



## Orc Software AB – Year-End Financial Report January 1 – December 31, 2003

- **Revenue for 2003 decreased by 9 percent to SEK 249 (275) million.**
- **Operating income for 2003 decreased by 36 percent to SEK 74 (115) million, giving an operating margin of 29.9 (41.6) percent. Income after taxes amounted to SEK 56 (87) million.**
- **Revenue for October-December 2003 amounted to SEK 62 (71) million with an operating income of SEK 16 (27) million, giving an operating margin of 24.9 (37.7) percent. Income after taxes amounted to SEK 12 (15) million.**
- **Earnings per share for 2003 amounted to SEK 3.78 (5.87).**
- **The Board of Directors recommends a dividend of SEK 3.40 (3.00) per share for 2003.**

### Markets

The first half of the year was characterized by a continued general review of costs among banks and brokerage houses and a consistently cautious approach to technology investments. Further consolidations were completed and less profitable participants left the market. Orc Software's clients traded on more geographical markets, but due to cost reasons they are localizing to fewer geographical sites. During the second half of the year, however, there was an increased activity and investment enthusiasm among the market's participants.

In Europe sales to clients increased especially in Germany and Austria, while sales development in the Nordic region remained weak. In Asia and Australia additional clients trade on a greater number of marketplaces, which presents interesting growth opportunities for Orc ExNet in particular.

The transition to electronic trading in the US is now a reality, which creates good growth opportunities for Orc Software who offers a system with access to many different marketplaces and the possibility of integrating the system with proprietary solutions. Among other things the planned launch of Eurex US in Chicago has placed a pressure on the other exchanges in Chicago to offer electronic solutions. Another clear example is the electronic options exchange ISE (International Securities Exchange) who after three years in business has attained larger trading

*Orc Software provides technology for advanced market making, trading and brokerage. Orc Software's system is used in 19 countries and allows users to access more than 70 markets. The company is listed at Stockholmsbörsen and has operations in Chicago, Frankfurt, Hong Kong, London, Milan, Moscow, New York, Stockholm, St Petersburg, Sydney, Tokyo, Toronto, Vienna and Zurich. In 2003, the company's total revenue amounted to SEK 249 million with an operating income of SEK 74 million.*

volumes in stock options than the traditional floor trading on the CBOE (Chicago Board Options Exchange).

During the fourth quarter Orc Software launched Orc Liquidator, which makes it possible for the users to pre-program their own trading strategies, which is then executed automatically. More and more of the market's most advanced participants are starting to realize that automatic trading is a prerequisite for success, and the launch of Orc Liquidator was received with great interest from the clients.

## **Future outlook**

Orc Software has a positive outlook for future market development, which is strengthened by increased activity and investment willingness among the market's participants. However, this is not estimated to have any significant financial impact in the short run, since the international market is still characterized by an obvious focus on costs with longer lead times as a result. During the upcoming quarters Orc Software will partly be affected by previously obtained client cancellations, and partly by an increasing influence from the weakening of the US dollar. In the long run, however, Orc Software expects an increase in demand and the company therefore believes that now is the right time for making further investments in development and sales. Some of these initiatives were already initiated during the last quarter of the year.

## **Significant events**

### **Setting up in Chicago**

During the fourth quarter 2003 Orc Software opened a sales and support office in Chicago focused on taking advantage of the market opportunities created by the increase in electronic trading in Chicago. Orc Software's technology makes it possible to trade on all the leading options and futures markets in Chicago.

### **Reuters alliance**

Following the formation of the Reuters/Orc alliance, Reuters launched the ROMEX (Reuters Order Management for Exchange Execution) product suite in Europe in Q1 2003. ROMEX is Reuters new trading tool based on Orc Software's technology and is targeted at sell side firms across Europe, particularly those with a need for efficient order execution. Reuters is also planning to offer the trading community an ASP (Application Service Provider) service for ROMEX, which will help reduce overall customer costs.

During 2003, the interest in the European market place was high and Reuters sold ROMEX to clients in Belgium, Denmark, France, Germany, Italy, The Netherlands, Spain and Sweden.

### **Orc ExNet**

During 2003 Orc ExNet added additional partners to its network. Agreements have been signed with Morgan Stanley and SEB Futures for trading on American and European exchanges as well as Capital Futures Corporation, a Taiwanese brokerage house, for trading on the Taiwanese markets. In addition, agreements have been signed with SEB Merchant Banking, which provides Orc Software's clients with the ability to trade currencies electronically in the Orc System via SEB. During the fourth quarter contracts were signed with among others Fimat Australia for trading on equities and derivatives exchanges in Asia and Australia.

As of December 31, 2003 Orc ExNet offered trading possibilities on 32 markets in Asia, Australia, Europe and North America, via its cooperation partners.

## **Market connections**

As of December 31, 2003, the Orc System was connected to 64 exchanges. Connections were established with the following 13 exchanges in 2003:

- Amsterdam Switch, The Netherlands
- Boston Options Exchange, US
- Chicago Board Options Exchange, US
- Chicago Board of Trade (e-cbot), US
- Chicago Mercantile Exchange, US
- Euronext.liffe, Belgium, France and UK
- Korea Stock Exchange, South Korea
- London Stock Exchange (SETS CW), UK
- MTS (Bonds), Europe
- Osaka Stock Exchange, Japan
- Quotrix, Germany
- Tokyo Stock Exchange (Cash), Japan
- Tokyo Stock Exchange (Derivatives), Japan

## **Product development**

Orc Software launched a number of new products during the year. The new products bring possibilities of both widening the usage of the Orc Technology for current clients as well as the ability to offer new clients a more complete product selection. Furthermore, clients can reduce their costs by limiting the number of system suppliers.

During the last two years Orc Software has dedicated significant resources to the development of the new advanced product, Orc Liquidator. This product, which is designed for the most advanced users, is a high performance, server based and automated trading platform. The Orc Liquidator's easily understood programming language allows the user to program their own trading strategies, according to which the system automatically monitors and executes transactions. The system detects price differences at speeds that cannot be attained through manual trading. This creates the possibility of making profits on the market's order flow and allows the user more time to analyze market trends as well as research and further develop trading strategies.

Orc Futures is a new client application specially designed for futures traders. A major part of trading in Chicago is made up of futures and Orc Software's new futures product is an important addition to the product portfolio in order to be able to increase sales in the US.

By agreement with the Norwegian software development company Infront, Orc Software has the possibility to distribute Infront's information and trading system on a global basis. The product, which is called Orc Online, was introduced during the third quarter and is an Internet application offering real time prices, news and completely integrated order management.

Furthermore the first versions that were based on the new components developed in St Petersburg were put into operation.

A total of 13 new market connections were completed during the year. In addition, maintenance, updates and performance optimization on a number of current market connections took place. The Orc System was further enhanced with a number of new functions in the new versions, which were completed during the year. Among other things the following was added: new order types such as parent-child-order, bait orders, and the ability to place orders based on a volume weighted average price. Additionally, the automated alert functions were improved and further functionality for making the management of a large number of client orders more efficient for brokers was added.

## **Organization**

During 2003 certain organizational changes were made. Among other things a smaller management group was established consisting of Nils Nilsson, CEO, Jonas Hansbo, Executive Vice

President and CTO, and Lars Johansson, Executive Vice President and COO. The new formation of the management group enhanced synchronization of product development with current activities in the market.

**Revenue<sup>1</sup>**

**Full year 2003**

The Group's revenue decreased during 2003 by 9 percent to SEK 249 (275 in the corresponding period 2002) million.

Systems revenue decreased by 9 percent to SEK 224 (247) million and amounted to 90 (90) percent of total revenue. The decrease is primarily due to cancellations of contracts and user licenses as well as the weakening of the US dollar. Initial revenue for Orc Liquidator and sales of technology components to OMHEX amounted to a total of approximately 7 percent of systems revenue for 2003.

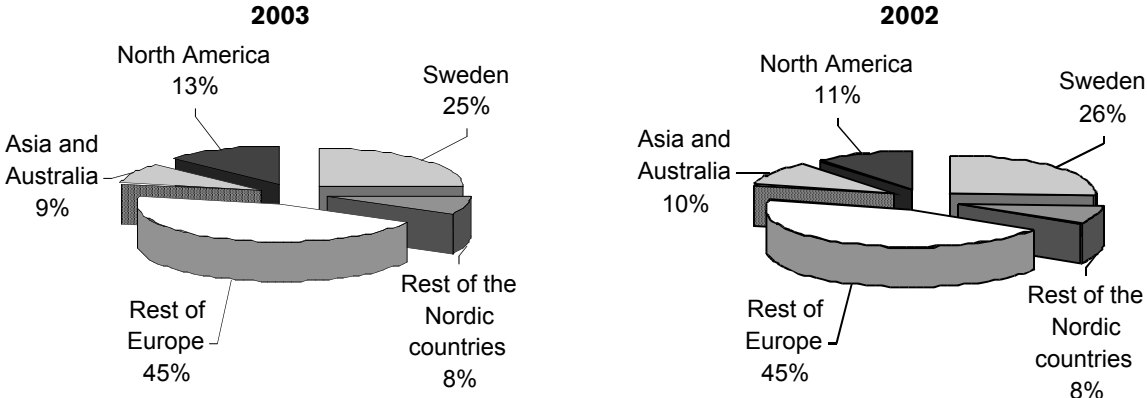
Other operating revenue decreased by 13 percent to SEK 13.2 (15.2) million and primarily represents hardware sales as well as consulting revenue.

The remaining revenue is related to development work performed by the company for its own use and capitalized, which decreased from SEK 13.4 to 12.0 million.

Orc ExNet continued to perform well during 2003. The total financial impact still represents a minor part of the Group's sales.

During 2003, revenue from clients located outside Sweden represented 75 (74) percent of total revenue. At the end of December 2003, OrcSoftware had clients in a total of 19 (19) countries.

**Revenue per geographic market**



<sup>1</sup> Revenue and operating margin for 2002 and 2003 are calculated after taking into account an increase in revenue of SEK 12.0 (13.4) million for 2003 subsequent to the capitalized work performed by the company for its own use, in accordance with the Swedish Financial Accounting Standards Council's recommendation no.15 (RR15).

SEK million	2003	2002	Change in %
Sweden	59	69	-14
Rest of the Nordic countries	18	21	-14
Rest of Europe	107	117	-9
Asia and Australia	22	27	-19
North America	31	28	11
Work performed by the company for its own use and capitalized	12	13	-8
<b>Total</b>	<b>249</b>	<b>275</b>	<b>-9</b>

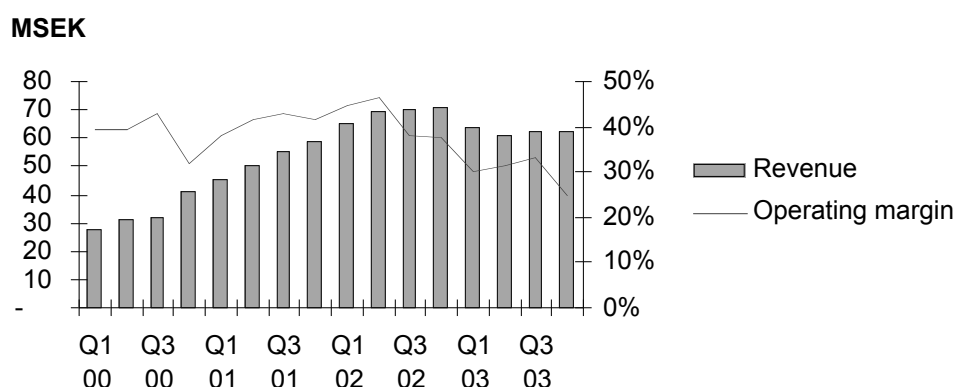
Sales to the North American market grew by 11 percent to SEK 31 million, primarily due to sales of Orc Liquidator. Sales decreased on other markets. Sweden and the remainder of Europe, excluding the Nordic region, accounted for the largest decrease in absolute terms.

The number of client sites<sup>2</sup> amounted to 154 (164) at the end of 2003. Average revenue per client site<sup>3</sup> amounted during the year to SEK 1.4 (1.6) million.

The Group's five largest clients represented a total of 18 percent of revenue during 2003. No individual client represented more than 5 percent of revenue.

#### Fourth quarter 2003

##### Quarterly revenue and operating margin



The Group's revenue decreased in the fourth quarter of 2003 by 13 percent to SEK 62 (71) million. Compared to the previous quarter revenue increased by 1 percent.

Systems revenue increased by 4 percent compared to the previous quarter, due to among other things, two new sales of Orc Liquidator. Other operating revenue decreased somewhat. Work performed by the company for its own use and capitalized decreased by SEK 1.8 million as a result of the company completing a development project in St Petersburg.

During the fourth quarter 6 new client sites were added in Japan, UK and the US. The number of lost client sites equaled 9 and consisted mostly of a number of smaller sites in the Nordic region and Asia. During the period Orc Software received cancellations regarding 7 client sites, which will impact the number of client sites during the upcoming quarters.

<sup>2</sup> The number of client sites includes the sites that as of year-end pay a license fee.

<sup>3</sup> Calculated as the total systems revenue divided by the average number of client sites for the period.

## Earnings

### Full year 2003

Operating income for 2003 decreased by 36 percent to SEK 74 (115) million, representing an operating margin of 29.9 (41.6) percent.

The lower operating income is primarily due to lower revenues. Furthermore, the focus on development and sales, which aims to generate future growth and accordingly did not have an immediate affect on revenue, increased costs.

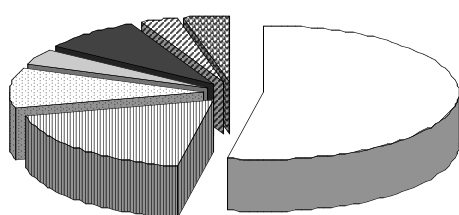
### Fourth quarter 2003

Operating income for the fourth quarter 2003 decreased by 41 percent to SEK 16 (27) million. The operating margin amounted to 24.9 (37.7) percent. Compared to the previous quarter operating income decreased by 25 percent.

The lower operating margin was mostly related to the increased focus on marketing and sales activities and higher amortizations. Among other things, the launch of Orc Liquidator increased marketing costs. Additionally a sales and support office was established in Chicago. Amortizations of intangible assets increased significantly as a result of the completion of the development project in St Petersburg.

## Operating expenses<sup>4</sup>

### Breakdown of operating expenses 2003



- Personnel costs 53% (51%)
- ▨ Other external expenses 18% (19%)
- ▩ Cost of premises 10% (9%)
- ▧ Consulting fees 4% (4%)
- Depreciation and amortization 8% (7%)
- ▤ Purchase cost of goods sold 3% (5%)
- ▦ Telecom expenses 4% (5%)

Operating expenses increased for 2003 by 9 percent to SEK 175 (161) million. In comparison to the previous quarter operating expenses increased by 13 percent.

Personnel costs increased by 13 percent to SEK 93 (82) million during 2003. The average number of employees increased by 10 percent for the same period. In comparison to the third quarter, personnel costs increased by 9 percent for the fourth quarter, which was primarily due to new employment and higher sales commissions, a consequence of the increased systems revenue.

The purchase cost of goods sold decreased during 2003 compared to the previous year, as a result of decreased hardware sales. The cost in comparison to the third quarter increased by SEK 0.9 million.

As a result of the expansion of the Stockholm office, as well as the office in Tokyo, cost of premises increased by 13 percent to SEK 17 (15) million for 2003. The Chicago office was established

<sup>4</sup> Due to OrcSoftware's working methods, whereby there is a considerable overlap between sales- and support work and sales- and development work, OrcSoftware reports its results according to the principles for an income statement presented by type of cost.

during the fourth quarter but had only a minor effect on cost of premises. The cost in comparison to the previous quarter was largely unchanged.

Telecom expenses decreased for 2003 by 7 percent and amounted to SEK 7.5 (8.1) million. The cost in comparison to the previous quarter was unchanged.

Consulting fees for product development increased somewhat compared to the previous year and amounted to SEK 7.8 (7.0) million. In comparison to the previous quarter these costs decreased from SEK 2.0 to 1.0 million.

Other external expenses increased for 2003 by 3 percent to SEK 30 (29) million. In comparison to the previous quarter these costs increased by 31 percent from SEK 6.8 to 8.9 million primarily due to the launch of Orc Liquidator.

Depreciation and amortization increased by 22 percent and amounted to SEK 13.1 (10.7) million. In comparison to the previous quarter depreciation and amortization increased by 45 percent. This is due to the completion of the development project in St Petersburg and that amortization of this intangible asset thereby began during the fourth quarter.

## Development expenses

Orc Software constantly invests considerable resources in product development of new and existing applications. The main part of development expenses consists of salaries. At the end of the year, 61 (58) people worked with product development in Frankfurt, London, Moscow, St Petersburg, Stockholm, Sydney and Toronto. Other product development expenses include computer equipment and premises for product developers, as well as external consultants.

As of January 1, 2002 Orc Software capitalizes the part of the Group's expenses that are related to the development of new market connections. Expenses for the development of new components for Orc Software's products, which took place in St Petersburg, were capitalized from the beginning of 2001 until the project was completed at the end of the third quarter of 2003. The people involved in this project currently work with continued development of the Orc System, which is not capitalized. Orc Software's policy for the amortization period is three years from completion.

Capitalized development expenditure during 2003 amounted to SEK 12.0 (13.4) million. Amortization of the accumulated capitalized development expenditure during 2003 amounted to SEK 3.9 (1.3) million.

The total development expenditure increased by 7 percent for 2003 and amounted to approximately 25 (21)<sup>5</sup> percent of revenue. In absolute terms the development expenses increased mostly due to an increase in internal development resources for the subsidiaries as well as the use of external resources for development. The development expenses are expected to represent a significant part of operating expenses also in the future.

## Net financial income

Net financial income decreased to SEK 5.6 (8.5) million as a result of a decrease in liquid funds and lower interest rates as well as lower income from associated companies. The Group's liquid funds decreased during the year from SEK 274 to 252 million, of which SEK 216 (240) million consisted of short-term investments.

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<sup>5</sup> Previously these figures included amortization of capitalized development expenditure. The comparable figure is recalculated.

Income after financial items decreased by 35 percent to SEK 80 (123) million.

## **Taxes**

The tax rate for 2003 amounted to 30 (29) percent. Tax expenses are calculated based on the expected tax for the parent company and each subsidiary.

Income after tax decreased by 36 percent to SEK 56 (87) million.

## **Operating capital and working capital commitment**

OrcSoftware's operating capital amounted to SEK -8 (-29) million at the end of 2003. The increase in operating capital was primarily due to the decrease in liquid funds. The Group did not have any interest bearing debt for the period.

The working capital<sup>6</sup> increased by SEK 2 million to SEK -30 (-32) million. The principal reason behind the negative working capital commitment is the large item of accrued expenses and prepaid income that for the most part consists of license fees, which are invoiced quarterly in advance.

## **Asset turnover ratio**

The balance sheet total decreased during 2003 by 3 percent to SEK 354 (365) million and the asset turnover ratio amounted to 1.0 (1.3).

## **Equity/assets ratio and earning capacity**

The equity/assets ratio amounted at year-end to 69 (67) percent. During 2003 the return on capital employed amounted to 33 (57) percent and the return on shareholders' equity amounted to 23 (40) percent.

## **Cash flow and investments**

The Group's cash flow, before changes in working capital and investments, amounted at year-end to SEK 59 (111) million. The decrease in cash flow was mostly due to a lower operating income and a decrease in tax liabilities.

The Group's investments for the year amounted to SEK 22 (32) million, primarily consisting of capitalized development expenses amounting to SEK 12.0 million as well as computer and office equipment for SEK 6.1 million.

The Group's cash flow after investments amounted to SEK 34 (84) million during 2003.

Cash flow from financing activities amounted to -56 (-33), which corresponds to the repurchase of own shares of SEK 11.2 (0) million and the payment of dividends equaling SEK 45 (33) million.

Liquid funds amounted to SEK 252 (274) million as of December 31, 2003.

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<sup>6</sup> Tax liabilities/receivables were previously included in the calculation for working capital but are now excluded in accordance with the definition of working capital in Swedish Accounting Standards Council's recommendation no. 7. The comparable figures are adjusted for this change.



The ratio between cash flow, before financial items and tax, and the operating income, before depreciation and amortization, amounted at year-end to 0.7 (0.8).

## Financial risk management

### Foreign exchange risks

#### i) Transaction Exposure

The majority of OrcSoftware's invoicing to clients in the Nordic countries takes place in Swedish kronor. Clients outside the Nordic countries are invoiced primarily in US dollars and Euro, although invoicing is also done in Australian dollars, Danish kronor, Canadian dollars as well as to some extent in British pounds. The Group has significant exposure in US dollars and Euro, for which invoicing exceeds expenses, as well as in British pounds where expenses exceed revenue since the invoicing for UK clients is primarily denominated in US dollars.

The Group's exposed net inflow amounted to approximately SEK 103 million in 2003, allocated as set out in the table below.

<b>Inflow 2003</b>	<b>SEK million</b>
USD	69
EUR	30
AUD	2
DKK	2
<b>Total</b>	<b>103</b>
<b>Outflow 2003</b>	
GBP	16
JPY	6
HKD	2
CAD	1
CHF	1
<b>Total</b>	<b>26</b>

The effect of exchange rate fluctuations, calculated as a change of the relevant average exchange rates between 2002 and 2003, amounted to approximately SEK -11.1 million, and was primarily due to the weakened USD, which at year-end equaled 7.28 Swedish kronor. Foreign exchange hedging affected earnings on an operating level by SEK 13.7 (3.0) million.

In accordance with the Group's policy, significant net exposure in each respective currency is hedged for the coming 3-12 months, with a certain possibility of deviation in special cases. As of December 31, 2003, future flows equivalent to SEK 94 (162) million had been hedged<sup>7</sup>, consisting of USD 6.0 (11.0) million hedged against the Swedish krona at an average forward rate of 9.99 (10.43) and EUR 3.7 (5.0) million hedged against the Swedish krona at an average forward rate of 9.30 (9.37). The total average remaining duration is approximately 3 (10) and 3 (9) months respectively. These foreign exchange hedges represent approximately 7-10 (15) months of future net flows.

At financial year-end, non-realized foreign exchange gains amounted to SEK 7.5 (11.8) million, valued at the SEK/USD exchange rate of 7.28 (8.83) and the SEK/EUR rate of 9.09 (9.19).

<sup>7</sup> OM Treasury AB is the counterpart on SEK 47 million of this amount.

ii) Balance Sheet Exposure

It is OrcSoftware's policy to hedge significant exposure in foreign currencies. At year-end, OrcSoftware did not have any significant balance sheet exposure in foreign currencies.

### Liquidity management

As to liquidity risk and credit risk, investments may only take place in instruments that have high liquidity and credit value. This implies that Swedish issuers must be ranked "K1" as per Standard & Poor's ratings and that non-Swedish issuers must be ranked "A-1" and "P-1" as per Standard & Poor's and Moody's ratings.

The Group's short-term investments, which at year-end amounted to a nominal value of SEK 218 (243) million, consisted of Swedish commercial papers with "K1" credit ratings and bank time deposits.

### Credit risks

In general, OrcSoftware's clients, who among others consist of investment banks, banks and brokerage houses, represent a capital-strong segment with a consequent low risk for credit losses. The Group's credit losses are negligible due to the fact that clients, on a quarterly or even longer basis, pay in advance and that Orc Software works actively to inform its clients of the importance of paying on time. During 2003, there were no significant credit losses.

### Sensitivity analysis

The sensitivity analysis below describes the full-year effect on the Group's operating income due to a change in a number of factors.

Factor	Change	Effect on Operating Income for Full Year 2003, SEK million
License price	+/- 5%	11.2
Salary costs	+/- 5%	4.4
Development expenses	+/- 5%	3.0
SEK/USD	+/- 5%	3.9 <sup>8</sup>
SEK/GBP	+/- 5%	0.8 <sup>8</sup>
SEK/EUR	+/- 5%	1.7 <sup>8</sup>

### Employees

During 2003 the number of employees increased from 138 to 141, an increase of 2 percent. The average number of employees was 137 (124). As a consequence of the uncertainty in the market Orc Software decreased the number of new employments for 2003 in comparison to previous years. The number of female employees at year-end equaled 24 (23) and the number of male employees equaled 117 (115). The average age of the employees is 31 (30) years.

	Employees by office		Employees by function		
	Dec 31, 2003	Dec 31, 2002	Dec 31, 2003	Dec 31, 2002	
Sweden	60	62	Product development	61	58
Russia	32	35	Support	35	36
Rest of Europe	30	24	Sales	21	21
Asia & Australia	11	10	Company-wide functions	24	23
North America	8	7	<b>Total</b>	<b>141</b>	<b>138</b>
<b>Total</b>	<b>141</b>	<b>138</b>			

<sup>8</sup> Without taking into consideration existing hedging contracts.

## Incentive scheme

Orc Software's employees including the Group Management have the possibility of receiving a bonus directly related to sales, and a bonus that is paid if the Group's revenue growth and operating income significantly exceed the internally set goals. Income for 2003 encompasses only sales related bonuses, including social security expenses, of SEK 2.3 (0) million. The Board of Directors' remuneration committee prepares the incentive program.

## Options program

Carnegie has issued two option programs for Orc Software's employees. One program issued in 2000, covered the purchase of 519 000 options by 55 employees and expired during the year. The exercise price equaled SEK 60 per option with maturity on March 31, 2003. The second program issued in 2001 covers the purchase of 270 000 call options by 39 employees with an exercise price of SEK 210 per option, maturing on March 1, 2004. The options were purchased at a price calculated by Carnegie.

A new option program for Orc Software's employees was launched during the first quarter of 2003. All employees in the Group have been granted the opportunity to purchase call options issued by Hagströmer & Qviberg FK at market price. A total of 71 employees purchased a total of 304900 call options from Hagströmer & Qviberg. The exercise price for the call option has been set at SEK 80 and the expiration date is March 1, 2006. The option premium amounted to SEK 11.50 per option.

All options will be cash-settled by a third party and the option programs will therefore not result in any dilution and will not affect OrcSoftware's earnings.

## Shareholders

The number of shareholders in OrcSoftware on December 31, 2003 equaled 3277 (2468).

<b>OrcSoftware's ten largest shareholders</b>	<b>No. of shares</b>	<b>% of shares</b>
OM Technology	4 488 075	30.7
Cancale Förvaltnings*	1 533 200	10.5
Third Swedish National Pension Fund	664 800	4.5
SEB Sweden Small Cap Fund	621 140	4.2
Goldman Sachs	530 815	3.6
Hagströmer & Qviberg	520 329	3.6
Fidelity funds	476 700	3.3
Nordea Bank Finland	462 631	3.2
Carnegie funds	380 000	2.6
Robur funds	298 300	2.0
Other shareholders	4 649 010	31.8
<b>Total</b>	<b>14 625 000</b>	<b>100.0</b>

Source: VPC AB, direct and nominee shareholders December 30, 2003.

As of December 31, 2003 Orc Software has purchased 225000 shares and the total number of shares, reduced by Orc Software's repurchase of own shares, amounted to 14625000.

\*Cancale Förvaltnings AB is jointly owned in equal shares by Ulrika Hagdahl and Nils Nilsson. In addition Ulrika Hagdahl and Nils Nilsson privately own 46 000 respective 20 000 shares.

## Proposed dividend

The Board of Directors has resolved to recommend a dividend of SEK 3.40 (3.00) per share for 2003, representing a total of SEK 50 (45) million and 89 (51) percent of net income. The Board proposes a higher dividend given that the company expects positive market development and today has a strong capital base. The proposed record day for dividends is Monday, April 26, 2004. If the Annual General Meeting votes in favor of the proposal, the expected payment date for the dividends is Thursday, April 29, 2004. The dividends are paid through VPC AB.

## Share repurchase and reduction of share premium reserve

During the fourth quarter of 2003 Orc Software did not purchase any Orc shares. During 2003 Orc Software purchased a total of 225 000 shares for SEK 11.2 million, which equals 1.5 percent of the 14 850 000 shares issued, in accordance with the decision from the General Annual Meeting 2003. Excluding Orc Software's shares the number of shares equals 14 625 000. The nominal value of the acquired shares is SEK 22 500. The purpose of the acquisitions is to provide the Board with the opportunity to create additional value for the company's shareholders by adjusting the capital structure of the Group.

The Annual General Meeting 2003 decided to reduce the share premium reserve by SEK 50 million. The District Court's decision regarding the reduction was made on January 14, 2004 and becomes law on February 4, 2004, at which time the period for appeal expires. As of December 31, 2003 restricted and non-restricted reserves are accounted for including the unapproved reduction of the share premium reserve.

## Transactions with affiliated companies

During 2003 Orc Software sold technology components to OM Technology AB for SEK 3 million. Orc Software has also purchased development services for SEK 3.3 million from Game Federation Development AB, in which Orc Software owns 49 percent, and from E2E infotech Limited, in which Orc Software owns 34 percent, for SEK 2.0 million.

## The Parent company

The parent company's revenue<sup>9</sup> decreased 9 percent to SEK 230 (254) million. Income after financial items decreased and amounted to SEK 74 (114) million. Liquid funds amounted at the end of the year to SEK 228 (258) million, of which SEK 211 (240) million consisted of short-term investments.

## Accounting principles

This interim report has been prepared in accordance with the Swedish Accounting Standards Council's recommendation on interim reporting (RR 20). The same accounting principles have been used as in the last annual accounts, with the following additions:

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<sup>9</sup> Most of Orc Software's invoicing is administered by the Parent company. The subsidiaries invoice the Parent company an amount that is based on the subsidiaries' actual costs plus a profit margin mark-up. Revenues in the Parent company's accounting have previously offset these costs. As of the fourth quarter the Parent company's revenues and costs are accounted for in gross terms. Comparable figures have been adjusted for this change.

In 2003 new recommendations were made on the Format of financial statements (RR22), Reporting per segment (RR25), Events after the accounting year-end (RR26) and Financial instruments (RR27). The recommendations will add to the disclosure requirements for Orc Software's financial reports.

As of January 1, 2004, OrcSoftware will implement the new recommendation from the Swedish Accounting Standards Council, Remuneration to employees (RR29). The recommendation will require greater disclosure in Orc Software's financial reports. According to the recommendation, programs for remuneration following discontinued employment shall either be classified as a defined contribution plan or as a defined benefit plan. Orc Software only has defined contribution plan and shall therefore continue to expense fees for pensions and other commitments such as benefits following discontinued employment. This principle is in total agreement with the financial reports for previous years.

## Income statement

SEK thousands	2003	2002	Oct-Dec 2003	Oct-Dec 2002
<b>Operating revenue</b>				
Systems revenue	223 943	246 688	58 888	61 123
Work performed by the company for its own use and capitalized	11 988	13 412	540	4 007
Other operating revenue	13 177	15 234	3 071	5 765
<b>Total revenue</b>	<b>249 109</b>	<b>275 334</b>	<b>62 499</b>	<b>70 895</b>
<b>Operating expenses</b>				
Purchase cost of goods sold	-5 742	-8 169	-1 780	-3 004
External expenses				
Cost of premises	-17 030	-14 914	-4 293	-4 386
Telecom expenses	-7 542	-8 147	-1 922	-2 495
Consulting fees	-7 839	-6 995	-1 028	-2 285
Other external expenses	-30 165	-29 294	-8 912	-8 514
Personnel costs	-93 222	-82 443	-24 819	-20 454
Depreciation and amortization	-13 076	-10 747	-4 201	-2 995
<b>Total expenses</b>	<b>-174 616</b>	<b>-160 709</b>	<b>-46 955</b>	<b>-44 133</b>
<b>Operating income</b>	<b>74 493</b>	<b>114 625</b>	<b>15 544</b>	<b>26 762</b>
<b>Financial items</b>				
Income from participation in associated companies	-1 379	-564	-169	-398
Financial income	7 316	9 123	1 568	2 508
Financial expenses	-332	-59	-101	-37
<b>Net financial income</b>	<b>5 605</b>	<b>8 500</b>	<b>1 298</b>	<b>2 073</b>
<b>Income after financial items</b>	<b>80 098</b>	<b>123 125</b>	<b>16 842</b>	<b>28 835</b>
Tax on net income for the period	-23 717	-36 047	-4 747	-13 594
Minority's part of the income for the period	-775	141	-43	-53
<b>Net income for the period</b>	<b>55 606</b>	<b>87 219</b>	<b>12 052</b>	<b>15 188</b>
Earnings per share <sup>10</sup> , SEK	3.78	5.87	0.82	1.02
Number of shares at the end of period, reduced by Orc Software's repurchase of own shares, thousands	14 625	14 850	14 625	14 850
Average number of shares, reduced by Orc Software's repurchase of own shares, thousands	14 712	14 850	14 625	14 850

<sup>10</sup> Orc Software does not have any convertible loans or warrants.

## Balance sheet

SEK thousands	Dec 31, 2003	Dec 31, 2002
<b>ASSETS</b>		
<b>Fixed assets</b>		
Intangible assets		
Capitalized development expenditure	21 888	13 832
Goodwill	286	382
Other intangible fixed assets <sup>11</sup>	2 164	2 906
Tangible assets		
Equipment	17 530	19 750
Financial assets		
Shares in associated companies	1 545	1 827
Other long-term financial fixed assets	5 229	4 115
<b>Total fixed assets</b>	<b>48 642</b>	<b>42 812</b>
<b>Current assets</b>		
Current receivables		
Accounts receivable	40 681	36 206
Other receivables	6 165	7 500
Prepaid expenses and accrued income	6 868	4 776
Short-term investments	216 206	240 299
Cash and bank balances	35 661	33 523
<b>Total current assets</b>	<b>305 581</b>	<b>322 304</b>
<b>TOTAL ASSETS</b>	<b>354 223</b>	<b>365 116</b>
<b>EQUITY AND LIABILITIES</b>		
<b>Equity<sup>12</sup></b>		
Restricted equity		
Share capital	1 485	1 485
Restricted reserves	101 461	138 818
Non-restricted equity		
Non-restricted reserves	85 726	17 621
Net income for the year	55 606	87 219
<b>Total equity</b>	<b>244 278</b>	<b>245 143</b>
<b>Minority interest</b>	<b>1 259</b>	<b>484</b>
<b>Provisions</b>		
Deferred tax liability	23 636	19 573
<b>Total provisions</b>	<b>23 636</b>	<b>19 573</b>
<b>Current liabilities</b>		
Accounts payable	5 969	7 445
Tax liabilities	1 685	19 106
Other liabilities	4 596	5 066
Accrued expenses and prepaid income	72 800	68 299
<b>Total current liabilities</b>	<b>85 050</b>	<b>99 916</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>354 223</b>	<b>365 116</b>
Pledged assets	None	None
Contingent liabilities	None	None

<sup>11</sup> This item pertains to Orc ExNet.

<sup>12</sup> As of December 31, 2003 restricted and non-restricted reserves are accounted for including a non-registered reduction of the share premium reserve. The District Court's decision regarding the reduction was made on January 14, 2004 and becomes law on February 4, 2004, at which time the period for appeal expires.

## Specification of the Group's goodwill

The goodwill arose in conjunction with the establishment of Orc ExNet and is being amortized over a period of 60 months, with the adjustment for possible write-downs.

	SEK thousands
Acquisition value less accumulated amortization January 1, 2003	382
Amortization for the year	-96
Acquisition value less accumulated amortization December 31, 2003	286

## Specification of equity (SEK thousands)

<b>2003</b>	<b>Share Capital</b>	<b>Restricted Reserves</b>	<b>Non-restricted Equity</b>	<b>Total</b>
Opening balance January 1, 2003	1 485	138 818	104 840	245 143
Dividend for 2002	-	-	-44 550	-44 550
Share repurchase	-	-	-11 177	-11 177
The affect on shareholders' equity due to the acquisition of the remaining portion of associated company	-	-	-145	-145
Reduction of share premium reserve, unregistered	-	-50 000	50 000	0
Adjustments between restricted and non-restricted shareholders' equity	-	12 916	-12 916	0
Translation difference etc.	-	-273	-326	-599
Net income for the year	-	-	55 606	55 606
Closing balance December 31, 2003	1 485	101 461	141 332	244 278

<b>2002</b>	<b>Share Capital</b>	<b>Restricted Reserves</b>	<b>Non-restricted Equity</b>	<b>Total</b>
Opening balance January 1, 2002	1 485	119 615	70 707	191 807
Dividend for 2001	-	-	-32 670	-32 670
Transfer to statutory reserve in accordance with distribution of earnings	-	20	-20	0
Adjustments between restricted and non-restricted shareholders' equity	-	19 446	-19 446	0
Translation difference	-	-263	-950	-1 213
Net income for the year	-	-	87 219	87 219
Closing balance December 31, 2002	1 485	138 818	104 840	245 143

<b>Oct-Dec 2003</b>	<b>Share Capital</b>	<b>Restricted Reserves</b>	<b>Non-restricted Equity</b>	<b>Total</b>
Opening balance October 1, 2003	1 485	138 614	91 948	232 047
The affect on shareholders' equity due to the acquisition of the remaining portion of associated company	-	-	-145	-145
Reduction of share premium reserve, unregistered	-	-50 000	50 000	0
Adjustments between restricted and non-restricted shareholders' equity	-	12 917	-12 917	0
Translation difference	-	-70	394	324
Net income for the period	-	-	12 052	12 052
Closing balance December 31, 2003	1 485	101 461	141 332	244 278

<b>Oct-Dec 2002</b>	<b>Share Capital</b>	<b>Restricted Reserves</b>	<b>Non-restricted Equity</b>	<b>Total</b>
Opening balance October 1, 2002	1 485	119 635	109 159	230 279
Adjustments between restricted and non-restricted shareholders' equity	-	19 446	-19 446	0
Translation difference	-	-263	-61	-324
Net income for the period	-	-	15 188	15 188
Closing balance December 31, 2002	1 485	138 818	104 840	245 143



## Cash flow statement

SEK thousands	2003	2002
<b>Operating activities</b>		
Operating income	74 493	114 625
Adjustment for items not included in cash flow		
Depreciation and amortization	13 075	10 747
Other adjustments for items not included in cash flow	376	1 037
Financial items	7 102	8 850
Income tax paid <sup>13</sup>	-36 404	-24 016
<b>Cash flow from operating activities before changes in working capital</b>	<b>58 642</b>	<b>111 243</b>
<b>Changes in working capital</b>		
Changes to accounts receivable	-4 242	2 732
Changes in operating assets	-1 157	-6 029
Changes to accounts payable	-1 479	4 394
Changes in operating liabilities <sup>13</sup>	4 252	3 126
<b>Total change in working capital</b>	<b>-2 626</b>	<b>4 223</b>
<b>Cash flow from operating activities</b>	<b>56 016</b>	<b>115 466</b>
<b>Investment activities</b>		
Investments in intangible fixed assets	-11 988	-13 413
Investments in tangible fixed assets	-6 125	-12 835
Changes in financial fixed assets	-3 421	-5 605
<b>Cash flow from investment activities</b>	<b>-21 534</b>	<b>-31 853</b>
<b>Financing activities</b>		
Share repurchase	-11 177	-
Dividend	-44 550	-32 670
<b>Cash flow from financing activities</b>	<b>-55 727</b>	<b>-32 670</b>
Change in liquid funds	-21 245	50 943
Opening liquid funds	273 822	224 289
Translation difference/exchange differences in liquid funds	-710	-1 410
Closing liquid funds	251 867	273 822

## Key ratios

	2003	2002	Oct-Dec 2003	Oct-Dec 2002
Operating margin, %	29.9	41.6	24.9	37.7
Return on equity, %	23	40	20	26
Return on capital employed, %	33	57	29	48
Asset turnover ratio	1.0	1.3	1.0	1.2
Equity/assets ratio, %	69	67	69	67
Average number of employees	137	124	139	138
Earnings per share, SEK	3.78	5.87	0.82	1.02
Equity per share, SEK	16.70	16.51	16.70	16.51
Share price at end of the period, SEK	84.50	67.50	84.50	67.50
Number of shares at end of period, reduced by Orc Software's repurchase of own shares, thousands	14 625	14 850	14 625	14 850

<sup>13</sup> Tax debt was previously included in changes in operating liabilities but is now accounted in income tax paid in accordance with the Swedish Accounting Standards Council's recommendation no. 7. Comparative figures have been adjusted accordingly.

## Quarterly figures

### Income statement

SEK thousands	Q1 2002	Q2 2002	Q3 2002	Q4 2002	Q1 2003	Q2 2003	Q3 2003	Q4 2003
<b>Operating revenue</b>								
Systems revenue	60 167	63 849	61 549	61 123	54 005	54 593	56 457	58 888
Work performed by the company for own use and capitalized	3 422	2 783	3 200	4 007	4 931	4 181	2 336	540
Other operating revenue	1 638	2 455	5 376	5 765	4 575	2 148	3 383	3 071
<b>Total revenue</b>	<b>65 227</b>	<b>69 087</b>	<b>70 125</b>	<b>70 895</b>	<b>63 511</b>	<b>60 922</b>	<b>62 176</b>	<b>62 499</b>
<b>Operating expenses</b>								
Personnel costs	-21 521	-19 715	-20 753	-20 454	-23 071	-22 496	-22 836	-24 819
Depreciation and amortization	-2 361	-2 492	-2 849	-2 995	-2 949	-3 025	-2 900	-4 201
Other expenses	-12 057	-14 810	-19 969	-20 684	-18 233	-16 346	-15 804	-17 935
<b>Total expenses</b>	<b>-35 939</b>	<b>-37 017</b>	<b>-43 571</b>	<b>-44 133</b>	<b>-44 253</b>	<b>-41 867</b>	<b>-41 540</b>	<b>-46 955</b>
<b>Operating income</b>	<b>29 288</b>	<b>32 070</b>	<b>26 554</b>	<b>26 762</b>	<b>19 258</b>	<b>19 055</b>	<b>20 636</b>	<b>15 544</b>
<b>Net financial items</b>	<b>1 766</b>	<b>2 020</b>	<b>2 589</b>	<b>2 073</b>	<b>1 817</b>	<b>1 814</b>	<b>676</b>	<b>1 298</b>
Tax on income for the period	-8 576	-8 578	-5 298	-13 594	-6 328	-6 254	-6 388	-4 747
Minority's part of the income for the period	99	100	-5	-53	-97	-369	-266	-43
<b>Net income for the period</b>	<b>22 577</b>	<b>25 612</b>	<b>23 840</b>	<b>15 188</b>	<b>14 650</b>	<b>14 246</b>	<b>14 658</b>	<b>12 052</b>

### Balance Sheet

SEK thousands	Mar 2002	Jun 2002	Sept 2002	Dec 2002	Mar 2003	Jun 2003	Sept 2003	Dec 2003
<b>Fixed assets</b>								
Intangible assets	8 921	11 273	14 033	17 120	21 211	24 447	25 814	24 338
Tangible assets	16 798	16 906	16 855	19 750	19 021	17 862	16 623	17 530
Financial assets	749	1 987	2 225	5 942	4 358	7 055	6 256	6 774
<b>Total fixed assets</b>	<b>26 468</b>	<b>30 166</b>	<b>33 113</b>	<b>42 812</b>	<b>44 590</b>	<b>49 364</b>	<b>48 693</b>	<b>48 642</b>
<b>Current assets</b>								
Accounts receivable	34 973	33 946	41 904	36 206	29 727	38 024	37 164	40 681
Other receivables	10 627	11 065	10 540	12 276	11 507	7 809	9 800	13 033
Cash and bank balances and short-term investments	251 758	241 757	254 848	273 822	274 914	219 155	237 558	251 867
<b>Total current assets</b>	<b>297 358</b>	<b>286 768</b>	<b>307 292</b>	<b>322 304</b>	<b>316 148</b>	<b>264 988</b>	<b>284 522</b>	<b>305 581</b>
<b>TOTAL ASSETS</b>	<b>323 826</b>	<b>316 934</b>	<b>340 405</b>	<b>365 116</b>	<b>360 738</b>	<b>314 352</b>	<b>333 215</b>	<b>354 223</b>
Equity	213 674	206 252	230 279	245 143	259 155	217 864	232 047	244 278
Minority interest	526	426	431	484	581	950	1 216	1 259
Provisions for deferred tax liability	12 415	12 415	12 415	19 573	19 573	19 573	19 573	23 636
Current non interest-bearing liabilities	97 211	97 841	97 280	99 916	81 429	75 965	80 379	85 050
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>323 826</b>	<b>316 934</b>	<b>340 405</b>	<b>365 116</b>	<b>360 738</b>	<b>314 352</b>	<b>333 215</b>	<b>354 223</b>

## Forthcoming financial events

March 2004	Annual Report 2003
April 16, 2004	Interim Report for January-March
April 21, 2004	Annual General Meeting
July 13, 2004	Interim Report for January-June
October 14, 2004	Interim Report for January-September

The full annual report will be available at Orc Software's Swedish office in the middle of March 2004. It will also be distributed to the shareholders.

## Annual General Meeting

The Annual General Meeting will be held on Wednesday April 21, 2004 at 4 p.m. at Orc Software, Birger Jarlsgatan 32A, 5 floors, Stockholm, Sweden.

The nominating committee consists of Magnus Böcker (OMHEX AB), Ulrika Hagdahl (Cancale Förvaltnings AB), Mats Gustafsson (SEB Asset Management) and Tomas Nicolin (Third Swedish National Pension Fund). Contact details for the nominating committee:

E-mail: [nominering@orcsoftware.com](mailto:nominering@orcsoftware.com)

Address: Nominating committee, Orc Software, Box 7742, SE-103 95 Stockholm, Sweden

## Analyst and press meeting, and telephone conference

An analyst and press meeting will be held on January 27, 2004 in Stockholm at 2 p.m. A telephone conference will be held on January 27, 2004 at 4 p.m. (CET). For more information about these events visit [www.orcsoftware.com](http://www.orcsoftware.com), Company, Investor Relations, Calendar.

Stockholm, January 27, 2004

The Board of Directors

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Definitions can be found at [www.orcsoftware.com](http://www.orcsoftware.com), Company, Investor Relations, Interim Reports.

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