

**NEONODE**

**CONFIDENTIAL BUSINESS PLAN  
May 2003**

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# I. Executive Summary

During the last decade, mobile communications industry leaped up on centre stage to become one of the biggest and fastest growing technology sectors of all times. Yet, with over 1,3 billion active users worldwide and over 405 million mobile phones sold in 2002<sup>1</sup>, the mobile industry is still considered by many to be in its early stages of development.

From an industry perspective, the key driving forces behind this exceptional growth has been *rapid technological innovation* and *proprietary solutions*. Equipment manufacturers, such as Ericsson, Nokia and Motorola, have been able to seize leadership positions by investing heavily in high-margin, proprietary solutions and integrating the whole value chain by supplying infrastructure, handsets and key applications.

But the mobile communications industry's exclusive focus on developing proprietary technology and the lack of a dominant design is currently slowing down the growth and development of new applications and services. In the battle for new customers and market leadership, new technology is being developed to give mobile phones access to information, applications and services already available on the World Wide Web. This has captured the attention of thousands of hardware and software companies active in the PC industry that see a tremendous opportunity for growth in supplying hardware, software, services and content to their customers' mobile handsets.

From a customer perspective, there is a whole new generation of tech-savvy end-users that have grown up during the 1980's and 1990's with the evolution of the PC and the World Wide Web (and is currently driving the market growth in the mobile communications industry). These end-users, aged 13 – 25, see the mobile phone as something more than an advanced "cordless phone" – it is a multi-purpose information and communication device that can be used to play games, listen to music, surf the web and communicate with others – just like they do on their PC at home.

This opens up a whole new world of opportunities to current and future leaders in the mobile communications industry. To satisfy the demands of a young and tech-savvy generation of mobile users, the future market leaders in the mobile communications industry must:

- a) be able to deliver mobile communications devices that give its owner unprecedented freedom in the customization and personalization of their mobile handset to fit and reflect their individual lifestyles
- b) develop new mobile communications devices that support the tremendous variety of features and applications that can be found in the PC and on the World Wide Web.

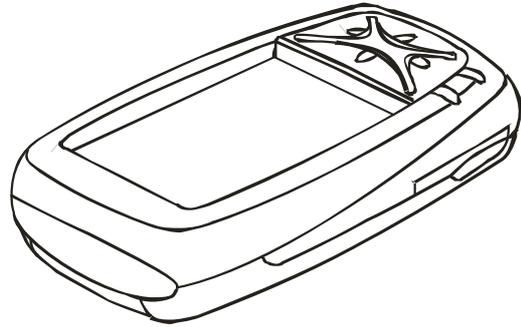
To effectively seize this market opportunity, Magnus Goertz and Thomas Eriksson sat down to analyze and identify the technology, market focus, core competencies and competitive advantages needed to seize a leadership position in this rapidly emerging industry. Their research and analysis led to the founding of Neonode AB in June of 2000, a limited-liability corporation based in Kista, a few miles north of Stockholm, Sweden.

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<sup>1</sup> Cellular News 2003-03-28 ([www.cellular-news.com/story/8178.html](http://www.cellular-news.com/story/8178.html))

Neonode has spent over two and a half years developing its first product, the N-1, which represents a paradigm shift in mobile communications device design.

The N-1 is a credit card-sized, state-of-the-art mobile handset that offer end-users unprecedented freedom and endless possibilities to customize their mobile handset with features, applications and services that fit their lifestyle.



More than just a mobile phone, the N-1 is also a full-featured entertainment and information center that allows its owner to listen to hours and hours of music in MP3-format with true HiFi quality, to download games and video clips from the World Wide Web, to take photos with the built-in digital camera, and so much more...

When exhibited at the CeBIT industry trade show, the N-1 created such a buzz in the industry that Neonode received over 16,000 pre-orders by individual customers and was contacted by hundreds of operators and companies seeking to partner with Neonode.

The N-1 is ready to be launched on the European Market in the end of August 2003. Neonode currently employs a team of 14 people under the direction of a young, talented and dedicated management team with complementary skills and relevant industry experience. The team has been able to take the product through its entire development phase without external funding.

Neonode's projected revenues are estimated to € 3,9M in 2003 and € 56M in 2004. The company expects to break-even in July 2004 and become profitable in May 2005. Net profit in 2005 is at present estimated to €10M.

Neonode's is currently seeking a strong financial partner that can secure first-round funding and take an active role in the company's current and future development.

Neonode is seeking to raise € 6,5M in funding over the next 6 - 12 months and intends to provide early-stage investors with an exit during an IPO scheduled for 2006.

## II. Market Opportunity

### A. Background

During the last decade, mobile communications industry leaped up on center stage to become one of the biggest and fastest growing technology sectors of all times. Yet, with over 1,3 billion active users worldwide and over 405 million mobile phones sold in 2002<sup>2</sup>, the mobile industry is still considered by many to be in its early stages of development.

From an industry perspective, the key driving forces behind this exceptional growth has been *rapid technological innovation* and *proprietary solutions*. Equipment manufacturers, such as Ericsson, Nokia and Motorola, have been able to seize leadership positions by investing heavily in high-margin, proprietary solutions and integrating the whole value chain by supplying infrastructure, handsets and key applications.

Mobile phone operators have been able to seize leadership positions by investing heavily in infrastructure needed for geographical coverage and accessibility and by offering end-users elaborate service plans that includes partially subsidized handsets and proprietary service offerings.

From a consumer perspective, the key driving force to rapid market acceptance has primarily been the convenience, sense of freedom and security that this technology brings to the end-user. The ability to be reached and to communicate with others at "any time, any place" is not only an attractive service that many people are willing to pay for – it has also had a profound impact on people's personal and professional lives and forever changed the way we communicate with each other.

### B. Trends

From an industry perspective, several companies with proprietary technologies are currently fighting for market leadership, but none have yet been able to reach true market dominance.

In the battle for new customers and market leadership, new technology is being developed to give mobile phones access to information, applications and services already available on the World Wide Web. This has captured the attention of thousands of hardware and software companies active in the PC industry that see a tremendous opportunity for growth in supplying hardware, software, services and content to their customers mobile handsets.

At present, the mobile communications industry's exclusive focus on developing proprietary technology and the lack of a dominant design is actually slowing down the growth and development of new applications and services.

Today's industry leaders do not wish to see their current leadership positions threatened by allowing more players to bring new products and services to market that are not based on their own proprietary designs. At the same time, these industry leaders lack the expertise and experience needed to develop their own respective proprietary technologies so that their mobile phones can run the tremendous variety of applications and services that have been developed for the PC and the World Wide Web.

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<sup>2</sup> Cellular News 2003-03-28 ([www.cellular-news.com/story/8178.html](http://www.cellular-news.com/story/8178.html))

For these reasons, the mobile communications industry finds itself at a highly decisive moment in time. The biggest industry players may choose to continue to invest heavily in developing their own proprietary technologies to deliver greater value to its customers and hope that they will eventually become the dominant design that enables them to seize a dominant market position.

They may also choose to open up their proprietary platforms to a critical mass of specialized players that have the expertise necessary to develop new applications and services that more effectively serve customer's demands.

Another possibility is that the market leaders in the PC industry acquire the expertise needed to adapt their market-leading technology. This way, they will better address the needs of mobile handset customers, thus posing a significant threat to "pure" telecom companies who have invested heavily in developing their own proprietary technology, and pave the way for thousands of highly specialized hardware, software and application development companies to deliver new features, applications, services and content that add value to the end-user.

### **C. Market Opportunity**

From a consumer perspective, the mobile phone is rapidly becoming something more than merely an advanced "cordless phone" that can be used at "any time, any place".

For a whole new generation of tech-savvy end-users that have grown up during the 1980's and 1990's with the evolution of the PC and the World Wide Web, they see the mobile phone as a multi-purpose information and communication device that can be used to play games, listen to music, surf the web and communicate with others – just like they do on their PC at home.

Just like the PC and the World Wide Web allow them to play and interact with others, the mobile phone is also becoming a tool that enables them to play and interact with their friends in new, innovative ways. Moreover, the mobile phone is rapidly becoming a fashion item among teenagers and young adults – the mobile handset is very much a statement of who they are and how they would like to be perceived by others.

This opens up a whole new world of opportunities to current and future leaders in the mobile communications industry. In order to satisfy the demands of a young and tech-savvy generation of mobile users, the future market leaders in the mobile communications industry must:

- c) be able to deliver mobile communications devices that gives its owner unprecedented freedom in the customization and personalization of their mobile handset to fit and reflect their individual lifestyles
- d) develop new mobile communications devices that support the tremendous variety of features and applications that can be found in the PC and on the World Wide Web.

To effectively seize this market opportunity, a new generation of mobile communications devices will need to be developed that combines the power and performance of a small PC computer with the price and portability of a mobile phone.

## **D. Seizing the Opportunity**

With a firm belief that the mobile phone industry is destined to evolve in ways similar to the evolution of the PC industry during the 1980's and 1990's, Neonode's two founders – Magnus Goertz and Thomas Eriksson – sat down to analyze and identify the technology, market focus, core competencies and competitive advantages needed to seize a leadership position in a rapidly emerging industry. Magnus' and Thomas' research led to the definition of four fundamental principles upon which Neonode will build a new generation of mobile handsets to effectively seize the current market opportunity.

### **Technology**

By focusing on the User Experience and providing an intuitive and versatile User Interface to an open system architecture, Neonode can become the "market enabler" that provides the tools and a common framework for software developers, hardware manufacturers and service providers alike to develop new end-user applications and solutions that will better serve the customer's individual needs and drive market growth.

### **Market Focus**

By focusing on serving the needs of a specific market segment and developing a close dialogue with the end-users, Neonode can gain the exceptional market understanding needed to build brand loyalty and develop new products and services that effectively meet customer's expectations.

### **Core Competencies**

By focusing on the company's core competencies in open architectural design, exceptional market understanding and strong alliances and partnerships with leading technology suppliers and service providers, Neonode can focus on building and developing the customer relations and brand loyalty needed to reach a market leadership position.

### **Competitive Advantages**

As an industry moves away from attempting to integrate the whole value chain with proprietary solutions to a higher degree of specialization in developing value-adding hardware, software and services under a common open architectural framework, new industry players will emerge to seize market-leading positions. With an exceptional understanding of the market and a clear focus on integrating and delivering "best of breed" technology and services to build brand loyalty, Neonode can seize a market-leading position by becoming a "market enabler" in a specific target market segment that provide industry players with the tools and architectural design needed to add value to a carefully targeted segment of end-users.

## **E. Vision**

Neonode will seek a market leadership position by leading the development of the next generation of mobile communication devices that combines the power and performance of a small PC with the price and portability of a mobile phone.

Neonode will leverage its core competences in architectural design, exceptional market understanding and strong industry alliances and partnerships to become the leading brand and premier supplier of state-of-the-art mobile handsets to teenagers and young adults, aged 13 – 25, by 2007.

## III. Company

### A. Introduction

During the summer of 2000, Magnus Goertz and Thomas Eriksson began the development of a new mobile communications device that would be based on the four core principles they had defined for a company to reach a market leadership position.

#### **Technology**

By using the Microsoft CE.NET platform as the operating system in a mobile phone, together with Neonode's own intuitive and versatile User Interface, Neonode can provide hardware manufacturers, software developers and service providers alike with the tools and the architectural framework needed to develop new features, applications and services in an environment they are already familiar with from the PC industry.

#### **Market Focus**

By focusing on serving the needs of teenagers and young adults, aged 13-25, Neonode will be able to tap into a very large and active market segment, inadequately served by other players in the mobile communications industry, that has a in-depth understanding of and extensive experience in using both PC technology and the World Wide Web. By providing this market segment with the first mobile handsets that truly enables an unprecedented degree of personalization and seamless integration between the PC and the World Wide Web, Neonode can get ahead – and stay ahead – of competitors by earning the recognition as the innovator that strives to meet their needs by breaking the barriers to true mobile freedom.

#### **Core Competencies**

By leveraging the company's core competencies - open architectural design, exceptional market understanding and strong alliances and partnerships - Neonode can focus on providing its customers with an exceptional User Experience and the freedom to customize their mobile handsets with features, applications and services that fit their individual lifestyle.

#### **Competitive Advantage**

Neonode's competitive advantage lies in its "Market Enabling" role, i.e. to provide a majority of the industry players with the tools and the framework needed to be able to add value to the end-user by developing new features, applications and services. By giving customers an unprecedented degree of freedom to customize their mobile handset, the demand for new features and applications will create new opportunities that are expected to drive future market growth.

### B. Mission

Neonode's mission is to seek a market leadership position by leading the development and marketing of state-of-the-art mobile handsets that fully harness the power and potential of seamless integration between the mobile handset, the PC and the Internet.

Neonode will reach a market leadership position within five years by focusing on developing products that offer an unparalleled user experience, by acquiring an exceptional market understanding in a targeted market segment and by integrating "best of breed" technology to meet customer expectations.

## C. Important Milestones

|                |  |
|----------------|--|
| June 2000      | While working at RadioDesign, Magnus Goertz and Thomas Eriksson discusses trends in architectural designs of future mobile handsets and decide to make an in-depth analysis of the market and identify the opportunities in introducing a new type of mobile handset.  |
| September 2000 | Based on their research and analysis of the market, Magnus and Thomas decide to start a company together – Neonode - to begin the development of a new type of mobile handset. Neonode AB is founded and incorporated in October 2000.   |
| February 2001  | Magnus and Thomas leave their respective positions at RadioDesign AB to work full-time with their new venture and the development of their first prototype.  |
| March 2001     | Magnus and Thomas exhibit their first prototype, equipped with conventional Resistive Touch Screen Technology, at CeBIT in Hannover, Germany. Following discussions with potential suppliers, Magnus and Thomas decide to develop their own proprietary Touch Screen technology.   |
| October 2001   | The second prototype, with Neonode’s own “Movement-Sensitive Touch Screen” technology – NeoTouch - is completed and tested in-house.   |
| December 2001  | Neonode files a patent with the Swedish Patent and Trademark Office (PRV) for its NeoTouch® technology.  |
| March 2002     | Magnus and Thomas present Neonode’s third prototype at CeBit and receive massive attention from the industry and trade press.  |
| April 2002     | Neonode adds more features to its prototype and begin negotiations with potential industrial design partners.  |
| May 2002       | Swedish design company <i>No PicNic</i> is selected to finalize the design of Neonode’s first mobile handset – the N-1. A joint venture is created with No PicNic and Neonode.   |
| September 2002 | Neonode’s fourth prototype, with new components and a new mechanical design, is completed. Neonode files a second patent for its NeoTouch® technology and continue its development of a new, proprietary User Interface software.  |
| December 2002  | Neonode applies for a patent with the US Patent and Trademark Office for its new User Interface software - NeoShell®. The official launch of Neonode’s new web site at Fryshuset in Stockholm, together with a product showcase, gets massive TV and media coverage. Neonode receives thousands of pre-order requests for its first 1000 units of the N-1. |
| January 2003   | Over 15.000 pre-order requests registered through Neonode’s web site. Neonode recruits a Software Development Team from Microsoft to complete final development and testing of the software platform, as well as key personnel to fill key positions in marketing, IT and Logistics functions.   |
| May 2003       | Neonode intensify its search for new financial partners in order to secure financing to launch its first product in Europe.  |

## **D. Management**

Neonode's current management team comprises of talented and dedicated professionals with extensive experience in their respective fields and the complementary skills needed to manage and build a highly successful company.

### **Magnus Goertz, 34** **Managing Director, co-founder**

Magnus has extensive technical and entrepreneurial experience and is the founder of two other Swedish high-tech companies, *Rector AB* and *Brace AB*. Rector AB was a consultancy firm specialized in the design and development of Man-Machine Interface systems. Brace AB was a successful manufacturer of Thin-Client Network Computers. Following the sale of Brace AB in 2000 to Swedish technology company *RadioDesign AB*, Magnus worked as a Strategic Advisor at Radio Design's Business Innovation Department, prior to founding Neonode AB with Thomas Eriksson in October 2000.

### **Thomas Eriksson, 34** **Chief Technical Designer, co-founder**

Thomas holds a Master's Degree in Electrical Engineering from the Royal Institute of Technology (KTH) in Stockholm, Sweden. Thomas has over 15 years of experience in Product Design and Engineering. Prior to founding Neonode AB with Magnus, Thomas worked at Wireless Toys AB as a Founder/CTO, developing innovative products sold worldwide. At Neonode, Thomas currently supervises a team of 10 engineers in the development of N1.

### **Jonas Löfgren, 29** **Business & Partner Development Manager**

Jonas holds a Master of Science Degree in Physical Therapy and is currently completing his Executive MBA at the University of Gävle in Gävle, Sweden. Jonas has done extensive research in the area of Health Sciences prior to starting his own independent consultant company, specialized in Software Development and User Interface Design for the Health Sciences industry. At Neonode, Jonas supervises a team in the development of partnerships worldwide.

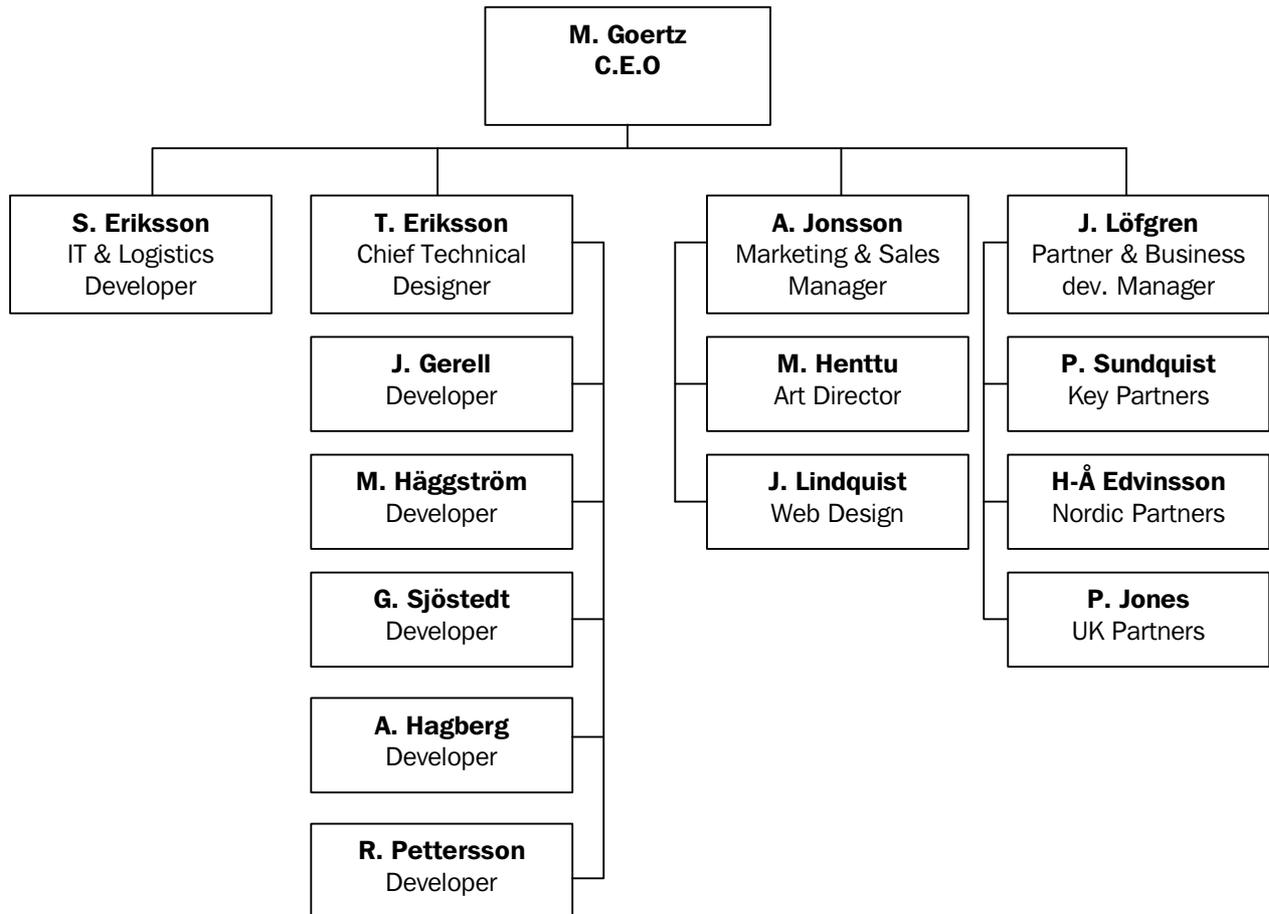
### **Alexandra Jansson, 28** **Marketing & Sales Manager**

Alexandra holds a Bachelor Degree in Business Administration from the University Federal of Uberlândia, Brazil and has completed additional courses in Marketing at the University of California in Berkeley, USA. Alexandra has several years of experience as a Strategic Marketing consultant and has gained wireless industry knowledge while working for Ericsson as a Marketing Communications Manager. At Neonode, Alexandra supervises a team in the development of the areas of marketing and sales.

## E. Organization

Neonode currently employs 14 people in four key areas - System Development, IT & Logistics, Marketing and Sales and Business Development.

Fig 1: Current Organization



## F. Alliances and Relationships

Neonode has developed a number of strategic partnerships and alliances to ensure access to the latest and most advanced technology and complementary skills and specialized knowledge to effectively take the products to market. These partners include:

### MICROSOFT

Neonode is one of five companies that have been accredited OEM Partner status at Microsoft, which gives the company the right to develop CE.NET embedded phones and Stinger smart phones. Neonode is thus able to embed Microsoft products in any of its own products and has priority access to all beta version and technical documents.

#### SAMSUNG SEMICONDUCTOR

Neonode has a strategic alliance with Samsung Semiconductors in the development of TFT LCD Displays and low-power memories. Samsung customize their technology to our product platform, which ensures short lead-times and high quality components.

#### SANDISK

SanDisk is the inventors and manufacturer of the SD-Card (Secure Digital Card). The SD-Card is a solid-state mass storage technology used in MP3-players and digital cameras. Neonode has partnered with SanDisk in the development of their technology in mobile phones, which guarantees us preferred pricing and priority in testing the latest technology.

#### WAVECOM

Wavecom is the supplier of Neonode's GSM/GPRS network interface. Wavecom considers the N-1 to be the most interesting new product on the market and have agreed to actively collaborate in network testing and product qualification.

#### IV PLAST

IV Plast is one of the leading suppliers of plastic parts for the mobile industry in the Nordic region. IV Plast is a Norwegian Injection Mode tool manufacturer with a production facility in Sweden. Neonode has signed an exclusive production agreement for the first 200.000 units of the N-1 against their investing in the needed tools to produce the plastic parts the mobile handset.

#### ELEKTROMEKAN

Elektromekan is Neonode's production partner and one of the leading subcontractors in the Telecom Industry. Elektromekan has agreed to invest in a new production site and all necessary test equipment and procedures for the production of the N-1.

#### PRICEWATERHOUSECOOPERS

PriceWaterhouseCoopers handles the company's accounting.

#### HELLE & WESTERMARK

Helle & Westermarck provides legal council to the company in all matters related to Technology, Venture Capital and Growth.

#### GROTH & Co

GROTH & Co provides council and assistance in all issues related to patents and trademarks.

### **G. Board of Directors**

Neonode's Board of Directors currently consists of the company's two founders, Magnus Goertz and Thomas Eriksson. Neonode is actively searching for three to five highly experienced professionals with complementary skills and backgrounds, to strengthen the company's Board of Directors.

## **H. Advisory Board**

Neonode is fortunate to have a small, but very active advisory board with experienced professionals that assists the company and its management in this early development phase with support, advice and an extensive network of contacts:

### **Peter Helle**

Helle & Westermark Law Office

Prior to founding Helle & Westermark, a Swedish law firm specializing in advising domestic and international companies on legal issues concerning TVG (Technology, Venture Capital, and Growth), Peter Helle worked as a Senior Law Officer at Price WaterhouseCoopers and at Sweden's largest full-service law office, Lindahls. At Lindahls, Peter led the development of an innovative and comprehensive service line customized to meet the needs of high-growth clients.

### **Arne Engvall**

PriceWaterhouseCoopers

Arne Engvall is a Senior Accountant at PriceWaterhouse Coopers and has extensive experience in working with several Swedish technology companies in early stages of their development. Arne Engvall provides Neonode's management team with valuable guidance and know-how in corporate structure and development.

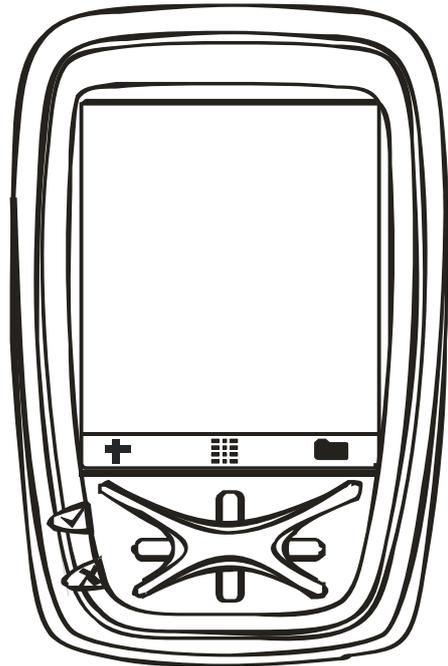
Neonode and its management team is actively searching to develop its network of experienced advisors with additional key competence in the fields of Telecom, Hardware and Software Development, Marketing, Finance and Organizational Development.

## IV. Products and Services

### A. Introduction

Neonode's first product, the N-1, is a credit card-sized, state-of-the-art mobile handset that represents a paradigm shift in mobile communications device design.

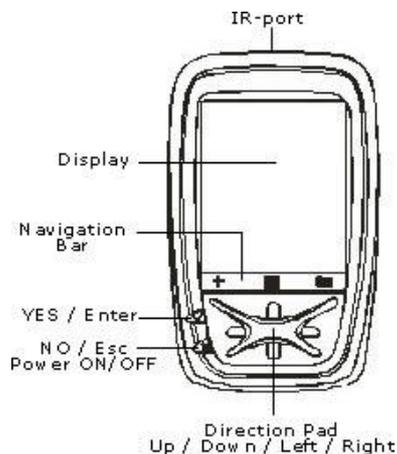
Equipped with a fast 100 MHz ARM-7 processor, 64Mb SD-RAM (upgradeable to 4Gb), Microsoft Windows CE.NET operating system and Neonode's own patent-pending NeoTouch® User Interface for intuitive, navigation and control and a USB-port for seamless integration with a PC and the World Wide Web, the N-1 offer end-users unprecedented freedom and endless possibilities to customize their mobile handset with features, applications and services that fit their lifestyle.



Neonode N-1 (natural size)

### B. Product Overview

Fig X: N-1 Front Panel



The Front Panel is dominated by a 2.2" TFT Touch Screen Display and features only three mechanical buttons:

- Direction Pad (Up/Down/Left/Right)
- YES / Enter
- NO / Esc / Power ON/OFF

The N-1 does not feature a mechanical keyboard – all major functions are managed directly on the Touch Screen Display.

Fig 2: N-1 Back Panel



The Back and Side Panels provides easy access to the N-1's many features, including:

- Built-in Camera
- External Access to SIM card
- Removable SD Memory Storage Card
- USB port for peripherals / battery charge
- Hifi Stereo Output
- Built-in loudspeaker

## 1. Product Features

The N-1 is a full-featured mobile handset that provides the end-user with all the latest mobile phone technology available on the market today:

- **Built-in Camera**  
The N-1 allows you to take digital pictures and send them to your friends using MMS or E-mail.
- **Personal Music Jukebox**  
You can listen to MP3-files in true HiFi stereo sound. With one gigabyte of memory, the N-1 can store the equivalent of up to 40 CD's for hours of listening to your favorite music.
- **Entertainment Center**  
With Microsoft Windows Media Player 7 installed, you can download movies and video clips from the Internet and view them directly on the N-1.
- **Personal Communication Device**  
The N-1 can work as your personal organizer and synchronize your contacts with MS Outlook on your PC, use Microsoft Internet Explorer to visit your favorite on-line community or chat board, and use Microsoft Outlook Express to send and receive e-mails.
- **Mobile Game Machine**  
With a 2,2" TFT display, a fast ARM processor, Windows CE.NET operating system and up to 4 gigabyte of memory storage, the N-1 is a very powerful pocket computer that can allow you to play your favorite PC games whilst on the move or at home.
- **PC and Web Connectivity**  
With an USB-cable, you can connect your N-1 to your PC to add or delete programs and games. You can also connect an external keyboard and a mouse to speed up your text editing, connect a wireless headset, a FM-radio, a GPS or simply charge the battery of your N-1 while surfing the web in search for new applications.

The N-1 not only offers the latest and most advanced features in mobile telephony technology – the N-1 is the natural mobile extension of the PC and the World Wide Web, giving the end-users the power, versatility and technical standards of a traditional PC, combined with the portability and accessibility of a mobile phone.

## 2. Complementary Services

The N-1 can be connected to a PC with a standard USB cable. Upon connection, the PC will automatically detect the N-1 and open a Desktop User Interface on the PC, offering the end-user a series of additional services, including:

### 1) Latest software and applications

By logging in on Neonode's secure web site, the end-user will be given access to the latest software and applications that can easily be downloaded and installed on the N-1

### 2) Maintenance

The Desktop User Interface offer end-users the possibility to easily add new applications, but also to update, delete and manage existing programs and files.

### 3) Support Service

A special support section on the web site allows the end-user to make an automated check-up on all main functionalities in the N-1. Whenever a software-based error is detected, an attempt to update the N-1 will be made to correct the error. If the error is fatal, or if there is a hardware problem that can't be resolved on-line, the customer is automatically given the needed guidance and instructions to send the damaged unit to the closest service shop for repair or exchange.

More complementary services are continuously being developed in-house and in close partnership with other companies, and will be made available on Neonode's web site on an on-going basis.

### 3. Value Proposition

The Neonode N-1 will be the most versatile, full-featured and powerful mobile handset available on the market, offering end-users unprecedented freedom and endless possibilities to customize their mobile handset to fit their lifestyle.

As a natural extension to a PC and the World Wide Web, the Neonode N-1's innovative design, exceptional user experience and state-of-the-art technology represents a paradigm shift in mobile communication, putting the end-user in control of the functionality of their mobile handset and creating a unified architectural platform and framework for software developers and service providers to develop new applications and services.

### C. Product Line Plans

Neonode's architectural design enables significantly reduced lead times to implement software and hardware changes that brings new and improved functionality and performance to Neonode's current and future mobile handsets.

Neonode has defined a tentative roadmap for software revisions and the development of new features for its future products:

#### **N-2** (Q1 '2004)

A revision of the N-1 platform to reduce power consumption and enable more features, including:

- SDIO, to integrate new features, such as W-LAN and BlueTooth, on the storage card.
- Multi-Directional Camera w/ 1.3M pixel resolution
- Increased CPU performance, enabling Video Recording
- Reduced size with fewer, price-optimized components

#### **N-3** (Q3 '2004)

A revision of the N-1 platform to enable more features, reduce power consumption and enable more features, including:

- WCDMA/TDD (3G)
- Integrated W-LAN and optional IP Telephony
- Multi-Directional Camera w/ 3.2M pixel resolution
- Video conferencing
- Shock-proof and water-resistant

#### **N-3D** (Q2 '2005)

A revision of the N-1 platform to enable more features, reduce power consumption and enable more features, including:

- 3D-accelerated platform for goggle technology and virtual reality applications

#### **N-4** (Q4 '2005)

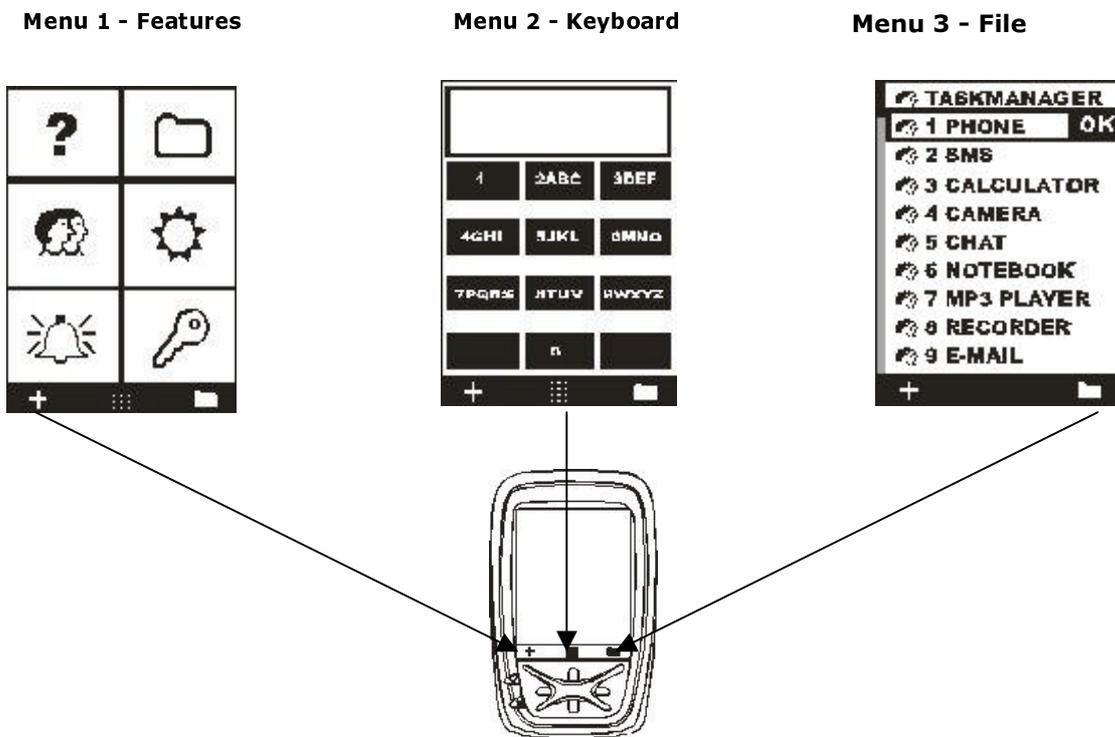
- Voice Recognition and Speech Synthesis to enable hands-free applications

## D. Technology Overview

### 1. User Interface

Neonode has developed a proprietary technology, NeoShell®, to give the N-1 an intuitive, versatile and powerful Graphic User Interface (GUI) for easy navigation and control.

The NeoShell® User Interface consists of three primary menus, directly accessible from the navigation bar located at the bottom of the Movement-Sensitive Touch Screen Display:



#### Menu 1 – Features

The Feature Menu provides easy access to all the functionality available in a specific application.

#### Menu 2 – Keyboard

The Keyboard menu replaces the mechanical keyboard on ordinary mobile phones and enables swift data entry and text editing.

#### Menu 3 – File Manager

The File Manager gives easy and immediate access to all applications available in the handset.

NeoShell® has been designed to give the end-user the freedom to operate the mobile handset with only one hand. All applications, files and functionality are activated, operated and terminated by a simple touch or thumb-slide on the Movement-Sensitive Touch Screen, or by pushing one of the two buttons or the direction pad below.

This unique, proprietary solution eliminates the need for a separate stylus pen or use of both hands to operate the N-1.

## **2. Operating System**

Neonode has chosen Microsoft CE.NET as the operating system for its mobile handsets. CE.NET is Microsoft's latest and most sophisticated operating system and a key component in their .NET strategy, where Internet content is connected with handheld devices through standardized channels.

CE.NET support C#, a clone of SUN's popular Java technology, already widely accepted in stationary devices and likely to become a standard programming language in the future.

Neonode is the first mobile handset manufacturer that fully enables the end-user to harness the power of Microsoft's .NET strategy, which will allow for rapid development of new applications and secure interoperability with other systems.

## **3. Hardware Components**

Neonode has chosen to partner with the world's leading manufacturers and suppliers of mobile communication hardware components to develop its state-of-the-art handsets, including companies such as Samsung Semiconductors, Wavecom, Epson and SanDisk.

Close partnerships and cooperation with the leading hardware and component manufacturers will ensure priority access, preferred pricing and rapid integration of the latest technology in Neonode's future products.

## **4. Applications**

Neonode does not develop applications in-house for its mobile handsets. Instead, Neonode has chosen to partner with leading software developers and supply them with the technical information needed to adapt their software to Neonode's architectural platform.

Neonode has also chosen to encourage smaller, independent software developers to create new applications that can be run on a Neonode mobile handset. By offering qualified developers a Software Development Kit (SDK), which includes an advanced emulator to program and test applications on Neonode's software platform, Neonode will actively assist developers in the development of new applications and functionality to Neonode's mobile handsets.

## **5. Proprietary Technology**

Neonode currently has three (3) different patent-pending proprietary technologies integrated in the N-1:

### **NeoTouch® Movement-Sensitive Touch Screen Technology**

- 1) A Optical Sensor Technology that uses light to determine the position of the finger on the Touch Screen
- 2) A design to enable the industrial manufacturing of Neonode's Movement-Sensitive Touch Screen Technology

### **NeoShell® Graphical User Interface**

- 3) An intuitive, versatile and powerful Graphical User Interface, i.e. a software that allows the end-user to take full advantage of the NeoTouch technology for easy and accurate navigation through menus and applications in the mobile handset.

## **E. Custom Contract Development**

### **1. Production and Packaging**

ELEKTROMEKAN is Neonode's production partner and one of the leading subcontractors in the Telecom Industry. As a production partner, Elektromekan will be responsible for:

- Component Storage and Inventory
- Circuit Assembly
- Software Installation
- Mechanical Assembly
- Testing and Quality Control
- Packaging
- Labeling - Customer Address and Shipping Information

Elektromekan has agreed to invest in a new production site and all necessary test equipment and procedures for the production of the N-1.

Furthermore, Neonode has taken the strategic decision not to carry a large inventory of finished products. Instead, Neonode is developing a "Just-in-Time" Order Processing System that will enable the order processing and manufacturing process to be fully automated, thus reducing lead times between orders and shipping to an absolute minimum.

Neonode has also initiated discussions with several other potential production partners located in Asia and Europe. When sales of Neonode products exceeds 5 000 units per month, new production partnership agreements will be entered in order to reduce unit production costs and serve local geographical markets.

### **2. Fulfillment**

Neonode will work with Swedish Postal Services to find optimal solutions for the shipping of Neonode products directly to the end-users, primarily in the Nordic countries and the rest of Europe.

Swedish Postal Services will pick up all shippable products at Elektromekan's production facility on a daily basis.

The customer will in the near future have the added option to request other delivery services, such as DHL, for premium-priced over-night delivery.

### **3. Service and Support**

Neonode has partnered with the ANOVO Group, one of Europe's leading full-service houses, to administrate and manage all after sales services and customer support through its international network of call centers and repair shops.

Neonode also intends to develop a sophisticated extranet solution, in close collaboration with ANOVO, to enable the development of a shared FAQ/Information Database and a fully automated, web-based support service, allowing end-users to have their mobile handset software and hardware tested over the Internet.

## **F. Research & Development**

Neonode's Product Management Team will be responsible for gathering all the Market Intelligence necessary to ensure that the development of new mobile handsets is based on the company's exceptional market understanding and that all products incorporate "best-of-breed" technology.

The Product Management team, located at Neonode's corporate headquarters, will be comprised of highly accomplished individuals with extensive experience in Product Management, Consumer Marketing, Sales, Application Development and Technical Design.

Neonode's corporate Intranet will serve as a Market Intelligence Information System, where all relevant data and information from relevant market research activities in key geographical markets will be centralized.

Neonode will also have Market Intelligence staff present in all key geographical markets, reporting directly to the Product Management, to ensure that Neonode possesses the latest and most up-to-date information on its local customers.

The Product Management will use the Market Intelligence Information System as the primary tool for monitoring the latest customer and technology trends, and make the technical specifications needed for the Product Development Team to design state-of-the-art

## V. MARKET STRATEGY

### A. Market Analysis

#### 1. Market Size

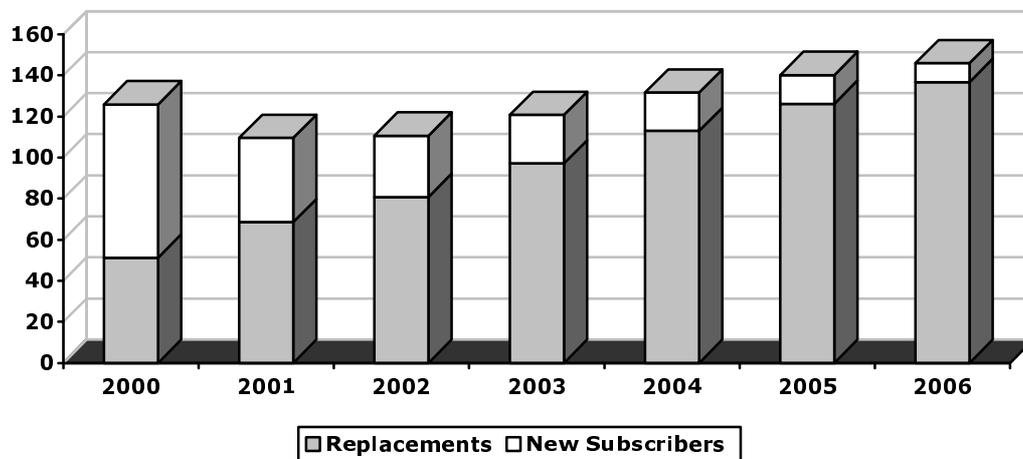
From 1997 to 2002, the European Mobile Telephony market has grown with over 550% to reach over 285 million subscribers<sup>3</sup>. Nearly 80% of the current subscriber base can be found in five countries: Germany, Italy, United Kingdom, France and Spain.

**Fig 1. European Mobile Telephony subscriptions by Country (March 2002)<sup>4</sup>**

| Country         | Subscriptions<br>(in millions) | Percentage<br>of population | Annual Growth<br>(2002) |
|-----------------|--------------------------------|-----------------------------|-------------------------|
| Germany         | 53,411                         | 64,5%                       | +1,0%                   |
| Italy           | 49,953                         | 86,7%                       | +12,3%                  |
| United Kingdom  | 46,296                         | 77,8%                       | +6,2%                   |
| France          | 37,309                         | 62,0%                       | +22,1%                  |
| Spain           | 29,875                         | 74,7%                       | +17,2%                  |
| Netherlands     | 11,916                         | 75,0%                       | +6,0%                   |
| Portugal        | 8,554                          | 85,1%                       | +19,9%                  |
| Greece          | 7,527                          | 71,0%                       | +17,9%                  |
| Sweden          | 7,413                          | 83,5%                       | +11,3%                  |
| Belgium         | 7,137                          | 69,7%                       | +13,0%                  |
| Austria         | 6,375                          | 78,3%                       | +3,8%                   |
| Switzerland     | 5,476                          | 75,4%                       | +13,6%                  |
| Finland         | 4,295                          | 83,1%                       | +11,9%                  |
| Denmark         | 3,610                          | 67,6%                       | +4,3%                   |
| Norway          | 3,398                          | 75,8%                       | +2,5%                   |
| Ireland         | 2,980                          | 78,5%                       | +15,1%                  |
| Other Countries | 1,508                          | 66,6%                       | +40,4%                  |
| <b>Total:</b>   | <b>287,033</b>                 | <b>73,3%</b>                | <b>+10,4%</b>           |

Sales of Mobile Handsets in Europe have been estimated to 110,1 million units in 2002. The majority of mobile handsets sold in Europe today are sold to existing subscribers as replacements, a trend which is expected to become even more predominant over the next five years<sup>5</sup>.

**Fig 2. Sales Forecast of Mobile Handsets in Europe (in millions of units)**



<sup>3</sup> Idate, European Commission, 2002

<sup>4</sup> Baskerville, Global Mobile and ART - March 2002

<sup>5</sup> Strategy Analytics, June 2002

## 2. Market Growth

The European market for Mobile Handsets is expected to continue to grow over the next five years, but at a much less dramatic rate than during the past five years.

**Fig 3. Expected Market Growth - Mobile Handsets in Europe 2002-2006<sup>6</sup>.**

| <b>European Market</b>   | <b>2002</b> | <b>2003</b> | <b>2004</b> | <b>2005</b> | <b>2006</b> |
|--------------------------|-------------|-------------|-------------|-------------|-------------|
| Units sold (in millions) | 110,1       | 120,7       | 131,7       | 140,2       | 145,9       |
| Forecasted Annual Growth | 9,6%        | 9,1%        | 6,4%        | 4%          | 1,5%        |

The continued growth and higher replacement frequency of mobile handsets in the European Market is primarily driven by two forces:

1. New Technology
2. Value-Added Services.

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<sup>6</sup> Strategy Analytics, June 2002

### 3. Target Market

Neonode will primarily focus on serving the needs of one specific user segment – teenagers and young adults between the age of 13 and 25, also known as the *Generation Y*.

The term *Generation Y* was coined to describe a generation of teenagers and young adults, born between 1979 and 1994. The number of children born during these 15 years has been estimated to 60 million in the U.S alone, which is three times the size of the *Generation X* and the biggest new generation of consumers since the baby boomers.

Although the *Generation Y* is a far less homogenous group of consumers than previous generations, such as the baby boomers, recent reports indicate that many of them do share a certain number of general characteristics<sup>7</sup>:

- They are racially and ethnically diverse
- Raised in dual-income and single-parent families, they have a distinctly practical world view and have already been given a considerable financial responsibility
- They are willing and able to spend money on fashion, entertainment, music and films
- At a young age, they are already sophisticated and seasoned consumers
- They are more concerned and less cynical about social issues and actively demonstrate support for those less fortunate, the environment, animal rights and other social issues.
- Growing up in a media-saturated, high-speed information age, they respond to ads differently and they prefer to encounter these ads in different places - they can switch their loyalty to a given brand in an instant in favor of those who are ahead on the style curve
- Their primary medium of choice is the Internet, not the TV (“TV drives passive homogeneity, the Internet drives active diversity”)
- They are quick to adopt new technologies and services, such as the PC and the World Wide Web, that enable them to communicate, play and interact with others

Neonode has chosen to serve this market segment for the following reasons;

- They have an interest in learning new technologies
- They are using computers and access the World Wide Web on a close to daily basis
- 65% of consumers aged 16 to 24 are used to buy CDs, books, hardware, software and tickets through the World Wide Web<sup>8</sup>.
- They are willing and able to spend up to 13,6% of their disposable income on mobile products and services<sup>9</sup>.
- They consider their mobile phone to be a fashion item and frequently upgrade or replace their mobile phones to gain access to the latest and most advanced technology and features
- They drive market demand for new mobile products and services

The unique features of Neonode’s current and future products have and will be specifically designed to meet the demands of this sophisticated and tech-savvy market segment that is not being adequately served by other industry players.

<sup>7</sup> “The Teens Market Report”, Business Week ([www.businessweek.com/1999/99\\_07/b3616001.htm](http://www.businessweek.com/1999/99_07/b3616001.htm))

<sup>8</sup> MTV Survey: “Planet Youth – en guide till dagens unga generation”, 2000

<sup>9</sup> Mobile Youth 2003, W2 Forum

#### 4. Customer Buying Criteria

Teenagers and young adults tend to view computers and mobile phones in very similar ways that previous generations viewed cars and hotrods - they constantly compare features and styling with their friends and exchange information on how to get a hold of the latest and greatest hardware, software, services and content.

Based on a recent Neonode survey among 340 teenagers in six different high schools in the Stockholm area, performed in close collaboration with students from the Royal Institute of Technology (KTH), the following features were considered the most important when buying a new mobile phone:

- Design (size, weight, color)
- Camera (the possibility to take pictures and create a personal photo album)
- Color Display/Screen
- Price
- Personalization (the freedom to decide which applications they want to have in their mobile phone)
- Entertainment (to be able to see small video clips or listen to music in MP3-format)

A common opinion shared by a majority of the surveyed group of teenagers where that the mobile phone had a key role in their daily interaction with friends and that the mobile phone would likely be of *even greater importance* if new services and applications, such as multi-player games and chats that are readily available on PC's and the World Wide Web, would become available or accessible from the mobile phone.

#### 5. Trends

Other research reports indicate that the brand is beginning to play a more important role when choosing to upgrade or replace a mobile phone. According to Neonode's own survey and more general research on brand loyalty, teenagers are indeed very sensitive and attracted to brands that represent a new trend or a specific aspect of a lifestyle, but they have shown little or no signs of long-term brand loyalty.

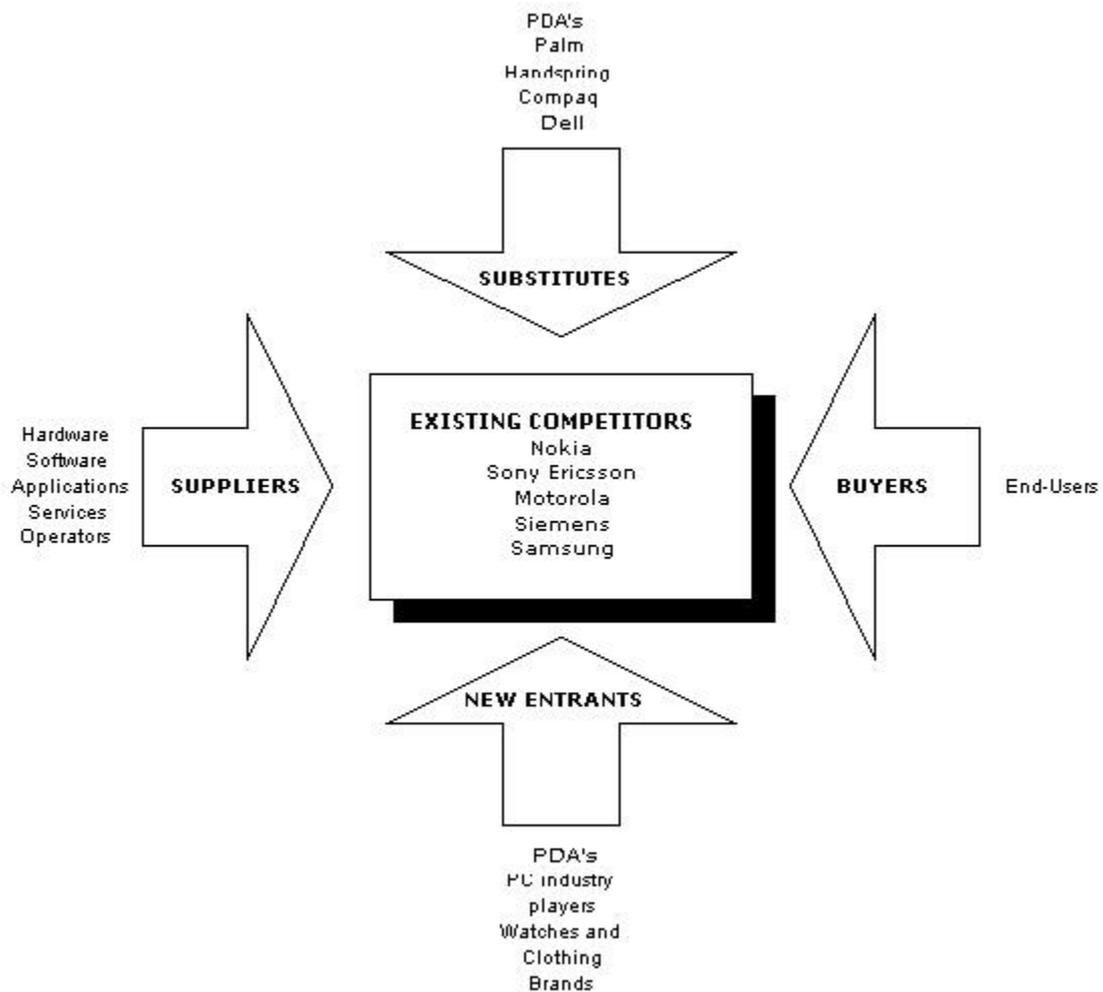
Most importantly, they do not generally like the so-called "big brands" often deemed anonymous and prefer to select a unique combination of different brands that they feel accurately reflect their own identity, personality and group belonging.

In this sense, the brand does indeed play a pivotal role in the life, consumer habits and buying criteria of teenagers and young adults - but the building of a brand and the influence it has on a given set of consumers does not follow the generally accepted patterns and principles taught in traditional marketing and advertising books. In order to get the attention of this new generation of savvy consumers, companies have to "find and follow" them and use new, innovative and non-intrusive ways to meet and serve their customers.

Neonode will proactively seek to stay abreast of the latest trends and shifts in their customer's needs and desires by ensuring that the Marketing and Product Management teams continuously strive to develop a close dialogue and relationship with customers through its web site, through extensive research with key strategic partners and by participating in and sponsoring events that attract significant number of current and future Neonode customers.

## B. Competitive Analysis

In order to make a comprehensive competitive analysis of the market environment in which Neonode will seek a leadership position in, Neonode uses Michael Porter's model for Five Forces, as illustrated below.

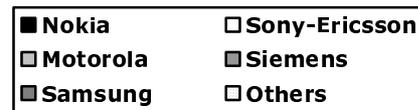
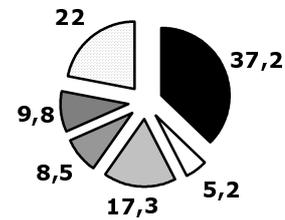


**Fig X: Competitive Overview using Michael Porters model of Five Forces**

## 1. Existing Competitors

Today's leading manufacturers of mobile handsets consist of a small group of large players. They have all developed their own proprietary solutions and their respective market share has not changed significantly during the last few years.

None of these players focus on one exclusive market segment – they have developed product lines that cover a wide range of product, from low-end to high-end, targeting both younger and older customers.



Several attempts to segment the market and develop handsets specifically for teenagers or young adults have not been very successful.

## 2. Suppliers

All major mobile phone manufacturers were originally developing every aspect of the mobile phone's operating system and functionality in-house, while buying the components from specialized component manufacturers.

But, much like the evolution in the PC industry during the 1980's, the mobile industry is beginning to shift towards a greater degree of specialization in hardware, software and applications:

### HARDWARE

There are a growing number of specialized hardware suppliers on the market, but the demand for the most sought-after components and items remain extremely high, and demand often exceeds supply. With a future emergence of a dominant design, it is likely that the degree of specialization will increase further, which will better balance supply and demand in the market and lower the price of hardware and components.

### OPERATING SYSTEM / SOFTWARE

As the features of mobile phones is getting increasingly advanced and complex, their architectural design and functionality tend to become more and more similar to a personal computer.

At present, there are two major operating systems for advanced mobile phones – the Symbian OS and the Microsoft Windows CE. Both these operating systems were originally developed for low-end, portable computers and have been adapted to work in mobile phones through special User Interfaces, also known as platforms or shells.

Both operating systems offer shells that can support either keyboard or touch screen data input. Symbian OS offers two different shells, developed by Nokia and UIQ. Windows CE offers only one shell for touch screen input – the Microsoft SmartPhone platform. Neonode has made the strategic choice to develop their own patent-pending shell - Neoshell® - to further optimize navigation, access and application management on the Windows CE.NET operating system.

## APPLICATIONS / SERVICES

The ongoing industry specialization in hardware and software development has also had an impact on application and service provisioning. The industry is moving away from server-based text services/applications (such as WAO) and towards two different types of solutions:

- 1) applications that are installed in the same way as they are on a PC
- 2) graphical or text-based services and applications that are run in a similar way as in a web browser

Both these solutions are paving the way for the migration of PC-based applications to the mobile phones and enabling companies with extensive experience and expertise from the PC industry to develop new applications that can be run in a mobile phone.

Neonode will initially focus on enabling a wide variety of applications to be installed through the connection with a PC, thus eliminating the need to wait for operators to upgrade their networks.

## OPERATORS

Mobile handsets are at present entirely dependent on operator's cellular networks and should be viewed as one of the most powerful supplier of infrastructure, even if recent technological development (such as W-LAN 802.11 hot spots and IP-telephony) may change this in a near future.

All major operators subsidize the consumer price on mobile handsets by locking in their customers in different service plans and are usually close partners to the major equipment manufacturers, either through equity ownership or through strategic alliances.

Neonode will seek all necessary approvals to enable their phones to work in any cellular network and enable them to deliver all current and future services that an operator may propose its customers. Neonode will also seek partnerships with operators that will result in offers of subsidized handsets.

### **3. Substitutes**

There are a few substitute products that would like to take an active role in the future development of the mobile communications industry, such as Palm, Pocket PC, RIM Blackberry, etc). The definition of a mobile handset is rather non-specific and most actual and potential substitutes will be called mobile handsets and classified as "new entrants".

The convergence of a variety of different technologies will enable mobile phones to integrate functionality from other products, such as digital cameras and MP3 players. On the other side of the spectrum, PDA manufacturers are concurrently seeking to integrate mobile phone technology to enable their customers to use their products in cellular networks.

Neonode first product, the N-1, will offer its customer an unprecedented number of features and applications in its mobile handsets that offer the same functionality as a large number of separate products and devices, such as an MP3-players and digital cameras.

## C. Competitive Strategy

### 1. SWOT Analysis

| Strengths                                     |  | Weaknesses                              |  |
|---|--|---|--|
| High competence, motivated personnel          |  | New player                              |  |
| Product with technical advance                |  | Small player on a big market            |  |
| Patent-pending value-adding technology        |  | Unknown brand                           |  |
| Market-driven technology                      |  |   |  |
| Small, flexible player – close to the market  |  |   |  |
| Exclusive focus on serving one market segment |  |   |  |
| No investments in proprietary technology      |  |   |  |
| Not locked in network infrastructure          |  |   |  |
| Partnership with Microsoft                    |  |   |  |
|   |  |   |  |
| Opportunities                                 |  | Threats                                 |  |
| A large market                                |  | Unstable, early-stage development phase |  |
| Innovative product with market potential      |  | Low financial endurance                 |  |
| High margin due to low R&D expenditures       |  | A rapidly changing market               |  |
|   |  |   |  |
|   |  |   |  |
|   |  |   |  |

### 2. SWOT Strategies

Neonode has developed a set of strategies to compensate its weaknesses and leverage its strengths to seize the opportunities and manage the threats in the market.

#### STRENGTHS vs. OPPORTUNITIES STRATEGY

A close collaboration and partnership with Microsoft is an important strength that opens up a lot of opportunities. Microsoft's successful history in different markets, coupled with their financial power and a vast community of application developers will help Neonode attract both new partners and new customers.

In an industry characterized by proprietary solutions and where no dominant design has emerged, studies indicate that new companies that focus on architectural innovation and entering carefully targeted emerging markets are more likely to succeed than companies that enters markets with component-level technological innovation in established markets<sup>10</sup>.

#### WEAKNESSES vs. OPPORTUNITIES STRATEGY

Neonode's open software platform will be beneficial for hardware, software and applications developers and operators alike.

Without any significant investments in proprietary technologies, Neonode does not have to choose side in their choice of technology (Windows CE vs. Symbian OS, CDMA2000 vs. WCDMA). Neonode's flexibility and independent position will enable a great number of different companies to join us in our development of new, state-of-the-art mobile handsets.

Neonode can take advantage of its rebel-like approach to the market and gain rapid acceptance and appreciation from teenagers and young adults.

<sup>10</sup> Cristensen, Suarez, Utterback – "Strategies for Survival in fast-changing Industries, Management Science, Vol. 44, No 12, Part 2 of 2, December 1998

## STRENGTHS vs. THREATS STRATEGY

Neonode's small size and carefully targeted market segment allows the company to quickly adapt to market changes. Without extensive R&D investments in a given technology, we can integrate the most widely accepted technology (No SMS, MMS or WAP gateways) and support the development of new technologies, such as W-LAN and TDD.

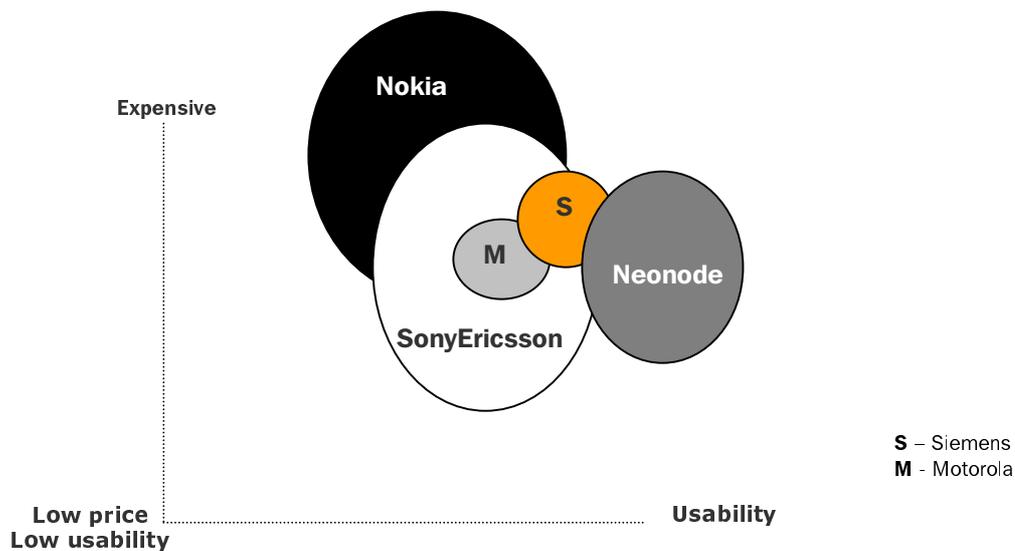
## WEAKNESSES vs. THREATS STRATEGY

We can leverage our limited financial endurance by leveraging our exceptional market understanding and experience of the World Wide Web to attract a critical mass of new customers without massive, multi-million dollar image-building campaigns.

## D. Marketing Strategy

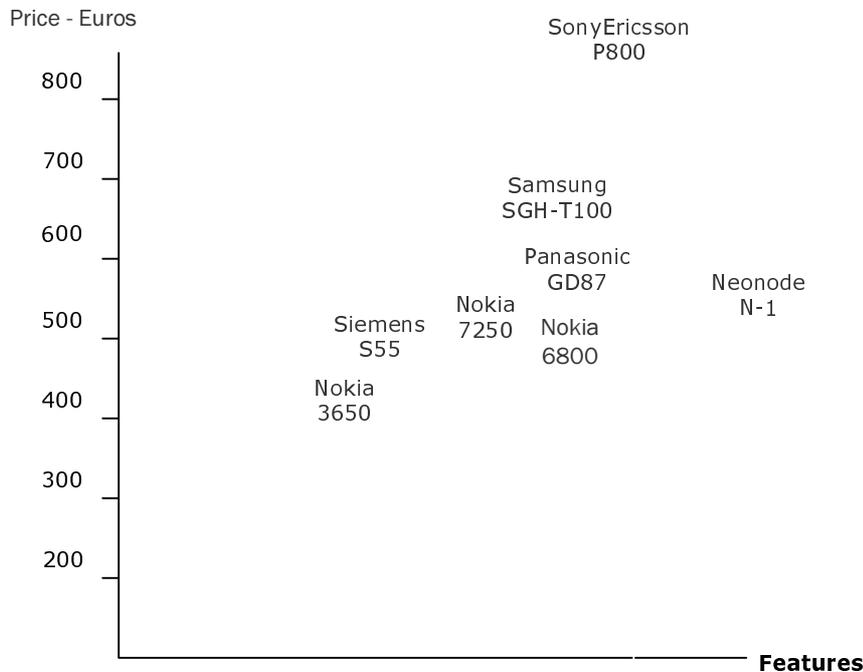
### 1. Strategic Positioning

Neonode will position itself as a company that is capable of developing feature-rich, state-of-the-art mobile phones at price/functionality-ratio previously unmatched by existing competitors.



## 2. Product Positioning

Below is chart illustrating Neonode's first product, the N-1, and how it is positioned against existing competing products with respect to price and features.



## E. Sales Strategy

### 1. Web Strategy

Neonode has taken the strategic decision to sell all of its mobile handsets exclusively through their web site on the World Wide Web, like many other successful companies such as DELL Computers.

This choice of strategy is based on the following key priorities:

- 1) Maximize customer's options to customize their handhelds to fit their own specific needs, with a wide selection of colors and features
- 2) Enable the development of an integrated "Just-in-Time Order Processing and Manufacturing System" to minimize inventory-related costs and enable delivery of products directly to the end-user within five (5) business days
- 3) Receive full payment for all products prior to assembly and delivery
- 4) Centralize all interaction with Neonode customers to one single location on the World Wide Web, where they can buy, update, upgrade and service their mobile handsets.
- 5) Build customer relations and brand loyalty by offering a high degree of interaction and a complete and up-to-date search engine to find the latest applications (Freeware, Shareware, demos and Applications) available for all Neonode handsets.

Neonode has had a very simple product presentation on-line for nearly six months now, including an interactive user forum, and the site already receives an average of 150.000 visitors per month – even though the company has yet to ship its first product.

The massive interest for Neonode's N-1 and its web site has so far resulted in over 16.000 pre-orders of the N-1 and over 8.000 registered members visiting the User Forum regularly to get the latest news and stay informed on the development of the products.

A new and updated web site will be launched simultaneously when Neonode's first product, the N-1, becomes available in Q3 2003. This new web site will comprise the following main sections:

#### COMPANY

Basic information about the company's mission, core values, career opportunities, history and contact information

#### PARTNERS

Presentation of Neonode's partners, FAQ, NeoLabel and contact information

#### PRESS ROOM

Latest information, Press Release archive, Photo Library, Media Kit, Product Presentations (PPT, PDF) and contact information

#### WEB SHOP

A full-featured web shop that offer new and prospective customers an extensive array of options to view all Neonode products and accessories available for sale. Customers will be given unprecedented liberty in customizing the styles and look of their mobile handset and choose between different secure payment options (Credit Card, Bank Account Transfer, etc).

The Web Shop will also be prepared for special extranet purposes to allow future Distribution partners to effectively manage and monitor their orders on-line.

The Web Shop Interface will be hosted by Swedish ISP *IT-Norr* and the Swedish Transaction Specialist *WALLIT* will manage all financial transactions in the Web Shop.

#### USER FORUM

A special section on the web site will be dedicated to providing all Neonode customers with an interactive tutorial, the latest software updates and a powerful search engine to find all applications (Freeware, Shareware, Demos and Applications) that are compatible with Neonode products and readily available for download.

The user forum can be accessed by logging in directly on the web site or by simply connecting a Neonode handset to the owner's PC using a standard USB-cable. Upon connection, a PC desktop interface will be opened automatically and invite the customer to log-in and gain access the member section, the user forum and all available software and applications.

## DEVELOPER'S CORNER

A special section on Neonode's web site will be dedicated to the many developers of new applications for all Neonode products. This section will feature an interactive on-line and off-line tutorial, a downloadable SDK (Standard Development Kit) in PDF-format, SDK software with an integrated Neonode Emulator to test new applications and all other relevant information and software needed to the rapid development of new applications.

Neonode will also host a series of special development conferences and contests and reward the best and most popular applications.

Neonode is developing the web site's design and all back-office functionality in-house, including integration with an ERP system and the "Just-in-Time" Order Processing and Manufacturing System.

## **2. Distribution Channels and Partners**

Neonode will partner with all major operators in selected key markets to package attractive offers consisting of subsidized handsets bundled with price-optimized subscriptions that fit teenagers and young adults.

However, Neonode has taken the strategic decision to not sell mobile handsets "over the counter" in retail stores. Instead, Neonode is currently in the process of evaluating the option of putting a special Neonode Product Stand in carefully selected retail outlets, thus allowing customers to test the Neonode and then place their order on-line by using a screen integrated in the product stand and directly connected to Neonode's extranet. This option could also give the customer the option to pay for the mobile phone in cash "over the counter", should they prefer this alternative to the standard secure payment methods available on-line.

## **G. Marketing Communications**

One of Neonode's core competencies is its exceptional market understanding and ability to communicate and build brand loyalty by using non-intrusive, non-traditional forms of communications, specifically adapted to fit their target segment.

Neonode's marketing mix will consist of five key components:

### **1. Advertising**

Neonode will be extremely careful and selective in choosing the right opportunity to advertise its products. Neonode will primarily seek joint advertising opportunities with partners that provide content and/or applications to the end-user.

Neonode is at present primarily interested in evaluating the ROI of product placement in movies and advertising integrated in PC games, which may prove to be a more effective alternative to traditional on-line and off-line advertising campaigns.

## **2. Events**

Neonode will be a very active participant and sponsor of different events that are expected to attract a significant number of actual or potential Neonode customers. These events will include sporting events, such as the X games and music festivals, such as the Swedish Hultsfredsfestivalen.

By being present with a stand at these type of events, Neonode will not only be able to display its products, but also interact and develop the relationship with the customers, which is critical to the future growth and success of Neonode.

## **3. Trade Shows, Conferences and Seminars**

Neonode will be present on all the major industry trade shows. However, the company will not be present at these shows to demonstrate products to end-users, but to serve the communities of developers that are developing new applications to Neonode's products.

Neonode will use their presence at major trade shows, such as Comdex in Las Vegas, USA and CeBIT in Hannover, Germany to host special developer's conferences and seminars. A close collaboration with thousands of application developers is also critical to Neonode's future growth and success.

## **4. Newsletters**

Neonode will develop a series of different newsletters to keep its respective stakeholders adequately informed on all relevant news and information:

- A quarterly newsletter destined to Neonode's PARTNERS
- A quarterly newsletter destined to Neonode's INVESTORS
- A monthly newsletter destined to Neonode's DEVELOPERS
- A monthly newsletter destined to REGISTERED NEONODE OWNERS
- A mailing list to send out special announcements to JOURNALISTS and PRESS SERVICES.

## **5. Promotion Partners**

Neonode will seek strategic partnership agreements and alliances with a wide variety of companies in different countries to communicate the Neonode brand through and together with them.

These partners will belong to one of two different categories:

### **NICHE PARTNERS**

Niche Partners are companies and individuals that have signed a contractual agreement to promote Neonode's products and brand through various means. This may include event organizers, entertainment companies, software and application developers and even individuals, such as carefully selected artists and athletes. Many of these partners will also provide applications and content to Neonode's web site and all of its products.

Neonode are currently in the process of negotiating its first Niche Partnership Agreements with three different companies.

#### CO-MARKETING PARTNERS

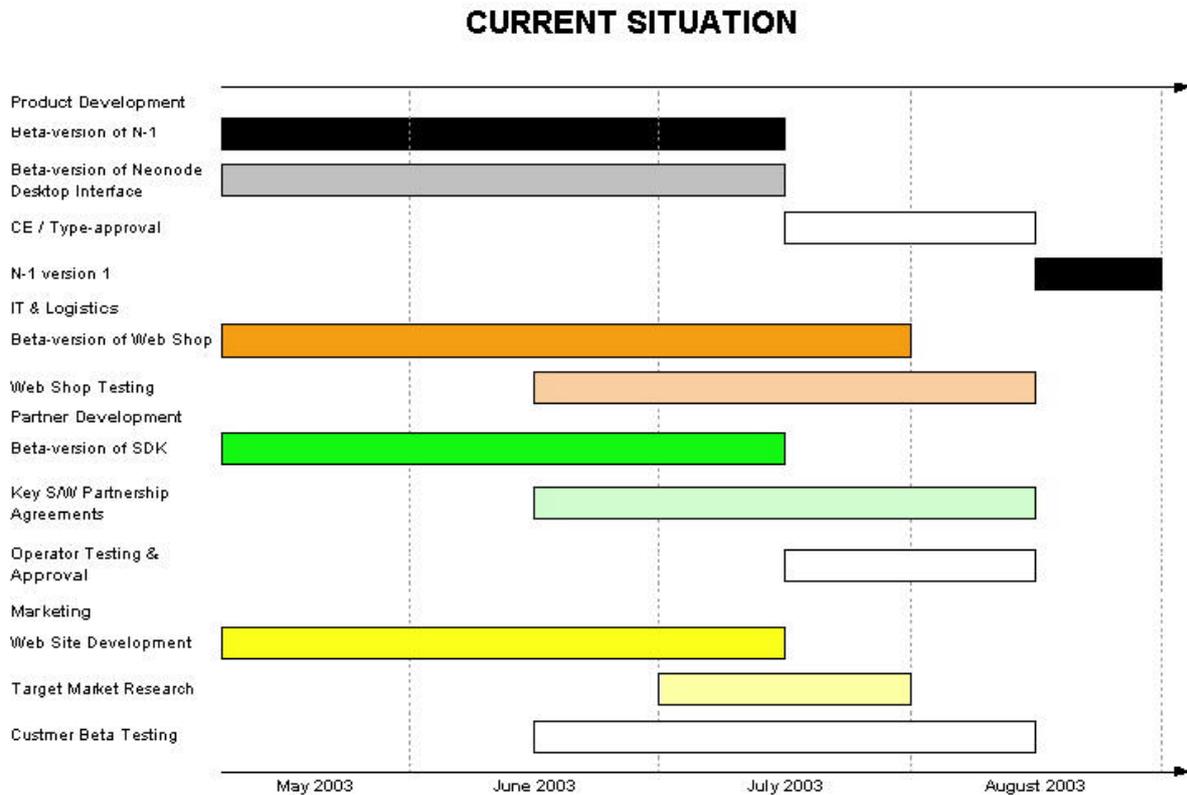
Companies with an exceptionally strong brand in the targeted market segment and that could benefit from joint marketing activities.

These partners may include online communities, such as Lunarstorm and Banana Island; content providers such as MusicBrigade or bigger brands, such as Nike, Adidas and H&M.

Neonode is currently negotiating its first Co-marketing partnership agreements with two companies in Sweden.

# VI. Action Plan

## A. Current Situation



### 1. Key Objectives

- Secure financing
- Complete development of company's first product, the N-1, and obtain necessary CE-/Type approvals
- Successfully test the N-1 in two operator networks – Vodafone and Tele2
- Sign first partnership contracts – Content (3), Applications (3) and Operators (2)
- Beta-test and launch N-1 (1000 units)

### 2. Organization

- Recruit 19 people to fill positions in Management, Product Development, Marketing, Sales and MIS (Total employees in August: 37)

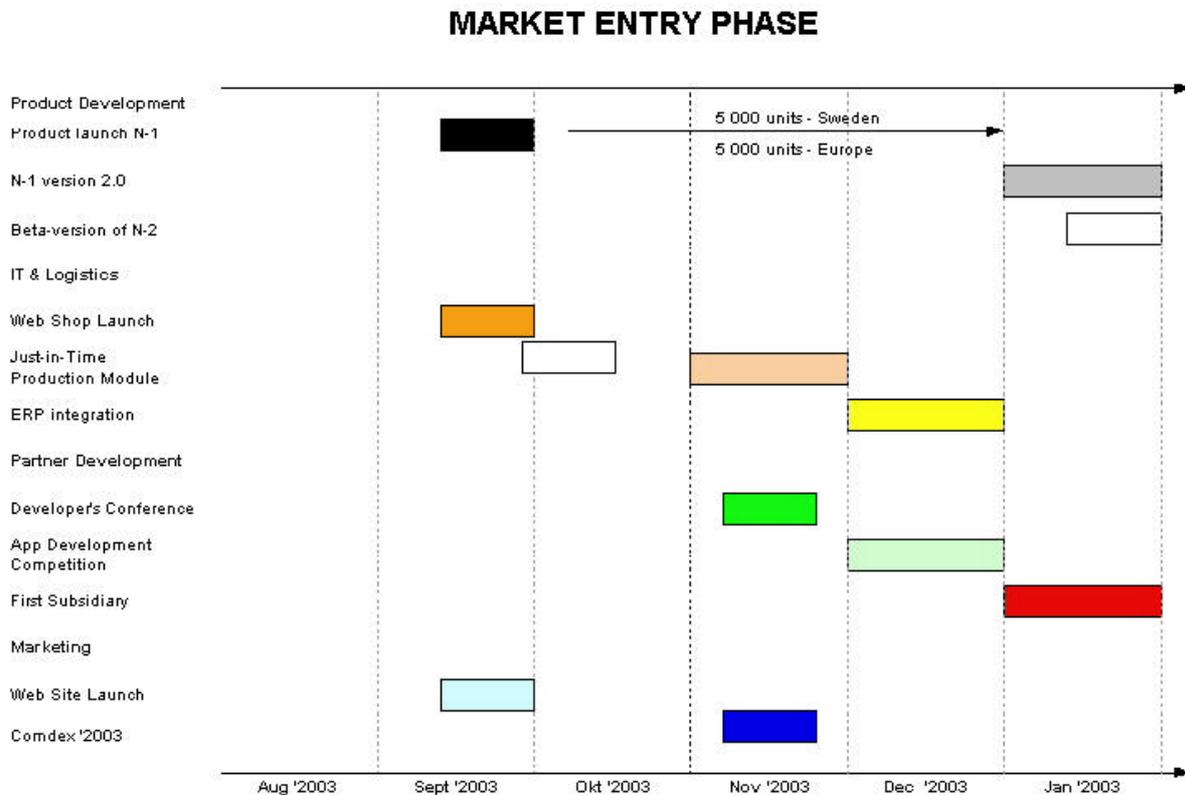
### 3. Critical Success Factors

- Funding secured in July 2003
- Product Development completed by mid-August

### 4. Risks

- Delays in securing first-round financing
- Delays in development of beta-version
- Difficulties in recruiting additional technical staff

## B. Market Entry Phase



### 1. Key Objectives

- Sell first 10 000 units in Sweden (5000) and Europe (5000)
- Complete MIS and Intranet Development, including ERP
- Organize first Neonode Developer's Conferences in Sweden and UK
- Sign strategic partnerships with European Operators (10) and Developers (10)
- Finalize expansion plan for 2004 – Europe and Asia
- Begin development of N-2 platform

### 2. Organization

- Recruit 15 people for Int'l Sales & Product Management positions and at least two Country Managers for int'l sales offices (Europe/Asia) (Total employees by year-end: 55+2)

### 3. Critical Success Factors

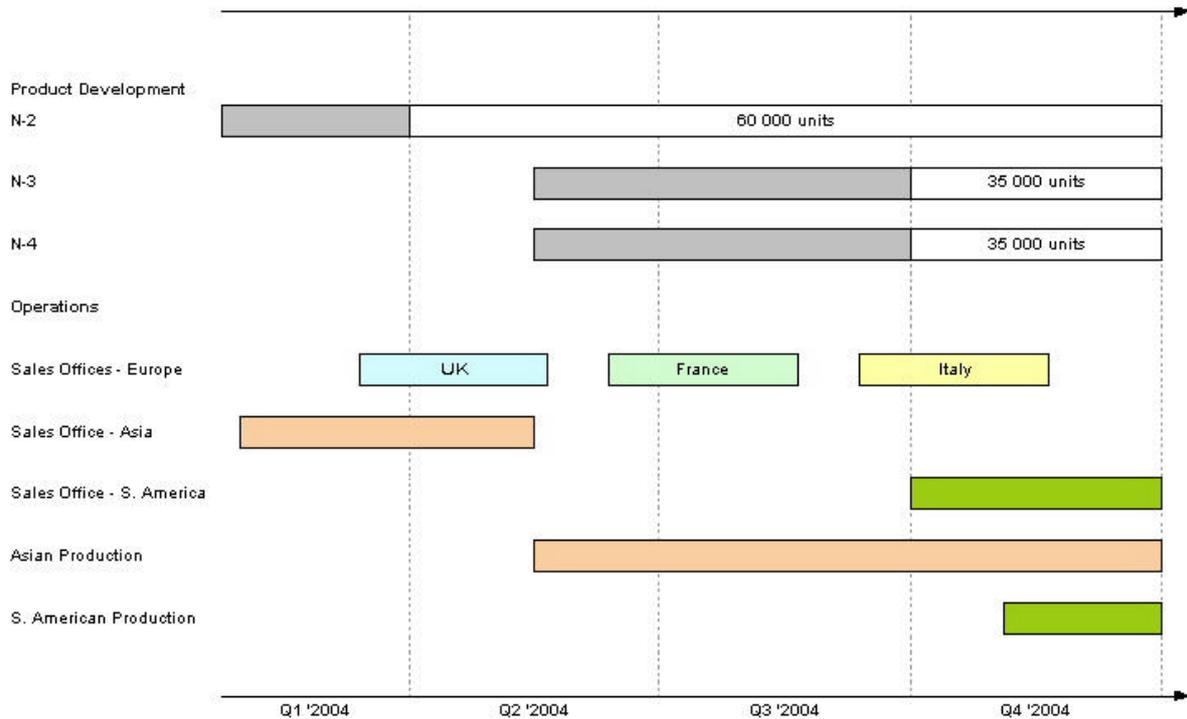
- Attain at least 75% of Sales Objectives (€ 3,5M) and sign at least 5+5 partners
- Complete MIS, Intranet and ERP Development

### 4. Risks

- Difficulties in recruiting key personnel
- Delays in closing key partnerships agreements
- Delays in Product Development which results in deferred Market Entry

## C. Market Penetration Phase

### MARKET PENETRATION PHASE



#### 1. Key Objectives

- Complete development and launch of three new models
- Begin international expansion and establish three new int'l sales offices
- Complete Market Intelligence System Development in Q2
- Finalize expansion plan for 2005 – Europe, Asia and South America
- Sell 180 000 units in Europe and Asia (€ 62M) and reach break-even (YTD)

#### 2. Organization

- Establish three sales offices in Europe + Asia and recruit Regional Manager for South America (Total employees by year-end: 90+30)

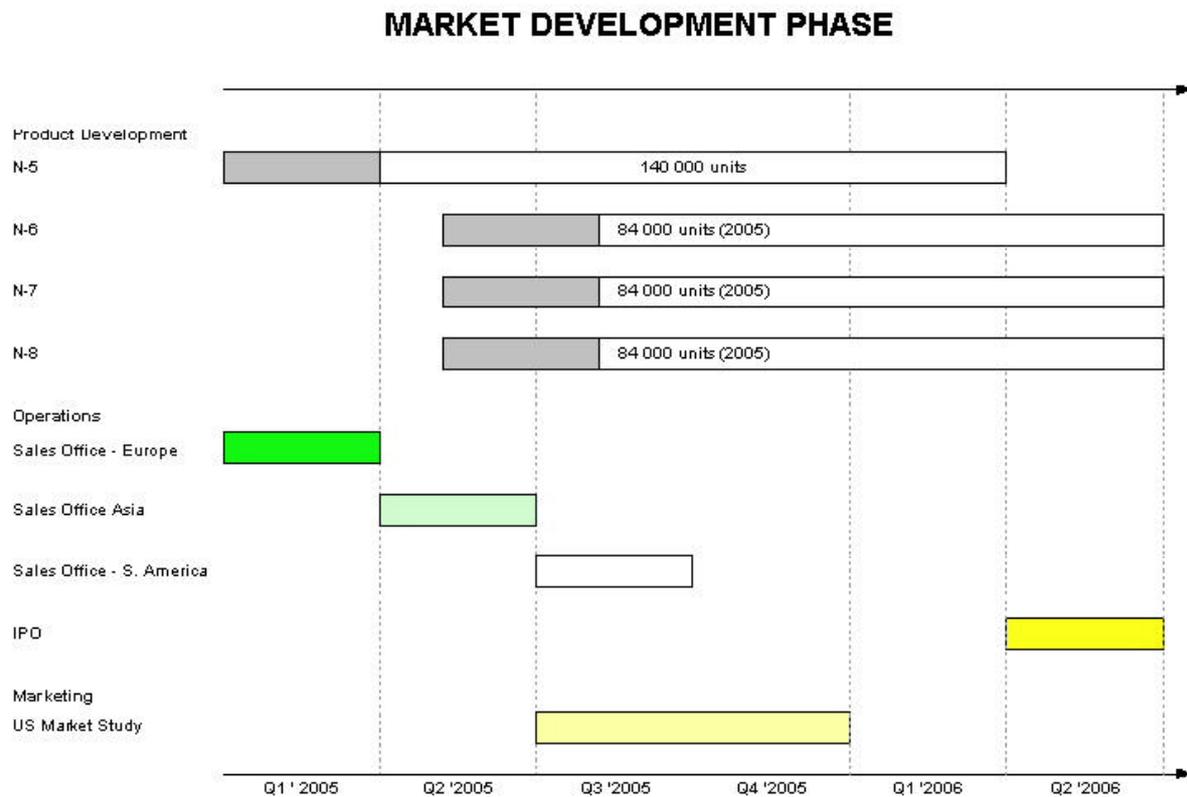
#### 3. Critical Success Factors

- Organization and MIS for International Expansion
- Critical mass of applications and strategic partnerships in key markets

#### 4. Risks

- Problems in getting sales offices operational within 90 days of establishment
- Slow growth in the development of new applications for Neonode products
- Challenges in developing company brand to attract new customers
- Slow int'l expansion and sales delays break-even

## D. Market Development Phase



### 1. Key Objectives

- Complete development and launch of three new models
- Continued international expansion in Europe, Asia and South America
- Transfer all production in Sweden to Asia and South America
- Sell 650 000 units in Europe and Asia (2005) and achieve six consecutive profitable quarters
- Initial Public Offering Q2 '2006
- Feasibility Study - US Market Entry

### 2. Organization

- Three additional sales offices in Europe, Asia and South America  
(Total employees by year-end 2005: 120+60)

### 3. Critical Success Factors

- Controlled expansion in key geographical markets
- Transfer production to Asia and South America

### 4. Risks

- Problems in transferring production to international facilities
- Uncontrolled international expansion
- Slow growth in South America

## VII. Finance

### A. Financial Summary

The company plans to launch its first product, the N-1, in the beginning of September 2003. The objective is to sell 10 000 units in Sweden and Europe before the end of the year.

The company will begin expand its operations in key select markets in Europe in 2004 and establish an Asian subsidiary to coordinate Production, Sales and Marketing activities in the region.

During 2005, the company will establish a subsidiary in Brazil to coordinate all activities in South America.

#### Projected Sales 2003 – 2005 (in Units)

| Region        | 2003          | 2004           | 2005           |
|---------------|---------------|----------------|----------------|
| Sweden        | 5 000         | 40 000         | 100 000        |
| Europe        | 5 000         | 60 000         | 150 000        |
| Asia          | -             | 80 000         | 250 000        |
| South America | -             | -              | 150 000        |
| <b>Total:</b> | <b>10 000</b> | <b>180 000</b> | <b>650 000</b> |

Projected Revenues from Sales during 2003 have been estimated to € 4,7M. In 2004, the company expects 45% of its revenues from sales to come from Asia.

#### Projected Revenues from Sales 2003 – 2005 (by region)

| Region               | 2003               | 2004                | 2005                 |
|----------------------|--------------------|---------------------|----------------------|
| <b>Sweden</b>        | € 1 950 000 (50%)  | € 12 600 000 (22%)  | € 28 000 000 (15%)   |
| <b>Europe</b>        | € 1 950 000 (50%)  | € 18 300 000 (32%)  | € 42 500 000 (23%)   |
| <b>Asia</b>          | -                  | € 25 500 000 (46%)  | € 74 800 000 (40%)   |
| <b>South America</b> | -                  | -                   | € 41 900 000 (22%)   |
| <b>Total:</b>        | <b>€ 3 900 000</b> | <b>€ 56 400 000</b> | <b>€ 187 200 000</b> |

The company is planning to develop eight (8) different mobile handset models based on the Neonode Platform over the next 24 months.

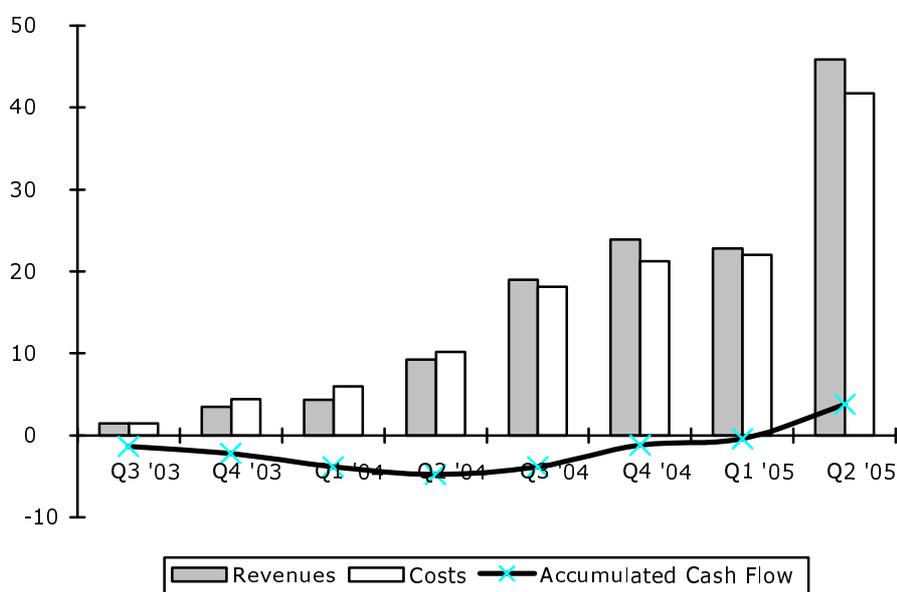
#### Unit Sales Objectives 2003 – 2005 (by Product)

| Product Model | 2003   | 2004   | 2005    |
|---------------|--------|--------|---------|
| <b>N-1</b>    | 10 000 | 48 500 | 0       |
| <b>N-2*</b>   | 0      | 60 500 | 19 000  |
| <b>N-3*</b>   | 0      | 35 500 | 98 000  |
| <b>N-4*</b>   | 0      | 35 500 | 141 500 |
| <b>N-5*</b>   | 0      | 0      | 140 500 |
| <b>N-6*</b>   | 0      | 0      | 84 000  |
| <b>N-7*</b>   | 0      | 0      | 84 000  |
| <b>N-8*</b>   | 0      | 0      | 83 000  |

\* = The following product(s)/model(s) have not yet been named.

The company expects to break-even (MTD) in July 2004 and will begin to generate a net profit (YTD) in April 2005.

#### Cash Flow Analysis 2003 - 2004



## B. Business Model and Revenue Sources

Neonode's principal revenues come from sales of mobile handsets directly to the end-user through its web shop.

However, there will be a difference in the cost structure and revenue between those units sold without a mobile phone subscription and those units sold with a mobile phone subscription:

Revenues from mobile phones sold without an operator subscription:

| Cost Structure         | N-1          | N-2          | N-3          | N-4          | N-5          |
|------------------------|--------------|--------------|--------------|--------------|--------------|
| Bill of Material       | € 180        | € 140        | € 110        | € 110        | € 200        |
| + License              | € 15         | € 15         | € 15         | € 15         | € 15         |
| + Accessories          | € 30         | € 20         | € 13         | € 13         | € 13         |
| + Assembly + Packaging | € 50         | € 40         | € 20         | € 20         | € 20         |
| Cost of Production:    | € 275        | € 215        | € 158        | € 158        | € 248        |
| + Warranty             | € 60         | € 30         | € 20         | € 20         | € 30         |
| <b>Total Cost:</b>     | <b>€ 335</b> | <b>€ 245</b> | <b>€ 178</b> | <b>€ 178</b> | <b>€ 278</b> |
| <b>Customer Price:</b> | <b>€ 529</b> | <b>€ 449</b> | <b>€ 349</b> | <b>€ 349</b> | <b>€ 499</b> |
| European VAT (25%)     | € 106        | € 90         | € 70         | € 70         | € 100        |
| Price excluding VAT:   | <b>€ 423</b> | <b>€ 359</b> | <b>€ 279</b> | <b>€ 279</b> | <b>€ 399</b> |
| Profit margin:         | 20,84%       | 31,79%       | 36,25%       | 36,25%       | 30,36%       |

Revenues from mobile phones sold with an operator subscription:

| <b>Cost Structure</b>  | <b>N-1</b>   | <b>N-2</b>   | <b>N-3</b>   | <b>N-4</b>   | <b>N-5</b>   |
|------------------------|--------------|--------------|--------------|--------------|--------------|
| Bill of Material       | € 180        | € 140        | € 110        | € 110        | € 200        |
| + License              | € 15         | € 15         | € 15         | € 15         | € 15         |
| + Accessories          | € 30         | € 20         | € 13         | € 13         | € 13         |
| + Assembly + Packaging | € 50         | € 40         | € 20         | € 20         | € 20         |
| <b>Total Cost</b>      | <b>€ 275</b> | <b>€ 215</b> | <b>€ 158</b> | <b>€ 158</b> | <b>€ 248</b> |

|                              |              |              |              |              |              |
|------------------------------|--------------|--------------|--------------|--------------|--------------|
| <b>Partner Price (-10%):</b> | <b>€ 416</b> | <b>€ 474</b> | <b>€ 294</b> | <b>€ 294</b> | <b>€ 419</b> |
| European VAT (25%)           | € 83         | € 75         | € 59         | € 59         | € 84         |
| Price excluding VAT:         | <b>€ 333</b> | <b>€ 299</b> | <b>€ 235</b> | <b>€ 235</b> | <b>€ 335</b> |
| Profit margin:               | 17,39%       | 28,16%       | 32,85%       | 32,85%       | 26,03%       |

## C. Assumptions

In our financial projections, we have made the following assumptions:

- ❑ Secure € 6,5M over the next 6-12 months
- ❑ Component Cost will not increase by more than 10% over the next 30 months
- ❑ Launch first Product in September 2003 in Sweden and Europe
- ❑ 50% of revenues from sales will be units sold without subscription
- ❑ 50 % of revenues from sales will be from units sold with subscriptions

## D. Projected Revenues from Sales 2003 – 2005

See Appendix D – Financials

## E. Projected Sales by Region 2003 – 2005

See Appendix D – Financials

## F. Projected Costs & Investments 2003 – 2005

See Appendix D – Financials

## G. Cash Flow Analysis 2003 – 2005

See Appendix D – Financials

## H. Funding Requirements

Neonode will be seeking to raise a maximum of € 6,5M in equity financing over the next 6 -12 months in order to ensure a successful Market Entry and reach a market leadership position within 36 months.

Neonode will provide an exit for early-stage investors through an Initial Public Offering planned for 2006.