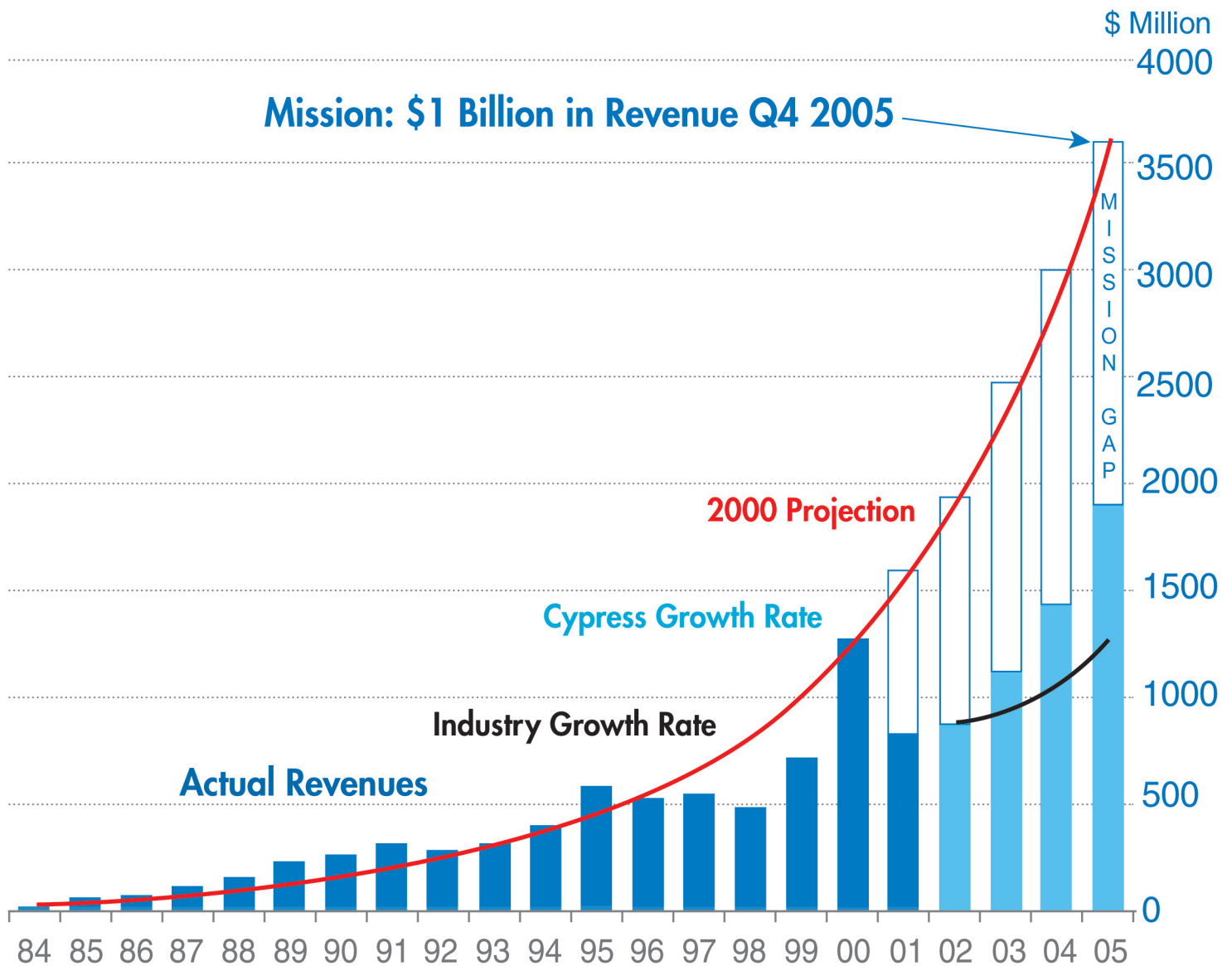


# CYPRESS

## 2 0 0 1      A N N U A L      R E P O R T

*We believe that 2001 will be a difficult year for the semiconductor industry. We also believe Cypress will traverse the year stably and profitably, despite industry problems.*

T.J.Rodgers, 2000 Annual Report



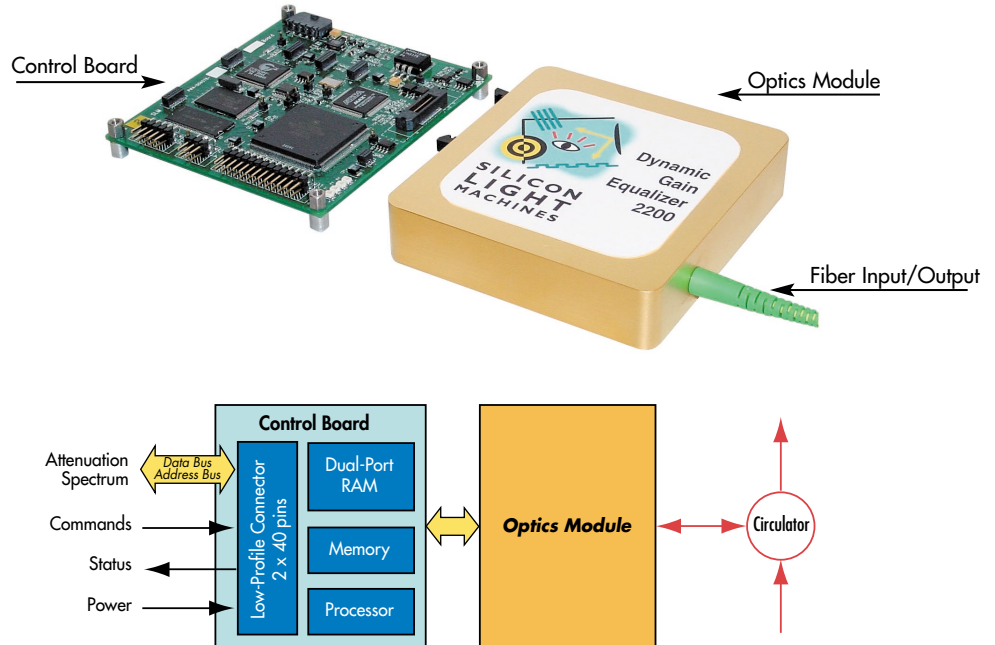
Driving the Communications Revolution™

# Cypress and Silicon Light Machines Bringing the Power of Silicon to Light™

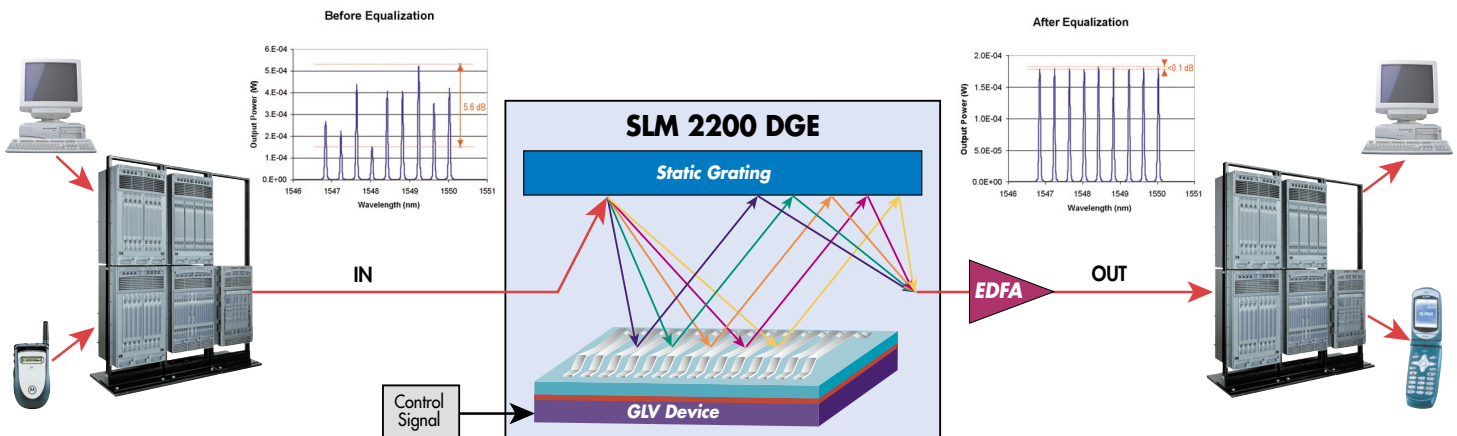
*Optical technology is necessary to drive large volumes of data over long distances. Cypress acquired Silicon Light Machines in August 2000 to produce optical telecommunications products that bridge the gap between current and future performance levels.*

## The SLM 2200 Dynamic Gain Equalizer

SLM recently announced its first optical telecommunications product: the SLM 2200 dynamic gain equalizer (DGE). The SLM 2200 is comprised of three parts: an input/output to guide light-waves through an optics module; an optics module containing an optical MEMS (microelectromechanical machine system) device based on SLM's proprietary Grating Light Valve™ (GLV™) technology, which separates light into its individual colors (wavelengths) and performs the wavelength equalization; and a control board that enables a telecom company to reprogram the DGE in real-time, rather than having to turn off a system and endure costly downtime.



The control board includes a variety of Cypress integrated circuits. The MEMS device in the optical module is fabricated with standard CMOS process technology in Cypress's Fab 2 facility in Round Rock, Texas. The complex algorithms required to program the DGE on the fly are the product of SLM's expert staff of PhDs. The features and technical requirements of the DGE were defined in conjunction with Cypress's key networking and telecom customers, many of whom designate Cypress as a preferred supplier due to its systems and architectural expertise.



At the heart of the DGE is a mirror-like grating. The DGE continuously and precisely equalizes the multiple laser signals on a fiber in the dense wave division multiplexing (DWDM) transmission systems used by telecom companies to amplify transmissions and to pack more voice, data, and multimedia on a fiber, in lieu of the costly alternative of installing more fiber.

Though silicon-based, the SLM 2200 is a complex electronics subsystem that leverages Cypress's technical and product expertise, as well as its cost-effective, high-volume manufacturing capabilities. The subsystem also marks a step up the value-chain for Cypress, underscoring the company's design partnerships with its strategic customers and establishing it as a provider of integrated, pure-optical and optoelectronic solutions. Industry and financial analysts believe that SLM's MEMS technology can play a role in optical solutions of the future, including next-generation switching systems for all-optical networks.

## CORPORATE PROFILE

Cypress Semiconductor Corporation, now in its second decade, provides a broad range of high-performance integrated-circuit solutions to leading networking, telecommunications, and computer companies worldwide. With a focus on emerging communications applications, Cypress combines its core competencies and IP in programmable logic, high-speed physical-layer communications links, interface solutions, communications memory, and timing technology to produce ICs optimized for high-speed systems that feed bandwidth-hungry Internet applications and other communications markets. Cypress aims to become the preferred silicon supplier for Internet switching systems and for every Internet data stream to pass through at least one Cypress IC.

Cypress focuses on four core communications market segments: wide area networks (WAN), storage area networks (SAN), wireless terminals (WIT) and wireless infrastructure (WIN). More than two-thirds of Cypress's sales come from these markets and from dynamic companies such as Alcatel, Cisco, Ericsson, Lucent, Motorola, Nortel Networks, and 3Com.

Cypress markets its products through direct sales offices in North America, Europe, and Asia and a worldwide network of distributors and sales representatives. In 2001 exports accounted for 50% of total revenues.

Cypress manufactures its products at wafer manufacturing plants in California, Minnesota, and Texas. The Company operates an advanced test-and-assembly facility in the Philippines.

Cypress was founded in 1982 and is listed on the New York Stock Exchange under the symbol CY. Corporate headquarters are located in San Jose, California. Company information can be accessed on the worldwide web at [www.cypress.com](http://www.cypress.com).

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## FINANCIAL HIGHLIGHTS

(In thousands, except per-share data)

	2001	2000	1999
For the year:			
Revenues	\$ 819,192	\$ 1,287,787	\$ 745,042
Operating income (loss)	(459,618)	328,839	51,607
Net income (loss) before extraordinary gain	(411,757)	277,308	88,130
Net income (loss)	(407,412)	277,308	88,130
Basic net income (loss) per share:			
Before extraordinary gain	\$ (3.32)	\$ 2.29	\$ 0.81
Extraordinary gain (net of tax)	0.04	—	—
Net income (loss)	\$ (3.28)	\$ 2.29	\$ 0.81
Diluted net income (loss) per share:			
Before extraordinary gain	\$ (3.32)	\$ 2.29	\$ 0.76
Extraordinary gain (net of tax)	0.04	—	—
Net income (loss)	\$ (3.28)	\$ 2.29	\$ 0.76
Weighted average common and common equivalent shares outstanding			
Basic	124,135	121,126	108,156
Diluted	124,135	144,228	115,527
At year-end:			
Total assets	\$ 1,886,436	\$ 2,361,754	\$ 1,146,958
Cash, cash equivalents and short-term investments	205,422	884,601	280,947
Stockholders' equity	868,428	1,327,668	718,620
Stockholders' equity per share	\$ 7.00	\$ 10.96	\$ 6.64

## TO OUR SHAREHOLDERS

In the last paragraph of Cypress's 2000 Annual Report, I wrote, "We believe that 2001 will be a difficult year for the semiconductor industry. We also believe Cypress will traverse the year stably and profitably, despite industry problems."

We were not successful in achieving that goal. When we made that projection, Cypress had just reported record quarterly revenues of \$370 million. We knew that 2001 first quarter revenue was going to be lower, but we did not project that the dot-com recession of 2001 would be severe enough to reduce our quarterly revenue 51% from a peak of \$370 million in the fourth quarter of 2000 to a low of \$180 million in the third quarter of 2001.

In the third quarter of 2001, we restructured and wrote off \$79.6 million of excess inventory. That inventory write-off reduced our pro forma 2001 net earnings from a profit of \$2.2 million to a loss of \$77.4 million. Nonetheless, we maintained a solid cash position—even while making six strategic acquisitions.

## INVESTOR DISCLOSURE

We are making a special effort in this report to ensure that our disclosures are absolutely clear to our investors.

In 1994 I wrote a memo to all Cypress employees entitled "Looking Good Versus Doing What's Right for Cypress." This is an excerpt from that memo:

### Your Mom, The Investor

"There is also another important aspect to my communication to shareholders that has to do with human values and trust. I do not believe in giving the minimum legal information to investors. I believe in giving investors the information they need to manage their money.

"Think about *your mom the investor*. Suppose that she had just called you up and told you she was about to invest her *entire retirement fund* in Cypress stock, would you give her legally minimal information, or would you tell her exactly what was going on? Beyond that, if she did not understand what you had told her, would you then explain carefully a second or third time to make sure that she understood all the facts? That degree of concern is the difference between "minimum legal communication" and "positive communication"—a term I define as the communication in which the person sending the message *takes responsibility* to make sure the person receiving the message understands it completely.

*"Positive communication is my standard of behavior for every Cypress employee."*

Consequently, in our 10-K report for 2001, investors will find a transparently described version of every issue we felt would not be obvious, based on standard financial reporting methods. This extra reporting effort unearthed no surprises. However, there are certain Cypress transactions whose details are not obvious from reading standard financial reports. One example is the method by which Cypress finances its buildings. In the most straightforward transaction, a company would buy or build a building which would show up in the financial reports as follows (for a hypothetical \$10 million building):

- Cash would decrease by \$10 million.
- Pre-tax profit would decrease by \$100,000 per quarter due to lost interest income (assuming the cash was returning 4% interest).
- The building asset would show up on the books as a \$10 million asset, typically depreciated over a 20-year period.
- The depreciation would further reduce pre-tax earnings by \$125,000 per quarter.
- Net earnings would be reduced by \$135,000 per quarter, the after-tax effect of the depreciation and lost interest income.

Cypress has a much more effective way of "renting" its buildings. We arrange for banks to buy the buildings we want. They then charge us interest on the \$10 million loan. In return for the low interest we pay on that loan, we are required to keep "restricted cash" in an account so that the bank can access it if we default on our obligations. Typically, the interest we receive on our money in the restricted account is equal to (or sometimes even greater than) the interest we pay the bank that owns the building. The reason that a bank is willing to enter into a contract with us that gives us essentially "free rent" is that they are guaranteed by our restricted funds that they will never be left with an empty building. We are required to either renew our lease periodically, or to buy the building. Under this scenario, given that most of our buildings are on prime real estate in the center of Silicon Valley, we would probably make a capital gain in the future, as the purchase price is set at the beginning of lease.

The transaction just described—a transaction known as a synthetic lease—is not unique to Cypress; it is typically used throughout Silicon Valley. But, the only requirement for reporting this transaction is to show "restricted cash" on the balance sheet as part of the discussion on "leasing" the building. Given the philosophy outlined in my memo about "Your Mom, The Investor," we aim to take our disclosure one step further in this report.



Consequently, in our 2001 10-K, we have taken care, in the Management Discussion and Analysis section and in the Financial Statement Notes, to carefully explain every transaction at Cypress that may not be easily understandable.

## 2005 MISSION STATEMENT

Cypress updates its Mission Statement about every five years, as we achieve our prior mission statement. Our “mission statement” is actually a set of four different statements, created using a methodology installed at Cypress by Stanford Professors Jim Collins (now at the University of Colorado) and Jerry Porras, the authors of “Built to Last,” the best-selling business book which outlines the operating principles of 13 of the world’s most innovative and enduring companies. Using the Collins-Porras system, Cypress created a “mission statement” with four parts:

- A Statement of Core Values, which declares the basic beliefs shared by Cypress employees. Three examples from our 28 Core Value statements: “We are smart, tough and work hard.” “We tell the truth and don’t make excuses.” “We deplore politicians (referring to the corporate type).”
- The Statement of Purpose, which synthesizes the Core Values and states succinctly why employees choose to stay at Cypress, rather than going elsewhere.
- The Mission Statement, which, given the information contained in the other statements, is a simple numerical objective.
- The Vivid Description, which states the inspiring vision describing the company after it has achieved its Mission Statement.

These combined statements at Cypress are carefully constructed, posted on a bulletin board in every Cypress building and too lengthy to include here. However, let me share our Statement of Purpose and an excerpt from our Mission Statement here.

### Statement of Purpose (Why We Are Here)

“Cypress is smart, hard-working people who thrive on competition, demand victory, and will not tolerate defeat. We make the world’s best semiconductors for communications.”

### Mission Statement (What We Will Do)

“We will grow our business to \$1 billion per quarter with \$250 million in pre-tax profits by 2005.”

Our first mission statement in 1993 set a goal to grow our start-up company to \$1 billion in annual revenue.

We achieved that objective in 2000. In that year, we decided to continue with a simple sales-oriented numerical mission statement, because it is an easily understood objective. Cypress’s new mission is much more ambitious: to grow revenue profitably to achieve a billion-dollar *quarter* by 2005. The front cover of this report shows in red the revenue projection curve that is required to meet our Mission Statement. The dot-com collapse of 2001 caused us to fall below that projection in the first year after it was made. Nonetheless, our Mission Statement remains unchanged. We will simply have to do more to get there.

The light blue bars on the front-cover graph show our current estimate of how Cypress’s core businesses will grow over the next four years. We believe, given the communications market setback of 2001, that our core businesses will carry us to a revenue of approximately \$1.9 billion in 2005. That revenue figure is \$1.8 billion short of the \$3.7 billion of revenue needed in 2005 to achieve a billion-dollar fourth quarter. In this letter, I will outline our current strategy in the communications market to reach \$1.9 billion in revenue in 2005, and then discuss what we are doing to close the gap between that revenue and the revenue target set in our Mission Statement.

## COMMUNICATIONS STRATEGY

In our last annual report, I outlined how Cypress had reorganized from an organization driven by product line profit-and-loss (P&L) centers into an organization driven by four market segment divisions, designed to serve certain end markets, for example, the Wide Area Network. The market segment divisions are chartered to offer a market-oriented offering of products designed by our five product lines, which, in turn, contain 19 business unit P&L centers. Cypress’s four market segment divisions are as follows:

- Wide Area Networks (WAN). Serving the wired communications infrastructure. Major customers: Cisco, Lucent, Motorola, Nortel.
- Storage Area Networks (SAN). Serving the Storage Area Network and Network Attached Storage markets. Major customers: Compaq, EMC, IBM.
- Wireless Infrastructure (WIN). Serving the market for the infrastructure of cellular communications. Major customers: Ericsson, Intel, Motorola, NEC.
- Wireless Terminals (WIT). Serving the market for cellular telephony and personal digital assistants. Major customers: Alcatel, Intel, Motorola.

The relationship of our segment market divisions to Cypress’s product lines and business units is outlined in *Figure 1*. Our \$1.9 billion 2005 core-business revenue projection is based on the growth of this organization.

## Cypress Organization

MARKET SEGMENT DIVISIONS	PRODUCT LINE PROFIT AND LOSS CENTERS				
	MPD MEMORY PROD	DCD DATACOM PROD	PCD PERSONAL COMM	TTD TIMING PROD	SLM SILICON LIGHT
WIT WIN	MoBL™	BLUETOOTH®			
WAN SAN	SYNC®	MULTI-PORT FIFO PHY® CPLD FRAMER® NET SRCH ENG®	BUSINESS UNITS	RoboClock® ZERO DELAY EMI CLOCK® Com-Link®	OPTICS® O/E CONV®
OTHER	ASYNCR	USB® NEURON®		PROG CLOCK PC CLOCK®	
	GALVANTECH	HIBAND ARCUS LARA NET SAHASRA SILICON PKTS	RADIOCOM ALATION ISD ANCHOR CHIPS SCANLOGIC	IC WORKS IMI	ACQUIRED COMPANIES

e/c=Business Unit Enhanced/Created by Acquisition

**Figure 1.** Cypress's basic strategy is executed by its original four divisions (Memory Products, Data Communications, Personal Communications, and Timing Technology), along with the new Silicon Light Machines subsidiary. Cypress focuses on its key markets through our four market segment divisions: Wide Area Networks (WAN), Storage Area Networks (SAN), Wireless Infrastructure (WIN), and Wireless Terminals (WIT). The business units which constitute each product line are also listed. Those business units are also organized with the market segment division that they support. In addition to Silicon Light Machines, Cypress has acquired 13 other companies in the last three years. They are listed below the product line into which they were integrated.

## STRATEGIC ACQUISITIONS

Over the last three years, we have focused on building our communications businesses both internally, by redirecting R&D efforts, and externally, through acquisitions. The acquired companies are listed in *Figure 1* below the product line into which they were integrated. The business units highlighted with an "e" or "c" are those that have either been enhanced or created by an acquisition.

Cypress has acquired 14 companies over the last three years, as shown in *Figure 2*. The companies tend to be small (averaging 25 engineers), in the development

phase of an exciting new technology, and strategically aligned to Cypress's end markets. The figure also shows excellent 84% retention of technical people from our acquisitions, a turnover rate lower than that for the Cypress population at large. One benefit of the current downturn is that with a strong cash position, we were able to acquire these companies at a price below Cypress's current price-to-sales (P/S) ratio as shown in *Figure 3*. In aggregate, we paid \$988 million for the 14 companies, a figure which is 3.29 times the revenue we expect them to bring to Cypress in 2002. This price is below Cypress's current P/S ratio of approximately 3.70.

Our acquisitions were dilutive to earnings in 2001, because our typical acquired company was in its new product phase. We expect the company to achieve profitability in 2002, as those new products ramp. The compelling new products and technologies of our acquisitions are outlined below.

## Optoelectronics

Silicon Light Machines (SLM) invented a proprietary, silicon-based, solid-state projection system that it licensed to Sony for \$75 million, just before being acquired by Cypress. We acquired SLM to refocus the efforts of its excellent technical team on extending Cypress's capability into the optical domain. SLM succeeded in two efforts in 2001, both of which should bring product revenue to Cypress in 2002. Their optical transceiver module prototype, shown in *Figure 4*, is the realization of a new-product concept presented in last year's Annual Report. The device receives data from an optical fiber on one port and converts that data to electronic signals on the other port. In other words, we have developed the capability for a Cypress product to turn electrical signals into optical signals and vice versa.

### Good Acquisition Retention

COMPANY	TECHNOLOGY	TOTAL	TECHNICAL
SILICON LIGHT	OPTOELECTRONICS	34/44	26/33
ALATION	DSP/RF	16/19	12/14
RADIOCOM	RF	5/5	5/5
ANCHOR CHIPS	USB	24/27	17/17
IC WORKS	TIMING CIRCUITS	83/128	22/33
GALVANTECH	SYNC SRAM	27/50	12/18
IMI	TIMING CIRCUITS	65/80	29/30
HIBAND	10-Gbps PHY	13/15	12/14
LARA NETWORKS	NSE/COPROCESSOR	76/77	40/40
SCANLOGIC	EMBEDDED HOST	15/17	12/12
ISD	USB 2.0 MASS STORAGE	72/73	52/52
ARCUS	OC-48 FRAMER	31/68	26/55
SILICON PACKETS	OC-48/OC-192 FRAMER	27/28	24/24
SAHASRA	ALGORITHMIC NSE	5/5	5/5
TOTAL		493/636	294/352
		78%	84%

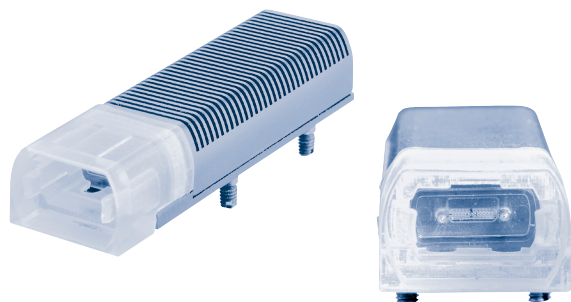
**Figure 2.** Cypress has retained 84% of the technical employees from its 14 acquisitions.

### Good Acquisition Price

COMPANY	TECHNOLOGY	\$ PAID	2002 SALES
SILICON LIGHT	OPTOELECTRONICS	\$164M	\$25M
ALATION	DSP/RF	24	2
RADIOCOM	RF	10	2
ANCHOR CHIPS	USB	15	46
IC WORKS	TIMING CIRCUITS	128	70
GALVANTECH	SYNC SRAM	142	55
IMI	TIMING CIRCUITS	156	42
HIBAND	10-Gbps PHY	34	1.5
LARA NETWORKS	NSE/COPROCESSOR	200	10.7
SCANLOGIC	EMBEDDED HOST	30	16
ISD	USB 2.0 MASS STORAGE	43	28
ARCUS	OC-48 FRAMER	18	1.4
SILICON PACKETS	OC-48/OC-192 FRAMER	27	0.4
SAHASRA	ALGORITHMIC NSE	3	0
TOTAL PRICE		\$988	\$300M

**Figure 3.** Cypress paid \$988 million for its 14 acquisitions. The acquisitions are expected to produce \$300 million in revenue in 2002. The price paid for the acquisitions is therefore 3.29 times their expected revenue for 2002, a figure which is lower than Cypress's current 3.7 multiple on sales.

## Optoelectronic (O/E) Module



**Figure 4.** Cypress and Silicon Light Machines codeveloped the technologies required to offer a family of optical modules. These modules will be critical components in high-bandwidth interconnects in next-generation switches and routers. The technologies developed to produce the module—including mechanical, optical, opto-mechanical and electronic—will enable high-speed optical interconnects.

The second major product developed by SLM in 2001 is their Dynamic Gain Equalizer (DGE), illustrated on the front inside cover of this report. Currently, voice and data move across the U.S. as modulated (on/off) light streams carried on optical fibers. By varying the wavelength (color) of the light streams, as many as 80 of them can be carried independently without interference on the same fiber, vastly multiplying its data carrying capability. This major technology advance, called Dense Wavelength Division Multiplexing (DWDM), poses a new problem, which SLM has solved. Because new light streams are added to or dropped from the fiber at various points, and because of the non-uniform amplification of the light streams as they traverse a long haul fiber system, the intensity of the multiple beams in a fiber can vary so much that the weakest beams can actually be lost. Our dynamic gain equalizer does just what its name implies, it automatically and continuously adjusts the gain of the amplifiers in a fiber transport system to make sure that each of the light streams in the fiber has the same intensity—to a tolerance that is currently unachievable by SLM's competitors.

## Data Communications

The majority of Cypress's acquisitions have been focused on strengthening our data communications capabilities. An excellent proxy for defining the skills required to compete in the data communications market is shown in *Figure 5*. It is a linecard, used multiple times in every data router. A line-card in a router functions to take in a data stream through its port terminal, a physical layer device that connects the router to the outside world, for example, to the telephone system or another router. The data stream is then run through the linecard packet processor, which, among other functions, determines the next address for each Internet

## Line Card Solution



**Figure 5.** A typical linecard in a router contains three sections: a port, which receives signals from the outside; the packet processing section, which decomposes the signal into IP packets; and a backplane, which sends those packets to the core of the machine to be routed to the appropriate next destination. When the packets come out of the router, they make the reverse trip from the backplane out through a port to the next destination. The Cypress chips applicable to line cards are shown. The acquired companies that improved our strategic position on the line card products are listed in the appropriate spot.

Protocol (IP) packet. The packets then flow through the backplane of the router into a switching matrix, where they are forwarded to other linecards and launched to their next destination. *Figure 5* shows the broad variety of products that Cypress makes for linecards. It also shows where our acquired companies have added expertise.

In 1999, Cypress acquired Arcus, a Bangalore-based communications company now part of our 100-person Bangalore design center. We have been working with Arcus employees for two years to develop a “framer” chip, the second chip in on the linecard from the port-side physical layer (PHY). A framer is a big logic chip, which takes in the bit stream from the port and unloads the IP packets contained in it so that they can be processed and routed. The framer is considered to be an essential part of the architecture of any switching system. Our first framer, the 4.5-million-transistor Packet Over SONET Integrated Circuit (POSIC™) is now sampling to customers. POSIC operates at a standard data rate of 2.5 gigabits per second (Gbps), a data rate known as OC-48 in the Synchronous Optical Network, or SONET (telephone), system. The framer chips of our competitors typically provide a rudimentary multiplexing capability, for example, multiplexing sixteen OC-3 (155 Megabits per second) bit streams into a single OC-48 bit stream. POSIC is unique in that it not only allows the multiplexing of 16 tributary bit streams into one OC-48 bit stream, but it also frees the user from the restriction of forcing the 16 tributaries to be fixed in size. This dynamic allocation of bandwidth is very difficult to achieve and unique in the industry. It enables equipment manufacturers to dynamically allocate different amounts of



data capacity to different channels for the first time. Obviously, the ability to electronically allocate capacity is a big advantage for our customers, compared to their current method of rewiring. The POSIC framer from our Arcus acquisition will launch Cypress squarely into that key market in 2002.

The next higher speed in the SONET hierarchy is OC-192 at 10 Gbps. We acquired Silicon Packets, a San Jose-based start-up company, to accelerate our entry into the OC-192 framer market. We expect to be sampling their product before midyear.

The packet processing section of the linecard shown in *Figure 5* performs the essential task of reading the source and destination addresses of an IP packet to forward that packet to the next appropriate station in the system. Prior to last year, a specialized computer, called a network processor, did that task with software. As line speeds approach the 10 Gbps rate of OC-192, it is extremely difficult for network processors to move the packets forward at the high speeds required, using only software solutions. The hardware solution to the “packet forwarding” problem is called a Network Search Engine (NSE). Lara Networks, a Silicon Valley company acquired by Cypress in 2001, is the top NSE firm in the world. An NSE is a combined logic and memory chip that can process packets—by reading each of them and giving them the appropriate forwarding address—at a rate of 10 Gbps. The newest routers from Cisco Systems use NSE technology, which is generally regarded to be the next step for packet forwarding at speeds of OC-192 and above.

The next challenge for Network Search Engines is to make them not only fast but very big in capacity. That new challenge will require a new architecture. For that reason, Cypress acquired Sahasra, a five-man brain trust out of Stanford with a new way to make NSEs that we see as a breakthrough. We plan to spend 2002 capturing Sahasra’s architecture in silicon and to announce our product in 2003.

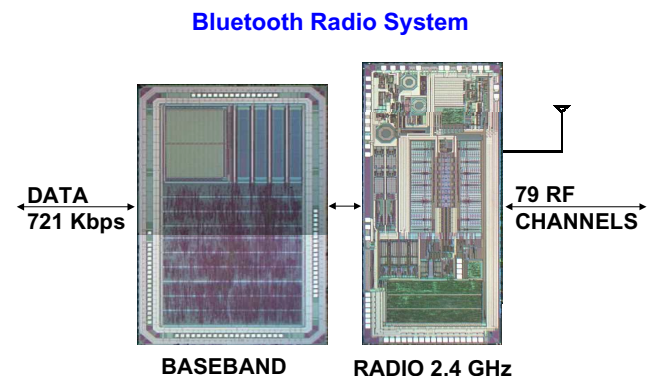
## Wireless Communications Products

Bluetooth™ is an industry trade name for a low-cost wireless communication system for use in “personal area networks” (100-foot range). Bluetooth systems are able to replace the cables in consumer systems. For example, Bluetooth enables products such as personal computers with completely wireless peripherals, cell phones with no wire between the earpiece and the body of the phone, video games with no wires, etc. As usual, more user friendliness implies a bigger engineering challenge. The Bluetooth radio is a complicated device, which transmits by hopping back and forth among 79 different channels in the 2.4 GHz radio frequency (RF) band. (“Frequency hopping” technology has its origin in secure military communi-

cations.) The computer-controlled frequency hopping sequence prevents one Bluetooth radio from interfering with another, and allows some channels to be blocked without losing the entire transmission. The Bluetooth radio signal is turned into usable information by a second “baseband” chip that uses digital signal processing (DSP) techniques to recover the data from the complicated, noisy radio signal. The big challenge is that this sophisticated, two-chip RF system has to sell for the price of a cable, \$5.00 or less, in order to be accepted by the market!

Bluetooth is complementary to our Universal Serial Bus (USB) technology, in which Cypress holds the No. 1 position with well over \$100 million in projected 2002 sales. We decided to make acquisitions to achieve the vision of wireless USB. The first acquisition to provide us with this new capability was Alation, a small Silicon Valley company, specializing in DSP technology. Alation’s baseband chip is already being manufactured in one of our very-low-cost SRAM technologies. The second, key acquisition was that of Radiocom, a Portland-based RF company, now housed at our Oregon Design Center. We are currently debugging that chip, which is manufactured on our 0.25-micron BiCMOS technology, a process with both high performance (35 GHz transistors) and very low cost. We expect the most cost-effective Bluetooth solution in the marketplace by mid-year to be the Cypress product shown in *Figure 6*.

We believe that our current communications strategy, including the contributions of our acquisitions, will carry us to a projected revenue level of \$1.9 billion in 2005. But to achieve our billion-dollar quarter, we must also grow our revenue in areas other than communications, which is growing at the fastest rate we can manage.



**Figure 6.** The baseband chip of a Bluetooth radio system receives data at rates up to 721,000 bits per second. That data is encoded and transferred to a radio chip which sends it out in parallel on 79 different RF channels in the 2.4 GHz band, which is not FCC regulated. The radio hops from channel to channel at the rate of 1,600 times per second. This “frequency hopping” technique allows for simultaneous transmission without interference from other Bluetooth sources, as well as the loss of a single channel without the loss of the entire transmission.



## THE GAP

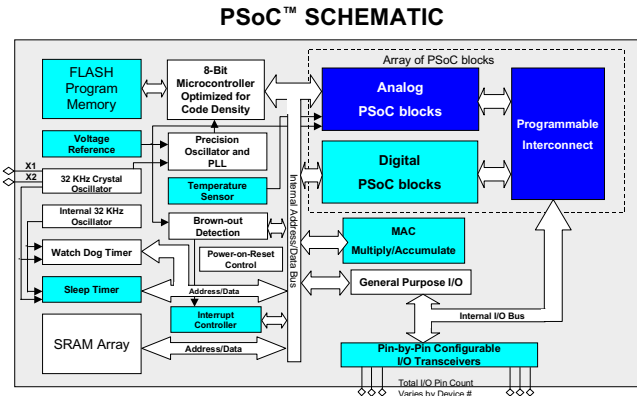
Since our management bandwidth is saturated by the execution of our communications strategy, any incremental revenue growth must come from initiatives with two attributes: (1) from a market segment other than communications, and (2) from a business with modest demands on management bandwidth. The second requirement mandates that we close the gap through investment-level interactions with independent corporations that we later acquire, but not through organizations that we are required to manage daily.

Our first revenue gap initiative, which meets both of the requirements above, was to form Cypress MicroSystems (CMS) in 1999. CMS was launched to attack a new market for Cypress, the \$7 billion, 8-bit microcontroller market. CMS is an independent corporation with three Cypress directors. I am the chairman of CMS, but Cypress does not manage CMS on a daily basis.

CMS's strategy to enter the huge, but mature, microcontroller market is to offer several new technical innovations. The architecture of a microcontroller is nothing more than a small computer that contains several so-called peripheral devices to interface the computer with the physical world. One example of a peripheral device is an analog-to-digital converter, a circuit that measures a voltage (perhaps to test for a dying battery) and converts it into a digital number the computer can use. A computer connected to an analog-to-digital converter becomes capable of interacting with the physical world, for example, by comparing the measured voltage to a reference voltage stored in its memory, enabling it to make a decision on whether or not the battery is dying. Later, the computer might activate a second peripheral device, perhaps to switch on a warning light. Microcontroller applications like this one are ubiquitous. For example, modern automobiles each have dozens of microcontrollers in them.

The catalogs of most microcontroller companies contain thousands of devices that feature a basic computer offered with numerous product configurations of varying memory sizes, peripheral device types, pin counts, etc. CMS's first product, the Programmable System-on-Chip™ (PSoC™) device, is a breakthrough in the inventory-laden microcontroller market. Instead of having fixed-function peripherals that mandate dozens of chip designs, the PSoC chip has a series of programmable analog blocks that can be configured into very different analog functions. In addition to programmable analog blocks, the PSoC chip also features programmable digital blocks to create custom logic. The PSoC microcontroller is so configurable that it is

## Programmable System-on-Chip™ (PSoC™)



**Figure 7.** Cypress MicroSystems was founded as an independent company to begin filling the gap between Cypress's base business revenue plan and the revenue called for in our Mission Statement. Their first product, the PSoC™ microcontroller, not only garnered a cover of *Electronic Design*, but won *EDN's* award for being the most innovative microcontroller product of 2001. This single device has both programmable digital and programmable analog circuitry, allowing it to be configured to replace 40% of all 8-bit microcontrollers offered worldwide (thousands of different products). Once programmed into a custom configuration, the microcontroller can then be further programmed as a computer capable of achieving four million instructions per second.

capable of producing literally millions of different products—a complexity problem for a typical user. CMS has solved this problem with unique software that makes the PSoC chip very user friendly.

CMS's proprietary software allows a user to specify a unique configuration for a PSoC chip in a Windows®-like environment, creates custom PSoC peripherals and hooks them up with programmable interconnects to create a fully custom 8-bit microcontroller. The software also provides the capability to program a blank PSoC chip into a custom engineering sample in minutes, using a pod attached to the printer port of a personal computer.

The PSoC chip is a breakthrough product. That's why it won not only a cover story in *Electronic Design*, but also *EDN's* best microcontroller product award in the 8- and 16-bit category for 2001.

Cypress has a contractual right to buy Cypress MicroSystems when CMS achieves certain revenue and profit targets. CMS is a new business, just entering its revenue phase, and it is chartered to fill in part of our Mission Statement revenue gap.

Cypress anticipates that it will engage as a close investor in other new businesses in 2002 to create additional opportunities like the one afforded by CMS.

## CONCLUSION

The dot-com implosion set back Cypress's revenue growth plans in 2001. Nonetheless, our sound financial position and clear strategic direction allowed us to

take advantage of the chaotic marketplace by making strategic acquisitions that would have been impossible in better economic times. In 2001, Cypress's technical DNA was forever improved.

It now appears that the third quarter of 2001 was the bottom of the current recession.\* The market remains very sluggish, but Cypress is loaded with great new products to drive growth. I have focused on the new products attributable to our strategic acquisitions in this report, but the majority of our 2002 new-product dollars will come from internally developed new products.

One figure of merit for new product health is the age of the products contributing to revenue. Having 50% of revenue attributable to products that are three years old or less is considered exemplary. *Figure 8* shows that Cypress surpasses that standard with 50% of its revenue coming from products two years old or less.

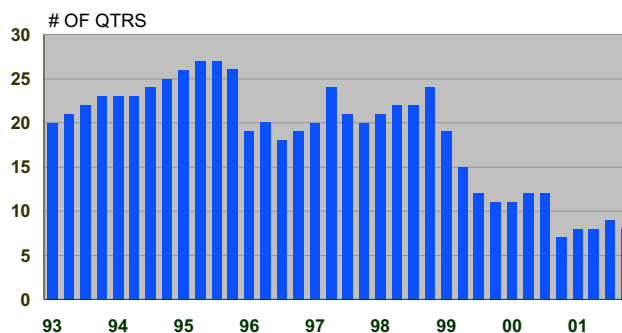
We expect to grow steadily, if modestly, in 2002—and to return to profitability, based on the success of our broad portfolio of new products.



T.J. Rodgers  
President and CEO

\*Speaking honestly, I wrote an equivalent recovery statement regarding the end of the 1996 semiconductor recession. Then, the Asian financial crisis triggered a second semiconductor recession in 1998. Investors should not rely on my macroeconomic views.

**Age of Cypress Revenue**  
**50% Percent of Revenue**



**Figure 8.** Since 1998, Cypress has focused heavily on new product development. Currently, products that are only 2 years old account for half of Cypress's revenue.

## Selected Consolidated Financial Data

(In thousands, except per-share amounts)

Year Ended<sup>(1, 2)</sup>

	2001	2000	1999	1998	1997
<b>Operating Results:</b>					
Revenues	\$ 819,192	\$ 1,287,787	\$ 745,042	\$ 588,915	\$ 632,969
Restructuring, acquisition and other non-recurring costs, net	293,366	55,729	34,091	60,737	13,551
Operating income (loss)	(459,618)	328,839	51,607	(115,559)	4,324
Income (loss) before income taxes and extraordinary gain	(444,437)	370,170	95,169	(112,702)	9,305
Net income (loss) before extraordinary gain	(411,757)	277,308	88,130	(101,594)	3,196
Extraordinary gain (net of tax of \$2,896)	4,345	—	—	—	—
Net income (loss)	\$ (407,412)	\$ 277,308	\$ 88,130	\$ (101,594)	\$ 3,196
<b>Basic net income (loss) per share:</b>					
Before extraordinary gain	\$ (3.32)	\$ 2.29	\$ 0.81	\$ (0.97)	\$ 0.03
Extraordinary gain	0.04	—	—	—	—
Net income (loss)	\$ (3.28)	\$ 2.29	\$ 0.81	\$ (0.97)	\$ 0.03
<b>Diluted net income (loss) per share:</b>					
Before extraordinary gain	\$ (3.32)	\$ 2.03	\$ 0.76	\$ (0.97)	\$ 0.03
Extraordinary gain	0.04	—	—	—	—
Net income (loss)	\$ (3.28)	\$ 2.03	\$ 0.76	\$ (0.97)	\$ 0.03
<b>Weighted average common and common equivalent shares outstanding:</b>					
Basic	124,135	121,126	108,156	105,238	102,920
Diluted	124,135	144,228	115,527	105,238	110,820
<b>Balance sheet data:</b>					
Cash, cash equivalents and short-term investments	\$ 205,422	\$ 884,601	\$ 280,947	\$ 174,513	\$ 213,939
Working capital	372,333	983,359	360,639	250,889	319,836
Total assets	1,886,436	2,361,754	1,146,958	850,645	1,000,597
Long-term debt and capital lease obligations (excluding current portion)	525,673	631,055	170,884	170,540	188,467
Stockholders' equity	\$ 868,428	\$ 1,327,668	\$ 718,620	\$ 517,825	\$ 658,643

(1) We operate on a 52- or 53-week fiscal year. Fiscal years 2001, 2000 and 1999 were 52-week fiscal years ending on the Sunday closest to December 31. 1998 was a 53-week fiscal year ending on the Sunday closest to December 31. Fiscal year 1997 was a 52-week fiscal year ending on the Monday closest to December 31.

(2) The preceding table presents financial information including the fourteen acquisitions completed in fiscal 2001, 2000 and 1999. See Notes 3 and 4 of the Consolidated Financial Statements included in this report for discussions of the acquisitions, which may affect the comparability of the data.

## Management's Discussion and Analysis of Financial Condition and Results of Operations

This report may contain forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, that involve risks and uncertainties that could cause our results to differ materially from those expressed or implied in the forward-looking statements. These forward-looking statements relate to future events or our future financial performance and may include statements about our prospects as well as the prospects of the semiconductor industry more generally, including without limitation, statements about the general economy and its impact to the market segments we serve, changing environment and the cycles of the semiconductor industry, competitive pricing and the rate at which new products are introduced, successful integration and achieving the objectives of the acquired businesses, cost goals emanating from manufacturing efficiencies, adequacy of cash and working capital and other liquidity risks. Actual results could differ materially from those described in the forward-looking statements as a result of various factors including, but not limited to, the factors identified in Risk Factors.

### Overview

	(In thousands, except per-share amounts)			Year Ended	
	December 30, 2001	December 31, 2000	January 2, 2000		
Revenue	\$ 819,192	\$ 1,287,787	\$ 745,042		
Net income (loss)	(407,412)	277,308	88,130		
Diluted earnings per share	\$ (3.28)	\$ 2.03	\$ 0.76		

We recorded revenues of \$819.2 million for fiscal year 2001, a decrease of 36.0% from fiscal 2000 record revenues of \$1,287.8 million. Fiscal 2001 was a challenging year characterized by a fundamental slowdown in end customer demand in all the markets we serve. The first half of fiscal 2001 was characterized by inventory reduction efforts by customers that led to order cancellations and a large drop in volume. During the latter half of 2001, order cancellations returned to historical average levels with a book to bill ratio of close to 1.0. However order levels remained below 2000 levels and the levels that we were forecasting earlier in 2001. In addition, we saw some stabilization of customer inventories along with a continued shift by customers to the practice of placing orders for shipment in the same quarter. This practice of “turns” orders reduces our visibility into future sales. Throughout the year, there was continued pressure on gross margins from further declines in average selling prices (“ASP”), underutilization of factories and large provision for inventory reserves.

On December 27, 2001, Cypress completed its acquisition of Silicon Packets, Inc. (“Silicon Packets”), a company that specializes in designing 10 Gigabit-per-second framers for OC-192/STM-64 SONET/SDH and 10-Gigabit Ethernet (10GbE) transport solutions. Silicon Packets is part of the Non-Memory business segment and the WAN/SAN market segment. The acquisition is expected to accelerate Cypress’s current schedule to develop 10 Gigabit-per-second solutions for MAN/WAN infrastructure equipment such as switches and routers. Cypress acquired Silicon Packets for total consideration of \$27.3 million, including 0.7 million shares of Cypress common stock valued at \$14.2 million, \$7.1 million in cash, options to purchase 0.2 million shares of Cypress common stock valued at \$3.2 million and direct acquisition costs of \$2.8 million for underwriting, legal, valuation, accounting and regulatory fees. We may be required to make additional payments of up to \$5.0 million based on the achievement of defined performance milestones. The acquisition was accounted for using the purchase method of accounting in accordance with SFAS No. 141 and, accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress’s consolidated balance sheet as of December 27, 2001, the effective date of the purchase. Other than the charge for in-process research and development, Silicon Packet’s results of operations from the date of purchase to the end of the fiscal year were not significant because the acquisition was completed during the last week of the fiscal year and are therefore not included in Cypress’s consolidated results of operations for the year ended December 30, 2001.

On September 14, 2001, Cypress completed its acquisition of In-System Design, Inc. (“ISD”), a system-on-chip design company specializing in personal communications solutions. Cypress acquired ISD for total consideration of \$43.0 million, including \$36.7 million in cash, options to purchase 0.3 million shares of Cypress common stock valued at \$5.4 million and direct acquisition costs of \$0.9 million for legal and accounting fees. We may be required to make additional payments of up to \$27.5 million based on the achievement of defined performance milestones. The



acquisition was accounted for using the purchase method of accounting in accordance with SFAS No. 141. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of September 14, 2001, the effective date of the purchase. ISD revenues of \$8.8 million were included in Cypress's consolidated results of operations for fiscal 2001. The ISD acquisition reduced net income by \$6.8 million during the year, due primarily to charges of \$0.8 million for in-process research and development, \$2.7 million for amortization of intangibles and \$2.8 million in non-cash deferred compensation charges, as well as net operating losses of \$0.5 million.

On July 3, 2001, Cypress completed its acquisition of Lara Networks, Inc. ("Lara"), a provider of high-performance, silicon-based packet processing solutions for wide area network infrastructure equipment. Cypress acquired Lara for total consideration of \$200.1 million, including \$185.3 million in cash, options to purchase 0.4 million shares of Cypress common stock valued at \$8.1 million and direct acquisition costs of \$6.7 million for underwriting, legal, valuation, accounting and regulatory fees. We may be required to pay additional compensation based on the achievement of defined performance milestones. The acquisition was accounted for using the purchase method of accounting in accordance with SFAS No. 141. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of July 3, 2001, the effective date of the purchase. Lara revenues of \$7.5 million were included in Cypress's consolidated results of operations during fiscal 2001. The Lara acquisition reduced net income by \$18.6 million during the year, due primarily to charges of \$4.6 million for in-process research and development, \$2.1 million for amortization of intangibles and \$8.1 million in non-cash deferred compensation charges, as well as net operating losses of \$3.8 million.

On May 29, 2001, Cypress completed its acquisition of ScanLogic Corporation ("ScanLogic"), a provider of USB controllers for embedded and PC applications. Cypress acquired ScanLogic for total consideration of \$30.1 million, including \$15.6 million in cash, options to purchase 0.5 million shares of Cypress common stock valued at \$11.7 million, notes payable to shareholders of \$1.9 million and direct acquisition costs of \$0.9 million for legal and accounting fees and broker commissions. The acquisition was accounted for using the purchase method of accounting. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of May 29, 2001, the effective date of the purchase. ScanLogic revenues of \$7.4 million were included in Cypress's consolidated results of operations during fiscal 2001. The ScanLogic acquisition reduced net income by \$5.8 million during the year, due primarily to charges of \$1.5 million for in-process research and development, \$3.4 million for amortization of intangibles and goodwill and \$2.6 million in non-cash deferred compensation charges and contingent cash compensation charges, which were partially offset by net operating results of \$1.7 million.

On March 27, 2001, Cypress acquired all of the outstanding capital stock of HiBand Semiconductors, Inc. ("HiBand"). HiBand is a provider of mixed-signal integrated circuits for high-speed communications markets. Cypress acquired HiBand for total consideration of \$34.0 million, including 1.4 million shares of Cypress common stock valued at \$28.2 million, options to purchase 0.2 million shares of Cypress common stock valued at \$4.0 million, an existing \$1.3 million cash advance and direct acquisition costs of \$0.5 million for legal and accounting fees. The acquisition was accounted for using the purchase method of accounting. In-process research and development of \$6.5 million was included in the results of operations for fiscal 2001. The acquisition reduced net income by \$21.6 million during the year, due primarily to charges of \$6.5 million for in process research and development, \$3.8 million for the amortization of intangibles and goodwill and \$6.6 million in non-cash deferred compensation charges and contingent cash compensation charges, as well as net operating losses of \$4.7 million.

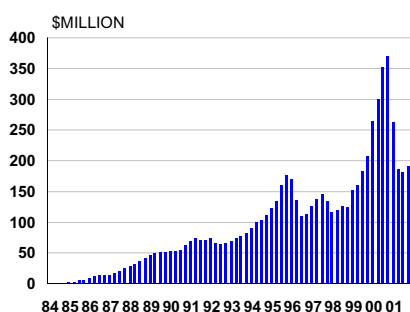
On February 23, 2001, Cypress completed its acquisition of International Microcircuits, Inc. ("IMI"), a company specializing in timing technology integrated circuits for network applications. IMI's product portfolio includes programmable clocks, electromagnetic interference suppression devices, clock distribution products and application-specific products. IMI has clock products for applications in communications, cable and DSL modems, office automation, digital cameras, DVDs and video games. Cypress acquired IMI for total consideration of \$150.3 million, including \$111.2 million in cash, options to purchase 1.3 million shares of Cypress common stock valued at \$32.8 million, notes payable to shareholders of \$3.3 million, and direct acquisition costs of \$3.0 million for investment banking, legal and accounting fees. The acquisition was accounted for using the purchase method of accounting. IMI was fully integrated into Cypress's existing timing technology business in the third quarter of fiscal 2001 and its results are no longer separately tracked. Prior to integration, IMI revenues were \$20.6 million and the IMI acquisition reduced net income

by \$42.7 million, due primarily to charges of \$4.9 million for in-process research and development, \$26.8 million for amortization of intangibles and goodwill and \$13.9 million in non-cash deferred compensation charges, which were offset by net operating results of \$2.9 million.

## Results of Operations

### Revenues

#### Revenues\*



\*Historical data does not include effect of Galvantech, Alation, and IC Works (ICW) prior to their mergers.

### Business Segment Net Revenues

(In thousands)

	2001	2000	1999
Memory products	\$ 350,908	\$ 638,111	\$ 309,002
Non-Memory products	468,284	649,676	436,040
<b>Total consolidated revenues</b>	<b>\$ 819,192</b>	<b>\$ 1,287,787</b>	<b>\$ 745,042</b>

Revenues from the sale of Memory products for fiscal 2001 decreased \$287.2 million or 45.0% versus revenues from the sale of these products for fiscal 2000. The decrease in Memory product revenues, as compared to fiscal 2000, resulted from a 52.1% decrease in unit demand for semiconductor products particularly in the wireless and networking markets. In 2001 ASPs increased as a result of a continuing increase in the average density (Mbits/unit) of static random access memories (“RAMs”) products sold. This increase was driven by new product revenues, particularly the 4- and 8-Mbit More Battery Life™ (“MoBL™”) family of parts and the 9-Mbit and 18-Mbit synchronous family of static RAMs. Adjusted for this mix change, ASPs declined by 5.0% from 1999 to 2000 and by 26% from 2000 to 2001 on a same product basis.

Revenues from the sale of Memory Products for fiscal 2000 increased \$329.1 million or 106.5% over revenues from the sale of these products for fiscal 1999. The increase in Memory Product revenues, as compared to fiscal 1999, resulted from both higher ASP and an increase in unit sales. ASP grew 47.9% from fiscal 1999 to fiscal 2000 and unit sales increased 39.6% over the same period. The increase in unit sales in fiscal 2000 can be attributed primarily to new product revenues, particularly in the 4-Mbit synchronous family, which includes the No Bus Latency™ (“NoBL™”) static RAM, the 2- and 4-Mbit MoBL and the 1-Mbit micro-power family of products. The synchronous demand was driven by the surge in the networking market, while sales for MoBL and other micro-power devices were driven by growth in the cellular phone market. High ASPs resulted from strong demand for static RAMs and the continuing increase in the average density (Mbits/unit) of static RAM products sold.

Revenues in 2001 from the sale of Non-Memory products decreased \$181.4 million or 27.9% when compared to revenues from the sale of these products for fiscal 2000. The decrease in Non-Memory product revenues, as compared to fiscal 2000, resulted primarily from a 26.7% decrease in unit sales. The decrease in unit sales resulted from decreases in unit demand in all aspects of the networking end markets, and reduced end customer demand in the personal computer market in the first half of fiscal 2001. Demand for PC-related clock chips and USB related products recovered in the second half of the year.

Revenues in 2000 from the sale of Non-Memory products increased \$213.6 million or 49.0% from 1999. The growth was predominantly unit related and can be attributed to the market acceptance of Cypress’s Physical Layer (“PHY”), data communications, clock and USB products. Key products in the portfolio include our HOTLink® optical transceivers, the Roboclock® family of clock buffers, our low-skew and low-jitter programmable clocks, our broad portfolio of specialty multi-port memories and our plug-and-play USB devices.

As is typical in the semiconductor industry, ASP of products generally declines over the lifetime of the products. To increase revenues, Cypress seeks to expand its market share in the markets it cur-

rently serves and to introduce and sell new products with higher ASP. Cypress will seek to remain competitive with respect to its pricing to prevent a further decline in sales.

## Cost of Revenues

Cost of revenue as a percent of revenues for fiscal 2001 was 67.0% compared to 44.0% for fiscal 2000. The increase in cost of revenues as a percentage of revenues was caused by increased inventory reserves, underutilization in our factories and continued declines in the ASP of memory, USB and clock devices. Cost of revenue as a percent of revenues decreased to 44.0% in fiscal 2000 from 55.0% for fiscal 1999 due to a significant increase in unit sales in 2000, resulting in a lower fixed cost per unit sold, and to the introduction of new products with higher margins.

During the third quarter of fiscal 2001, Cypress received feedback from our customers that indicated that the downturn in sales would last longer than previously anticipated. Accordingly, we increased inventory reserves during the quarter for inventory that we did not expect to sell. Cost of revenues in the third quarter of fiscal 2001 included an unusual charge of \$93.1 million for inventory reserves; during fiscal 2001, including the \$93.1 million unusual charge, total net charges for inventory reserves were \$125.4 million. Additional charges to cost of revenues to increase inventory reserves may be necessary in the future if demand continues to decline.

Cost of revenues for fiscal 2000 were 43.9% of revenues, compared to 54.9% of revenues for fiscal 1999. The decrease in cost of revenues as a percent of revenues was primarily due to a significant increase in unit sales, resulting in a lower fixed cost per unit sold and to the introduction of new products with higher margins.

Assembly and test factory utilization decreased from 75% in 2000 to 50% in 2001. Wafer fabrication factory utilization did not change significantly as we built inventory in the first half of the year anticipating a shorter downturn. When the severity and length of the downturn became clear, we restructured Cypress and took capital equipment out of service and are now holding this equipment for sale.

ASP, on a same device basis, decreased in 2001 compared to 2000 (see Business Segment Net Revenues section above). Cypress is continuing its strong emphasis on new product development and improvements in manufacturing technologies and yields, which Cypress expects will reduce manufacturing costs and help offset some of the impact of near term margin declines.

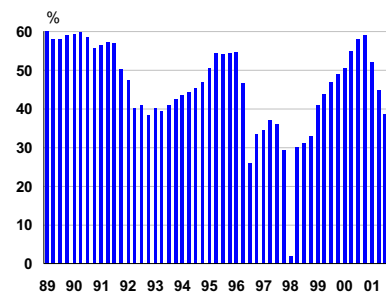
Property, plant and equipment with a net book value of \$3.1 million were also written off to cost of revenues as one-time charges as a result of a periodic physical count of property, plant and equipment completed during the third quarter of fiscal 2001.

## Research and Development

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Revenues	\$ 819,192	\$ 1,287,787	\$ 745,042
Research and development	267,522	184,471	136,858
R&D as percent of revenues	32.7%	14.3%	18.4%
One-time charges	5,500	—	—
Acquisition related compensation	25,412	3,192	254
R&D excluding acquisition related compensation and one-time charges	\$ 236,610	\$ 181,279	\$ 136,604
R&D excluding acquisition related compensation and one-time charges as percent of revenues	28.9%	14.1%	18.3%

Research and development (“R&D”) expenditures in fiscal 2001 increased from fiscal 2000 and fiscal 1999 as Cypress continued its effort to accelerate the development of new products and migrate to more advanced process technologies. In fiscal 2001, spending in Cypress’s design centers grew due to increased headcount and capital spending. R&D efforts associated with the acquisitions of Lara, ISD, ScanLogic, HiBand, IMI, Alation, RadioCom and Silicon Light Machines (“SLM”) also contributed to the increase in R&D expenditures in fiscal 2001. Cypress believes that its future success will depend on its ability to develop and introduce new products that will compete effectively on the basis of price, performance and ability to address customer needs. The major focus of process technology research is the continuous migration to smaller geometries. During 2001, we were ramping our latest 0.15-micron technology in manufacturing and simultaneously transferring our

Gross Margin as a Percentage of Revenues\*



\*Historical data does not include effect of Galvantech, Alation, and ICW prior to their mergers.

0.12-micron technology from our eight-inch R&D Fab in San Jose, California to our eight-inch manufacturing fab in Minnesota and initiating development of our 0.10-micron technology at the San Jose R&D Fab. The R&D Fab, which was converted from six-inch wafer to eight-inch wafer capability in fiscal 2000, is now compatible with our manufacturing fab in Minnesota.

During fiscal 2001, we recorded \$25.4 million in non-cash deferred stock compensation and contingent cash compensation related to acquisitions. Acquisition related compensation charged in fiscal 2001 is primarily attributed to the SLM, IMI, HiBand and Lara acquisitions.

We recorded charges of \$5.5 million in the third quarter of fiscal 2001 upon reaching an agreement to settle a patent infringement suit for \$8.0 million, of which \$5.5 million pertained to prior periods. The remainder relates to future product shipments and has been recorded as a prepaid asset that will be expensed over the next three years.

Property, plant and equipment with a net book value of \$1.5 million in R&D expense were also written off to R&D as one-time charges as a result of a periodic physical count of property, plant and equipment completed during the third quarter of fiscal 2001.

### Selling, General and Administrative

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Revenues	\$ 819,192	\$ 1,287,787	\$ 745,042
Selling, general and administrative	165,655	153,909	113,601
SG&A as percent of revenues	20.2%	12.0%	15.2%
Acquisition related compensation	11,135	2,415	358
SG&A excluding acquisition-related compensation	\$ 154,520	\$ 151,494	\$ 113,243
SG&A excluding acquisition-related compensation as a percent of revenue	18.9%	11.8%	15.2%

Selling, general and administrative ("SG&A") expenses in fiscal 2001 increased from fiscal 2000 due primarily to increased sales and marketing headcount from our acquisitions during the year, acquisition-related compensation charges and several major customer support initiatives, including expanded e-business capabilities and improvements to the web infrastructure and site. Expenses for legal and professional services related to patent infringement litigation, patent filing and tax services have also contributed to an increase in administrative costs in the periods under comparison. Lower sales commission expenses and employee bonus expenses partially offset these increases.

SG&A expenses in fiscal 2000 increased from 1999 due primarily to increased selling and marketing expenses. The increase in selling expenses was primarily due to commission expenses, which have risen in proportion to our revenue growth. In addition, the marketing area has increased expenditures due to building a worldwide infrastructure. Legal and professional costs related to patent infringement litigation, patent filing and tax services have contributed to increases in administrative costs over the two-year period.

During fiscal 2001, we recorded \$11.1 million in non-cash deferred compensation and contingent cash compensation related to acquisitions. Acquisition-related compensation charged in fiscal 2001 is primarily attributed to the SLM, IMI, and ScanLogic acquisitions.

Property, plant and equipment with a net book value of \$1.0 million were also written off to SG&A as one-time charges as a result of a periodic physical count of property, plant and equipment completed during the third quarter of fiscal 2001.

### Acquisition and Other Non-Recurring Costs

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Amortization of intangibles	\$ 71,493	\$ 21,825	\$ 9,654
In-process research and development	23,200	32,425	4,019
Other non-recurring costs	66,560	1,964	24,229
<b>Total acquisition and other non-recurring costs</b>	<b>\$ 161,253</b>	<b>\$ 56,214</b>	<b>\$ 37,902</b>



We completed six acquisitions during fiscal 2001: IMI, HiBand, ScanLogic, Lara, ISD and Silicon Packets. Acquisition costs in 2001 consisted of in-process research and development from these acquisitions and amortization of intangibles related to current and prior acquisitions. The increase in amortization from fiscal 2000 to fiscal 2001 relates primarily to the acquisitions of SLM, IMI, HiBand, ScanLogic, and Lara.

In-process research and development charges during fiscal 2001 relate to the acquisitions of IMI, HiBand, ScanLogic, Lara, ISD and Silicon Packets, which were completed during fiscal 2001. The valuation method used to value in-process technology is a form of discounted cash flow method commonly known as the “percentage of completion” approach. This approach is a widely recognized appraisal method and is commonly used to value technology assets. The value of the in-process technology is the sum of the discounted expected future cash flows attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets and the technological risk associated with completing the development of the technology. The cash flows derived from the in-process technology projects were discounted at rates ranging from 25% to 30%. Cypress believes these rates were appropriate given the risks associated with the technologies for which commercial feasibility had not been established. The percentage of completion for each in-process project was determined by identifying the elapsed time invested in the project as a ratio of the total time required to bring the project to technical and commercial feasibility. The percentage of completion for in-process projects acquired ranged from 10% to 90% for IMI, 5% to 75% for HiBand, 28% to 79% for ScanLogic, 1% to 89% for Lara, 10% to 70% for ISD and 9% to 87% for Silicon Packets. Schedules were based on management’s estimate of tasks completed and the tasks to be completed to bring the project to technical and commercial feasibility. As of December 30, 2001, the actual development timelines and costs are in line with management’s estimates.

Non-recurring charges recorded during fiscal 2001 were \$66.6 million. These charges relate primarily to an impairment loss of \$65.9 million. Based on a review of the intangibles related to our acquisitions and other long-lived assets, we recognized an impairment loss of \$65.9 million, the amount by which the carrying value of the acquired existing technology and pro-rata portion of the related goodwill exceeded the present value of the estimated future cash flows of the existing technology of SLM, a part of the Non-Memory business segment. During 2001, the optical market in which SLM participates experienced a severe economic downturn. Reduced demand for SLM’s products places increased risk on the future revenue streams anticipated from the existing display and monitor technology. Other non-recurring charges recorded during fiscal 2001 included a \$0.7 million charge related to the settlement of an intellectual property dispute.

During fiscal 2000, Cypress recorded acquisition and merger-related costs of \$54.2 million. Costs of \$39.9 million were incurred in relation to the acquisition of SLM, which was completed on August 30, 2000. SLM acquisition costs consisted of \$30.5 million for in-process research and development, and \$9.4 million for the amortization of intangible assets. Additional costs related to the amortization of intangible assets from the acquisitions of Anchor Chips, Inc. (“Anchor”), Arcus Technology (USA) and Arcus Technology (India) Limited (referred to as “Arcus” on a combined basis), the MAX<sup>®</sup> 5000 Programmable Logic Device (“PLD”) product line from Altera, and RadioCom were \$8.9 million. Acquisition costs of \$3.4 million were incurred in relation to the acquisitions of Galvantech, Alation, and RadioCom, which consist primarily of non-cash deferred compensation charges, legal, accounting and investment banking fees. In addition, Cypress recorded \$2.0 million for in-process research and development due to the acquisition of RadioCom. Cypress incurred a one-time charge of \$2.0 million in the second quarter of fiscal 2000 due to the acceleration of contractual obligations related to the Arcus acquisition.

During fiscal 1999, Cypress recorded \$37.9 million in merger and acquisition and other non-recurring costs. One-time, non-recurring costs were \$24.2 million, which included a \$12.3 million write-off of a manufacturing asset that was not being used and was subsequently scrapped, and an \$11.9 million one-time compensation charge associated with retention and performance payments to key employees in December 1999. Acquisition-related costs incurred during fiscal 1999 were \$13.7 million. In the first quarter of fiscal 1999, Cypress recorded one-time charges of \$3.8 million associated with the merger with IC Works. These charges were for investment banking fees and other professional fees. Cypress also recorded \$8.8 million in costs associated with the purchase of Anchor and Arcus consisting of \$4.0 million for in-process technology, \$1.6 million for transaction costs and \$3.2 million in amortization of intangible assets. During the fourth quarter of fiscal 1999, Cypress acquired Altera’s MAX 5000 Programmable Logic Device product line and its equity

interest in Cypress's wafer fabrication facility in Round Rock, Texas. As part of the transaction, Cypress recorded intangible assets associated with the product rights and incurred a charge of \$0.3 million for the amortization of these intangibles. Transaction costs and non-cash compensation costs incurred for other acquisitions were \$0.8 million.

## Restructuring

On July 16, 2001, Cypress announced a restructuring plan that involved resizing its manufacturing facilities, reducing its workforce, and combining facilities. The restructuring was precipitated by the worldwide economic slowdown, particularly in the business areas in which Cypress operates. The intended effect of the plan was to size the manufacturing operations and facilities to meet future demand and reduce expenses in all operations areas. During the third quarter of 2001, Cypress recorded restructuring charges of \$132.1 million related to property, plant and equipment, leased facilities and personnel. Cypress expects to recognize a benefit of up to \$12.0 million per quarter from lower depreciation and payroll costs in future periods. However, the net benefit to the Statement of Operations will be much less since we are operating at lower output rates and not building inventory that would have otherwise improved the operating results through greater absorption of costs.

The following table summarizes the restructuring reserve and charges for the year ended December 30, 2001.

(In thousands)

	Provision	Non-Cash Charges	Cash Charges	Reserves And Write-Downs at 12/30/2001
Property, plant and equipment	\$ 113,350	\$ 7,269	\$ 1,619	\$ 104,462
Leased facilities	4,079	—	213	3,866
Personnel	14,684	9,056	4,243	1,385
<b>Total</b>	<b>\$ 132,113</b>	<b>\$ 16,325</b>	<b>\$ 6,075</b>	<b>\$ 109,713</b>

The following paragraphs describe in more detail the components of the restructuring charges.

Restructuring costs related to property, plant and equipment amounted to \$113.4 million. In sizing Cypress to meet future demand, Cypress has taken out of service and is holding for sale manufacturing assets with a net book value of \$122.1 million. The charge represents the difference between the net book value of the assets less the estimated amount to be realized upon sale of the equipment, net of the estimated cost to dispose of the equipment. This amount has been recorded as a reduction in the carrying amount of the assets. The restructuring affects our facilities in Minnesota, Texas, California and the Philippines. If the actual amount realized upon the sale of equipment is less than estimated, we would incur an additional charge to earnings. Property, plant and equipment sales and/or dispositions are expected to be completed within one year. In each case, the asset was removed from service prior to September 30, 2001.

During the quarter ended September 30, 2001, Cypress incurred a \$4.1 million restructuring charge for three excess leased facilities. The costs to terminate or sublease these facilities are estimated to be approximately \$4.1 million, which is included in other current liabilities. This estimate is based on current comparable rates for leases in the respective markets. If facilities rental rates continue to decrease in these markets or if it takes longer than expected to sublease these facilities, the actual loss could exceed this estimate. Costs will be incurred over the remaining terms of the leases, the longest of which is three years.

Cypress implemented a reduction in force that affected employees at all significant locations. Under the restructuring plan, Cypress announced in July 2001 that it would terminate the employment of several hundred people. Those individuals were notified in July that their employment would cease on September 30, 2001. Cypress has terminated the employment of 714 people, of whom 709 employees had left Cypress as of December 30, 2001. The remainder will be leaving during the next six months after the completion of certain projects in which they are involved.

Personnel costs related to the reduction in force amounted to \$14.7 million. Severance and related employee benefit costs amounted to \$5.8 million. For those people whose employment ended on September 30, 2001, severance costs were paid at that time. For people leaving subsequent to September 30, 2001, severance costs will be paid at the time of their separation. In addition, effective August 14, 2001, the Cypress Board of Directors made a one-time decision to extend for those terminated employees the stock option exercise period from one month to twelve months after termi-

nation. Cypress recorded non-cash stock compensation expense of \$8.9 million for this modification during the quarter ended September 30, 2001.

During fiscal 2000, we reversed \$0.5 million of previously provided restructuring costs related to the decision to close down our wafer fab located in San Jose, California. We determined in the second quarter of fiscal 2000 that no outstanding commitments related to this restructuring remained.

During fiscal 1999, we recorded restructuring credits of \$3.8 million, which included a reversal of \$3.1 million of the 1998 restructuring reserve. The reversed charges of \$2.5 million primarily related to excess accruals for severance and other employee related charges. We also reversed \$0.6 million of excess fixed asset write-downs from the 1998 restructuring. In addition, during fiscal 1999, Cypress reversed \$0.7 million of excess fixed assets write-downs of the 1996 restructuring.

### Interest Income, Interest Expense and Other Income and (Expense), Net

Interest income, interest expense and other income and (expense), net, was \$15.2 million for fiscal 2001 compared to \$41.3 million for fiscal 2000 and \$43.6 million for fiscal 1999. Interest income and other, net, includes interest income, amortization of bond issuance costs, foreign exchange gains and losses and other non-operating items.

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Interest income	\$ 48,231	\$ 59,152	\$ 18,297
Interest expense	(22,398)	(23,633)	(9,643)
Other income and (expense), net	(10,652)	5,812	34,908
<b>Total interest income, interest expense and other income and (expense), net</b>	<b>\$ 15,181</b>	<b>\$ 41,331</b>	<b>\$ 43,562</b>

Interest income decreased \$10.9 million or 18.5% when comparing fiscal 2000 to 2001. This decrease in interest income in 2001 compared to 2000 is primarily due to lower average cash and investment balances in fiscal 2001. Interest income increased \$29.9 million or 163.6% when comparing fiscal 1999 to 2001. This increase is primarily due to higher average cash and investment balances in fiscal 2001 than in fiscal 1999.

Interest expense was \$22.4 million for fiscal 2001, compared to \$23.6 million for fiscal 2000 and \$9.6 million for fiscal 1999. Interest expense in fiscal 2001 is primarily associated with the 4.0% Convertible Subordinated Notes ("4.0% Notes"), issued in January 2000, due in 2005, and the 3.75% Convertible Subordinated Notes ("3.75% Notes"), issued in June 2000, due in 2005. The decrease in interest expense in fiscal 2001 compared to fiscal 2000 is primarily associated with a reduction in interest expense due to the conversion on October 2, 2000 of substantially all of the then outstanding 6.0% Convertible Subordinated Notes ("6.0% Notes"), issued in September 1997, due in 2002. The increase in interest expense from fiscal 1999 to fiscal 2001 is due to interest expense associated with the 4.0% Notes and 3.75% Notes, which were issued in January and June of fiscal 2000, respectively. The increase in interest expense was partially offset by a reduction in interest expense due to the conversion on October 2, 2000 of substantially all of the then outstanding 6.0% Notes.

Other income (expense), net of \$(10.6) million, for fiscal 2001 primarily reflects a \$8.9 million write-down of long-term investments, and \$3.3 million related to the amortization of bond issuance costs. Cypress took a charge in the third quarter of fiscal 2001 to reduce the carrying value of two long-term investments including startup, development stage and technology companies to their estimated net realizable values. These investments were reduced by \$1.5 million and \$7.4 million to \$1.5 million and \$4.2 million, respectively. Other income and (expense), net, for fiscal 2000 primarily reflects a \$5.0 million gain on the sale of the Fast CMOS Technology ("FCT") product line and a \$4.5 million gain on the disposal of assets partially offset by other items. Other income and (expense), net, for fiscal 1999 included a \$36.2 million gain from the sale of a certain investment. Other components of other income and (expense), net include \$1.0 million related to the amortization of bond issuance costs, and \$0.2 million in foreign exchange gains in 1999.

### Taxes

Cypress's effective tax rates for fiscal years 2001, 2000 and 1999 were (6.8%), 25.0%, and 7.4%, respectively. A tax benefit of (\$29.8) million was realized during fiscal 2001 compared to expenses of \$92.9 million and \$7.0 million during fiscal 2000 and fiscal 1999, respectively. The fiscal 2001 tax benefit was attributable primarily to current year net operating losses; however, the tax benefit

of these losses was limited, under generally accepted accounting principles, since there is uncertainty as to whether the full benefit of these losses may be realized. Accordingly, the valuation allowance against the net deferred tax assets increased from zero to \$60.3 million from fiscal 2000 to 2001, as Cypress believes it is more likely than not that the net deferred tax asset will not be realized. Management's assessment was based on the losses incurred in 2001 and Cypress's projections for future periods. The valuation allowance against net deferred tax assets decreased from \$42.6 million to \$0.0 million from fiscal 1999 to fiscal 2000, as Cypress believed it would realize the tax benefit of all of its deferred tax assets. Management's assessment was based on Cypress's profitability and forecasts for future periods.

As compared to the effective tax rate in fiscal 2000, the fiscal year 2001 effective tax rate was also affected by non-deductible in-process research and development charges and acquisition charges offset by research and development tax credits. Cypress's effective tax rate varies from the U.S. statutory rate primarily due to utilization of loss carryovers, earnings of foreign subsidiaries taxed at different rates, and tax credits. Cypress's global operations involve manufacturing, research and development, and selling activities outside the U.S. Cypress's operations outside the U.S. are in certain countries that impose a statutory tax rate higher than the U.S., as well as countries that impose a lower statutory tax rate than the U.S. U.S. tax has not been provided on profits from certain non-U.S. sales, until such profits are repatriated back to the U.S. Overall, we expect our foreign earnings to be taxed at a rate lower than the statutory tax rate in the U.S.

### **Extraordinary Gain**

In the fourth quarter of fiscal 2001, we retired a total of \$52.8 million principal of our \$287.5 million 3.75% Notes, for \$44.6 million, resulting in a pre-tax net gain of \$7.2 million. The net after-tax gain of \$4.3 million was recorded as an extraordinary gain.

### **Pro Forma Earnings (Loss) (Previously Referred to as Earnings Before Goodwill)**

In addition to our financial statements prepared in accordance with Generally Accepted Accounting Principles ("GAAP"), we provide our stockholders with pro forma financial information. We believe that our presentation of pro forma results is a useful addition to information provided to our investors. Our presentation of pro forma information excludes non-cash expenses resulting from acquisition or issuance of stock options, cash charges for payments based on the achievement of certain performance milestones under acquisition agreements, as well as unusual or infrequent expenses or credits that are not directly attributable to our ongoing operations and are expected to be incurred over a limited period of time. Because of these exclusions, our pro forma presentation is not in accordance with GAAP. Additionally, our presentation of pro forma information may not be consistent with that of other companies. PRO FORMA INFORMATION IS NOT, AND SHOULD NOT BE CONSIDERED, A SUBSTITUTE FOR FINANCIAL INFORMATION PREPARED IN ACCORDANCE WITH GAAP. We recognize that we must be consistent in our identification of unusual or infrequent items including both favorable and unfavorable items that meet these criteria.

We continuously review our pro forma practices to improve the presentation of our pro forma results. We have historically referred to our pro forma net income (loss) as "earnings before goodwill" or "EBG." Pursuant to our on-going review, we will now refer to this information as pro forma net income or loss. This change will make us more consistent with other companies that provide pro forma financial results.

Also, as a result of our on-going review, we decided not to adjust earnings or losses for any inventory adjustments in determining pro forma earnings. This change will be reflected currently and in all future periods and is reflected in the 2001 information included below. Previously, we added back to our net (loss) a \$93.1 million (before tax) charge for inventory reserves in calculating our pro forma net loss for the third quarter of 2001 as reported in both our third quarter 2001 press release and in our quarterly report on form 10-Q for that quarter and in calculating our pro forma net income presentation in our 2001 annual earnings press release issued in January 2002. We have not added this charge back to our earnings in the calculation below. As a result, our reported 2001 pro forma net income of \$2.2 million (as reported in our press release) has been reduced to a pro forma net loss of \$74.5 million.



(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Net income (loss)	\$ (407,412)	\$ 277,308	\$ 88,130
Goodwill and acquisition costs <sup>(1)</sup>	135,773	62,082	39,396
Restructuring costs (credits) <sup>(2)</sup>	132,113	(485)	(3,811)
Write-downs of certain investments and intangibles <sup>(3)</sup>	74,810	—	—
Gains on sales of certain assets <sup>(4)</sup>	—	(11,630)	(36,237)
Unusual costs <sup>(5)</sup>	11,776	1,898	—
Tax effects of pro forma adjustments	(20,075)	63	632
Income (loss) before extraordinary gain	(73,015)	329,236	88,110
Extraordinary gain net of taxes	(4,345)	—	—
Pro forma earnings (loss) <sup>(6)</sup>	\$ (77,360)	\$ 329,236	\$ 88,110

(1) In-process technology, non-cash stock compensation costs, cash charges based on the achievement of milestones under acquisition agreements, and the amortization of intangible assets and goodwill related to those acquisitions.

(2) In 2001 charges related to the resizing of facilities including the writing off of property, plant and equipment, the reduction in personnel, and exiting certain leased facilities.

(3) An impairment loss related to a wholly owned subsidiary (SLM) and the write-down of two long-term investments.

(4) Non-operating gains related to the sale of certain assets and investments.

(5) Unusual or one-time charges to reflect the result of a physical count of property, plant and equipment, settlement of legal disputes and the write-off of bond costs.

(6) For purposes of pro forma earnings as discussed, Cypress's effective tax rates for the fiscal years 2001, 2000, and 1999, were 14.2%, 22.0%, and 5.0%, respectively.

This information should be read in conjunction with our audited financial statements prepared in accordance with generally accepted accounting principles.

## Liquidity and Capital Resources

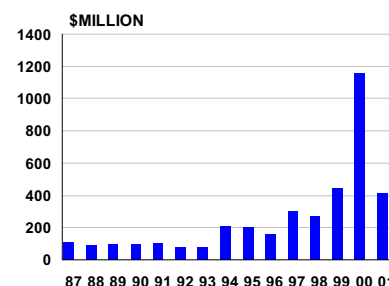
(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Cash, cash equivalents and short-term investments	\$ 205,422	\$ 884,601	\$ 280,947
Working capital	372,333	983,359	360,639
Long-term debt and capital lease obligations (excluding current portion)	525,673	631,055	170,884
Stockholders' equity	868,428	1,327,668	718,620
Net cash flow generated from operating activities	\$ 95,148	\$ 521,097	\$ 157,622

Cypress's cash, cash equivalents and short-term investments totaled \$205.4 million at December 30, 2001, a \$679.2 million decrease from the end of fiscal 2000. Working capital decreased \$611.0 million during the same period. These decreases are attributed primarily to net cash flows from our investing and financing activities.

During fiscal 2001, cash provided by operating activities of \$95.1 million was primarily attributed to changes in working capital of \$70.0 million and earnings less non-cash items.

Net cash flows used in investing activities of \$322.5 million, for fiscal 2001 related primarily to the use of \$352.1 million in cash for the acquisitions of IMI, ScanLogic, Lara, ISD and Silicon Packets, net of cash acquired, \$176.8 million for the purchases of property, plant and equipment and \$117.2 million for loans made by Cypress to employees under the stockholder-approved Stock Purchase Assistance Plan ("SPAP"). Purchases of investments totaled \$183.2 million during fiscal 2001, while investments, which were sold or matured, totaled \$502.7 million.

**Cash, Cash Equivalents,  
and Investments\***



\*Includes cash & short-term investments, restricted and long-term investments. Historical data does not include effect of Galvantech, Alation, and ICW prior to their mergers.

Net cash flows used for financing activities were \$213.6 million during fiscal 2001. Repurchases of common stock were \$190.5 million, redemption of convertible debt was \$45.4 million and purchases of private placement equity options, net were \$13.9 million. These cash outflows were offset primarily by cash inflows of \$10.6 million related to the premiums received from the writing of stock put options and \$30.8 million related to the issuance of common shares from the exercise of options or purchases through the Employee Stock Purchase Program ("ESPP").

During fiscal 2001, Cypress purchased \$176.8 million in capital equipment, a \$161.9 million decrease from the \$338.7 million purchased in 2000, and a \$62.4 million increase from the \$114.4 million purchased in 1999. Cypress purchased equipment for its domestic wafer fabrication plants, its assembly and test facility in the Philippines, its back-end manufacturing subcontractors and its design and technology groups. Capital expenditures in 2002 are expected to be slightly lower when compared to 2001 and will primarily be on projects which increase wafer manufacturing, assembly and test, and research and design capabilities. In fiscal 2002, Cypress expects to purchase approximately \$165 million in capital equipment.

For the year ended December 31, 2000, cash provided by operating activities of \$521.1 million was primarily attributable to earnings of \$277.3 million, tax benefits from stock options of \$56.7 million, acquired in-process research and development of \$32.4 million, depreciation and amortization of \$150.7 million and changes in working capital of \$2.0 million.

Net cash flows used in investing activities of \$642.8 million, for fiscal 2000 related primarily to purchases of investments, which totaled \$492.9 million and purchases of property, plant and equipment of \$338.7 million. Investments that were sold or matured totaled \$181.0 million in fiscal 2000.

For the year ended January 2, 2000, cash provided by operating activities of \$157.7 million was primarily attributable to earnings of \$88.1 million, depreciation and amortization of \$109.9 million, gain on sale of investment of \$36.2 million, loss on write down of assets of \$11.0 million, tax benefits from stock options of \$13.7 million and changes in working capital of \$15.2 million.

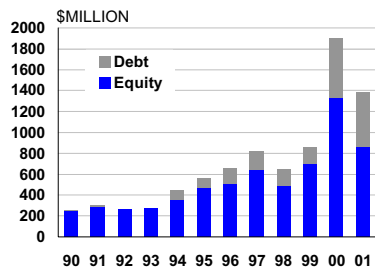
On January 31, 2000, Cypress filed a registration statement on Form S-3 with the Securities and Exchange Commission. Under this shelf registration statement, which was effective February 8, 2000, as amended by a post-effective amendment thereto effective March 7, 2000, Cypress can sell any combination of debt securities, preferred stock and common stock in one or more offerings up to a total amount of \$400.0 million. The shelf registration statement allows Cypress flexibility to raise funds from the offering of debt securities, common stock, preferred stock or a combination thereof, subject to market conditions and Cypress's capital needs. At December 30, 2001, the balance remaining related to the shelf registration statement was \$112.5 million.

On June 26, 2000, Cypress completed a \$287.5 million registered-placement of 5-year convertible subordinated notes. The notes are due in 2005, with a coupon rate of 3.75% and an initial conversion premium of 27.0%. The notes are convertible into approximately 4.6 million shares of common stock and are callable by Cypress no earlier than July 5, 2003.

On January 19, 2000, Cypress completed a \$283.0 million registered-placement of 5-year convertible subordinated notes. The notes are due in 2005, with a coupon rate of 4.00% and an initial conversion premium of 28.5%. The notes are convertible into approximately 6.1 million shares of common stock and are callable by Cypress no earlier than February 5, 2003.

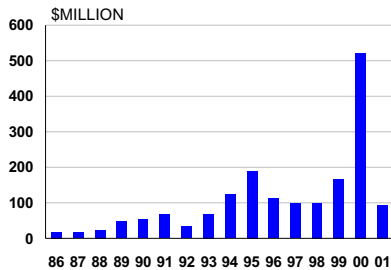
Cypress has entered into several synthetic operating lease agreements for manufacturing and office facilities. Synthetic leases are leases that qualify as capital leases for tax purposes, but qualify as operating leases for financial reporting. As such, synthetic leases represent a form of "off balance sheet" financing. The synthetic leases to which Cypress is a party require periodic payments that vary based on the London Interbank Offering Rate ("LIBOR"), plus a spread. Each of these leases provide Cypress with an option for renewal at mutually agreed upon terms, to acquire the property at the lessor's cost or to arrange for the property to be acquired by a third party at market value. If Cypress had exercised its right to purchase all the off balance sheet leases at December 30, 2001, it would have been required to make a payment and record assets totaling \$76.3 million. Cypress is required to maintain restricted cash or investments to serve as collateral for these leases. As of December 30, 2001, the amount of restricted cash recorded was \$75.0 million, which was classified as a non-current asset on the consolidated balance sheet. The leases also contain financial covenants. Cypress was not in compliance with the financial covenants of one of the agreements at December 30, 2001. In February 2002, Cypress obtained a waiver for this default and renegotiated the covenants for future periods. While Cypress expects to maintain compliance with the cove-

**Capitalization\***



\*Historical data does not include effect of Galvantech, Alation, and ICW prior to their mergers.

**Cash Generated by Operations\***



\*Historical data does not include effect of Galvantech, Alation, and ICW prior to their mergers.

nants, our ability to meet these financial covenants can be effected by events beyond its control and we cannot assure you that we will meet these covenants in the future.

At December 30, 2001, Cypress had purchase commitments aggregating \$33.4 million, principally for manufacturing equipment, and facilities and bulk gas and nitrogen. These commitments relate to purchases to be made in 2002 of \$29.9 million and the remainder is committed through 2008.

In June 1997, Cypress borrowed 700 million yen at 2.1% from Sumitomo Bank - Japan in order to set up and fund our Japanese business operations. Borrowing under this arrangement, which aggregated \$5.8 million at December 30, 2001, is due in fiscal 2003.

In the next twelve months the current economic downturn may negatively impact cash and cash equivalent balances and cash flow from operations; however, Cypress believes that existing cash, cash equivalents and investments, and cash from operations will be sufficient to meet present and anticipated working capital requirements and other cash needs for at least the next twelve months. Beyond twelve months, a continuation of the economic downturn, changes in market demand and the possible need to change manufacturing capacity and capability, may cause Cypress to raise additional capital through debt or equity financing. Although additional financing may be required, there can be no assurance that it would be available to Cypress or available at terms Cypress deems satisfactory.

Below is a summary of fixed payments related to certain contractual obligations, including off balance sheet arrangements. Payment timing may be subject to change.

(In thousands)

	<b>Total</b>	<b>Less than 1 Year</b>	<b>1-3 Years</b>	<b>4-5 years</b>	<b>After 5 Years</b>
Convertible subordinated notes - including interest	\$ 593,515	\$ 21,112	\$ 40,242	\$ 532,161	\$ —
Operating leases, including synthetic leases	66,235	20,297	31,938	11,829	2,171
Purchase commitments	33,448	29,934	1,990	762	762
Customer advances	65,058	30,497	34,561	—	—
Sumitomo Bank - Japan - including interest	5,791	—	5,791	—	—
<b>Total</b>	<b>\$ 764,047</b>	<b>\$ 101,848</b>	<b>\$ 114,522</b>	<b>\$ 544,752</b>	<b>\$ 2,933</b>

## Critical Accounting Policies

Our discussion and analysis of our financial condition and the results of our operations are based upon our consolidated financial statements included in this report and the data used to prepare them. Our financial statements have been prepared in accordance with accounting principles generally accepted in the United States and we are required to make estimates, judgments and assumptions in the course of such preparation. On an ongoing basis, we re-evaluate our judgments and estimates including those related to revenue recognition, product returns, reserves for doubtful accounts receivable and employee loans, inventories, long-lived assets, investments, restructuring charges, income taxes, litigation and contingencies. We base our estimates and judgments on our historical experience, knowledge of current conditions and our beliefs of what could occur in the future considering available information. Actual results may differ from these estimates under different assumptions or conditions. Our estimates are guided by observing the following critical accounting policies.

### *Revenue Recognition*

We generate revenue by selling our products to original equipment manufacturers and distributors. Our policy is to recognize revenue from sales to customers when title and the rights and risks of ownership have passed to the customer, when persuasive evidence of an arrangement exists, the product has been delivered, the price is fixed and determinable and collection of the resulting receivable is reasonably assured.

We allow certain distributors, primarily based in the United States, extensive rights of return and other credits for price protection. Given the uncertainties associated with the levels of returns and other credits issuable to these distributors, we defer recognition of revenue from sales to these distributors until they have resold our products. Our method of deferral is based on certain assump-

tions, including average gross margins. If actual results differ from our estimates, future operating results could be adversely affected.

Sales to certain other primarily non-U.S. based distributors carry either no or very limited rights of return. We have historically been able to estimate returns and other credits from these distributors and accordingly have historically recognized revenue from sales to these distributors on shipment, with a related allowance for potential returns established at the time of our sale. We must make estimates of potential future product returns and revenue adjustments related to current period product revenue. Management analyzes historical returns, current economic trends in the semiconductor industry, changes in customer demand and acceptance of our products when evaluating the adequacy of our allowance for sales returns. If management made different judgments or utilized different estimates, material differences in the amount of our reported revenue may result. We provide for these situations based on our experience with specific customers and our expectations for revenue adjustments based on economic conditions within the semiconductor industry. At December 30, 2001 and December 31, 2000 our reserves for sales returns were \$3.6 million and \$4.2 million, respectively.

We maintain an allowance for doubtful accounts for losses that we estimate will arise from our customers' inability to make required payments. We make our estimates of the uncollectibility of our accounts receivable by analyzing historical bad debts, specific customer creditworthiness and current economic trends. At December 30, 2001 the allowance for doubtful accounts was \$3.7 million and at December 31, 2000 it was \$2.0 million.

#### *Accounting for Income Taxes*

We record a valuation allowance to reduce our net deferred tax asset to the amount that is more likely than not to be realized. In assessing the need for a valuation allowance, we consider historical levels of income, expectations and risks associated with estimates of future taxable income and ongoing prudent and feasible tax planning strategies. In the event we determine that we would be able to realize deferred tax assets in the future in excess of the net recorded amount, we would record an adjustment to the deferred tax asset valuation allowance. This adjustment would increase income in the period such determination was made. Likewise, should we determine that we would not be able to realize all or part of the net deferred tax asset in the future, an adjustment to increase the deferred tax asset valuation allowance would be charged to income in the period such determination would be made. We have recorded a valuation allowance against our net deferred tax asset of \$60.3 million at December 30, 2001 and \$0.0 million at December 31, 2000.

#### *Valuation of Inventory*

We write down our inventory for "lower of cost or market" reserves, aged inventory reserves, obsolescence reserves and research and development reserves. Inventory reserves are generally recorded when the inventory for a device exceeds nine months of demand for that device and when individual parts have been in inventory for greater than six months. Our inventories represent high-technology parts that may be subject to rapid technological obsolescence and that are sold in a highly competitive industry. If actual product demand or selling prices are less favorable than we estimate, we may be required to take additional inventory write-downs. Likewise, if we sell more inventory, or at more favorable prices than we have forecasted, our future margins may be higher.

#### *Valuation of Long-Lived Assets*

Our business requires heavy investment in manufacturing facilities that are technologically advanced but can quickly become significantly underutilized or rendered obsolete by rapid changes in demand for semiconductors produced in those facilities.

We estimate the useful life of our manufacturing equipment, which is the largest component of our long-lived assets, to be five years. We base our estimate on our experience with acquiring, using and disposing of equipment over time. Depreciation expense is a major element of our manufacturing cost structure. We begin depreciation on new equipment when it is put into use for production. The aggregate amount of fixed assets under construction for which depreciation was not being recorded amounted to \$94 million at December 30, 2001 and \$119 million at December 31, 2000.

Our other long-lived assets are principally comprised of intangible assets from acquisitions accounted for under the purchase method.

We assess the impairment in value to our company of long-lived assets whenever events or circumstances indicate that their carrying value may not be recoverable. Factors we consider important that could trigger an impairment review include the following:

- significant negative industry trends;
- significant underutilization of the assets;
- significant changes in how we use the assets or our plans for their use;
- underperformance relative to historical or projected future operating results; and
- significant changes in company strategy.

If our review determines the future undiscounted cash flows related to these assets will not be sufficient to recover their carrying value we will reduce the carrying values of these assets down to our estimate of fair market value and continue depreciating them over their remaining useful lives. Our estimates of fair market value are generally based on discounted cash flow analyses or outside appraisals.

## Subsequent Events

In January 2002 the Department of Commerce revoked a 1998 antidumping order that had been imposed on SRAMs fabricated in Taiwan and imported into the United States. The Customs Service was ordered to refund, with interest, all duties deposited under the 1998 antidumping order. Between 1998 and 2001 Cypress incurred \$10.3 million to costs of revenues for such duties. As of February 28, 2002, Cypress has received \$4.0 million of the refund and expects \$8.0 million during the remainder of 2002. The refunds will be recorded as an offset to cost of revenues and the interest will be recorded as interest income as received.

During 2001, the Board of Directors authorized the repurchase of up to \$143.8 million of 3.75% Convertible Subordinated Notes. In January 2002, we repurchased a total principal amount of \$30.0 million for \$25.4 million, resulting in a pre-tax net gain of \$3.9 million. The net after-tax gain will be recorded as an extraordinary item in the 2002 consolidated statements of operations. Cumulatively we have repurchased \$82.8 million in principal.

## Recent Accounting Pronouncements

In July 2001, the FASB issued SFAS Nos. 141 and 142, "Business Combinations" and "Goodwill and Other Intangible Assets," respectively. SFAS No. 141 replaces APB Opinion No. 16 and eliminates pooling-of-interests accounting prospectively. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill will be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. In connection with the adoption of SFAS No. 142, Cypress will be required to perform a transitional goodwill impairment assessment. Cypress will adopt SFAS No. 142 in fiscal 2002. Cypress has not yet determined what impact SFAS No. 142 will have on our results of operations and financial position. In accordance with FAS No. 142, Cypress has not amortized goodwill on acquisitions completed after July 1, 2001. Cypress will stop amortizing goodwill for all other acquisitions on December 31, 2001 (the first day of fiscal 2002). Goodwill amortization was \$34.4 million in 2001.

In August 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations," which Cypress will adopt in fiscal 2002. SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. Cypress does not expect the adoption of SFAS No. 143 to have a significant impact on our financial position or results of operations.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", which supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," and portions of APB Opinion No. 30, "Reporting the Results of Operations – Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions." While SFAS No. 144 carries forward many of the provisions of SFAS No. 121 and APB Opinion No. 30, some of the key differences in the new standard are that goodwill is excluded from its scope, assets to be abandoned will be viewed as held for use and amortized over their remaining service period,



and the standard broadens the presentation of discontinued operations. Cypress will adopt SFAS No. 144 in fiscal 2002. Cypress does not expect the adoption of FAS No. 144 will have a significant effect on its results of operations or financial condition.

In December 2001, the Emerging Issues Task Force ("EITF") released Issue No. 01-09, "Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products." EITF Issue No. 01-09 generally requires companies to present consideration given to a customer as a reduction of revenue. EITF Issue No. 01-09 will be adopted in the first quarter of 2002 and will not have a material impact on our financial statements.

## **QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

### **Interest and Foreign Currency Exchange Rates**

Cypress is exposed to financial market risks, including changes in interest rates and foreign currency exchange rates. To mitigate these risks, Cypress utilizes derivative financial instruments. Cypress does not use derivative financial instruments for speculative or trading purposes.

The fair value of Cypress's investment portfolio, which is primarily invested in commercial paper and other similar instruments, would not be significantly impacted by either a 100 basis point increase or decrease in interest rates due mainly to the short-term nature of the major portion of Cypress's investment portfolio. An increase in interest rates would not significantly increase interest expense due to the fixed nature of Cypress's debt obligations.

A majority of Cypress's revenue and capital spending is transacted in U.S. dollars. However, Cypress does enter into these transactions in other currencies, primarily Japanese yen and Euro. To protect against reductions in value and the volatility of future cash flows caused by changes in foreign exchange rates, Cypress has established revenue and balance sheet hedging programs. Cypress's hedging programs reduce, but do not always eliminate, the impact of foreign currency exchange rate movements. Based on Cypress's overall currency rate exposure at December 30, 2001, a near-term 10% appreciation or depreciation in the U.S. dollar, relative to the Japanese Yen or the Euro, would have an immaterial effect on Cypress's financial position, results of operations and cash flows over the next fiscal year.

All of the potential changes noted above are based on sensitivity analyses performed on Cypress's balances as of December 30, 2001.

### **Equity Options**

At December 30, 2001, Cypress had outstanding a series of equity options (on Cypress common stock) in the amount of \$26.0 million. The options require physical settlement and expire in March and June 2002. Upon expiration of the options, if Cypress's stock price is above the trigger price, Cypress will have its capital returned with a premium. If below the trigger price, Cypress will receive a specified number of shares of Cypress common stock instead of a return of capital. The range of the trigger prices is \$20.60 - \$23.42. The transaction is recorded in stockholders' equity in the accompanying consolidated balance sheet.

At December 30, 2001, Cypress had outstanding 250,000 put options (on Cypress common stock) with a \$14.58 strike price. Upon expiration of the options, if Cypress's stock price is below the strike price, Cypress could take delivery of the underlying shares and be required to pay \$3.6 million. If above the strike price, Cypress will have no further obligations. The transaction is recorded in stockholders' equity in the accompanying consolidated balance sheet.

### **Investments in Development Stage Companies**

Cypress has also invested in several privately held companies, all of which can be considered in the startup or development stages. These investments are inherently risky as the market for the technologies or products they have under development are typically in the early stages and may never materialize. At December 30, 2001, Cypress had invested \$15.2 million, directly or indirectly, in development stage companies, all of which could be lost if the companies are not successful.

### **Stock Purchase Assistance Plan**

Cypress has loaned \$117.2 million to employees under the shareholder-approved Stock Purchase Assistance Plan for the purpose of purchasing Cypress common stock (see Note 11 to the Consolidated Financial Statements). Each loan was evidenced by a full recourse promissory note executed by the employee in favor of Cypress and was secured by all of the employee's assets, as well as, a pledge of the shares of our common stock purchased with the proceeds of the loan. Cypress maintains an allowance for doubtful accounts. For the period ending December 30, 2001, Cypress has written off \$6 thousand of such loans. If the price of Cypress common stock declined from its year end level of \$20.62 by 10%, Cypress's exposure to loans with the underlying common stock collateral worth less than the face value of the notes would be \$6.8 million.

## Consolidated Balance Sheets

(In thousands, except per-share amounts)

Year Ended

	December 30, 2001	December 31, 2000
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 109,999	\$ 551,025
Short-term investments	<u>95,423</u>	<u>333,576</u>
Total cash, cash equivalents and short-term investments	205,422	884,601
Accounts receivable, net	97,817	193,525
Inventories, net	73,268	104,935
Other current assets	250,328	99,725
<b>Total current assets</b>	<b>626,835</b>	<b>1,282,786</b>
Property, plant and equipment, net	499,795	571,475
Other assets	759,806	507,493
<b>Total assets</b>	<b>\$ 1,886,436</b>	<b>\$ 2,361,754</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 73,916	\$ 95,735
Accrued compensation and employee benefits	62,669	61,379
Other current liabilities	104,691	60,108
Deferred income on sales to distributors	11,926	34,084
Income taxes payable	1,300	48,121
<b>Total current liabilities</b>	<b>254,502</b>	<b>299,427</b>
Convertible subordinated notes	517,700	570,500
Deferred income taxes	203,272	103,604
Other long-term liabilities	42,534	60,555
<b>Total liabilities</b>	<b>1,018,008</b>	<b>1,034,086</b>
Commitments and contingencies (See Note 15)		
Stockholders' equity:		
Preferred stock, \$.01 par value, 5,000 shares authorized; none issued and outstanding	—	—
Common stock, \$.01 par value, 650,000 and 250,000 shares authorized; 139,052 and 136,895 issued; 121,495 and 125,659 outstanding at December 30, 2001 and December 30, 2000	1,391	1,369
Additional paid-in-capital	1,162,642	1,008,211
Deferred stock compensation	(53,141)	(10,360)
Accumulated other comprehensive income	2,722	—
Retained earnings	<u>103,860</u>	<u>513,649</u>
	1,217,474	1,512,869
Less: shares of common stock held in treasury, at cost; 17,557 shares and 11,236 shares at December 30, 2001 and December 30, 2000	<u>(349,046)</u>	<u>(185,201)</u>
<b>Total stockholders' equity</b>	<b>868,428</b>	<b>1,327,668</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 1,886,436</b>	<b>\$ 2,361,754</b>

The accompanying notes are an integral part of these Consolidated Financial Statements.

# Consolidated Statements of Operations

(In thousands, except per-share amounts)

Year Ended

	December 30, 2001	December 31, 2000	January 2, 2000
<b>Revenues</b>	<b>\$ 819,192</b>	<b>\$ 1,287,787</b>	<b>\$ 745,042</b>
Cost of revenues	552,267	564,839	408,885
Research and development	267,522	184,471	136,858
Selling, general and administrative	165,665	153,909	113,601
Acquisition and other non-recurring costs	161,253	56,214	37,902
Restructuring	132,113	(485)	(3,811)
<b>Total operating costs and expenses</b>	<b>1,278,810</b>	<b>958,948</b>	<b>693,435</b>
Operating income (loss)	(459,618)	328,839	51,607
Interest income	48,231	59,152	18,297
Interest expense	(22,398)	(23,633)	(9,643)
Other income and (expense), net	(10,652)	5,812	34,908
Income (loss) before income taxes and extraordinary gain	(444,437)	370,170	95,169
(Provision) benefit for income taxes	<u>32,680</u>	<u>(92,862)</u>	<u>(7,039)</u>
Net income (loss) before extraordinary gain	(411,757)	277,308	88,130
Extraordinary gain (net of tax \$2,896)	4,345	—	—
<b>Net income (loss)</b>	<b>\$ (407,412)</b>	<b>\$ 277,308</b>	<b>\$ 88,130</b>
Basic net income (loss) per share:			
Before extraordinary gain	\$ (3.32)	\$ 2.29	\$ 0.81
Extraordinary gain (net of tax)	0.04	—	—
Net income (loss)	\$ (3.28)	\$ 2.29	\$ 0.81
Diluted net income (loss) per share:			
Before extraordinary gain	\$ (3.32)	\$ 2.03	\$ 0.76
Extraordinary gain (net of tax)	0.04	—	—
Net income (loss)	\$ (3.28)	\$ 2.03	\$ 0.76
Weighted average common and common equivalent shares outstanding:			
Basic	124,135	121,126	108,156
Diluted	124,135	144,228	115,527

The accompanying notes are an integral part of these Consolidated Financial Statements.

# Consolidated Statements of Stockholders' Equity

(In thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Deferred Stock Compensation	Accumulated Other Comprehensive Income	Retained Earnings	Treasury Stock	Total Stockholders' Equity
<b>Balances at January 3, 1999</b>	<b>100,819</b>	<b>\$ 1,141</b>	<b>\$ 476,821</b>	<b>\$ (1,961)</b>	<b>\$ —</b>	<b>\$ 175,669</b>	<b>\$ (133,845)</b>	<b>\$ 517,825</b>
Cypress (Galvantech) activities for the quarter ended March 31, 1999	—	—	—	—	—	232	—	232
Re-issuance of treasury shares and issuance of common stock under employee stock plans and other	13,292	50	40,265	—	—	(27,690)	91,914	104,539
Tax benefit resulting from stock option transactions	—	—	13,772	—	—	—	—	13,772
Notes receivable from stockholders	—	—	(8,186)	—	—	—	—	(8,186)
Conversion of note payable into common stock	—	—	300	—	—	—	—	300
Compensation expense to outside consultants	—	—	234	—	—	—	—	234
Provision for and amortization of deferred compensation	—	—	1,745	29	—	—	—	1,774
Net income for the year	—	—	—	—	—	88,130	—	88,130
<b>Balances at January 2, 2000</b>	<b>114,111</b>	<b>1,191</b>	<b>524,951</b>	<b>(1,932)</b>	<b>—</b>	<b>236,341</b>	<b>(41,931)</b>	<b>718,620</b>
Issuance of common stock in relation to acquisitions	3,513	35	186,390	(15,053)	—	—	—	171,372
Repurchase of common stock under stock repurchase program	(6,256)	—	—	—	—	—	(143,270)	(143,270)
Issuance of common stock under employee stock plans and other	7,519	75	67,891	—	—	—	—	67,966
Issuance of common stock due to conversion of notes	6,772	68	159,918	—	—	—	—	159,986
Amortization of deferred compensation	—	—	—	6,625	—	—	—	6,625
Notes receivable from stockholders	—	—	6,040	—	—	—	—	6,040
Premiums received from issuance of put options	—	—	6,288	—	—	—	—	6,288
Tax benefit resulting from stock option transactions	—	—	56,733	—	—	—	—	56,733
Net income for the year	—	—	—	—	—	277,308	—	277,308
<b>Balances at December 31, 2000</b>	<b>125,659</b>	<b>1,369</b>	<b>1,008,211</b>	<b>(10,360)</b>	<b>—</b>	<b>513,649</b>	<b>(185,201)</b>	<b>1,327,668</b>
Issuance of common stock in relation to acquisitions	2,157	22	107,566	(42,140)	—	—	—	65,448
Repurchase of common stock under stock repurchase program	(9,534)	—	—	—	—	—	(190,459)	(190,459)
Re-issuance of treasury shares and issuance of common stock under employee stock plans and other	3,213	—	6,604	—	—	(2,377)	26,614	30,841
Provision for and amortization of deferred compensation	—	—	42,676	(641)	—	—	—	42,035
Notes receivable from stockholders	—	—	871	—	—	—	—	871
Premiums received from issuance of put options	—	—	10,648	—	—	—	—	10,648
Structured purchase of options, net	—	—	(13,934)	—	—	—	—	(13,934)
Other comprehensive income	—	—	—	—	2,722	—	—	2,722
Net loss for the year	—	—	—	—	—	(407,412)	—	(407,412)
<b>Balances at December 30, 2001</b>	<b>121,495</b>	<b>\$ 1,391</b>	<b>\$1,162,642</b>	<b>\$ (53,141)</b>	<b>\$ 2,722</b>	<b>\$ 103,860</b>	<b>\$ (349,046)</b>	<b>\$ 868,428</b>

The accompanying notes are an integral part of these Consolidated Financial Statements.



# Consolidated Statements of Cash Flows

(In thousands)

Year Ended

	December 30, 2001	December 31, 2000	January 2, 2000
Cash flow from operating activities:			
Net income (loss)	\$ (407,412)	\$ 277,308	\$ 88,130
Adjustments to reconcile net income (loss) to net cash generated by operating activities:			
Depreciation and amortization	249,003	150,704	109,920
Acquired in-process research and development	23,200	32,425	4,019
Extraordinary gain on early retirement of debt	(4,345)	—	—
Loss on write down of assets	—	—	11,047
Deferred gain on sale of fixed assets	—	—	(3,959)
Gain on sales of assets	—	(5,000)	(36,237)
Restructuring costs (credits)	115,333	(485)	(3,811)
Other non-recurring costs	80,436	1,964	—
Tax benefit resulting from stock option transactions	—	56,733	13,722
Deferred income taxes	(31,085)	5,434	(9,971)
Changes in operating assets and liabilities, net of effects of acquisitions:			
Accounts receivable, net	102,262	(89,166)	(30,416)
Inventories, net	40,718	(7,162)	(30,149)
Other assets	(7,197)	(14,367)	(13,507)
Accounts payable, accrued and other liabilities	(43,454)	71,876	58,676
Deferred income	(22,158)	13,023	7,221
Income taxes payable	(153)	27,810	(7,002)
<b>Net cash flow generated from operating activities</b>	<b>95,148</b>	<b>521,097</b>	<b>157,683</b>
Cash flow from investing activities:			
Purchase of investments	(183,168)	(492,855)	(218,383)
Sale or maturities of investments	502,658	181,018	66,872
Acquisition of property, plant and equipment	(176,793)	(338,740)	(114,364)
Cash paid for acquisitions	(352,096)	—	(41,726)
Proceeds from sale of investment	—	7,500	36,237
Issuance of notes to employees, net	(117,220)	—	—
Proceeds from sale of equipment	4,132	325	16,179
<b>Net cash flow used for investing activities</b>	<b>(322,487)</b>	<b>(642,752)</b>	<b>(255,185)</b>
Cash flow from financing activities:			
Issuance of convertible subordinated notes, net of issuance costs	—	554,812	—
Redemption of convertible debt	(45,406)	—	—
Repurchase of common stock	(190,459)	(143,270)	—
Re-issuance of treasury shares and issuance of common stock	30,841	63,538	116,982
(Issuance) repayment of notes to stockholders, net	871	6,040	(8,186)
Premiums received from put options	10,648	6,288	—
Structured purchase of options, net	(13,934)	—	—
Other liabilities, including minority interest	(6,248)	17,566	(1,257)
<b>Net cash flow generated from (used for) financing activities</b>	<b>(213,687)</b>	<b>504,974</b>	<b>107,539</b>
Net change in cash during the period due to mergers and acquisitions	—	8,618	(2,339)
Net increase (decrease) in cash and cash equivalents	(441,026)	391,937	7,698
Cash and cash equivalents, beginning of year	551,025	159,088	151,390
<b>Cash and cash equivalents, end of year</b>	<b>\$ 109,999</b>	<b>\$ 551,025</b>	<b>\$ 159,088</b>
Supplemental disclosures:			
Cash paid (received) during the year for:			
Interest	\$ 23,559	\$ 15,734	\$ 9,626
Income taxes	\$ (9,778)	\$ 15,252	\$ 5,467
Non-cash flow items:			
Common stock and options issued for acquisitions	\$ 107,588	\$ 186,425	\$ 6,200

The accompanying notes are an integral part of these Consolidated Financial Statements.

# Notes to Consolidated Financial Statements

## Note 1: Summary of Significant Accounting Policies

**Cypress** — Cypress Semiconductor Corporation (“Cypress”) designs, develops, manufactures and markets a broad line of high-performance digital and mixed-signal integrated circuits for a range of markets, including data communications, telecommunications, computation, consumer products, and industrial control. With a focus on emerging communications applications, Cypress’s product portfolios include: networking-optimized and micropower static RAMs; high-bandwidth multiport and FIFO memories; datacom products; high-density programmable logic devices; timing technology for PCs and other digital systems; and controllers for Universal Serial Bus (“USB”).

Cypress’s operations outside of the U.S. include its assembly and test plant in the Philippines and several sales offices and design centers located in various parts of the world. Revenues to international customers were 50%, 49% and 49% of total revenues in 2001, 2000 and 1999, respectively.

The consolidated financial statements include the accounts of Cypress and all of its subsidiaries. Intercompany transactions and balances have been eliminated in consolidation.

**Fiscal Year** — The Cypress fiscal year ends on the Sunday closest to December 31. Fiscal years 2001, 2000 and 1999 ended December 30, 2001, December 31, 2000 and January 2, 2000, respectively, and each included 52 weeks.

**Management Estimates** — The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates in these financial statements include reserves for deferred income, reserves for price adjustment on sales to distributors, the sales return reserve, restructuring charges, allowances for doubtful accounts receivable, estimates for future cash flows associated with assets, asset impairments, reserves for loans under the Stock Purchase Assistance Program, net realizable value for inventories, certain accrued liabilities and income taxes and tax valuation allowances. Actual results could differ from those estimates, although such differences are not expected to be material to the financial statements.

**Reclassifications** — Certain prior year amounts have been adjusted to conform to current year presentation.

**Fair Value of Financial Instruments** — For certain of Cypress’s financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and other current liabilities, the carrying amounts approximate their fair value due to the relatively short maturity of these items. Investments in debt securities are carried at fair value based on quoted prices. At December 30, 2001, the estimated fair value of the Convertible Subordinated Notes was approximately \$443.0 million. Foreign currency derivative financial instruments are carried at fair value based on changes in forward rate from quoted market sources (see Note 9).

The estimated fair values have generally been determined by Cypress using available market information. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of the amounts that Cypress could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies could have a material effect on the estimated fair value amounts.

**Cash Equivalents** — Highly liquid investments purchased with an original maturity of ninety days or less are considered equivalent to cash.

**Investments** — All Cypress investments in debt securities are classified as available-for-sale. Investments in available-for-sale securities are reported at fair value with unrealized gains and losses, net of related tax, as a component of stockholders’ equity. Unrealized gains and (losses) were \$4.5 million, and were \$2.7 million net of related taxes, for the year ended December 30, 2001. Unrealized gains and (losses) net of related taxes were immaterial for prior years.

Cypress also has other minority equity investments in nonpublicly traded companies. These investments are included in other assets on the balance sheet and are generally carried at cost. Cypress monitors these investments for impairment and makes appropriate reductions in carrying values when declines are deemed to be other than temporary.

**Inventories** — Inventories are stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or market. Market is based on estimated net realizable value. Cypress establishes “lower of cost or market” reserves, aged inventory reserves, obsolescence reserves and research and development reserves. Inventory reserves are generally recorded when the inventory for a device exceeds nine months of demand for that device and when individual parts have been in inventory for greater than six months.

**Property, Plant and Equipment** — Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation is computed for financial reporting purposes using the straight-line method over the estimated useful lives of the assets as presented below. Leasehold improvements and leasehold interests are

amortized over the shorter of the estimated useful lives of the assets or the remaining term of the lease. Accelerated methods of computing depreciation are used for tax purposes.

	Useful Lives in Years
Equipment	3 to 7
Buildings and leasehold improvements	5 to 20
Furniture and fixtures	5 to 7

**Pre-operating Costs** — Pre-operating costs incurred in connection with developing major production capability at new manufacturing plants are expensed as incurred.

**Long-Lived Assets** — Cypress currently evaluates its long-lived assets, including intangible assets, in accordance with the provisions of SFAS No. 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of,” for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or intangibles may not be recoverable. Factors Cypress considers important that could result in an impairment review include, but are not limited to, significant underperformance relative to expected historical or projected future operating results, significant changes in the manner of use of the acquired assets or the strategy for Cypress’s overall business, significant underutilization of the assets, the negative industry or economic trends, a significant decline in our stock price for a sustained period of time, and Cypress’s market capitalization relative to net book value. When it is determined that the carrying value of a long-lived asset may not be recoverable based upon the existence of one or more of the above indicators of impairment, Cypress measures any impairment based on projected discounted cash flows using a discount rate commensurate with the risk inherent in our current business model.

**Revenue Recognition** — In December 1999, the staff of the Securities and Exchange Commission (“SEC”) issued Staff Accounting Bulletin No. 101 (“SAB 101”) “Revenue Recognition in Financial Statements,” which provides guidance on the recognition, presentation, and disclosure of revenue in financial statements filed with the SEC. SAB 101 outlines the basic criteria that must be met to recognize revenue and provides guidance for disclosures related to revenue recognition policies. The adoption of SAB 101 in fiscal 2000 did not have a material effect on Cypress’s results.

Revenues from product sales are generally recognized when persuasive evidence of an arrangement exists, the price is fixed or determinable, collection is reasonably assured and delivery of product has occurred. Reserves are provided for estimated returns. A portion of Cypress’s sales are made to distributors under agreements that allow certain rights of return and price protection on products unsold. Accordingly, Cypress defers recognition of revenues, cost of sales and profit on such sales until these distributors resell these products. Inventory is relieved, accounts receivable are recorded and reserves for deferred income and price adjustments are provided at the time the products are shipped to the distributors.

Cypress also sells to certain international distributors whose contracts have provisions for price adjustments on certain products without a right of return. Cypress generally recognizes revenue upon shipment to these distributors and reserves for estimated price adjustments at that time.

Cypress also has inventory that is held by certain customers on a consignment basis. Revenues are recorded when title and risk of loss transfers as defined per the respective consignment agreements.

**Earnings Per Share** — Basic Earnings Per Share (“EPS”) is computed using weighted average common shares outstanding. Diluted EPS is computed using weighted average common shares outstanding plus any potentially dilutive securities, except when their effect is anti-dilutive. Dilutive securities include stock options, convertible debt and put options.

**Translation of Foreign Currencies** — Cypress uses the U.S. dollar as its functional currency for all foreign subsidiaries. Accordingly, gains and losses from translation of foreign currency financial statements into U.S. dollars are included in results of operations. Sales to customers are primarily denominated in U.S. dollars. Translation gains and losses have not been material in any year.

**Concentration of Credit Risk** — Financial instruments that potentially subject Cypress to concentrations of credit risk are primarily investments and trade accounts receivable. Cypress’s investment policy requires cash investments to be placed with high-credit quality institutions and to limit the amount of credit risk from any one issuer.

Cypress sells its products to original equipment manufacturers and distributors throughout the world. Cypress performs ongoing credit evaluations of its customers’ financial condition whenever deemed necessary and generally does not require collateral. Cypress maintains an allowance for doubtful accounts receivable based upon the expected collectibility of all accounts receivable. No individual customer represented greater than 10% of accounts receivable at December 30, 2001. No individual customer accounted for greater than 10% of total revenues in 2001. Sales to Motorola, Inc. accounted for 10.9% of total revenues in fiscal 2000. In fiscal 1999 no individual customer accounted for greater than 10% of total revenues. No individual distributor accounted for greater than 10% of total revenues in either fiscal 2001 or fiscal 2000. Sales to Arrow Electron-

ics, Inc., a distributor, accounted for 10% of total revenues in fiscal 1999. Write-offs of accounts receivable have been immaterial during the preceding three fiscal years.

**Accounting for Stock-Based Compensation** — Cypress accounts for its stock option plans and its employee stock purchase plan using the intrinsic value method in accordance with provisions of the Accounting Principles Board (“APB”) Opinion No. 25, “Accounting for Stock Issued to Employees” and complies with the disclosure provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123, “Accounting for Stock-Based Compensation.” If there is any compensation cost under the rules of APB Opinion No. 25, the expense is amortized using an accelerated method prescribed under the rules of Financial Accounting Standards Board (“FASB”) Interpretation 28.

**Comprehensive Income** — Comprehensive income is defined as the change in equity during a period from non-owner sources. Cypress’s comprehensive income is comprised of net income and unrealized gains and losses (net of taxes) on investments classified as available for sale.

**Recent Accounting Pronouncements** — In July 2001, FASB issued SFAS Nos. 141 and 142, “Business Combinations” and “Goodwill and Other Intangible Assets,” respectively. SFAS No. 141 replaces APB Opinion No. 16 and eliminates pooling-of-interests accounting prospectively. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill will be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. In connection with the adoption of SFAS No. 142, Cypress will be required to perform a transitional goodwill impairment assessment. Cypress will adopt SFAS No. 142 in fiscal 2002. Cypress has not yet determined what impact SFAS No. 142 will have on its results of operations and financial position. In accordance with SFAS No. 142, Cypress has not amortized goodwill on acquisitions completed after July 1, 2001. Cypress will stop amortizing goodwill for all other acquisitions on December 31, 2001 (the first day of fiscal 2002). Goodwill amortization was \$34.4 million in 2001.

In August 2001, FASB issued SFAS No. 143, “Accounting for Asset Retirement Obligations,” which Cypress will adopt in fiscal 2002. SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. Cypress does not expect the adoption of SFAS No. 143 to have a significant impact on its financial position or results of operations.

In October 2001, FASB issued SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” which supersedes SFAS No. 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of,” and APB Opinion No. 30, “Reporting the Results of Operations – Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions.” While SFAS No. 144 carries forward many of the provisions of SFAS No. 121 and APB Opinion No. 30, some of the key differences in the new standard are that goodwill is excluded from its scope, assets to be abandoned will be viewed as held for use and amortized over their remaining service period, and the standard broadens the presentation of discontinued operations. Cypress will adopt SFAS No. 144 in fiscal 2002. Cypress does not expect the adoption of SFAS No. 144 to have a significant impact on our financial position or results of operations.

In December 2001, the Emerging Issues Task Force (“EITF”) released Issue No. 01-09, “Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor’s Products.” EITF Issue No. 01-09 generally requires companies to present consideration given to a customer as a reduction of revenue. EITF Issue No. 01-09 will be adopted in the first quarter of 2002 and will not have a material impact on our financial statements.

## Note 2: Balance Sheet Components

### Available-For-Sale Securities

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Corporate debt securities	\$ 164,394	\$ 515,352
Federal, state and municipal obligations	77,405	117,336
Money markets funds	60,616	425,359
Other	17,832	14,089
<b>Available-for-sale securities</b>	<b>\$ 320,247</b>	<b>\$ 1,072,136</b>

Available-for-sale securities include cash and cash equivalents, short-term investments, plus long-term investments shown below in Other Assets. Cash of \$19.7 million and \$23.9 million is excluded from available-for-sale securities as of December 30, 2001 and December 31, 2000, respectively. At December 30, 2001 the net unrealized holding gains and losses on securities were \$4.5 million gross (\$2.7 million net of tax) and prior to 2001 it was not material. The securities at December 30, 2001 and December 31, 2000 are shown by contractual maturity below.

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Due in one year or less	\$ 185,752	\$ 860,692
Due after one year through two years	134,495	211,444
<b>Available-for-sale securities</b>	<b>\$ 320,247</b>	<b>\$ 1,072,136</b>

### Accounts Receivable, Net

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Accounts receivable, gross	\$ 105,156	\$ 199,730
Allowance for doubtful accounts and customer returns	(7,339)	(6,205)
<b>Accounts receivable, net</b>	<b>\$ 97,817</b>	<b>\$ 193,525</b>

### Inventories, Net

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Raw materials	\$ 6,708	\$ 11,387
Work-in-process	42,624	63,200
Finished goods	23,936	30,348
<b>Inventories, net</b>	<b>\$ 73,268</b>	<b>\$ 104,935</b>

### Other Current Assets

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Employee stock purchase assistance plan, net	\$ 117,220	\$ —
Deferred tax assets	104,798	61,772
Other current assets	28,310	37,953
<b>Other current assets</b>	<b>\$ 250,328</b>	<b>\$ 99,725</b>

### Property, Plant and Equipment, Net

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Land	\$ 14,426	\$ 14,448
Equipment	956,667	984,395
Buildings and leasehold improvements	165,089	152,606
Furniture and fixtures	11,015	10,046
Total property, plant and equipment	1,147,197	1,161,495
Accumulated depreciation and amortization	(647,402)	(590,020)
<b>Property, plant and equipment, net</b>	<b>\$ 499,795</b>	<b>\$ 571,475</b>

### Other Assets

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Restricted investments	\$ 74,968	\$ 60,698
Long-term investments	134,495	211,444
Intangible assets	196,680	191,569
Goodwill	300,024	23,068
Deferred tax asset	36,791	853
Other	16,848	19,861
<b>Other assets</b>	<b>\$ 759,806</b>	<b>\$ 507,493</b>



## Other Current Liabilities

(In thousands)

	Year Ended	
	December 30, 2001	December 31, 2000
Customer advances	\$ 30,497	\$ 20,159
Accrued interest payable	9,139	10,305
Sales representative commissions	3,057	7,301
Accrued royalties	3,975	4,007
Other	58,023	18,336
<b>Other current liabilities</b>	<b>\$ 104,691</b>	<b>\$ 60,108</b>

## Note 3: Acquisitions Using Purchase Accounting

### 2001 Acquisitions

#### Acquisition of Silicon Packets, Inc.

On December 27, 2001, Cypress acquired 100% of the outstanding common and preferred stock of Silicon Packets, Inc. ("Silicon Packets") a company that specializes in designing 10 Gigabit-per-second framers for OC-192/STM-64 Synchronous Optical Network/Synchronous Digital Hierarchy ("SONET/SDH") and 10-Gigabit Ethernet transport solutions. Silicon Packets will be part of the Non-Memory business segment and the Wide Area Network/ Storage Area Network ("WAN/SAN") market segment. The acquisition accelerates Cypress's current schedule to develop 10 Gigabit-per-second solutions for MAN (Metropolitan Area Networks), which is part of the SAN/WAN market segment, and WAN infrastructure equipment such as switches and routers. The acquisition was accounted for using the purchase method of accounting per FASB SFAS No. 141. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of December 27, 2001, the effective date of the purchase. Other than the charge for in-process research and development, Silicon Packet's results of operations from the date of purchase to the end of the fiscal year were not significant because the acquisition was completed during the last week of the fiscal year and are therefore not included in Cypress's consolidated results of operations for the year ended December 30, 2001. There were no significant differences between the accounting policies of Cypress and Silicon Packets.

Cypress acquired Silicon Packets for total consideration of \$27.3 million, including 0.7 million shares of Cypress common stock valued at \$14.2 million, \$7.1 million in cash, options for 0.2 million shares of Cypress common stock valued at \$3.2 million and direct acquisition costs of \$2.8 million for underwriting, legal, valuation, accounting and regulatory fees. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as set forth in the following table:

(In thousands)

Current assets	\$ 968
Property, plant and equipment, net	951
Deferred tax asset	2,110
Other assets	58
Goodwill	9,751
Current technology	4,300
Non-complete agreements	800
Total assets acquired	18,938
Current liabilities	(745)
Long term liabilities	(509)
Deferred tax liabilities	(2,040)
Total liabilities assumed	(3,294)
Deferred stock compensation (See Note 8)	6,589
Net assets acquired	22,233
In-process research and development	5,100
<b>Total consideration</b>	<b>\$ 27,333</b>

The amounts allocated to current technology and non-compete agreements have weighted average useful lives of 4 years and 3 years, respectively. These intangible assets are amortized using the straight-line method over their respective estimated useful lives. None of the \$9.8 million in goodwill recorded is expected to be deductible for tax purposes, and, in accordance with SFAS No. 142, will not be amortized.

The agreement with Silicon Packets includes provisions for contingent cash payments of up to \$5.0 million through December 2002 based on the achievement of specific targets in future periods. These cash payments are also contingent upon the payees remaining employed by Cypress and will be accounted for as compensation for services and expensed in the appropriate periods.

### Acquisition of In-System Design, Inc.

On September 14, 2001, Cypress acquired 100% of the outstanding capital stock of In-System Design, Inc. ("ISD"), a system-on-chip design company specializing in personal communications solutions. ISD will be part of the Non-Memory business segment and the Computation and Other market segment. The immediate benefit to Cypress relates to ISD's 300A product, a USB 2.0 to ATA/ATAPI bridge device that enables PCs and other information appliances to connect to external mass storage devices including hard disk drives, CD-ROMs, CD-RWs DVD-Rams, and ZIP drives. The acquisition will also bring a veteran development team with an average eight years of experience to Cypress. The ISD team has a wide range of engineering competencies, including system-on-a-chip ("SoC") expertise, software design, board-level design, test and validation, that are expected to accelerate Cypress's current and future development projects. The acquisition was accounted for using the purchase method of accounting per SFAS No. 141. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of September 14, 2001, the effective date of the purchase. The results of operations are included in Cypress's consolidated results of operations as of and since the effective date of the purchase. There were no significant differences between the accounting policies of Cypress and ISD.

Cypress acquired ISD for total consideration of \$43.0 million, including \$36.7 million in cash, options for 0.3 million shares of Cypress common stock valued at \$5.4 million and direct acquisition costs of \$0.9 million for legal, appraisal and accounting fees. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as set forth in the following table:

(In thousands)

Current assets	\$ 4,554
Property, plant and equipment	632
Deferred tax asset	5,378
Goodwill	19,922
Current technology	17,200
Non-complete agreements	12,350
Trademarks	2,400
Customer purchase orders	450
Total assets acquired	62,886
Current liabilities	(9,445)
Deferred tax liabilities	(12,960)
Total liabilities assumed	(22,405)
Deferred stock compensation (See Note 8)	1,679
Net assets acquired	42,160
In-process research and development	800
<b>Total consideration</b>	<b>\$ 42,960</b>

The amounts allocated to current technology, non-compete and customer purchase orders and trademarks have weighted average useful lives of 4 years, 3 years, 1 year and 4 years, respectively. These intangible assets are amortized using the straight-line method over their respective estimated useful lives. None of the \$19.9 million in goodwill recorded is expected to be deductible for tax purposes, and, in accordance with SFAS No. 142, will not be amortized.

The agreement with ISD includes provisions for contingent cash payments of up to \$27.5 million through September 2004 based on USB product revenues achieving specific targets in future periods. These cash payments are also contingent upon the payees remaining employed by Cypress. The agreement with ISD provides for additional contingent cash payments of up to \$12.0 million through September 2004 based on continued employment with Cypress. All of these contingent payments will be accounted for as compensation for services and expensed in the appropriate periods.

### Acquisition of Lara Networks, Inc.

On July 3, 2001, Cypress acquired 100% of the outstanding common and preferred stock of Lara Networks, Inc. ("Lara"), a provider of high-performance, silicon-based packet processing solutions for WAN infrastructure equipment. Lara will be part of the Non-Memory business segment and the SAN/WAN market segment. Lara fits strategically and leverages Cypress's core competencies in data communications and specialty memories. Lara was acquired to expand Cypress's portfolio of solutions across the linecard. Lara's products will

enable Cypress to address the core functionality of packet processing. The acquisition was accounted for using the purchase method of accounting per SFAS No. 141. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of July 3, 2001, the effective date of the purchase. The results of operations are included in Cypress's consolidated results of operations as of and since the effective date of the purchase. There were no significant differences between the accounting policies of Cypress and Lara.

Cypress acquired Lara for total consideration of \$200.1 million, including \$185.3 in cash, options for 0.4 million shares of Cypress common stock valued at \$8.1 million and direct acquisition costs of \$6.7 million for underwriting, legal, valuation, accounting and regulatory fees. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as follows:

(In thousands)

Current assets	\$ 11,234
Property, plant and equipment	4,789
Deferred tax asset	17,016
Other assets	1,222
Goodwill	158,322
Current technology	14,850
Trademarks	2,250
Non-complete agreements	1,550
Customer purchase orders	150
Total assets acquired	211,383
Current liabilities	(13,969)
Deferred tax liabilities	(7,520)
Total liabilities assumed	(21,489)
Deferred stock compensation (See Note 8)	5,662
Net assets acquired	195,556
In-process research and development	4,550
<b>Total consideration</b>	<b>\$ 200,106</b>

The amounts allocated to current technology, trademarks, non-compete and customer purchase orders have weighted average useful lives of 5 years, 5 years, 3 years and 0.5 years, respectively. These intangible assets are amortized using the straight-line method over their respective estimated useful lives. None of the \$158.3 million in goodwill recorded is expected to be deductible for tax purposes, and, in accordance with SFAS No. 142, will not be amortized.

The agreement with Lara includes provisions for contingent cash payments of up to \$80.0 million through December 2002 based on certain Lara products achieving specific revenue targets in future periods, which will be recorded as an increase in the purchase price if paid. As of December 30, 2001, no such payments have been made.

The agreement with Lara further provides for contingent cash payments of up to \$3.9 million to certain Lara employees through December 2004 based on certain conditions including continued employment with Cypress. As such, this contingency will be accounted for as compensation for services and expensed in the appropriate periods.

### Acquisition of ScanLogic Corporation

On May 29, 2001, Cypress completed its acquisition of ScanLogic Corporation ("ScanLogic"), a provider of USB controllers for embedded and PC applications. The acquisition was accounted for using the purchase method of accounting per APB Opinion No. 16. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of May 29, 2001, the effective date of the purchase. The results of operations are included in Cypress's consolidated results of operations as of and since the effective date of the purchase. There were no significant differences between the accounting policies of Cypress and ScanLogic.

Cypress acquired ScanLogic for total consideration of \$30.1 million, including \$15.6 million in cash, options for 0.5 million shares of Cypress common stock valued at \$11.7 million, notes payable to shareholders of \$1.9 million and direct acquisition costs of \$0.9 million for legal and accounting fees and broker commissions. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as follows:

(In thousands)

Fair value of tangible assets and liabilities	\$ (1,446)
In-process research and development	1,450
Current technology	11,950
Assembled workforce and non-complete agreements	1,400
Deferred stock compensation (See Note 8)	7,330
Excess of purchase price over identifiable net assets acquired	9,419
<b>Total</b>	<b>\$ 30,103</b>

The amounts allocated to current technology, assembled workforce and residual goodwill are being amortized using the straight-line method over their respective estimated useful lives, which range from three to four years.

#### Acquisition of HiBand Semiconductors, Inc.

On March 27, 2001, Cypress acquired all of the outstanding capital stock of HiBand Semiconductors, Inc. ("HiBand"). HiBand is a provider of mixed-signal integrated circuits for high-speed communications markets. The acquisition was accounted for using the purchase method of accounting per APB Opinion No. 16. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of March 27, 2001, the effective date of the purchase.

Cypress acquired HiBand for total consideration of \$34.0 million, including 1.4 million shares of Cypress common stock valued at \$28.2 million, options for 0.2 million shares of Cypress common stock valued at \$4.0 million, an existing \$1.3 million cash advance and direct acquisition costs of \$0.5 million for legal and accounting fees. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as follows:

(In thousands)

Fair value of tangible assets and liabilities	\$ (181)
In-process research and development	6,450
Current technology	2,800
Assembled workforce and non-complete agreements	2,650
Deferred tax liability	(2,180)
Deferred stock compensation (See Note 8)	1,793
Excess of purchase price over identifiable net assets acquired	22,634
<b>Total</b>	<b>\$ 33,966</b>

The amounts allocated to current technology, assembled workforce and residual goodwill are being amortized using the straight-line method over their respective estimated useful lives, which range from three to six years.

The agreement with HiBand includes provisions for contingent cash payments of up to \$28.0 million through March 2004 based upon the achievement of established performance milestones and continued employment with Cypress. As such, this contingency will be accounted for as compensation for services and expensed in the appropriate periods.

#### Acquisition of International Microcircuits, Inc.

On February 23, 2001, Cypress completed its acquisition of International Microcircuits Inc. ("IMI"), a company specializing in timing technology integrated circuits. IMI's product portfolio includes programmable clocks, clock distribution products, electromagnetic interference suppression devices, and application-specific products. The acquisition was accounted for using the purchase method of accounting per APB Opinion No. 16. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of February 23, 2001, the effective date of the purchase. The results of operations are included in Cypress's consolidated results of operations as of and since the effective date of the purchase. There were no significant differences between the accounting policies of Cypress and IMI.

Cypress acquired IMI for total consideration of \$150.3 million, including \$111.2 million in cash, options for 1.3 million shares of Cypress common stock valued at \$32.8 million, notes payable to shareholders of \$3.3 million, and direct acquisition costs of \$3.0 million for investment banking, legal and accounting fees. The total purchase price was preliminarily allocated to the estimated fair value of assets acquired and liabilities assumed as follows:

(In thousands)

Fair value of tangible assets	\$ 14,847
Fair value of liabilities assumed	(11,517)
In-process research and development	4,850
Current technology	14,700
Assembled workforce and non-complete agreements	7,450
Other intangibles	7,550
Deferred tax liability	(11,880)
Deferred stock compensation (See Note 8)	19,087
Excess of purchase price over identifiable net assets acquired	105,179
<b>Total</b>	<b>\$ 150,266</b>

The amounts allocated to current technology, assembled workforce, other intangibles and residual goodwill are being amortized using the straight-line method over their respective estimated useful lives, which range from three to five years.

### Valuation Methodology – IMI, HiBand, ScanLogic, Lara, ISD and Silicon Packets

The valuation method used to value in-process technology is a form of discounted cash flow method commonly known as the “percentage of completion” approach. This approach is a widely recognized appraisal method and is commonly used to value technology assets. The value of the in-process technology is the sum of the discounted expected future cash flows attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets and the technological risk associated with completing the development of the technology. The cash flows derived from the in-process technology projects were discounted at a rate of 27% for IMI, 30% for HiBand, 25% for ScanLogic, 30% for Lara, 29% for ISD and 30% for Silicon Packets. Cypress believes these rates were appropriate given the risks associated with the technologies for which commercial feasibility had not been established. The percentage of completion for each in-process project was determined by identifying the elapsed time invested in the project as a ratio of the total time required to bring the project to technical and commercial feasibility. The percentage of completion for in-process projects acquired ranged from 10% to 90% for IMI, 5% to 75% for HiBand, 28% to 79% for ScanLogic, 1% to 89% for Lara, 10% to 70% for ISD and 9% to 87% for Silicon Packets. Schedules were based on management’s estimate of tasks completed and the tasks to be completed to bring the project to technical and commercial feasibility. As of December 30, 2001, the actual development timelines and costs are in line with management’s estimates.

The value of current technology was determined by estimating the future cash flows to be derived from products based on existing commercially feasible technologies at the date of the acquisition, and discounting associated cash flows using discount rates ranging from 20% to 27%. Cypress believes these rates were appropriate given the business risks inherent in manufacturing and marketing these products. Factors considered in estimating the discounted cash flows to be derived from the existing technology include risks related to the characteristics and applications of the technology, existing and future markets and an assessment of the age of the technology within its life span.

The value of non-compete agreements was based on the estimated loss of cash flow that would be suffered due to a loss of members of the workforce to a competitor in the absence of the non-compete agreements. The value of the assembled workforce was based on estimated costs to replace the existing staff, including recruiting, hiring and training costs for employees in all categories, and fully deploy a work force of similar size and skill to the same level of productivity as the existing work force.

Other intangibles include the value of an existing customer base, existing customer orders, existing trademarks and a facilities lease with below market rental rates. These intangible assets were valued using discount rates ranging from 15.0% to 28.5%.

Development of in-process technology remains a substantial risk to Cypress due to a variety of factors including the remaining effort to achieve technical feasibility, rapidly changing customer requirements and competitive threats from other companies and technologies. Additionally, the value of other intangible assets acquired may become impaired. The in-process research and development valuation, as well as the valuation of other intangible assets was prepared by management or an independent appraisal firm, based on input from Cypress and the acquired companies’ management, using valuation methods that are recognized by the United States SEC staff. However, there can be no assurance that the SEC staff will not take issue with assumptions used in the appraiser’s valuation model and require Cypress to revise the amount allocated to in-process research and development.



## Pro Forma Financial Information

Summarized below are the unaudited pro forma results of Cypress as though IMI, HiBand, ScanLogic, Lara, ISD and Silicon Packets had been acquired at the beginning of the periods indicated. Adjustments have been made for the estimated increases in amortization of intangibles, amortization of stock-based compensation and other appropriate pro forma adjustments. The charges for purchased in-process research and development are not included in the pro forma results, because they are non-recurring. The pro forma results do not include goodwill amortization for the Lara, ISD and Silicon Packets acquisitions. Pro forma results of operations are not included for fiscal 1999, as they are not materially different.

	Year Ended	
	December 30, 2001	December 31, 2000
(In thousands, except per share amount)		
Total revenue	\$ 842,634	\$ 1,402,617
Net income	\$ (478,647)	\$ 162,838
Net income (loss) per share:		
Basic	\$ (3.79)	\$ 1.35
Diluted	\$ (3.79)	\$ 1.19

The above amounts are based upon certain assumptions and estimates, which we believe are reasonable and do not reflect any benefit from economies of scale, which might be achieved from combined operations. The pro forma financial information presented above is not necessarily indicative of either the results of operations that would have occurred had the acquisitions taken place at the beginning of the periods indicated or of future results of operations of the combined companies.

## 2000 Acquisitions

### Acquisition of Silicon Light Machines

On August 30, 2000, Cypress acquired all of the outstanding capital stock of Silicon Light Machines (“SLM”) that Cypress did not previously own. SLM is a supplier of microelectromechanical systems (“MEMS”) technology applicable to fiber-optic networks and other applications. The acquisition was accounted for using purchase accounting. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress’s consolidated balance sheet as of August 30, 2000, the effective date of the purchase. There were no significant differences between the accounting policies of Cypress and SLM.

Cypress acquired SLM for a total consideration of \$164.0 million, including \$161.2 million in stock, an existing \$2.2 million investment, and direct acquisition costs of \$0.6 million for legal and accounting fees. The total purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed based on appraisals prepared by an independent appraisal firm using estimates and projections provided by management. The asset values estimates are as follows:

(In thousands)	
Fair value of tangible net assets	\$ 17,017
In-process research and development	30,400
Current technology	107,200
Assembled workforce and non-complete agreement	4,700
Deferred tax liability	(44,760)
Excess of purchase price over identifiable net assets acquired	49,456
<b>Total</b>	<b>\$ 164,013</b>

The valuation method used to value the in-process technology of SLM is a form of discounted cash flow method commonly known as the “percentage of completion” approach whereby the cash flow derived from the technology is multiplied by the percentage of completion of the in-process technology. This approach is a widely recognized appraisal method and is commonly used to value technology assets. The value of the in-process technology of SLM is the discounted expected future cash flow attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets, and the technological risk associated with completing the development of the technology. The cash flow derived from the in-process technology projects was discounted using a discount rate of 30.0%, which Cypress believes was appropriate for the risk of this technology for which commercial feasibility had not been established. The percentage of completion for each in-process project was determined by identifying the elapsed time invested in the project as a ratio of the total time required to complete the project to technical and commercial feasibility. Schedules were based on management’s estimate of tasks completed and the tasks to be completed to bring the project to technical and commercial feasibility. As of December 30, 2001, the actual development timelines and costs are in line with management’s estimates.

The value of current technology was determined by estimating the future cash flows to be derived from products based on existing commercially feasible technologies at the date of the acquisition, and discounting associated cash flow using discount rates of 10.0% and 27.0% (depending on the products), which Cypress believes was appropriate for the business risks inherent in manufacturing and marketing these products. Factors considered in estimating the future cash flow to be derived from the existing technology include risks related to the characteristics and applications of the technology, existing and future markets, and assessment of the age of the technology within its life span.

The value of the assembled workforce is based on estimated costs to replace the existing staff, including recruiting, hiring and training costs for employee in all categories, to fully deploy a work force of similar size and skill to the same level of productivity as the existing work force.

The amounts allocated to current technology, assembled workforce and residual goodwill are being amortized over their respective estimated useful lives of between four and seven years using the straight-line method.

Summarized below are the unaudited pro forma results of Cypress as though SLM had been acquired at January 4, 1999. Adjustments have been made for the estimated increases in amortization related to the purchased core technology, completed products, workforce, amortization of stock-based compensation and other appropriate pro forma adjustments.

(In thousands, except per share amount)	Year Ended	
	December 31, 2000	January 2, 2000
Total revenue	\$ 1,291,106	\$ 744,872
Net income	\$ 296,015	\$ 30,021
Net income (loss) per share:		
Basic	\$ 2.44	\$ 0.28
Diluted	\$ 2.44	\$ 0.26

The above amounts are based upon certain assumptions and estimates, which Cypress believes are reasonable and do not reflect any benefit from economies of scale, which might be achieved from combined operations. The pro forma financial information presented above is not necessarily indicative of either the results of operations that would have occurred had the acquisition taken place at the beginning of fiscal 1999 or of future results of operations of the combined companies. The charge for purchased in-process research and development has not been included in the pro forma results above because it is non-recurring and directly related to the acquisition.

### Acquisition of RadioCom Corporation

On June 29, 2000, Cypress acquired all of the outstanding capital stock of RadioCom Corporation ("RadioCom"). RadioCom specializes in the design and development of semiconductor radio frequency ("RF") integrated circuits. The acquisition was accounted for using purchase accounting. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of June 29, 2000, the effective date of the purchase. The results of operations of RadioCom from June 29, 2000 through Cypress's quarter ended July 2, 2000 were not significant and were therefore excluded from that quarter's reported results. There are no significant differences between the accounting policies of Cypress and RadioCom.

Cypress acquired RadioCom for a total consideration of \$10.2 million in stock. The total purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed based on appraisals prepared by management. The asset values estimates are as follows:

(In thousands)	
Fair value of tangible net assets	\$ 51
In-process research and development	2,025
Current technology	1,752
Assembled workforce	802
Excess of purchase price over identifiable net assets acquired	5,584
<b>Total</b>	<b>\$ 10,214</b>

The valuation method used to value the in-process technology of RadioCom is the "percentage of completion" approach. The value of the in-process technology of RadioCom is the discounted expected future cash flow attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets, and the technological risk associated with completing the development of the technology. The cash flow derived from the in-process technology projects was discounted using a discount rate of 20.0%, which Cypress believes was appropriate for the risk of this technology for which commercial feasibility had not been established. The percentage of completion for each in-pro-

cess project was determined by identifying milestones of completed project steps as compared to the remaining milestones to be completed to bring the project to technical and commercial feasibility. Milestones were based on management's estimate of tasks completed, value added and degree of difficulty of the portion of the project completed as of the acquisition date, in comparison with the tasks to be completed to bring the project to technical and commercial feasibility. As of December 30, 2001, the actual development timelines and costs are in line with management's estimates.

The value of current technology was determined by estimating the future cash flows to be derived from products based on existing commercially feasible technologies at the date of the acquisition, and discounting associated cash flow using a discount rate of 35.0%, which Cypress believes was appropriate for the business risks inherent in manufacturing and marketing these products. Factors considered in estimating the future cash flow to be derived from the existing technology include risks related to the characteristics and applications of the technology, existing and future markets, and assessment of the age of the technology within its life span.

The value of the assembled workforce is based on estimated costs to replace the existing staff, including recruiting, hiring and training costs for employees in all categories, to fully deploy a work force of similar size and skill to the same level of productivity as the existing work force.

The amounts allocated to current technology, assembled workforce and residual goodwill are being amortized over their respective estimated useful lives of between six and ten years using the straight-line method. During the third quarter of 2001, the useful life of current technology was reduced by four years to six years.

## 1999 Acquisitions

### Acquisition of Arcus Technology Companies

On June 30, 1999, Cypress acquired all of the outstanding capital stock of Arcus Technology (USA), Inc. and the assets of Arcus Technology (India) Limited (referred to as "Arcus" on a combined basis). Arcus specializes in data communications technologies including dense wave multiplexing (which allows multiple signals to be transmitted over a single fiber optic cable) and "IP over SONET" (the technology used to code and decode Internet traffic to send it over the telephone system). The acquisition was accounted for using purchase accounting. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of and since June 30, 1999, the effective date of the purchase. There are no significant differences between the accounting policies of Cypress and Arcus. The results of operations of Arcus are included in Cypress's consolidated results of operations during the second half of Cypress's fiscal year 1999.

Cypress acquired Arcus for a total consideration of \$17.7 million, including cash of \$11.5 million and stock of \$6.2 million. Through December 31, 2000 Cypress paid \$10.5 million in cash and issued \$6.2 million in stock. Cypress incurred a one-time charge of \$2.0 million in fiscal 2000 due to the acceleration of contractual obligation. The remaining \$1.0 million in cash will be paid as certain performance milestones are reached. The total purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed at the time of the acquisition based on independent appraisals and management estimates as follows:

(In thousands)

Fair value of tangible net assets	\$ 391
In-process research and development	2,500
Current technology	4,400
Assembled workforce	1,600
Deferred compensation	5,553
Excess of purchase price over identifiable net assets acquired	3,264
<b>Total</b>	<b>\$ 17,708</b>

The valuation method used to value the in-process technology of Arcus is the "percentage of completion" approach. The value of the in-process technology of Arcus is the discounted expected future cash flow attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets, and the technological risk associated with completing the development of the technology. The cash flow derived from the in-process technology projects was discounted using a discount rate of 32.5%, which Cypress believes was appropriate for the risk of this technology for which commercial feasibility had not been established. The percentage of completion for each in-process project was determined by identifying milestones of completed project steps as compared to the remaining milestones to be completed to bring the project to technical and commercial feasibility. Milestones were based on management's estimate of tasks completed, value added and degree of difficulty of the portion of the project completed as of the acquisition date, in comparison with the tasks to be completed to bring the project to technical and commercial feasibility. A deduction of 7.5% to 12.0% of expected future revenue was made in calculating future cash flows from in-process technology and attributed to previously existing technology.

The value of current technology was determined by estimating the future cash flows to be derived from products based on existing commercially feasible technologies at the date of the acquisition, and discounting associated cash flow using a discount rate of 25.0%, which Cypress believes was appropriate for the business risks inherent in manufacturing and marketing these products. Factors considered in estimating the future cash flow to be derived from the existing technology include risks related to the characteristics and applications of the technology, existing and future markets, and assessment of the age of the technology within its life span.

The value of the assembled workforce is based on estimated costs to replace the existing staff including recruiting, hiring and training costs for employees in all categories, to fully deploy a work force of similar size and skill to the same level of productivity as the existing work force. Deferred compensation value is the cash and stock consideration to be paid upon the future achievement of established performance milestones.

The amounts allocated to current technology, assembled workforce, and residual goodwill are being amortized over their respective estimated useful lives between six and ten years using the straight-line method. The deferred compensation is being amortized on a straight-line basis over the estimated timeframe required to achieve the performance milestones, which is two years. During the third quarter of 2001, the useful life of current technology was reduced by five years to five years.

### **Acquisition of Anchor Chips, Inc.**

On May 25, 1999, Cypress acquired all of the outstanding capital stock of Anchor Chips, Inc. ("Anchor"), a company that designs and markets microcontroller chips that support Universal Serial Bus applications. The acquisition was accounted for using purchase accounting. Accordingly, the estimated fair value of assets acquired and liabilities assumed were included in Cypress's consolidated balance sheet as of and since May 25, 1999, the effective date of the purchase. There are no significant differences between the accounting policies of Cypress and Anchor. The results of operations of Anchor were included in Cypress's consolidated results of operations as of and since the effective date of the purchase.

Cypress paid approximately \$15.0 million in cash. In addition, Cypress assumed net liabilities of approximately \$0.9 million. The total purchase consideration of \$15.9 million was allocated to the estimated fair value of assets acquired and liabilities assumed based on a valuation completed by management, as follows:

In thousands	
Fair value of tangible net liabilities	\$ (919)
In-process research and development	1,519
Assembled workforce	1,320
Current technology	13,036
<b>Total</b>	<b>\$ 14,956</b>

The valuation method used to value the in-process technology of Anchor is the "percentage of completion" approach. The value of the in-process technology of Anchor is the discounted expected future cash flow attributable to the in-process technology, taking into consideration the percentage of completion of products utilizing this technology, utilization of pre-existing technology, the risks related to the characteristics and applications of the technology, existing and future markets, and the technological risk associated with completing the development of the technology. The cash flow derived from the in-process technology projects was discounted using a discount rate of 32.5%, which Cypress believes was appropriate for the risk of this technology for which commercial feasibility had not been established. The percentage of completion for each in-process project was determined by identifying milestones of completed project steps as compared to the remaining milestones to be completed to bring the project to technical and commercial feasibility. Milestones were based on management's estimate of tasks completed, value added and degree of difficulty of the portion of the project completed as of the acquisition date, in comparison with the tasks to be completed to bring the project to technical and commercial feasibility. A deduction of 7.5% to 12.0% of expected future revenue was made in calculating future cash flows from in-process technology and attributed to previously existing technology. As of December 30, 2001, the actual development timelines and costs are in line with management's estimates.

The value of the assembled workforce is based on estimated costs to replace the existing staff including recruiting, hiring and training costs for employees in all categories, to fully deploy a work force of similar size and skill to the same level of productivity as the existing work force.

The value of current technology was determined by estimating the future cash flows to be derived from products based on existing commercially feasible technologies at the date of the acquisition, and discounting associated cash flow using a discount rate of 25.0%, which Cypress believes was appropriate for the business risks inherent in manufacturing and marketing these products. Factors considered in estimating the future cash flow to be derived from the existing technology include risks related to the characteristics and applications of the technology, existing and future markets, and assessment of the age of the technology within its life span.

The amounts allocated to current technology, and assembled workforce are being amortized over their estimated useful lives of five years using the straight-line method. There was no goodwill associated with the acquisition of Anchor.

Development of in-process technology remains a substantial risk to Cypress due to factors including the remaining effort to achieve technical feasibility, rapidly changing customer requirements and competitive threats from other companies and technologies. Additionally, the value of other intangible assets acquired may become impaired. The in-process research and development valuation as well as the valuation of other intangible assets was prepared by management or an independent appraisal firm, based on inputs from Cypress and the acquired company's management, utilizing valuation methods that are recognized by the SEC staff. However, there can be no assurance that the SEC staff will not take issue with assumptions used in the appraiser's valuation model and require Cypress to revise the amount allocated to in-process research and development.

Pro forma results of operations for Arcus, Anchor and RadioCom are not presented, as they are not materially different.

## Acquisition Costs

(In thousands)

	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Amortization of intangibles and merger-related cost	\$ 71,493	\$ 21,825	\$ 9,654
In-process research and development	23,200	32,425	4,019
<b>Total acquisition costs</b>	<b>\$ 94,693</b>	<b>\$ 54,250</b>	<b>\$ 13,673</b>

Acquisition costs are included in Acquisition and other non-recurring costs in the Consolidated Statement of Operations. Acquisition costs in fiscal 2001 consisted of amortization of intangibles related to acquisitions, as well as in-process research and development charges related to the acquisitions of IMI, HiBand, ScanLogic, Lara, ISD and Silicon Packets. However, in accordance with SFAS No. 141, goodwill recognized in the Lara, ISD and Silicon Packets acquisitions is not being amortized.

During fiscal 2000, Cypress recorded acquisition and merger-related costs of \$54.2 million. In-process research and development costs were \$32.4 million. Amortization of intangible assets relating to current and prior year acquisitions totaled \$18.4 million. Transaction costs of \$3.4 million, which consist primarily of non-cash deferred compensation charges, legal, accounting and investment banking fees, were expensed during the fiscal year.

Acquisition-related costs incurred during fiscal 1999 were \$13.7 million. In the first quarter of fiscal 1999, Cypress recorded one-time charges of \$3.8 million associated with the merger with IC Works. These charges were for investment banking fees and other professional fees. Cypress also recorded \$8.8 million in costs associated with the purchase of Anchor and Arcus consisting of \$4.0 million for in-process technology, \$1.6 million for transaction costs and \$3.2 million in amortization of intangible assets. During the fourth quarter of fiscal 1999, Cypress acquired Altera's MAX 5000 Programmable Logic Device product line and its equity interest in Cypress's wafer fabrication facility in Round Rock, Texas. As part of the transaction, Cypress recorded intangible assets associated with the product rights and recorded \$0.3 million for the amortization of these intangibles. Transaction costs and non-cash compensation costs incurred for other acquisitions were \$0.8 million.

## Note 4: Mergers Using Pooling of Interests

### Merger with Alation Systems, Incorporated

On May 24, 2000, Cypress completed a merger with Alation Systems, Inc. ("Alation"), which was accounted for as a pooling of interests. Cypress issued 0.5 million shares of its common stock plus options in exchange for all outstanding stock and options of Alation. These consolidated financial statements and the notes to the consolidated financial statements give effect to the merger for all periods presented. The fiscal years of Cypress and Alation were different, and Alation has changed its fiscal periods to coincide with that of Cypress. Cypress's consolidated balance sheets as of January 2, 2000 and January 3, 1999 have been combined with Alation's consolidated balance sheets as of December 31, 1999 and December 31, 1998, respectively. For the purpose of the consolidated statements of operations for the periods ended January 2, 2000 and January 3, 1999, Cypress's statements of operations have been combined with Alation's statements of operations for the periods ended December 31, 1999 and December 31, 1998 respectively.

During the quarter ended July 2, 2000, Cypress recorded merger-related costs of \$1.4 million related to the acquisition of Alation. These charges, which consist primarily of non-cash deferred compensation charges, legal, and accounting, have been included under acquisition and other non-recurring costs in the consolidated statements of operations.



## Merger with Galvantech Incorporated

On March 2, 2000, Cypress completed a merger with Galvantech, Inc. and its subsidiaries (“Galvantech”), which was accounted for as a pooling of interests. Cypress issued 3.0 million shares of common stock plus options in exchange for all outstanding stock and options of Galvantech. These consolidated financial statements and the notes to the consolidated financial statements give effect to the merger for all periods presented. The fiscal years of Cypress and Galvantech were different, and Galvantech has changed its fiscal periods to coincide with that of Cypress. Cypress’s consolidated balance sheets as of April 2, 2000 and January 2, 2000 have been combined with Galvantech’s consolidated balance sheets as of April 2, 2000 and December 31, 1999 respectively. For the purpose of the consolidated statements of operations for the periods ended April 2, 2000 and April 4, 1999, Cypress’s statements of operations have been combined with Galvantech’s statements of operations for the three-month periods ended April 2, 2000 and March 31, 1999, respectively. As a result of combining Cypress’s and Galvantech’s financial statements for the fiscal years ended January 2, 2000 and January 3, 1999, the results of operations of Galvantech for the quarter ended March 31, 1999 were included in the consolidated statements of operations of both 1998 and 1999. Therefore, the balance sheet and cash and cash equivalents for the quarter ended December 31, 1998 and March 31, 1999 are the same.

During the quarter ended April 2, 2000, Cypress recorded merger-related costs of \$1.8 million related to the acquisition of Galvantech. These charges, which consist primarily of legal, accounting and investment banking fees, have been included under acquisition and other non-recurring costs in the consolidated statements of operations.

## Combined Financial Statements of Cypress with Merged Companies

The results of operations previously reported by the separate companies prior to the mergers and included in the results of operations for the fiscal year ended January 2, 2000 is presented below.

(In thousands)

Year ended January 2, 2000	Cypress	Galvantech	Alation	Total
Revenue	\$ 705,487	\$ 39,316	\$ 239	\$ 745,042
Net income (loss)	\$ 91,054	\$ 908	\$ (3,832)	\$ 88,130

## Note 5: Other Business Transactions

### Sale of FCT Business

On February 25, 2000, Cypress sold its Fast CMOS Technology (“FCT”) business including inventories, product software, all technical data, and a license for the related intellectual property. Total proceeds from the sale were \$7.5 million and Cypress recorded a gain of \$5.0 million from the sale. In conjunction with this sale, Cypress entered into a supply agreement for the related existing inventories and future requirements, based on historical run rates. Cypress completed its obligations under the supply agreement during the fourth quarter of fiscal 2000. Revenues from FCT products were approximately 1% of 1999 revenues.

### Acquisition from Altera

On October 5, 1999, Cypress announced that it had signed a definitive agreement with Altera Corporation (“Altera”) to acquire Altera’s MAX 5000 Programmable Logic Device (“PLD”) product line and its equity interest in Cypress’s wafer fabrication facility in Round Rock, Texas (“Fab 2”) for approximately \$13.0 million in cash. In 1988, Altera had licensed its MAX 5000 family of products to Cypress in consideration for manufacturing capacity. Altera later acquired a 17% equity interest in the Round Rock wafer fabrication facility. By acquiring Altera’s equity interest in October 1999, Fab 2 is now 100% owned by Cypress.

## Note 6: Restructuring Costs

On July 16, 2001, Cypress announced a restructuring plan that involved resizing its manufacturing facilities, reducing its workforce, and combining facilities. The restructuring was precipitated by the worldwide economic slowdown, particularly in the business areas in which Cypress operates. The effect of the plan was to size the manufacturing operations and facilities to meet future demand and reduce expenses in all operations areas. During the third quarter of 2001, Cypress recorded restructuring charges of \$132.1 million related to property, plant and equipment, leased facilities and personnel.

The following table summarizes the restructuring reserve and charges for the year ended December 30, 2001.

(In thousands)

	<b>Provision</b>	<b>Non-Cash Charges</b>	<b>Cash Charges</b>	<b>Reserves And Write-Downs at 12/30/2001</b>
Property, plant and equipment	\$ 113,350	\$ 7,269	\$ 1,619	\$ 104,462
Leased facilities	4,079	—	213	3,866
Personnel	14,684	9,056	4,243	1,385
<b>Total</b>	<b>\$ 132,113</b>	<b>\$ 16,325</b>	<b>\$ 6,075</b>	<b>\$ 109,713</b>

## Property, Plant and Equipment

Restructuring costs related to property, plant and equipment amounted to \$113.4 million. In sizing Cypress to meet future demand, Cypress has taken out of service and is holding for sale manufacturing assets with a net book value of \$122.1 million (and a gross book value of \$168.0 million). The charge represents the difference between the net book value of the assets less the estimated amount to be realized upon sale of the equipment, net of the estimated cost to dispose of the equipment. This amount has been recorded as a reduction in the carrying amount of the assets. The restructuring affects Cypress's facilities in Minnesota, Texas, California and the Philippines. Fixed asset sales and/or dispositions are expected to be completed within one year. In each case, the asset was removed from service prior to September 30, 2001.

## Leased Facilities

For fiscal 2001, Cypress incurred a \$4.1 million restructuring charge for three excess leased facilities. The estimated costs to terminate or sublease these facilities are estimated to be approximately \$4.1 million, which is included in other current liabilities. This estimate is based on current comparable rates for leases in the respective markets. Should facilities rental rates continue to decrease in these markets or should it take longer than expected to sublease these facilities, the actual loss could exceed this estimate. Costs will be incurred over the remaining terms of the leases, the longest of which is three years.

## Personnel

Cypress implemented a reduction in force that affected employees at all significant locations. Under the program Cypress announced in July 2001 that it would terminate the employment of several hundred people. Those individuals were notified in July that their employment would cease on September 30, 2001. Cypress has terminated the employment of 714 people, which was approximately 15% of the workforce, of whom 709 employees had left Cypress as of December 30, 2001. The remainder will leave during the next six months after the completion of certain projects in which they are involved.

Personnel costs related to the reduction in force amounted to \$14.7 million. Severance and related employee benefit costs amounted to \$5.8 million. For those people whose employment ended on September 30, 2001, severance costs were paid at that time. For people leaving subsequent to September 30, 2001, severance costs will be paid at the time of their separation. In addition, effective August 14, 2001, the Cypress Board of Directors made a one-time decision to extend for those terminated employees the option exercise period from one month to twelve months after termination. Cypress recorded non-cash stock compensation expense of \$8.9 million for this modification during the quarter ended September 30, 2001.

## Restructuring Credits

During fiscal 2000, Cypress reversed \$0.5 million of previously provided restructuring costs related to the decision to close down the wafer fab located in San Jose, California. During fiscal 1999, Cypress recorded restructuring credits of \$3.8 million, which included a reversal of \$3.1 million of the 1998 restructuring reserve. The reversed charges of \$2.5 million primarily related to excess accruals for severance and other employee related charges. Cypress also reversed \$0.6 million of the 1998 restructuring reserve for excess fixed asset write-downs from the 1998 restructuring. In addition, during fiscal 1999, Cypress reversed \$0.7 million of excess fixed asset write-downs of the 1996 restructuring.

## Note 7: Provisions for Inventory and Other Charges

### 2001 Provision for Inventory

Cypress recorded an unusual provision of \$93.1 million to cost of sales during the quarter ended September 30, 2001 for excess inventory and related purchase commitments, which Cypress did not expect to sell. The excess was a result of the continuing decline in revenue, greater uncertainty with respect to the timing of the recovery, which then appeared later than previously anticipated and the slower rate of expected recovery.

## **2001 Impairment of Intangibles and Long-lived Asset Review**

During the third quarter of 2001, Cypress reviewed the carrying values and remaining useful lives of its long-lived assets, particularly the intangible assets acquired in recent years. Based on this review, the remaining useful lives on certain intangible assets were reduced and an impairment loss of \$65.9 million related to the SLM subsidiary was recorded during fiscal 2001.

During 2001, the optical market in which SLM participates experienced a severe economic downturn. Reduced demand for SLM's products places increased risk on the future revenue streams anticipated from the existing display and monitor technology. For these reasons, Cypress then reviewed SLM's long-lived assets for impairment and recognized an impairment loss totaling \$65.9 million, the amount by which the carrying value of the acquired existing technology and a pro-rata portion of the related goodwill exceeded the present value of the estimated future cash flows of the existing technology of SLM. Goodwill was impaired \$29.1 million, and existing technology was impaired \$36.8 million. This impairment loss is reported on the consolidated statements of operations under the caption acquisition and other non-recurring costs, net.

The remaining useful lives on intangible assets were reviewed in light of current product offerings, discounted projected revenue streams, competitive environments and other business factors. Based on this review, the acquired intangibles and other long-lived assets continue to be fairly stated; however, the remaining useful lives of several assets were reduced. The useful life of assembled workforce acquired with RadioCom was reduced by two years to four years. The useful lives of the existing technology and goodwill acquired with RadioCom were reduced by four years to six years. The useful life of the assembled workforce acquired with Arcus was reduced by three years to three years. The useful lives of existing technology and goodwill acquired with Arcus were reduced by five years to five years. The effect of these changes was to increase amortization by \$1.0 million in fiscal 2001. Amortization will decrease by approximately \$1 million annually thereafter as goodwill and assembled workforce will no longer be amortized in accordance with SFAS Nos. 141 and 142.

## **2001 Other Long-term Investments, Property, Plant and Equipment and Certain Settlements**

Other one-time charges of \$20.7 million included in the fiscal 2001 results were related to the write-down of investments and property, plant and equipment and the settlement of two intellectual property-related disputes.

Cypress recorded a one-time charge to reduce the carrying value of two long-term investments including startup, development stage and technology companies to their estimated net realizable values. These investments were reduced by \$1.5 million and \$7.4 million to \$1.5 million and \$4.2 million, respectively. The charge of \$8.9 million is reported on the consolidated statements of operations in other income and (expense), net.

Property, plant and equipment with a net book value of \$5.6 million were also written off to operating expenses as one-time charges as a result of a periodic physical count of property, plant and equipment completed during the third quarter of fiscal 2001.

During the third quarter, Cypress recorded charges of \$8.7 million on the resolution of two disputes including an agreement in principle to settle a patent infringement suit for \$8.0 million, of which \$5.5 million pertained to prior periods and was included in the consolidated statements of operations with research and development costs. The remaining \$2.5 million relates to future product shipments and has been recorded as a prepaid asset and will be expensed over the next three years (see Note 15 for additional information).

## **2000 Other Non-Recurring Costs**

Cypress incurred a one-time charge of \$2.0 million due to the acceleration of contractual obligations related to the Arcus acquisition.

## **1999 Other Non-Recurring Costs**

During fiscal 1999, Cypress recorded \$24.2 million in other non-recurring costs. One-time, non-recurring costs included a \$12.3 million write-off of a manufacturing asset that was not being used and was subsequently scrapped and an \$11.9 million one-time compensation charge associated with retention and performance payments to key employees in December 1999.

## **Note 8: Equity and Debt Transactions**

At December 30, 2001, Cypress had outstanding a series of equity options (on Cypress common stock) in the amount of \$26.0 million. The options require physical settlement and expire in March and June 2002. Upon expiration of the options, if Cypress's stock price is above the trigger price, Cypress will have its capital returned with a premium. If below the trigger price, Cypress will receive a specified number of shares of Cypress common stock instead of a return of capital. The range of the trigger prices is \$20.60 - \$23.42. The transaction is recorded in stockholders' equity in the accompanying consolidated balance sheet.

In 2000 and 2001, the Board of Directors of Cypress authorized the repurchase of 15.0 million shares of Cypress's outstanding common stock and sell put options for 2.5 million shares. During fiscal 2001, Cypress repurchased 9.5 million shares at an average cost of \$19.98 per share, bringing the total repurchases through December 30, 2001 to 15.8 million shares at an average cost of \$21.14 per share. In fiscal 2001, Cypress sold put warrants through private placements for which Cypress received premiums of \$10.6 million, bringing the total premiums received under the program to \$16.9 million. As of December 30, 2001, Cypress had a maximum potential obligation to purchase 0.3 million shares of its common stock at an aggregate price of \$3.6 million. The puts expire in April 2002. Cypress has the right to settle the put warrants with cash or settle with shares of Cypress's common stock. The transaction is recorded in stockholders' equity in the accompanying consolidated balance sheet.

On January 31, 2000, Cypress filed a registration statement on Form S-3 with the SEC. Under this shelf registration statement, which was effective February 8, 2000, as amended by a post-effective amendment thereto effective March 7, 2000, Cypress can, through January 2002, sell any combination of debt securities, preferred stock and common stock in one or more offerings up to a total amount of \$400.0 million. The shelf registration statement allows Cypress flexibility to raise funds from the offering of debt securities, common stock, preferred stock or a combination thereof, subject to market conditions and Cypress's capital needs. At December 30, 2001, the balance remaining related to the shelf registration statement was \$112.5 million.

Cypress recorded provisions for deferred stock compensation related to acquisitions and certain other grants of approximately \$76.8 million, \$15.1 million and \$1.7 million in fiscal years ended December 30, 2001, December 31, 2000 and January 2, 2000, respectively. These amounts are being amortized over the vesting period of the individual stock options or stock, generally a period of four to five years. Deferred stock compensation expense totaled approximately \$42.0 million, \$6.6 million and \$1.8 million in fiscal years 2001, 2000 and 1999, respectively.

In March 1999, Cypress announced a program whereby all U.S. employees were offered loans to facilitate the exercise of vested stock options. Under the terms of the program, only options which were vested as of March 1, 1999 and whose exercise price was less than or equal to \$9.75 could qualify for a loan. The loans, including interest, are due at the earlier of three days following the sale of the shares, within thirty days of the date the individual ceases to be an employee of Cypress or 3 years from the grant date of the loan. The loans bear interest and are secured by our common shares. At December 30, 2001, loans receivable and accrued interest under this program totaled \$0.8 million. Amounts receivable under subsidiary loan programs were \$0.4 million at December 30, 2001.

### **Convertible Subordinated Notes**

During 2001, the Board of Directors authorized the repurchase from time to time of up to \$143.8 million of 3.75% Convertible Subordinated Notes (3.75% Notes"). In the fourth quarter of 2001, Cypress retired a total of \$52.8 million principal of its \$287.5 million notes, for \$44.6 million, resulting in a pre-tax net gain of \$7.2 million. The gain was net of the write-off of bond issuance costs of \$1.0 million (pre-tax). The net after-tax gain was recorded as an extraordinary item in our consolidated statement of operations.

On September 7, 2000, Cypress called for the redemption of all its 6.0% Convertible Subordinated Notes ("6.0% Notes") due in 2002. The aggregate amount of principal outstanding at the time of the call was approximately \$160 million. Holders of the 6.0% Notes could convert their 6.0% Notes into shares of Cypress's common stock at a conversion rate of approximately 42.33 shares of stock per \$1,000 principal amount of the 6.0% Notes. Substantially all of the 6.0% Notes were converted prior to the redemption deadline of October 2, 2000 increasing the amount of common stock outstanding by 6.8 million shares.

On June 26, 2000, Cypress completed a \$287.5 million registered-placement of 5-year convertible subordinated notes. The notes are due in 2005, with a coupon rate of 3.75% and an initial conversion premium of 27.0%. The notes are convertible into approximately 4.6 million shares of common stock and are callable by Cypress no earlier than July 5, 2003. Net proceeds were \$279.6 million, after issuance costs of \$7.9 million.

On January 19, 2000, Cypress completed a \$283.0 million registered-placement of 5-year convertible subordinated notes. The notes are due in 2005, with a coupon rate of 4.00% and an initial conversion premium of 28.5%. The notes are convertible into approximately 6.1 million shares of common stock and are callable by Cypress no earlier than February 5, 2003. Net proceeds were \$275.2 million, after issuance costs of \$7.8 million.

In 1998, Cypress retired a total of \$15.0 million principal of its \$175.0 million, 6.0% Notes for \$12.9 million, resulting in a pre-tax net gain of \$1.7 million. The gain was offset by the write-off of bond issuance costs of \$0.4 million (pre-tax). The net gain was recorded as interest income and other. The 6.0% Notes were called on October 2, 2000.

## Customer Advances and Other Liabilities

As of December 30, 2001 Cypress has recorded \$65.1 million in customer advances, of which \$30.5 million is recorded in Other current liabilities and \$34.6 million is recorded in Other long-term liabilities. The customer advance is related to a financing and supply agreement into which Cypress entered with a specific customer in October 2000. The agreement called for the customer to provide funding to Cypress for the purpose of purchasing equipment and increasing fabrication capacity in order to supply product at future dates according to the supply agreement. The customer maintains a security interest in the equipment purchased. The supply agreement calls for Cypress to make available to the customer a minimum quantity of wafers each year from 2001 through 2003.

In June 1997, Cypress borrowed 700 million yen at 2.1% from Sumitomo Bank - Japan in order to set up and fund our Japanese business operations. Borrowing under this arrangement, which aggregated \$5.8 million at December 30, 2001, is due in fiscal 2003.

## Note 9: Foreign Currency Derivatives

Cypress has foreign subsidiaries that operate and sell Cypress's products in various global markets. As a result, Cypress is exposed to risks associated with changes in foreign currency exchange rates. At any point in time, Cypress might use various hedge instruments, primarily forward contracts, to manage the exposures associated with forecasted purchases of equipment, and net asset or liability positions. Cypress does not enter into derivative financial instruments for speculative or trading purposes.

On January 1, 2001, Cypress adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. SFAS No. 133 requires that all derivatives be recorded at fair value. The adoption of SFAS No. 133 did not have a material effect on Cypress's financial condition or results of operations. Cypress estimates the fair value of its forward contracts based on changes in forward rates from published sources.

Under SFAS No. 133, Cypress accounts for its hedges of committed purchases of equipment as cash flow hedges, such that changes in fair value for the effective portion of hedge contracts, if material, are recorded in other comprehensive income in stockholders' equity. Amounts deferred in other comprehensive income will be recorded in the statement of operations in the period in which the underlying transactions impact earnings, and are not material at December 30, 2001. As of December 30, 2001, such forward contracts for Euro exposures had an aggregate notional value of \$15.8 million.

Cypress records its hedges of foreign currency denominated assets and liabilities at fair value with the related gains or losses recorded in other income. The gains and losses on these contracts are substantially offset by transaction losses and gains on the underlying balances being hedged. As of December 30, 2001, Cypress held forward contracts with an aggregate notional value of \$9.2 million to hedge the risks associated with Yen foreign currency denominated assets and liabilities. Aggregate foreign exchange gains and (losses) on these hedging transactions and foreign currency remeasurement gains and (losses) of \$0.3 million, \$1.6 million and \$(0.2) million are included in other income and (expense), net during fiscal 2001, 2000 and 1999, respectively.

## Note 10: Comprehensive Income

The components of comprehensive income (loss), net of tax, are as follows:

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Net income (loss)	\$ (407,412)	\$ 277,308	\$ 88,130
Other comprehensive income:			
Change in net unrealized gains on investments, net of tax of \$1,814	2,722	—	—
<b>Total</b>	<b>\$ (404,690)</b>	<b>\$ 277,308</b>	<b>\$ 88,130</b>

## Note 11: Employee Stock Purchase Assistance Plan

On May 3, 2001, Cypress stockholders approved the adoption of the 2001 Employee Stock Purchase Assistance Plan. The Plan allowed for loans to employees to purchase shares of Cypress common stock on the open market. Employees of Cypress and its subsidiaries, including executive officers of Cypress, were allowed to participate in the Plan. Each loan was evidenced by a full recourse, promissory note executed by the employee in favor of Cypress and was secured by all of the employee's assets, as well as a pledge of the shares of common stock purchased with the proceeds of the loan. If a participant sells the shares of Cypress common stock purchased with the proceeds of the loan, the proceeds of the sale must first be used to repay the principal and interest on the loan before being received by the employee. The loans are callable and bear interest at a rate at the applicable federal rate under Section 1274 of the Internal Revenue Code for long-term loans, compounded



annually. As the loans are at rates below the rate at which a stock broker would charge, Cypress has recorded \$1.7 million of compensation expense which is based on the difference between the applicable federal rate and an estimated market rate for each employee. In addition, Cypress is recording interest income on the outstanding loan balances. The Plan became effective on May 3, 2001 and will terminate on the earlier of May 3, 2011, or such time as determined by the Board of Directors. As of December 30, 2001 loans outstanding under the Plan were \$117.2 million, and this amount is classified on the consolidated balance sheet as other current assets. Cypress has created a reserve with a charge to operating expenses for estimated uncollectible balances.

## Note 12: Earnings (Loss) Per Share

As required by SFAS 128, following is a reconciliation of the numerators and the denominators of the basic and diluted earnings (loss) per share computation:

(In thousands, except per-share amounts)

	2001			2000			1999		
	(Loss)	Shares	Per-Share Amount	Income	Shares	Per-Share Amount	Income	Shares	Per-Share Amount
Net income (loss) before extraordinary gain	\$ (411,757)	124,135	\$ (3.32)	\$ 277,308	121,126	\$ 2.29	\$ 88,130	108,156	\$ 0.81
Extraordinary gain (net of tax of \$2,896)	4,345	—	0.04	—	—	—	—	—	—
Basic EPS:									
Net income (loss)	\$ (407,412)	124,135	<u>\$ (3.28)</u>	\$ 277,308	121,126	<u>\$ 2.29</u>	\$ 88,130	108,156	<u>\$ 0.81</u>
Effects of dilutive securities:									
6.0% Convertible notes	—	—		4,800	5,079		—	—	
4.0% Convertible notes	—	—		6,848	5,749		—	—	
3.75% Convertible notes	—	—		3,361	2,387		—	—	
7.0% Convertible notes	—	—		6	16		—	—	
Options	—	—		—	9,871		—	7,371	
Diluted EPS:									
Net income (loss)	<u>\$ (407,412)</u>	<u>124,135</u>	<u>\$ (3.28)</u>	<u>\$ 292,323</u>	<u>144,228</u>	<u>\$ 2.03</u>	<u>\$ 88,130</u>	<u>115,527</u>	<u>\$ 0.76</u>

For the years ended December 30, 2001, December 31, 2000 and January 2, 2000 options to purchase 8,738,000, 6,278,000 and 47,000 shares, respectively, of common stock were outstanding, but were excluded from the computation of diluted EPS, as their effect was anti-dilutive. Convertible debentures outstanding at December 30, 2001 and January 2, 2000 were convertible to 9,871,000 and 6,772,000 shares, respectively, of common stock but were also excluded from diluted EPS, as their effect was anti-dilutive.

## Note 13: Common Stock Option and Other Employee Benefit Plans

### Cypress Stock Option Plans

Cypress has two stock option plans: the 1999 Stock Option Plan and the 1994 Stock Option Plan.

In 1999, Cypress adopted the 1999 Non-Qualified Stock Option Plan. Under the terms of the 1999 Stock Option Plan, which is a non-shareholder approved plan, options may be granted to qualified employees, including those of acquired companies and consultants of Cypress or its majority-owned subsidiaries, but options may not be granted to Officers. Options become exercisable over a vesting period as determined by the Board of Directors and expire over terms not exceeding ten years from the date of grant. The plan allows for the granting of options at exercise prices less than fair market value of the common stock at grant date.

In 1994, Cypress adopted the 1994 Stock Option Plan, which replaced Cypress's 1985 Incentive Stock Option Plan and the 1988 Directors' Stock Option Plan (the "Terminated Plans") with respect to future option grants. Under the terms of the 1994 Stock Option Plan, options may be granted to qualified employees, consultants, officers and directors of Cypress or its majority-owned subsidiaries. Options become exercisable over a vesting period as determined by the Board of Directors and expire over terms not exceeding ten years from the date of grant. The option price for shares granted, under the 1994 Stock Option Plan, is equal to the fair market value of the common stock at the date of grant. The 1994 Stock Option Plan provides for an annual increase in shares available for issuance equal to 4.5% of Cypress's outstanding common stock at the end of each fiscal year.

In March 2001, Cypress employees were offered the opportunity to exchange stock options for a promise to receive new options six months and one day after the cancellation of the forfeited options. The new options were granted on October 8, 2001 with an exercise price equal to the New York Stock Exchange closing price on the same day. Any remaining grant issued prior to April 4, 2000 was eligible for this program. The new

options were issued with 12 months vested. The balance will vest 1/48<sup>th</sup> per month regardless of how many options were vested at the time of the cancellation election. Employees canceled 4,563,800 options with exercise prices between \$16.73 and \$54.19 per share.

In December 2000, Cypress employees were offered the opportunity to exchange their stock options for a promise to receive new options six months and one day after the cancellation of the forfeited options. The new options were granted on June 13, 2000 with an exercise price equal to the NYSE closing price on the same day. Any remaining grant issued prior to December 11, 2000 was eligible for this program. The new options were issued with 12 months vested. The balance will vest 1/48<sup>th</sup> per month regardless of how many options were vested at the time of the cancellation election. Employees canceled 3,701,080 options with exercise prices between \$20.90 and \$54.20 per share.

### Shares Under Cypress Stock Option Plans

The following table summarizes Cypress's stock option activity and related weighted average exercise price for each category for the years ended December 30, 2001, December 31, 2000, and January 2, 2000.

(In thousands, except per-share amounts)

	2001		2000		1999	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options outstanding, beginning of year	24,382	\$ 16.93	25,712	\$ 11.40	26,810	\$ 8.25
Options forfeited	(6,141)	27.80	(5,818)	32.51	(2,061)	9.81
Options granted	21,117	16.29	10,415	39.42	8,776	17.27
Options exercised	(2,412)	7.62	(5,927)	8.25	(7,813)	7.57
Options outstanding, end of year	<u>36,946</u>	15.08	<u>24,382</u>	16.93	<u>25,712</u>	11.40
Options exercisable at December 30, 2001	<u>13,584</u>	\$ 12.96	<u>9,134</u>	\$ 10.90	<u>9,692</u>	\$ 8.49

Cypress has, in connection with the acquisitions of various companies, assumed the stock option plans of each acquired company. During fiscal 2001 and 2000, respectively, a total of approximately 2.9 million and 0.6 million shares of Cypress's common stock have been reserved for issuance under the assumed plans and the related options are included in the preceding table. At December 30, 2001, stock options available for grant were 0.4 million. The increase in options available for grant was 13.1 million under all option plans during fiscal 2001.

The weighted average estimated fair value at the date of grant, as defined by SFAS No. 123, for options granted in 2001, 2000, and 1999 was \$19.33, \$33.17 and \$8.96 per option, respectively. The estimated grant date fair value is calculated using the Black-Scholes model. The Black-Scholes model, as well as other currently accepted option valuation models, was developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differ from Cypress's stock option awards. These models also require highly subjective assumptions, including future stock price volatility and expected time until exercise, which greatly affect the calculated grant date fair value.

The following weighted average assumptions were used in the estimated grant date fair value calculations for Cypress's stock option awards:

	2001	2000	1999
Expected life	5 years	5 years	7 years
Risk-free interest rate	4.46%	5.54%	5.76%
Volatility	0.6219	1.7701	0.5668
Dividend yield	0.00%	0.00%	0.00%

Significant option groups outstanding as of December 30, 2001 and the related weighted average exercise price and contractual life information, are as follows:

(In thousands, except per-share amounts)

Range of Option Exercise Prices	Outstanding		Exercisable		
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Remaining Life (years)
\$ 0.01 — \$ 5.91	5,159	\$ 4.13	1,437	\$ 3.35	7.87
\$ 6.81 — \$ 8.75	3,799	8.38	2,767	8.43	6.21
\$ 8.94 — \$ 9.75	4,398	9.93	3,772	9.92	5.45
\$ 9.86 — \$16.73	4,077	14.12	1,251	12.93	6.72
\$16.84 — \$16.84	8,084	16.84	1,389	16.84	9.77
\$17.56 — \$22.81	4,406	21.39	1,432	21.56	8.14
\$22.90 — \$23.82	5,278	23.61	1,184	23.72	9.37
\$24.07 — \$54.19	<u>1,745</u>	<u>31.14</u>	<u>352</u>	<u>34.20</u>	<u>8.99</u>
<u>\$ 0.01 — \$54.19</u>	<u>36,946</u>	<u>\$15.08</u>	<u>13,584</u>	<u>\$12.96</u>	<u>8.00</u>

### Subsidiary Stock Option Plans

In 2001, Cypress's Silicon Magnetic Systems ("SMS") and Silicon Light Machines ("SLM") subsidiaries each adopted a stock option plan. SMS made available for grant 25 million shares under the terms of its plan. SLM made available for grant 11 million shares under the terms of its plan. The plans allow the subsidiaries to grant options to qualified employees and consultants. Options become exercisable over a five year period and expire over terms not exceeding ten years from the date of grant. The exercise price for options granted under the plans have been the estimated fair value of each subsidiary's common stock at the date of grant.

The following table summarizes SMS and SLM stock option activity and related weighted average exercise price for each category for the year ended December 30, 2001.

(In thousands, except per-share amounts)

	SMS		SLM	
	Shares	Exercise Price	Shares	Exercise Price
Options outstanding, beginning of year	—	NA	—	NA
Options canceled	—	NA	—	NA
Options granted	19,550	\$ 0.058	3,263	\$ 0.65
Options exercised	—	NA	—	NA
Options outstanding, end of year	<u>19,550</u>	\$ 0.058	<u>3,263</u>	\$ 0.65
Options exercisable at December 30, 2001	<u>—</u>	NA	<u>—</u>	NA

### Subsidiary Restricted Stock Purchase Plan

Cypress Microsystems, Inc. ("CMS") 1999 Stock Purchase Plans allows eligible employees of CMS, a subsidiary of Cypress, to purchase restricted CMS stock. This stock has a vesting period of five years. Of the 15,500,000 shares authorized under the plan, 15,077,100 shares were issued through fiscal 2001. The purchase price of the restricted shares has a range of \$0.01 to \$0.02 per share, which equals the estimated grant date fair value.

### Employee Qualified Stock Purchase Plan

In 1998, Cypress amended and re-stated its Employee Qualified Stock Purchase Plan ("ESPP"), the plan allows eligible employees of Cypress and its subsidiaries to purchase shares of Cypress common stock through payroll deductions. The ESPP consists of consecutive 24-month offering periods composed of four 6-month exercise periods. The shares can be purchased at the lower of 85% of the fair market value of the common stock at the date of commencement of this two-year offering period or at the last day of each 6-month exercise period. Purchases are limited to 10% of an employee's eligible compensation, subject to a maximum annual employee contribution limited to a \$25,000 market value. Of the 13,030,746 shares authorized under the ESPP, 9,434,000 shares were issued through 2001 including 801,000 in 2001, 1,314,000 in 2000, and 953,000 in 1999. The plan provides for an annual increase in shares available for issuance equal to 2.5% of the number of outstanding Cypress common stock on the last day of the fiscal year.

The following weighted average assumptions are included in the estimated grant date fair value calculations for rights to purchase stock under the ESPP:

	2001	2000	1999
Expected life	6 months	6 months	6 months
Risk-free interest rate	3.77%	5.99%	5.94%
Volatility	0.7755	2.5507	0.5773
Dividend yield	0.00%	0.00%	0.00%

The weighted average estimated grant date fair value, as defined by SFAS No. 123, for rights to purchase stock under the ESPP granted in 2001, 2000 and 1999 were \$15.95, \$27.31 and \$7.50 per share, respectively.

### Pro Forma Net Income (Loss) and Net Income (Loss) Per Share

If Cypress had recorded compensation costs based on the estimated grant date fair value, as defined by SFAS No. 123, for awards granted under its stock option plans and its Employee Stock Purchase Plan, Cypress's pro forma net income (loss) and earnings per share for the years ended would have been as follows:

(In thousands, except per-share amounts)

	2001	2000	1999
Pro forma net income (loss):			
Basic	\$ (517,101)	\$ 202,242	\$ 55,424
Diluted	\$ (517,101)	\$ 217,256	\$ 55,424
Pro forma net income (loss) per share:			
Basic	\$ (4.17)	\$ 1.67	\$ 0.51
Diluted	\$ (4.17)	\$ 1.51	\$ 0.48

### Other Employee Benefit Plans

Cypress maintains a Section 401(k) Plan, New Product Bonus Plan, Key Employee Bonus Plan and Deferred Compensation Plan. The 401(k) Plan provides participating employees with an opportunity to accumulate funds for retirement and hardship. Eligible participants may contribute up to 15% of their eligible earnings to the Plan Trust. Cypress does not make contributions to the plan.

Under the New Product Bonus Plan, which was adopted in 1997, all qualified employees are provided bonus payments based on Cypress attaining certain levels of new product revenue, plus attaining certain levels of profitability. In 2001, 2000, and 1999, \$1.0 million, \$14.3 million and \$6.9 million, respectively, were charged to operations.

In 1994, a Key Employee Bonus Plan was established, which provides for bonus payments to selected employees upon achievement of certain Cypress and individual performance targets. In 2001, 2000 and 1999, \$0.0 million, \$15.0 million and \$4.9 million, respectively, were charged to operations in connection with this program.

In 1995, Cypress adopted a deferred compensation plan, which provides certain key employees with an opportunity to defer income and related taxes and an opportunity to accumulate funds for retirement on a tax deferred basis. Cypress does not make contributions to the plan. Costs incurred by Cypress for the Key Employee Deferred Compensation Plan during fiscal years 2001, 2000 and 1999 were insignificant.

## Note 14: Income Taxes

The geographic distribution of income (loss) and the components of the provision for income taxes are summarized below:

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
U.S. income (loss) before provision for taxes	\$ (406,589)	\$ 278,679	\$ 62,890
Foreign income (loss) before provision for taxes	(30,607)	91,491	32,279
Income (loss) before provision for taxes	(437,196)	370,170	95,169
Current tax expense			
U.S. Federal	-0-	81,267	15,732
State and local	137	4,284	518
Foreign	1,164	1,877	760
Total current	1,301	87,428	17,010
Deferred tax expense (benefit)			
U.S. Federal	(25,652)	(169)	(9,971)
State and local	(5,433)	5,603	—
Total deferred	(31,085)	5,434	(9,971)
<b>Total</b>	<b>\$ (29,784)</b>	<b>\$ 92,862</b>	<b>\$ 7,039</b>

The tax provision (benefit) differs from the amounts obtained by applying the statutory U.S. federal income tax rate to income before taxes as shown below.

(In thousands)	Year Ended		
	December 30, 2001	December 31, 2000	January 2, 2000
Statutory rate	35%	35%	35%
Tax at U.S. statutory rate	\$ (142,306)	\$ 129,559	\$ 33,309
Foreign income at other than U.S. rates	55	(30,145)	(11,443)
State income taxes, net of federal benefit	137	4,214	114
Tax credits	(7,500)	(5,500)	(9,568)
Prior year net operating losses, credits and other benefits recognized	—	(26,180)	(8,968)
Future benefits not recognized	60,256	—	—
Nondeductible restructuring	24,652	—	—
Nondeductible goodwill and other charges	34,802	20,746	4,326
Other, net	160	168	(731)
<b>Total</b>	<b>\$ (29,744)</b>	<b>\$ 92,862</b>	<b>\$ 7,039</b>

The components of deferred tax assets and liabilities at December 30, 2001 and December 31, 2000, under SFAS 109 were as follows:

(In thousands)	Year Ended	
	December 30, 2001	December 31, 2000
Deferred tax assets:		
Deferred income on sales to distributors	\$ 1,562	\$ 23,287
Reserves and accruals	106,527	33,934
Credits and net operating loss carryovers	93,756	17,644
<b>Total deferred tax assets</b>	<b>201,845</b>	<b>74,865</b>
Deferred tax liabilities:		
Excess of tax over book depreciation	(75,228)	(45,095)
Intangibles arising from acquisitions	(66,246)	(58,402)
Other, net	(115)	(107)
<b>Total deferred tax liabilities</b>	<b>(141,589)</b>	<b>(103,604)</b>
Net deferred tax asset (liability)	60,256	(28,739)
Valuation allowance	(60,256)	—
<b>Net deferred tax assets (liabilities) after valuation allowance</b>	<b>\$ -0-</b>	<b>\$ (28,739)</b>



Tax benefits arising from employee stock transactions of \$56.7 million and \$13.8 million were realized in fiscal 2000 and 1999, respectively, and were credited to shareholders' equity. Deferred tax assets of approximately \$7.9 million as of December 30, 2001 pertain to certain net operating loss carryforwards resulting from the exercise of employee stock options. When recognized, the tax benefit of these loss carryforwards will be accounted for as a credit to additional paid-in capital rather than a reduction of the income tax provision.

At December 31, 2001, Cypress had net federal operating loss carryovers of approximately \$237.4 million, which, if not utilized, will expire from 2016 through 2021. A significant portion of these net operating loss carryovers relate to recent acquisitions and are subject to certain limitations under the U.S. Internal Revenue Code. In addition, Cypress had U.S. federal and state tax credit carryforwards of approximately \$9.8 million which, if not utilized, will expire in 2021.

U.S. income taxes and foreign withholding taxes were not provided for on a cumulative total of \$167.9 million of undistributed earnings for certain non-U.S. subsidiaries. Cypress intends to reinvest these earnings indefinitely in operations outside the United States. If these earnings are repatriated, additional U.S. tax will be due. Cypress's global operations involve manufacturing, research and development, and selling activities outside the U.S. Cypress's operations outside the U.S. are in certain countries that impose a statutory tax rate higher than the U.S., as well as countries that impose a lower statutory tax rate than the U.S. U.S. tax has not been provided on profits from certain non-U.S. sales, until such profits are repatriated back to the U.S. Overall, Cypress expects its foreign earnings to be taxed at a rate lower than the statutory tax rate in the U.S.

In connection with acquisitions in the current year, Cypress recorded deferred tax assets of \$24.5 million and deferred tax liabilities of \$36.6 million. The deferred tax assets valuation allowance of \$60.3 million in 2001 is attributed to U.S. federal and state deferred tax assets, which result primarily from restructuring and other one-time charges, and net operating loss carryovers. The recognition of deferred tax assets was limited to the extent that management believes it is more likely than not that the net deferred tax asset will not be realized.

## Note 15: Commitments and Contingencies

### Operating Lease Commitments

Cypress leases most of its manufacturing facilities, office facilities and some equipment under non-cancelable operating lease agreements that expire at various dates through 2012. Some leases include renewal options, which would permit extensions of the expiration dates at rates approximating fair market rental values.

The aggregate gross annual rental commitments under non-cancelable operating leases, as of December 30, 2001, are as follows:

(In thousands)

<b>Fiscal Year</b>	
2002	\$ 20,297
2003	19,406
2004	12,532
2005	7,556
2006	4,273
2007 and thereafter	2,171
<b>Total</b>	<b>\$ 66,235</b>

Such rental expenses totaled approximately \$20.9 million in fiscal 2001, \$18.9 million in 2000 and \$19.5 million in 1999. In addition, these leases require us to pay taxes, insurance, maintenance and other expenses with respect to the properties.

In April 1997, Cypress sold capital equipment located in its Minnesota wafer fabrication facility to Fleet Capital Leasing for \$25 million in a sale-leaseback agreement. Cypress paid \$9.6 million upon termination of the lease in March 2000.

### Synthetic Lease Transactions

In 1994, Cypress entered into a synthetic lease agreement with respect to our office and manufacturing facilities in San Jose, which was renewed in 1999 and now expires in 2004. In 1995, Cypress entered into a synthetic lease agreement with respect to our manufacturing facility in Minnesota, which expires in 2004. In 1996, Cypress entered into an additional synthetic lease agreement that renewed in 2001 and expires in 2006 for two additional office facilities in San Jose. In addition, Cypress entered into a synthetic lease agreement with a lessor to construct and lease an additional headquarters facility in San Jose to support consolidation from acquired companies onto one main campus. This facility is expected to be completed and rental fees will begin in the first quarter of 2002. The lease will expire in 2007. Synthetic leases are leases that qualify as capital leases for tax purposes, but qualify as operating leases for financial reporting. As such, synthetic leases represent a form of "off balance sheet" financing.

These agreements require periodic payments that vary based on the London Interbank Offering Rate (“LIBOR”), plus a spread. The total amount of such payments in 2001 was \$3.7 million, in 2000 was \$4.7 million, and in 1999 was \$4.0 million. All synthetic leases provide us with (i) the options for renewal at mutually agreed upon terms, and (ii) if the leases are not extended, the right and duty to acquire the property at the Lessor’s cost or to arrange for the property to be acquired by a third party at market value.

If Cypress had purchased all the properties subject to synthetic leases at December 30, 2001, we would have been required to make a payment and record assets totaling \$76.3 million. Cypress is required to maintain (and does maintain) restricted cash or investments to serve as collateral for our obligations under these leases. The aggregate amount of such restricted cash recorded as of December 30, 2001 and December 31, 2000 was \$75.0 million and \$60.7 million, respectively, and was classified on the Balance Sheet as a non-current asset.

If Cypress does not purchase the properties subject to the synthetic leases on the required dates (including any acceleration of such date due to a default) and the property is sold to a third party at a price below lessor’s cost, then Cypress is contingently liable for such shortfall in an aggregate amount of up to \$62.2 million as of December 30, 2001. Based on management’s estimate of the fair value of the properties, no liability was required to be recorded at December 30, 2001 or December 31, 2000.

The amounts Cypress must pay (or find a third party to pay) for all of the properties subject to synthetic leases and the dates such payments are scheduled to be made are as follows:

<b>Synthetic Lease Obligations Maturing:</b>	
Within one year	none
1 to 3 years	\$43.9 million
4 to 5 years	\$18.4 million
Beyond 5 years	\$14.0 million
<b>Total</b>	<b>\$76.3 million</b>

Synthetic lease transactions require compliance by Cypress with certain financial covenants. Failure to meet these requirements can result in an event of default. Upon any such default, the lessors could require Cypress to immediately purchase the applicable facilities at cost or sell it to a third party at the fair market value. At December 30, 2001 Cypress was in violation of one financial covenant related to one synthetic lease agreement. Cypress received a waiver from the lessor for this covenant violation and have negotiated new covenants for future periods in an amendment to the lease, effective February 15, 2002. Cypress was in compliance with all other financial covenants as of December 30, 2001. While Cypress expects to maintain compliance with the covenants, Cypress’s ability to meet these financial covenants can be effected by events beyond its control and Cypress cannot assure that it will meet these covenants in the future.

## **Litigation and Asserted Claims**

The semiconductor industry has experienced a substantial amount of litigation regarding patent and other intellectual property rights. From time to time, Cypress has received, and may receive in the future, communications alleging that our products or our processes may infringe on product or process technology rights held by others. Cypress is currently, and may in the future be, involved in litigation with respect to alleged infringement by us of another party’s patents. In the future, Cypress may be involved with litigation to:

- enforce our patents or other intellectual property rights;
- protect our trade secrets and know-how;
- determine the validity or scope of the proprietary rights of others; and
- defend against claims of infringement or invalidity.

Such litigation has in the past, and could in the future, result in substantial costs and diversion of management resources. Such litigation could also result in payment of substantial damages and/or royalties or prohibitions against utilization of essential technologies, and could have a material adverse effect on our business, financial condition, results of operations and cash flows.

In July 2001, we filed a complaint in the United States International Trade Commission (“ITC”) against Integrated Circuit Systems, Inc. (“ICS”) and Pericom Semiconductor Corporation (“Pericom”) for infringement of a U.S. patent. The ITC subsequently instituted an investigation based upon Cypress’s complaint. In December 2001, Cypress agreed to settle this dispute with Pericom. Trial in the ITC against ICS is scheduled for April 2002. We will vigorously pursue and/or protect our rights in this matter. In November 2001, ICS filed a complaint in the ITC against us for infringement of two U.S. patents, one of which is also asserted against us in an earlier-filed action in California (see below). We have investigated the allegations in ICS’ complaint. We find at least some of the allegations to be completely without merit, and we are confident that we have meritorious defenses to the remainder of the allegations. While no assurance can be given regarding the outcome of this action, we believe that the final outcome of the matter will not have a material effect on our consolidated financial position or results of operations. However, because of the nature and inherent uncertainties of litigation,

tion, should the outcome of this action be unfavorable, we may be required to pay expenses, which could (but is not expected to) have a material adverse effect on our financial position, results of operations and cash flows.

In March 2001, we filed a complaint in the United States District Court for the District of Delaware against ICS, for infringement of three U.S. patents. One of these patents is the basis for Cypress's complaint in the ITC (see above), and proceedings on this patent in Delaware have been stayed pending resolution of the ITC action. In April 2001, ICS filed a complaint in the United States District Court for the Northern District of California against Cypress. We have investigated the allegations in ICS' complaint and find them completely without merit. We will vigorously pursue and/or protect our rights in this matter. While no assurance can be given regarding the outcome of this action, we believe that the final outcome of the matter will not have a material effect on our consolidated financial position or results of operations. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, we may be required to pay damages and/or expenses, which could (but is not expected to) have a material adverse effect on our financial position, results of operations and cash flows.

On November 16, 2000, Momentum, Inc. filed a complaint in the Santa Clara County Superior Court against Cypress for breach of warranty and deceit, in which it seeks consequential, indirect and punitive damages and costs. In February 2001, the Momentum complaint was dismissed, but they were given thirty days to refile. Momentum filed its Amended Complaint on April 16, 2001. We have reviewed and are investigating the allegations in the Amended Complaint. Based on the information available at this time, we believe that the suit against us is without merit. We will continue to vigorously defend ourselves in this matter. While no assurance can be given regarding the outcome of this action, we believe that the final outcome of the matter will not have a material effect on our consolidated financial position or results of operations. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, we may be required to pay damages and other expenses, which could have a material adverse effect on our financial position, results of operations and cash flows.

On October 3, 2000, U.S. Philips Corp. filed a complaint in the United States District Court for the Southern District of New York against Cypress and five codefendants for infringement of a U.S. patent. In March 2001, we filed a complaint in the United States District Court for the District of Delaware against Philips Semiconductors, Inc., for infringement of four U.S. patents. We have agreed with Philips on a resolution of the disputes, and the suits were dismissed with prejudice in December 2001.

On June 12, 2000, Cypress filed a complaint in the Superior Court of California against Altera Corporation for tortious interference with existing contractual relations, tortious interference with prospective economic relations, misappropriation of trade secrets and unfair competition. The complaint arises from Altera's interference with a multi-year agreement to collaborate on research and development between Cypress and Right Track CAD Corporation. In February 2001, we amended our complaint to add a cause of action based on fraud. We believe that we will ultimately prevail in this matter. While no assurance can be given regarding the outcome of this action, Cypress believes that the final outcome of the matter will not have a material effect on Cypress's consolidated financial position or results of operations. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, Cypress may be required to pay legal fees and other expenses that are not expected to have a material adverse effect on Cypress's financial position, results of operations and cash flows.

During 1998, EMI Group of North America, Inc. ("EMI") filed suit against Cypress in the Federal Court in Delaware, claiming that Cypress infringed on four patents owned by EMI. Cypress and EMI entered into a license agreement in February 1999, for one of the four patents in the lawsuit. EMI withdrew two of the four patents from the lawsuit, including the patent related to the licensing agreement. The case involving the two remaining patents went to trial in October 1999. The jury ruled in our favor, finding that we infringed none of the patents and that each asserted claim was invalid due to prior art and physical impossibility (i.e., the patents require a step that is physically impossible to perform). EMI's Motion for Judgment notwithstanding the Verdict was denied in part and granted in part, leaving the verdicts on noninfringement and invalidity due to physical impossibility intact, but reversing the prior art invalidity verdicts. EMI filed an appeal, and the Court of Appeals for the Federal Circuit ("CAFC") recently ruled in our favor, upholding the noninfringement and invalidity due to physical impossibility verdicts and reversing the District Court on the prior art invalidity verdicts, thereby reinstating the jury's finding that the patents are invalid in view of the prior art. We therefore believe that our defenses are meritorious, and we intend to continue to defend ourselves vigorously, should it be necessary to do so. The deadline for EMI to file an appeal to the U.S. Supreme Court has passed, and we understand that EMI has not filed or petitioned for such an appeal. However, should the outcome of this action be unfavorable, our business, financial condition, results of operations and cash flows could be materially and adversely affected.

In January 1998, an attorney representing the estate of Mr. Jerome Lemelson contacted us and charged that we infringed certain patents owned by Mr. Lemelson and/or a partnership controlled by Mr. Lemelson's estate. On February 26, 1999, the Lemelson Partnership sued us and 87 other companies in United States District Court for District of Arizona for infringement of 16 patents. In May 2000, the Court stayed litigation on 14 of the 16

patents in view of concurrent litigation in Nevada on the same 14 patents, brought against the Lemelson Partnership by manufacturers of machine vision and bar coding equipment. In October 2001, the Lemelson Partnership amended its complaint to add allegations that two (2) more patents were infringed. The two new patents are related to one of the two patents in the litigation that were not stayed. We have reviewed and investigated the allegations in both the original and amended complaints, and we believe that the suit against us is without merit. We will vigorously defend ourselves in this matter. While no assurance can be given regarding the outcome of this action, we believe that the final outcome of the matter will not have a material effect on our consolidated financial position or results of operations. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, we may be required to pay damages and other expenses, which could have a material adverse effect on our financial position, results of operations and cash flows.

On October 2, 1997, we filed an action against Kevin Yourman, Joseph Weiss, and their associated law offices in the Superior Court of California (“Superior Court”) in Santa Clara County for malicious civil prosecution in the underlying securities fraud actions initiated by Messrs. Yourman and Weiss in 1992. The underlying securities fraud actions were dismissed because the court found that none of our officers made any actionable false or misleading statements or omissions. An appeal affirmed the lower court’s finding that Messrs. Yourman and Weiss failed to put forth evidence showing a genuine issue of fact with regard to any statements by our officers. On May 4, 1999, the Superior Court granted a summary judgment motion by Messrs. Yourman and Weiss, holding that Messrs. Yourman and Weiss had probable cause to bring the underlying litigation. Our appeal of this decision has been denied. This action has not had a material effect on our consolidated financial position, results of operations and cash flows.

### **Purchase Commitments**

At December 3, 2001, Cypress had purchase commitments aggregating \$33.4 million, principally for manufacturing equipment, and facilities and bulk gas and nitrogen. These commitments relate to purchases to be made in 2002 of \$29.9 million and the remainder is committed through 2008.

### **Note 16: Related Parties**

Between 1992 and 1995, Cypress made cost-basis investments in QuickLogic Corporation (“QuickLogic”) Series D and Series E preferred stock. In addition, during 1996 Cypress had other various arrangements, including supply and licensing arrangements, which increased Cypress’s ownership in QuickLogic. In October 1999, QuickLogic announced its initial public offering. Cypress sold its investment in QuickLogic in October 1999 and as a result, recorded a \$36.2 million gain. Cypress recorded sales to QuickLogic of \$7.1 million in 1999.

On February 22, 2001 Cypress’s Chief Executive Officer, T.J. Rodgers made an investment in Sunpower Corporation, a private company developing solar cells using semiconductor technology. The investment by Mr. Rodgers was a \$750,000 bridge loan with an interest rate of 6%, which is convertible into Preferred Stock with a conversion feature priced at a 15% discount to the next round of financing. In the fourth quarter of 2001, Cypress made loans to Sunpower aggregating \$450,000 with the same terms as described above through the Cypress Venture Fund (CVF). Cypress is evaluating further investments in Sunpower Corp.

### **Note 17: Segment Information**

Historically, Cypress has disclosed two reportable business segments, Memory Products and Non-Memory Products. The Memory Products business segment includes static Random Access Memories (“RAMs”) and is characterized by high unit sales volume and generally subject to greater pricing pressures. The Non-Memory Products business segment includes data communications devices, programmable logic products, specialty memories, timing and interface products.

In October 2000, Cypress announced the formation of new divisions in order to enhance its focus on communications market segments. The WAN (Wide Area Networks) and SAN (Storage Area Networks) divisions are helping provide product definition in the networking arena. Similarly, the WIT (Wireless Terminals) and WIN (Wireless Infrastructure) divisions help focus our efforts in the wireless space. The Computation and Other market segment includes products used in computers, peripherals and other applications. Cypress’s current Memory and Non-Memory business segments continue to operate as they have in the past. The market focus is expected to provide systems knowledge, cross-product-line product portfolio definition, early engagement with strategic accounts and added management of research and development (“R&D”) spending.

Cypress evaluates the performance of its segments based on profit or loss from operations before income taxes, excluding acquisition costs and non-recurring gains and losses.

### **Market Segment Information**

The tables below set forth information about the market segments formed during fiscal 2000. Cypress does not allocate interest income and expense, income taxes or acquisition costs and non-recurring items to segments.

Cypress does not allocate assets to segments. In addition, market segments do not have significant non-cash items other than depreciation and amortization in reported profit or loss.

### Market Segment Net Revenues

(In thousands)

	2001	2000
Wide area networks/storage area networks	\$ 341,760	\$ 536,566
Wireless terminals/wireless infrastructure	225,949	473,738
Computation	251,483	277,483
<b>Total consolidated revenues</b>	<b>\$ 819,192</b>	<b>\$ 1,287,787</b>

### Market Segment Income (Loss) Before Provision for Income Taxes

(In thousands)

	2001	2000
Wide area networks/storage area networks	\$ (79,851)	\$ 166,224
Wireless terminals/wireless infrastructure	(35,245)	156,046
Computation	(51,156)	62,298
Acquisition, restructuring and other non-recurring costs	(293,366)	(55,729)
Interest income	48,231	59,152
Interest expense	(22,398)	(23,633)
Other income and (expense) net	(10,652)	5,812
<b>Income (loss) before provision for income taxes</b>	<b>\$ (444,437)</b>	<b>\$ 370,170</b>

### Business Segment Net Revenues

Cypress's reportable business segments are business units that offer different products. Products that fall under the two business segments differ in nature, are manufactured utilizing different technologies and have a different end-purpose. As such, they are managed separately. Memory Products are characterized by high unit sales volume and generally subject to greater pricing pressures. These products are manufactured using more advanced technology. A significant portion of the wafers produced for Memory Products are manufactured at Cypress's technologically advanced, eight-inch wafer production facility located in Minnesota (Fab 4). Memory Products are used by a variety of end-users but the product is used specifically for the storage and retrieval of information. In contrast to Memory Products, unit sales of Non-Memory Products are generally lower than Memory Products, but sell at higher gross margins. Some Non-Memory Products are manufactured utilizing less technologically advanced processes. A majority of wafers for Non-Memory Products are manufactured at Cypress's six-inch wafer production facility located in Texas (Fab 2), while some wafers are procured from foundries. Products in the Non-Memory segment perform functions such as timing management, data transfer and routing in computer, communications and storage systems. Products range from high-volume Universal Serial Bus ("USB") interfaces for personal computers to high-value products such as our OC-48 SERDES device for optical communications systems.

The tables below set forth information about the reportable business segments for fiscal years 2001, 2000 and 1999. Cypress does not allocate interest income and expense, income taxes or acquisition costs and non-recurring items to segments. Cypress does not allocate assets to segments. In addition, business segments do not have significant non-cash items other than depreciation and amortization in reported profit or loss.

(In thousands)

	2001	2000	1999
Memory	\$ 350,908	\$ 638,111	\$ 309,002
Non-Memory	468,284	649,676	436,040
<b>Total consolidated revenues</b>	<b>\$ 819,192</b>	<b>\$ 1,287,787</b>	<b>\$ 745,042</b>



## Business Segment Income (Loss) Before Provision for Income Taxes

(In thousands)

	2001	2000	1999
Memory	\$ (71,503)	\$ 184,279	\$ (19,091)
Non-Memory	(94,749)	200,289	104,789
Acquisitions, restructuring and other non-recurring costs	(293,366)	(55,729)	(34,091)
Interest income	48,231	59,152	18,297
Interest expense	(22,398)	(23,633)	(9,643)
Other income and (expense), net	(10,652)	5,812	34,908
<b>Income (loss) before provision for income taxes</b>	<b>\$ (444,437)</b>	<b>\$ 370,170</b>	<b>\$ 95,169</b>

## Business Segment Depreciation and Amortization

(In thousands)

	2001	2000	1999
Memory	\$ 123,400	\$ 73,067	\$ 67,306
Non-Memory	125,603	77,637	42,614
<b>Total consolidated depreciation and amortization</b>	<b>\$ 249,003</b>	<b>\$ 150,704</b>	<b>\$ 109,920</b>

## Geographic Area

Revenues are attributed to countries based on the customer location. Revenues by geographic locations were:

(In thousands)

	2001	2000	1999
United States	\$ 406,692	\$ 657,388	\$ 377,625
Europe	131,578	281,574	131,528
Japan	105,998	133,669	69,041
Other foreign countries	174,924	215,156	166,848
<b>Total revenues</b>	<b>\$ 819,192</b>	<b>\$ 1,287,787</b>	<b>\$ 745,042</b>

Long-lived assets (property, plant and equipment, net) by geographic locations were:

(In thousands)

	2001	2000	1999
United States	\$ 441,188	\$ 498,843	\$ 276,576
Philippines	52,983	65,503	77,426
Other foreign countries	5,624	7,129	4,204
<b>Total long-lived assets</b>	<b>\$ 499,795</b>	<b>\$ 571,475</b>	<b>\$ 358,206</b>

## Note 18: Subsequent Events

In January 2002 the Department of Commerce revoked a 1998 antidumping order that had been imposed on SRAMs fabricated in Taiwan and imported into the United States. The Customs Service was ordered to refund, with interest, all duties deposited under the 1998 antidumping order. Between 1998 and 2001 Cypress charged \$10.3 million to costs of revenues for such duties. As of February 28, 2002 Cypress has received \$4.0 million and expects that it may receive up to \$8.0 million during the remainder of 2002. The refunds will be recorded as an offset to cost of revenues and the interest will be recorded as interest income as received.

During 2001, the Board of Directors authorized the repurchase of up to \$143.8 million of 3.75% Convertible Subordinated Notes. In January 2002, we repurchased a total principal amount of \$30.0 million for \$25.4 million, resulting in a pre-tax net gain of \$3.9 million. The net after-tax gain will be recorded as an extraordinary item in the 2002 consolidated statements of operations. Cumulatively we have repurchased \$82.8 million in principal.

## Report of Independent Accountants

To the Board of Directors and Stockholders  
of Cypress Semiconductor Corporation

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Cypress Semiconductor Corporation and its subsidiaries at December 30, 2001 and December 31, 2000 and the results of their operations and their cash flows for each of the three years in the period ended December 30, 2001 in conformity with accounting principles generally accepted in the United States of America. 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 of these statements in accordance with auditing standards generally accepted in the United States of America, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

San Jose, California

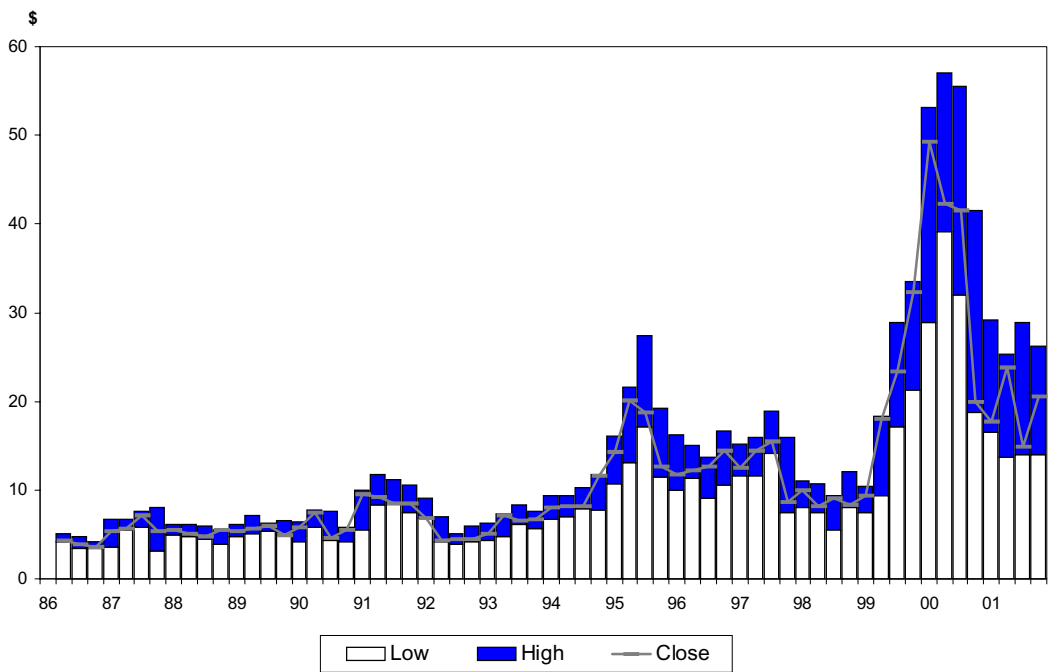
January 23, 2002, except as to Notes 15 and 18,  
which are as of February 28, 2002

# About Your Investment

Our common stock is listed on the New York Stock Exchange under the trading symbol “CY”. The following table sets forth, for the periods indicated, the low, high and closing price for the common stock. We have not paid cash dividends and have no present plans to do so. At February 28, 2002, there were approximately 74,000 holders of record of our Common Stock.

Price Range of Common Stock (\$)			
	Low	High	Close
Fiscal year ended December 30, 2001:			
First Quarter	16.50	29.25	17.73
Second Quarter	13.72	25.36	23.85
Third Quarter	14.04	28.95	14.86
Fourth Quarter	14.00	26.20	20.62
Fiscal Year ended December 31, 2000:			
First Quarter	28.94	53.19	49.31
Second Quarter	39.19	57.00	42.25
Third Quarter	32.00	55.56	41.56
Fourth Quarter	18.81	41.50	19.69

## Share Price



## Summary Annual and Quarterly Financial Data

(In thousands, except per-share data, percents and employee headcount)

(Unaudited)

Year Ended

	Dec. 30, 2001	Dec. 31, 2000	Jan. 2, 2000	Jan. 3, 1999	Dec. 29, 1997	Dec. 30, 1996	Jan. 1, 1996	Jan. 2, 1995
Revenues	\$ 819,192	\$1,287,787	\$ 745,042	\$ 588,915	\$ 632,969	\$ 600,032	\$ 645,823	\$ 432,368
Costs and expenses:								
Cost of revenues	552,267	564,839	408,885	429,599	424,462	368,852	305,949	238,082
Research and development	267,522	184,471	136,858	116,871	105,570	96,610	80,706	59,089
Selling, general and administrative	165,655	153,909	113,601	97,267	85,062	72,356	78,093	56,800
Acquisition and other non-recurring costs	161,253	56,214	37,902	—	3,669	(17,800)	17,800	—
Restructuring	132,113	(485)	(3,811)	60,737	9,882	28,732	—	—
Total costs and expenses	1,278,810	958,948	693,435	704,474	628,645	548,750	482,548	353,971
Operating income (loss)	(459,618)	328,839	51,607	(115,559)	4,324	51,282	163,275	78,397
Interest expense	(22,398)	(23,633)	(9,643)	(11,276)	(8,461)	(7,743)	(7,543)	(4,747)
Interest income and other	37,579	64,964	53,205	14,133	13,442	9,349	8,784	6,529
Income (loss) before income taxes and extraordinary gain	(444,437)	370,170	95,169	(112,702)	9,305	52,888	165,516	80,179
(Provision) benefit for income taxes	32,680	(92,862)	(7,039)	11,108	(6,109)	(30,476)	(59,343)	(29,628)
Net income (loss) before extraordinary gain	(411,757)	277,308	88,130	(101,594)	3,196	22,412	105,173	50,551
Extraordinary gain (net of tax \$2896)	4,345	—	—	—	—	—	—	—
Net income (loss)	\$ (407,412)	\$ 277,308	\$ 88,130	\$ (101,594)	\$ 3,196	\$ 22,412	\$ 105,173	\$ 50,551
<u>Basic net income (loss) per share:</u>								
Before extraordinary gain	\$ (3.32)	\$ 2.29	\$ 0.81	\$ (0.97)	\$ 0.03	\$ 0.24	\$ 1.13	\$ 0.62
Extraordinary gain (net of tax)	0.04	—	—	—	—	—	—	—
Net income (loss)	\$ (3.28)	\$ 2.29	\$ 0.81	\$ (0.97)	\$ 0.03	\$ 0.24	\$ 1.13	\$ 0.62
<u>Diluted net income (loss) per share:</u>								
Before extraordinary gain	\$ (3.32)	\$ 2.03	\$ 0.76	\$ (0.97)	\$ 0.03	\$ 0.23	\$ 0.99	\$ 0.55
Extraordinary gain (net of tax)	0.04	—	—	—	—	—	—	—
Net income (loss)	\$ (3.28)	\$ 2.03	\$ 0.76	\$ (0.97)	\$ 0.03	\$ 0.23	\$ 0.99	\$ 0.55
<u>Weighted average common and common equivalent shares outstanding:</u>								
Basic	124,135	121,126	108,156	105,238	102,920	92,317	92,735	81,917
Diluted	124,135	144,228	115,527	105,238	110,820	97,767	109,672	96,096
Depreciation/ amortization expense	249,003	150,704	109,920	117,204	114,350	100,506	67,203	46,576
Cash, cash equivalents and short-term investments	205,422	884,601	280,947	174,513	213,939	98,353	166,387	201,618
Stockholders' equity	868,428	1,327,668	718,620	517,825	658,643	514,287	495,711	360,648
Number of employees	4,119	4,435	3,859	3,068	3,007	2,442	2,078	1,589
<u>Percent of revenue</u>								
Cost of revenue	67%	44%	55%	73%	67%	61%	47%	55%
Research & development	33%	14%	18%	20%	17%	16%	12%	14%
Selling, general & administrative	30%	12%	15%	17%	13%	12%	12%	13%
Total costs and expenses	60%	74%	93%	120%	99%	91%	75%	82%
Operating income (loss)	-56%	26%	7%	-20%	1%	9%	25%	18%

**Three Months Ended**

	Dec. 30, 2001	Sep. 30, 2001	Jul. 1, 2001	Apr. 1, 2001	Dec. 31, 2000	Oct. 1, 2000	July 2, 2000	April 2, 2000
\$	191,099	\$ 180,284	\$ 185,546	\$ 262,263	\$ 370,025	\$ 352,687	\$ 300,834	\$ 264,241
	114,930	208,111	103,517	125,709	151,087	147,783	135,143	130,826
	71,093	77,496	61,509	57,424	55,382	47,954	42,742	38,393
	40,148	41,571	37,644	46,292	43,420	40,350	36,513	33,626
	27,096	91,566	19,543	23,048	8,856	35,557	7,592	4,209
	—	132,113	—	—	—	—	(485)	—
	253,267	550,857	222,213	252,473	258,745	271,644	221,505	207,054
	(62,168)	(370,573)	(36,667)	9,790	111,280	81,043	79,329	57,187
	(5,517)	(5,653)	(5,657)	(5,571)	(5,613)	(7,953)	(5,501)	(4,566)
	6,366	1,142	14,586	15,485	21,260	16,987	12,315	14,402
	(61,319)	(375,084)	(27,738)	19,704	126,927	90,077	86,143	67,023
	19,270	12,775	9,882	(9,247)	(29,337)	(28,028)	(20,514)	(14,983)
	(42,049)	(362,309)	(17,856)	10,457	97,590	62,049	65,629	52,040
	4,345	—	—	—	—	—	—	—
\$	(37,704)	\$ (362,309)	\$ (17,856)	\$ 10,457	\$ 97,590	\$ 62,049	\$ 65,629	\$ 52,040
	(0.35)	(2.92)	(0.14)	0.08	0.75	0.51	0.56	0.45
	0.04	—	—	—	—	—	—	—
\$	(0.31)	\$ (2.92)	\$ (0.14)	\$ 0.08	\$ 0.75	\$ 0.51	\$ 0.56	\$ 0.45
	(0.35)	(2.92)	(0.14)	0.08	0.68	0.45	0.50	0.40
	0.04	—	—	—	—	—	—	—
\$	(0.31)	\$ (2.92)	\$ (0.14)	\$ 0.08	\$ 0.68	\$ 0.45	\$ 0.50	\$ 0.40
	120,501	124,107	125,515	126,417	129,335	121,139	118,186	115,841
	120,501	124,107	125,515	132,050	147,575	148,474	142,113	138,750
	53,503	63,478	66,605	65,417	44,107	40,620	34,936	31,041
	205,422	222,010	585,840	701,828	884,601	831,245	840,378	517,163
	868,428	1,197,326	1,284,429	1,383,121	1,327,668	1,139,002	897,399	794,984
	4,119	4,026	4,625	4,570	4,435	4,277	3,896	3,876
	60%	115%	56%	48%	41%	42%	45%	50%
	37%	43%	33%	22%	15%	14%	14%	15%
	21%	23%	20%	18%	12%	11%	12%	13%
	133%	306%	120%	96%	70%	77%	74%	78%
	−33%	−206%	−20%	4%	30%	23%	26%	22%



## CORPORATE INFORMATION

<b>BOARD OF DIRECTORS</b>	Eric Benhamou <sup>(1,2)</sup>	Chairman of the Board, Chairman of the Board of 3COM Corporation
	Fred B. Bialek	Business Consultant
	John C. Lewis <sup>(1,2,3)</sup>	Former Chairman of the Board of Amdahl Corporation
	James R. Long <sup>(1,2)</sup>	Former Executive Vice President of Nortel Networks
	T. J. Rodgers <sup>(4)</sup>	President and Chief Executive Officer
	Alan F. Shugart <sup>(3)</sup>	Former Chief Executive Officer of Seagate
	T. J. Rodgers, President and Chief Executive Officer	
<b>EXECUTIVE VICE PRESIDENTS</b>	Antonio Alvarez, Vice President, Memory Products Division and Research and Development	
	Anthony Cantu, Vice President, Quality/Reliability Assurance	
	Emmanuel Hernandez, Vice President, Finance and Administration and Chief Financial Officer	
	Jeff Kaszubinski, Vice President, President, Silicon Magnetic Systems	
	Paul Keswick, Vice President, New Product Development	
	Ilhan Refioglu, Vice President, Timing Technology	
	Robert McConnell, Vice President, President, Cypress MicroSystems, Inc	
	Daniel Morris, Vice President, WAN/SAN Business Segment	
	Christopher Norris, Vice President, Data Communications	
	Cathal Phelan, Vice President, Interface Products Division	
	Ralph Schmitt, Vice President, Marketing and Sales	
	Christopher Seams, Vice President, Technology and Worldwide Wafer Manufacturing	
	Thomas Werner, Vice President, President, Silicon Light Machines	
	Steve Whelan, Vice President, Wireless Business Segment	
	Arthur Woodward, Vice President, Worldwide Backend Manufacturing	
<b>LEGAL MATTERS</b>	Questions regarding legal matters should be directed to: Emmanuel Hernandez, Vice President, Finance and Administration and Chief Financial Officer	
<b>LEGAL COUNSEL</b>	Wilson, Sonsini, Goodrich & Rosati 650 Page Mill Road Palo Alto, California 94304-1050 (650) 493-9300	
<b>INDEPENDENT ACCOUNTANTS</b>	PricewaterhouseCoopers LLP 10 Almaden Blvd., Suite 1600 San Jose, California 95113 (408) 817-3700	
<b>CORPORATE HEADQUARTERS</b>	Cypress Semiconductor Corporation 3901 North First Street San Jose, California 95134-1599	Telephone: (408) 943-2600 Facsimile: (408) 943-4730 Internet: <a href="http://www.cypress.com">http://www.cypress.com</a>
<b>REGISTRAR AND TRANSFER AGENT</b>	EquiServe, L.P. 150 Royall Street Canton, MA 02021 (781) 575-3981	

(1) Member of the Audit Committee

(2) Member of the Compensation Committee

(3) Member of the Nominating Committee

(4) Founder

The Letter to Shareholders, the 2001 Annual Report cover, and "Management's Discussion and Analysis" may contain forward-looking statements about the prospects for Cypress as well as the semiconductor industry more generally including without limitation statements about revenues for the first quarter of fiscal 2002, increases in gross margin, rate of growth of research and development expenditures as a percent of revenues, rate of growth of selling, general and administrative expenses, profitability goals, revenue goals, growth rate goals, market share goals, market size and growth projections, new product introductions, planned manufacturing capacity, and efficiency and cost goals. Actual results could differ materially from those described in the forward-looking statements as a result of various factors including, but not limited to, the factors identified in the Letter to Shareholders, the 2001 Annual Report cover, and the Management's Discussion and Analysis section, particularly "Factors Affecting Future Results," as well as the following:

- (1) increased competition which could result in lost sales or price erosion;
- (2) changes in product demand by the electronics and semiconductor industries, which are noted for rapidly changing needs, coupled with an inability by Cypress to generate product enhancements or new product introductions which keep pace with or meet those rapidly changing needs;
- (3) failure by Cypress to develop or introduce successfully new products in areas of expected new or increased demand, or development and introduction of superior new products serving those areas by others;
- (4) failure of expected growth in demand for, or areas of expected new demand for, semiconductor products to materialize;
- (5) failure to successfully bring on line and utilize additional manufacturing capacity, or to transition existing capacity to new uses;
- (6) inability to develop and/or adopt more advanced manufacturing technology;
- (7) inability of Cypress's patents or other proprietary rights to ensure adequate protection against encroachment on Cypress's technology by competitors; and
- (8) failure to attract and/or retain key personnel.

Cypress employees produced this report to provide the maximum amount of useful information on the Company in an accessible form, at a minimum of cost. We appreciate their time and effort.

### ANNUAL MEETING

The annual meeting of stockholders for Cypress Semiconductor Corporation will be held on Thursday, May 2, 2002 10:00 a.m., local time, at Cypress's offices at 3939 North First Street, San Jose, California 95134-1599.

### COMMON STOCK

Cypress Semiconductor Corporation's common stock is traded on the New York Stock Exchange under the symbol "CY."

### FORM 10K

A copy of Cypress's Annual Report on Form 10K, as filed with the Securities and Exchange Commission, will be made available without charge to all stockholders upon written request to Cypress. Direct requests to the Attention of the Chief Financial Officer at the corporate office listed above.

# Driving the Communications Revolution™ With the Right Products for the Right Markets

Cypress components are at the heart of the world's finest electronic products, targeting communications markets such as wide area networks (WAN), storage area networks (SAN), wireless terminals (WIT) and wireless infrastructure (WIN), along with markets for consumer, computation, home networking and automotive products.

Sony Computer Entertainment's Playstation® 2 computer entertainment system incorporates a Cypress programmable clock chip.

NEC's 3G handsets enable web access for users; Cypress Dual-Port RAMs enable NEC 3G handsets.

Force10 Networks Inc.'s E1200 uses Cypress's Network Search Engines (NSEs) to deliver the industry's highest-capacity 10-gigabit Ethernet (10GbE) switch/router.

Eagle Test Systems' next-generation ETS600 mixed-signal semiconductor test system can easily test up to 64 mixed-signal devices simultaneously. The system uses Cypress's Delta39K™ and Ultra37000™ complex programmable logic devices (CPLDs).

NexSAN's family of ATAbay2® products, which recently won the award for "Best Enterprise Storage" at the COMDEX Fall 2001 tradeshow, use Cypress Delta39K™ CPLDs.

lomega's USB 2.0 Predator™ compact disc read/write (CD-RW) drive uses Cypress USB connectivity to enable leading-edge design; USB 2.0 runs at 480 Mbps—40x the speed of first-generation USB 1.1 connections.

Cypress (with logo), HOTLink, and RoboClock are registered trademarks and Com-Link, Delta39K, Driving the Communications Revolution, FLEx36, HOTLinkIII, MoBL, More Battery Life, NoBL, No Bus Latency, POSIC, PSI, Programmable System-on-Chip, PSoC, QuadPort DSE, RoboClockII, and Ultra37000 are trademarks of Cypress Semiconductor Corporation. The SLM logo, Bringing the Power of Silicon to Light, Grating Light Valve and GLV are trademarks of Silicon Light Machines, Inc. Alcatel is a registered trademark of Alcatel. ATAbay2 is a registered trademark of NexSAN. Bluetooth is a trademark of Bluetooth SIG, Inc. Foundry Networks and Nettron are registered trademarks of Foundry Networks, Inc. Microsoft, Xbox and the Xbox Logos are either registered trademarks or trademarks of Microsoft Corporation in the U.S. and/or in other countries and are used with permission from Microsoft. Neuron is a registered trademark of Echelon Corp. Passport is a registered trademark of Nortel Networks. Playstation is a registered trademark of Sony. Predator is a trademark of lomega. QDR is a trademark of the QDR Memory Consortium. V66 is a trademark of Motorola. Other names may be service marks or trademarks of their respective holders and may be registered in certain jurisdictions. Customer photographs used in this report were provided by Alcatel, Eagle Test Systems, Ericsson, Force10 Networks, Foundry Networks, Intel, lomega, Microsoft, Motorola, NEC, NexSAN, Nortel Networks, and Sony and are used by permission. The product names are trademarks or registered trademarks of the respective companies.



# Cypress Connects™ From Last Mile to First Mile

*Wireless or wireline, digital or optical: High-speed Cypress connectivity drives key end-market products across the communications topology. Cypress connections rely on emerging transmissions standards and target a broad range of applications.*

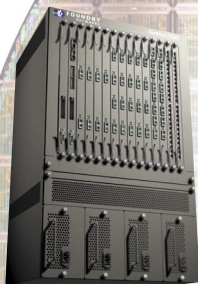
Motorola's V66™ model cellular handset uses Cypress More Battery Life™ (MoBL™) memory technology to extend talk time and provide portable communication capability to the global community.



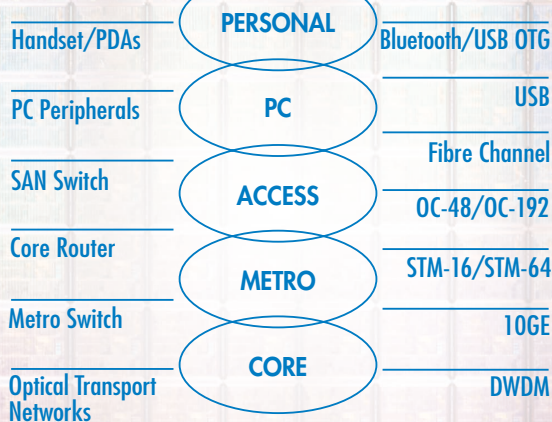
Nortel Networks' Passport® 15000 is the industry's most versatile multiservice switch, supporting frame relay, internet protocol (IP), asynchronous transfer mode (ATM), and voice services. Cypress SRAMs, clocks and specialty memories make this possible.



Foundry Networks® NetIron® product family, using Cypress Network Search Engines (NSEs), implements Metro strategy to focus on Multi Protocol Label Switching (MPLS) and Layer 2 Metro architectures embracing SONET and 10-gigabit Ethernet.



Alcatel®'s 7670 Routing Switch Platform uses Cypress FIFO, Dual-Port RAM, synchronous SRAM, SRAM, CPLD, RoboClock® and other clock products.



Ericsson's T60d mobile phone uses Cypress 4-Mbit MoBL™ memories to enable users to communicate quickly from anywhere in the world.



Microsoft's new Xbox™ video game system provides the latest in gaming experience. Cypress provides timing technology and USB controller solutions for Xbox.

Intel's Hannacroix concept PC, which uses Cypress's USB controllers, exemplifies how PC designers can integrate leading-edge, value-added features into their motherboards.



Driving the Communications Revolution™

3901 North First Street, San Jose, CA 95134  
(408) 943-2600 ■ [www.cypress.com](http://www.cypress.com)