Net identifiable assets acquired	**40,480**
Goodwill arising on acquisition	**13,675**
Consideration	**54,155**

Identifiable intangible assets acquired comprised developed technology and know-how, customer relationships, the FCI™ trade name and computer software and licences.

Goodwill recognised on the acquisition of FCI is principally attributable to the benefits expected to be derived from the development of new technology and product offerings by FCI in the future, the assembled workforce and the opportunities to cross-sell FCI's products to Dialog's customers.

None of the goodwill is deductible for tax purposes.

Finalisation of the purchase price allocation is subject to our agreeing with the seller any adjustment to the purchase consideration to reflect FCI's actual cash and working capital on completion.

During 9M 2019, FCI contributed US$6,431 to the Group's revenue and a loss after tax of US$2,483. If FCI had been acquired on 1 January 2019, the Group's revenue for 9M 2019 would have been US$10,397 higher at US$1,196,054 and its net income US$2,853 lower at US$253,805.

During 9M 2019, we incurred transaction costs of US$2,180 in relation to the acquisition of FCI (included within general and administrative expenses).

Notes to the condensed consolidated financial statements continued

7. Business combinations continued

Consideration payable for Silego

We completed the acquisition of Silego Technology Inc. ("Silego") on 1 November 2017.

Deferred consideration
On completion of the acquisition, unvested employee options were converted into deferred cash rights and the fair value of those rights was apportioned between a deferred consideration element and a future compensation element. During 9M 2019, we paid US$1,716 in settlement of vested deferred consideration and recognised a credit of US$148 to profit or loss in respect of forfeitures. As at 27 September 2019, we held a liability of US$1,310 in relation to the remaining deferred consideration that is payable over the period to March 2021.

Contingent consideration
Contingent consideration of up to US$30,400 was payable for the acquisition of Silego in two instalments based on Silego's revenue for 2017 and 2018.

Silego's revenue for 2018 was such that US$17,874 of the second instalment of up to US$20,400 was payable. In February 2019, we paid US$16,729 in settlement of the element of the second instalment that was attributable to the shares and vested options acquired and attributed the balance to the deferred cash rights.

Since the total contingent consideration paid was below our initial estimate at the time of the acquisition, the payments are shown within cash flows from investing activities.

8. Cash and cash equivalents

Cash and cash equivalents may be analysed as follows:

	As at 27 September 2019 US$000	As at 31 December 2018 US$000
Cash at bank	**14,696**	3,920
Cash held by employee benefit trusts	**5,719**	2,829
Cash available from receivables financing facilities	**74,473**	96,099
Bank deposits	**350,000**	325,000
Money market funds	**726,000**	250,000
Total	**1,170,888**	677,848

As at 27 September 2019 and 31 December 2018, no amounts had been drawn from the cash available from receivables financing facilities.

9. Inventories

Inventories were as follows:

	As at 27 September 2019 US$000	As at 31 December 2018 US$000
Raw materials	**20,436**	36,579
Work in progress	**55,430**	48,416
Finished goods	**48,819**	64,741
Total	**124,685**	149,736

10. Goodwill and other intangible assets

Movements on goodwill and other intangible assets during 9M 2019 may be summarised as follows:

	Goodwill US$000	**Other intangible assets US$000**
Net book value		
As at 31 December 2018	**439,508**	**217,445**
Acquisition of FCI (note 7)	**13,675**	**34,396**
Additions	**–**	**15,146**
Amortisation charge for the period	**–**	**(38,127)**
Impairment of product development assets	**–**	**(3,130)**
Transfer to assets held for sale	**–**	**(9)**
Disposals	**–**	**(590)**
Effect of movements in foreign currency	**(148)**	**(287)**
As at 27 September 2019	**453,035**	**224,844**

11. Property, plant and equipment

Movements on property, plant and equipment during 9M 2019 may be summarised as follows:

	Owned US$000	Leased US$000
Net book value		
As at 31 December 2018	66,359	–
Adjustment on initial application of IFRS 16 (note 18)	–	66,390
Adjusted balance as at 1 January 2019	66,359	66,390
Acquisition of FCI (note 7)	872	762
Additions	9,968	876
Depreciation charge for the period	(21,051)	(9,621)
Transfer to assets held for sale	(2,906)	(4,287)
Disposals	(838)	(60)
Effect of movements in foreign currency	(144)	(163)
As at 27 September 2019	52,260	53,897

12. Investments

Investments were as follows:

	As at 27 September 2019 US$000	As at 31 December 2018 US$000
Equity investments:		
– Energous shares	5,776	10,073
Derivative financial instruments:		
– Energous warrants	47	1,465
Total investments	5,823	11,538

Energous Corporation ('Energous') is the developer of WattUp®, a wire-free charging technology. We entered into a strategic alliance with Energous in November 2016. At that time, we subscribed for common shares in Energous and were granted warrants to purchase additional common shares. We subscribed for more common shares and were granted further warrants in July 2017.

We hold a total of 1,739,691 common shares in Energous and warrants to purchase up to 1,417,565 common shares. As at 27 September 2019, we held approximately 5.7% of the issued common shares in Energous.

During 9M 2019, we recognised a fair value loss on the common shares of US$4,297 (9M 2018: loss of US$16,249) in other comprehensive income and recognised a fair value loss of US$1,418 (9M 2018: loss of US$8,631) on the warrants in profit or loss (as other finance expense). Also during 9M 2019, we recognised a credit of US$1,172 (9M 2018: credit of US$1,176) in profit or loss on the amortisation of the fair value on initial recognition of the second tranche of the warrants (against other finance expense).

Notes to the condensed consolidated financial statements continued

13. Assets classified as held for sale

Assets and associated liabilities transferred to Apple

On 11 October 2018, we entered into an agreement with Apple Inc. (“Apple”), inter alia, to transfer to Apple certain patents and design centre assets. Details of the agreement are set out in note 6.

As at 31 December 2018, the carrying amounts of the assets to be transferred and directly associated liabilities were as follows:

	As at 27 September 2019 US$000	As at 31 December 2018 US$000
Assets held for sale		
Other current assets	–	311
Other intangible assets	–	215
Property, plant and equipment – owned	–	10,769
	–	11,295
Liabilities directly associated with assets held for sale		
Trade and other payables	–	100
Income taxes payable	–	63
Other current liabilities	–	1,721
Provisions	–	1,283
	–	3,167

Completion of the transaction with Apple took place on 8 April 2019.

Investment in associate

On 7 December 2018, we agreed to sell our shareholding in Dyna Image Corporation (“Dyna Image”) for consideration of between US$2.4 million and US$5.0 million.

We obtained the necessary regulatory approvals but the purchaser was unable to complete the transaction. As a result, the sale agreement was terminated on 2 September 2019 and we entered into a new agreement to sell our shareholding to another purchaser for a nominal amount.

Since the end of 2018, the carrying amount of the Group’s investment in Dyna Image has been nil, so no additional loss will be recognised on the sale.

The transaction is expected to close in the fourth quarter of 2019.

14. Additional disclosures on financial instruments

Analysis by class and category

In the following table, the carrying amounts of the financial assets and financial liabilities held by the Group as at 27 September 2019 are analysed by class and category:

	Amortised cost US$000	At fair value through profit or loss US$000	At fair value in designated hedges US$000	At fair value through other comprehensive income US$000	Net book value US$000	Fair value US$000
Financial assets						
Cash and cash equivalents	1,170,888	–	–	–	1,170,888	1,170,888
Trade and other receivables	153,369	–	–	–	153,369	153,369
Energous shares	–	–	–	5,776	5,776	5,776
Energous warrants	–	47	–	–	47	47
Other investments	–	47	–	5,776	5,823	
Currency derivatives	–	446	135	–	581	581
Rental and other deposits	2,177	–	–	–	2,177	2,177
Other financial assets	2,177	446	135	–	2,758	
Total financial assets	1,326,434	493	135	5,776	1,332,838	
Financial liabilities						
Trade and other payables	(115,993)	–	–	–	(115,993)	(115,993)
Lease liabilities	(55,145)	–	–	–	(55,145)	(56,632)
Prepayment from Apple	(242,628)	–	–	–	(242,628)	(244,233)
Currency derivatives	–	(6,995)	(5,470)	–	(12,465)	(12,465)
Share buyback obligation	(127,846)	–	–	–	(127,846)	(127,846)
Deferred consideration	(1,310)	–	–	–	(1,310)	(1,310)
Other financial liabilities	(371,784)	(6,995)	(5,470)	–	(384,249)	
Total financial liabilities	(542,922)	(6,995)	(5,470)	–	(555,387)	

Notes to the condensed consolidated financial statements continued

14. Additional disclosures on financial instruments continued

Fair value measurement

a) Financial instruments carried at fair value
All financial instruments that are carried at fair value are revalued on a recurring basis. We have not designated any financial instruments at fair value through profit or loss on initial recognition.

We measured the fair value of these financial assets using the following methods and assumptions:

- Common shares in Energous (listed on NASDAQ) – measured at the quoted bid price at the close of business on the balance sheet date.
- Energous warrants – measured using a Black Scholes valuation model based on the quoted bid price of Energous' common shares and other inputs such as implied share price volatility that is modelled based on historical price data for Energous' common shares.

We measure the fair value of currency derivatives as the present value of the future contractual cash flows, which is estimated using observable spot exchange rates and by applying a discount rate that is based on the yield curves of the respective currencies and reflects the credit risk of the counterparties.

In the following table, the financial instruments that were carried at fair value as at 27 September 2019 are categorised into one of three levels in a fair value hierarchy according to the nature of the significant inputs to the valuation techniques that are used to determine their fair value as follows:

- Level 1 – Quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 – Inputs other than Level 1 that are observable either directly (as market prices) or indirectly (derived from market prices).
- Level 3 – Unobservable inputs, such as those derived from internal models or using other valuation methods.

	Level 1 US$000	Level 2 US$000	Level 3 US$000	Total US$000
Financial assets carried at fair value				
Investments:				
– Energous shares	5,776	–	–	5,776
Derivative financial instruments:				
– Currency derivatives	–	581	–	581
– Energous warrants	–	–	47	47
Total financial assets carried at fair value	5,776	581	47	6,404
Financial liabilities carried at fair value				
Derivative financial instruments:				
– Currency derivatives	–	(12,465)	–	(12,465)
Total financial liabilities carried at fair value	–	(12,465)	–	(12,465)

During 9M 2019, there were no transfers between Level 1 and Level 2.

14. Additional disclosures on financial instruments continued

Changes in the Level 3 fair values during 9M 2019 may be reconciled as follows:

Financial assets carried at fair value

	Energous warrants US$000
As at 31 December 2018	1,465
Unrealised fair value loss recognised in profit or loss (other finance expense)	(1,418)
As at 27 September 2019	47

Financial liabilities carried at fair value

	Contingent consideration US$000
As at 31 December 2018	(16,414)
Unwinding of discount recognised in profit or loss (interest expense)	(315)
Settlements	16,729
As at 27 September 2019	–

When measuring the fair value of the Energous warrants, the most significant unobservable input is the implied volatility of the market price of Energous's common stock over the period to expiry of the warrants. We estimate that if the implied volatility of 160.12% incorporated in the valuation of the first tranche of Energous warrants that expire in November 2019 and that of 105.38% incorporated in the valuation of the second tranche of warrants that expire in July 2020 had been ten percentage points higher or lower, the fair value of the warrants as at 27 September 2019 would have been US$32 higher at US$79 or US$21 lower at US$26, respectively. In each case, the effect of the increase/(decrease) in fair value would have been recognised in profit or loss as other finance income/(expense).

b) Financial instruments not carried at fair value
We have calculated the fair value of the non-interest bearing prepayment from Apple by discounting the future scheduled recoupments based upon the observable yield curve at the balance sheet date for US dollar-denominated debt with an equivalent risk profile (Level 2).

We have calculated the fair value of lease liabilities by discounting the future lease payments at incremental borrowing rates based on observable yield curves at the balance sheet date and, where the lease payments are denominated in a foreign currency, by translating the resulting present values into US dollars using the relevant currency exchange rate at the balance sheet date (Level 2).

Other financial assets and financial liabilities that are not carried at fair value are of short maturity and/or bear interest at floating rates. We therefore consider that their carrying amounts approximate to their fair values (Level 2).

Notes to the condensed consolidated financial statements continued

15. Share-based compensation

The Company operates a number of share-based compensation plans under which it grants options and awards over its ordinary shares to certain of the Group's employees.

Development of plans

Movements in the total number of share options outstanding during 9M 2019 were as follows:

	Options	Weighted average exercise price €
Outstanding at the beginning of the period	5,472,635	0.65
Granted	1,003,962	0.09
Exercised	(1,279,410)	2.23
Forfeited	(841,768)	0.12
Outstanding at the end of the period	**4,355,419**	**0.16**
Options exercisable at the end of the period	526,302	0.63

Shares held by employee benefit trusts

The Company provides finance to two trusts to purchase its ordinary shares in order to meet its obligations under its share-based compensation plans. As at 27 September 2019, the trusts held 1,327,849 ordinary shares (as at 31 December 2018: 2,607,259 ordinary shares).

Movements in the number of shares held by the trusts during 9M 2019 were as follows:

	Number of shares	Cost US$000
At the beginning of the period	2,607,259	22,514
Sale or transfer of shares	(1,279,410)	(161)
At the end of the period	**1,327,849**	**22,353**

16. Other reserves

Movements on other reserves were as follows:

	Capital redemption reserve US$000	Currency translation reserve US$000	Fair value reserve US$000	Hedging reserve US$000	Treasury shares US$000	Total US$000
Nine months ended 27 September 2019						
As at 31 December 2018	571	(4,304)	(14,927)	(4,759)	–	(23,419)
Other comprehensive income/(loss):						
– Currency translation differences on foreign operations	–	22	–	–	–	22
– Fair value loss on equity investments	–	–	(4,297)	–	–	(4,297)
– Cash flow hedges:						
Fair value loss recognised on effective hedges	–	–	–	(8,096)	–	(8,096)
Fair value loss transferred to profit or loss	–	–	–	8,635	–	8,635
– Income tax expense	–	(123)	–	(102)	–	(225)
Other changes in equity:						
– Purchase of own shares into treasury	–	–	–	–	(148,948)	(148,948)
As at 27 September 2019	**571**	**(4,405)**	**(19,224)**	**(4,322)**	**(148,948)**	**(176,328)**
Nine months ended 28 September 2018						
As at 31 December 2017	571	(3,699)	7,822	5,283	–	9,977
Other comprehensive loss:						
– Currency translation differences on foreign operations	–	(444)	–	–	–	(444)
– Fair value loss on equity investments	–	–	(16,249)	–	–	(16,249)
– Cash flow hedges:						
Fair value loss recognised on effective hedges	–	–	–	(6,897)	–	(6,897)
Fair value gain transferred to profit or loss	–	–	–	(5,183)	–	(5,183)
– Income tax (expense)/credit	–	(111)	1,015	2,312	–	3,216
As at 28 September 2018	571	(4,254)	(7,412)	(4,485)	–	(15,580)

17. Share buyback programme

We initiated our share buyback programme in May 2016.

By the end of 9M 2019, the Company had purchased 9,225,668 of its own ordinary shares at a total cost of US$335,469 (including transaction costs of US$2,691), of which 4,483,816 shares had been cancelled and 4,741,852 shares were held in treasury.

Shares purchased during the period

At the Company's 2018 AGM, the Directors were granted an authority to purchase up to 7,638,214 of the Company's ordinary shares. On 6 November 2018, the Company announced the sole tranche of the share buyback programme pursuant to the 2018 AGM authority under which it committed to purchase shares with a minimum cost of €100.0 million and a maximum cost of €150.0 million.

On inception of this tranche, we recognised a liability and a corresponding debit to retained earnings of €150.0 million (US$171,173) in respect of the maximum obligation to purchase shares. We also debited transaction costs incurred of US$14 to retained earnings.

We completed the first and final settlement of this tranche on 31 May 2019. We purchased 3,941,852 shares under this tranche at a cost of €100.0 million (US$111,470) and incurred transaction costs amounting to US$639. On conclusion of the tranche, we credited back to retained earnings the remainder of the obligation to purchase shares initially recognised of US$55,847 and showed a debit to retained earnings of US$2,645, which mirrored the gain recognised in profit or loss since inception of the tranche on the translation into US dollars of the Euro-denominated liability that existed in relation to the shares that were purchased during the period.

First tranche pursuant to the 2019 AGM authority

At the Company's 2019 AGM, the Directors were granted a new authority to purchase up to 11,457,321 of the Company's ordinary shares, representing approximately 15% of the issued ordinary share capital of the Company as at 27 March 2019. Such authority shall (unless previously renewed, varied or revoked) expire on the day before the next AGM of the Company or on 30 June 2020, whichever is the earlier.

Purchases made under the share buyback programme are off-market and are effected by way of contingent forward purchase contracts entered into with brokers. Barclays, Goldman Sachs, HSBC or Merrill Lynch may be appointed as brokers for purchases under the 2019 AGM authority.

On 5 June 2019, we announced details of the first tranche of share purchases pursuant to the 2019 AGM authority under which the Company committed to purchase shares with a minimum cost of €125.0 million and a maximum cost of €150.0 million. On initiation of this tranche, we recognised a liability and a corresponding debit to retained earnings of €150.0 million (US$168,915) in respect of the maximum obligation to purchase shares.

We completed the first intermediate settlement of this tranche on 19 September 2019. We purchased 800,000 shares at an initial cost of €33.1 million (US$36,655) and incurred transaction costs amounting to US$184.

As at 27 September 2019, the carrying amount of the liability for the maximum remaining obligation to purchase shares under this tranche was €116.9 million (US$127,846).

We hedge the currency translation exposure on outstanding liabilities to purchase shares using currency forwards and swaps. After taking into account hedging, we recognised a net currency translation loss of US$4,415 in profit or loss in relation to liabilities to purchase shares outstanding during 9M 2019.

Notes to the condensed consolidated financial statements continued

18. Adoption of IFRS 16

Background

We adopted IFRS 16 *Leases* with effect from 1 January 2019. IFRS 16 replaced IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease* and other related interpretations. IFRS 16 changes the way in which lessees recognise, measure, present and disclose leases.

Under IAS 17, a lessee accounted for leases differently according to whether they were classified as a finance lease or an operating lease. IFRS 16 provides a single lessee accounting model, requiring lessees to recognise a right-of-use asset and a lease liability for all leases, except, by election, those with a short lease term and/or involving an underlying asset of low value.

Previous accounting for leases under IAS 17

Under IAS 17, leases that confer rights and obligations similar to those that attach to owned assets were classified as finance leases. All other leases were classified as operating leases. Assets held under finance leases were recognised as assets within property, plant and equipment, initially measured at the fair value of the leased asset or, if lower, the present value of the minimum lease payments, and a corresponding liability was recognised. Subsequently, the assets were depreciated over the shorter of the expected useful life of the asset or the term of the lease. At inception of the lease, the lease payments were apportioned between a capital element and an interest element so as to achieve a constant periodic rate of interest on the outstanding liability. Subsequently, the interest element was recognised as an expense in profit or loss while the capital element was applied to reduce the outstanding liability.

Operating lease payments, net of any incentives receivable, were recognised in profit or loss on a straight-line basis over the term of the lease.

New accounting for leases under IFRS 16

Definition of a lease

A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Control exists if, throughout the period of use, the lessee has the right to obtain substantially all of the benefits from the use of the asset and the right to direct the use of the asset.

Right-of-use asset

On the commencement date of a lease, the lessee recognises a right-of-use asset which comprises the amount of the initial measurement of the lease liability, and, where applicable, lease payments made at or before the commencement date, less any lease incentives received, initial direct costs incurred by the lessee and an estimate of any costs to be incurred by the lessee in restoring or removing the underlying asset, unless those costs are incurred to produce inventories.

After the commencement date, the right-of-use asset is measured at cost less accumulated depreciation and any accumulated impairment losses and is adjusted for any remeasurement of the lease liability.

Right-of-use assets are depreciated so as to charge their cost to profit or loss (in arriving at operating profit), usually over the period from the commencement date to the end of the lease term.

Lease liability

On the commencement date of a lease, the lessee recognises a lease liability measured at the present value of the future lease payments discounted using the interest rate implicit in the lease, if that rate can be readily determined, or using the lessee's incremental borrowing rate. Lease payments comprise fixed payments, less any lease incentives receivable, variable payments that depend on an index or rate and, where applicable, any amounts expected to be paid by the lessee under a residual value guarantee, purchase option or by way of termination penalties.

Variable lease payments that do not depend on an index or rate are recognised in profit or loss in the period in which the event that triggers those payments occurs.

After the commencement date, the lease liability is measured by increasing the carrying amount to reflect interest on the lease liability, reducing the carrying amount to reflect lease payments made and remeasuring the carrying amount to reflect certain changes in the lease payments or lease modifications.

Interest accrued on the lease liability in each period during the lease term is the amount that produces a constant periodic rate of interest on the remaining balance of the lease liability and is recognised in profit or loss (within interest expense).

Short-term leases and leases of low value assets

As permitted by IFRS 16, we have elected not to recognise right-of-use assets and lease liabilities in respect of short-term leases (leases that have a lease term of 12 months or less) and/or leases involving an underlying asset of low value (an asset with a value when new of less than US$5 or foreign currency equivalent).

We recognise the lease payments for those leases as an expense in profit or loss (in arriving at operating profit) on a straight-line basis over the lease term.

18. Adoption of IFRS 16 continued

Transition to IFRS 16

As permitted by IFRS 16, we did not reassess whether any contract existing on the transition date was, or contained, a lease and applied IFRS 16 only to contracts that were previously identified as leases applying IAS 17 and IFRIC 4.

We applied IFRS 16 using a modified retrospective approach whereby prior periods were not restated but we recognised cumulative effect adjustments to the opening consolidated balance sheet on 1 January 2019.

We recognised the following for each contract that is, or contains, a lease on the transition date:

→ a lease liability measured at the present value of the remaining lease payments discounted at the lessee's incremental borrowing rate on the transition date; and

→ a right-of-use asset measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments that was recognised as at 31 December 2018.

We also recognised related adjustments to deferred tax assets and liabilities.

We recognised an overall cumulative effect credit of US$40 against the opening balance of retained earnings on 1 January 2019 that may be analysed as follows:

	US$000
Right of use asset	66,390
Lease liability	(67,631)
Net accrued lease payments	1,241
	–
Income taxes	40
Increase in net assets	40

Financial effect of adopting IFRS 16

We summarise in the following tables the effect of adopting IFRS 16 on the consolidated statement of income for the three- and nine-month periods ended 27 September 2019 and on the consolidated balance sheet as at 27 September 2019.

Consolidated statement of income for the three- and nine-month periods ended 27 September 2019

	Three months ended 27 September 2019			Nine months ended 27 September 2019		
	As reported under IFRS 16 US$000	Adjustment for effect of IFRS 16 US$000	Amounts under IAS 17 US$000	**As reported under IFRS 16 US$000**	Adjustment for effect of IFRS 16 US$000	Amounts under IAS 17 US$000
Revenue	**408,803**	–	408,803	**1,185,657**	–	1,185,657
Cost of sales	**(207,645)**	(29)	(207,674)	**(527,263)**	(115)	(527,378)
Gross profit	**201,158**	(29)	201,129	**658,394**	(115)	658,279
Operating expenses, net	**(122,457)**	(298)	(122,755)	**(371,041)**	(1,105)	(372,146)
Other operating income	**5,156**	–	5,156	**38,807**	139	38,946
Operating profit	**83,857**	(327)	83,530	**326,160**	(1,081)	325,079
Net finance income	**2,778**	(166)	2,612	**4,813**	1,337	6,150
Profit before income taxes	**86,635**	(493)	86,142	**330,973**	256	331,229
Income tax expense	**(18,439)**	35	(18,404)	**(74,315)**	(77)	(74,392)
Profit after income taxes	**68,196**	(458)	67,738	**256,658**	179	256,837
Net income	**68,196**	(458)	67,738	**256,658**	179	256,837
Earnings per share (US$)						
Basic	**0.96**	–	0.96	**3.53**	0.01	3.54
Diluted	**0.91**	–	0.91	**3.33**	–	3.33

Notes to the condensed consolidated financial statements continued

18. Adoption of IFRS 16 continued

Consolidated balance sheet as at 27 September 2019

	As reported under IFRS 16 US$000	Adjustment for effect of IFRS 16 US$000	Amounts under IAS 17 US$000
Assets			
Other current assets	**23,266**	257	23,523
Total current assets	**1,472,789**	257	1,473,046
Property, plant and equipment – leased	**53,897**	(53,897)	–
Deferred tax assets	**7,587**	(101)	7,486
Total non-current assets	**800,049**	(53,998)	746,051
Total assets	**2,272,838**	(53,741)	2,219,097
Liabilities and equity			
Lease liabilities	**12,027**	(12,027)	–
Total current liabilities	**550,761**	(12,027)	538,734
Lease liabilities	**43,118**	(43,118)	–
Other non-current liabilities	**98,528**	1,160	99,688
Total non-current liabilities	**242,794**	(41,958)	200,836
Retained earnings	**1,260,100**	36	1,260,136
Other reserves	**(176,328)**	208	(176,120)
Total equity	**1,479,283**	244	1,479,527
Total liabilities and equity	**2,272,838**	(53,741)	2,219,097

19. Subsequent events

Agreement to acquire Creative Chips

On 7 October 2019, we announced that we had agreed to acquire a 100% equity interest in Creative Chips, a supplier of integrated circuits ("ICs") to the Industrial Internet of Things ("IIoT") market.

Headquartered near Frankfurt, Germany, with an additional design centre in Dresden, Germany, Creative Chips has a growing IC business supplying a broad portfolio of industrial ethernet and other mixed-signal products to manufacturers of industrial and building automation systems. Creative Chips is also developing a range of highly complementary standard IO-Link IC products, driving broader connectivity in the Industry 4.0 revolution.

We completed the acquisition on 31 October 2019.

We acquired Creative Chips for US$80.0 million on a cash- and debt-free basis. Additional consideration of up to US$23.0 million in cash may be payable contingent on Creative Chips' performance against revenue targets for 2020 and 2021.

On completion, we paid initial consideration of US$83.7 million in cash, including US$3.7 million in respect of Creative Chip's estimated cash, debt and working capital levels on completion that may be subject to adjustment once those amounts have been finalised.

Share buyback programme

On 31 October 2019, we completed the second intermediate settlement of the first tranche of share purchases under the 2019 AGM authority. We purchased 865,000 shares at an initial cost of €37.1 million (US$41.3 million). We have a remaining maximum obligation to purchase shares under this tranche of €79.8 million. The broker may continue to purchase shares under this tranche until 5 December 2019.

Financial performance measures

Use of non-IFRS measures

Our use of non-IFRS measures is explained on pages 156 to 161 of our 2018 Annual Report and Accounts.

Underlying measures of performance and free cash flow are non-IFRS measures because they exclude amounts that are included in, or include amounts that are excluded from, the most directly comparable measure calculated and presented in accordance with IFRS or are calculated using financial measures that are not calculated in accordance with IFRS. We do not regard non-IFRS measures as a substitute for, or superior to, the equivalent IFRS measures. Non-IFRS measures presented by Dialog may not be directly comparable with similarly-titled measures used by other companies.

Underlying measures of performance

During the periods presented, we excluded from the underlying measures of performance the following specific items of income and expense that were recognised in profit or loss in accordance with IFRS because we consider that they hinder comparison of the financial performance of our businesses from one period to another, with each other or with other similar businesses:

- the following items relating to the licensing and asset transfer agreement with Apple in 9M 2019:
  - the non-recurring fee for the perpetual licence over our existing Power Management IP;
  - the gain on the transfer of design centre businesses;
- the share-based compensation expense and related payroll taxes;
- the following items relating to the accounting for business combinations:
  - acquisition-related costs for FCI and Creative Chips in 9M 2019;
  - the amortisation of identifiable intangible assets recognised in business combinations;
  - the recognition in cost of sales of the consumption of the fair value uplift to inventory held by the acquired businesses at the acquisition date for FCI in 9M 2019 and Silego in 9M 2018;
  - the element of deferred amounts payable for Silego that is recognised as a compensation expense;
  - credits recognised on the forfeiture of deferred consideration payable for Silego;
  - the credit arising in 9M 2018 from the change in estimate of the liabilities for the contingent consideration payable for Silego and related fees and the interest expense recognised on the unwinding of the discount on the liabilities;
- integration costs incurred in 9M 2019 in relation to FCI and 9M 2018 in relation to Silego;
- corporate transaction costs incurred in relation to the licensing and asset transfer agreement with Apple and, in 9M 2018, the aborted acquisition of Synaptics;
- non-cash interest expense recognised in 9M 2018 on a patent licensing agreement that was accounted for as a finance lease;
- the effect on profit or loss of the measurement at fair value of strategic investments (comprising the shares and the warrants that we hold in Energous); and
- the income tax effect of the above items, which is calculated by considering the specific tax treatment of each item and by applying the relevant statutory tax rate to those items that are taxable or deductible for tax purposes.

Reconciliation of underlying measures to equivalent IFRS measures

Reconciliations of the underlying measures of performance to the equivalent IFRS measures for the three- and nine-month periods ended 27 September 2019 and 28 September 2018 are presented in the following tables:

Three months ended 27 September 2019

US$000 unless stated otherwise	IFRS basis	Share-based compensation and related payroll taxes	Accounting for business combinations	Integration costs	Corporate transaction costs	Strategic investments	Underlying basis
Revenue	408,803	–	–	–	–	–	408,803
Cost of sales	(207,645)	696	483	–	–	–	(206,466)
Gross profit	201,158	696	483	–	–	–	202,337
Gross margin %	*49.2%*						*49.5%*
SG&A expenses	(43,611)	6,141	5,343	306	235	–	(31,586)
R&D expenses	(78,846)	3,881	2,877	–	–	–	(72,088)
Other operating income	5,156	–	–	–	–	–	5,156
Operating profit	83,857	10,718	8,703	306	235	–	103,819
Operating margin %	*20.5%*						*25.4%*
Net finance income	2,778	–	–	–	–	(121)	2,657
Profit before income taxes	86,635	10,718	8,703	306	235	(121)	106,476
Income tax expense	(18,439)	(2,204)	(1,127)	(58)	(3)	24	(21,807)
Net income	68,196	8,514	7,576	248	232	(97)	84,669
EBITDA	n/a						120,818
EBITDA margin %	*n/a*						*29.6%*

Financial performance measures continued

Three months ended 28 September 2018

US$000 unless stated otherwise	IFRS basis	Share-based compensation and related payroll taxes	Accounting for business combinations	Integration costs	Corporate transaction costs	Strategic investments	Underlying basis
Revenue	383,574	–	–	–	–	–	383,574
Cost of sales	(197,599)	284	335	–	–	–	(196,980)
Gross profit	185,975	284	335	–	–	–	186,594
Gross margin %	*48.5%*						*48.6%*
SG&A expenses	(42,926)	4,734	3,673	940	3,880	–	(29,699)
R&D expenses	(82,180)	5,187	2,272	–	–	–	(74,721)
Other operating income	2,619	–	(1,113)	–	–	–	1,506
Operating profit	63,488	10,205	5,167	940	3,880	–	83,680
Operating margin %	*16.6%*						*21.8%*
Net finance (expense)/income	(1,196)	–	459	–	–	3,199	2,462
Profit before income taxes	62,292	10,205	5,626	940	3,880	3,199	86,142
Income tax expense	(15,504)	(1,829)	(761)	(197)	(571)	(607)	(19,469)
Profit after income taxes	46,788	8,376	4,865	743	3,309	2,592	66,673
Share of loss of associate	(367)	–	–	–	–	–	(367)
Net income	46,421	8,376	4,865	743	3,309	2,592	66,306
EBITDA	n/a						98,698
EBITDA margin %	*n/a*						*25.7%*

Nine months ended 27 September 2019

US$000 unless stated otherwise	**IFRS basis**	**Licence and asset transfers to Apple**	**Share-based compensation and related payroll taxes**	**Accounting for business combinations**	**Integration costs**	**Corporate transaction costs**	**Strategic investments**	**Underlying basis**
Revenue	**1,185,657**	**(145,750)**	**–**	**–**	**–**	**–**	**–**	**1,039,907**
Cost of sales	**(527,263)**	**–**	**2,036**	**886**	**–**	**–**	**–**	**(524,341)**
Gross profit	**658,394**	**(145,750)**	**2,036**	**886**	**–**	**–**	**–**	**515,566**
Gross margin %	***55.5%***							***49.6%***
SG&A expenses	**(136,006)**	**–**	**16,573**	**14,577**	**502**	**10,894**	**–**	**(93,460)**
R&D expenses	**(235,035)**	**–**	**15,496**	**7,605**	**–**	**–**	**–**	**(211,934)**
Other operating income	**38,807**	**(15,898)**	**–**	**–**	**–**	**–**	**–**	**22,909**
Operating profit	**326,160**	**(161,648)**	**34,105**	**23,068**	**502**	**10,894**	**–**	**233,081**
Operating margin %	***27.5%***							***22.4%***
Net finance income	**4,813**	**–**	**–**	**315**	**–**	**–**	**245**	**5,373**
Profit before income taxes	**330,973**	**(161,648)**	**34,105**	**23,383**	**502**	**10,894**	**245**	**238,454**
Income tax expense	**(74,315)**	**33,907**	**(5,228)**	**(2,795)**	**(95)**	**(259)**	**(46)**	**(48,831)**
Net income	**256,658**	**(127,741)**	**28,877**	**20,588**	**407**	**10,635**	**199**	**189,623**
EBITDA	**n/a**							**283,156**
EBITDA margin %	***n/a***							***27.2%***

Nine months ended 28 September 2018

US$000 unless stated otherwise	IFRS basis	Share-based compensation and related payroll taxes	Accounting for business combinations	Integration costs	Corporate transaction costs	Effective interest	Strategic investments	Underlying basis
Revenue	1,011,393	–	–	–	–	–	–	1,011,393
Cost of sales	(529,794)	1,432	3,129	13	–	–	–	(525,220)
Gross profit	481,599	1,432	3,129	13	–	–	–	486,173
Gross margin %	*47.6%*							*48.1%*
SG&A expenses	(121,419)	12,656	11,026	1,862	4,653	–	–	(91,222)
R&D expenses	(241,358)	15,211	6,873	228	–	–	–	(219,046)
Other operating income	3,776	–	(1,477)	–	–	–	–	2,299
Operating profit	122,598	29,299	19,551	2,103	4,653	–	–	178,204
Operating margin %	*12.1%*							*17.6%*
Net finance (expense)/income	(3,737)	–	1,630	–	–	50	7,455	5,398
Profit before income taxes	118,861	29,299	21,181	2,103	4,653	50	7,455	183,602
Income tax expense	(35,832)	129	(2,747)	(442)	(654)	(9)	(401)	(39,956)
Profit after income taxes	83,029	29,428	18,434	1,661	3,999	41	7,054	143,646
Share of loss of associate	(1,116)	–	–	–	–	–	–	(1,116)
Net income	81,913	29,428	18,434	1,661	3,999	41	7,054	142,530
EBITDA	n/a							221,869
EBITDA margin %	*n/a*							*21.9%*

Notes

(i) Accounting for business combinations

We excluded from the underlying measures of performance the following specific items arising from business combinations accounting under IFRS:

US$000	**Q3 2019**	Q3 2018	**9M 2019**	9M 2018
Acquisition-related costs	**1,021**	–	**2,696**	–
Amortisation of acquired intangible assets	**6,964**	5,658	**18,724**	16,972
Consumption of the fair value uplift of acquired inventory	**483**	335	**886**	3,129
Consideration accounted for as compensation expense	**285**	342	**910**	1,146
Forfeiture of deferred consideration	**(50)**	(14)	**(148)**	(177)
Remeasurement of contingent consideration	**–**	(1,154)	**–**	(1,519)
Increase in operating profit	**8,703**	5,167	**23,068**	19,551
Unwinding of discount on contingent consideration	**–**	459	**315**	1,630
Increase in profit before income taxes	**8,703**	5,626	**23,383**	21,181
Income tax credit	**(1,127)**	(761)	**(2,795)**	(2,747)
Increase in net income	**7,576**	4,865	**20,588**	18,434

(ii) Underlying earnings per share

Earnings for calculating underlying EPS measures were as follows:

US$000	**Q3 2019**	Q3 2018	**9M 2019**	9M 2018
Underlying measures				
Net income	**84,669**	66,306	**189,623**	142,530
Earnings for calculating basic and diluted EPS	**84,669**	66,306	**189,623**	142,530

Underlying earnings per share measures are calculated using the weighted average number of shares that are used in calculating the equivalent measures under IFRS as presented in note 5 to the interim financial statements as follows:

Number	**Q3 2019**	Q3 2018	**9M 2019**	9M 2018
Weighted average number of ordinary shares				
Basic	**70,779,673**	73,966,230	**72,605,208**	73,849,706
Diluted	**74,777,271**	77,971,351	**77,043,366**	77,753,984

Underlying earnings per share measures were therefore as follows:

US$	**Q3 2019**	Q3 2018	**9M 2019**	9M 2018
Underlying earnings per share				
Basic	**1.20**	0.90	**2.61**	1.93
Diluted	**1.13**	0.85	**2.46**	1.83

Financial performance measures continued

(iii) Underlying EBITDA
Underlying EBITDA may be reconciled to net income determined in accordance with IFRS as follows:

US$000	Q3 2019	Q3 2018	9M 2019	9M 2018
Net income	**68,196**	46,421	**256,658**	81,913
Net finance (income)/expense	**(2,778)**	1,196	**(4,813)**	3,737
Income tax expense	**18,439**	15,504	**74,315**	35,832
Depreciation expense	**10,189**	8,138	**30,672**	24,074
Amortisation expense	**13,774**	12,538	**38,127**	36,563
EBITDA	**107,820**	83,797	**394,959**	182,119
Licence and asset transfers to Apple	**–**	–	**(161,648)**	–
Share-based compensation and related payroll taxes	**10,718**	10,205	**34,105**	29,299
Acquisition-related costs	**1,021**	–	**2,696**	–
Consumption of the fair value uplift of acquired inventory	**483**	335	**886**	3,129
Consideration accounted for as compensation expense	**285**	342	**910**	1,146
Forfeiture of deferred consideration	**(50)**	(14)	**(148)**	(177)
Remeasurement of contingent consideration	**–**	(1,154)	**–**	(1,519)
Corporate transaction costs	**235**	3,880	**10,894**	4,653
Integration costs	**306**	940	**502**	2,103
Share of loss of associate	**–**	367	**–**	1,116
Underlying EBITDA	**120,818**	98,698	**283,156**	221,869

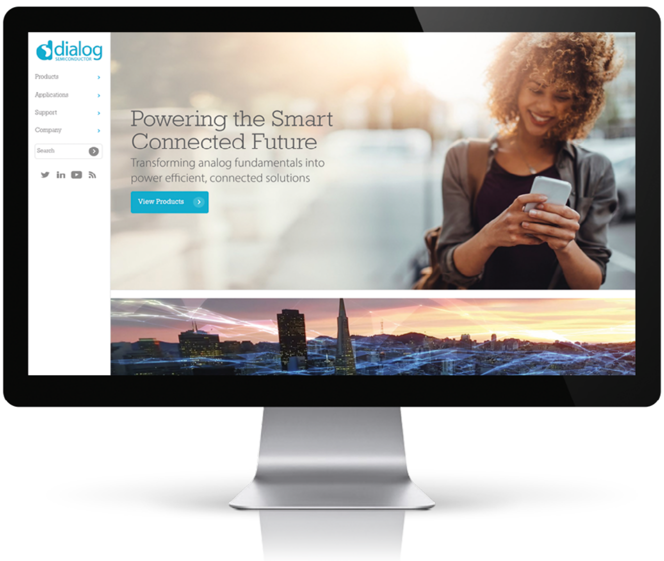
Free cash flow

Free cash flow was calculated as follows:

US$000	Q3 2019	Q3 2018	9M 2019	9M 2018
Cash flow from operating activities	**97,316**	86,896	**439,017**	192,183
Purchase of property, plant and equipment	**(3,157)**	(3,462)	**(10,142)**	(20,245)
Purchase of intangible assets	**(1,770)**	(653)	**(3,957)**	(3,891)
Payments for capitalised development costs	**(2,618)**	(3,731)	**(11,189)**	(18,950)
Capital element of lease payments	**(2,981)**	–	**(8,662)**	(1,650)
Free cash flow	**86,790**	79,050	**405,067**	147,447

Registered office

Dialog Semiconductor Plc
Tower Bridge House
St Katharine's Way
London E1W 1AA
UK
www.dialog-semiconductor.com



www.dialog-semiconductor.com