

Our mission:

To be the premier supplier
of high-bandwidth silicon
for the world's intelligent
optical networks.



CORPORATE PROFILE

Applied Micro Circuits Corporation (AMCC) designs, develops, manufactures and markets high-performance, high-bandwidth silicon solutions for the world's optical networks. The Company utilizes a combination of high-frequency, analog, digital and mixed-signal design expertise, system-level knowledge and multiple silicon process technologies. This enables AMCC to offer integrated circuit products for the optical networking markets that utilize such protocols as multi-protocol label switching (MPLS), synchronous optical network (SONET)/synchronous digital hierarchy (SDH), asynchronous transfer mode (ATM), and 10 Gigabit Ethernet transmission standards. Among the Company's many customers are Alcatel, Ciena, Cisco Systems, Fujitsu, JDS Uniphase, Juniper Networks, Lucent Technologies, Marconi Communications, Nortel Networks, ONI, and Sycamore Networks.

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This Annual Report contains forward-looking statements, including statements regarding the Company's financial performance, that are subject to certain risks and uncertainties, including, but not limited to, those associated with the integration of companies acquired in recent mergers and acquisitions; reductions, rescheduling or cancellation of orders by our customers; successful and timely development of products; internal and external manufacturing capacity and execution; customer demand for our products; concentration of revenues with major customers; the businesses of the Company's major customers; costs associated with current and future litigation; and general economic conditions, as well as the "Risk Factors" set forth in the Company's Annual Report on Form 10-K for the year ended March 31, 2001 and the Company's other filings with the Securities and Exchange Commission. Actual results could differ materially, as a result of such factors, from those set forth in the forward-looking statements.

Financial highlights

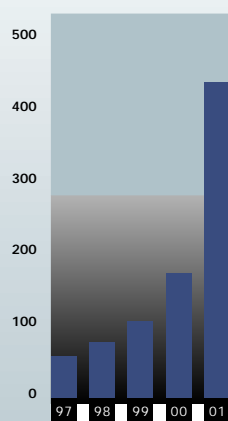
(in millions, except per share data)

	FY 97	FY 98	FY 99	FY 00	FY 01
FOR THE FISCAL YEAR ENDED MARCH 31					
Net revenues	\$ 57.5	\$ 76.6	\$ 105.0	\$ 172.4	\$ 435.5
<i>Reported (GAAP basis)</i>					
Operating income (loss)	\$ 7.0	\$ 14.8	\$ 23.9	\$ 61.1	\$ (492.7)
Net income (loss)	\$ 6.3	\$ 15.2	\$ 17.1	\$ 48.6	\$ (436.2)
Earnings (loss) per share—diluted	\$ 0.04	\$ 0.09	\$ 0.08	\$ 0.20	\$ (1.63)
<i>Pro forma⁽¹⁾</i>					
Operating income	\$ 7.0	\$ 14.8	\$ 26.3	\$ 61.6	\$ 156.6
Net income	\$ 6.3	\$ 15.2	\$ 19.5	\$ 49.0	\$ 139.9
Earnings per share—diluted	\$ 0.04	\$ 0.09	\$ 0.09	\$ 0.21	\$ 0.48

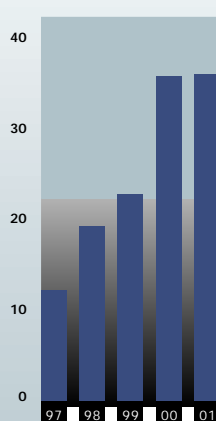
MARCH 31

Cash, cash equivalents & short-term investments	\$ 13.6	\$ 67.9	\$ 86.5	\$ 954.6	\$1,132.1
Working capital	\$ 19.4	\$ 77.4	\$ 103.6	\$ 977.6	\$1,208.2
Total assets	\$ 41.8	\$ 112.8	\$ 150.7	\$1,046.9	\$5,453.3
Total stockholders' equity	\$ 27.7	\$ 91.6	\$ 121.7	\$1,013.8	\$5,238.1

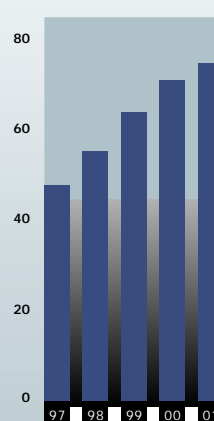
⁽¹⁾See Page 13 in the financial section for an explanation of the pro forma financials and amounts reconciling to GAAP basis results.



Net Revenues
(in millions of dollars)



Pro Forma Operating Margin (%)



Pro Forma Gross Margin (%)

To our stockholders and friends

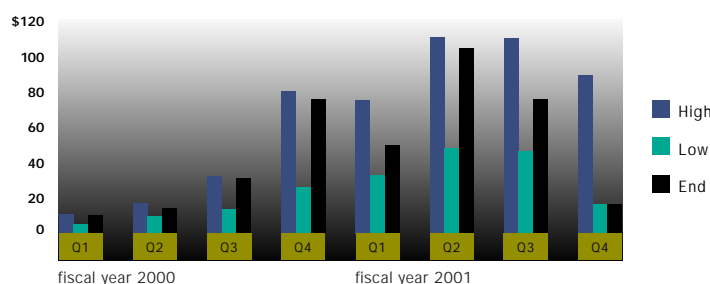
Overall, this past year has been one of substantial growth at AMCC. We extended our market expertise through technological breakthroughs and our strategic acquisitions. As a result, we saw significant revenue increases. However, we also saw dramatic market shifts in the fourth quarter that pose significant challenges to AMCC, our industry and our markets moving forward.

In our fourth quarter, the communications integrated circuit (IC) industry and its customers experienced an unanticipated downturn. This decline was the result of an inventory buildup in our targeted equipment segment due to a rapid and unexpected change in the buying patterns of telecommunications service providers. Service provider capital expenditures (CAPEX) were much lower than our customers anticipated, which resulted in excess inventory at the network capacity level and compounded the uncertainty about equipment-level inventory. We believe that this adjustment in spending patterns was a result of service providers moving from a “build it and they will come” to a “build it when it will generate profit” philosophy.

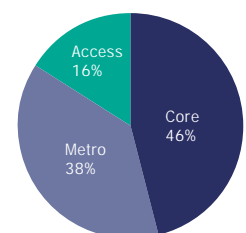
We believe this slowdown is not a trend, but a bump in the road. Although the duration of the slowdown remains uncertain, we remain confident about the long-term viability of the markets we serve and our ability to meet the needs of these markets. Overall, fiscal 2001 represented solid growth compared to the prior year. Revenue reached \$435.5 million, an increase of 153% from the \$172.4 million of fiscal 2000. This included a growth in communications revenue of 182% from \$138.1 million to \$388.5 million. Pro forma net income⁽¹⁾ also improved to \$139.9 million, up 186% from the previous year, with pro forma earnings per share⁽¹⁾ increasing from \$0.21 to \$0.48 in fiscal 2001. In addition, AMCC became a member of the Nasdaq 100 and S&P 500.

Despite near-term industry weakness and poor visibility, we remain confident in our end markets and feel that AMCC is well positioned in those markets long-term. The Company's strong commitment to innovation continues, allowing us to introduce the industry's first commercially available

⁽¹⁾See page 13 in the financial section for an explanation of pro forma financials and amounts reconciling to GAAP basis results.



AMCC High-Low Stock Chart



FY 2001 Design Win Lifetime Value (LTV) by Market Segment

optical carrier (OC)-768, 40 gigabit-per-second (Gbps) transimpedance amplifier (TIA). In addition, we continued to add compelling new OC-48 and OC-192 products to our portfolios that will remain the heart of our growth over the next couple of years.

Moving forward, we intend to expand our market share and leadership in the industry. It is our belief that market leaders that remain aggressive in a weakened market gain momentum and market share, emerging even stronger than before. Demand creation, through the introduction of new products and obtaining design wins, is now more critical than ever. To this end, we continue to focus our efforts on developing breakthrough products that will drive future growth and are fully staffing all critical projects and support resources. AMCC will also trim all discretionary expenses that do not help near-term revenue, new product development or design wins. Otherwise, we will continue to leverage our technological, financial and industry expertise to expand AMCC's leadership in the markets we serve. AMCC has a solid cash position and has managed to a low breakeven point relative to some of our competitors.

During fiscal 2001, AMCC also saw the fruition of our acquisition strategy. In October 2001, for example, AMCC acquired MMC Networks, which complements our existing solutions with software-programmable network processor and traffic management engine components. This critical technology enables AMCC to deliver a total solution for our customers.

In short, we are not playing merely to survive, but to win. By remaining focused and aggressive, we will realize our corporate mission: To be the premier supplier of high-bandwidth silicon for the world's intelligent optical networks.

Organizationally, I am pleased to welcome Wayne Price to AMCC's board of directors. As co-founder of Valiant Networks and former chief technology officer for Williams Communications, Wayne's unique perspective on our customers' customers will prove extremely valuable in helping us develop future business strategies. I would also like to thank every AMCC employee, customer and stockholder for their continued support and dedication.



David M. Rickey
Chairman of the Board,
Chief Executive Officer and President

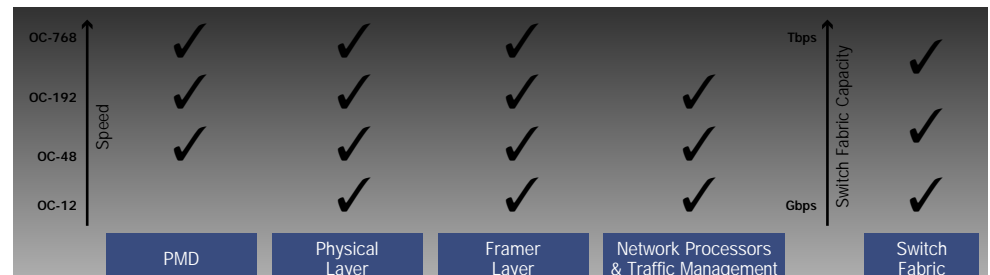


Positioned for sustained growth

Looking ahead, AMCC expects factors other than just end-market demand and CAPEX to play an important role in its success. In fact, the Company has identified several critical market trends that it believes will drive the industry, and thereby the success of AMCC.

The first factor is the market trend to higher speeds in the network. As the demands of end users continue to grow, faster, more cost-efficient and reliable networking solutions will play a major part in the success of bandwidth providers. AMCC's advanced capabilities in network processing and switching solutions, as well as its demonstrated track record in OC-48, OC-192 and OC-768 technology, position the Company for significant growth in this area.

AMCC expects to continue to expand its market penetration into the higher-level digital functions. In today's highly competitive equipment market, the Company expects a faster migration from customers developing their own custom devices, application-specific integrated circuits (ASICs), to using application-specific standard products (ASSPs) that AMCC provides. The Company's customers will also increasingly need ASSPs that can help them meet tight time-to-production ramp schedules due to volatile and demanding service provider requirements. As the proliferation of digital



AMCC delivers solutions for a wide range of speeds.

Milestones



Wayne Price elected to board of directors.

Delivery of the S76800, the industry's first commercially available SiGe TIA for OC-768.

Introduction of the S3097 transmitter and S3098 receiver chipset with clock and data recovery and post amplifier.

Expansion of the Andover-based Digital Products Group to a new complex.

Introduction of the S3086, a 30 Mbps to 2.7 Gbps continuous-rate clock and data recovery unit with unmatched jitter performance capabilities.

Introduction of Orinoco (S1204), the industry's first fully integrated framing and mapping device capable of aggregating 12 DS3/E3/EC-1s to an OC-12.

March 2001

January 2001

products continues to drive content, AMCC's expanded ability to provide high-level framing, switching and network-processing solutions will be an increasingly important competitive differentiator for the Company.

One of the most important factors in AMCC's future success will be the continued growth of the optical networking equipment market and the Company's ability to gain significant design wins in this arena. With the optical equipment market expected to grow faster than CAPEX, AMCC's expertise in high-end, high-bandwidth technology puts the Company in a solid position for greater leadership. To meet this demand, AMCC offers first-to-market OC-768 products and a complete line of pre-integrated OC-192 solutions—including physical medium dependent (PMD), physical layer (PHY), framer and forward error correction (FEC) products—that provide rapid time to market, low power and excellent performance.

AMCC is also uniquely qualified for leadership in the Metropolitan Area Network (MAN) market. The Company offers the broadest OC-48 product line in the industry, including pre-integrated PMD, PHY, framer, FEC, serializer/deserializer (SerDes), network processor, traffic manager and switch fabric products. The Company delivers proven experience and scalability in these technologies, including being first to market with a fully programmable OC-48c network processor, a 10 Gbps fine-grained traffic manager and a compatible family of backplane fabrics ranging from 20 gigabit to terabit capabilities. In addition, AMCC is well positioned to be the first to introduce a programmable OC-192 network processor.

It is through a balanced mix of these growth factors that AMCC plans to expand the Company's leadership in high-speed, high-bandwidth networking solutions well into the future.



Reliability testing being conducted at the AMCC Switching & Network Processing Business Unit in Sunnyvale, CA.



State-of-the-art training facility at AMCC's new engineering building in San Diego.

Added to the S&P 500 index.

Introduction of the Hudson (S19203), the industry's first 10 Gbps silicon device architected to support both the evolving G.709 digital wrapper and traditional SONET/SDH infrastructures.

Introduction of the Danube (S4805), the industry's first highly integrated OC-48 SONET/SDH framing and pointer processor device with on-chip features that are critical for next-generation optical networking equipment. The Danube is complemented by AMCC's S3455 best-in-class CMOS OC-48 4-bit LVDS transceiver IC, which completes an end-to-end chipset solution that meets the power, cost and space requirements of new intelligent optical networking equipment.

Introduction of the S3095, the industry's first 12.5 Gbps SiGe integrated TIA and automatic gain control amplifier for DWDM links.

Two-for-one stock split in the form of a 100% stock dividend.

Merger with MMC Networks complete.

December 2000

November 2000

October 2000

End-to-end solutions

During fiscal 2001, AMCC made significant technological advancements and strategic acquisitions that expanded the Company's product offering to cover the entire optical network. This included the introduction of a number of notable products. The Company announced its second-generation OC-192 physical layer chipset and also introduced Orinoco, the first fully integrated framing and mapping device capable of aggregating 12 synchronous transport signal (STS)-1s, digital signal (DS)3s or CEPT (E3)s to an OC-12 in a single chip. In addition, AMCC demonstrated the first 40 Gb silicon-based product, an OC-768 TIA.

With the acquisition of MMC Networks, AMCC's software-programmable network processor and traffic management engine components have played a significant part in expanding AMCC's capabilities into the access network. Over the past year, the Company introduced a host of advanced network processor, switch fabric and backplane fabric solutions. This combination of products gives AMCC a truly unique offering for applications ranging from digital subscriber line access multiplexers (DSLAMs), wireless access devices and voice over Internet protocol (VoIP) gateways to the most demanding multi-protocol, multi-service optical MAN switches and routers.

AMCC is also poised to profit from industry shifts such as the transition from Bipolar/BiCMOS to CMOS and Silicon Germanium (SiGe) process technologies. AMCC's established leadership in these key technologies has already launched it into a leading role in 10+ Gbps capabilities and, we believe, will continue to provide the Company with a competitive edge. AMCC is well positioned to meet these new market demands and expects to grow faster than the overall market because of these factors.

Acquisition of SiLUTIA.

Creation of Gigabit Ethernet and 10 Gigabit Ethernet design center for excellence in Bedford, New Hampshire.

Introduction of the S3055, the industry's first .18 micron CMOS OC-48 transceiver.

Acquisition of YuniNetworks, Inc.

Introduction of the S7022, the industry's first 2.5 Gbps Quad VCSEL driver, and the S7025, the industry's first SiGe 2.5 Gbps Quad TIA.

The S7022 and S7025 chipset were enhanced in February 2001 to enable higher optical backplane speeds for greater bandwidth density.

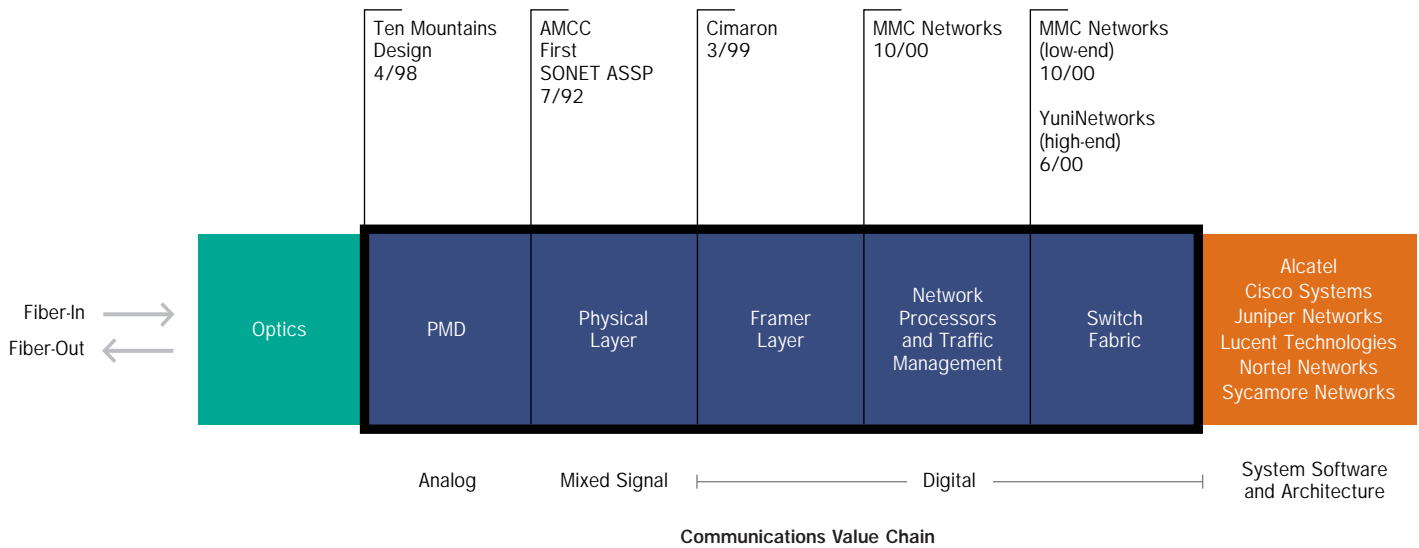
Introduction of the S2080, the industry's first SiGe differential crosspoint switch with over 100 Gbps of switching capacity.

Introduction of the Ganges (S19202), the industry's first OC-192/STM-64 framer device to support both channelized and concatenated 10 Gigabit traffic.

September 2000

June 2000

May 2000



AMCC's strategic acquisitions enable the Company to deliver complete fiber-to-switch optical networking solutions.

Expansion of digital capabilities with acquisitions of Chameleon Technologies, Inc. and pBaud Logic, Inc.



Reinforcing AMCC's leadership

AMCC views the current slowdown as a time to reinforce and build on its technological and market leadership. The Company's past success has put AMCC in a strong position to do just that.

AMCC built a solid competitive advantage through acquisitions during fiscal 2001, enabling the Company to provide products that span the entire optical network. Along with the exceptional array of MMC products, AMCC is also reaping the rewards of framer layer and switch fabric solutions from its Cimaron and YuniNetworks acquisitions. In fact, AMCC is expecting its switch fabric offerings to increase demand for its traffic management and networking processing products, which will in turn increase demand for the rest of the Company's product lines.

Expansion, both domestic and global, will continue to be an important element in the Company's market growth plans. At the end of fiscal 2001, AMCC had 12 design centers, 14 field sales and technical support offices and 34 manufacturing representatives and distributors located around the world. This includes two new engineering facilities in San Diego that are in full operation today.

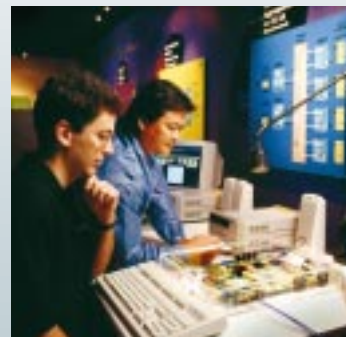
Most importantly, AMCC is committed to meeting technology and time-to-market demands without sacrificing customer satisfaction. AMCC's goal is not only providing better service but also delivering the superior products and partnership that will provide unique value to each customer. This capability will be the ultimate component to the Company's ongoing success and AMCC's ability to accomplish its mission.



AMCC's advanced jitter testing results in exceptional performance.



Design engineer at AMCC's new Switching & Network Processing facility.



At our Applications Lab in San Diego, customers can view AMCC's full product line.



AMCC OFFICES

Baltimore, MD	Philadelphia, PA
Boston, MA	Raleigh, NC
Dallas, TX	San Diego, CA
London, United Kingdom	Shanghai P.R. China
Munich, Germany	Shenzhen P.R. China
Ottawa, Canada	Sunnyvale, CA
Paris, France	

AMCC DESIGN CENTERS

Bedford, NH	Ottawa, Canada
Boston, MA	Manchester, United Kingdom
Chelmsford, MA	Minneapolis, MN
Chicago, IL	Netanya, Israel
Ft. Collins, CO	Raleigh, NC
Irvine, CA	San Diego, CA

Glossary

ASIC (APPLICATION-SPECIFIC INTEGRATED CIRCUIT) An integrated circuit custom designed for a specific application or to perform specific tasks.

ASSP (APPLICATION-SPECIFIC STANDARD PRODUCT) An integrated circuit that, like an ASIC, performs functions for a specific application or task but is offered “off the shelf” as a standard, commercial product.

ATM (ASYNCHRONOUS TRANSFER MODE) Very high-speed transmission technology. ATM is a high-bandwidth, low-delay, connection-oriented, cell-based (fixed-length data units) switching/multiplexing technique.

BACKPLANE The physical area, usually at the rear of the electronics frame, where modules and cables plug into the system.

BICMOS A process that combines the speed of bipolar technology with the low power capability of CMOS technology.

BIPOLAR A process technology that employs silicon as the substrate upon which to fabricate circuits. The circuits are based on fast-switching bipolar transistor structures.

CEPT European standards-setting body that defines how the bits of a PCM carrier system of the 32-channel European type T-1/E-1 will be used and in what sequence.

CMOS (COMPLEMENTARY METAL OXIDE SEMICONDUCTOR) A process technology that employs silicon as the substrate upon which to fabricate circuits. The CMOS IC design is based on MOS Field Effect Transistor (FET) structures and features low power consumption and small component dimensions.

DATA COMMUNICATIONS The transfer of encoded information over electrical or optical transmission systems between points.

DS (DIGITAL SIGNAL) A hierarchy of digital signal speeds used to classify the capacities of lines and trunks. The fundamental speed level is DS-0 (64 kilobits per second) and the highest is DS-4 (about 274 million bits per second).

DSLAM (DIGITAL SUBSCRIBER LINE ACCESS MULTIPLEXER) Used to receive multiple users' DSL signals, multiplex them together using ATM, IP or Frame Relay and transmit multiplexed signal to the WAN. Usually located at a telephone company's central office.

FEC (FORWARD ERROR CORRECTION) A system of data transmission in which redundant bits generated at the transmitted end are used at the receiving end to detect, locate and correct any transmission errors before delivery to the data communications link.

FIBRE CHANNEL A set of standards developed by ANSI (American National Standards Institute). Fibre Channel provides a practical and inexpensive means of rapidly transferring data between workstations, mainframes, supercomputers, desktop computers, storage devices, displays and other peripherals.

FRAMER A device that adjusts the timing of the receiver component to coincide with that of the receiving framing signals.

GBPS Gigabits per second.

IC (INTEGRATED CIRCUIT) A chip etched or imprinted with a network of electronic components.

LTV (LIFETIME VALUE) The total dollar value of a design win is estimated by determining the number of units expected to ship over the lifetime of the product for that opportunity multiplied by the average selling price over that period.

MAN (METROPOLITAN AREA NETWORK) A high-speed data, intra-city network that links multiple locations within a campus, city or LATA.

MIXED-SIGNAL IC Monolithic ICs that contain both digital and analog circuitry.

MPLS (MULTI-PROTOCOL LABEL SWITCHING) Used to increase the

speed of network traffic flow by inserting the information about a specific path the packet takes to its destination. This saves time needed for a router to look up the address for the next node to which the packet is supposed to be sent. MPLS works with IP, ATM and Frame Relay communications methods.

NPU (NETWORK PROCESSOR) A software-programmable microprocessor optimized for networking and communications functions. It presents network equipment vendors with an off-the-shelf alternative for building routers, switches and access devices offering faster time-to-market versus designing a custom ASIC chip. Customers may program an NPU to perform classification analysis, modification and forwarding of incoming data packets/cells, as well as identifying and enforcing security and quality of service rules. MMC Networks coined the term in 1997.

OC-48,-192,-768 (OPTICAL CARRIER LEVEL-48,-192,-768) A SONET optical signal. SONET data rates of 2.5 Gbps, 10 Gbps and 40 Gbps, respectively.

PHY PHYSICAL, as in physical specifications. OSI Physical Layer: The physical layer provides for transmission of cells over a physical medium connecting two ATM devices. This layer is comprised of two sublayers: PMD (see below) and TC (Transmission Convergence).

PMD (PHYSICAL MEDIA DEPENDENT) The sublayer defining the parameters at the lowest level, i.e., speed of the bits on the media.

SDH (SYNCHRONOUS DIGITAL HIERARCHY) A set of standard fiber optic-based serial standards very similar to SONET used throughout the world except in North America and Japan.

SERDES (SERIALIZER/DESERIALIZER) Technology that changes data from parallel-by-byte to serial-by-bit and back again.

SIGE (SILICON GERMANIUM) A process technology that employs a Germanium-doped silicon substrate upon which to fabricate circuits. This enables much higher data rates than are possible with traditional silicon processes.

SILICON Traditional semiconducting material used for fabricating ICs.

SONET (SYNCHRONOUS OPTICAL NETWORK) An optical interface standard used in North America and Japan that allows interoperability of transmission products from multiple vendors very similar to SDH. The standard specifies a family of fiber-optic transmission rates from 52 Mbps to 10 Gbps, created to provide the flexibility needed to transport many digital signals with different capacities and to provide a design standard for manufacturers.

STS (SYNCHRONOUS TRANSPORT SIGNAL) The electrical equivalent of SONET OC level. The signal begins as electrical and is converted into optical prior to presentation to the fiber optic medium.

SWITCH FABRIC A chip, or set of chips, used as the central, high-speed interconnection among multiple ports in a networking platform. Typically, a switch fabric passes traffic among packet- or cell-processing chipsets, whether ASICs or off-the-shelf network processors and traffic managers.

TELECOMMUNICATIONS The transmission, reception and the switching of signals, such as electrical or optical, by wire, fiber or electromagnetic means.

TIA (TRANSIMPEDANCE AMPLIFIER) Used to improve the performance of a detector in a fiber-optic system. The TIA takes the photodiode output current, multiplies it by the transimpedance gain and outputs a voltage signal.

TRAFFIC MANAGER A chip, or set of chips, in a networking platform used to implement Quality of Service policies, including the provisioning of bandwidth (both guaranteed minimums and enforced maximums) to individual users/subscribers, flow control, etc.

VoIP (VOICE OVER INTERNET PROTOCOL) Technology that enables devices of disparate manufacture to support voice communications over packet networks such as the Internet.

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PRO FORMA FINANCIAL HIGHLIGHTS (UNAUDITED)

AMCC is providing pro forma financial information so investors can compare our ongoing operating results without nonrecurring and non-cash charges. Pro forma operating results differ from GAAP basis operating results. See the schedule of pro forma adjustments on page 13 for a reconciliation to our GAAP basis operating results.

(in thousands, except per share data and percentages)		Fiscal 2000					Fiscal 2001				
Fiscal quarter	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total	
Net revenues	\$31,643	\$37,898	\$45,762	\$57,049	\$172,352	\$74,188	\$97,007	\$143,269	\$121,079	\$435,543	
Cost of revenues	10,283	11,326	13,209	15,355	50,173	19,273	24,403	34,316	32,728	110,720	
Gross profit	21,360	26,572	32,553	41,694	122,179	54,915	72,604	108,953	88,351	324,823	
Operating expenses:											
Research and development	6,354	7,194	8,281	10,788	32,617	14,542	18,610	30,900	39,205	103,257	
Selling, general and administrative	5,569	6,548	7,061	8,736	27,914	10,425	13,430	19,886	21,228	64,969	
Total operating expenses	11,923	13,742	15,342	19,524	60,531	24,967	32,040	50,786	60,433	168,226	
Operating income	9,437	12,830	17,211	22,170	61,648	29,948	40,564	58,167	27,918	156,597	
Interest income, net	884	1,005	1,225	9,758	12,872	12,277	13,465	14,771	14,936	55,449	
Income before income taxes	10,321	13,835	18,436	31,928	74,520	42,225	54,029	72,938	42,854	212,046	
Provision for income taxes	3,535	4,738	6,324	10,914	25,511	14,356	18,370	24,800	14,571	72,097	
Net income	\$ 6,786	\$ 9,097	\$12,112	\$21,014	\$ 49,009	\$ 27,869	\$ 35,659	\$ 48,138	\$ 28,283	\$139,949	
Earnings per share (diluted)	\$ 0.03	\$ 0.04	\$ 0.05	\$ 0.08	\$ 0.21	\$ 0.11	\$ 0.13	\$ 0.16	\$ 0.09	\$ 0.48	
Shares used in calculating diluted earnings per share	228,224	231,728	235,216	258,048	238,304	265,162	271,798	305,791	315,741	289,623	

Statement of Operations Data as a Percent of Revenue

Gross margin	67.5%	70.1%	71.1%	73.1%	70.9%	74.0%	74.8%	76.0%	73.0%	74.6%
Operating margin	29.8%	33.9%	37.6%	38.9%	35.8%	40.4%	41.8%	40.6%	23.1%	36.0%
Net margin	21.4%	24.0%	26.5%	36.8%	28.4%	37.6%	36.8%	33.6%	23.4%	32.1%

Sequential Growth Rates

Revenue increase (decrease)	10%	20%	21%	25%	64%	30%	31%	48%	(15)%	153%
Net income increase (decrease)	102%	34%	33%	73%	186%	33%	28%	35%	(41)%	186%
Diluted earnings per share increase (decrease)	99%	32%	31%	58%	163%	29%	25%	20%	(43)%	135%

SCHEDULE OF PRO FORMA ADJUSTMENTS (UNAUDITED, IN THOUSANDS)

The following amounts have been eliminated from GAAP basis statements of operations to derive the pro forma statements of income. The amounts eliminated are primarily related to the Company's acquisitions and are substantially non-cash.

(in thousands, except per share data)		Fiscal 2000					Fiscal 2001				
Fiscal quarter	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total	
Cost of revenues:											
Amortization of developed core technology	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$ 10,696	\$ 14,584	\$ 25,280
Amortization of purchased inventory fair value adjustment	—	—	—	—	—	—	—	16,144	10,763	26,907	
Deferred compensation related to acquired companies	—	—	—	—	—	—	—	1,203	1,617	2,820	
Payroll taxes on stock options	—	—	—	45	45	41	129	40	49	259	
Total pro forma eliminations from cost of revenues	—	—	—	45	45	41	129	28,083	27,013	55,266	
Operating expenses:											
Amortization of goodwill and purchased intangibles	—	—	—	—	—	2,284	8,563	127,574	170,414	308,835	
Deferred compensation related to acquired companies	—	—	—	113	113	134	610	34,751	41,415	76,910	
Acquired in-process R&D	—	—	—	—	—	21,800	3,600	176,700	—	202,100	
Payroll taxes on stock options	—	—	—	370	370	347	1,936	997	2,951	6,231	
Total pro forma eliminations from operations	—	—	—	483	483	24,565	14,709	340,022	214,780	594,076	
Total pro forma eliminations	\$—	\$—	\$—	\$528	\$528	\$24,606	\$14,838	\$368,105	\$241,793	\$649,342	

The pro forma effective tax rate has been adjusted to 34% for fiscal 2001.

Pro forma adjustment for the first three quarters of fiscal 2000 are not presented as the differences were not material.

Fiscal 1999 included one pro forma adjustment amounting to \$2.3 million for the merger fees paid in association with the pooling-of-interests acquisition of Cimaron Communications Corporation ("Cimaron").

CONSOLIDATED STATEMENTS OF OPERATIONS DATA

We effected two-for-one stock splits in the form of 100% stock dividends on each of September 9, 1999, March 23, 2000, and October 30, 2000. All share and per share information has been restated to reflect these events.

(in thousands, except per share data)	Years Ended March 31,				
	1997	1998	1999	2000	2001
Net revenues	\$57,468	\$76,618	\$105,000	\$172,352	\$ 435,543
Cost of revenues ⁽¹⁾	<u>30,057</u>	<u>34,321</u>	<u>37,937</u>	<u>50,218</u>	<u>163,166</u>
Gross profit	27,411	42,297	67,063	122,134	272,377
Operating expenses:					
Research and development ⁽¹⁾	7,870	13,268	22,301	32,527	105,225
Selling, general and administrative ⁽¹⁾	12,537	14,278	17,795	28,035	69,232
Stock-based compensation ⁽¹⁾	—	—	701	452	79,730
Amortization of goodwill and purchased intangibles	—	—	—	—	308,835
Acquired in-process research and development	—	—	—	—	202,100
Merger-related costs	—	—	2,350	—	—
Total operating expenses	<u>20,407</u>	<u>27,546</u>	<u>43,147</u>	<u>61,014</u>	<u>765,122</u>
Operating income (loss)	7,004	14,751	23,916	61,120	(492,745)
Interest income (expense), net	(29)	871	3,450	12,872	55,449
Income (loss) before income taxes	6,975	15,622	27,366	73,992	(437,296)
Income tax expense (benefit)	659	406	10,233	25,367	(1,081)
Net income (loss)	<u>\$ 6,316</u>	<u>\$15,216</u>	<u>\$ 17,133</u>	<u>\$ 48,625</u>	<u>\$ (436,215)</u>
Basic earnings (loss) per share:					
Earnings (loss) per share	<u>\$ 0.16</u>	<u>\$ 0.18</u>	<u>\$ 0.09</u>	<u>\$ 0.23</u>	<u>\$ (1.63)</u>
Shares used in calculating basic earnings (loss) per share	<u>40,048</u>	<u>84,752</u>	<u>196,112</u>	<u>215,640</u>	<u>267,363</u>
Diluted earnings (loss) per share:					
Earnings (loss) per share	<u>\$ 0.04</u>	<u>\$ 0.09</u>	<u>\$ 0.08</u>	<u>\$ 0.20</u>	<u>\$ (1.63)</u>
Shares used in calculating diluted earnings (loss) per share	<u>143,256</u>	<u>162,352</u>	<u>219,440</u>	<u>238,304</u>	<u>267,363</u>

⁽¹⁾For presentation purposes, the functional line items exclude stock-based compensation charges related to acquired companies as follows (in thousands):

Cost of revenues	\$ —	\$ —	\$ —	\$ —	\$ 2,820
Research and development	—	—	171	288	41,303
Selling, general and administrative	—	—	530	164	35,607
	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 701</u>	<u>\$ 452</u>	<u>\$ 79,730</u>

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)	March 31,				
	1997	1998	1999	2000	2001
Assets					
Current assets:					
Cash, cash equivalents and short-term investments	\$13,597	\$ 67,896	\$ 86,540	\$ 954,551	\$1,132,093
Accounts receivable, net	8,418	12,179	19,275	25,459	83,892
Inventories	7,530	8,185	9,813	10,925	32,740
Deferred income taxes	—	3,882	4,573	4,148	27,597
Other current assets	698	2,384	4,819	10,321	24,775
Total current assets	30,243	94,526	125,020	1,005,404	1,301,097
Property and equipment, net	10,768	17,218	23,128	37,842	112,953
Purchased intangibles, net	—	—	—	—	4,008,440
Strategic equity and convertible debt investments	—	—	—	—	28,023
Other assets	803	1,090	2,507	3,636	2,765
Total assets	<u>\$41,814</u>	<u>\$112,834</u>	<u>\$150,655</u>	<u>\$1,046,882</u>	<u>\$5,453,278</u>
Liabilities and Stockholders' Equity					
Current liabilities:					
Accounts payable	\$ 2,428	\$ 5,215	\$ 5,131	\$ 8,818	\$ 38,069
Other current liabilities	5,789	9,274	13,335	16,842	53,538
Current portion of long-term debt and capital lease obligations	2,662	2,620	2,937	2,123	1,264
Total current liabilities	10,879	17,109	21,403	27,783	92,871
Long-term debt and capital lease obligations, less current portion	3,192	4,091	7,558	5,294	2,266
Deferred income taxes	—	—	—	—	120,040
Stockholders' equity	27,743	91,634	121,694	1,013,805	5,238,101
Total liabilities and stockholders' equity	<u>\$41,814</u>	<u>\$112,834</u>	<u>\$150,655</u>	<u>\$1,046,882</u>	<u>\$5,453,278</u>

OTHER FINANCIAL INFORMATION

(in thousands, except percentages and employee data)	March 31,				
	1997	1998	1999	2000	2001
Statements of Operations:					
Revenue growth year over year	14%	33%	37%	64%	153%
Capital depreciation and amortization	\$ 5,185	\$ 5,174	\$ 7,045	\$ 8,039	\$ 16,135
% of revenues	9%	7%	7%	5%	4%
Amortization of purchased intangibles	—	—	—	—	\$ 308,835
Amortization of stock-based compensation related to acquired companies	—	—	\$ 701	\$ 452	\$ 79,730
EBITDA	\$12,189	\$ 20,052	\$ 31,821	\$ 69,770	\$ 166,360
Balance Sheets:					
Working capital	\$19,364	\$ 77,417	\$103,617	\$ 977,621	\$1,208,226
Total long-term debt and capital lease obligations	\$ 5,854	\$ 6,711	\$ 10,495	\$ 7,417	\$ 3,530
Total long-term debt and capital lease obligations to equity ratio	21%	7%	9%	1%	—%
Additions to property, plant and equipment	\$ 4,055	\$ 11,624	\$ 16,490	\$ 22,753	\$ 78,217
% of revenues	7%	15%	16%	13%	18%
Number of employees at end of year	256	320	361	477	1,169

BUSINESS OVERVIEW

We design, develop, manufacture and market high-performance, high-bandwidth silicon solutions for the world's optical networks. We utilize a combination of high-frequency analog, mixed-signal and digital design expertise coupled with system-level knowledge and multiple silicon process technologies to offer integrated circuit products that enable the transport of voice and data over fiber-optic networks. Our system solution portfolio includes PMD layer, physical layer, framing layer, network processing layer and traffic management and switching layer devices that address the high-performance needs of the evolving intelligent optical network. Our products target the SONET/SDH, ATM, DWDM, Gigabit Ethernet and Fibre Channel semiconductor markets. We provide our customers with complete silicon IC solutions including PMD devices such as laser drivers, physical layer products such as transceivers, framing layer products such as framers and mappers and higher layer processors such as network processors and switch fabrics. Our products currently target data rates up to 40 gigabits per second (a rate known as "OC-768").

We continue to supply silicon ICs for the Automated Test Equipment ("ATE"), high-speed computing and military markets. The revenues from these products have become less important as we have focused our business and operations on communications markets.

PRODUCT CATEGORIES

We have several types of communications IC products categorized by the order in which they receive and transmit signals and information within communication equipment. These categories are:

PMD LAYER: Our PMD layer ICs typically work in conjunction with the lasers or photo diodes that provide the electrical-to-optical and optical-to-electrical signal conversions. These ICs include various amplifiers that take very weak analog electrical signals (e.g., a few millivolts) and increase them for use by the physical layer. Our PMD layer products transmit signals at rates ranging from 1 to 40 gigabits per second ("Gbps").

PHYSICAL LAYER: Our physical layer ICs transmit and receive signals to and from the PMD layer in a very high-speed serial format (over 10 Gbps today) and reduce overall system "noise." This low noise capability permits the transmission of signals over greater distances with fewer errors. Our physical layer ICs also convert analog signals from the PMD layer to digital signals for the framing layer and vice versa.

FRAMING LAYER: Our framing layer ICs transmit and receive signals to and from the physical layer in a parallel format and are used predominately in systems such as very high-speed transmission equipment, add-drop multiplexers, digital and optical cross-connects, edge and core routers and DWDM. After receiving the signals, these ICs then perform a number of additional functions, including framing, terminating the overhead, performance monitoring, forward error correction and mapping the data payload to/from the transmission format. The framing layer ICs then pass the data either directly to a switch fabric product, which switches the information to its destination, or to a network processor, which further processes the data prior to forwarding it to a switch fabric product. Framing layer ICs similarly process signals received from the network processing and switching layers for transmission to the physical layer on their return to the optical network.

NETWORK PROCESSING LAYER: Our network processor ICs are software programmable processors that receive and transmit signals from and to the framing layer and perform the processing of packet and cell headers, including such functions as real-time parsing, matching and table look-up, as well as bit stream manipulations, such as adding, deleting, substituting, appending and pre-pending. They can perform intelligent packet classification for policy-based network services. After processing, the signals are sent on to the traffic management and switch fabric layer.

TRAFFIC MANAGEMENT AND SWITCHING LAYER: Our traffic management ICs receive and transmit signals from and to the network processor and primarily perform the queuing and buffering required on packets before sending on to the switch fabric. Our switch fabric ICs then switch the information in the proper priority and to the proper destinations.

PRODUCTS AND CUSTOMERS

PMD PRODUCTS: During fiscal 2001, we introduced our first-generation OC-768 transimpedance amplifier and 3.2 Gbps quad VCSEL laser driver and amplifier products. In addition, we introduced our second-generation PMD product, the S3095 integrated transimpedance amplifier with automatic gain control amplifier. Our current customers for PMD products include Alcatel, Ciena, Fujitsu, Mitel, NEC, Sumitomo and Sycamore Networks.

PHYSICAL LAYER PRODUCTS: We introduced our first generation of physical layer products in 1993. We have since developed several generations of these products improving cost, power, functionality and performance. During fiscal 2001, we introduced several OC-48 (2.5 Gbps) integrated physical layer transceiver devices, including our first OC-48 devices manufactured using the CMOS fabrication process. In addition, we introduced our second-generation OC-192 transmitter and receiver chipset. Our current customers for physical layer products include Alcatel, Ciena, Cisco, Fujitsu, Hitachi, JDS Uniphase, Juniper Networks, Lucent, Marconi Communications, Nortel, Sycamore Networks and Tellabs.

FRAMING LAYER PRODUCTS: During fiscal 2001, we introduced several framing layer products for the OC-12 (625 megabits per second), OC-48 and OC-192 markets. The Ganges device is the first commercially available OC-192 framer. The Hudson device supports OC-192 forward error correction, digital wrapper and performance monitoring. Additionally, we introduced Danube, our second-generation OC-48 pointer processing device, and Orinoco, a DS-3 to OC-12 mapping device. Our current customers for framing layer products include Ciena, Cisco, Lucent, Marconi Communications, NEC, Nortel, Sycamore Networks, Tellabs and Tellium.

NETWORK PROCESSING LAYER PRODUCTS: All of our current network processing products come from the acquisition of MMC Networks, Inc. ("MMC") completed on October 25, 2000. These products include the nP7120 packet processor. Our current customers for network processing products include Cisco, Fujitsu and Nortel.

TRAFFIC MANAGEMENT AND SWITCHING LAYER PRODUCTS: All of our current traffic management and switching layer products also come from the acquisition of MMC. These products include the second-generation nPX5410, a fully integrated 22 Gbps full-duplex switching and traffic management IC, and the first-generation nPX5500 integrated 20 Gbps full-duplex switching and traffic manager. Our current customers for traffic management and switching layer products include Cisco, Fujitsu and Nortel.

ATE PRODUCTS

We are not currently developing new products for the ATE market. We continue to manufacture and sell ASIC products to customers such as Agilent, LTX, Schlumberger, Teradyne and Texas Instruments.

HIGH-SPEED COMPUTING PRODUCTS

We offer a PCI product line that addresses the high-speed computing market. However, we are not currently developing new products for this market. The S5933 is a standard master/slave PCI controller chip. The S5920 is a standard target-only PCI controller chip. These devices are supported with comprehensive development kits and third-party driver software. We sell these products to a very large and diverse customer base. Current customers of our PCI products include Cisco, Ericsson, IBM, Nortel and Sagem.

MILITARY PRODUCTS

We are not currently developing new products for military applications. We continue to manufacture and sell ASIC products for military applications to customers such as Northrop Grumman and Raytheon Systems.

The following discussion of the financial condition and results of our operations should be read in conjunction with the consolidated financial statements and notes thereto included elsewhere in our Annual Report and in conjunction with our Annual Report on Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including but not limited to, those described in the "Risk Factors." Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect our analysis only as of the date hereof. We assume no obligation to update these forward-looking statements to reflect actual results or changes in factors or assumptions affecting such forward-looking statements.

RESULTS OF OPERATIONS

The following table sets forth certain selected consolidated statement of operations data in dollars and as a percentage of revenues for the periods indicated:

(in thousands, except per share data)	Fiscal Year Ended March 31,					
	1999		2000		2001	
Net revenues	\$ 105,000	100.0%	\$ 172,352	100.0%	\$ 435,543	100.0%
Cost of revenues ⁽¹⁾	<u>37,937</u>	<u>36.1</u>	<u>50,218</u>	<u>29.1</u>	<u>163,166</u>	<u>37.5</u>
Gross profit	67,063	63.9	122,134	70.9	272,377	62.5
Operating expenses:						
Research and development ⁽¹⁾	22,301	21.2	32,527	18.9	105,225	24.2
Selling, general and administrative ⁽¹⁾	17,795	16.9	28,035	16.3	69,232	15.9
Stock-based compensation ⁽¹⁾	701	0.7	452	0.3	79,730	18.3
Amortization of goodwill and purchased intangibles	—	—	—	—	308,835	70.9
Acquired in-process research and development	—	—	—	—	202,100	46.4
Merger-related costs	<u>2,350</u>	<u>2.2</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total operating expenses	<u>43,147</u>	<u>41.1</u>	<u>61,014</u>	<u>35.4</u>	<u>765,122</u>	<u>175.7</u>
Operating income (loss)	23,916	22.8	61,120	35.5	(492,745)	(113.1)
Interest income, net	<u>3,450</u>	<u>3.3</u>	<u>12,872</u>	<u>7.5</u>	<u>55,449</u>	<u>12.7</u>
Income (loss) before income taxes	27,366	26.1	73,992	42.9	(437,296)	(100.4)
Income tax expense (benefit)	<u>10,233</u>	<u>9.7</u>	<u>25,367</u>	<u>14.7</u>	<u>(1,081)</u>	<u>(0.2)</u>
Net income (loss)	<u>\$ 17,133</u>	<u>16.3%</u>	<u>\$ 48,625</u>	<u>28.2%</u>	<u>\$(436,215)</u>	<u>(100.2)%</u>
Diluted earnings (loss) per share:						
Earnings (loss) per share	<u>\$ 0.08</u>		<u>\$ 0.20</u>		<u>\$ (1.63)</u>	
Shares used in calculating diluted earnings (loss) per share	<u>219,440</u>		<u>238,304</u>		<u>267,363</u>	

⁽¹⁾For presentation purposes, the functional line items exclude stock-based compensation charges related to acquired companies as follows (in thousands):

Cost of revenues	\$ —	—%	\$ —	—%	\$ 2,820	0.6%
Research and development	171	0.2	288	0.2	41,303	9.5
Selling, general and administrative	<u>530</u>	<u>0.5</u>	<u>164</u>	<u>0.1</u>	<u>35,607</u>	<u>8.2</u>
	<u>\$ 701</u>	<u>0.7%</u>	<u>\$ 452</u>	<u>0.3%</u>	<u>\$ 79,730</u>	<u>18.3%</u>

COMPARISON OF THE YEAR ENDED MARCH 31, 2001 TO THE YEAR ENDED MARCH 31, 2000

On September 9, 1999, March 23, 2000 and October 30, 2000, we effected two-for-one stock splits (in the form of 100% stock dividends); accordingly, all share and per share amounts in this discussion of the results of operations have been restated to reflect the stock splits.

NET REVENUES. Net revenues for the year ended March 31, 2001 were approximately \$435.5 million, representing an increase of 152.7% over net revenues of approximately \$172.4 million for the year ended March 31, 2000. Revenues from sales of communications products increased 181.5% to \$388.8 million, or 89% of net revenues, for the year ended March 31, 2001 from \$138.1 million, or 80% of net revenues, for the year ended March 31, 2000. Of this increase, \$45.5 million is attributable to the revenues generated by MMC since the date of acquisition. The remaining increase reflects both unit growth in shipments of existing products and the introduction of new communications products. Revenues from sales of non-communications products, consisting of the ATE, high-speed computing and military markets, decreased from 20% of net revenues for the year ended March 31, 2000 to 11% of net revenues for the year ended March 31, 2001.

In the fourth quarter of fiscal 2001, we experienced a decline in our revenues, bookings and backlog from the previous quarter. Many of our customers have announced that they anticipate lower revenues and profits for fiscal 2002 as a result of a slowdown or reduction of capital expenditures by their customers. This factor, coupled with indicators of a general economic slowdown in the United States, has reduced demand for our products. We expect that revenues will decline materially for at least the first two quarters of fiscal 2002, when compared to the last two quarters of fiscal 2001.

Based on direct shipments, net revenues to customers exceeding 10% for the years ending March 31, were as follows:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Nortel	19%	26%	10%
Insight	13%	17%	19%
Raytheon	16%	—	—

Looking through product shipments to distributors and subcontractors, net revenues on an end customer basis exceeding 10% for the years ending March 31, were as follows:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Nortel	20%	38%	20%
Raytheon	16%	—	—

GROSS MARGIN. Gross margin was 62.5% for the year ended March 31, 2001, as compared to 70.9% for the year ended March 31, 2000. Gross margin was adversely affected by a \$26.9 million purchase accounting charge to cost of revenues based on an increase in the value of the MMC inventory as of the acquisition date, as well as \$25.3 million of developed core technology amortization (see Note 3 of the notes to the consolidated financial statements). Excluding the effect of these purchase accounting charges, gross margin actually increased to 74.5% for the year ended March 31, 2001. This increase in gross margin was driven principally by the increased percentage of revenues derived from our communications standard products, which have higher average selling prices, and the increased utilization of our wafer fabrication facility. We anticipate that gross margin will decline in fiscal 2002 as a result of decreasing utilization of our manufacturing facilities and the potential for lower average selling prices as a result of the current softness in demand for our products.

RESEARCH AND DEVELOPMENT. Research and development ("R&D") expenses increased 224% to approximately \$105.2 million, or 24.2% of revenues, for the year ended March 31, 2001, from approximately \$32.5 million, or 18.9% of net revenues, for the year ended March 31, 2000. The increase is a result of new product and process development efforts, investments made in new design tools for the development of new products, and increases in personnel costs as a result of acquisitions and internal hiring of R&D personnel. We believe that a continued commitment to R&D is vital to maintain a leadership position with innovative communications products. Accordingly, we expect R&D expenses to increase in the future. Currently, R&D expenses are focused on the development of products and processes for the communications markets, and we expect to continue this focus.

SELLING, GENERAL AND ADMINISTRATIVE. Selling, general and administrative (“SG&A”) expenses were approximately \$69.2 million, or 15.9% of revenues, for the year ended March 31, 2001, as compared to approximately \$28.0 million, or 16.3% of net revenues, for the year ended March 31, 2000. The increase in SG&A expenses in absolute dollars for the year ended March 31, 2001 was primarily attributable to investments made in our corporate infrastructure, an increase in the size of our sales force and related commissions, additional marketing and advertising investments associated with the introduction of new products, general corporate branding and increases in our reserves for bad debt. The remaining increase is the result of our acquisition of MMC in the third quarter, which had similar expenses not included in the prior year as a result of purchase accounting. We expect SG&A expenses to increase in the future due principally to additional staffing in our sales and marketing departments, as well as increased spending on information technology and product promotion, although we do expect that the rate of increase will be reduced.

STOCK-BASED COMPENSATION. During the year ended March 31, 2001, deferred compensation of \$438.8 million was recorded related to restricted stock and unvested options granted to employees of acquired companies in accordance with FASB interpretation No. 44 (“FIN 44”). Prior to FIN 44, the fair value of these stock awards would have been included as part of the purchase price of the acquisitions, probably resulting in additional goodwill. Stock-based compensation charges were \$79.7 million and \$0.5 million for the years ended March 31, 2001 and March 31, 2000, respectively. The increase is directly related to the acquisitions of MMC, SiLUTIA, Inc. (“SiLUTIA”), YuniNetworks, Inc. (“YuniNetworks”), pBaud Logic, Inc. (“pBaud”), Chameleon Technologies (“Chameleon”), and Raleigh Technology Corporation (“RTC”). We currently expect to record amortization of deferred compensation with respect to these option grants of approximately \$147.2 million, \$134.1 million, \$63.5 million and \$4.1 million during the fiscal years ended March 31, 2002, 2003, 2004 and 2005, respectively. These charges could be reduced based on the level of employee turnover. Future acquisitions of businesses may result in substantial additional charges. Such charges may cause fluctuations in our interim or annual operating results.

AMORTIZATION OF GOODWILL AND PURCHASED INTANGIBLES. Amortization of goodwill and purchased intangible assets was \$308.8 million for the year ended March 31, 2001. These charges are related to the purchases of MMC, SiLUTIA, YuniNetworks, pBaud, Chameleon and RTC. There were no amortization charges arising from purchase acquisitions in the year ended March 31, 2000. Currently, we expect amortization expense to be \$736.4 million, \$736.3 million, \$734.4 million, \$731.6 million and \$704.0 million for the years ended March 31, 2002, 2003, 2004, 2005 and 2006, respectively. There can be no assurance that acquisitions of businesses by us in the future will not result in substantial changes to the expected amortization, which may cause fluctuations in our interim or annual operating results. The estimated amortization of goodwill expense is based on the current guidance for the amortization of intangible assets and does not reflect the exposure draft regarding the impairment only approach to goodwill amortization expected to be effective in fiscal 2002. If the new guidance becomes effective as it is currently drafted, the amortization of goodwill would no longer be required.

ACQUIRED IN-PROCESS RESEARCH AND DEVELOPMENT. For the year ended March 31, 2001, we recorded \$202.1 million of acquired in-process research and development (“IPR&D”) resulting from the acquisition of YuniNetworks, SiLUTIA and MMC. This amount was expensed on the acquisition date because the acquired technology had not yet reached technological feasibility and had no future alternative uses.

The following table summarizes the significant assumptions underlying the valuations related to the IPR&D at the date of acquisition:

(dollars in thousands)	IPR&D Charge	Estimated Cost to Complete Technology	Discount Rate Applied to IPR&D	Weighted- Average Cost of Capital
MMC Networks, Inc.	\$176,700	\$11,494	20%	14%
SiLUTIA, Inc.	3,600	276	22%	17%
YuniNetworks, Inc.	<u>21,800</u>	<u>3,078</u>	21%	16%
Total	<u>\$202,100</u>	<u>\$14,848</u>		

Included below are additional details regarding the in-process technology acquired in these transactions:

MMC NETWORKS, INC. MMC designs, develops, manufactures and markets network processors, traffic management and switch fabric ICs. The total IPR&D charge related to eight projects, which at the date of acquisition were between 20% and 90% complete. Three projects accounted for approximately 62% of the value assigned to IPR&D. These projects were estimated to be completed in fiscal 2002 and are on schedule. The remaining projects, which accounted for 38% of the charge, are at various stages of completion and are also on schedule except for general insignificant delays related to resource constraints.

SILUTIA, INC. SiLUTIA specializes in digital and mixed-signal IC designs. Ninety-five percent of the IPR&D charge related to one project that was 60% complete at the date of acquisition. At March 31, 2001, the project is estimated to be approximately 95% complete and is on budget.

YUNINETWORKS, INC. YuniNetworks develops scalable switch fabric silicon ICs. The IPR&D charge related to one chipset consisting of six ICs. At the date of acquisition, the project was estimated to be 32% complete. The original project was completed on time and on budget. The chipset has not been production released and is currently being modified to include additional functionality not planned in the original project.

There can be no assurance that acquisitions of businesses, products or technologies by us in the future will not result in substantial charges for acquired in-process research and development that may cause fluctuations in our interim or annual operating results.

NET INTEREST INCOME. Net interest income increased to \$55.4 million for the year ended March 31, 2001, compared to \$12.9 million for the year ended March 31, 2000. This increase was due principally to increased funds available for investment generated by our operations, public stock offerings and employee stock option exercises.

INCOME TAXES. Income taxes for the year ended March 31, 2001 differed from statutory rates primarily due to the utilization of certain federal and state tax credits and the nondeductibility of IPR&D and the amortization of purchased intangibles.

BACKLOG. Our sales are made primarily pursuant to standard purchase orders for delivery of products. Quantities of our products to be delivered and delivery schedules are frequently revised to reflect changes in customer needs, and customer orders can be canceled or rescheduled without significant penalty to the customer. For these reasons, our backlog as of any particular date is not representative of actual sales for any succeeding period, and we therefore believe that backlog is not a good indicator of future revenue. Our backlog for products requested to be shipped and non-recurring engineering services to be completed in the next six months was \$100.3 million on March 31, 2001, compared to \$86.1 million on March 31, 2000.

COMPARISON OF THE YEAR ENDED MARCH 31, 2000 TO THE YEAR ENDED MARCH 31, 1999

NET REVENUES. Net revenues for the year ended March 31, 2000 were approximately \$172.4 million, representing an increase of 64% over net revenues of approximately \$105.0 million for the year ended March 31, 1999. Revenues from sales of communications products increased 141% to \$138.1 million or 80% of net revenues, for the year ended March 31, 2000 from \$57.3 million, or 55% of net revenues, for the year ended March 31, 1999. This increase reflected both unit growth in shipments of existing products, as well as the introduction of new products for the communications market. Revenues from sales of non-communications products decreased from 45% of net revenues for the year ended March 31, 1999 to 20% of net revenues for the year ended March 31, 2000.

GROSS MARGIN. Gross margin was 70.9% for the year ended March 31, 2000, as compared to 63.9% for the year ended March 31, 1999. The increase in gross margin resulted primarily from increased utilization of our wafer fabrication facility.

RESEARCH AND DEVELOPMENT. R&D expenses increased 46% to approximately \$32.5 million, or 18.9% of revenues, for the year ended March 31, 2000, from approximately \$22.3 million, or 21.2% of net revenues, for the year ended March 31, 1999. The increase in R&D expenses in absolute dollars is a reflection of our aggressive product development efforts. Factors contributing to the increase in R&D expenses are an increase in compensation-related costs, as a result of both increased headcount and increased average compensation costs, an increase in the cost of design tools and software and an increase in prototyping and outside contractor costs.

SELLING, GENERAL AND ADMINISTRATIVE. SG&A expenses were approximately \$28.0 million, or 16.3% of net revenues, for the year ended March 31, 2000, as compared to approximately \$17.8 million, or 16.9% of net revenues, for the year ended March 31, 1999. The increase in SG&A expenses for the year ended March 31, 2000 was primarily due to increases in personnel and travel costs, commissions earned by sales representatives, product promotion expenses and professional fees related to legal, accounting and strategic developments.

NET INTEREST INCOME. Net interest income increased to \$12.9 million for the year ended March 31, 2000, compared to \$3.5 million for the year ended March 31, 1999. This increase was due principally to higher interest income from larger cash and short-term investment balances generated from operations and the net proceeds of approximately \$815 million from our public offering completed in January 2000.

INCOME TAXES. Our annual effective tax rate for the year ended March 31, 2000 was 34.3%, compared to an effective tax rate of 37.4% for the year ended March 31, 1999. The effective tax rate for the year ended March 31, 2000 was decreased from statutory rates due to the utilization of certain federal and state tax credits. The rate for fiscal 2000 was lower than fiscal 1999 due to the nondeductibility of certain merger-related costs incurred in fiscal 1999.

LIQUIDITY AND CAPITAL RESOURCES

Our principal source of liquidity as of March 31, 2001 consisted of \$1.1 billion in cash, cash equivalents and short-term investments. Working capital as of March 31, 2001 was \$1.2 billion, compared to \$1.0 billion as of March 31, 2000. This increase in working capital was primarily due to net cash provided by operating activities and proceeds from the issuance of common stock, offset by the purchase of property and equipment.

For the years ended March 31, 2001, 2000 and 1999, net cash provided by operating activities was \$199.8 million, \$65.3 million and \$22.0 million, respectively. Net cash provided by operating activities in fiscal 2001 and 2000 primarily reflected net income before depreciation and amortization expense, acquired IPR&D and the tax benefit of disqualifying dispositions, offset by increases in deferred tax liabilities.

Capital expenditures totaled \$78.2 million, \$22.8 million and \$16.5 for the years ended March 31, 2001, 2000 and 1999, respectively, which primarily consisted of engineering hardware and design software, manufacturing and test equipment and land. As we continue to expand our operations and as we integrate and upgrade the capital equipment, software and facilities of our acquired companies, we intend to increase our capital expenditures for computer hardware/software, manufacturing and test equipment and real estate.

In addition, we continue to explore alternatives for the expansion of our manufacturing capacity, including entering into additional strategic relationships to obtain capacity, qualifying second-source manufacturers of our products, building a new manufacturing facility and purchasing a manufacturing facility. Any of these alternatives could require a significant investment by us, and there can be no assurance that any of the alternatives for the expansion of our manufacturing capacity will be available on a timely basis.

We believe that our available cash, cash equivalents and short-term investments and cash generated from operations, will be sufficient to meet our capital requirements for at least the next 12 months, although we could elect or could be required to raise additional capital during such period. There can be no assurance that such additional debt or equity financing will be available on commercially reasonable terms or at all.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the potential loss arising from adverse changes in market rates and prices, such as foreign currency exchange, interest rates and a decline in the stock market. We do not enter into derivatives or other financial instruments for trading or speculative purposes. We are exposed to market risks related to changes in interest rates and foreign currency exchange rates.

We are exposed to market risk as it relates to changes in the market value of our investments. At March 31, 2001, our investment portfolio includes fixed-income securities classified as available-for-sale investments with a fair market value of \$1,074 million and a cost basis of \$1,070 million. The gross unrealized gains of \$3.9 million and gross unrealized losses of \$0.1 million have been recorded net of deferred taxes of \$1.4 million as a separate component of accumulated other comprehensive income. These securities are subject to interest rate risk and will decline in value if interest rates increase. Because the maturity dates of our investment portfolio are relatively short, an immediate 100 basis point increase in interest rates would have no material impact on our financial condition or results of operations.

We invest in equity instruments of private companies for business and strategic purposes, most of which are communications IC companies. These investments are classified as long-term strategic equity and convertible debt investments and are valued based on prices recently paid for the securities. The estimated fair values are not necessarily representative of the amounts that the Company could realize in a current transaction.

We generally conduct business, including sales to foreign customers, in U.S. dollars. As a result, we have limited foreign currency exchange rate risk. The effect of an immediate 10 percent change in foreign exchange rates would not have a material impact on our financial condition or results of operations.

RISK FACTORS

Our results of operations have varied significantly in the past and may continue to do so in the future. These variations have been, and may in the future be, due to a number of factors, any of which could have a material adverse effect on our business, financial condition and results of operations. These factors include, but are not limited to: the rescheduling or cancellation of orders by customers; fluctuations in the timing and amount of customer requests for product shipments; fluctuations in manufacturing yields and inventory levels; changes in product mix of sales; our ability to introduce new products and technologies on a timely basis; the introduction of products and technologies by our competitors; the availability of external foundry capacity, purchased parts and raw materials; competitive pressures on selling prices; the timing of investments in research and development; market acceptance of products and the products of our customers; the ability of our customers to obtain components from their other suppliers; the timing of depreciation and other expenses to be incurred by us in connection with the increase of our manufacturing capacity; the amount and timing of the costs associated with payroll taxes related to the exercise of employee stock options; the timing and amount of recruiting and relocation expenses, prototyping costs and product promotional expenses; costs associated with current and future litigation, including but not limited to, our shareholder suit and litigation relating to the use or ownership of intellectual property; costs associated with compliance with applicable environmental regulations; general semiconductor industry conditions; and general economic conditions. Historically, average selling prices in the semiconductor industry have decreased over the life of a product; as a result, the average selling prices of our products may be subject to significant pricing pressures in the future. Because we are continuing to increase our operating expenses for personnel and new product development, and because we are limited in our ability to reduce expenses quickly in response to any revenue shortfalls, our business, financial condition and operating results would be adversely affected if anticipated sales are not achieved. In addition, our operating results may be below the expectations of public market analysts or investors, which could have a material adverse effect on the market price of the common stock.

CONSOLIDATED BALANCE SHEETS

(in thousands, except par value)	March 31,	
	2000	2001
Assets		
Current assets:		
Cash and cash equivalents	\$ 170,102	\$ 58,197
Short-term investments—available-for-sale	784,449	1,073,896
Accounts receivable, net of allowance for doubtful accounts of \$314 and \$4,575 at March 31, 2000 and 2001, respectively	25,459	83,892
Inventories	10,925	32,740
Deferred income taxes	4,148	27,597
Current portion of notes receivable from officers and employees	81	25
Other current assets	10,240	24,750
Total current assets	1,005,404	1,301,097
Property and equipment, net	37,842	112,953
Notes receivable from officers and employees, less current portion	48	120
Purchased intangibles, net of \$334,116 of accumulated amortization at March 31, 2001	—	4,008,440
Strategic equity and convertible debt investments	—	28,023
Other assets	3,588	2,645
Total assets	<u>\$1,046,882</u>	<u>\$5,453,278</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 8,818	\$ 38,069
Accrued payroll and related expenses	7,618	17,868
Other accrued liabilities	6,448	30,583
Deferred revenue	2,776	5,087
Current portion of long-term debt	1,394	668
Current portion of capital lease obligations	729	596
Total current liabilities	27,783	92,871
Long-term debt, less current portion	3,599	1,216
Long-term capital lease obligations, less current portion	1,695	1,050
Deferred income taxes	—	120,040
Commitments and contingencies (Notes 7 and 10)		
Stockholders' equity:		
Preferred stock, \$0.01 par value:		
Authorized shares—2,000, none issued and outstanding	—	—
Common stock, \$0.01 par value:		
Authorized shares—630,000 at March 31, 2001		
Issued and outstanding shares—243,684 and 299,822 at March 31, 2000 and 2001, respectively	2,437	2,998
Additional paid-in capital	943,293	5,947,682
Deferred compensation, net	(1,443)	(348,894)
Accumulated other comprehensive income (loss)	(166)	2,438
Retained earnings (deficit)	70,139	(366,076)
Notes receivable from stockholders	(455)	(47)
Total stockholders' equity	<u>1,013,805</u>	<u>5,238,101</u>
Total liabilities and stockholders' equity	<u>\$1,046,882</u>	<u>\$5,453,278</u>

See accompanying notes.

(in thousands, except per share data)	Year Ended March 31,		
	1999	2000	2001
Net revenues	\$105,000	\$172,352	\$ 435,543
Cost of revenues ⁽¹⁾	<u>37,937</u>	<u>50,218</u>	<u>163,166</u>
Gross profit	67,063	122,134	272,377
Operating expenses:			
Research and development ⁽¹⁾	22,301	32,527	105,225
Selling, general and administrative ⁽¹⁾	17,795	28,035	69,232
Stock-based compensation ⁽¹⁾	701	452	79,730
Amortization of goodwill and purchased intangibles	—	—	308,835
Acquired in-process research and development	—	—	202,100
Merger-related costs	<u>2,350</u>	<u>—</u>	<u>—</u>
Total operating expenses	<u>43,147</u>	<u>61,014</u>	<u>765,122</u>
Operating income (loss)	23,916	61,120	(492,745)
Interest income, net	<u>3,450</u>	<u>12,872</u>	<u>55,449</u>
Income (loss) before income taxes	27,366	73,992	(437,296)
Income tax expense (benefit)	<u>10,233</u>	<u>25,367</u>	<u>(1,081)</u>
Net income (loss)	<u>\$ 17,133</u>	<u>\$ 48,625</u>	<u>\$ (436,215)</u>
Basic earnings (loss) per share:			
Earnings (loss) per share	<u>\$ 0.09</u>	<u>\$ 0.23</u>	<u>\$ (1.63)</u>
Shares used in calculating basic earnings (loss) per share	<u>196,112</u>	<u>215,640</u>	<u>267,363</u>
Diluted earnings (loss) per share:			
Earnings (loss) per share	<u>\$ 0.08</u>	<u>\$ 0.20</u>	<u>\$ (1.63)</u>
Shares used in calculating diluted earnings (loss) per share	<u>219,440</u>	<u>238,304</u>	<u>267,363</u>

⁽¹⁾For presentation purposes, the functional line items exclude stock-based compensation charges related to acquired companies as follows (in thousands):

Cost of revenues	\$ —	\$ —	\$ 2,820
Research and development	171	288	41,303
Selling, general and administrative	<u>530</u>	<u>164</u>	<u>35,607</u>
	<u>\$ 701</u>	<u>\$ 452</u>	<u>\$ 79,730</u>

See accompanying notes.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)	Common Stock		Additional Paid-In Capital	Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Deficit)	Notes Receivable From Stockholders	Total Stockholders' Equity
	Shares	Amount						
Balance, March 31, 1998	180,288	\$ 1,802	\$ 85,083	\$ (472)	\$ —	\$5,722	\$ (501)	\$ 91,634
Issuance of stock upon formation of Cimaron	18,752	186	4,478	(230)	—	—	—	4,434
Issuance of common stock under employee stock purchase plans	3,336	34	3,145	—	—	—	—	3,179
Issuance of stock pursuant to exercise of stock options	10,520	106	2,431	(964)	—	—	—	1,573
Tax benefit of disqualifying dispositions	—	—	4,209	—	—	—	—	4,209
Payment on notes	—	—	—	—	—	—	46	46
Deferred compensation related to stock options and restricted stock	—	—	1,317	(1,317)	—	—	—	—
Amortization of deferred compensation	—	—	—	860	—	—	—	860
Adjustment for change in Cimaron's year end	—	—	—	—	—	(1,341)	—	(1,341)
Comprehensive income:								
Net income	—	—	—	—	—	17,133	—	17,133
Unrealized loss on short-term investments, net of tax	—	—	—	—	(33)	—	—	(33)
Total comprehensive income	—	—	—	—	—	—	—	17,100
Balance, March 31, 1999	212,896	2,128	100,663	(2,123)	(33)	21,514	(455)	121,694
Issuance of stock, net of issuance costs	24,010	240	814,740	—	—	—	—	814,980
Issuance of common stock under employee stock purchase plans	524	6	2,498	—	—	—	—	2,504
Issuance of stock pursuant to exercise of stock options	6,366	63	10,313	—	—	—	—	10,376
Repurchase of restricted stock	(112)	—	(11)	—	—	—	—	(11)
Amortization of deferred compensation	—	—	—	611	—	—	—	611
Elimination of deferred compensation related to stock options forfeited	—	—	(69)	69	—	—	—	—
Tax benefit of disqualifying dispositions	—	—	15,159	—	—	—	—	15,159
Comprehensive income:								
Net income	—	—	—	—	—	48,625	—	48,625
Unrealized loss on short-term investments, net of tax	—	—	—	—	(133)	—	—	(133)
Total comprehensive income	—	—	—	—	—	—	—	48,492
Balance, March 31, 2000	243,684	2,437	943,293	(1,443)	(166)	70,139	(455)	1,013,805
Issuance of stock related to purchase acquisitions	46,232	462	4,775,395	—	—	—	(47)	4,775,810
Issuance of common stock under employee stock purchase plans	299	3	6,653	—	—	—	—	6,656
Issuance of stock pursuant to exercise of stock options	9,727	97	64,917	—	—	—	—	65,014
Repurchase of restricted stock	(120)	(1)	(8)	—	—	—	—	(9)
Deferred compensation related to stock options and restricted stock assumed as a result of acquisitions	—	—	—	(438,845)	—	—	—	(438,845)
Amortization of deferred compensation	—	—	—	79,848	—	—	—	79,848
Elimination of deferred compensation related to stock options forfeited	—	—	(11,546)	11,546	—	—	—	—
Tax benefit of disqualifying dispositions	—	—	168,978	—	—	—	—	168,978
Payment on notes	—	—	—	—	—	—	455	455
Comprehensive income:								
Net loss	—	—	—	—	—	(436,215)	—	(436,215)
Foreign currency translation loss	—	—	—	—	(73)	—	—	(73)
Unrealized gain on short-term investments, net of tax	—	—	—	—	2,677	—	—	2,677
Total comprehensive loss	—	—	—	—	—	—	—	(433,611)
Balance, March 31, 2001	299,822	\$2,998	\$5,947,682	\$ (348,894)	\$2,438	\$ (366,076)	\$ (47)	\$5,238,101

(in thousands)	Year Ended March 31,		
	1999	2000	2001
Operating Activities			
Net income (loss)	\$ 17,133	\$ 48,625	\$ (436,215)
Adjustment to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	7,045	8,039	16,135
Write-offs of inventories	180	701	172
Amortization of purchased intangibles and inventory fair value adjustment . . .	—	—	361,022
Acquired in-process research and development	—	—	202,100
Amortization of deferred compensation	860	611	79,848
Tax benefit of disqualifying dispositions	4,209	15,159	168,978
Loss on disposals of property	221	—	—
Adjustment for change in Cimaron year end	(1,341)	—	—
Changes in operating assets and liabilities:			
Accounts receivables	(7,096)	(6,184)	(42,272)
Inventories	(1,808)	(1,813)	(11,601)
Other assets	(678)	(7,417)	(9,621)
Accounts payable	(84)	3,687	16,416
Accrued payroll and other accrued liabilities	4,495	2,170	31,956
Deferred income taxes	(691)	425	(178,550)
Deferred revenue	(434)	1,337	1,403
Net cash provided by operating activities	22,011	65,340	199,771
Investing Activities			
Proceeds from sales and maturities of investments	187,787	1,847,446	2,773,758
Purchases of investments	(199,394)	(2,559,018)	(3,088,500)
Repayments (advances) on notes receivable from officers and employees	262	786	(18)
Purchase of property, equipment and other assets	(16,490)	(22,753)	(78,217)
Cash received from purchase acquisitions, net of cash paid and merger expenses . .	—	—	14,325
Net cash used for investing activities	(27,835)	(733,539)	(378,652)
Financing Activities			
Proceeds from issuance of common stock, net	9,062	827,860	71,670
Repurchase of common stock	—	(11)	(9)
Payments on notes receivable from stockholders	46	—	455
Payments on capital lease obligations	(2,110)	(1,214)	(779)
Payments on long-term debt	(792)	(1,864)	(4,288)
Proceeds from equipment financed under capital leases	2,342	—	—
Issuance of long-term debt	4,346	—	—
Other	—	—	(73)
Net cash provided by financing activities	12,894	824,771	66,976
Net increase (decrease) in cash and cash equivalents	7,070	156,572	(111,905)
Cash and cash equivalents at beginning of year	6,460	13,530	170,102
Cash and cash equivalents at end of year	\$ 13,530	\$ 170,102	\$ 58,197
Supplemental disclosure of cash flow information:			
Cash paid for:			
Interest	\$ 542	\$ 634	\$ 403
Income taxes	\$ 4,274	\$ 12,273	\$ 3,943

See accompanying notes.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BUSINESS

The Company designs, develops, manufactures and markets high-performance, high-bandwidth silicon solutions for the world's optical networks.

BASIS OF PRESENTATION

On September 9, 1999, March 23, 2000 and October 30, 2000, the Company effected two-for-one stock splits (in the form of 100% stock dividends); accordingly, all prior share, per share, common stock and stock option amounts in these financial statements have been restated to reflect the stock splits.

The consolidated financial statements include all the accounts of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS

Cash and cash equivalents consist of money market type funds and highly liquid debt instruments with original maturities of three months or less at the date of acquisition. Short-term investments consist of U.S. Treasury notes, obligations of U.S. government agencies, State, Municipal and County governments notes and bonds and corporate bonds. The Company maintains its excess cash in financial institutions with strong credit ratings and has not experienced any significant losses on its investments.

The Company classifies its short-term investments as "Available-for-Sale" and records such assets at the estimated fair value with unrealized gains and losses excluded from earnings and reported, net of tax, in comprehensive income (loss). The basis for computing realized gains or losses is by specific identification.

The following is a summary of available-for-sale securities (in thousands):

	Amortized Cost	Gross Unrealized		Estimated Fair Value
		Gains	Losses	
At March 31, 2001:				
U.S. Treasury securities and obligations				
of U.S. government agencies	\$ 26,984	\$ 109	\$ 5	\$ 27,088
State, Municipal and County government notes and bonds	388,689	1,510	—	390,199
Corporate debt securities	<u>654,418</u>	<u>2,304</u>	<u>113</u>	<u>656,609</u>
	<u>\$ 1,070,091</u>	<u>\$ 3,923</u>	<u>\$ 118</u>	<u>\$ 1,073,896</u>
At March 31, 2000:				
U.S. Treasury securities and obligations				
of U.S. government agencies	\$ 25,942	\$ —	\$ 118	\$ 25,824
State, Municipal and County government notes and bonds	397,645	30	14	397,661
Corporate debt securities	<u>361,132</u>	<u>26</u>	<u>194</u>	<u>360,964</u>
	<u>\$ 784,719</u>	<u>\$ 56</u>	<u>\$ 326</u>	<u>\$ 784,449</u>

Available-for-sale securities by contractual maturity are as follows:

(in thousands)	March 31, 2001
Due in one year or less	\$ 860,737
Due after one year through two years	146,269
Greater than two years	<u>66,890</u>
	<u>\$ 1,073,896</u>

STRATEGIC EQUITY AND CONVERTIBLE DEBT INVESTMENTS

The Company enters into certain equity investments for the promotion of business and strategic objectives, and typically does not attempt to reduce or eliminate the inherent market risks on these investments. These strategic investments are classified separately as strategic equity and convertible debt investments totaling \$28.0 million at March 31, 2001. The strategic equity and convertible debt instruments are valued at cost because the Company does not have the ability to exercise significant influence over the investees' operations and financial policies.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying value of cash equivalents, short-term investments, accounts receivable, accounts payable, accrued liabilities and long-term debt approximates fair value.

CONCENTRATION OF CREDIT RISK

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of available-for-sale securities and trade receivables. The Company believes that the credit risk in its trade receivables is mitigated by the Company's credit evaluation process, relatively short collection terms and dispersion of its customer base. The Company generally does not require collateral and has not experienced significant losses on trade receivables from any particular customer or geographic region for any period presented.

The Company invests its excess cash in debt instruments of the U.S. Treasury, governmental agencies and corporations with strong credit ratings. The Company has established guidelines relative to diversification and maturities that attempt to maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates. The Company has not experienced any significant losses on its cash equivalents or short-term investments.

USE OF ESTIMATES

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and disclosures made in the accompanying notes to the financial statements. These estimates include assessing the collectibility of accounts receivable, the use and recoverability of inventory, estimates to complete engineering contracts, costs of future product returns under warranty and provisions for contingencies expected to be incurred. Actual results could differ from those estimates.

INVENTORIES

Inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market. The Company's inventory valuation process is done on a part-by-part basis. Lower of cost or market adjustments, specifically identified on a part-by-part basis, reduce the carrying value of the related inventory and take into consideration reductions in sales prices, excess inventory levels and obsolete inventory. Once established, these adjustments are considered permanent and are not reversed until the related inventory is sold or disposed of. Additionally, in fiscal 2001, the Company has established general reserves to cover exposure related to the economic slowdown.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost and depreciated over the estimated useful lives of the assets (3 to 7 years) using the straight line method. Leasehold improvements are stated at cost and amortized over the useful life of the asset. Property and equipment under capital leases are recorded at the net present value of the minimum lease payments and are amortized over the useful life of the assets.

IMPAIRMENT OF LONG-LIVED ASSETS

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 121, "Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of," the Company records impairment losses on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated

to be generated by those assets are less than the assets' carrying amounts. SFAS No. 121 also addresses the accounting for long-lived assets that are expected to be disposed of. Through March 31, 2001, the Company has not experienced any such impairments.

ADVERTISING COST

Advertising costs are expensed as incurred.

REVENUES

Revenues related to product sales are generally recognized when title and risk of loss passes, which is generally when the products are shipped to the customer. Recognition of revenues and the related cost of revenues on shipments to distributors that are subject to terms of sale allowing for price protection and right of return on products unsold by the distributor are deferred until the distributor's ability to return the products or its rights to price protection lapse or have been limited. Revenues on engineering design contracts are recognized using the percentage-of-completion method based on actual cost incurred to date compared to total estimated costs of the project. Deferred revenue represents both the margin on shipments of products to distributors that will be recognized when the distributors ship the products to their customers or the right of return has lapsed and billings in excess and estimated earnings on uncompleted engineering design contracts.

WARRANTY RESERVES

Estimated expenses for warranty obligations are accrued as revenue is recognized. Reserve estimates are adjusted periodically to reflect actual experience.

RESEARCH AND DEVELOPMENT

Research and development costs are expensed as incurred. Substantially all research and development expenses are related to new product development, designing significant improvements to existing products and new process development.

STOCK-BASED COMPENSATION

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations in accounting for its employee and director stock options because the alternative fair value accounting provided for under SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), requires the use of option valuation models that were not developed for use in valuing employee and director stock options. Under SFAS 123, compensation cost is determined using the fair value of stock-based compensation determined as of the grant date and is recognized over the periods in which the related services are rendered. The statement also permits companies to elect to continue using the current implicit value accounting method specified in APB 25 to account for stock-based compensation and disclose in the footnotes to the financial statements the pro forma effect of using the fair value method for its stock-based compensation.

SEGMENTS OF A BUSINESS ENTERPRISE

FASB Statement No. 131 ("Statement No. 131"), "Disclosures about Segments of an Enterprise and Related Information," establishes standards for the way that public business enterprises report selected information about operating segments in annual consolidated financial statements and requires those enterprises report selected information about operating segments in interim financial reports. Statement No. 131 also establishes standards for related disclosures about products and services, geographic areas and major customers. The Company operates in one segment.

RECENT ACCOUNTING PRONOUNCEMENTS

In September 2000, the Emerging Issues Task Force issued EITF 00-23, "Issues Related to the Accounting for Stock Compensation under APB 25 and FASB Interpretation No. 44" ("EITF 00-23"). EITF 00-23 addresses, among other things, the treatment of the tax benefits realized from the exercise of certain stock options assumed in an acquisition. The Company has made certain adjustments to the value of goodwill recorded in its purchase acquisitions in accordance with this guidance.

In March 2000, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 44 (“Interpretation”), “Accounting for Certain Transactions Involving Stock Compensation—An Interpretation of Accounting Principles Board Opinion No. 25,” clarifying the guidance for certain stock compensation issues, including the treatment of unvested stock and stock options issued in purchase business combinations. The Interpretation requires that unvested stock and stock options granted by the acquiring Company in exchange for unvested stock and stock options held by employees of the target company be accounted for at fair value and such amount be recorded as deferred compensation by the acquiring company. Accordingly, the Company recorded approximately \$2.4 million, \$43.4 million, \$391.8 million and \$1.2 million in deferred compensation in conjunction with the acquisitions of YuniNetworks, SiLUTIA, MMC and RTC, respectively (Note 2). Additionally, the Interpretation requires companies to value vested options at fair value and include such value in the determination of the total value of consideration issued in a transaction.

In December 1999, the Securities and Exchange Commission (“SEC”) issued Staff Accounting Bulletin (“SAB”) No. 101, “Revenue Recognition in Financial Statements,” which provides guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC. The Company adopted SAB No. 101 in the quarter ended March 31, 2001. The adoption of SAB No. 101 did not have an impact on the Company’s results of operation.

In June 1998, the FASB issued SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities,” which establishes accounting and reporting standards for derivative instruments and hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. Management does not believe this will have a material effect on the Company’s operations. Implementation of this standard has recently been delayed by the FASB for a 12-month period. The Company will now adopt SFAS No. 133 as required for its first quarterly filing of fiscal year 2002.

RECLASSIFICATION

Certain prior period amounts have been reclassified to conform to the current period presentation.

EARNINGS (LOSS) PER SHARE

Shares used in basic earnings (loss) per share are computed using the weighted-average number of common shares outstanding during each period. Shares used in diluted earnings (loss) per share include the dilutive effect of common shares potentially issuable upon the exercise of stock options. The reconciliation of shares used to calculate basic and diluted earnings (loss) per share consists of the following:

(in thousands)	Year Ended March 31,		
	1999	2000	2001
Shares used in basic earnings (loss) per share computations—			
weighted-average common shares outstanding	196,112	215,640	267,363
Net effect of dilutive common share equivalents based on treasury stock method	<u>23,328</u>	<u>22,664</u>	<u>—</u>
Shares used in diluted earnings (loss) per share computations	<u>219,440</u>	<u>238,304</u>	<u>267,363</u>

Because the Company incurred a loss in the year ended March 31, 2001, the effect of dilutive securities totaling 22,260,000 equivalent shares have been excluded from the loss per share computation as their impact would be antidilutive.

2. ACQUISITIONS

FISCAL 2001 ACQUISITIONS

The Company completed a number of acquisitions in fiscal 2001 using the purchase method of accounting. The accompanying consolidated financial statements include the results of operations of each company acquired from the date of acquisition. The acquired companies are as follows:

MMC Networks, Inc.—On October 25, 2000, the Company acquired MMC, a fabless semiconductor company that provides network processors, traffic management and switch fabric ICs. Under the terms of the merger agreement,

in exchange for all of the outstanding stock of MMC, the Company issued 41,392,404 shares of its common stock and assumed options to purchase 7,981,595 shares of its common stock.

YuniNetworks, Inc.—On June 8, 2000, the Company completed the acquisition of YuniNetworks, a developer of scalable switch fabric ICs. Under the terms of the merger agreement, in exchange for all YuniNetworks' shares of common and preferred stock, the Company issued 4,048,646 shares of its common stock and assumed options to purchase 225,776 shares of its common stock. Pursuant to a separate agreement, AMCC purchased 10% of the YuniNetworks' shares held by the majority stockholder of YuniNetworks for \$8.9 million in cash.

Other—The Company also completed the acquisitions of pBaud, Chameleon, SiLUTIA and RTC for a total purchase price of \$73.2 million.

In connection with these transactions, the Company conducted independent valuations of the intangible assets acquired in order to allocate the purchase price in accordance with Accounting Principles Board Opinion No. 16. The Company has allocated the excess purchase price over the fair value of net tangible assets acquired to the following identifiable intangible assets: developed core and existing technology, assembled workforce, acquired in-process research and development (“IPR&D”) and trademarks/tradenames. The total purchase price was allocated as follows:

(in thousands)	MMC	YuniNetworks	Other	Total
Net tangible assets (liabilities)	\$ 126,866	\$ 2,118	\$ (1,457)	\$ 127,527
In-process research and development	176,700	21,800	3,600	202,100
Goodwill and other intangibles	4,128,686	192,365	42,935	4,363,986
Deferred tax liabilities	(301,129)	—	(16,420)	(317,549)
Deferred compensation	391,821	2,488	44,536	438,845
Purchased inventory fair value adjustment	26,907	—	—	26,907
Total consideration	<u>\$4,549,851</u>	<u>\$218,771</u>	<u>\$ 73,194</u>	<u>\$4,841,816</u>

Total consideration issued in the purchase acquisitions is as follows:

(in thousands)	MMC	YuniNetworks	Other	Total
Value of securities issued	\$3,919,108	\$197,545	\$ 62,356	\$4,179,009
Assumption of options	<u>578,093</u>	<u>11,467</u>	<u>7,288</u>	<u>596,848</u>
	4,497,201	209,012	69,644	4,775,857
Cash paid and merger fees	<u>52,650</u>	<u>9,759</u>	<u>3,550</u>	<u>65,959</u>
	<u>\$4,549,851</u>	<u>\$218,771</u>	<u>\$ 73,194</u>	<u>\$4,841,816</u>

In accordance with EITF 00-23, which was issued in September 2000, the amount of goodwill has been adjusted for certain tax benefits related to the exercise of stock options assumed through our acquisitions. The total adjustment to goodwill related to these totaled \$21.4 million for the year ended March 31, 2001.

The purchased inventory fair value adjustment represents the difference between the carrying value of work in process and finished goods inventory and the estimated selling price of the related inventory at the date of acquisition. This adjustment was fully charged to cost of sales in the year ended March 31, 2001 as the related inventory was sold.

The related purchased IPR&D for each of the above acquisitions represents the present value of the estimated after-tax cash flows expected to be generated by the purchased technology, which, at the acquisition dates, had not yet reached technological feasibility. The cash flow projections for revenues were based on estimates of relevant market sizes and growth factors, expected industry trends, the anticipated nature and timing of new product introductions by the Company and its competitors, individual product sales cycles and the estimated life of each product's underlying technology. Estimated operating expenses and income taxes were deducted from estimated revenue projections to arrive at

estimated after-tax cash flows. Projected operating expenses include cost of goods sold, marketing and selling expenses, general and administrative expenses and research and development, including estimated costs to maintain the products once they have been introduced into the market and are generating revenue. The remaining identified intangibles, including goodwill, will be amortized on a straight-line basis over lives ranging from one to six years.

The following unaudited pro forma summary presents the consolidated results of operations of the Company, excluding acquired IPR&D charges above, as if the acquisitions had occurred at the beginning of each period presented and does not purport to be indicative of what would have occurred had the acquisition been made as of that date or of the results that may occur in the future:

(in thousands, except per share data)	Year Ended March 31,	
	2000	2001
Net sales	\$ 227,315	\$ 508,092
Net loss	\$ (843,530)	\$ (849,414)
Basic loss per share	\$ (3.91)	\$ (3.18)

FISCAL 1999 ACQUISITIONS

In March 1999, the Company acquired all of the outstanding common stock and common stock equivalents of Cimaron in exchange for approximately 24 million shares of the Company's common stock. Cimaron designs and develops high-bandwidth silicon solutions for communication equipment manufacturers. The acquisition was accounted for using the pooling-of-interests method of accounting. Prior to the combination, Cimaron had a fiscal year end of December 31. In recording the business combination, Cimaron's results of operations for the fiscal year ended December 31, 1998 were combined with AMCC's for the fiscal year ended March 31, 1999. Cimaron's net sales and net loss for the three-month period ended March 31, 1999 were \$110,000 and \$(1,341,000), respectively. Cimaron's results of operations and cash flows for the three-month period ended March 31, 1999 have been added directly to the retained earnings and cash flows of AMCC and excluded from reported fiscal 1999 results of operations.

In April 1998, the Company acquired Ten Mountains Design, which designs and develops high-bandwidth analog devices for communications equipment suppliers and optical module manufacturers. The financial statements include the results of operations for Ten Mountains Design from the date of acquisition.

Net goodwill and other acquisition-related intangibles at fiscal years ending March 31 were as follows:

(in thousands)	Life in Years	2000	2001
Goodwill	1-6	\$—	\$3,708,191
Developed core technology	5	—	268,836
Other intangibles	3-5	—	31,413
		\$—	\$4,008,440

Other intangibles include items such as trademarks and workforce-in-place. The total balances presented above are net of accumulated amortization of \$334.1 million at March 31, 2001.

During 2001, the Company recorded acquisition-related purchase consideration of \$438.8 million as deferred stock-based compensation. This amount represents the portion of the purchase consideration related to shares issued contingent on continued employment of certain employee stockholders and the intrinsic value of stock options assumed that are earned as future services are provided by the employees. The compensation is being recognized over the related vesting period. The related expenses are identified with research and development, cost of revenues and selling, general and administrative depending on the function of the individual employee providing services. However, for presentation purposes, the amounts have been footnoted on the face of the income statement and excluded from the functional line items.

3. CERTAIN FINANCIAL STATEMENT INFORMATION

(in thousands)	March 31,	
	2000	2001
Inventories:		
Finished goods	\$ 2,666	\$ 16,363
Work in process	6,966	14,560
Raw materials	1,293	1,817
	<u>\$ 10,925</u>	<u>\$ 32,740</u>
Property and equipment:		
Machinery and equipment	\$ 46,302	\$ 70,358
Leasehold improvements	8,352	18,292
Computers, office furniture and equipment	20,743	73,181
Land	4,881	22,122
	<u>80,278</u>	<u>183,953</u>
Less accumulated depreciation and amortization	<u>(42,436)</u>	<u>(71,000)</u>
	<u>\$ 37,842</u>	<u>\$ 112,953</u>
Other accrued liabilities:		
Income taxes payable	\$ 839	\$ 12,564
Other	5,609	18,019
	<u>\$ 6,448</u>	<u>\$ 30,583</u>

Cost of revenues includes certain amortization of purchased intangibles and other acquisition-related charges as follows:

(in thousands)	Fiscal Year Ended March 31,		
	1999	2000	2001
Amortization of developed core technology	\$—	\$ —	\$ 25,280
Amortization of purchased inventory fair value adjustment (see Note 2)	—	—	26,907
	<u>\$—</u>	<u>\$ —</u>	<u>\$ 52,187</u>

The cost and accumulated amortization of machinery and equipment under capital leases at March 31, 2001 were approximately \$3.1 million and \$1.7 million, respectively (\$10.5 million and \$8.7 million at March 31, 2000, respectively). Amortization of assets held under capital leases is included with depreciation expense.

During the years ended March 31, 1999, 2000 and 2001, the Company earned interest income of \$3,992,000, \$13,506,000 and \$55,852,000, respectively, and incurred interest expense of \$542,000, \$634,000 and \$403,000, respectively.

4. LONG-TERM DEBT

The Company has various term notes, with monthly payments totaling \$64,000 including interest, payable over 60 months, at interest rates between 6.5% and 7.35%. At March 31, 2001, approximately \$1.9 million was outstanding on the notes.

Principal maturities of the notes payable at March 31, 2001 are as follows (in thousands):

Year Ending March 31,	
2002	\$ 668
2003	714
2004	502
	<u>\$ 1,884</u>

5. STOCKHOLDERS' EQUITY

AUTHORIZED SHARES

On August 29, 2000, the Company's stockholders approved an increase in the number of authorized shares of common stock to 630 million.

STOCK OPTIONS AND OTHER STOCK AWARDS

The Company has in effect several stock-based plans under which nonqualified and incentive stock options have been granted to employees and directors. At March 31, 2001, approximately 54.5 million stock options were outstanding and 25.7 million shares were available for future grant under these plans.

The Compensation Committee of the Board of Directors determines eligibility, vesting schedules and exercise prices for options granted under the plans. Options and other stock awards under the plans expire not more than ten years from the date of grant and are either exercisable immediately after the date of grant and subject to certain repurchase rights by the Company until such ownership rights have vested or are exercisable upon vesting. Vesting generally occurs over four to five years. At March 31, 2000 and 2001, 1.1 million and 2.0 million shares of common stock were subject to repurchase, respectively. Options are granted at prices at least equal to fair value of the Company's common stock on the date of grant.

Pro forma information regarding net income and net income per share is required by SFAS No. 123 and has been determined as if the Company had accounted for its employee stock options under the fair value method of that statement. The fair value of the options was estimated at the date of grant using the Black Scholes method.

The fair value of options granted in fiscal 1999, 2000 and 2001 reported below has been estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions:

	Fiscal Year Ended March 31,		
	1999	2000	2001
Expected life (in years)	4.5	4.0	4.0
Risk-free interest rate	6.0%	6.0%	6.0%
Volatility	0.89	0.82	1.33
Dividend yield	0%	0%	0%

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in the opinion of management, the existing models do not necessarily provide a reliable single measure of the fair value of its options. The weighted-average estimated fair value of employee stock options granted during fiscal 1999, 2000 and 2001, including options assumed through acquired companies, was \$2.64, \$20.14 and \$52.86 per share, respectively. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods. The Company's pro forma information is as follows:

(in thousands, except per share amounts)	Fiscal Year Ended March 31,		
	1999	2000	2001
Pro forma net income (loss)	\$13,202	\$19,385	\$(681,862)
Pro forma basic earnings (loss) per share	\$ 0.07	\$ 0.09	\$ (2.55)
Pro forma diluted earnings (loss) per share	\$ 0.06	\$ 0.08	\$ (2.55)

A summary of the Company's stock option activity, including those issued outside of the plans, and related information are as follows:

	Fiscal Year Ended March 31,					
	1999	2000		2001		
(shares in thousands)	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding at beginning of year	21,460	\$0.86	21,388	\$ 2.02	40,566	\$22.16
Granted and assumed	12,162	2.31	27,596	31.76	24,580	47.90
Exercised	(10,520)	0.15	(6,366)	1.63	(9,727)	6.68
Forfeited	(1,714)	1.04	(2,052)	4.83	(953)	39.83
Outstanding at end of year	<u>21,388</u>	<u>\$2.02</u>	<u>40,566</u>	<u>\$22.16</u>	<u>54,466</u>	<u>\$36.22</u>
Vested at end of year	<u>5,428</u>	<u>\$0.91</u>	<u>7,798</u>	<u>\$ 4.20</u>	<u>13,757</u>	<u>\$23.02</u>

The following is a further breakdown of the options outstanding at March 31, 2001 (shares in thousands):

Range of Exercise Prices	Number Outstanding	Weighted-Average Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$ 0.03-\$ 3.44	6,873	6.59	\$ 1.70	4,115	\$ 1.42
\$ 3.45-\$ 6.48	8,522	7.98	\$ 5.85	2,625	\$ 5.78
\$ 6.49-\$ 22.97	7,926	8.38	\$14.75	2,149	\$13.56
\$22.98-\$ 35.98	6,845	8.89	\$31.91	1,704	\$33.17
\$35.99-\$ 53.88	7,973	9.53	\$50.97	562	\$48.25
\$53.89-\$ 69.25	5,531	9.47	\$65.16	296	\$59.40
\$69.26-\$ 70.44	7,338	8.95	\$70.43	1,704	\$70.43
<u>\$70.45-\$104.25</u>	<u>3,458</u>	<u>9.40</u>	<u>\$84.61</u>	<u>602</u>	<u>\$75.24</u>
<u>\$ 0.03-\$104.25</u>	<u>54,466</u>	<u>8.58</u>	<u>\$36.22</u>	<u>13,757</u>	<u>\$23.02</u>

EMPLOYEE STOCK PURCHASE PLANS

The Company has in effect various employee stock purchase plans under which 6.6 million shares of common stock have been reserved for issuance. Under the terms of the plans, purchases are made semiannually and the purchase price of the common stock is equal to 85% of the fair market value of the common stock on the first or last day of the offering period, whichever is lower. At March 31, 2001, approximately 4.2 million shares had been issued under the plans and approximately 2.4 million shares were available for future issuance.

COMMON SHARES RESERVED FOR FUTURE ISSUANCE

At March 31, 2001, the Company has the following shares of common stock reserved for issuance upon the exercise of equity instruments (in thousands):

Stock options:	
Issued and outstanding	54,466
Authorized for future grants	25,699
Stock purchase plans	<u>2,443</u>
	<u>82,608</u>

6. INCOME TAXES

The provision for income taxes consists of the following:

(in thousands)	Fiscal Year Ended March 31,		
	1999	2000	2001
Current:			
Federal	\$ 9,860	\$21,966	\$ —
Foreign	—	—	202
State	1,064	2,976	308
Total current	10,924	24,942	510
Deferred:			
Federal	(362)	65	(1,392)
State	(329)	360	(199)
Total deferred	(691)	425	(1,591)
	<u>\$10,233</u>	<u>\$25,367</u>	<u>\$ (1,081)</u>

The provision for income taxes reconciles to the amount computed by applying the federal statutory rate (35%) to income before income taxes as follows:

(in thousands)	Fiscal Year Ended March 31,					
	1999		2000		2001	
	\$	%	\$	%	\$	%
Tax at federal statutory rate	\$ 9,578	35%	\$25,897	35%	\$ (153,053)	35%
Goodwill	—	—	—	—	70,735	(16)
In-process research and development	—	—	—	—	106,152	(24)
Foreign sales corporation	(387)	(1)	(873)	(1)	—	—
Tax exempt interest	—	—	(312)	—	(8,231)	2
State taxes, net of federal benefit	478	1	2,294	3	3,042	(1)
Federal tax credits	(1,216)	(5)	(2,122)	(3)	(17,000)	4
State tax credits	—	—	(1,097)	(2)	(5,760)	1
Merger costs and deferred compensation	763	3	213	—	2,841	(1)
Other	1,017	4	1,367	2	193	—
	<u>\$10,233</u>	<u>37%</u>	<u>\$25,367</u>	<u>34%</u>	<u>\$ (1,081)</u>	<u>—</u>

Significant components of the Company's deferred tax assets and liabilities for federal and state income taxes are as shown below:

(in thousands)	March 31,		
	1999	2000	2001
Deferred tax assets:			
Inventory write-downs and other reserves	\$1,850	\$2,433	\$ 14,470
Net operating loss carryforwards	1,719	—	127,531
Capitalization of inventory and research and development costs	313	405	2,208
Research and development credit carryforwards	298	1,364	29,126
State income taxes	47	140	—
Other credit carryforwards	447	—	1,235
Total deferred tax assets	4,674	4,342	174,570
Deferred tax liabilities:			
Depreciation and amortization	(101)	(194)	(547)
Purchase accounting	—	—	(266,466)
Total deferred tax liabilities	(101)	(194)	(267,013)
Net deferred tax assets (liabilities)	<u>\$4,573</u>	<u>\$4,148</u>	<u>\$ (92,443)</u>

At March 31, 2001, the Company has federal and state research and development tax credit carryforwards of approximately \$22.0 million and \$10.0 million, respectively, which will begin to expire in 2019 unless previously utilized. The Company also has federal and state net operating loss carryforwards of approximately \$352.0 million and \$95.0 million, respectively, which will begin to expire in 2012 and 2004, respectively.

7. COMMITMENTS

The Company leases certain of its facilities under long-term operating leases, which expire at various dates through 2010. The lease agreements frequently include renewal provisions, which require the Company to pay taxes, insurance and maintenance costs and contain escalation clauses based upon increases in the Consumer Price Index or defined rent increases. The Company also leases certain engineering design software tools under noncancellable operating leases expiring through 2003.

Annual future minimum lease payments, including machinery and equipment under capital leases as of March 31, 2001 are as follows (in thousands):

Year Ending March 31,	Operating Leases	Capital Leases
2002	\$22,285	\$ 691
2003	15,144	449
2004	9,159	679
2005	7,880	—
2006	3,943	—
Thereafter	<u>6,979</u>	—
Total minimum lease payments	<u>\$65,390</u>	1,819
Less amount representing interest		<u>173</u>
Present value of remaining minimum capital lease payments (including current portion of \$596)		<u>\$1,646</u>

Rent expense (including short-term leases and net of sublease income) for the years ended March 31, 1999, 2000 and 2001 was \$1.4 million, \$1.6 million and \$3.7 million, respectively.

8. EMPLOYEE RETIREMENT PLAN

Effective January 1, 1986, the Company established a 401(k) defined contribution retirement plan (the "Retirement Plan") covering all full-time employees with greater than three months of service. The Retirement Plan provides for voluntary employee contributions from 1% to 20% of annual compensation, subject to a maximum limit allowed by Internal Revenue Service guidelines. The Company may contribute such amounts as determined by the Board of Directors. Employer contributions vest to participants at a rate of 20% per year of service, provided that after five years of service all past and subsequent employer contributions are 100% vested. The Company has an additional plan that it sponsors. This plan was assumed through the acquisition of MMC. The total contributions under both plans charged to operations totaled \$573,000, \$677,000 and \$1.2 million for the years ended March 31, 1999, 2000 and 2001, respectively.

9. SIGNIFICANT CUSTOMER AND GEOGRAPHIC INFORMATION

During the years ended March 31, 1999, 2000 and 2001, 19%, 26% and 10%, respectively, of net revenues were from Nortel. In fiscal 1999, 2000 and 2001, Insight Electronics, a domestic distributor, accounted for 13%, 17% and 19% of net revenues, respectively. Additionally, in 1999, Raytheon Systems Co. accounted for 16% of net revenues. No other customer accounted for more than 10% of revenues in any fiscal year.

Net revenues by geographic region were as follows:

(in thousands)	Year Ended March 31,		
	1999	2000	2001
Net revenues:			
North America	\$ 79,771	\$132,119	\$337,644
Europe and Israel	18,136	28,980	56,807
Asia	<u>7,093</u>	<u>11,253</u>	<u>41,092</u>
	<u>\$105,000</u>	<u>\$172,352</u>	<u>\$435,543</u>

10. CONTINGENCIES

The Company is party to various claims and legal actions arising in the normal course of business, including notification of possible infringement on the intellectual property rights of third parties.

Starting in April 2001, a series of similar federal complaints were filed against the Company and its chief executive officer, chief financial officer and certain other executive officers and directors of the Company. These complaints allege essentially identical violations of the Securities Exchange Act of 1934 (the "1934 Act"). The complaints have been brought as purported shareholder class actions under Sections 10(b) and 20(a) of the 1934 Act and Rule 10b-5 promulgated thereunder and seek unspecified monetary damages on behalf of the shareholder class. In general, the complaints allege that the Company and the individual defendants misrepresented the Company's financial prospects for the fourth quarter of fiscal 2001 to inflate the value of the Company's stock. We anticipate that the complaints pending in federal court will be consolidated into a single proceeding. In addition, in May 2001, certain individuals filed derivative actions against the directors and certain executive officers in the California state courts. These state court derivative complaints allege overstatement of the financial prospects of the Company, mismanagement, inflation of stock value, and sale of stock at inflated prices for personal gain during the time period from November 2000 through February 2001. The Company has not yet responded to any of these lawsuits, and no discovery has been conducted. The Company believes that the allegations in each of these actions are without merit and intends to defend the actions vigorously. The actions have been tendered to the Company's insurance carriers.

Since 1993, the Company has been named as a potentially responsible party ("PRP") along with a large number of other companies that used Omega Chemical Corporation ("Omega") in Whittier, California to handle and dispose of certain hazardous waste material. The Company is a member of a large group of PRPs that has agreed to fund certain remediation efforts at the Omega site for which the Company has accrued approximately \$100,000. On September 14, 2000, the Company entered into a consent decree with the Environmental Protection Agency, pursuant to which the Company agreed to fund its proportionate share of the initial remediation efforts at the Whittier site. Although the ultimate outcome of these matters is not presently determinable, management believes that the resolution of all such pending matters, net of amounts accrued, will not have a material adverse affect on the Company's financial position or liquidity; however, there can be no assurance that the ultimate resolution of these matters will not have a material impact on the Company's results of operations in any period.

11. RELATED PARTY TRANSACTIONS

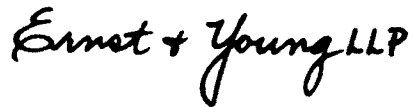
In August 2000, the Company made a strategic equity investment of \$10 million in Raza Foundries, which is included in the total strategic equity investments of \$28 million as of March 31, 2001. The Chief Executive Officer and Chairman of the Board of Directors of Raza Foundries is a member of the Company's Board of Directors.

THE BOARD OF DIRECTORS
APPLIED MICRO CIRCUITS CORPORATION

We have audited the accompanying consolidated balance sheets of Applied Micro Circuits Corporation as of March 31, 2000 and 2001, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended March 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Applied Micro Circuits Corporation at March 31, 2000 and 2001, and the consolidated results of its operations and its cash flows for each of the three years in the period ended March 31, 2001, in conformity with accounting principles generally accepted in the United States.

The logo for Ernst & Young LLP, featuring the company name in a stylized, handwritten script font.

Ernst & Young LLP
San Diego, California
April 20, 2001

QUARTERLY FINANCIAL INFORMATION FOR FISCAL 2000 AND FISCAL 2001

(in thousands, except per share data)	Fiscal Year Ended March 31,							
	2000				2001			
Fiscal quarter	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net revenues	\$31,643	\$37,898	\$45,762	\$57,049	\$74,188	\$97,007	\$ 143,269	\$ 121,079
Gross profit	\$21,360	\$26,572	\$32,553	\$41,649	\$54,874	\$72,475	\$ 82,073	\$ 62,955
Net income (loss)	\$ 6,786	\$ 9,097	\$12,112	\$20,630	\$ 3,395	\$23,615	\$ (269,487)	\$ (193,738)
Basic earnings								
(loss) per share	\$ 0.03	\$ 0.04	\$ 0.06	\$ 0.09	\$ 0.01	\$ 0.09	\$ (0.95)	\$ (0.65)
Diluted earnings								
(loss) per share	\$ 0.03	\$ 0.04	\$ 0.05	\$ 0.08	\$ 0.01	\$ 0.09	\$ (0.95)	\$ (0.65)

MARKET PRICE OF COMMON STOCK

The Company's common stock is traded on the Nasdaq Market System ("Nasdaq") under the symbol AMCC. The table below sets forth, for the fiscal quarters indicated, the high, low and quarter-end sale prices of the common stock as reported by Nasdaq (rounded to the nearest whole cent).

Fiscal quarter	Fiscal Year Ended March 31,							
	2000				2001			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
High	\$10.63	\$16.75	\$32.09	\$79.44	\$74.63	\$109.75	\$109.25	\$88.25
Low	\$ 5.14	\$ 9.53	\$13.59	\$25.27	\$32.75	\$ 47.75	\$ 45.88	\$16.13
End	\$10.28	\$14.25	\$31.32	\$75.03	\$49.38	\$103.53	\$ 75.05	\$16.50

The Company has never paid dividends on its common stock and presently intends to continue this policy. There were approximately 816 stockholders of record as of March 31, 2001.

CORPORATE HEADQUARTERS
APPLIED MICRO CIRCUITS CORPORATION
(AMCC)

6290 Sequence Drive
San Diego, CA 92121-4358
Phone: (858) 450-9333
Fax: (858) 450-9885

INVESTOR INFORMATION

Exchange: Nasdaq Stock Market
Symbol: AMCC

INQUIRIES CONCERNING THE COMPANY

Applied Micro Circuits Corporation welcomes inquiries from its stockholders and other interested investors. For additional copies of this report, the Form 10-K or other information, please contact:

AMCC

Debra K. Hart
Investor Relations Manager
6290 Sequence Drive
San Diego, CA 92121-4358
Phone: (858) 535-4217
Fax: (858) 597-7326

You are invited to visit our home page on the World Wide Web at www.amcc.com for more information. You'll find background on the Company and its products, financial data and other information that may be of interest to investors.

TRANSFER AGENT AND REGISTRAR

Questions regarding misplaced stock certificates, change of address or the consolidation of accounts should be addressed to the Company's transfer agent:

Computershare Investor Services, LLC
Shareholder Communications Team
P.O. Box A3504
Chicago, IL 60690-3504
Phone: (312) 588-4143
www.computershare.com
www.webqueries@computershare.com

ANNUAL MEETING

The AMCC annual meeting of stockholders will be held at 10:00 a.m. on Thursday, August 30, 2001, at AMCC's facility located at 6290 Sequence Drive, San Diego, CA.

INDEPENDENT AUDITORS

Ernst & Young LLP
501 W. Broadway, Suite 1100
San Diego, CA 92101

CORPORATE COUNSEL

Cooley Godward LLP
4365 Executive Drive, Suite 1100
San Diego, CA 92121

BOARD OF DIRECTORS

David M. Rickey
Chairman of the Board,
Chief Executive Officer and President
Applied Micro Circuits Corporation

Roger A. Smullen, Sr.
Vice Chairman of the Board

William K. Bowes, Jr.⁽²⁾
General Partner
US Venture Partners

Franklin P. Johnson, Jr.⁽²⁾
General Partner
Asset Management Company

L. Wayne Price⁽²⁾
Chief Technical Officer
Valiant Networks

S. Atiq Raza^{(1),(3)}
President and CEO
Raza Foundries, Inc.

Douglas C. Spreng
Senior Vice President, Switch Fabric
and Network Processing Business Unit
and President of MMC Networks

Arthur B. Stabenow^{(1),(3)}
Former Chairman,
President and Chief Executive Officer
Micro Linear Corporation

Harvey P. White^{(1),(3)}
Chairman, President and
Chief Executive Officer
Leap Wireless International

⁽¹⁾Member of the Compensation Committee

⁽²⁾Member of the Audit Committee

⁽³⁾Member of the Nominating Committee

OFFICERS

David M. Rickey
Chairman of the Board,
Chief Executive Officer and President

Roger A. Smullen, Sr.
Vice Chairman of the Board

William E. Bendush
Senior Vice President,
Chief Financial Officer and Secretary

Brent E. Little
Senior Vice President, Marketing

Douglas C. Spreng
Senior Vice President, Switch Fabric
and Network Processing Business Unit
and President of MMC Networks

Ramakrishna P. Sudireddy
Senior Vice President,
Digital Products

Thomas L. Tullie
Senior Vice President, Sales and Operations

Gregory A. Winner
Senior Vice President, Engineering

Vincent J. DeMaioribus
Vice President, Manufacturing

Joel O. Holliday
Vice President

Candace H. Kilburn
Vice President, Human Resources

John J. LoMedico
Vice President, Marketing and Applications,
Digital Products

Gary D. Martin
Chief Technical Officer, Digital Products

Patrick McGinty
Chief Information Officer

Monte H. Reed
Vice President, Controller

Terrence S. Rogers
Vice President, North American Sales

Stephen M. Smith
Vice President, Business Development

David Mersten
General Counsel and Assistant Secretary

Other MMC Networks Officers:
Frederick J. Berkowitz
Senior Vice President, Engineering

Ari Birger
Vice President, Customer Engineering

Jeffrey J. Cashen
Vice President, Sales

Andrew J. Gottlieb
Vice President, Marketing

Timothy M. Heenan
Vice President, Operations

Alexander Joffe
Chief Technical Officer

Yehuda Shaik
Vice President
Managing Director, Israel

Technology Office of the CEO:

Bruce H. Coy
Alexander Joffe
Dr. Gary D. Martin
Dr. Kenneth Y. Yung



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