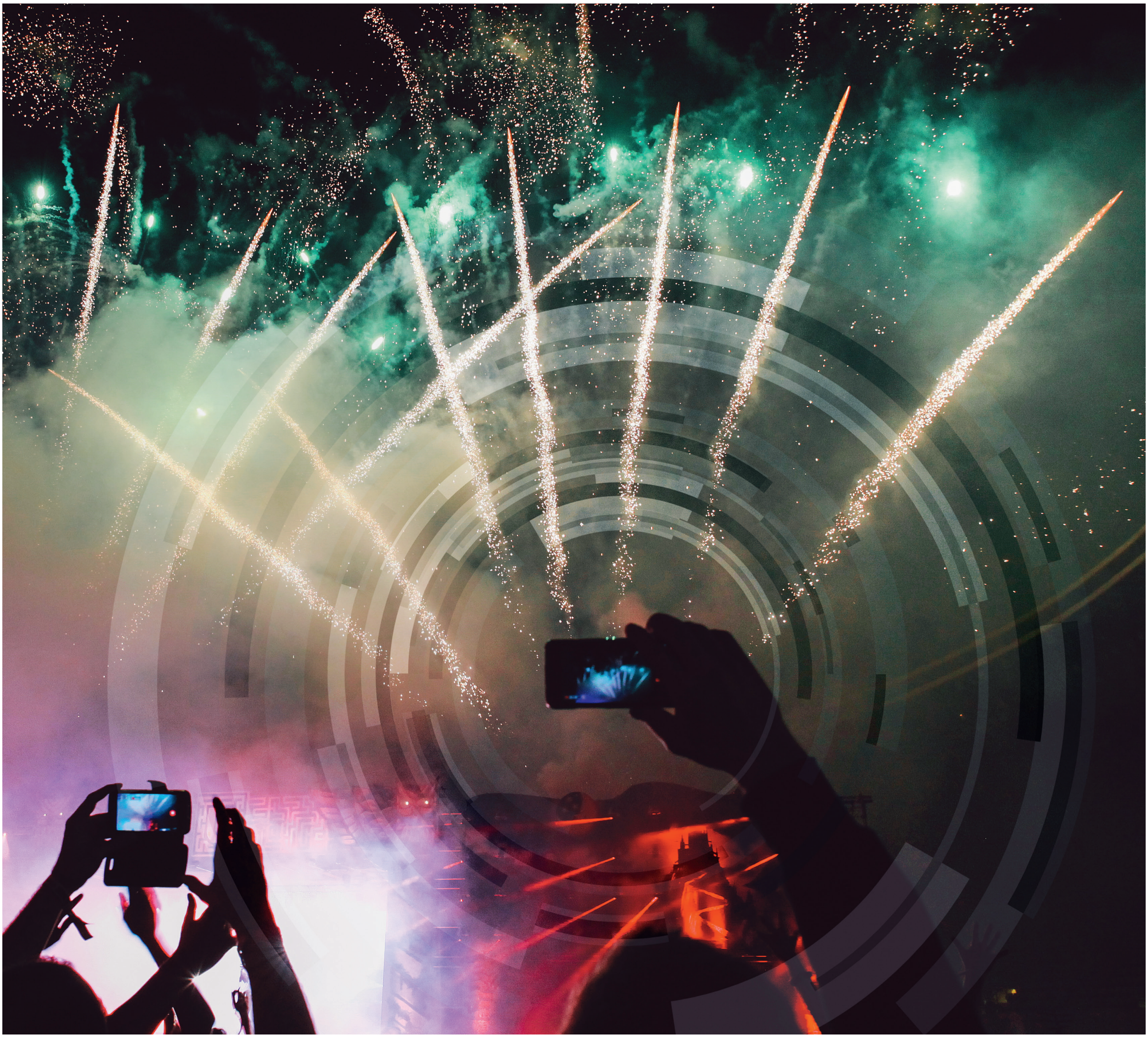
Dialog Semiconductor Plc

Interim Report for the three months ended 31 March 2017

Always moving



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Key products




Press release – 9 May 2017

DIALOG SEMICONDUCTOR REPORTS RESULTS FOR THE FIRST QUARTER ENDED 31 MARCH 2017

Q1 2017 revenue up 12% year-on-year and strong cash flow generation

London, UK, May 9, 2017 - Dialog Semiconductor Plc (XETRA: DLG), a provider of highly integrated power management, AC/DC, solid state lighting and Bluetooth® low energy wireless technology, today reports results for the first quarter ended 31 March 2017.

Q1 2017 financial highlights

- Revenue of US$271 million slightly above the mid-point of February guidance.
- All operational business segments delivered year-on-year revenue growth.
- Gross margin at 45.3% and underlying[1] gross margin at 46.1%, in line with the February guidance.
- Operating profit of US$29.1 million, 81% below Q1 2016 which included US$137 million of the Atmel termination fee.
- Underlying[1] operating profit of US$43.2 million, up 44% year-on-year.
- All operational business segments delivered operating profits on an underlying[1] basis.
- Diluted EPS of US$0.29 and underlying[1] diluted EPS of US$0.43.
- US$41.4 million returned to shareholders through the share buyback programme.
- Cash flow from operating activities of US$100.7 million (Q1 2016: US$107.1 million). US$85.9 million of free cash flow[1,2] generated in Q1 2017. US$723 million of cash and cash equivalents, US$61 million above 1 April 2016.

Subsequent to the end of the quarter, the first intermediate settlement of the third tranche of the share buyback programme took place. On 25 April 2017, the Company purchased 650,000 ordinary shares at an average price of €48.2459.

Q1 2017 operational highlights

- Continued momentum and design-in engagements for custom Power Management ICs (PMICs) at leading OEMs, for next generation smartphones, tablets, computing and wearable products.
- Partnership with Spreadtrum announced, with first power related mixed signal IC for Spreadtrum's latest LTE platform demonstrated.
- Diversification and expansion of our PMIC portfolio into the automotive market announcing Renesas as an automotive processor platform partner.
- Smartphone high efficiency charger standard product family launched, a new high growth ASSP market segment for Dialog.
- First RF-transmit wireless charging IC sampled, following the strategic partnership with Energous.
- Company's first Bluetooth® low energy System-on-Chip qualified, supporting latest Bluetooth 5.0 standard.

1) Underlying measures and free cash flow quoted in this Press Release are non-IFRS measures (see page 4).
2) The definition of free cash flow has changed to align it with our peers'. Free cash flow now represents cash flow from operating activities less capital expenditure. Free cash flow was previously defined as net income before depreciation, amortisation, plus/minus net finance income/(expense), net decrease/(increase) in working capital, and minus capital expenditure.

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

"This has been a positive start to the year and I'm pleased to report double-digit revenue growth, in line with our guidance. Particularly encouraging is the strong revenue growth recorded across all of our business segments. Our leadership position in the rapid charge market and the continued expansion of our portfolio of Bluetooth® low energy products are both helping to drive our momentum.

We remain focused on new areas of growth where we can differentiate with our innovative technology. Addressing high-efficiency smartphone charging and our partnership with Spreadtrum, offer exciting opportunities to increase our market share in Asia. All of this, combined with the increasing value we bring to our customers, underpins my confidence in our growth prospects for this year and over the medium-term."

Outlook

Based on our current visibility, we anticipate revenue for Q2 2017 to be in the range of US$235-US$265 million.

Good business momentum and a pipeline of key product launches in the second half of the year, give us confidence in expecting 2017 to be a year of good revenue growth. As in previous years, revenue performance will be strongly weighted towards the second half of the year.

In line with the revenue performance, we expect gross margin for Q2 2017 and the full year 2017 to be broadly in line with Q1 2017.

Financial overview

IFRS

US$ millions	**Q1 2017**	Q1 2016	Change
Revenue	**271.0**	241.4	+12%
Gross margin	**45.3%**	44.6%	+70bps
R&D %[3]	**22.5%**	23.8%	–130bps
SG&A %[3]	**12.0%**	15.1%	–310bps
Other operating income[3,4]	**–**	56.9%	nm
Operating profit	**29.1**	151.2	–81%
Operating margin	**10.7%**	62.6%	nm
Net income	**23.1**	142.9	–84%
Basic EPS (US$)	**0.31**	1.89	–84%
Diluted EPS (US$)	**0.29**	1.80	–84%
Cash flow from operating activities	**100.7**	107.1	–6%

Underlying[1]

US$ millions	**Q1 2017**	Q1 2016	Change
Revenue	**271.0**	241.4	+12%
Gross margin	**46.1%**	45.5%	+60bps
R&D %[3]	**20.7%**	22.3%	–160bps
SG&A %[3]	**9.4%**	10.9%	–150bps
EBITDA	**57.4**	40.7	+41%
EBITDA %	**21.2%**	16.9%	+430bps
Operating profit	**43.2**	29.9	+44%
Operating margin	**15.9%**	12.4%	+350bps
Net income	**34.4**	21.6	+59%
Basic EPS (US$)	**0.46**	0.29	+59%
Diluted EPS (US$)	**0.43**	0.28	+54%

3) R&D, SG&A and other operating income as a percentage of revenue.
4) Other operating income in 2016 includes US$137 million Atmel termination fee.

Revenue in Q1 2017 was up 12% year on year to US$271 million. All business segments delivered year-on-year revenue growth. Mobile Systems was up 9% year-on-year due to higher sales volumes. Power Conversion delivered 22% year-on-year revenue growth, the sixth consecutive quarter of strong double digit growth. Connectivity was up 29% year-on-year on the solid performance of Bluetooth® low energy and DECT products. Automotive & Industrial was up 12% year-on-year.

Q1 2017 gross margin was 45.3%, 70bps above Q1 2016. Q1 2017 underlying[1] gross margin was 46.1%, 60bps above Q1 2016. The year-on-year increase in gross margin is primarily the result of a favourable product mix combined with higher sales volumes.

OPEX, comprising SG&A and R&D expenses, in Q1 2017 was US$93.6 million, broadly in line with Q1 2016. As a percentage of revenue, OPEX in Q1 2017 was 34.5% of revenue, representing a reduction of 440bps year-on-year. Underlying[1] OPEX, comprising of underlying SG&A and R&D expenses, in Q1 2017 was US$81.7 million, 2% above Q1 2016. As a percentage of revenue, underlying OPEX was 30.1%, representing a reduction of 310bps year-on-year. On a trailing twelve month basis, underlying[1] OPEX was 27.4% of revenue, 50bps below the previous quarter.

R&D expense in Q1 2017 was up 6% from Q1 2016. As a percentage of revenue, R&D in Q1 2017 was down 130bps year-on-year to 22.5%. On an underlying[1] basis, R&D expense was up 5% from Q1 2016. As a percentage of revenue, underlying[1] R&D in Q1 2017 was down 160bps year-on-year to 20.7%. This moderate increase in R&D expense was predominantly driven by the on-going investment in large application-specific customer opportunities as well as in programmes supporting new growth areas and the diversification of the business. The year-on-year reduction in R&D as a percentage of revenue is the result of the higher revenue in the quarter partially offset by the moderate increase in R&D.

SG&A expense in Q1 2017 was down 11% from Q1 2016. This decrease was predominantly due to US$3.6 million of Atmel related costs accounted for in Q1 2016. As a percentage of revenue, SG&A in Q1 2017 was 310bps below Q1 2016. Underlying[1] SG&A expense in Q1 2017 was down 3% on Q1 2016. As a percentage of revenue, underlying SG&A was 150bps below Q1 2016 to 9.4%. This decrease was the result of a decrease in SG&A costs and the higher revenue.

Operating profit in Q1 2017 was US$29.1 million, down 81% year-on-year. The primary driver of this decrease was the Atmel termination fee (US$137 million) accounted for in Q1 2016. Operating profit margin in the quarter was 10.7%, also below Q1 2016. Underlying[1] operating profit was US$43.2 million, up 44% year-on-year, as a result of the higher revenue and moderate increase in underlying operating expenses. Underlying[1] operating margin in the quarter was 15.9%, 350bps above Q1 2016.

The effective tax rate in Q1 2017 was 21.2% (FY2016: 15.4%). The low effective tax rate in Q1 2016 reflected the tax treatment of the US$137 million Atmel termination fee. The underlying[1] effective tax rate in Q1 2017 was 22.7%, down 130bps on the FY2016 underlying effective tax rate (FY2016: 24.0%).

In Q1 2017, net income was down 84% year-on-year. This decline was mainly due to the Atmel termination fee accounted for in Q1 2016. Underlying[1] net income was up 59% year-on-year as a result of the increase in underlying[1] operating profit. Underlying[1] diluted EPS in Q1 2017 was up 54% year-on-year.

At the end of Q1 2017, our total inventory level was US$89.2 million, 15% below the previous quarter and representing 54 days of inventory, a 6-day increase from the previous quarter. During Q2 2017, we expect inventory value and days of inventory to increase from Q1 2017 ahead of the ramp of new products in H2 2017.

On 17 February 2017, the final settlement of the second tranche of the buyback programme took place. During Q1 2017, the Company returned €38.8 million (US$ 41.4 million) to shareholders through the share buyback programme. Subsequent to quarter end, on 25 April 2017, the first settlement of the third tranche of the share buyback programme took place. The Company purchased 650,000 ordinary shares at an average price of €48.2459. The total number of shares purchased by the Company under the buyback programme as of the 25 April 2017 was 3,433,206.

Share buybacks are a core element of our capital allocation framework and the company remains committed to returning excess cash to shareholders through the share buyback programme. At the Company's Annual General Meeting on 4 May 2017, shareholders granted approval to purchase up to 10% of the issued ordinary share capital.

At the end of Q1 2017, we had a cash and cash equivalents balance of US$723 million. Cash flow from operating activities in Q1 2017 was US$100.7 million, 6% below Q1 2016 which included $137 million for the Atmel termination fee.

Operational overview

Our proven success with top OEM customers for custom solutions continued through Q1 2017. We have a number of new PMIC design-wins and further engagements for future smartphone generations and other consumer mobile platforms. These key custom engagements offer significant benefits in space and power savings, encouraging a trend of increasing custom mixed signal power content across future platforms for mobile devices, computing and wearables, in 2017 and over the medium term.

We also announced that Dialog will provide its highly-integrated mixed signal power related technologies for Spreadtrum's next generation LTE platforms, targeting global mainstream LTE smartphone markets. The first phase of the partnership will see Dialog's latest custom SC2705 included in Spreadtrum's

LTE platform SC9861G-IA offering an opportunity for us to increase our market share in Asia. Additional derivatives of the technology from both companies are also under development, targeting different smartphone entry levels and regional markets.

In line with our strategic objective to expand our standard product portfolio, the Mobile Systems Business Group introduced a next generation Charger IC, the DA9313. Targeting mobile devices, this new IC delivers industry leading efficiency as high as 98%.

Additionally, subsequent to the quarter end, Dialog announced a PMIC chipset powering the Renesas R-Car H3 automotive computing platform for driving support systems and in-vehicle infotainment systems. The chipset comprises of the DA9063-A system PMIC and two sub PMICS, the DA9213-A and DA9214-A, expanding our portofolio of PMICs into the automotive market.

The Power Conversion Business Group delivered its sixth consecutive quarter of year-on-year revenue growth. Dialog Rapid Charge™ power adapter solutions continue to be adopted for new smartphone models by leading Asian OEMs. Dialog enjoys a commanding market share in this fast charging segment.

Our strategic partnership with Energous continues to attract strong market interest with the launch of the first WattUp™ RF-transmit wireless charging IC, the DA4100. This is the first IC made available since the partnership was announced in November 2016. Radio Frequency based charging technology has the potential to revolutionalize the wireless charging landscape. Through this partnership, Dialog became the exclusive component supplier of the WattUp ICs.

The Connectivity Business Group expanded its SmartBond™ product portfolio with the introduction of its first Bluetooth® low energy System-on-Chip (SoC), the DA14586, which achieved early qualification for the new Bluetooth 5.0 standard. The DA14586 brings increasing value to customers, building on the SmartBond credentials of flexibility and low power consumption with additional features allowing customers to add intuitive intelligent voice control to any cloud connected IoT product.

Non-IFRS measures

Underlying measures of profitability and free cash flow quoted in this Press Release are non-IFRS measures. Our use of underlying measures and reconciliations of the underlying measures to the nearest equivalent IFRS measures for Q1 2017 and Q1 2016 are presented in Section 3 of the Q1 2017 Interim Results Report. For ease of reference, we present below reconciliations for the non-IFRS measures quoted in this Press Release:

Income statement items

Q1 2017

US$'000	IFRS basis	Share-based compensation and related payroll taxes	Amortisation of acquired intangible assets	Effective interest	Strategic investments	Underlying basis
Revenue	270,974	–	–	–	–	270,974
Gross profit	122,646	536	1,768	–	–	124,950
SG&A expenses	(32,602)	5,243	1,824	–	–	(25,535)
R&D expenses	(60,951)	4,737	–	–	–	(56,214)
Operating profit	29,093	10,516	3,592	–	–	43,201
Net finance income/(expense)	246	–	–	95	973	1,314
Profit before income taxes	29,339	10,516	3,592	95	973	44,515
Income tax expense	(6,220)	(3,355)	(209)	(18)	(318)	(10,120)
Net income	23,119	7,161	3,383	77	655	34,395

Q1 2016

US$'000	IFRS basis	Share-based compensation and related payroll taxes	Amortisation of acquired intangible assets	Aborted merger with Atmel	Effective interest	Underlying basis
Revenue	241,408	–	–	–	–	241,408
Gross profit	107,661	519	1,751	–	–	109,931
SG&A expenses	(36,430)	4,513	1,900	3,606	–	(26,411)
R&D expenses	(57,524)	3,743	–	–	–	(53,781)
Other operating income	137,478	–	–	(137,300)	–	178
Operating profit	151,185	8,775	3,651	(133,694)	–	29,917
Net finance income/(expense)	(4,279)	–	–	1,913	153	(2,213)
Profit before income taxes	146,906	8,775	3,651	(131,781)	153	27,704
Income tax expense	(4,015)	(1,451)	(215)	(383)	(31)	(6,095)
Net income	142,891	7,324	3,436	(132,164)	122	21,609

EBITDA

US$'000	**Q1 2017**	Q1 2016
Underlying measures		
Net income	**34,395**	21,609
Net finance income/(expense)	**(1,314)**	2,213
Income tax expense	**10,120**	6,095
Depreciation expense	**7,414**	6,434
Amortisation expense	**6,827**	4,394
EBITDA	**57,442**	40,745

FREE CASH FLOW - HISTORICAL DATA

US$'000	**Q1 2017**	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Q1 2015	Q2 2015	Q3 2015	Q4 2015
Underlying measures									
Cash flow from operating activities	**100,653**	107,077	13,498	39,281	88,904	119,565	45,717	42,718	109,663
Purchase of property, plant and equipment	**(6,899)**	(5,668)	(5,528)	(6,974)	(7,604)	(5,687)	(10,939)	(5,861)	(10,468)
Purchase of intangible assets	**(1,690)**	(2,480)	(2,139)	(2,156)	(5,015)	(3,232)	(3,125)	(2,290)	(3,031)
Payments for capitalised development costs	**(6,212)**	(5,741)	(4,136)	(1,839)	(4,086)	(5,454)	(5,889)	(5,420)	(8,015)
Free cash flow	**85,852**	93,188	1,695	28,312	72,199	105,192	25,764	29,147	88,149

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Dialog Semiconductor invites you today at 09.30 am (London) / 10.30 am (Frankfurt) to take part in a live conference call and to listen to management's discussion of the Company's Q1 2017 performance, as well as guidance for Q2 2017. Participants will need to register using the link below labelled 'Online Registration'. 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:

http://members.meetingzone.com/selfregistration/registration.aspx?booking=EMtGZMCviBDVpbIkRd5RigmRuvyIwRx3qvEYCSpf0bM=&b=d58ae4ab-80e5-47f2-8295-e04d92bbba83

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

http://webcast.openbriefing.com/semiconductor_q1_results_090517/

The full release including the Company's condensed consolidated income statement, consolidated balance sheet, consolidated statements of cash flows and selected notes for the quarter ended 31 March 2017 is available under the investor relations section of the Company's website at:

http://www.dialog-semiconductor.com/investor-relations

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Note to editors

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 the employees, 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. In 2016, it had US$1.2 billion in revenue and approximately 1,770 employees worldwide. The company is listed on the Frankfurt (FWB: DLG) stock exchange (Regulated Market, Prime Standard, ISIN GB0059822006) and is a member of the German TecDax index.

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

Three months ended 31 March 2017

Background

Interim financial statements

The unaudited interim financial statements of Dialog Semiconductor Plc ("the Company") and its subsidiaries (together, "Dialog" or "the Group") for the three months ended 31 March 2017 are set out in Section 2 of this Interim Report.

The Group's significant accounting policies are unchanged compared with the year ended 31 December 2016 (see pages 94 to 102 of our Annual Report and Accounts 2016).

Additional investment in Dyna Image

In January 2017, the Group participated in a new issue of shares by its subsidiary, Dyna Image Corporation. We invested the equivalent of US$1.9 million and Lite-On Semiconductor Corp, one of the non-controlling shareholders in Dyna Image, invested the equivalent of US$1.1 million.

As a result of the share issue, our shareholding in Dyna Image increased from 45.7% to 48.5%. We reflected the increase in our shareholding as a transfer of US$0.3 million within equity from non-controlling interests to retained earnings.

We continue to hold a call option over the shares in Dyna Image that we do not already own that expires in June 2018.

Disposal of investment in Arctic Sand

On 15 March 2017, Peregrine Semiconductor Corporation, a subsidiary of Murata Manufacturing Co Ltd, agreed to acquire Arctic Sand Technologies, Inc. by way of a merger.

Dialog held approximately 3.5% of the issued equity shares in Arctic Sand. As at 31 March 2017, we reclassified our shares in Arctic Sand as assets held for sale measured at the amount of US$1.2 million that we received on 1 May 2017 following completion of the merger.

During Q1 2017, we recognised the resulting impairment loss of US$0.2 million in profit or loss (within other finance expense).

Aborted merger with Atmel

In January 2016, Atmel Corporation, Inc. terminated the merger agreement that existed with Dialog. Under the terms of the agreement, Atmel paid us a termination fee of US$137.3 million, which we recognised as other operating income in Q1 2016.

During Q1 2016, we recognised related transaction costs of US$3.6 million and commitment fees of US$1.9 million in relation to the US$2.1 billion borrowing facility that was arranged to finance the transaction before the cancellation of the facility in January 2016.

Results of operations

Analysis by operating segment

	Revenue			Operating profit/(loss)	
US$ millions	**Q1 2017**	Q1 2016	Change	**Q1 2017**	Q1 2016
Q1 2017 compared with Q1 2016					
Mobile Systems	**204.4**	187.8	+9%	**46.2**	39.8
Automotive & Industrial	**8.0**	7.1	+12%	**3.0**	2.7
Connectivity	**26.6**	20.6	+29%	**0.7**	(3.4)
Power Conversion	**29.3**	24.0	+22%	**(1.8)**	(6.3)
Total segments	**268.3**	239.5	+12%	**48.1**	32.8
Corporate activities	**2.7**	1.9	+42%	**(19.0)**	118.4
Total	**271.0**	241.4	+12%	**29.1**	151.2

Mobile Systems segment revenue was US$204.4 million in Q1 2017 compared with US$187.8 million in Q1 2016, an increase of 9%. Revenue increased principally due to higher sales of our PMICs resulting from improved demand for high-end smart phones. Mobile Systems represented 75.5% of the Group's revenue in Q1 2017 (Q1 2016: 77.8%).

Mobile Systems' operating profit was US$46.2 million in Q1 2017 compared with US$39.8 million in Q1 2016, an increase of 16%. Operating profit improved in response to the increase in revenue but this was partially offset by higher amortisation of capitalised development costs. Operating margin improved to 22.6 % (Q1 2016: 21.2%), principally reflecting the higher contribution to fixed costs.

Mobile Systems' underlying operating profit was US$47.3 million in Q1 2017 compared with US$41.1 million in Q1 2016. Underlying operating margin was also higher at 23.1% (Q1 2016: 21.9%).

Mobile Systems' underlying operating profit excludes payroll taxes arising on share-based compensation of its employees, which amounted to US$1.1 million in Q1 2017 (Q1 2016: US$1.2 million).

Automotive & Industrial segment revenue was US$8.0 million in Q1 2017 compared with US$7.1 million in Q1 2016, an increase of 12%. Revenue increased primarily because of improved demand for traditional industrial lighting products. Automotive & Industrial represented 2.9% of the Group's revenue in Q1 2017 (Q1 2016: 3.0%).

Automotive & Industrial's operating profit was US$3.0 million in Q1 2017 compared with US$2.7 million in Q1 2016, an increase of 11%. Operating margin improved to 38.2% (Q1 2016: 37.8%) reflecting more selective investment in R&D projects.

Automotive & Industrial's underlying operating profit was US$3.1 million in Q1 2017 compared with US$2.7 million in Q1 2016. Underlying operating margin was also higher at 38.9% (Q1 2016: 37.8%).

Automotive & Industrial's underlying operating profit excludes payroll taxes arising on share-based compensation of its employees, which amounted to US$0.1 million in Q1 2017 (Q1 2016: US$0.1 million).

Underlying measures of profitability quoted in the Finance 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.

Financial review continued

Three months ended 31 March 2017

Connectivity segment revenue was US$26.6 million in Q1 2017 compared with US$20.6 million in Q1 2016, an increase of 29%. Strong growth in Bluetooth® low energy was accompanied by higher demand for DECT-based products, in particular for cordless headsets and microphones. Connectivity represented 9.8% of the Group's revenue in Q1 2017 (Q1 2016: 8.5%).

Connectivity returned an operating profit of US$0.7 million in Q1 2017 compared with an operating loss of US$3.4 million in Q1 2016, with the improvement due largely to higher revenue and lower expenditure on R&D projects.

Connectivity's underlying operating profit was US$0.8 million in Q1 2017 compared with an underlying operating loss of US$3.2 million in Q1 2016. Underlying operating margin was 3.0% in Q1 2017 compared with (15.5)% in Q1 2016.

Connectivity's underlying operating profit excludes payroll taxes arising on share-based compensation of its employees, which amounted to US$0.2 million in Q1 2017 (Q1 2016: US$0.2 million).

Power Conversion segment revenue increased by 22% to US$29.3 million in Q1 2017 compared with US$24.0 million in Q1 2016. Revenue increased principally due to strong demand for our AC/DC solutions, with continued success in Rapid Charge™ for smartphone power adapters being accompanied by higher sales of 10W converters. Power Conversion represented 10.8% of the Group's revenue in Q1 2017 (Q1 2016: 9.9%).

Power Conversion incurred an operating loss of US$1.8 million in Q1 2017 but this was an improvement compared with its operating loss of US$6.3 million in Q1 2016. Power Conversion's improved operating result primarily reflected higher sales but there was also a reduction in R&D costs. Operating margin improved to (6.2)% in Q1 2017 compared with (26.2)% in Q1 2016.

Power Conversion delivered an underlying operating profit of US$1.6 million in Q1 2017 compared with an underlying operating loss of US$2.8 million in Q1 2016. Underlying operating margin was 5.5% in Q1 2017 compared with (11.7)% in Q1 2016.

Power Conversion's underlying operating result excludes payroll taxes arising on share-based compensation of its employees, which amounted to US$0.1 million (Q1 2016: US$0.2 million) and additional amortisation of US$3.3 million (Q1 2016: US$3.3 million) on the fair value uplift of intangible assets acquired with iWatt, Inc. in 2013.

Corporate activities include emerging market businesses (principally Dyna Image and those involved in the development of low cost PMICs for the Chinese consumer markets). Corporate's revenue of US$2.7 million (Q1 2016: US$1.9 million) was mostly attributable to Dyna Image.

Corporate activities also include the costs of operating central corporate functions, and the Group's share-based compensation expense and certain other unallocated costs.

Corporate activities showed an operating loss of US$19.0 million in Q1 2017 compared with an operating profit of US$118.4 million in Q1 2016. Excluding the Atmel termination fee and related transaction costs, Corporate showed an operating loss of US$15.3 million in Q1 2016.

Corporate's underlying operating result additionally excludes the Group's share-based compensation expense of US$9.0 million (Q1 2016: US$7.1 million), payroll taxes arising on share-based compensation of Corporate employees of US$0.1 million (Q1 2016: US$0.1 million) and additional amortisation of US$0.3 million (Q1 2016: US$0.3 million) on the fair value uplift of intangible assets acquired with Dyna Image.

Corporate's underlying operating loss was US$9.7 million in Q1 2017 compared with US$7.9 million in Q1 2016, with the increase principally due to higher R&D costs which were only partially offset by a reduction in advisory fees.

Analysis of the Group's results

Revenue was US$271.0 million in Q1 2017 compared with US$241.4 million in Q1 2016, an increase of 12%. Revenue increased principally due to higher demand for our PMICs in Mobile Systems, while strong revenue growth was also experienced in Connectivity and Power Conversion.

Cost of sales was US$148.3 million in Q1 2017 compared with US$133.7 million in Q1 2016, an increase of 11% that principally reflected higher sales volumes.

Gross profit was US$122.6 million in Q1 2017 compared with US$107.7 million in Q1 2016, an increase of 14%.

Gross margin was 70 basis points higher at 45.3% in Q1 2017 compared with 44.6% in Q1 2016. Gross margin improved principally due to the greater contribution to fixed costs arising from increased sales volumes.

Underlying gross profit was also 14% higher at US$124.9 million in Q1 2017 compared with US$109.9 million in Q1 2016. Underlying gross margin was 60 basis points higher at 46.1% in Q1 2017 compared with 45.5% in Q1 2016.

Selling and marketing expenses were broadly unchanged at US$15.7 million in Q1 2017 compared with US$15.4 million in Q1 2016. We further increased our sales and marketing efforts in our Connectivity segment, but maintained tight control over our overall costs.

Underlying selling and marketing expenses were also broadly unchanged at US$12.9 million in Q1 2017 compared with US$12.5 million in Q1 2016, and were lower as a percentage of the Group's revenue at 4.7% in Q1 2017 compared with 5.2% in Q1 2016.

Underlying selling and marketing expenses exclude share-based compensation expenses and related payroll costs totaling US$1.0 million (Q1 2016: US$1.0 million) and additional amortisation of US$1.8 million (Q1 2016: US$1.9 million) on the fair value uplift of acquired intangible assets.

General and administrative expenses were lower at US$16.9 million in Q1 2017 compared with US$21.0 million in Q1 2016.

General and administrative expenses in Q1 2016 included Atmel related transaction costs of US$3.6 million. Excluding these costs, general and administrative expenses were broadly unchanged in Q1 2017 compared with Q1 2016.

Underlying general and administrative expenses additionally exclude share-based compensation and related payroll costs totaling US$4.2 million (Q1 2016: US$3.5 million).

Underlying general and administrative expenses were US$12.7 million in Q1 2017 compared with US$14.0 million in Q1 2016, a reduction of 9%, and were also lower as a percentage of the Group's revenue at 4.7% in Q1 2017 compared with 5.8% in Q1 2016.

R&D expenses were US$60.9 million in Q1 2017 compared with US$57.5 million in Q1 2016, an increase of 6%. R&D expenditure was US$68.8 million in Q1 2017 (Q1 2016: US$64.3 million), of which US$6.2 million (Q1 2016: US$5.7 million) was capitalised, and we recognised R&D expenditure credits of US$1.7 million (Q1 2016: US$1.1 million).

Underlying R&D expenses were US$56.2 million in Q1 2017 compared with US$53.8 million in Q1 2016, an increase of 5%, but were lower as a percentage of the Group's revenue at 20.7% in Q1 2017 compared with 22.3% in Q1 2016.

Underlying R&D expenses exclude share-based compensation expenses and related payroll costs totaling US$4.7 million (Q1 2016: US$3.7 million).

Other operating income was less than US$0.1 million in Q1 2017 compared with US$0.2 million in Q1 2016 (excluding the Atmel termination fee of US$137.3 million).

Operating profit was US$29.1 million in Q1 2017 compared with US$151.2 million in Q1 2016. Excluding the Atmel termination fee and related transaction costs, operating profit was US$17.5 million in Q1 2016.

Underlying operating profit was higher at US$43.2 million in Q1 2017 compared with US$29.9 million in Q1 2016, with the effect of higher sales volumes being only marginally offset by the increase in underlying operating expenses. Underlying operating margin was 350 basis points higher at 15.9% in Q1 2017 compared with 12.4% in Q1 2016.

Interest income was US$1.5 million in Q1 2017 compared with US$0.8 million in Q1 2016, reflecting an increase in market interest rates and higher cash balances.

Interest expense was US$0.1 million in Q1 2017 compared with US$2.3 million in Q1 2016.

Excluding the Atmel commitment fees of US$1.9 million incurred in Q1 2016, the interest expense was broadly unchanged in Q1 2017 compared with Q1 2016.

Other finance expense was US$1.1 million in Q1 2017 compared with US$2.7 million in Q1 2016.

Other finance income (expense) comprises foreign currency translation gains and losses that arise on monetary assets and liabilities that are denominated in currencies other than the functional currencies of the entities by which they are held and fair value gains and losses recognised in relation to certain of our strategic investments.

We recognised a net currency translation loss of US$0.1million in Q1 2017 compared with a net loss of US$2.7 million in Q1 2016.

During Q1 2017, we recognised a loss of US$0.8 million on the decline in the fair value of the warrants that we hold over shares in Energous Corporation and an impairment loss of US$0.2 million in relation to the shares we held in Arctic Sand.

Income tax expense was US$6.2 million (Q1 2016: US$4.0 million) on profit before tax of US$29.3 million (Q1 2016: US$146.9 million), an effective tax rate for the period of 21.2% (Q1 2016: 2.7%).

Our income tax expense for the first quarter is calculated by applying the expected effective tax rate for the full year to the profit before tax for the quarter after adjusting for specific items that distort the tax rate including, in Q1 2016, the Atmel termination fee of US$137.3 million. Having obtained tax advice, we consider that the termination fee is not taxable in the UK.

Our underlying income tax expense was US$10.1 million (Q1 2016: US$6.1 million) on underlying profit before tax of US$44.5 million (Q1 2016: US$27.7 million). Our underlying effective tax rate for Q1 2017 was therefore 22.7%, which compares with 24.0% for FY 2016.

The reduction in our underlying effective tax rate is a result of the ongoing exercise to realign the ownership of the Group's Intellectual Property, which is the subject of an application for a Bilateral Advance Pricing Agreement. Our income tax expense for Q1 2017 reflects our expectation of the likely final agreement.

Net income was US$23.1 million (Q1 2016: US$142.9 million), of which a loss of US$0.2 million (Q1 2016: US$0.8 million) was attributable to the non-controlling interest in Dyna Image. Underlying net income was US$34.4 million compared with US$21.6 million in Q1 2016, an increase of 59%.

Basic earnings per share were US$0.31 (Q1 2016: US$1.89) based on the weighted average of 75.3 million shares (Q1 2016: 76.1 million shares) that were in issue during the period excluding 3.2 million shares (Q1 2016: 1.7 million shares) held by employee benefit trusts and, in Q1 2017, 2.3 million of our own shares held in treasury. Underlying basic earnings per share were US$0.46 (Q1 2016: US$0.29).

Diluted earnings per share were US$0.29 (Q1 2016: US$1.80). Diluted earnings per share additionally reflect the weighted average of 3.9 million (Q1 2016: 3.7 million) dilutive employee share options. Underlying diluted earnings per share were US$0.43 (Q1 2016: US$0.28).

Cash flows

Cash and cash equivalents increased by US$25.6 million during Q1 2017 (Q1 2016: increased by US$95.4 million).

Cash flow from operating activities was US$100.7 million in Q1 2017 compared with US$107.1 million in Q1 2016.

Cash generated from operations before changes in working capital was US$50.8 million in Q1 2017 compared with US$170.3 million in Q1 2016. Excluding the receipt of the Atmel termination fee cash generated

Financial review continued

Three months ended 31 March 2017

from operations before changes in working capital was US$33.0 million in Q1 2016.

Net working capital decreased by US$46.0 million (Q1 2016: increased by US$35.2 million).

Demand for our products is typically highest in the fourth quarter of the year and lower in the first quarter. During the first quarter, we typically see the settlement of receivables built up in the fourth quarter and a reduction in inventory and payables as we make lower purchases from our suppliers. Movements in working capital during Q1 2017 were broadly consistent with this pattern.

Trade and other receivables declined during Q1 2017, releasing cash of US$43.7 million. Gross receivables sold under our receivables financing facilities declined by US$6.2 million to stand at US$98.8 million at the end of Q1 2017 compared with US$105.0 million at the end of 2016. At the end of Q1 2017, trade and other receivables represented 12 days sales in the preceding quarter (end of 2016: 20 days sales).

Inventory levels were reduced during Q1 2017, releasing cash of US$16.9 million. At the end of Q1 2017, inventories represented 54 days cost of sales in the preceding quarter (end of 2016: 48 days cost of sales).

Trade and other payables declined during Q1 2017, absorbing cash of US$18.5 million, principally as a consequence of lower quantity of materials purchased in Q1 2017 compared with Q4 2016.

Changes in other assets and liabilities had the effect of releasing cash of US$5.9 million during Q1 2017.

Interest paid was less than US$0.1 million in Q1 2017 compared with US$2.2 million in Q1 2016. Excluding the payment of commitment fees in relation to the Atmel borrowing facility of US$1.9 million, interest paid in Q1 2016 was US$0.3 million. Interest received was US$1.5 million in Q1 2017 compared with US$0.6 million in Q1 2016.

Net income tax receipts amounted to US$2.4 million in Q1 2017 compared with net tax payments of US$26.4 million in Q1 2016. 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. During Q1 2017, we received US$21.2 million in respect of income taxes overpaid in respect of earlier years.

Summary cash flow statement

US$ millions	Q1 2017	Q1 2016
Cash generated from operations	**96.8**	135.1
Interest received/(paid), net	**1.5**	(1.6)
Income taxes received/(paid)	**2.4**	(26.4)
Cash flow from operating activities	**100.7**	107.1
Purchase of property, plant and equipment	**(6.9)**	(5.7)
Purchase of intangible assets	**(1.7)**	(2.5)
Capitalised development expenditure	**(6.2)**	(5.7)
Purchase of own shares into treasury	**(41.6)**	–
(Purchase)/sale of Dialog shares by EBTs, net	**(19.7)**	1.9
Other cash flows, net	**0.9**	–
Net cash inflow during the period	**25.5**	95.1
Currency translation differences	**0.1**	0.3
Increase in cash and cash equivalents	**25.6**	95.4

Cash flow used for investing activities was US$15.5 million in Q1 2017 compared with US$13.9 million in Q1 2016.

Cash outflows in relation to the purchase of property, plant and equipment and intangible assets and capitalised development expenditure totalled US$14.8 million in Q1 2017, broadly unchanged compared with US$13.9 million in Q1 2016.

Cash flow used for financing activities was US$59.6 million in Q1 2017 compared with a cash inflow from financing activities of US$1.9 million in Q1 2016, the substantial change being due to purchases made under the Company's share buyback programme and significant purchases of the Company's shares by employee benefit trusts to satisfy the exercise of share options awarded under employee share schemes.

During Q1 2017, we completed the second tranche of the share buyback programme, purchasing 977,456 of the Company's shares at a cost of US$41.6 million (including related transaction costs of US$0.2 million).

Also during Q1 2017, employee benefit trusts purchased 456,724 of the Company's shares in the market at a cost of US$24.3 million (Q1 2016: US$nil) and received proceeds of US$4.6 million (Q1 2016: US$1.9 million) on the exercise of share options.

Slightly offsetting these outflows during Q1 2017, we received the equivalent of US$1.1 million on the subscription for new shares in Dyna Image by one of its non-controlling shareholders.

Liquidity

At the end of Q1 2017, cash and cash equivalents amounted to US$722.8 million (end of 2016: US$697.2 million), which principally comprised short-term deposits with a maturity of three months or less.

We have no committed borrowing facilities, but utilise uncommitted non-recourse receivables financing facilities provided by two financial institutions in an aggregate amount of US$240 million. At the end of Q1 2017, cash and cash equivalents included US$84.5 million (end of 2016: US$88.9 million) in relation to receivables sold under these facilities.

We are confident that the receivables financing facilities together with our significant cash balances and cash generation will be more than sufficient to satisfy the Group's working capital requirements in the near to medium term.

Share buyback programme

Second and third tranches

We completed the first intermediate settlement under the second tranche of the share buyback programme on 30 December 2016. We made a further intermediate settlement of the second tranche on 9 February 2017 and final settlement and conclusion of the tranche took place on 17 February 2017.

We purchased 1,451,048 shares in total under the second tranche at a cost of €56.25 million (US$59.8 million) and incurred transaction costs of US$0.4 million.

On 27 February 2017, the Company announced details of the third tranche of the share buyback programme under which it committed to purchase shares with a minimum cost of €56.25 million and a maximum cost of €75.0 million.

At the end of Q1 2017, we had not purchased any shares from the broker in relation to the third tranche and recognised a debit to retained earnings amounting to US$80.5 million, which comprised the maximum obligation to purchase shares under the third tranche of €75.0 million (US$80.1million) and related transaction costs of US$0.4 million.

On 25 April 2017, we completed the first intermediate settlement under the third tranche, purchasing 650,000 shares at an initial cost of €31.4 million (US$34.1 million).

Under the first three tranches of the share buyback programme, we have so far purchased 3,433,206 shares into treasury representing 4.2% of the Company's issued share capital at a cost of US$137.4 million (including transaction costs of US$1.5 million).

Renewal of authority

At the Company's AGM on 4 May 2017, the Directors were granted the authority to purchase up to a further 7,808,280 ordinary shares in the capital of the Company, representing approximately 10% of the issued ordinary share capital of the Company (excluding treasury shares) as at 27 March 2017.

Such authority shall (unless previously renewed, varied or revoked) expire on the day before the next AGM of the Company or on 30 June 2018, whichever is the earlier. Purchases made under the renewed authority will be off-market from the perspective of the Company and will be effected by way of contingent forward purchase contracts entered into with Barclays, Goldman Sachs, HSBC or Merrill Lynch acting as brokers.

Balance sheet

Non-current assets totalled US$493.2 million at the end of Q1 2017, broadly unchanged compared with US$496.2 million at the end of 2016.

Current assets totalled US$894.1 million at the end of Q1 2017 (end of 2016: US$934.3 million), a decrease of US$40.2 million. Cash and cash equivalents increased by US$25.6 million to US$722.8 million. Other current assets decreased by US$65.9 million to US$171.2 million, principally due to decreases of US$43.7 million in trade and other receivables and US$16.1 million in inventories.

Current liabilities totalled US$221.0 million at the end of Q1 2017, broadly unchanged compared with US$224.1 million at the end of 2016. Trade and other payables decreased by US$18.5 million to US$71.1 million but this was partially offset by the increase of US$10.6 million in other current financial liabilities to US$88.6 million which largely reflected the higher share buyback obligation.

Non-current liabilities totalled US$10.0 million at the end of Q1 2017 (end of 2016: US$11.6 million).

Total equity was US$1,156.3 million at the end of Q1 2017 (end of 2016: US$1,194.9 million), comprised of shareholders' equity of US$1,150.6 million (end of 2016: US$1,189.8 million) and non-controlling interests in Dyna Image of US$5.7 million (end of 2016: US$5.1 million). At the end of Q1 2017, Dialog shares held by employee benefit trusts amounted to US$15.1 million (end of 2016: US$20.6 million) and own shares held in treasury amounted to US$103.1 million (end of 2016: US$61.5 million).

Consequences of Brexit

On 29 March 2017, the UK Government invoked Article 50 of the Lisbon Treaty and it is therefore now expected that the UK will leave the EU on or before 29 March 2019.

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 two-thirds 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 any likely consequential changes to the rights of UK nationals to work in the EU.

While the Brexit negotiations are ongoing, we will operate on a business as usual basis within the existing regulations and our continuing focus will be on growing our business.

Other information

Members of the Management Team and the Board of Directors

Management Team

Dr Jalal Bagherli, Chief Executive Officer; Vivek Bhan, Senior Vice President, Engineering; Christophe Chene, Senior Vice President, Asia; Mohamed Djadoudi, Senior Vice President, Global Manufacturing Operations and Quality; Wissam Jabre, CFO, Senior Vice President Finance; Udo Kratz, Senior Vice President and General Manager, Mobile Systems Business Group; Davin Lee, Senior Vice President and General Manager Power Conversion Business Group; Sean McGrath, Senior Vice President and General Manager, Connectivity, Automotive and Industrial Business Group; Julie Pope, Senior Vice President, Human Resources (from 2 May 2017); Martin Powell, Senior Vice President, Human Resources (retires on 31 May 2017); Tom Sandoval, Senior Vice President, Worldwide Sales; Colin Sturt, Senior Vice President, General Counsel; Mark Tyndall, Senior Vice President, Corporate Development and Strategy and General Manager Emerging Products Business Group.

Board of Directors

Rich Beyer, Chairman; Dr Jalal Bagherli, Chief Executive Officer; Chris Burke; Alan Campbell; Mike Cannon; Mary Chan; Aidan Hughes; Eamonn O'Hare; Nick Jeffrey; Russ Shaw (until 4 May 2017).

Going concern

After making enquiries, the Directors have formed a judgement at the time of approving the interim financial statements that there is a reasonable expectation that the Group has adequate resources to continue for the foreseeable future. As at 31 March 2017, the Group had no outstanding borrowings and held US$722.8 million of cash and cash equivalents. (including US$84.5 million from receivables sold under its receivables financing facilities). The Group has profitable forecasts and longer-term plans. For these reasons, the Directors have adopted the going concern basis in preparing the interim financial statements for the three-month period ended 31 March 2017.

Principal risks and uncertainties

We describe the principal risks and uncertainties that could have a material adverse effect on the achievement of Dialog's three-year mid-range strategy on pages 52 to 56 of our Annual Report and Accounts 2016. In the opinion of the Directors, there has been no change in the principal risks and uncertainties affecting Dialog since the approval of the Annual Report and Accounts 2016.

Responsibility statement

We confirm that, to the best of our knowledge, the interim financial statements for the three-month period ended 31 March 2017 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 three-month period ended 31 March 2017, 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 2017.

9 May 2017

Dr Jalal Bagherli	Wissam Jabre
CEO	CFO, Senior Vice President, Finance

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 months ended 31 March 2017 which comprises the condensed consolidated statement of income, the condensed consolidated statement of comprehensive income, the condensed consolidated balance sheet, the condensed consolidated statements of cash flows, the condensed consolidated statement of changes in equity and the related notes 1 to 16. 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 Auditing Practices Board. 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 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 International Accounting Standard 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 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 Ireland) 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 in the interim report for the three months ended 31 March 2017 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority and the disclosure requirements of the German Securities Trading Act (WpHG).

Deloitte LLP

Chartered Accountants and Statutory Auditor

Reading, UK

9 May 2017

Condensed consolidated statement of income

For the three months ended 31 March 2017

	Notes	Three months ended 31 March 2017 US$000 (Unaudited)	Three months ended 1 April 2016 US$000 (Unaudited)
Revenue	4	**270,974**	241,408
Cost of sales		**(148,328)**	(133,747)
Gross profit		**122,646**	107,661
Selling and marketing expenses		**(15,743)**	(15,415)
General and administrative expenses		**(16,859)**	(21,015)
Research and development expenses		**(60,951)**	(57,524)
Other operating income		**–**	137,478
Operating profit	4	**29,093**	151,185
Interest income		**1,480**	756
Interest expense		**(120)**	(2,332)
Other finance income/(expense)		**(1,114)**	(2,703)
Profit before income taxes		**29,339**	146,906
Income tax expense		**(6,220)**	(4,015)
Net income		**23,119**	142,891
Attributable to:			
– Shareholders in the Company		**23,284**	143,736
– Non-controlling interests		**(165)**	(845)
Net income		**23,119**	142,891

Earnings per share (in US$)	5		
Basic		**0.31**	1.89
Diluted		**0.29**	1.80
Weighted average number of shares (in thousands)	5		
Basic		**75,340**	76,148
Diluted		**79,194**	79,831

Condensed consolidated statement of comprehensive income

For the three months ended 31 March 2017

	Three months ended 31 March 2017 US$000 (Unaudited)	Three months ended 1 April 2016 US$000 (Unaudited)
Net income	**23,119**	142,891
Other comprehensive income		
Items that may be reclassified to profit or loss in subsequent periods		
Currency translation differences on foreign operations	**1,063**	790
Income tax relating to currency translation differences on foreign operations	**66**	26
Fair value loss on available-for-sale investments	**(970)**	–
Income tax relating to available-for-sale investments	**165**	–
Cash flow hedges:		
– Fair value gain recognised on effective hedges in the period	**1,929**	3,328
– Fair value loss transferred to profit or loss	**3,444**	2,595
Income tax relating to cash flow hedges	**(1,105)**	(1,383)
Other comprehensive income for the period	**4,592**	5,356
Total comprehensive income for the period	**27,711**	148,247
Attributable to:		
– Shareholders in the Company	**27,883**	149,004
– Non-controlling interests	**(172)**	(757)
Total comprehensive income for the period	**27,711**	148,247

Condensed consolidated balance sheet

As at 31 March 2017

	Notes	As at 31 March 2017 US$000 (Unaudited)	As at 31 December 2016 US$000 (Audited)
Assets			
Cash and cash equivalents		**722,808**	697,167
Trade and other receivables		**37,064**	80,773
Other current financial assets		**989**	–
Inventories	6	**89,221**	105,303
Income tax receivables		**27,253**	35,878
Other current assets		**15,453**	15,211
Assets held for sale	10	**1,267**	–
Total current assets		**894,055**	934,332
Goodwill	7	**251,619**	251,208
Other intangible assets	7	**122,339**	125,619
Property, plant and equipment	8	**68,721**	69,668
Non-current financial assets	9	**19,892**	22,332
Deferred tax assets		**30,647**	27,379
Total non-current assets		**493,218**	496,206
Total assets		**1,387,273**	1,430,538
Liabilities and equity			
Trade and other payables		**71,125**	89,645
Other current financial liabilities		**88,558**	77,978
Provisions		**1,491**	1,477
Income taxes payable		**450**	528
Other current liabilities		**59,355**	54,444
Total current liabilities		**220,979**	224,072
Provisions		**2,606**	3,370
Deferred tax liabilities		**1,969**	1,970
Other non-current liabilities		**5,465**	6,220
Total non-current liabilities		**10,040**	11,560
Ordinary shares		**14,775**	14,402
Share premium account		**403,687**	403,687
Retained earnings		**854,825**	862,914
Other reserves		**(107,622)**	(70,566)
Dialog shares held by employee benefit trusts		**(15,062)**	(20,608)
Equity attributable to shareholders in the Company		**1,150,603**	1,189,829
Non-controlling interests		**5,651**	5,077
Total equity		**1,156,254**	1,194,906
Total liabilities and equity		**1,387,273**	1,430,538

Condensed consolidated statement of cash flows

For the three months ended 31 March 2017

	Three months ended 31 March 2017 US$000 (Unaudited)	Three months ended 1 April 2016 US$000 (Unaudited)
Cash flows from operating activities		
Net income	23,119	142,891
Non-cash items within net income:		
– Depreciation of property, plant and equipment	7,414	6,434
– Amortisation of intangible assets	10,419	8,045
– Release of inventory reserve, net	(850)	(6)
– Share-based compensation expense	8,879	7,074
– Other non-cash items	(3,046)	267
Interest (income) expense, net	(1,360)	1,576
Income tax expense	6,220	4,015
Cash generated from operations before changes in working capital	50,795	170,296
Changes in working capital:		
– Trade and other receivables	43,709	37,849
– Inventories	16,932	(18,504)
– Prepaid expenses	(1,250)	(2,756)
– Trade accounts payable	(18,520)	(49,531)
– Provisions	(757)	(791)
– Other assets and liabilities	5,918	(1,486)
Cash generated from operations	96,827	135,077
Interest paid	(25)	(2,157)
Interest received	1,480	551
Income taxes received/(paid)	2,371	(26,394)
Cash flow from operating activities	100,653	107,077
Cash flows from investing activities		
Purchase of property, plant and equipment	(6,899)	(5,668)
Purchase of intangible assets	(1,690)	(2,480)
Payments for capitalised development costs	(6,212)	(5,741)
Change in other long term assets	(750)	25
Cash flow used for investing activities	(15,551)	(13,864)
Cash flows from financing activities		
Purchase of Dialog shares by employee benefit trusts	(24,301)	–
Sale of Dialog shares by employee benefit trusts	4,621	1,918
Purchase of own shares into treasury	(41,642)	–
Issue of shares by a subsidiary to non-controlling interests	1,107	–
Currency hedges on share buyback obligation	579	–
Cash flow used for financing activities	(59,636)	1,918
Net increase in cash and cash equivalents	25,466	95,131
Cash and cash equivalents at beginning of period	697,167	566,809
Currency translation differences	175	295
Cash and cash equivalents at end of period	722,808	662,235

Condensed consolidated statement of changes in equity

For the three months ended 31 March 2017

	Ordinary shares US$000	Share premium account* US$000	Retained earnings* US$000	Other reserves* (note 14) US$000	Dialog shares held by employee benefit trusts US$000	Equity attributable to shareholders in the Company US$000	Non-controlling interests US$000	Total US$000
Three months ended 1 April 2016 (Unaudited)								
As at 1 January 2016 – reclassified	14,402	403,687	631,548	(7,923)	(24,630)	1,017,084	7,801	1,024,885
Net income/(loss)	–	–	143,736	–	–	143,736	(845)	142,891
Other comprehensive income	–	–	–	5,268	–	5,268	88	5,356
Total comprehensive income (loss)	–	–	143,736	5,268	–	149,004	(757)	148,247
Other changes in equity:								
– Sale of shares by employee benefit trusts	–	–	687	–	1,231	1,918	–	1,918
– Share-based compensation, net of tax	–	–	9,153	–	–	9,153	–	9,153
As at 1 April 2016	14,402	403,687	785,124	(2,655)	(23,399)	1,177,159	7,044	1,184,203
Three months ended 31 March 2017 (Unaudited)								
As at 1 January 2017	**14,402**	**403,687**	**862,914**	**(70,566)**	**(20,608)**	**1,189,829**	**5,077**	**1,194,906**
Net income/(loss)	**–**	**–**	**23,284**	**–**	**–**	**23,284**	**(165)**	**23,119**
Other comprehensive income (loss)	**–**	**–**	**–**	**4,599**	**–**	**4,599**	**(7)**	**4,592**
Total comprehensive income (loss)	**–**	**–**	**23,284**	**4,599**	**–**	**27,883**	**(172)**	**27,711**
Other changes in equity:								
– Shares issued to employee benefit trusts	**373**	**–**	**–**	**–**	**(373)**	**–**	**–**	**–**
– Purchase of own shares into treasury	**–**	**–**	**(912)**	**(41,655)**	**–**	**(42,567)**	**–**	**(42,567)**
– Share buyback obligation	**–**	**–**	**(16,829)**	**–**	**–**	**(16,829)**	**–**	**(16,829)**
– Shares issued by a subsidiary	**–**	**–**	**361**	**–**	**–**	**361**	**746**	**1,107**
– Purchase of shares by employee benefit trusts	**–**	**–**	**–**	**–**	**(24,301)**	**(24,301)**	**–**	**(24,301)**
– Sale of shares by employee benefit trusts	**–**	**–**	**(25,599)**	**–**	**30,220**	**4,621**	**–**	**4,621**
– Share-based compensation, net of tax	**–**	**–**	**11,606**	**–**	**–**	**11,606**	**–**	**11,606**
As at 31 March 2017	**14,775**	**403,687**	**854,825**	**(107,622)**	**(15,062)**	**1,150,603**	**5,651**	**1,156,254**

* Comparative amounts reclassified – see note 14.

Notes to the condensed financial statements

For the three months ended 31 March 2017

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 (Regulated Market, Prime Standard, FWB:DLG, ISIS GB0059822006) and it is a member of the TecDax index, which tracks the performance of the largest technology companies 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. Dialog has four operating segments: Mobile Systems; Automotive & Industrial; Connectivity; and Power Conversion. Segment information is presented in note 4.

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 14 to 32 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).

Review and approval of the interim financial statements

The interim financial statements are unaudited, but have been reviewed by the Company's auditors, Deloitte LLP, whose report can be found on page 13. 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 2016 have been delivered to the Registrar of Companies in England and Wales. The auditors' 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 9 May 2017.

Basis of preparation

The interim financial statements are for the three months ended 31 March 2017 ("Q1 2017") with comparative information for the three months ended 1 April 2016 ("Q1 2016").

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.

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.

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. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Information about assets and liabilities that are measured at fair value is presented in note 11.

The Group's significant accounting policies are unchanged compared with the year ended 31 December 2016.

During 2017, subject to its endorsement for use in the European Union, the Group will adopt Amendments to IAS 7 *Statement of Cash Flows* (issued January 2016) that will introduce new disclosures in the Group's annual financial statements in relation to changes in liabilities arising from financing activities.

Assets held for sale

Non-current assets are classified as held for sale if it is expected that their carrying amount will be recovered by sale rather than from continuing use. For this to be the case, the asset must be available for immediate sale in its current condition and the sale must be expected to be completed within 12 months.

Presentation currency

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

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

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 Mobile Systems 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 have not yet adopted the following new or amended accounting standards that have been issued by the IASB and are relevant to Dialog:

- IFRS 9 *Financial Instruments*
- IFRS 15 *Revenue from Contracts with Customers*
- IFRS 16 *Leases*
- Amendments to IFRS 2 *Classification and Measurement of Share-based Payment Transactions*

We outlined these changes in note 1 to our consolidated financial statements for the year ended 31 December 2016. We have not yet completed our evaluation of the financial effect of these pronouncements.

2. Additional investment in Dyna Image

In January 2017, the Group participated in a new issue of shares by its subsidiary, Dyna Image Corporation. We invested the equivalent of US$1,893. As a result of the share issue, our shareholding in Dyna Image increased from 45.7% to 48.5%. We reflected the increase in our shareholding as a transfer of US$361 within equity from non-controlling interests to retained earnings.

We continue to hold a call option over the shares in Dyna Image that we do not already own that expires in June 2018.

3. Aborted merger with Atmel

In January 2016, Atmel Corporation Inc. ('Atmel') terminated the merger agreement that existed with Dialog. Under the terms of the agreement, Atmel paid us a termination fee of US$137,300. We recognised the termination fee as other operating income during Q1 2016.

Also during Q1 2016, we incurred residual transaction costs of US$3,606 (recognised within general and administrative expenses) and commitment fees of US$1,913 on the borrowing facility that was arranged to finance the transaction prior to the cancellation of the facility in January 2016 (recognised within interest expense).

4. Segment information

a) Analysis by operating segment

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 performance of the Group's businesses. Members of the Management Team during Q1 2017 are identified on page 12.

The Group's reportable segments are determined based on the nature of the products that they provide to our customers and are as follows: Mobile Systems; Automotive & Industrial; Connectivity; and Power Conversion.

→ Mobile Systems provides power management and audio chips designed to meet the needs of the wireless systems markets and a range of advanced driver technologies for low power display applications – from PMOLEDs to electronic paper and MEMS displays.

→ Automotive & Industrial's products address the safety, management and control of electronic systems in cars and for industrial applications.

→ Connectivity's products include short-range wireless, digital cordless, Bluetooth® and VoIP technology.

→ Power Conversion's products include AC/DC converter solutions for smaller, fast charging power adaptors for portable devices as well as LED drivers for solid-state lighting products.

No operating segments have been aggregated in determining our reportable segments. Each operating segment has a manager who is responsible for its performance and is accountable to the Chief Executive Officer.

The Management Team uses operating profit as the principal measure of the profitability of each of the Group's operating segments. Operating profit is, therefore, the measure of segment profit presented in the Group's segment disclosures. Whilst the Management Team also uses underlying operating profit to measure segment profitability, this is used as a supplement to operating profit.

In addition to our reportable segments, we present information for Corporate activities. Corporate activities do not meet the definition of an operating segment. Corporate activities include emerging market businesses (comprising Dyna Image and those developing low cost PMICs for the Chinese consumer market), together with central corporate costs, the share-based compensation expense and certain other unallocated costs. During Q1 2016, Corporate activities also included the termination fee of US$137,300 that was paid to us by Atmel.

Revenue and operating profit by segments are as follows:

	Revenue[1]		Operating profit	
	Three months ended 31 March 2017 US$000	Three months ended 1 April 2016 US$000	**Three months ended 31 March 2017 US$000**	Three months ended 1 April 2016 US$000
Mobile Systems	**204,451**	187,837	**46,178**	39,843
Automotive & Industrial	**7,967**	7,140	**3,045**	2,654
Connectivity	**26,578**	20,613	**657**	(3,363)
Power Conversion	**29,314**	23,957	**(1,812)**	(6,306)
Total segments	**268,310**	239,547	**48,068**	32,828
Corporate activities	**2,664**	1,861	**(18,975)**	118,357
Total Group	**270,974**	241,408	**29,093**	151,185
Interest income			**1,480**	756
Interest expense			**(120)**	(2,332)
Other finance income (expense)			**(1,114)**	(2,703)
Profit before income taxes			**29,339**	146,906

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

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

4. Segment information continued

b) Geographic information

	Three months ended 31 March 2017 US$000	Three months ended 1 April 2016 US$000
Revenue by shipment destination		
United Kingdom	**56**	154
Other European countries	**10,761**	10,633
China	**199,760**	180,752
Hong Kong	**43,695**	39,746
Other Asian countries	**13,037**	7,355
Rest of the world	**3,665**	2,768
Total	**270,974**	241,408

	As at 31 March 2017 US$000	As at 31 December 2016 US$000
Non-current assets[1] by location		
United Kingdom	**97,468**	96,876
Germany	**44,053**	44,992
Netherlands	**50,886**	49,960
USA	**230,254**	236,075
Taiwan	**13,704**	13,146
Rest of the world	**6,314**	5,446
Total	**442,679**	446,495

1 Non-current assets excluding financial instruments and deferred tax assets.

5. Earnings per share

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

Diluted earnings per share amounts are calculated by dividing the net profit attributable to ordinary shareholders of Dialog 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:

		Three months ended 31 March 2017 US$000	Three months ended 1 April 2016 US$000
Profit attributable to shareholders in the Company			
For calculating basic and diluted earnings per share	a	**23,284**	143,736
		Number	Number
Weighted average number of ordinary shares			
Shares in issue		**80,865,955**	77,865,955
Deduct:			
– Shares held in treasury		**(2,325,382)**	(1,717,531)
– Shares held by employee benefit trusts		**(3,200,735)**	–
For calculating basic earnings per share	b	**75,339,838**	76,148,424
Add:			
– Dilutive share options and awards		**3,853,908**	3,682,904
For calculating diluted earnings per share	c	**79,193,746**	79,831,328
		US$	US$
Basic EPS	a/b	**0.31**	1.89
Diluted EPS	a/c	**0.29**	1.80

During Q1 2017, the average number of anti-dilutive share options outstanding was 405,782 (Q1 2016: 446,559).

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

6. Inventories

Inventories were as follows:

	As at 31 March 2017 US$000	As at 31 December 2016 US$000
Raw materials	**10,370**	12,334
Work-in-process	**26,966**	29,337
Finished goods	**51,885**	63,632
Total	**89,221**	105,303

7. Goodwill and other intangible assets

Movements on goodwill and other intangible assets during Q1 2017 were as follows:

	Goodwill US$000	**Other intangible assets US$000**
Net book value		
As at 1 January 2017	**251,208**	**125,619**
Effect of movements in foreign currency	**411**	**240**
Additions	**–**	**7,054**
Amortisation charge for the period	**–**	**(10,419)**
Disposals	**–**	**(155)**
As at 31 March 2017	**251,619**	**122,339**

At the end of Q1 2017, the Group had contractual commitments for the acquisition of intangible assets of US$1,301 (end of 2016: US$922).

8. Property, plant and equipment

Movements on property, plant and equipment during Q1 2017 were as follows:

	US$000
Net book value	
As at 1 January 2017	**69,668**
Effect of movements in foreign currency	**276**
Additions	**6,351**
Depreciation charge for the period	**(7,414)**
Disposals	**(160)**
As at 31 March 2017	**68,721**

At the end of Q1 2017, the Group had contractual commitments for the acquisition of property, plant and equipment of US$25,571 (end of 2016: US$8,332).

9. Non-current financial assets

Non-current financial assets were as follows:

	As at 31 March 2017 US$000	As at 31 December 2016 US$000
Available-for-sale investments:		
– Shares in Energous Corporation	**11,896**	12,866
– Shares in Arctic Sand Technologies, Inc. (see note 10)	–	1,446
Derivative financial instruments:		
– Warrants over shares in Energous Corporation	**5,830**	6,624
– Call option over shares in Dyna Image Corporation	**142**	142
Rental and other deposits	**2,024**	1,254
Total	**19,892**	22,332

Energous shares and warrants

Energous Corporation ("Energous") is the developer of WattUp®, a revolutionary wire-free charging technology that provides over-the-air power at a distance. In November 2016, Dialog entered into a strategic alliance with Energous whereby it agreed to become the exclusive component supplier of the WattUp® integrated circuits. At the same time as entering into the strategic alliance, the Company subscribed for 763,552 common shares in Energous and was granted warrants to purchase up to 763,552 common shares in Energous that are exercisable in full or in part on a cashless basis at any time between May 2017 and November 2019.

We have classified the shares in Energous held by the Company as available-for-sale. During Q1 2017, the fair value of the shares decreased to US$11,896 and the resulting loss of US$970 was recognised in other comprehensive income.

We initially recognised the warrants at their grant date fair value of US$4,695 and an equivalent deferred credit within non-current liabilities. We will amortise the deferred credit to profit or loss in relation to the royalties that may be payable by Dialog for the use of Energous's Intellectual Property over the initial seven-year term of the strategic alliance. Amortisation of the deferred credit has not yet commenced. As at 31 December 2016, the fair value of the warrants was US$6,624. During Q1 2017, the fair value of the warrants decreased to US$5,830 and the resulting loss of US$794 was recognised in profit or loss (as other finance expense).

10. Assets held for sale

On 15 March 2017, Peregrine Semiconductor Corporation, a subsidiary of Murata Manufacturing Co Ltd, agreed to acquire Arctic Sand Technologies, Inc. by way of a merger. Dialog held approximately 3.5% of the issued equity shares in Artic Sand. We previously classified the shares as available-for-sale but carried them at their cost of US$1,446 because we were unable to measure reliably their fair value.

As at 31 March 2017, we reclassified our shares in Arctic Sand as assets held for sale measured at the amount of US$1,267 that we received on 1 May 2017 following completion of the merger. During Q1 2017, we recognised the resulting impairment loss of US$179 in profit or loss (within other finance expense). In due course, Dialog may receive up to a further US$68 that is being held in escrow pending the finalisation of the completion balance sheet and any indemnification claims.

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

11. 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 31 March 2017 are analysed by class and category:

	Loans and receivables US$000	Available-for-sale investments US$000	At fair value through profit or loss US$000	Held in designated hedging relationships US$000	Liabilities at amortised cost US$000	Total carrying amount US$000	Fair value US$000
Financial assets							
Cash and cash equivalents	722,808	–	–	–	–	722,808	722,808
Trade and other receivables	37,064	–	–	–	–	37,064	37,064
Investments:							
– Energous shares	–	11,896	–	–	–	11,896	11,896
– Arctic Sand shares(1)	–	1,267	–	–	–	1,267	1,267
Derivative financial instruments:							
– Currency forwards and swaps(2)	–	–	–	989	–	989	989
– Energous warrants	–	–	5,830	–	–	5,830	5,830
– Dyna Image call option	–	–	142	–	–	142	142
Rental and other deposits	2,024	–	–	–	–	2,024	2,024
Other financial assets	2,024	13,163	5,972	989	–	22,148	
Total financial assets	761,896	13,163	5,972	989	–	782,020	

	Loans and receivables US$000	Available-for-sale investments US$000	At fair value through profit or loss US$000	Held in designated hedging relationships US$000	Liabilities at amortised cost US$000	Total carrying amount US$000	Fair value US$000
Financial liabilities							
Trade and other payables	–	–	–	–	(71,125)	(71,125)	(71,125)
Hire purchase and finance lease obligations	–	–	–	–	(4,456)	(4,456)	(4,456)
Derivative financial instruments:							
– Currency forwards and swaps(2)	–	–	–	(4,364)	–	(4,364)	(4,364)
Share buyback obligation	–	–	–	–	(80,508)	(80,508)	(80,508)
Other financial liabilities	–	–	–	(4,364)	(84,964)	(89,328)	
Total financial liabilities	–	–	–	(4,364)	(156,089)	(160,453)	

1 Arctic Sand shares are classified as assets held for sale (see note 10).

2 Currency forwards and swaps that are not in designated hedging relationships are held to hedge the currency translation exposure on the Euro-denominated share buyback liability (see note 13).

11. Additional disclosures on financial instruments continued

Fair value measurement

a) Financial instruments carried at fair value

We have not designated any financial instruments at fair value through profit or loss on initial recognition.

We measured the fair values of the strategic investments set out in note 9 using the following methods and assumptions:

- Energous shares (listed on NASDAQ) – measured at the quoted bid price at the close of business on the balance sheet date.
- Arctic Sand shares – measured at the amount that we received on the sale of the shares (see note 10).
- Energous warrants – measured using a Black Scholes valuation model based on the quoted bid price of Energous's common shares and other inputs such as implied share price volatility that is modelled based on historical price data for Energous's common shares.
- Dyna Image call option – measured using a Monte Carlo valuation model in which the most significant inputs are management's estimates of the future revenue and profitability of Dyna Image and share price volatility that is modelled based on historical price data for comparable listed securities.

We measure the fair value of currency forwards and swaps at 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 are carried at fair value 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

	As at 31 March 2017			
	Level 1 US$000	Level 2 US$000	Level 3 US$000	Total US$000
Financial assets carried at fair value				
Investments:				
– Energous shares	11,896	–	–	11,896
– Arctic Sand shares[1]	–	–	1,267	1,267
Derivative financial instruments:				
– Currency forwards and swaps	–	989	–	989
– Energous warrants	–	–	5,830	5,830
– Dyna Image call option	–	–	142	142
Total financial assets carried at fair value	11,896	989	7,239	20,124
Financial liabilities carried at fair value				
Derivative financial instruments:				
– Currency forwards and swaps	–	(4,364)	–	(4,364)
Total financial liabilities carried at fair value	–	(4,364)	–	(4,364)

1 Arctic Sand shares are classified as assets held for sale (see note 10).

During Q1 2017, there were no transfers between Level 1 and Level 2.

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

11. Additional disclosures on financial instruments continued

In the following table, we present a reconciliation of the changes in the Level 3 fair values:

	Three months ended 31 March 2017 US$000	Three months ended 1 April 2016 US$000
At the beginning of the period	**6,766**	992
Transfer in of investment in Arctic Sand	**1,446**	–
Unrealised fair value losses recognised in profit or loss (other finance expense)		
– Arctic Sand shares	**(179)**	–
– Energous warrants	**(794)**	–
At the end of the period	**7,239**	992

We estimate that if the implied volatility of 78.6% incorporated in the valuation of the Energous warrants as at 31 March 2017 had been 10 percentage points higher, the fair value of the warrants would have been US$647 higher at US$6,477 and if the implied volatility had been 10 percentage points lower, the fair value of the warrants would have been US$687 lower at US$5,143. 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).

We do not consider that adjustment of one or more of the unobservable inputs to reflect reasonably possible alternative assumptions would be likely to cause a significant change in the fair value of the Dyna Image call option.

b) Financial instruments not carried at fair value

Hire purchase and finance lease obligations attract fixed interest rates that are implicit in the lease rentals. For disclosure purposes only, the fair value of these obligations has been calculated as the present value of the future contractual cash flows using observable yield curves (Level 2).

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

12. Share-based compensation

Development of plans

Stock option plan activity (including stock options granted under the LTIP and the EIP) during Q1 2017 was as follows:

	Options	Weighted average exercise price €
Outstanding at the beginning of the period	4,469,977	2.91
Granted	496,524	0.09
Exercised	(743,958)	5.54
Forfeited	(143,000)	0.09
Outstanding at the end of the period	**4,079,543**	**2.18**
Options exercisable at the end of the period	1,421,185	11.67

The Company established an employee benefit trust and a non-executive Director benefit trust (the "Trusts"). The Trusts purchase shares in the Company for the benefit of employees and non-executive Directors under the Group's share option schemes. As at 31 March 2017, the Trusts held 3,287,154 shares (31 December 2016: 574,600 shares).

13. Share buyback programme

Second tranche

On 8 November 2016, the Company announced details of the second tranche of the share buyback programme under which it committed to purchase shares with a minimum cost of €56.25 million and a maximum cost of €75.0 million.

On 30 December 2016, we completed the first intermediate settlement under the second tranche purchasing 473,592 shares at an initial cost of €17.45 million (US$18,383). As at 31 December 2016, we recognised a debit to equity amounting to US$63,077, which comprised the maximum remaining obligation to purchase shares under the second tranche of €57.55 million (US$62,759) and related transaction costs of US$318.

We made a further intermediate settlement of the second tranche on 9 February 2017 and final settlement and conclusion of the tranche took place on 17 February 2017. In these further settlements, we purchased 977,456 shares at a cost of €38.8 million (US$41,385) and incurred transaction costs amounting to US$270. On conclusion of the second tranche, we credited back to retained earnings the remainder of the liability to purchase shares initially recognised of US$20,061 (including transaction costs of US$100). During Q1 2017, we also showed a debit to retained earnings of US$912, which mirrored the gain recognised in profit or loss on the translation into US dollars of the Euro-denominated liability that existed in relation to shares that were purchased during the period.

Third tranche

On 27 February 2017, the Company announced details of the third tranche of the share buyback programme under which it committed to purchase shares with a minimum cost of €56.25 million and a maximum cost of €75.0 million. As at 31 March 2017, we had not purchased any shares from the broker and recognised a debit to retained earnings amounting to US$79,407, which comprised the maximum obligation to purchase shares of €75.0 million (US$79,012) and transaction costs of US$395.

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$275 in profit or loss in relation to liabilities to purchase shares under the second and third tranches during Q1 2017.

14. Share capital and reserves

Share capital and share premium

On 20 March 2017, the Company issued 3,000,000 of its £0.10 ordinary shares at par to its sponsored employee benefit trusts for the purpose of satisfying its obligations under its employee share schemes.

As at 31 March 2017, the Company had 80,865,955 ordinary shares in issue (31 December 2016: 77,865,955 ordinary shares), of which 2,783,206 ordinary shares (31 December 2016: 1,805,750 ordinary shares) were held in treasury.

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

14. Share capital and reserves continued

Reclassification of reserves

In preparing the Company's financial statements for the year ended 31 December 2016, the Directors decided to present the share premium account separately within reserves in order to show more clearly the Company's undistributable reserves. Previously, the share premium account was subsumed within additional paid-in capital, which also included gains recognised on the sale or transfer of shares held by employee benefit trusts and the equity component of the US$201 million 1% Convertible Bonds 2017 ("the Bonds") that were issued by the Company during 2012 and converted by the bondholders during 2015. As shown in the following table, comparative information for Q1 2016 has therefore been reclassified to reflect the following transfers from additional paid-in capital:

→ to transfer to the share premium account the cumulative premium (net of issue costs) recognised on the issue of shares prior to 1 January 2016 of US$390,194;

→ to transfer to retained earnings the cumulative gain of US$36,952 recognised on the sale or transfer of shares by employee benefit trusts prior to 1 January 2016 and the gain of US$687 on such sales or transfers during Q1 2016; and

→ on conversion of the Bonds during 2015, to transfer to retained earnings an amount of US$23,086 representing the cumulative interest expense recognised in relation to the Bonds and to transfer the balance of the equity component amounting to US$13,493 to the share premium account.

	Additional paid-in capital US$000	Share premium account US$000	Retained earnings US$000
As at 1 January 2016 – as previously stated	463,725	–	571,510
Reclassifications:			
– Premium on the issue of shares (net of issue costs)	(390,194)	390,194	–
– Gain on sale of shares by employee benefit trusts	(36,952)	–	36,952
– Equity component of Convertible Bonds	(36,579)	13,493	23,086
As at 1 January 2016 – reclassified	–	403,687	631,548
Three months ended 1 April 2016			
Movements – as previously stated	687	–	152,889
Reclassifications:			
– Gain on sale of shares by employee benefit trusts	(687)	–	687
As at 1 April 2016 – reclassified	–	403,687	785,124

14. Share capital and reserves continued

Other reserves

Movements on other reserves were as follows:

	Currency translation reserve US$000	Available-for-sale securities US$000	Hedging reserve US$000	Treasury shares US$000	Total US$000
Three months ended 1 April 2016					
As at 1 January 2016	(4,480)	–	(3,443)	–	(7,923)
Other comprehensive income (loss):					
– Currency translation differences on foreign operations	704	–	–	–	704
– Cash flow hedges:					
Fair value loss recognised on effective hedges in the period	–	–	3,328	–	3,328
Fair value loss transferred to profit or loss	–	–	2,595	–	2,595
– Income tax expense (credit)	24	–	(1,383)	–	(1,359)
As at 1 April 2016	(3,752)	–	1,097	–	(2,655)
Three months ended 31 March 2017					
As at 1 January 2017	**(4,400)**	**2,866**	**(7,560)**	**(61,472)**	**(70,566)**
Other comprehensive income (loss):					
– Currency translation differences on foreign operations	**1,070**	**–**	**–**	**–**	**1,070**
– Fair value loss on available-for-sale investments	**–**	**(970)**	**–**	**–**	**(970)**
– Cash flow hedges:					
Fair value loss recognised on effective hedges in the period	**–**	**–**	**1,929**	**–**	**1,929**
Fair value loss transferred to profit or loss	**–**	**–**	**3,444**	**–**	**3,444**
– Income tax expense (credit)	**66**	**165**	**(1,105)**	**–**	**(874)**
Other changes in equity :					
– Purchase of own shares into treasury	**–**	**–**	**–**	**(41,655)**	**(41,655)**
As at 31 March 2017	**(3,264)**	**2,061**	**(3,292)**	**(103,127)**	**(107,622)**

15. Transactions with related parties

Shares issued by Dyna Image

In January 2017, Lite-On Semiconductor Corp participated in a new issue of shares by Dyna Image Corporation. Dyna Image is an associate of Lite-On. Lite-On invested the equivalent of US$1,107, thereby increasing its shareholding in Dyna Image from 25.9% to 27.4%. Dialog's participation in the share issue is set out in note 2.

Key management personnel

The Group's key management personnel comprise the Management Team (which includes the Company's executive Director) and the Company's non-executive Directors, whose names are given on page 12. With the exception of their compensation, there were no transactions with key management personnel during Q1 2017. Compensation of key management personnel for the year ending 31 December 2017 will be disclosed in the 2017 Annual Report.

Notes to the condensed financial statements continued

For the three months ended 31 March 2017

16. Subsequent events

Sale of investment in Arctic Sand

On 1 May 2017, Dialog received US$1,267 in cash on completion of the sale of its investment in Arctic Sand Technologies, Inc.. Further information is presented in note 10.

Share buyback programme

On 25 April 2017, we completed the first intermediate settlement under the third tranche, purchasing 650,000 shares at an initial cost of €31.4 million (US$34,113).

At the Company's AGM on 4 May 2017, the Directors were granted the authority to purchase up to a further 7,808,280 ordinary shares in the capital of the Company, representing approximately 10% of the issued ordinary share capital of the Company (excluding treasury shares) as at 27 March 2017. Such authority shall (unless previously renewed, varied or revoked) expire on the day before the next AGM of the Company or on 30 June 2018, whichever is the earlier. Purchases made under the renewed authority will be off-market from the perspective of the Company and will be effected by way of contingent forward purchase contracts entered into with Barclays, Goldman Sachs, HSBC or Merrill Lynch acting as brokers.

Financial performance measures

Use of non-IFRS measures

Our use of non-IFRS measures is explained on pages 152 to 158 of our 2016 Annual Report.

Underlying measures of profitability 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 are not uniformly defined by all companies and therefore the non-IFRS measures used by Dialog may not be directly comparable with similarly-titled measures used by other companies.

Underlying measures of profitability

During the periods presented, we excluded from the underlying measures of profitability the following specific items of income and expense that were reported in accordance with IFRS:

- the share-based compensation expense and related payroll taxes;
- the amortisation of identifiable intangible assets that were recognised in business combinations;
- the termination fee received and the costs associated with the aborted merger with Atmel;
- the non-cash element of the interest expense recognised in relation to a patent licensing agreement that is accounted for as a finance lease within other intangible assets;
- the effect on profit or loss of changes in the fair value of strategic investments (including, in Q1 2017, the impairment loss recognised on our investment in Artic Sand Technologies, Inc.); 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 of profitability to equivalent IFRS measures

Reconciliations of the underlying measures of profitability used by Dialog to the equivalent IFRS measures for the three-month periods ended 31 March 2017 and 1 April 2016 are presented in the following tables:

Three months ended 31 March 2017

US$'000	IFRS basis	Share-based compensation and related payroll taxes	Amortisation of acquired intangible assets	Effective interest	Strategic investments	Underlying basis
Revenue	270,974	–	–	–	–	270,974
Cost of sales	(148,328)	536	1,768	–	–	(146,024)
Gross profit	**122,646**	**536**	**1,768**	**–**	**–**	**124,950**
Gross margin %	***45.3%***					***46.1%***
SG&A expenses	(32,602)	5,243	1,824	–	–	(25,535)
R&D expenses	(60,951)	4,737	–	–	–	(56,214)
Operating profit	**29,093**	**10,516**	**3,592**	**–**	**–**	**43,201**
Operating margin %	***10.7%***					***15.9%***
Net finance (income)/expense	246	–	–	95	973	1,314
Profit before income taxes	**29,339**	**10,516**	**3,592**	**95**	**973**	**44,515**
Income tax expense	(6,220)	(3,355)	(209)	(18)	(318)	(10,120)
Net income[1]	**23,119**	**7,161**	**3,383**	**77**	**655**	**34,395**
EBITDA[2]	n/a					57,442
EBITDA margin %	***n/a***					***21.2%***

Financial performance measures continued

Three months ended 1 April 2016

US$'000	IFRS basis	Share-based compensation and related payroll taxes	Amortisation of acquired intangible assets	Aborted merger with Atmel	Effective interest	Underlying basis
Revenue	241,408	–	–	–	–	241,408
Cost of sales	(133,747)	519	1,751	–	–	(131,477)
Gross profit	107,661	519	1,751	–	–	109,931
Gross margin %	*44.6%*					*45.5%*
SG&A expenses	(36,430)	4,513	1,900	3,606	–	(26,411)
R&D expenses	(57,524)	3,743	–	–	–	(53,781)
Other operating income	137,478	–	–	(137,300)	–	178
Operating profit	151,185	8,775	3,651	(133,694)	–	29,917
Operating margin %	*nm*					*12.4%*
Net finance expense	(4,279)	–	–	1,913	153	(2,213)
Profit before income taxes	146,906	8,775	3,651	(131,781)	153	27,704
Income tax expense	(4,015)	(1,451)	(215)	(383)	(31)	(6,095)
Net income[1]	142,891	7,324	3,436	(132,164)	122	21,609
EBITDA[2]	n/a					40,745
EBITDA margin %	*n/a*					*16.9%*

* Operating margin calculated on an IFRS basis did not give a meaningful portrayal of our trading performance in Q1 2016 because it included the Atmel termination fee of US$137,300.

Notes:

(1) Earnings per share

Earnings for calculating underlying basic and diluted EPS measures were as follows :

US$'000	**Q1 2017**	Q1 2016
Underlying measures		
Net income	**34,395**	21,609
Loss attributable to non-controlling interests	**(46)**	(717)
Earnings for calculating underlying basic and diluted EPS	**34,441**	22,326

(2) EBITDA

Underlying EBITDA may be reconciled to underlying net income as follows:

US$'000	Q1 2017	Q1 2016
Underlying measures		
Net income	**34,395**	21,609
Net finance expense	**(1,314)**	2,213
Income tax expense	**10,120**	6,095
Depreciation expense	**7,414**	6,434
Amortisation expense	**6,827**	4,394
EBITDA	**57,442**	40,745

Free cash flow

Free cash flow is a non-IFRS measure that represents cash flow from operating activities, less capital expenditure. Free cash flow is useful to investors because it provides a measure of the cash generated by our business that is available for expansion, to develop new products, to make strategic investments in, or acquire, other businesses and to fund share buybacks and other distributions to shareholders.

Free cash flow was calculated as follows:

US$'000	Q1 2017	Q1 2016
Cash flow from operating activities	**100,653**	107,077
Purchase of property, plant and equipment	**(6,899)**	(5,668)
Purchase of intangible assets	**(1,690)**	(2,480)
Payments for capitalised development costs	**(6,212)**	(5,741)
Free cash flow	**85,852**	93,188

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