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OPTI INC
Form 10-Q
August 06, 2001

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended June 30, 2001

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Transition Period from _____ to _____

Commission File Number 0-21422
OPTi Inc.

(Exact name of registrant as specified in this charter)

CALIFORNIA
(State or other jurisdiction of
incorporated or organization)

77-0220697
(I.R.S. Employer
Identification No.)

660 Alder Drive, Milpitas, California
(Address of principal executive office)

95035
(Zip Code)

Registrant's telephone number, including area code (408) 382-2600

Indicate by check mark whether the registrant (1) has filed all reports to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

The number of shares outstanding of the registrant's common stock as of June 30, 2001 was 11,633,903

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OPTi, Inc.

FORM 10-Q

For the Quarterly Period Ended June 30, 2001

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| | | | |
|---|---------|------------|---------|
| Costs and expenses: | | | |
| Cost of sales | 956 | 2,303 | 2,130 |
| Research and development | 285 | 112 | 386 |
| Selling, general, and administrative | 801 | 3,914 | 1,637 |
| | ----- | ----- | ----- |
| Total costs and expenses | 2,042 | 6,329 | 4,153 |
| | ----- | ----- | ----- |
| Operating income (loss) | (387) | (3,005) | (381) |
| Interest and other income, net | 436 | 519 | 884 |
| | ----- | ----- | ----- |
| Income (loss) before income tax provision | 49 | (2,486) | 503 |
| Income tax provision | 2 | 1 | 12 |
| | ----- | ----- | ----- |
| Net income (loss) | \$ 47 | \$ (2,487) | \$ 491 |
| | ===== | ===== | ===== |
| Basic net income (loss) per share | \$ 0.00 | \$ (0.21) | \$ 0.04 |
| | ===== | ===== | ===== |
| Diluted net income (loss) per share | \$ 0.00 | \$ (0.21) | \$ 0.04 |
| | ===== | ===== | ===== |
| Shares used in computing basic per share amounts | 11,634 | 11,646 | 11,641 |
| | ===== | ===== | ===== |
| Shares used in computing diluted per share amounts | 11,634 | 11,646 | 11,644 |
| | ===== | ===== | ===== |

See accompanying notes.

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OPTi Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS

| | June 30, 2001 | December 31, 2000 |
|---------------------------|------------------|----------------------|
| | ----- | ----- |
| Assets | | |
| | (000's omitted) | |
| Current assets | | |
| Cash and cash equivalents | \$11,989 | \$12,146 |
| Short-term investments | 36,239 | 45,980 |
| Accounts receivable, net | 307 | 1,131 |
| Inventories | 386 | 1,140 |
| Other current assets | 286 | 359 |
| | ----- | ----- |
| Total current assets | 49,207 | 60,756 |

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| | | |
|---|----------|----------|
| Property and equipment, net | 170 | 157 |
| Other assets | 328 | 359 |
| | ----- | ----- |
| Total assets | \$49,705 | \$61,272 |
| | ===== | ===== |
| Liabilities and Shareholders' Equity | | |
| Current liabilities | | |
| Accounts payable | \$310 | \$1,365 |
| Other current liabilities | 734 | 2,441 |
| | ----- | ----- |
| Total current liabilities | 1,044 | 3,806 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| Preferred stock, no par value: | | |
| Authorized shares -- 5,000 | | |
| No shares issued or outstanding | | |
| Common stock, no par value: | | |
| Authorized shares -- 50,000 | | |
| Issued and outstanding shares -- 11,634 in 2001 | | |
| 11,655 in 2000 | 22,567 | 22,646 |
| Accumulated other comprehensive income | 15,871 | 25,088 |
| Retained earnings | 10,223 | 9,732 |
| | ----- | ----- |
| Total shareholders' equity | 48,661 | 57,466 |
| | ----- | ----- |
| Total liabilities and shareholders' equity | \$49,705 | \$61,272 |
| | ===== | ===== |

Note 1 - The consolidated balance sheet at December 31, 2000 has been derived from the audited financial statements.

See accompanying notes.

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OPTi Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Six months Ended June 30, | |
|------------------------------------|---------------------------|----------|
| | 2001 | 2000 |
| | ----- | |
| | (000's omitted) | |
| Operating Activities: | | |
| Net income | \$ 491 | \$10,089 |
| Adjustments: | | |
| Depreciation | 88 | 268 |
| Changes in assets and liabilities: | | |
| Accounts receivable | 824 | (486) |

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| | | |
|--|-----------|----------|
| Inventories | 754 | (356) |
| Other assets | 104 | 903 |
| Accounts payable | (1,055) | 1,004 |
| Litigation accrual | - | 3,000 |
| Other current liabilities | (448) | (560) |
| | ----- | ----- |
| Net cash provided by operating activities | 758 | 13,862 |
| Investing Activities: | | |
| Purchase of property and equipment | (101) | (24) |
| Sale of property and equipment | - | 41 |
| Purchase of short-term investments | (19,318) | - |
| Cash impact of Sale of OPTi Japan KK | - | (1,102) |
| Sale of short-term investments | 18,583 | - |
| | ----- | ----- |
| Net cash used in investing activities | (836) | (1,085) |
| | ----- | ----- |
| Financing Activities: | | |
| Net proceeds from sale of common stock | - | 117 |
| Repurchase of common stock | (79) | - |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | (79) | 117 |
| | ----- | ----- |
| Net increase (decrease) in cash and cash equivalents | (157) | 12,894 |
| Cash and cash equivalents beginning of period | 12,146 | 23,722 |
| | ----- | ----- |
| Cash and cash equivalents end of period | \$ 11,989 | \$36,616 |
| | ===== | ===== |

See accompanying notes.

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OPTi Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2001

1. Basis of presentation

The information at June 30, 2001 and for the six month periods ended June 30, 2001 and 2000, is unaudited, but includes all adjustments (consisting of normal recurring accruals) which the Company's management believes to be necessary for the fair presentation of the financial position, results of operations and cash flows for the periods presented. Interim results are not necessarily indicative

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of results for a full year. The accompanying financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2000.

2. Net income (loss) per share

Basic net income per share and basic and diluted net loss per share are computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per share is calculated using the weighted average number of common and dilutive common equivalent shares outstanding during the period. Dilutive common equivalent shares consist of stock options.

The following table sets forth the computation of basic and diluted net income (loss) per share (in thousands except per share data):

| | Three Months ended June 30, | | Mon Jun |
|--|-----------------------------------|------------|------------|
| | 2001 | 2000 | 2001 |
| | ---- | ---- | ---- |
| Net income (loss) | \$ 47 | \$ (2,487) | \$ 491 |
| | ===== | ===== | ===== |
| Weighted average number of common shares outstanding | 11,634 | 11,646 | 11,641 |
| | ===== | ===== | ===== |
| Basic net income (loss) per share | \$ 0.00 | \$ (0.21) | \$ 0.04 |
| | ===== | ===== | ===== |
| Weighted average number of common shares outstanding | 11,634 | 11,646 | 11,641 |
| Effect of dilutive securities: | | | |
| Employee stock options | -- | -- | 3 |
| | ----- | ----- | ----- |
| Denominator for diluted net income per share | 11,634 | 11,646 | 11,644 |
| | ===== | ===== | ===== |
| Diluted net income (loss) per share | \$ 0.00 | \$ (0.21) | \$ 0.04 |
| | ===== | ===== | ===== |

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3. Short-Term Investments

At June 30, 2001, and December 31, 2000 the Company's short-term investments include an unrealized gain of \$16.2 million and \$26.7 million, respectively, related to its investment in Tripath Technology, Inc.

4. Inventories

Inventories consist of finished goods and work in process (in thousands):

| | |
|---------------|-------------------|
| June 30, 2001 | December 31, 2000 |
|---------------|-------------------|

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| | | |
|-----------------|-------|---------|
| | ----- | ----- |
| Finished Goods | \$309 | \$ 871 |
| Work in process | 77 | 269 |
| | ---- | ----- |
| | \$386 | \$1,140 |
| | ===== | ===== |

5. Segment Information

Sales of the Company's product based on customer location were as follows (in thousands):

| | Three months ended | | Six months ended | |
|-----------------|--------------------|---------|------------------|---------|
| | June 30, | | June 30, | |
| | 2001 | 2000 | 2001 | 2000 |
| | ---- | ---- | ---- | ---- |
| Taiwan | \$ 472 | \$ 976 | \$1,446 | \$1,695 |
| Japan | 255 | 769 | 517 | 1,182 |
| Other Far East | 218 | 462 | 421 | 786 |
| United States | 683 | 1,112 | 1,322 | 1,694 |
| Europe Other | 27 | 5 | 66 | 10 |
| | ----- | ----- | ----- | ----- |
| Total Net Sales | \$1,655 | \$3,324 | \$3,772 | \$5,367 |
| | ===== | ===== | ===== | ===== |

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6. Concentrations

Tripath Technology, Inc.

Tripath Technology, Inc. ("Tripath"), an investment held by the Company, became publicly traded in August 2000. This investment, with a cost of \$0.7 million, is reflected in the Company's June 30, 2001 balance sheet under short term investments at a fair market value of \$16.9 million and \$27.4 million at December 31, 2000. These shares were subject to lock-up agreements which restricted their transfer until January 27, 2001. Tripath to date has a limited operating history as it began to ship products in 1998 and many of its products have only recently been introduced. Tripath also has a history of losses. As of December 31, 2000, Tripath has an accumulated deficit of approximately \$111 million. It incurred net losses of approximately \$41 million in 2000, \$32 million in 1999 and \$34 million in 1998. It expects to continue to incur net losses in the future and these losses may be substantial. As of July 31, 2001, the fair market value of the Company's investment in Tripath has decreased by \$14.2 million from June 30, 2001 due to a decline in the trading price of Tripath stock.

Major Customers and Credit Risks

The Company primarily sells to PC, motherboard and add-in card manufacturers. The Company performs ongoing credit evaluations of its customers but does not require collateral. The Company maintains reserves for potential credit losses, and such losses have been within management's expectations. With the exception of sales to NCR and its subcontractors, Holystone Enterprises, a Taiwan based company and OPTi Japan, our former subsidiary, no other single customer represented more than 10% of sales for the first six months of 2001. In the first six months of 2001, the Company sold to Holystone Enterprises

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approximately \$1.4 million in USB controllers, representing approximately 37% of net sales for the period. Also in the first six months of 2001, the Company sold approximately \$0.7 million of its embedded core logic product to NCR and its subcontractors, representing approximately 18% of net sales for that period. The Company also sold approximately \$0.5 million of core logic product to OPTi Japan representing 13% of net sales for the period.

Many of the Company's customers, particularly the motherboard manufacturers in Taiwan, operate at very low profit margins and undertake significant inventory risks. To the extent the Company provides open terms of credit to some of the larger of these customers, the Company is exposed to significant credit risks if these customers are unable to remain profitable. Approximately 40% of the Company's receivables at June 30, 2001 were with these customers.

Suppliers

The Company's reliance on independent foundries, packaging houses and test facilities involves several risks, including the absence of adequate capacity, the unavailability of or interruptions in access to certain process technologies and reduced control over delivery schedules, manufacturing yields and costs. At times during the first three quarters of 2000, the Company was unable to meet the demand for certain of its products due to limited foundry capacity and the Company expects that it will experience other production shortfalls or difficulties in the future. Because the Company's purchase orders with its outside foundries are non-cancelable by OPTi, the Company is subject to inventory surpluses and has in the past experienced write-downs of inventories due to an unexpected reduction in demand for a certain product.

Products

The Company's product life cycles are typically very short and ramp into volume production very quickly. At any point in time, the Company may rely on a limited number of products for a significant share of the Company's revenue. In the first half of 2001, the Company was highly dependent on continued revenue contributions from its USB controller. For the first six months ended June 30, 2001, the Company sold approximately \$2.0 million of its two port USB controller, representing approximately 54% of revenue. In the second half of 2001, the Company anticipates that it will rely heavily upon existing products in

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production. Any significant shortfall in sales for the Company's current volume products will have a material adverse effect upon the Company's financials.

7. Comprehensive Income

The Company's total comprehensive income (loss) was as follows (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|-----------------------------------|-----------------------------------|------------|---------------------------------|----------|
| | 2001 | 2000 | 2001 | 2000 |
| | ---- | ---- | ---- | ---- |
| Net income (loss) | \$ 47 | \$ (2,487) | \$ 491 | \$10,089 |
| Other comprehensive income (loss) | 2,281 | --- | (9,217) | --- |

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| | | | | |
|-----------------------------|---------|------------|------------|----------|
| | ----- | ----- | ----- | ----- |
| Comprehensive income (loss) | \$2,328 | \$ (2,487) | \$ (8,726) | \$10,089 |
| | ===== | ===== | ===== | ===== |

Other comprehensive income includes unrealized gains on marketable securities net of taxes.

8. Litigation

The Company has been notified of claims that it may be infringing patents, maskwork rights, or copyrights owned by third parties. There can be no assurance that the Company will not become involved in litigation regarding the alleged infringements by the Company of third party intellectual property rights. However, the Company believes that the final disposition of such matters will not have a material adverse effect on the Company's financial position, results of operations and cash flows.

9. Use of 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. Actual results could differ from those estimates.

10. Taxes

The Company recorded a tax provision of approximately 4% for the quarter ended June 30, 2001. For the six months periods ended June 30, 2001 and 2000, the Company recorded a tax provision of approximately 2% and 3%, respectively. The Company's effective tax rate differed from the federal statutory rates during 2001 and 2000 primarily due to the utilization of prior year tax losses carried forward, federal alternative minimum taxes and foreign taxes.

11. Recent Pronouncements

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). SFAS 133 provides a comprehensive and consistent standard for the recognition and measurement of derivatives and hedging activities. In June 1999, FASB issued Financial Accounting Standards No. 137 which deferred the effective date of SFAS 133 to fiscal years beginning after June 15, 2000. The adoption of SFAS 133 did not have an impact on the Company's results of operations or financial condition as the Company held no derivative financial instruments and does not currently engage in hedging activities.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations

Information set forth in this report constitutes and includes forward looking information made within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities and Exchange Act of 1934, as

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amended, that involve risks and uncertainties. The Company's actual results may differ significantly from the results discussed in the forward looking statements as a result of a number of factors, including product mix, the Company's ability to obtain or maintain design wins, market conditions generally and in the electronics and semiconductor industries, product development schedules, competition and other matters. Readers are encouraged to refer to "Factors Affecting Earnings and Stock Price" found below in this Item 2.

From the Company's inception through 1998, the Company's principal segments had been desktop and mobile core logic. However, with increasingly aggressive competition in this area, the Company revised its strategy and focus on market opportunities where the Company had advantages. This led the Company to focus on the embedded and USB controller marketplaces where the Company has experienced limited success in the past several years.

The Net revenues for the second quarter ended June 30, 2001 were \$1,655,000, as compared to, net revenues of \$3,324,000 for the quarter ended June 30, 2000. For the six month periods ended June 30, 2001 and 2000, the Company reported net revenues of \$3,772,000 and \$18,678,000, respectively. Net revenues for the six months ended June 30, 2000, included net license revenues of \$13,311,000 resulting from a one-time non-exclusive licensing fee for certain OPTi patents. The decrease in net product sales for the three month and six month periods ending June 30, 2001, as compared to the three month and six month periods ending June 30, 2000, was due primarily to decreased sales of the Company's core logic chipsets used in various embedded designs and a slow down in the add-in marketplace for peripheral personal computer devices, such as the Company's USB controller chip. The Company anticipates that its net revenue for the second half of 2001 will continue to decline from its current levels.

Cost of product sales for the quarter ended June 30, 2001 decreased to \$956,000 resulting in a gross margin of approximately 42.2%, as compared to cost of sales of \$2,303,000, and a product gross margin of approximately 30.7% for the quarter ended June 30, 2000. Cost of sales for the first six months of 2001 was \$2,130,000, which resulted in a gross margin of approximately 43.5%, as compared with cost of sales of \$3,696,000, and a gross margin of approximately 31.1%, for product sales, for the six months ended June 30, 2000. The Company's actual gross margin for the six months ended June 30, 2000 was 80.2%, including the license revenue of \$13.3 million, which had no associated cost of goods sold. The increase in product gross margin as a percentage of sales for the three-month and six month periods ended June 30, 2001 as compared to the similar periods ended June 30, 2000 is primarily due to product mix and a reduction in assembly and test costs that the Company was able to negotiate during the first quarter of 2001.

Research and development costs increased to \$285,000 for the quarter ended June 30, 2001, as compared with \$112,000 for the quarter ended June 30, 2000. For the first six months of 2001 research and development costs were \$386,000 as compared to \$431,000 for the comparable period of 2000. The increase in research and development costs for the second quarter of 2001 as compared to the second quarter of 2000, was primarily due to outside contractor expenses for new product development during the period. As of June 30, 2001, the Company had one research and development person, who conducts virtually all of the Company's product development with outside contractors.

Selling, general, and administrative costs were \$801,000 in the quarter ended June 30, 2001 as compared with \$3,914,000 in the comparable period of 2000, and \$1,637,000 for the first six months of 2001 as compared to \$5,224,000, for the first six months of 2000. The decrease in selling, general, and administrative costs for the three-month and six month periods ended June 30, 2001 as compared to the three-month and six month periods

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ending June 30, 2000 is primarily attributable to lower headcount related expenses and lower legal expenses during the period. Selling, general and administrative expenses for the period ended June 30, 2000 included approximately \$3,000,000 resulting from additional costs incurred in settling the Crystal Semiconductor litigation.

Interest and other income, net was \$436,000 and \$519,000 for the quarters ended June 30, 2001 and 2000, respectively. Interest and other income, net for the six month periods ended June 30, 2001 and 2000, was \$884,000 and \$1,023,000, respectively. The decrease in the three and six month periods ended June 30, 2001 as compared to the three and six month periods ended June 30, 2000 is primarily due to a lower average cash balance due to the payment of \$7,000,000 during the second half of 2000 as settlement of the Crystal Semiconductor litigation.

The Company recorded a tax provision of approximately 4% for the quarter ended June 30, 2001. For the six months periods ended June 30, 2001 and 2000, the Company recorded a tax provision of approximately 2% and 3%, respectively. The Company's effective tax rate differed from the federal statutory rates during 2001 and 2000 primarily due to the utilization of prior year tax losses carried forward, federal alternative minimum taxes and foreign taxes.

Liquidity and Capital Resources

Cash, cash equivalents, and short-term investments decreased to \$48,228,000 at June 30, 2001 from \$58,126,000 at December 31, 2000. The decline in cash, cash equivalents and short-term investments of approximately \$9.9 million from December 31, 2000 to June 30, 2001, primarily relates to the decrease in value of the Company's investment in Tripath Technologies. The investment in Tripath Technologies, net of accrued taxes, decreased by approximately \$9.2 million during that period. Working capital as of June 30, 2001 decreased to \$48,163,000 from \$56,950,000 at December 31, 2000. This decrease also relates primarily to the decrease in the value of the Tripath Technologies investment. As of July 31, 2001, the fair market value of the Company's investment in Tripath Technologies has decreased by approximately \$14.2 million due to declines in the trading price of Tripath stock. During the first six months of 2001, operating activities generated approximately \$0.8 million of cash. Cash generated from operating activities was primarily due to a \$0.8 million reduction in accounts receivable, \$0.8 million reduction in inventories and a \$0.5 million of net income, partially offset by, a \$1.1 million reduction in accounts payable and a \$0.5 million reduction in other current liabilities. Investing activities used \$0.8 million of cash during the first six months of 2001. This use in cash was due to net purchases of short term investments of \$0.7 million and the purchase of \$0.1 million of property and equipment. Financing activities for the first six months of 2001 used \$0.1 million due to the stock repurchase program announced by the Company in December 2000.

At June 30, 2001, the Company's principal sources of liquidity included cash, cash equivalents and short-term investments of approximately \$48.2 million. The Company believes that its existing sources of liquidity will satisfy the Company's projected working capital and other cash requirements through at least the next twelve months.

Investigation of Strategic Alternatives

With respect to future plans of the Company, management is currently looking into all strategic alternatives in order to maximize shareholder value. The Company is unable to elaborate further but is hopeful that it can announce something further in August of 2001. However, there can be no assurance that such strategic alternatives will be determined by that time or at all.

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Factors Affecting Earnings and Stock Price

Fluctuations in Operating Results

The Company has experienced significant fluctuations in its quarterly operating results in the past and expects that it will experience such fluctuations in the future. In the past, these fluctuations have been caused by a variety of factors including increased competition from other suppliers, price competition, ongoing rapid price declines, changes in customer demand, the timing of delivery of new products, inventory adjustments, changes in the availability of foundry capacity and changes in the mix of products sold. In the future, the Company's operating results in any given period may be adversely affected by one or more of these factors.

Price Competition

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The market for the Company's products are subject to severe price competition and price declines. There can be no assurance that the Company will succeed in reducing its product costs rapidly enough to maintain or increase its gross margin level or that further substantial reduction in prices will not result in lower profitability or losses.

Changes in Customer Demand

The Company currently places non-cancelable orders to purchase products from independent foundries, while its customers generally place purchase orders with a significantly shorter lead time which may be canceled without significant penalty. In the past, the Company has experienced order cancellations and deferrals and expects that it will experience cancellations in the future from time to time. Any such order cancellations, deferrals, or a shortfall in a receipt of orders, as compared to order levels expected by the Company, could have a significant adverse effect on the Company's operating results in any given period.

Product Transitions and the Timing and Delivery of New Products

A substantial majority of the Company's net product sales is derived from its USB controller products. The market for USB controllers is characterized by frequent transitions in which this functionality can be and is incorporated into other semiconductor devices, such as the core logic. A failure to develop products with required feature sets or performance standards or a delay as short as a few months in bringing a new product to market could significantly reduce the Company's net sales for a substantial period, which would have a material adverse effect on the Company's business, financial condition and results of operations.

Continued Sales of Current Products

The Company's ability to maintain or increase its sales levels and profitability depends directly on its ability to continue to sell its existing products at current volumes. The Company will have few, if any, new product introductions for the foreseeable future. Any inability to continue sales at the current level could have an immediate and very significant adverse effect on the trading price of the Company's stock. Investors in the Company's securities must be willing to bear the risks of such fluctuations.

Each of the product segments in which the Company offers products are intensely competitive and the Company must compete with entrenched competitors who have

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established greater product breadth and distribution channels. The introduction of new products can result in a greater than expected decline and demand for existing products and create an imbalance between products ordered by customers and products which the Company has in inventory. This imbalance can result in surplus or obsolete inventory, leading to write-offs or other unanticipated costs or disruptions.

Customer Concentration

The Company primarily sells product to PC, motherboard, and add-in card manufacturers. The Company performs ongoing credit evaluations of its customers but does not require collateral. The Company maintains reserves for potential credit losses, and such losses have been within management's expectations. The Company expects that sales of its products to a relatively small group of customers will continue to account for a high percentage of its net product sales in the foreseeable future, although the Company's customers in any one period will continue to change.

However, there can be no assurance that any of these customers or any of the Company's other customers will continue to utilize the Company's products at current levels, if at all. The Company has experienced significant changes in the composition of its major customer base and expects that this variability will continue in the future. During 1999 and 1998 both Compaq and its subcontractors and Apple and its subcontractors were significant customers. At this time the Company is not shipping any products to either Compaq and its subcontractors or Apple and its subcontractors. The loss of any major customer or any reduction in orders by any such customer could have a material adverse effect on the Company's business, financial condition and results of operations.

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The Company has no long-term volume commitments from any of its major customers and generally enters into individual purchase orders with its customers. The Company has experienced cancellations of orders and fluctuations in order levels from period to period and expects it will continue to experience such cancellations and fluctuations in the future. Customer purchase orders may be cancelled and order volume levels can be changed or delayed with limited or no penalties. The replacement of cancelled, delayed or reduced purchase orders with new business cannot be assured. Moreover, the Company's business, financial condition and results of operations will depend in significant part on its ability to obtain orders from new customers, as well as on the financial condition and success of its customers. Therefore, any adverse factors affecting any of the Company's customers or their customers could have a material effect on the Company's business, financial condition and results of operation.

Credit Risks

Many of the Company's customers, particularly the motherboard manufacturers in Taiwan, operate at very low profit margins and undertake significant inventory risks. To the extent the Company provides open terms of credit to some of the larger of these customers, the Company is exposed to significant credit risks if these customers are unable to remain profitable. Approximately 40% of the Company's receivables at June 30, 2001 were with these customers.

Dependence on Foundries and Manufacturing Capacity

Almost all of the Company's products are manufactured by outside foundries pursuant to designs provided by the Company. In most instances, the Company provides foundries with a custom-tooled design ("Custom Production"), whereby the Company receives a finished die from the foundry which it sends to a third party for cutting and packaging. This process subjects the Company to the risk

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of low production yields as the die moves through the production and packaging process. The Company's reliance on independent foundries, packaging houses, and test houses involves several risks, including the absence of adequate capacity, the unavailability of or interruptions in access to certain process technologies and reduced control over delivery schedules, manufacturing yields and costs. At times during the second half of 1999 and the first three quarters of 2000, the Company was unable to meet the demand for certain of its products due to limited foundry capacity and the Company expects that it will experience other production shortfalls or difficulties in the future.

Because the Company's purchase orders with its outside foundries are non-cancelable by OPTi, the Company is subject to risks of, and has in the past experienced, excess or obsolete inventory due to an unexpected reduction in demand for a particular product. The manufacture of its products is a complex process and the Company may experience short-term difficulties in obtaining timely deliveries, which could affect the Company's ability to meet customer demand for its products. Should any of its major suppliers be unable or unwilling to continue to manufacture the Company's key products in required volumes, the Company would have to identify and qualify acceptable additional foundries. This qualification process could take up to six months or longer. No assurances can be given that any additional sources of supply could be in a position to satisfy any of the Company's requirements on a timely basis. The semiconductor industry experiences cycles of under-capacity and over-capacity which have resulted in temporary shortages of products in high demand. Any such delivery problems in the future could materially and adversely affect the Company's operating results.

The use of Custom Production requires the Company to purchase wafers from the foundry instead of finished products. As a result, the Company is required to increase its inventories and maintain inventories of unfinished products at packaging and test houses. The Company is also dependent on these packaging houses and third party test houses for adequate capacity.

Dependence on Intellectual Property position

The success of the Company's current strategy of licensing its core logic technology can be affected by new developments in intellectual property law generally and with respect to semiconductor patents in particular and upon the Company's success in defending its patent position. It is difficult to predict developments and changes in

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intellectual property law and in advance, however such changes could have an adverse impact on the Company's ability to license its previously developed technology.

Possible Volatility of Stock Price

There can be no assurances as to the Company's operating results in any given period. The Company expects that the trading price of its common stock will continue to be subject to significant volatility.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Interest Rate Sensitivity

We maintain our cash and cash equivalents primarily in money market funds. We do not have any derivative financial instruments. As of June 30, 2001, all of our debt investments mature in less than six months. Accordingly, we do not believe that our debt investments have significant exposure to interest rate

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risk.

We maintain an investment in the common shares of Tripath Technology, Inc. This investment is not hedged and is subject to extreme volatility. Assuming a hypothetical 75% adverse change in market prices, this investment would decrease in value by \$12.7 million, based on the value of this investment as of June 30, 2001. This estimate is not necessarily indicative of future performance, and actual results may differ materially.

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OPTi Inc.

Part II. Other Information

Item 1. Legal Proceedings.

See note 8 of Notes to Condensed Consolidated Financial Statements on page 9 of this report.

Item 2. Changes in Securities.

Not applicable and has been omitted.

Item 3. Defaults on Senior Securities.

Not applicable and has been omitted.

Item 4. Submission of Matters to a Vote of Shareholders.

Not applicable and has been omitted.

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits:

None

(b) Reports on Form 8-K:

None.

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OPTi Inc.

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

OPTi Inc.

Date: 8/6/01

By: \s\ Michael Mazzoni

Michael Mazzoni

Signing on behalf of the Registrant and as
Chief Financial Officer

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