

UTSTARCOM INC
Form 10-Q
May 11, 2001

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2001.

OR

☐ **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 000-29661

UTSTARCOM, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE

(State of Incorporation)

52-1782500

(I.R.S. Employer Identification No.)

**1275 HARBOR BAY PARKWAY,
ALAMEDA, CALIFORNIA**

(Address of principal executive offices)

94502

(zip code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: **(510) 864-8800**

Indicate by check mark whether the Registrant (1) has filed all reports required 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 ☐

As of April 27, 2001, there were 96,578,995 shares of the Registrant's Common Stock outstanding, par value \$0.00125.

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PART I FINANCIAL INFORMATION

ITEM 1 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UTSTARCOM, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)
(in thousands, except per share data)

| | <u>March 31, 2001</u> | <u>December 31, 2000</u> |
|---|---------------------------|------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 175,535 | \$ 149,112 |
| Short-term investments | 32,949 | 83,858 |
| Accounts receivable, net of allowances for doubtful accounts of \$13,629 and \$12,835 at March 31, 2001 and December 31, 2000, respectively | 169,708 | 161,330 |
| Receivable from related parties | 857 | 406 |
| Inventories | 153,142 | 118,995 |

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| | March 31, 2001 | December 31, 2000 |
|---|-------------------|----------------------|
| Other current assets | 36,399 | 17,674 |
| Total current assets | 568,590 | 531,375 |
| Property, plant and equipment, net | 28,494 | 21,999 |
| Long-term investments | 13,132 | 12,397 |
| Goodwill and intangible assets, net | 27,975 | 20,238 |
| Other long term assets | 3,863 | 5,828 |
| Total assets | \$ 642,054 | \$ 591,837 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 39,937 | \$ 44,564 |
| Debt | 55,427 | 43,381 |
| Amounts payable to related parties | 1,335 | |
| Income taxes payable | 5,026 | 7,170 |
| Deferred revenue | 43,989 | 31,678 |
| Other current liabilities | 38,984 | 34,721 |
| Total current liabilities | 184,698 | 161,514 |
| Long-term liabilities | 22,748 | 12,048 |
| Minority interest in consolidated subsidiaries | 5,844 | 5,956 |
| Total liabilities | 213,290 | 179,518 |
| Stockholders' equity: | | |
| Common stock: \$.00125 par value; authorized: 250,000,000 shares; issued and outstanding: 95,872,924 at March 31, 2001 and 95,032,657 at December 31, 2000 | 122 | 120 |
| Additional paid-in capital | 432,207 | 426,665 |
| Deferred stock compensation | (5,129) | (6,491) |
| Retained earnings (cumulative deficit) | 1,554 | (7,808) |
| Notes receivable from shareholders | (292) | (314) |
| Other comprehensive income | 302 | 147 |
| Total stockholders' equity | 428,764 | 412,319 |
| Total liabilities and stockholders' equity | \$ 642,054 | \$ 591,837 |

See accompanying notes to condensed consolidated financial statements.

UTSTARCOM, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(In thousands, except per share data)

Three months ended
March 31,

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| | Three months ended March 31, | |
|--|---------------------------------|------------|
| | 2001 | 2000 |
| Net sales | \$ 119,181 | \$ 58,587 |
| Cost of sales | 77,768 | 37,974 |
| Gross profit | 41,413 | 20,613 |
| Operating expenses: | | |
| Selling, general and administrative expenses (includes stock compensation expense of \$681 and \$1,802) | 14,131 | 11,064 |
| Research and development expenses (includes stock compensation expense of \$578 and \$4,595) | 12,412 | 10,909 |
| Amortization of intangible assets | 1,471 | 1,223 |
| Total operating expenses | 28,014 | 23,196 |
| Operating income | 13,399 | (2,583) |
| Interest income | 2,350 | 1,354 |
| Interest expenses | (861) | (757) |
| Other income (expenses) | (1,037) | 175 |
| Equity in net loss of affiliated companies | (244) | (279) |
| Income (loss) before income taxes, minority interest and cumulative effect of change in accounting principle | 13,607 | (2,090) |
| Income tax expense | 3,652 | 918 |
| Income (loss) before minority interest | 9,955 | (3,008) |
| Minority interest in earnings of consolidated subsidiary | (593) | (261) |
| Income (loss) before cumulative effect of change in accounting principle | 9,362 | (3,269) |
| Cumulative effect of change in accounting principle | | (980) |
| Net income (loss) | \$ 9,362 | \$ (4,249) |
| Basic earnings (loss) per share: | | |
| Income (loss) before cumulative effect of change in accounting principle | 0.10 | (0.09) |
| Cumulative effect of change in accounting principle | | (0.03) |
| Net income (loss) per share | \$ 0.10 | \$ (0.12) |
| Diluted earnings (loss) per share: | | |
| Income (loss) before cumulative effect of change in accounting principle | 0.09 | (0.09) |
| Cumulative effect of change in accounting principle | | (0.03) |
| Net income (loss) per share | \$ 0.09 | \$ (0.12) |
| Weighted average shares used in per-share calculation: | | |
| Basic | 95,873 | 35,867 |
| Diluted | 104,262 | 35,867 |

Three months ended
March 31,

See accompanying notes to condensed consolidated financial statements.

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UTSTARCOM, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In thousands)

| | Three months ended | |
|--|--------------------|----------------|
| | March 31, 2001 | March 31, 2000 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income (loss) | \$ 9,362 | \$ (4,249) |
| Adjustments to reconcile net income (loss) to net cash used in operating activities: | | |
| Cumulative effect of change in accounting principle | | 980 |
| Depreciation and amortization | 3,293 | 2,040 |
| Net loss on sale of assets | 18 | 83 |
| Impairment of long-term investment | 1,000 | |
| Stock compensation expense | 1,272 | 6,430 |
| Increase in allowance for doubtful accounts | 794 | 1,819 |
| Increase in inventory reserve | 1,674 | 800 |
| Equity in net loss of affiliated companies | 244 | 279 |
| Minority interest in earnings of consolidated subsidiary | 593 | 261 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable and receivable from related parties | (9,622) | (11,089) |
| Inventories | (35,822) | (23,769) |
| Other current and non-current assets | (18,461) | (9,975) |
| Accounts payable and payable to related party | (3,291) | (4,190) |
| Income taxes payable | 796 | (207) |
| Deferred revenue | 12,310 | 1,237 |
| Other current liabilities | 4,263 | 3,249 |
| Net cash used in operating activities | (31,577) | (36,301) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Additions to property, plant and equipment | (4,549) | (1,442) |
| Investment in affiliates, net of cash acquired | (1,979) | |
| Proceeds from disposal of property | 38 | 90 |
| Sales and (purchases) of short-term investments | 51,064 | (8,566) |
| Net cash provided by (used in) investing activities | 44,574 | (9,918) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Issuance of stock, net of expenses | 2,685 | 195,448 |
| Proceeds from borrowing, net | 10,711 | 25,059 |
| Proceeds from repayments of shareholder notes | 30 | 11 |

| | Three months ended | |
|--|--------------------|------------|
| | | |
| Net cash provided by financing activities | 13,426 | 220,518 |
| Net increase in cash and cash equivalents | 26,423 | 174,299 |
| Cash and cash equivalents at beginning of period | 149,112 | 87,364 |
| Cash and cash equivalents at end of period | \$ 175,535 | \$ 261,663 |

See accompanying notes to condensed consolidated financial statements.

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UTSTARCOM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

SIGNIFICANT ACCOUNTING POLICIES

1. BASIS OF PRESENTATION:

The accompanying unaudited condensed consolidated financial statements include the accounts of UTStarcom, Inc. (the "Company") and its wholly and majority (over 50 percent) owned subsidiaries, except for the Guangdong manufacturing subsidiary ("GUTS") which is accounted for using the equity method as the Company does not have voting control over all significant matters. All significant intercompany accounts and transactions have been eliminated in preparation of the consolidated financial statements. Minority interest in consolidated subsidiaries and equity in affiliated companies are shown separately in the consolidated financial statements. Investments in affiliated companies, of which none represent greater than 10 percent ownership, are accounted for using the cost method.

The accompanying financial data as of March 31, 2001 and for the three months ended March 31, 2001 and March 31, 2000, have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The December 31, 2000 balance sheet was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles. These condensed consolidated financial statements should be read in conjunction with the Company's audited December 31, 2000 financial statements including the notes thereto, and the other information set forth therein included in the Company's Annual Report on Form 10K/A.

In the opinion of management, the accompanying condensed consolidated financial statements reflect all adjustments (consisting of only normal recurring adjustments) considered necessary for a fair presentation of the Company's financial condition, the results of its operations and its cash flows for the periods indicated. The results of operations for the three months ended March 31, 2001 are not necessarily indicative of the operating results for the full year.

2. REVENUE RECOGNITION

Revenue from sales of equipment is recognized on delivery when contractual obligations are substantially complete, remaining obligations are inconsequential and perfunctory, and collection of the resulting receivable is reasonably assured. Revenue recognition from equipment sales with installations are recognized on final acceptance when contractual obligations are substantially complete, remaining obligations are inconsequential and perfunctory, and collection of the resulting receivable is reasonably assured. Where multiple elements exist, revenue is allocated to the different elements based upon verifiable objective evidence and recognized on completion of the element.

3. ACCOUNTING CHANGE (in thousands):

Effective January 1, 2000, the Company adopted Staff Accounting Bulletin 101 ("SAB 101") issued by the Securities and Exchange Commission in December 1999. As a result of adopting SAB 101, the Company changed the way it recognizes revenue in certain contracts that had previously led to revenue being recognized as contract stages were completed and accepted. The Company changed its method of revenue recognition to the point of contractual final acceptance for these contracts. In addition, certain contracts include service requirements for which revenue was previously recognized, and costs accrued, on contractual acceptance. In consideration of SAB 101, revenues associated with these service requirements are being deferred until the service obligations are completed. The Company recorded a cumulative adjustment of \$980 for

the effect of the change on prior years in first quarter fiscal 2000.

No revenue was recognized in the three months ended March 31, 2001 that was included in the cumulative effect of change in accounting principle. The combined impact of the cumulative adjustment and the retroactive adjustment resulted in a reduction in net income of \$286 or \$0.01 per share for the three months ended March 31, 2000.

4. EARNINGS (LOSS) PER SHARE (in thousands, except per share data):

Basic earnings (loss) per share is computed by dividing net income or loss applicable to common stockholders by the weighted average number of shares of the Company's common stock outstanding during the period. Diluted earnings (loss) per share is determined in the same manner as basic earnings (loss) per share except that the numbers of shares is increased by potentially dilutive common shares outstanding during the period. Potentially dilutive common shares consist of employee stock options, warrants and restricted stock. Dilutive potential shares are not included during periods when the Company experienced a net loss, as the impact would be anti-dilutive.

The following table presents the calculation of basic and diluted earnings (loss) per share:

| | Three Months Ended | |
|--|--------------------|----------------|
| | March 31, 2001 | March 31, 2000 |
| Numerator: | | |
| Income (loss) before cumulative effect of a change in accounting principle | \$ 9,362 | \$ (3,269) |
| Cumulative effect of a change in accounting principle | | (980) |
| Net income (loss) | \$ 9,362 | \$ (4,249) |
| Denominator: | | |
| Weighted average shares outstanding basic | 95,873 | 35,867 |
| Weighted average shares outstanding diluted | 104,262 | 35,867 |
| Basic earnings (loss) per share: | | |
| Income (loss) before cumulative effect of a change in accounting principle | \$ 0.10 | \$ (0.09) |
| Cumulative effect of a change in accounting principle | \$ | \$ (0.03) |
| Net income (loss) per share | \$ 0.10 | \$ (0.12) |
| Diluted earnings (loss) per share: | | |
| Income (loss) before cumulative effect of a change in accounting principle | \$ 0.09 | \$ (0.09) |
| Cumulative effect of a change in accounting principle | \$ | \$ (0.03) |
| Net income (loss) per share | \$ 0.09 | \$ (0.12) |

5. COMPREHENSIVE INCOME/(LOSS) (in thousands):

Statement of Financial Accounting Standards ("SFAS") No. 130 requires disclosure of total non-stockholder changes in equity, which include unrealized gains and losses on securities classified as available-for-sale under SFAS No. 115, foreign currency translation adjustments accounted for under SFAS No. 52, and minimum pension liability adjustments made pursuant to SFAS No. 87.

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The reconciliation of net income (loss) to comprehensive income (loss) for the three months ended March 31, 2001 and 2000 is as follows (in thousands):

| | Three Months Ended | |
|--|--------------------|----------------|
| | March 31, 2001 | March 31, 2000 |
| Net income (loss) | \$ 9,362 | \$ (4,249) |
| Cumulative translation adjustments | | 429 |
| Unrealized gains (losses) on investments | 155 | |
| Total comprehensive income (loss) | \$ 9,517 | \$ (3,820) |

6. SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION (in thousands):

| | Three Months Ended | |
|----------------------------------|--------------------|----------------|
| | March 31, 2001 | March 31, 2000 |
| Cash paid during the period for: | | |
| Interest | \$ 802 | \$ 725 |
| Income taxes | \$ 3,141 | \$ 1,240 |

Non-cash investing and financing activities were as follows:

| | Three Months Ended | |
|--|--------------------|----------------|
| | March 31, 2001 | March 31, 2000 |
| Unrealized foreign exchange gain | \$ | \$ 429 |
| Non-qualified stock option exercise tax benefits | \$ 2,940 | \$ 4,376 |
| Liability to issue common stock in conjunction with an acquisition | \$ 10,700 | \$ |
| Liability arising in conjunction with an acquisition | \$ 1,335 | \$ |

7. CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS (in thousands):

All of the Company's cash equivalents and short-term investments are classified as available-for-sale. At March 31, 2001, \$92,752 of available-for-sale securities was included in cash equivalents and \$32,949 of available-for-sale securities was included in short-term investments. These available-for-sale securities consisted of government sponsored entities' notes, commercial paper, floating rate corporate bonds and fixed income corporate bonds.

8. INVENTORIES (in thousands):

Inventories as of March 31, 2001 and December 31, 2000 consist of the following:

| | March 31, 2001 | December 31, 2000 |
|---------------------------------------|----------------|-------------------|
| Raw materials | \$ 51,563 | \$ 41,876 |
| Work-in-process | 31,032 | 23,432 |
| Finished goods | 81,423 | 62,888 |
| | \$ 164,018 | \$ 128,196 |
| Less allowance for obsolete inventory | (10,876) | (9,201) |
| | \$ 153,142 | \$ 118,995 |

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9. DEBT (in thousands):

The following represents the outstanding borrowings at March 31, 2001 and December 31, 2000:

| Note | Rate | Maturity | March 31, 2001 | December 31, 2000 |
|---|---------------------|---------------------|----------------|-------------------|
| Bank of China (1) | From 5.56% to 5.85% | From 05/01 to 03/02 | \$ 38,554 | \$ 28,917 |
| China Merchants Bank (2) | 6.44% | 03/02 | 6,024 | 3,614 |
| Commercial Bank of Hangzhou (3) | 6.21% | 06/10 | 12,048 | 12,048 |
| Industrial & Commercial Bank of China (4) | 5.85% | 05/01 | 6,024 | 6,024 |
| China Construction Bank (5) | 6.44% | 06/01 | 4,819 | 4,819 |
| Other | Various | Various | 6 | 7 |
| Total debt | | | \$ 67,475 | \$ 55,429 |
| Long-term bank borrowings | | | 12,048 | 12,048 |
| Short-term bank borrowings | | | \$ 55,427 | \$ 43,381 |

- (1) Guaranteed by the Company and the minority shareholder of HUTS. This represents drawings on the Company's line of credit with the bank. This line allows for borrowings of up to \$108,433.
- (2) Guaranteed by HUTS. This line allows for borrowings of up to \$6,024 and matures in March 2002.
- (3) Guaranteed by UTStarcom-China. This line allows for borrowings of up to \$24,096 and matures in June 2010.
- (4) Guaranteed by HUTS. This line allows for borrowings of up to \$6,024 and matures in May 2001.
- (5) Guaranteed by HUTS. This line allows for borrowings of up to \$4,819 and matures in June 2001.

10. ACQUISITIONS (in thousands):

On July 24, 2000, the Company entered into an agreement with Stable Gain International Ltd. ("Stable Gain") to purchase intellectual property and certain related fixed assets, and to transfer development employees to the Company for \$10,700. The terms of the purchase agreement provide that the Company will pay Stable Gain consideration of \$10,700 in the form of common stock of the Company, provided certain government approvals and other deliverables, as defined in the agreement, are obtained within twelve months. The final approvals were obtained in March 2001, and the transfer of the common stock is expected to be completed in the second quarter of fiscal 2001. At March 31, 2001, \$10,700 in respect of the purchase consideration is included in long-term liabilities. On August 18, 2000, the Company entered into a separate agreement to purchase certain related fixed assets for a total consideration of \$319. The total purchase consideration of \$11,019 was allocated to property and equipment, intangible assets and goodwill under the purchase method of accounting. Goodwill totaling \$7,449 was recorded on acquisition.

The following represents the allocation of the purchase price for Stable Gain:

| | |
|---|-----------|
| Fair value of net assets acquired | \$ 2,430 |
| Fair value of identified intangible assets | 1,140 |
| Excess of costs of acquiring Stable Gain over fair value of net assets acquired | 7,449 |
| | \$ 11,019 |

The Company, as part of its business operations in China, formed NST, a joint venture company with Zhejiang Nan Tian, and acquired a 65% holding. On February 5, 2001, the Company entered into an agreement to acquire the remaining 35% ownership in the joint venture company for a total consideration of \$1,335 payable in cash. The purchase price was allocated to property and equipment and goodwill under the purchase method of accounting. Goodwill totaling \$619 was recorded on acquisition. At March 31, 2001, the obligation in respect of the purchase consideration of \$1,335 is included in related party payables.

The following represents the allocation of the purchase price for NST:

| | | |
|---|----|-------|
| Fair value of net assets acquired | \$ | 716 |
| Excess of costs of acquiring NST over fair value of net assets acquired | | 619 |
| | \$ | 1,335 |

Had the acquisitions of Stable Gain and NST occurred on January 1, 2001, proforma net income for the three months ended March 31, 2001 would have been \$8,805 or \$0.09 per share basic, \$0.08 per share fully diluted. There was no impact on proforma revenues for the three months ended March 31, 2001. Proforma adjustments have been added to record the amortization of fixed assets, goodwill and other intangible assets as if the transaction occurred on January 1, 2001.

11. LONG TERM INVESTMENTS

During 2000, the Company formed a joint venture with SOFTBANK Corporation ("SOFTBANK") to invest \$100 million in Softbank China Holdings Pte. Ltd. ("Softbank China"), an investment fund. The Company's share in the joint venture was 10%. As of March 31, 2001, the Company had invested \$10 million in Softbank China. This fund focuses on investments in Internet companies in China. SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities" requires that a decline in value other than a temporary decline, be included in earnings. Based upon a review of the carrying value of the fund investments, the Company and SOFTBANK decided to write down the investment by approximately \$11 million of which \$1 million has been recognized as an impairment charge by the Company during the three months ended March 31, 2001, representing the Company's share in the joint venture.

12. SEGMENT REPORTING (in thousands):

The Company provides communications equipment through an integrated suite of network access systems, optical transmission products and subscriber terminal products. The Company primarily operates in two geographic areas, China and Other regions. Substantially all the Company's revenues are attributable from China. The chief operating decision makers evaluate performance, make operating decisions, and allocate resources based on consolidated financial data. Gross profit, operating income, income from operations, and income taxes are not allocated to specific individual departments within the organization. In accordance with SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information", the Company is considered a single reportable segment. We are required to disclose certain information about our product revenues, information about geographic areas, information about our major customers, and information about long-lived assets. Revenues from Shaoxing Telecommunications Bureau accounted for 14.0% of consolidated revenues during the three months ended March 31, 2001. Revenues from Hangzhou Telecommunications Bureau accounted for 39.6% of consolidated revenues during the three months ended March 31, 2000. Corporate assets consist of cash and cash equivalents, short- and long-term investments and deferred tax assets. As of March 31, 2001, \$346,197 or approximately 91.5% of non-corporate assets were located in China and \$32,106 or 8.5% of non-corporate assets were located in the United States. Corporate assets at March 31, 2001 were \$263,691. As of March 31, 2000, \$283,909 or approximately 90.4% of

non-corporate assets were located in China and \$29,951 or 9.5% of non-corporate assets were located in the United States. Corporate assets at March 31, 2000 were \$277,931.

Geographical area data and product data are as follows (in thousands):

| Three Months Ended March 31, 2001 | | | Three Months Ended March 31, 2000 | | |
|-----------------------------------|---------------------|-------|-----------------------------------|---------------------|-------|
| Communications Equipment | Subscriber Handsets | Total | Communications Equipment | Subscriber Handsets | Total |

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| | Three Months Ended March 31, 2001 | | | Three Months Ended March 31, 2000 | | |
|----------------|-----------------------------------|--------|-----------|-----------------------------------|-----------|-----------|
| Revenues: | | | | | | |
| China | \$ | 83,354 | \$ 33,424 | \$ 116,778 | \$ 42,940 | \$ 15,235 |
| Other | | 2,403 | | 2,403 | 412 | 412 |
| Total revenues | \$ | 85,757 | \$ 33,424 | \$ 119,181 | \$ 43,352 | \$ 15,235 |

Revenue attributable to North America was insignificant during the three months ended March 31, 2001 and March 31, 2000.

Long-lived assets are as follows (in thousands):

| | March 31, 2001 | December 31, 2000 |
|-------------------------|-------------------|----------------------|
| China | \$ 32,185 | \$ 17,855 |
| U.S. | 24,284 | 24,382 |
| Total long-lived assets | \$ 56,469 | \$ 42,237 |

13. RECENT ACCOUNTING PRONOUNCEMENTS:

In June 1998, the Financial Accounting Standards Board ("FASB") issued SFAS No. 133, "Accounting for Derivatives and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. In July 1999, the FASB issued SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133." SFAS No. 137 deferred the effective date of SFAS No. 133 until fiscal years beginning after June 15, 2000. The Company adopted SFAS No. 133 on January 1, 2001, and the adoption had no impact on the financial statements.

In September 2000, the FASB issued SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which revises the standards for accounting for securitizations and other transfers of financial assets and collateral and requires entities that have securitized financial assets to provide specific disclosures. SFAS 140 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. The Company adopted SFAS No. 140 on January 1, 2001, and the adoption had no impact on the financial statements.

14. COUNTRY RISKS:

Almost 98% of the Company's sales for the three months ended March 31, 2001 were made in China. Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environment in China, and by the general state of China's economy. The Company's operations in China are subject to special considerations and significant risks not typically associated with companies in the United States. These include risks associated with, among others, the political, economic and legal environments and foreign currency exchange. The Company's results may be adversely affected by, among other things, changes in the political, economic and social conditions in China, and by changes in governmental policies with respect

to laws and regulations, changes in China's telecommunications industry and regulatory rules and policies, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation.

Beginning in January 1, 1999, China's government required that all manufacturers of telecommunications equipment connected to public or private telecommunications networks within China obtain a network access license for each of its products. Sellers are prohibited from selling or advertising for sale equipment for which its manufacturer has not obtained a network access license and may be liable for penalties in an amount up to three times earnings from the sale of any equipment sold beginning January 1, 1999 without a license. Failure to obtain the required licenses could permit the authorities to force the Company to remove previously installed equipment and could preclude the Company from making further sales of the unlicensed products in China, which would substantially harm the Company's business.

In June 2000, the Ministry of Information Industry issued an internal notice concluding its review of PHS-based equipment. The Company's PAS system will continue to be allowed in China's county-level cities and counties, which are the Company's primary markets for the Company's PAS system. In large and medium-sized cities, the Company's PAS system may be used on a limited basis where there is a high concentration of population, such as campuses, commercial buildings and special development zones. New citywide PAS system deployments will not be allowed in large and medium-size cities. The evaluation group for access networks under the Ministry of Information Industry has recommended that the Ministry of Information Industry issue a license for the Company's PAS system. However, the Company does not yet have this network access license and the Company cannot provide any assurance that such a license will be issued for the Company's PAS system. In addition, there is no assurance that the Ministry of Information Industry will not conduct any further review/evaluation of PHS-based equipment or change its order regarding PHS-based system in the future. Management has also applied for network access licenses for other products, which the Company is no longer manufacturing but had previously sold. However, the Company has not yet received these access licenses and has no any assurance that a license will be issued. Management believes that no penalties or fines will be payable for non-compliance with the licensing requirements for both the PAS system and other products and that there will be no adverse effect on the Company's business or financial condition.

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This Report on Form 10-Q contains forward-looking statements within the meaning of the federal securities laws. These statements include those concerning the following: our expectation regarding continued growth in our business and operations; our expectation that our PAS network access system will continue to be allowed in China's county-level cities and counties; our expectation that there will be fluctuations in our overall gross profit, gross margin, product mix and selling prices; our plans for expanding the direct sales organization and our selling and marketing campaigns and activities; our expectation that we will build additional manufacturing facilities, most likely in China; our expectation that there will be increases in selling, marketing, research and development, general and administrative expenses; our expectation that we will continue to invest significantly in research and development; our expectation that we will fill the majority of its current backlog orders; our expectation regarding our future investments; our expectation that we will develop the capacity to manufacture our own handsets; and our expectation that existing cash and cash equivalents will be sufficient to finance the Company's operations for at least the next 12 months. These statements are subject to risks and uncertainties that may cause actual results and events to differ materially. For a detailed discussion of these risks and uncertainties, see the "Factors Affecting Future Operating Results" section of this Form 10-Q. UTStarcom undertakes no obligation to update the forward-looking statements to reflect events or circumstances occurring after the date of this Form 10-Q.

OVERVIEW

We provide communications equipment including network access systems, optical transmission products and subscriber terminal products for service providers that operate wireless and wireline networks. Our operations are conducted primarily by our foreign subsidiaries that manufacture, distribute, and support our products in international markets, principally the People's Republic of China ("China").

We provide communications equipment for service providers that operate wireless and wireline networks in rapidly growing communications markets. To date, substantially all of our sales have been to service providers in Mainland China. Our integrated suite of network access systems, optical transmission products and subscriber terminal products allows service providers to offer efficient and expandable voice, data and Internet access services. Because our systems are based on key international communications standards, service providers can easily integrate our systems into their existing networks and deploy our systems in new broadband, Internet Protocol ("IP"), and wireless network rollouts.

On March 3, 2000, we sold 11,500,000 shares of common stock, which included the underwriters' over-allotment option, at \$18.00 per share. The sale of the shares of common stock generated aggregate gross proceeds of approximately \$207.0 million. The aggregate net proceeds were approximately \$189.4 million, after deducting underwriting discounts and commissions and related expenses. The net proceeds may be used for general corporate purposes, including working capital and capital expenditures. A portion of the net proceeds may also be used to acquire or invest in complementary businesses, technologies or product offerings; however, there are no current material agreements or commitments with respect to any such activities. As of March 31, 2001 the Company has not used any of the net proceeds and the entire amount of net proceeds remains in our cash and cash equivalents and short-term investments accounts.

To date, we have derived substantially all of our revenues from sales of communications equipment to service providers in China. Each of the Telecommunication Bureaus to whom we sell our equipment in China is part of the China Telecom system and subject to its ultimate control. However, equipment

purchasing decisions are generally made at the individual Telecommunications Bureau level. Our customers often make a large initial purchase of our equipment followed by supplemental purchases of enhancements and upgrades. As a result, our largest revenue-producing customers typically vary from period-to-period.

Almost 98% of our sales for the three months ended March 31, 2001 were made in China. Accordingly, our business, financial condition and results of operations may be influenced by the political, economic and legal environment in China, and by the general state of China's economy. Our operations in China are subject to special considerations and significant risks not typically associated with companies in the United States. These include risks associated with, among others, the political, economic and legal environments and foreign currency exchange. Our results may be adversely affected by, among other things, changes in the political, economic and social conditions in China, and by changes in governmental policies with respect to laws and regulations, changes in China's telecommunications industry and regulatory rules and policies, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation.

Specifically, remittances from China, which are of a capital nature, such as the repayment of bank loans denominated in foreign currencies, require approval from appropriate governmental authorities before Renminbi can be used to purchase foreign currency. Although the payment of cash dividends is permitted so long as our subsidiaries have sufficient reserves and adequate amounts of Renminbi to purchase foreign currency, regulations restrict the ability of our subsidiaries to transfer funds to us through intercompany loans and advances.

We sell our products in China through a direct sales force. The evaluation period for our products may span a year or more. Revenue from sales of equipment is recognized on delivery when contractual obligations are substantially complete, remaining obligations are inconsequential and perfunctory, and collection of the resulting receivable is reasonably assured. Revenue recognition from equipment sales with installations are recognized on final acceptance when contractual obligations are substantially complete, remaining obligations are inconsequential and perfunctory, and collection of the resulting receivable is reasonably assured. Where multiple elements exist, revenue is allocated to the different elements based upon verifiable objective evidence and recognized on completion of the element.

Cost of sales consists primarily of material costs, third party commissions, costs associated with assembly and testing of products, costs associated with installation and customer training and overhead and warranty costs. Cost of sales also includes import taxes on components.

Our gross profit has been affected by material costs, product mix, average selling prices, and the type of distribution channel through which we sell our products. Our gross profit, as a percentage of net sales, varies among our product families. The gross profits, as a percentage of net sales, on our mobile phone handsets are very low. We expect that our overall gross profit, as a percentage of net sales, will fluctuate from period to period as a result of shifts in product mix, anticipated decreases in average selling prices and our ability to reduce product costs.

Selling, general and administrative expenses include compensation and benefits, professional fees, sales commissions, provision for uncollectible accounts receivable and travel and entertainment costs. We intend to pursue aggressive selling and marketing campaigns and to expand our direct sales organization and, as a result, our sales and marketing expenses will increase in future periods. We also expect that in support of our continued growth and our operations as a public company general and administrative expenses will continue to increase for the foreseeable future.

Research and development expenses consist primarily of salaries and related costs of employees engaged in research, design and development activities, the cost of parts for prototypes, equipment depreciation and third party development expenses. We believe that continued investment in research

and development is critical to our long-term success. Accordingly, we expect that our research and development expenses will increase in future periods.

No net deferred compensation expense was recorded during the three months ended March 31, 2001 in connection with the grant of stock options to employees. We recorded net deferred compensation of \$3.6 million during the three months ended March 31, 2000, representing the difference between the deemed fair value of common stock for accounting purposes and the option exercise price for these options at the date of grant. Deferred compensation is presented as a reduction of stockholders' equity, with amortization recorded over the vesting period of the option, which is generally four years. We recorded stock compensation expense of approximately \$1.3 million during the three months ended March 31, 2001 and \$6.4 million during the three months ended March 31, 2000. At March 31, 2001, approximately \$5.1 million remained to be amortized.

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Amortization of intangible assets consists primarily of the amortization of intangible assets associated with acquisitions in China, the acquisition of the minority interest in Wacos, Inc. and the acquisition of Stable Gain International Ltd. ("Stable Gain").

Consolidated equity in net income (loss) of affiliated companies comprises our share of the earnings from our Guangdong manufacturing subsidiary, which is accounted for using the equity method, as we do not have voting control over all significant matter.

Under current regulations in China, foreign investment enterprises that have been accredited as technologically advanced enterprises are entitled to additional tax incentives. These tax incentives vary in different locales and could include preferential national enterprise income tax treatment at 50% of the usual rates for different periods of time. All of our active subsidiaries in China were accredited as technologically advanced enterprises.

Minority interest in (earnings) loss of consolidated subsidiaries represents the share of earnings in our Zhejiang manufacturing joint venture that is owned by our subsidiary partner.

RECENT DEVELOPMENTS

On July 24, 2000, we entered into an agreement with Stable Gain to purchase intellectual property and certain related fixed assets, and to transfer development employees to our company for \$10.7 million. The terms of the purchase agreement provide that we will pay Stable Gain consideration of \$10.7 million in the form of common stock, provided certain government approvals and other deliverables, as defined in the agreement, are obtained within twelve months. The final approvals were obtained in March 2001, and the transfer of the common stock is expected to be completed in the second quarter of fiscal 2001. At March 31, 2001, the obligation in respect of the purchase consideration is included in long-term obligations. On August 18, 2000, we entered into a separate agreement to purchase certain related fixed assets for a total consideration of \$0.3 million. The total purchase consideration of \$11.0 million was allocated to property and equipment, intangible assets and goodwill under the purchase method of accounting. Goodwill totaling \$7.4 million was recorded on acquisition.

As part of our business operations in China, we formed a joint venture company named Hangzhou Nantian Starcom Telecommunication Equipment Ltd. ("NST") with Zhejiang Nan Tian and we acquired a 65% holding in February 1996. On February 5, 2001, we entered into an agreement to acquire the remaining 35% ownership in the joint venture company for a total consideration of \$1.3 million payable in cash. The purchase price was allocated to property and equipment and goodwill under the purchase method of accounting. Goodwill totaling \$0.6 million was recorded on acquisition. At March 31, 2001 the obligation in respect of the purchase consideration of \$1.3 million is included in related party payables.

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RESULTS OF OPERATIONS

QUARTERS ENDED MARCH 31, 2001 AND 2000

NET INCOME (LOSS)

For the three months ended March 31, 2001 we reported net income of \$9.4 million as compared to a net loss of \$4.2 million for the three months ended March 31, 2000.

NET SALES

Our net sales increased 103% to \$119.2 million for the three months ended March 31, 2001 from \$58.6 million for the corresponding period in 2000. Sales of communications equipment for the three months ended March 31, 2001 were \$85.8 million, an increase of \$42.4 million or 98%, as compared to the three months ended March 31, 2000. Sales of subscriber handsets for the three months ended were \$33.4 million, an increase of \$18.2 million or 120%, as compared to the three months ended March 31, 2000. Sales of communications equipment and sales of subscriber handsets increased due to the continued growth in spending on telecommunications infrastructure in China, as China continues to modernize its telecommunications infrastructure. For the three months ended March 31, 2001, sales to Shaoxing Telecommunications Bureau accounted for 14.0% of our net sales. For the three months ended March 31, 2000, sales to Hangzhou Telecommunications Bureau accounted for 39.6% of our net sales.

Effective January 1, 2000, we adopted Staff Accounting Bulletin 101 ("SAB 101") issued by the Securities and Exchange Commission in December 1999. As a result of adopting SAB 101, we changed the way we recognize revenue in certain contracts that had previously led to revenue being recognized as contract stages were completed and accepted. We changed our method of revenue recognition to the point of contractual final acceptance for these contracts. In addition, certain contracts include a service requirement for which revenue was previously

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recognized, and costs accrued, on contractual acceptance. In consideration of SAB 101, revenues associated with these service requirements are being deferred until the service obligations are completed. The Company recorded a cumulative adjustment of \$1.0 million for the effect of the change on prior years in first quarter fiscal 2000. No revenue was recognized in the three months ended March 31, 2001 that was included in the cumulative effect of change in accounting principle. The combined impact of the cumulative adjustment and the retroactive adjustment resulted in a reduction in net income of \$0.3 million or \$0.01 per share for the three months ended March 31, 2000.

GROSS PROFIT

Gross profit increased 101% to \$41.4 million for the three months ended March 31, 2001 from \$20.6 million for the corresponding period in 2000. Gross profit, as a percentage of net sales, decreased to 34.7% for the three months ended March 31, 2001 from 35.2% for the three months ended March 31, 2000. The decrease in gross profit, as a percentage of net sales, was primarily due to increases in sales of lower margin handsets, which comprised 28.0% of sales for the three months in 2001 compared to 26.0% in 2000.

SELLING, GENERAL AND ADMINISTRATIVE

Selling, general and administrative expenses increased 27.7% to \$14.1 million for the three months ended March 31, 2001 from \$11.1 million for the corresponding period in 2000. The increase in selling, general and administrative expenses was primarily due to increased sales and administrative personnel and related expenses, including sales commissions, associated with the growth in net sales and the expansion of our overall level of business activities. Selling, general and administrative expenses as a

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percentage of net sales decreased to 11.9% for the three months ended March 31, 2001 from 18.9% for the corresponding period in 2000. The decrease in selling, general and administrative expenses as a percentage of net sales were primarily due to economies of scale associated with the significant increases in net sales. We expect our selling, general and administrative expenses to increase in absolute dollar amounts in future periods as sales and marketing activities increase and we further invest in infrastructure and incur additional expenses related to anticipated growth of our business and operation as a publicly held company.

RESEARCH AND DEVELOPMENT

Research and development expenses increased 13.8% to \$12.4 million for the three months ended March 31, 2001 from \$10.9 million for the corresponding period in 2000. The increase in research and development expenses was primarily due to the hiring of additional technical personnel, increased prototype expenses and licensing fees to support our research and development efforts. As a percentage of net sales, research and development expenses decreased to 10.4% for the three months ended March 31, 2001 from 18.6% for the corresponding period in 2000, primarily due to the significant increases in net sales. We expect our research and development expenses to increase in absolute dollar amounts in future periods as we expand our research and development organization to support new product development.

AMORTIZATION OF INTANGIBLE ASSETS

Amortization of intangible assets was \$1.5 million for the three months ended March 31, 2001 and \$1.2 million for the three months ended March 31, 2000. The increase in amortization of intangible assets was due to amortization of additional goodwill that was recognized upon the acquisition of Stable Gain.

INTEREST INCOME (EXPENSES), NET

Net interest income was \$1.4 million for the three months ended March 31, 2001 and \$0.6 million for the corresponding period in 2000. The increase was primarily due to increased interest income from higher average cash balances as a result of the completion of our initial public offering in March 2000.

OTHER INCOME (EXPENSES), NET

Other income (expense) was \$(1.0) million for the three months ended March 31, 2001 and \$0.2 million for the corresponding period in 2000. The decrease was primarily due to an impairment charge of \$1.0 million relating to our investment in the Softbank China fund, based upon a review of the carrying value of this long-term investment.

EQUITY IN INCOME (LOSS) OF AFFILIATED COMPANIES

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Consolidated equity in the net loss of affiliated companies was \$0.2 million for the three months ended March 31, 2001 and consolidated equity in the net loss of affiliated companies was \$0.3 million for the corresponding period in 2000. The net loss at our Guangdong manufacturing subsidiary remained constant, as demand for its main product remained constant.

INCOME TAX EXPENSE

Income tax expense was \$3.7 million for the three months ended March 31, 2001 and \$0.9 million for the corresponding period in 2000. The increase in the income tax expense was due to our increasing income.

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MINORITY INTEREST IN EARNINGS OF CONSOLIDATED SUBSIDIARIES

Minority interest in earnings of consolidated subsidiaries was \$0.6 million for the three months ended March 31, 2001 and \$0.3 million for the corresponding period in 2000. The change between the two periods was primarily due to the increased profitability at our Zhejiang subsidiary.

LIQUIDITY AND CAPITAL RESOURCES

Prior to our initial public offering we financed our operations through the sales of preferred stock and, to a lesser extent, bank lines of credit. In November and December 1999, we secured private equity financing totaling \$55.0 million. In March 2000, we raised \$189.4 million in net proceeds from our initial public offering. We have available lines of credit totaling \$161.4 million as of March 31, 2001. As of March 31, 2001, total borrowings were \$67.5 million under these lines of credit, and of this amount, \$12.0 million is included in long-term debt. As of March 31, 2001, we had working capital of \$383.9 million, including \$175.5 million in cash and cash equivalents, \$32.9 million of short-term investments and \$55.4 million of Renminbi-denominated bank borrowings.

As of March 31, 2001, we had invested \$10.0 million in an investment fund established by SOFTBANK focused on investments in Internet companies in China. Our investment constitutes 10% of the funding for Softbank China, with SOFTBANK contributing the remaining 90%. We are a passive investor and have no decision-making authority with respect to investments by the fund. The fund has a separate management team, and none of our employees is employed by the fund. One of our directors serves as the Chief Executive Officer of the fund, and our Chief Executive Officer is the chairman of the board of the fund. We are not obligated to pay, nor do we receive, any fees in connection with services provided to the fund. We do not know what material fees will be paid to or by SOFTBANK or any other parties in connection with services provided to the fund. Many of the fund's investments will be in privately held companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky as the market for the technologies or products the companies have under development are typically in these early stages and may never materialize. During the three months ended March 31, 2001, based upon a review of the carrying value of this investment, an impairment charge of \$1.0 million was recognized to provide for the decline in the fair value below the carrying value of this investment. Due to the risky nature of these investments, we may experience further losses in connection with this investment in Softbank China.

Net cash used in operations for the three months ended March 31, 2001 was \$31.6 million, which was primarily due to an increase in inventories, accounts receivable and other current and non-current assets of \$34.1 million, \$8.8 million and \$18.5 million respectively, and a decrease in accounts payable of \$3.3 million. The uses of cash were partially offset by depreciation and amortization expense of \$3.3 million, amortization of deferred stock compensation expense of \$1.3 million, a long-term investment impairment charge of \$1.0 million, an increase in income taxes payable and other current liabilities of \$5.1 million and an increase in deferred revenue of \$12.3 million.

Net cash provided by investing activities for the three months ended March 31, 2001 of \$44.6 million was primarily due to sales and maturities of short-term investments of \$51.1 million, offset by the acquisition of property, plant and equipment of \$4.5 million, and investment in affiliates of \$2.0 million. Proceeds from sales and maturities of short-term investments were used to finance working capital requirements.

Net cash provided by financing activities for the three months ended March 31, 2001 of \$13.4 million was primarily due to net proceeds of \$10.7 million from borrowing under our lines of credit and \$2.7 million from the issuance of common stock through the exercise of stock options.

Our international sales are generally denominated in local currencies. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China.

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Although the impact of currency fluctuations to date has been insignificant, we cannot guarantee that fluctuations in currency exchange rates in the future will not have a material adverse effect on revenues from international sales and, correspondingly, on our business, financial condition and results of operations. We also have contracts negotiated in Japanese Yen for purchasing portions of our inventories and supplies. We have a multi-currency bank account in Japanese Yen for purchasing portions of our inventories and supplies. The balance of this Japanese Yen account as of March 31, 2001 is approximately \$7.0 million.

We believe that our existing cash and cash equivalents, short-term investments and cash from operations will be sufficient to finance our operations through at least the next 12 months. If additional financing is needed, there can be no assurance that such financing will be available to us on commercially reasonable terms, or at all.

FACTORS AFFECTING FUTURE OPERATING RESULTS:

OUR FUTURE SALES ARE UNPREDICTABLE, OUR OPERATING RESULTS ARE LIKELY TO FLUCTUATE FROM QUARTER TO QUARTER, AND IF WE FAIL TO MEET THE EXPECTATIONS OF SECURITIES ANALYSTS OR INVESTORS, OUR STOCK PRICE COULD DECLINE SIGNIFICANTLY

Our quarterly and annual operating results have fluctuated in the past and are likely to fluctuate in the future due to a variety of factors, some of which are outside of our control. As a result, period to period comparisons of our operating results are not necessarily meaningful or indicative of future performance. Furthermore, it is likely that in some future quarters our operating results will fall below the expectations of securities analysts or investors. If this occurs, the trading price of our common stock could decline.

Factors that may affect our future operating results include:

the timing, number and size of orders for our products, as well as the relative mix of orders for each of our products, particularly the volume of lower margin telephone handsets;

the evolving and unpredictable nature of the economic, regulatory and political environments in China and other countries in which we market or plan to market our products;

aggressive price reductions by our competitors;

currency fluctuations;

market acceptance of our products and product enhancements;

the lengthy and unpredictable sales cycles associated with sales of our products combined with the impact of this variability on our suppliers' ability to provide us with components on a timely basis; and

longer collection periods of accounts receivable in China and other countries.

The limited performance history of some of our products, our limited forecasting experience and processes and the emerging nature of our target markets make forecasting our future sales and operating results difficult. Our expense levels are based, in part, on our expectations regarding future sales, and these expenses are largely fixed, particularly in the short term. In addition, to enable us to promptly fill orders, we maintain inventories of finished goods, components and raw materials. As a result, we commit to considerable costs in advance of anticipated sales. In the past, a substantial portion of our sales in each quarter resulted from orders received and shipped in that quarter, and we have operated with a limited backlog of unfilled orders. Accordingly, we may not be able to reduce our costs in a timely manner to compensate for any unexpected shortfall between forecasted and actual

sales. Any significant shortfall of sales may require us to maintain higher levels of inventories of finished goods, components and raw materials than we require, thereby increasing our risk of inventory obsolescence and corresponding inventory write-downs and write-offs. Although we

have reserved against inventory obsolescence, we cannot guarantee that these reserves will be adequate to offset all write-downs or write-offs.

WE HAVE A HISTORY OF LOSSES

We sustained losses prior to the first quarter of fiscal 2001. At December 31, 2000, we had an accumulated deficit of \$7.8 million. As of March 31, 2001, we had retained earnings of approximately \$1.6 million. We anticipate continuing to incur significant sales and marketing, research and development and general and administrative expenses and, as a result, we will need to generate higher revenues to remain profitable. Numerous factors could negatively impact our results of operations, including a decrease in sales, price pressures and a fixed cost structure, which could limit our ability to respond to declining revenues. Although our sales have grown in recent quarters, our past results should not be relied on as indications of our future performance. We cannot assure you that we will be able to remain profitable in future periods.

COMPETITION IN OUR MARKETS MAY LEAD TO REDUCED PRICES, REVENUES AND MARKET SHARE

We face intense competition in our target markets and expect competition to increase. Our principal competitors in our various product lines include:

PAS: Lucent Technologies, Inc. and Zhongxing Telecommunications Equipment.

AN-2000: Advanced Fibre Communications, Inc.; Alcatel Alsthom CGE, S.A.; Huawei Technology Co., Ltd.; Lucent; NEC Corporation; and Zhongxing.

WACOS SYSTEM: Alcatel; Cisco Systems, Inc.; Clarent Corporation; Ericsson LM Telephone Co.; Huawei; Lucent; Motorola, Inc.; Nokia Corporation; Nortel Networks Corporation; Nuera Communications, Inc.; Siemens AG; and Vienna Systems Corp.

We are increasingly facing competition from domestic companies in China. We believe that our strongest competition in the future may come from these companies, many of which operate under lower cost structures and more favorable governmental policies and have much larger sales forces than we do. Furthermore, other companies not presently offering competing products may also enter our target markets. Many of our competitors have significantly greater financial, technical, product development, sales, marketing and other resources than we do. As a result, our competitors may be able to respond more quickly to new or emerging technologies and changes in service provider requirements. Our competitors may also be able to devote greater resources than we can to the development, promotion and sale of new products. These competitors may also be able to offer significant financing arrangements to service providers, in some cases facilitated by government policies, which is a competitive advantage in selling systems to service providers with limited financial and currency resources. Increased competition is likely to result in price reductions, reduced gross profit as a percentage of net sales and loss of market share, any one of which could materially harm our business, financial condition and results of operations.

Moreover, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties, including Telecommunications Administrations, Telecommunications Bureaus and other local organizations, to increase the ability of their products to address the needs of prospective customers in our target markets. Accordingly, alliances among competitors or between competitors and third parties may emerge and rapidly acquire significant market share. To remain competitive, we believe that we must continue to partner with

Telecommunications Administrations and other local organizations, maintain a high level of investment in research and development and in sales and marketing, and manufacture and deliver products to service providers on a timely basis and without significant defects. If we fail to meet any of these objectives, our business, financial condition and results of operations could be harmed.

The introduction of inexpensive wireless telephone service or other competitive services in China may also have an adverse impact on sales of our PAS system in China. We cannot assure you that we will be able to compete successfully against current or future competitors or that competitive pressures in the future will not materially adversely effect our business, financial condition and results of operations.

We believe that the principal competitive factors affecting the market for our network access products include:

total initial cost of solution;

short delivery and installation intervals;

design and installation support;

ease of integration with the backbone network;

flexibility in supporting multiple interfaces and services;

life-cycle cost determined by reliability; and

manageability of the solution and scalability.

We believe we have in the past generally competed favorably with offerings of our competitors on the basis of these factors. However, we may not be able to compete effectively against current and future competitors based on these or any other competitive factors in the future, and the failure to do so would have a material adverse effect on our business, financial condition and results of operations.

THE SUCCESS OF OUR BUSINESS DEPENDS ON A RELATIVELY SMALL NUMBER OF LARGE SYSTEM DEPLOYMENTS, AND ANY CANCELLATION, REDUCTION OR DELAY IN THESE DEPLOYMENTS COULD HARM OUR BUSINESS

Our business is characterized by large system deployments for a relatively small number of service providers. In the three months ended March 31, 2001, one customer, Shaoxing Telecommunications Bureau, accounted for 14.0% of our net sales. Our dependence on large system deployments makes our ability to provide systems in a timely and cost-effective manner critically important to our business. We have in the past experienced delays and encountered other difficulties in the installation and implementation of our systems. Various factors could cause future delays, including technical problems and the shortage of qualified technicians. Any delays or difficulties in deploying our systems, or the cancellation of any orders by service providers, could significantly harm our business.

WE DO NOT HAVE SOME OF THE LICENSES WE ARE REQUIRED TO HAVE TO SELL OUR NETWORK ACCESS PRODUCTS IN CHINA

Beginning January 1, 1999, China's government required that all telecommunications equipment connected to public or private telecommunications networks within China be approved by the Ministry of Information Industry and the manufacturer of the equipment obtain a network access license for each of its products. Sellers are prohibited from selling or advertising for sale equipment for which its manufacturer has not obtained a network access license and may be liable for penalties in an amount up to three times earnings from the sale of any equipment sold beginning January 1, 1999 without a license. In addition, any unlicensed equipment may be required to be removed from the network. Failure to obtain the required licenses could require us to remove previously installed equipment and

would prohibit us from making further sales of the unlicensed products in China, which would substantially harm our business.

The regulations implementing these requirements are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. Accordingly, we have obtained an opinion from our counsel in China as to which licenses we are required to obtain. Based upon this counsel's advice, we believe that we have obtained the required network access licenses for our AN-2000 system, bundled OMUX product and standard OMUX product. We have applied for a network access license for our PAS system. In June 2000, the Ministry of Information Industry issued an internal notice concluding its review of PHS-based equipment. Our PAS system will continue to be allowed in China's county-level cities and counties, which are our primary markets for our PAS system. In large and medium-sized cities, our PAS system may be used on a limited basis where there is a high concentration of population, such as communities, commercial buildings and special development zones. New city-wide PAS system deployments will not be allowed in large and medium-size cities. The evaluation group for access networks under the Ministry of Information Industry has recommended that the Ministry of Information Industry issue a license for our PAS system. However, we do not yet have this network access license and we cannot provide any assurance that

such a license will be issued for our PAS system. In addition, there is no assurance that the Ministry of Information Industry will not conduct any further review/evaluation of PHS-based equipment or change its order regarding PHS-based system in the future. We have also applied for network access licenses for other products which we are no longer manufacturing but had previously sold to service providers in China. Network access licenses will be required for any additional products that we may develop for sale in China, including our WACOS system. Based upon verbal inquiries made by our counsel in China to the Ministry of Information Industry, we believe that for products which we sold before January 1, 1999, such as the PAS system, no penalties will be imposed by the Ministry of Information Industry for sales we have made or will make during the period in which an application for a network access license is pending. However, our counsel in China has advised us that China's governmental authorities may interpret or apply the regulations with respect to which licenses are required and the ability to sell a product while an application for a network access license is pending in a manner that is inconsistent with the verbal representation received by our counsel in China, either of which could have a material adverse effect on our business and financial condition.

The State Council issued the Telecommunications Regulations of the People's Republic of China on September 25, 2000 ("Telecom Regulations"). The Telecom Regulations restate that the government implements license systems for telecommunications terminal equipment, wireless communications equipment and equipment used in network interconnection that is connected to public telecommunications networks. The above equipment must meet government standards, and a network access license must be obtained. The Telecom Regulations require that telecommunications equipment producers must ensure that the quality of the telecommunications equipment for which they have obtained a network access license is stable and reliable and they may not lower the quality or performance of their products. The State Council's product quality supervision department in concert with the Ministry of Information Industry shall perform spot checks to track and supervise the quality of telecommunications equipment for which a network access license has been obtained and publish the results of such spot checks. Because the Telecom Regulations are new and quite general and have not been further interpreted by the government, we have been unable to ascertain detailed guidance on the license system for telecommunications equipment connected to the network.

OUR BUSINESS MAY SUFFER IF WE ARE UNABLE TO COLLECT PAYMENTS FROM OUR CUSTOMERS ON A TIMELY BASIS

Our customers often must make a significant commitment of capital to purchase our products. As a result, any downturn in a customer's business that affected the customer's ability to pay us could

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harm our financial condition. Moreover, accounts receivable collection cycles historically tend to be much longer in China than in other markets. The failure of any of our customers to make timely payments could require us to write-off accounts receivable or increase our accounts receivable reserves, either of which could adversely affect our financial condition.

A DECLINE IN BUSINESS ACTIVITY DURING CHINA'S LUNAR NEW YEAR MAY RESULT IN DECREASED SALES DURING OUR FIRST QUARTER

Business activity in China declines considerably during the first quarter of each year in observance of the Lunar New Year. As a result, sales during the first quarter of our fiscal year have in the past typically been lower than sales during the fourth quarter of the preceding year and we expect this trend to continue in the future. We will continue to face this seasonality in the future and do not have the ability to forecast with any degree of certainty the impact of the decreased business activity during the Lunar New Year on our sales and operating results.

OUR MARKET IS SUBJECT TO RAPID TECHNOLOGICAL CHANGE, AND TO COMPETE EFFECTIVELY, WE MUST CONTINUALLY INTRODUCE NEW PRODUCTS THAT ACHIEVE MARKET ACCEPTANCE

The emerging market for communications equipment in developing countries is characterized by rapid technological developments, frequent new product introductions and evolving industry and regulatory standards. Our success will depend in large part on our ability to enhance our network access and switching technologies and develop and introduce new products and product enhancements that anticipate changing service provider requirements and technological developments. We may need to make substantial capital expenditures and incur significant research and development costs to develop and introduce new products and enhancements. If we fail to timely develop and introduce new products or enhancements to existing products that effectively respond to technological change, our business, financial condition and results of operations could be materially adversely affected.

From time to time, our competitors or we may announce new products or product enhancements, services or technologies that have the potential to replace or shorten the life cycles of our products and that may cause customers to defer purchasing our existing products, resulting in inventory obsolescence. Future technological advances in the communications industry may diminish or inhibit market acceptance of our existing or future products or render our products obsolete.

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Even if we are able to develop and introduce new products, we cannot assure you that they will gain market acceptance. Market acceptance of our products will depend on various factors including:

our ability to obtain necessary approvals from regulatory organizations;

the perceived advantages of the new products over competing products;

our ability to attract customers who have existing relationships with our competitors;

product cost relative to performance; and

the level of customer service available to support new products.

Specifically, sales of our AN-2000 system outside of China depend, in part, on the adoption of the V5.2 standard in these markets. Additionally, sales of our Personal Access System, or PAS, the mobile component of our PAS wireless system, will depend in part upon consumer acceptance of the mobility limitations of this service. The introduction of inexpensive wireless telephone service or other competitive services in China may have a material adverse effect on sales of our PAS systems in China. If our existing or new products fail to achieve market acceptance for any reason, our business could be seriously harmed.

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OUR BUSINESS WILL SUFFER IF WE ARE UNABLE TO DELIVER QUALITY PRODUCTS ON A TIMELY AND COST EFFECTIVE BASIS

Our operating results depend on our ability to manufacture products on a timely and cost effective basis. In the past, we have experienced reductions in yields as a result of various factors, including defects in component parts and human error in assembly. If we experience deterioration in manufacturing performance or a delay in production of any of our products, we could experience delays in shipments and cancellations of orders. Moreover, networking products frequently contain undetected software or hardware defects when first introduced or as new versions are released. In addition, our products are often embedded in or deployed in conjunction with service providers' products, which incorporate a variety of components produced by third parties. As a result, when a problem occurs, it may be difficult to identify the source of the problem. These problems may cause us to incur significant warranty and repair costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relation problems or loss of customers, any one of which could harm our business.

If future demand for our products requires additional manufacturing capacity, we may invest in and build additional manufacturing facilities, most likely in China. However, we cannot assure you that the new manufacturing facilities will attain the same quality or level of efficiencies as our existing facilities. Alternatively, or in addition, we may contract with third party manufacturing facilities over which we may be unable to exercise the same degree of quality control as we can over our own facilities. We currently have no arrangements with any independent manufacturing facility, and we may not be able to obtain independent manufacturing sources on commercially attractive terms if and when needed.

WE DEPEND ON SOME SOLE SOURCE AND OTHER KEY SUPPLIERS FOR HANDSETS, COMPONENTS AND MATERIALS USED IN OUR PRODUCTS, AND IF THESE SUPPLIERS FAIL TO PROVIDE US WITH ADEQUATE SUPPLIES OF HIGH QUALITY PRODUCTS AT COMPETITIVE PRICES, OUR COMPETITIVE POSITION, REPUTATION AND BUSINESS COULD BE HARMED

Some components and materials used in our products are purchased from a single supplier or a limited group of suppliers. If any supplier is unwilling or unable to provide us with high quality components and materials in the quantities required and at the costs specified by us, we may not be able to find alternative sources on favorable terms, in a timely manner, or at all. Our inability to obtain or to develop alternative sources if and as required could result in delays or reductions in manufacturing or product shipments. Moreover, these suppliers may delay product shipments or supply us with inferior quality products. If any of these events occur, our competitive position, reputation and business could suffer.

OUR ABILITY TO SOURCE A SUFFICIENT QUANTITY OF HIGH QUALITY HANDSETS AND OTHER COMPONENTS USED IN OUR PRODUCTS MAY BE LIMITED BY CHINA'S IMPORT RESTRICTIONS AND DUTIES AS WELL AS OUR ABILITY TO OBTAIN SUFFICIENT DOMESTIC MANUFACTURING CAPACITY

We require a significant number of imported components to manufacture our products in China. Imported electronic components and other imported goods used in the operation of our business are subject to a variety of permit requirements, approval procedures and import duties. Failure to obtain necessary permits or approvals, administrative actions by China's government to limit imports of certain components, or non-payment of required import duties could subject us to penalties and fines and could adversely affect our ability to manufacture and sell our products in China. In addition, import duties increase the cost of our products and may make them less competitive.

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In particular, an integral component of our PAS system is the handset used by subscribers to make and receive mobile telephone calls. Our inability to obtain a sufficient number of high quality handsets could severely harm our business. A worldwide shortage of handsets existed in 2000, and there continues to be a shortage in low-priced handsets, which we have found to be popular with many consumers in China. Although we have contracted with Japanese vendors to manufacture handsets under the UTStarcom label, we cannot assure you that they will be able to supply adequate quantities of handsets. Moreover, we must pay an import duty on each handset that we import into China, which may result in a competitive cost advantage for our competitors who produce handsets in China. As a result, we are evaluating various manufacturing alternatives within China. We are in the early stages of utilizing third parties to manufacture handsets for us in China. However, these manufacturers may be unable to produce adequate quantities of high-quality handsets to meet the demand of our customers. We continue to develop the capacity to manufacture our own handsets. However, we may be unsuccessful in our efforts to do so.

IF WE ARE UNABLE TO EXPAND OUR DIRECT SALES OPERATION IN CHINA AND INDIRECT DISTRIBUTION CHANNELS ELSEWHERE OR SUCCESSFULLY MANAGE OUR EXPANDED SALES ORGANIZATION, OUR OPERATING RESULTS MAY SUFFER

Our distribution strategy focuses primarily on developing and expanding our direct sales organization in China and our indirect distribution channels outside of China. We may not be able to successfully expand our direct sales organization in China and the cost of any expansion may exceed the revenue generated from these efforts. Even if we are successful in expanding our direct sales organization in China, we may not be able to compete successfully against the significantly larger and better-funded sales and marketing operations of current or potential competitors. In addition, if we fail to develop relationships with significant international resellers or manufacturers' representatives, or if these resellers or representatives are not successful in their sales or marketing efforts, we may be unsuccessful in our expansion efforts outside China.

WE EXPECT AVERAGE SELLING PRICES OF OUR PRODUCTS TO DECREASE WHICH MAY REDUCE OUR REVENUES, AND, AS A RESULT, WE MUST INTRODUCE NEW PRODUCTS AND REDUCE OUR COSTS IN ORDER TO MAINTAIN PROFITABILITY

The average selling prices for communications access and switching systems and subscriber terminal products, such as handsets, in China have been declining as a result of a number of factors, including:

increased competition;

aggressive price reductions by competitors;

rapid technological change; and

price and performance enhancements.

We have in the past experienced and expect in the future to experience substantial period-to-period fluctuations in operating results due to declining average selling prices. We anticipate that average selling prices of our products will decrease in the future in response to product introductions by us or our competitors or other factors, including price pressures from customers. Therefore, we must continue to develop and introduce new products and enhancements to existing products that incorporate features that can be sold at higher average selling prices. Failure to do so could cause our revenues and gross profit, as a percentage of net sales, to decline.

Our cost reduction efforts may not allow us to keep pace with competitive pricing pressures or lead to improved gross profit, as a percentage of net sales. In order to be competitive, we must continually reduce the cost of manufacturing our products through design and engineering changes. We

may not be successful in redesigning our products or delivering our products to market in a timely manner. We cannot assure you that any redesign will result in sufficient cost reductions to allow us to reduce the prices of our products to remain competitive or to improve or maintain our gross profit, as a percentage of net sales.

SHIFTS IN OUR PRODUCT MIX MAY RESULT IN DECLINES IN GROSS MARGIN PERCENTAGE OF NET SALES

Our gross profit margin percentage of net sales varies among our product groups. Our gross margin percentage of net sales is generally higher on our access network system products and our gross margin percentage of net sales is significantly lower on our handset products. We also anticipate that the gross margin percentage of net sales may be lower for our newly developed products due to start-up costs and may improve as unit volumes increase and efficiency can be realized. Our overall gross margin percentage of net sales has fluctuated from period to period as a result of shifts in product mix, the introduction of new products, decreases in average selling prices for older products and our ability to reduce product costs. As a result of a growth in sales of handset products over the past few quarters, we have experienced a sustained product shift toward a greater percentage of handset products resulting in a decline in overall gross margin percentage of net sales. In addition, we expect to introduce new products in the future periods. As a result of these recent trends, a potential decrease in overall gross margin percentage of net sales may be experienced.

SERVICE PROVIDERS SOMETIMES EVALUATE OUR PRODUCTS FOR LONG AND UNPREDICTABLE PERIODS WHICH CAUSES THE TIMING OF PURCHASES AND OUR RESULTS OF OPERATIONS TO BE UNPREDICTABLE

The period of time between our initial contact with a service provider and the receipt of an actual purchase order may span a year or more. During this time, service providers may subject our products to an extensive and lengthy evaluation process before making a purchase. The length of these qualification processes may vary substantially by product and service provider, making our results of operations unpredictable. We may incur substantial sales and marketing expenses and expend significant management effort during this process, which ultimately may not result in a sale. These qualification processes often make it difficult to obtain new customers, as service providers are reluctant to expend the resources necessary to qualify a new supplier if they have one or more existing qualified sources.

OUR INABILITY TO EXERCISE COMPLETE CONTROL OVER OUR SUBSIDIARIES MAY BE DETRIMENTAL TO OUR BUSINESS

A considerable portion of our operations is and will continue to be conducted through direct and indirect subsidiaries. For example, we own an 88% interest in a joint venture which operates the Zhejiang manufacturing facility and a 51% interest in a joint venture which operates the Guangdong manufacturing facility. Even though we may own a majority interest in these joint ventures, we do not have sole power to control all of the policies and decisions of these jointly-owned subsidiaries.

Under the law of China governing Sino-foreign joint ventures, equity holders exercise rights primarily through the board of directors, which constitutes the highest authority of the joint venture. Although we own a majority of the Guangdong joint venture, we are only entitled to appoint a minority of the directors to the joint venture's board of directors, which prevents us from controlling the actions of the board. Moreover, even though we hold a majority of the board seats in the Zhejiang joint venture, China law requires unanimous approval of the board of directors for some significant corporate actions, including:

amendment of the Articles of Association of the joint venture;

liquidation or dissolution of the joint venture;

any increase, decrease or transfer of equity interests of any party to the joint venture; and

a merger of the joint venture with another economic entity.

Our operating results and cash flow depend on the operating results and cash flow of our subsidiaries and the payment of funds by those subsidiaries to us. These subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to pay dividends or otherwise provide financial benefits to us. Moreover, with respect to our Guangdong manufacturing joint venture, any payment of dividends to us must be agreed to by our joint venture partner, whose interests in receiving dividend distributions may not coincide with ours. In addition, applicable law in some countries including China limits the ability of a subsidiary to pay dividends for various reasons including the absence of sufficient distributable reserves. In the event of any insolvency, bankruptcy or similar proceedings, creditors of the subsidiaries would generally be entitled to priority over us with respect to assets of the affected subsidiary. In addition, because our joint venture partners in both Zhejiang and Guangdong provinces are affiliated with the provincial Telecommunications Administrations that operate the telecommunication networks in these areas, if we fail to maintain these joint ventures, sales to our customers located in these areas may decrease.

OUR MULTI-NATIONAL OPERATIONS SUBJECT US TO VARIOUS ECONOMIC, POLITICAL, REGULATORY AND LEGAL RISKS

We market and sell our products in China and other markets. The expansion of our existing multi-national operations and entry into additional international markets will require significant management attention and financial resources. Multi-national operations are subject to inherent risks, including:

difficulties in designing products that are compatible with varying international communications standards;

longer accounts receivable collection periods and greater difficulty in accounts receivable collection;

unexpected changes in regulatory requirements;

changes to import and export regulations, including quotas, tariffs and other trade barriers;

delays or difficulties in obtaining export and import licenses;

potential foreign exchange controls and repatriation controls on foreign earnings;

exchange rate fluctuations and currency conversion restrictions;

the burdens of complying with a variety of foreign laws and regulations;

difficulties and costs of staffing and managing multi-national operations;

reduced protection for intellectual property rights in some countries;

potentially adverse tax consequences; and

political and economic instability.

Multinational companies are required to establish intercompany pricing for transactions between their separate legal entities operating in different taxing jurisdictions. These intercompany transactions are subject to audit by taxing authorities in the jurisdictions in which multinational companies operate. An additional tax liability may be incurred if it is determined that intercompany pricing was not done at arm's length. We believe we have adequately estimated and recorded our liability arising from intercompany pricing, but we cannot assure you that an additional tax liability will not result from audits of our intercompany pricing policies.

In markets outside of China, we rely on a number of original equipment manufacturers, or OEMs, and third-party distributors and agents to market and sell our network access products. If these OEMs, distributors or agents fail to provide the support and effort necessary to service developing markets effectively, our ability to maintain or expand our operations outside of China will be negatively impacted. We cannot assure you that we will successfully compete in these markets, that our products will be accepted or that we will successfully overcome the risks associated with international operations.

Our international sales are generally denominated in local currencies. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China. Although the impact of currency fluctuations to date has been insignificant, fluctuations in currency exchange rates in the future may have a material adverse effect on our results of operations. We have a multi-currency bank account in Japanese Yen for purchasing portions of our inventories and supplies. As of March 31, 2001, this Japanese Yen bank account is valued at \$7.0 million.

OUR FAILURE TO MEET INTERNATIONAL AND GOVERNMENTAL PRODUCT STANDARDS COULD BE DETRIMENTAL TO OUR BUSINESS

Many of our products are required to comply with numerous government regulations and standards, which vary by market. As standards for products continue to evolve, we will need to modify our products or develop and support new versions of our products to meet emerging industry standards, comply with government regulations and satisfy the requirements necessary to obtain approvals. Our inability to obtain regulatory approval and meet established standards could delay or prevent our entrance into or force our departure from markets.

OUR RECENT GROWTH HAS STRAINED OUR RESOURCES, AND IF WE ARE UNABLE TO MANAGE AND SUSTAIN OUR GROWTH, OUR OPERATING RESULTS WILL BE NEGATIVELY AFFECTED

We have recently experienced a period of rapid growth and anticipate that we must continue to expand our operations to address potential market opportunities. If we fail to implement or improve systems or controls or to manage any future growth and expansion effectively, our business could suffer.

Our expansion has placed and will continue to place a significant strain on our management, operational, financial and other resources. Many of the members of our management team have limited experience in the management of rapidly growing companies. To manage our growth effectively, we will need to take various actions, including:

enhancing management information systems and forecasting procedures;

further developing our operating, administrative, financial and accounting systems and controls;

maintaining close coordination among our engineering, accounting, finance, marketing, sales and operations organizations;

expanding, training and managing our employee base; and

expanding our finance, administrative and operations staff.

OUR SUCCESS IS DEPENDENT ON CONTINUING TO HIRE AND RETAIN QUALIFIED PERSONNEL, AND IF WE ARE NOT SUCCESSFUL IN ATTRACTING AND RETAINING THESE PERSONNEL, OUR BUSINESS WOULD BE HARMED

The success of our business depends in significant part upon the continued contributions of key technical and senior management personnel, many of whom would be difficult to replace. In particular, our success depends in large part on the knowledge, expertise and services of Hong Liang Lu, our

President and Chief Executive Officer, and Ying Wu, our Executive Vice President and Chief Executive Officer of China Operations. The loss of any key employee, the failure of any key employee to perform satisfactorily in his or her current position or our failure to attract and retain other key technical and senior management employees could have a significant negative impact on our operations.

To effectively manage our recent growth as well as any future growth, we will need to recruit, train, assimilate, motivate and retain qualified employees. Competition for qualified employees is intense, and the process of recruiting personnel with the combination of skills and attributes required to execute our business strategy can be difficult, time-consuming and expensive. We are actively searching for research and development engineers and sales and marketing personnel, who are in short supply. Additionally, we have a need for and have experienced difficulty in finding qualified accounting personnel knowledgeable in U.S. and China accounting standards. If we fail to attract, hire, assimilate or retain qualified personnel, our business would be harmed.

Competitors and others have in the past and may in the future attempt to recruit our employees. In addition, companies in the communications industry whose employees accept positions with competitors frequently claim that the competitors have engaged in unfair hiring practices. We may be the subject of these types of claims in the future as we seek to hire qualified personnel. Some of these claims may result in material litigation and disruption to our operations. We could incur substantial costs in defending ourselves against these claims, regardless of their merits.

ANY ACQUISITIONS THAT WE UNDERTAKE COULD BE DIFFICULT TO INTEGRATE, DISRUPT OUR BUSINESS, DILUTE OUR STOCKHOLDERS AND HARM OUR OPERATING RESULTS

We have acquired and may continue to acquire complimentary businesses, products and technology. There can be no assurance that any anticipated benefits of an acquisition may be realized. We will continue to evaluate acquisition prospects that would complement our existing product offerings, augment our market coverage, enhance our technological capabilities, or that may otherwise offer growth opportunities. Acquisitions of other companies may result in dilutive issuances of equity securities, the incurrence of debt and the amortization of expenses related to goodwill and other intangible assets. In addition, acquisitions involve numerous risks, including difficulties in the assimilation of operations, technologies, products and personnel of the acquired company, diversion of management's attention from other business concerns, risks of entering markets in which we have no direct or limited prior experience, and the potential loss of key employees of ours and the acquired company.

WE MAY EXPERIENCE DIFFICULTY IN IDENTIFYING, FORMING AND MAINTAINING NEW BUSINESS VENTURES THAT ARE IMPORTANT TO THE DEVELOPMENT OF OUR BUSINESS, AND INVESTMENTS IN THESE VENTURES MAY NOT GENERATE RETURNS

We have invested, and expect to continue to invest, significant capital in new business ventures that are important to the development of our business. We cannot assure you that we will be able to continue to identify suitable parties for new ventures and investments in the future. The failure to form or maintain new ventures, or to identify suitable investment opportunities, could significantly limit our ability to expand our operations. Many of our investments have been in privately held companies, many of which can still be considered in the start-up 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. We have recognized an impairment charge in respect of our long-term investments; there can be no assurance that we will not incur future investment losses. Moreover, these new ventures or investments require significant management time and will present significant challenges. We cannot assure you that these activities will be successful or that we will realize returns on these activities. Additionally, if any venture or investment fails, our business could be negatively impacted.

WE MAY BE UNABLE TO ADEQUATELY PROTECT OUR INTELLECTUAL PROPERTY AND MAY BE SUBJECT TO CLAIMS THAT WE INFRINGE THE INTELLECTUAL PROPERTY OF OTHERS, EITHER OF WHICH COULD SUBSTANTIALLY HARM OUR BUSINESS

We rely on a combination of patents, copyrights, trade secret laws and contractual obligations to protect our technology. Although we have applied for several patents in the United States, one of which has been issued, as well as in other countries, we cannot assure you that any additional patents will be issued as a result of pending patent applications or that our issued patents will be upheld. Moreover, we have not yet obtained patents in China. We can give no assurance that we will be able to obtain patents in China on our products or the technology that we use to manufacture our products. Our subsidiaries and joint ventures in China rely upon our trademarks, technology and know-how to manufacture and sell our products. We cannot guarantee that these and other intellectual property protection measures will be sufficient to prevent misappropriation of our technology or that our competitors will not independently develop technologies that are substantially equivalent or superior to ours. In addition, the legal systems of many foreign countries, including China, do not protect intellectual property rights to the same extent as the legal system of the United States. If we are unable to adequately protect our proprietary information, our business, financial condition and results of operations could be materially adversely affected.

The increasing dependence of the communications industry on proprietary technology has resulted in frequent litigation based on allegations of the infringement of patents and other intellectual property. In the future we may be subject to litigation to defend against claimed infringements of the rights of others or to determine the scope and validity of the proprietary rights of others. Future litigation also may be necessary to enforce and protect our trade secrets and other intellectual property rights. Any intellectual property litigation could be costly and could cause diversion of management's attention from the operation of our business. Adverse determinations in any litigation could result in the loss of our proprietary rights, subject us to significant liabilities or require us to seek licenses from third parties which may not be available on commercially reasonable terms, if at all. We could also be subject to court orders preventing us from manufacturing or selling our products.

BUSINESS INTERRUPTIONS COULD ADVERSELY AFFECT OUR BUSINESS

Our operations are vulnerable to interruption by fire, earthquake, power loss, telecommunications failure and other events beyond our control. We do not have a detailed disaster recovery plan. Our headquarters facility in the State of California is currently subject to electrical blackouts as a consequence of a shortage of available electrical power. In the event these blackouts continue or increase in severity, they could disrupt the operations at our headquarters. In addition, we do not carry sufficient business interruption insurance to compensate us for losses that may occur and any losses or damages incurred by us could have a material adverse effect on our business.

RISKS RELATING TO CONDUCTING OPERATIONS IN CHINA

Sales in China account for substantially all of our sales. Approximately \$116.8 million, or 98.0%, of our sales for the three months ended March 31, 2001, \$364.0 million, or 98.8%, of our sales in fiscal 2000, and \$186.1 million, or 99.3%, of our sales in fiscal 1999, occurred in China. Additionally, a substantial portion of our fixed assets are located in China. Of our total fixed assets, approximately 76.8% as of March 31, 2001, 75.0% as of December 31, 2000, and 53.7% as of December 31, 1999 were in China. We expect to make further investments in China in the future. Therefore, our business, financial condition and results of operations are to a significant degree subject to economic, political and social events in China.

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DEVALUATION IN THE VALUE OF THE RENMINBI AND FLUCTUATIONS IN EXCHANGE RATES COULD ADVERSELY AFFECT OUR FINANCIAL RESULTS

Exchange rate fluctuations could have a substantial negative impact on our financial condition and results of operations. We purchase substantially all of our materials in the United States and Japan and a significant portion of our cost of goods sold is incurred in U.S. dollars and Japanese yen. A significant portion of our operating expenses are incurred in U.S. dollars. At the same time, most of our sales are denominated in Renminbi. The value of the Renminbi is subject to changes in China's governmental policies and to international economic and political developments. Although the official exchange rate for the conversion of Renminbi to U.S. dollars has remained stable, with the Renminbi appreciating slightly against the U.S. dollar since 1994, the exchange rate experienced significant volatility prior to 1994 including periods of sharp devaluation. There can be no assurance that exchange rates will not become volatile or that the Renminbi will not devalue again against the U.S. dollar.

In the past, financial markets in many Asian countries have experienced severe volatility and, as a result, some Asian currencies have experienced significant devaluation from time to time. The devaluation of some Asian currencies may have the effect of rendering exports from China more expensive and less competitive and therefore place pressure on China's government to devalue the Renminbi. Any devaluation of the Renminbi could result in an increase in volatility of Asian currency and capital markets. Future volatility of Asian financial markets could have an adverse impact on our ability to expand our product sales into Asian markets outside of China. Moreover, due to the limitations on the convertibility of Renminbi, we are limited in our ability to engage in currency hedging activities in China and do not currently engage in currency hedging activities with respect to international sales outside of China.

CURRENCY RESTRICTIONS IN CHINA MAY LIMIT THE ABILITY OF OUR SUBSIDIARIES AND JOINT VENTURES IN CHINA TO OBTAIN AND REMIT FOREIGN CURRENCY NECESSARY FOR THE PURCHASE OF IMPORTED COMPONENTS AND MAY LIMIT OUR ABILITY TO OBTAIN AND REMIT FOREIGN CURRENCY IN EXCHANGE FOR RENMINBI EARNINGS

China's government imposes controls on the convertibility of Renminbi into foreign currencies and, in certain cases, the remittance of currency out of China. Under the current foreign exchange control system, sufficient foreign currency may not be available to satisfy our currency needs. Shortages in the availability of foreign currency may restrict the ability of our Chinese subsidiaries to obtain and remit sufficient foreign currency to pay dividends to us, or otherwise satisfy their foreign currency denominated obligations such as payments to us for components which we export to them and for technology licensing fees. We may also experience difficulties in completing the administrative procedures necessary to obtain and remit needed foreign currency. Moreover, we cannot assure you that China's government will continue the

policy of making the Renminbi convertible under current accounts. Our inability to convert and remit our sales received in Renminbi into U.S. dollars and make necessary remittances could have a material adverse effect on our business, financial condition and results of operations.

Our business could be substantially harmed if we are unable to convert our sales received in Renminbi into U.S. dollars. Under existing foreign exchange laws, Renminbi held by our China subsidiaries can be converted into foreign currencies and remitted out of China to pay current account items such as payments to suppliers for imports, labor services, payment of interest on foreign exchange loans and distributions of dividends so long as the subsidiaries have adequate amounts of Renminbi to purchase the foreign currency. Expenses of a capital nature such as the repayment of bank loans denominated in foreign currencies, however, require approval from appropriate governmental authorities before Renminbi can be used to purchase foreign currency and then remitted out of China. This system could be changed at any time by executive decision of the State Council to impose limits on current account convertibility of the Renminbi or other similar restrictions. Moreover, even though

the Renminbi is intended to be freely convertible under the current account, the State Administration of Foreign Exchange, which is responsible for administering China's foreign currency market, has a significant degree of administrative discretion in implementing the laws. From time to time, the State Administration of Foreign Exchange has used this discretion in ways which effectively limit the convertibility of current account payments and restrict remittances out of China. Furthermore, in many circumstances the State Administration of Foreign Exchange must approve foreign currency conversions and remittances. Under the current foreign exchange control system, sufficient foreign currency may not be available at a given exchange rate to satisfy our currency demands.

CHANGES WITHIN CHINA'S COMMUNICATIONS MARKET COULD HARM OUR BUSINESS

We derive substantially all of our sales from local telecommunications service providers in China which utilize network access equipment in the continued expansion and upgrading of China's communications infrastructure. The continued development of the communications infrastructure in China correspondingly depends, in part, on the demand for voice and data services in China and China's governmental policy. Although this industry has grown rapidly in the past, we cannot assure you that it will continue to grow in the future.

Any reduced demand for voice and data services, any other downturn or other adverse changes in the China communications industry or the adoption or enforcement of government policies that limit or prohibit our ability to manufacture, market or sell our products could severely harm our business.

CHINA'S TELECOMMUNICATIONS INDUSTRY IS SUBJECT TO EXTENSIVE GOVERNMENT REGULATION AND HAS RECENTLY BEEN RESTRUCTURED, WHICH HAS LED TO UNCERTAINTY

China's telecommunications industry is heavily regulated by the Ministry of Information Industry. The Ministry of Information Industry controls the 33 provincial Telecommunications Administrations that exercise regulatory responsibility over the telecommunications industries in their respective provinces. The Ministry of Information Industry has broad discretion and authority to regulate all aspects of the telecommunications and information technology industry in China including managing spectrum bandwidths, setting network equipment specifications and standards and drafting laws and regulations related to the electronics and telecommunications industries.

As part of the Chinese government's industry restructuring initiatives, the regulatory functions of the Ministry of Information Industry and the Telecommunications Administrations were separated from the operational functions of the state-owned companies under their control. Following this separation, the Ministry of Information Industry acts exclusively as the industry regulator and will no longer manage the day-to-day operations of telecommunications service providers in China.

China does not yet have a national telecommunications law. The Ministry of Information Industry, under the direction of the State Council, is currently preparing a draft of the Telecommunications Law of the People's Republic of China for ultimate submission to the National People's Congress for review and adoption. It is unclear if and when the Telecommunications Law will be adopted. If the Telecommunications Law is adopted, we expect it to become the basic telecommunications statute and the source of telecommunications regulations in China. Although we expect that a Telecommunications Law would have a positive effect on the overall development of the telecommunications industry in China, we do not know the nature and scope of regulation that it would create. Accordingly, we cannot predict whether it will have a positive or negative effect on us or on some or all aspects of our business.

The Telecom Regulations are deemed as the basic telecommunications regulations covering telecommunications services and market regulations, pricing, interconnection and connection, as well as telecommunications construction and security issues. Although we expect that the Telecom Regulations

would have a positive effect on the overall development of the telecommunications industry in China, the enforcement and interpretation of these regulations by government authorities may negatively affect our business.

The Ministry of Information Industry has broad discretion to apply standards in deciding what types of equipment may be connected to the national telecommunications networks, the forms and types of services that may be offered to the public and the content of material available in China over the Internet. If the Ministry of Information Industry sets standards with which we are unable to comply, our ability to sell product in China may be limited, resulting in substantial harm to our operations. For example, at the end of May 2000, we became aware of an internal notice, circulated within the Ministry of Information Industry, announcing a review of PHS-based telecommunications equipment for future installation into China's telecommunications infrastructure in which the Ministry of Information Industry requested service providers to temporarily halt new deployments of PHS-based telecommunications equipment, including our PAS system, pending conclusion of the Ministry of Information Industry review. Subsequently, at the end of June 2000, we learned that the Ministry of Information Industry had issued an internal notice concluding its review of PHS-based equipment and allowing the continued deployment of our PAS system in China's county-level cities and counties, the primary markets for our PAS system. In addition, deployments in large and medium-sized cities will be allowed on a limited basis where there is a high concentration of population, such as campuses, commercial buildings and special development zones, however, new city-wide deployments of our PAS system will not be allowed in such large and medium-sized cities. Failure of the Ministry of Information Industry to allow the deployment of our PAS system in the future could have a material adverse effect on our business and financial condition.

CHINA CLOSELY RESTRICTS ACTIVITIES OF FOREIGN INVESTORS IN THE TELECOMMUNICATIONS INDUSTRY

China's government and its agencies, including the Ministry of Information Industry and the State Council, regulate foreign investment in the telecommunications industry through the promulgation of various laws and regulations and the issuance of various administrative orders and decisions. Foreign investment enterprises, companies and individuals are prohibited from investing and participating in the operation and management of telecommunications networks without special approval by the State Council. We cannot assure you that China will not promulgate new laws or regulations, or issue administrative or judicial decisions or interpretations, which would further restrict or bar foreigners from engaging in telecommunications-related activities. The promulgation of laws or regulations or the issuance of administrative orders or judicial decisions or interpretations restricting or prohibiting telecommunications activities by foreigners could have a substantial impact on our ongoing operations.

MOST OF OUR CUSTOMERS IN CHINA ARE PART OF THE CHINA TELECOM SYSTEM AND ARE SUBJECT TO ITS ULTIMATE CONTROL

Each of the local Telecommunications Bureaus in China which comprise most of our existing or potential customers is part of the China Telecom system and subject to its ultimate control. Accordingly, China Telecom may issue policy statements or make other decisions which govern the equipment purchasing decisions of most of our customers in China. For example, in late 1999 China Telecom prohibited all Telecommunications Bureaus from purchasing PHS systems, such as our PAS systems, which are classified as low-mobility wireless access systems for implementation in large cities. In June 2000, the Ministry of Information Industry issued an internal notice concluding its review of PHS-based equipment. Our PAS system will continue to be allowed in China's county-level cities and counties, which are our primary markets for our PAS system. In large and medium-sized cities, our PAS system may be used on a limited basis where there is a high concentration of population. New city-wide PAS system deployments will not be allowed in large and medium-size cities. As virtually all of our

sales are generated from our operations in China, a change of this decision of China Telecom and the Ministry of Information Industry or other decisions by China Telecom and the Ministry of Information Industry could cause substantial harm to our business.

CHANGES IN TELECOMMUNICATIONS TARIFFS MAY RESULT IN DECREASED DEMAND FOR OUR PRODUCTS

In November 2000, the Ministry of Information Industry announced significant changes in telephone rates in China. While long distance, international, leased line and Internet connection fees were cut by up to 70%, the rates for local telephone services, which include certain types of wireless access services were increased, from approximately \$0.01 per minute to approximately \$0.02 per minute. The increase in rates may result in a reduced demand for our PAS system and other wireless access products. Additionally, the Ministry of Information Industry may implement future rate changes for wireline or wireless services in China, any of which may lead to reduced demand for our systems and products and result in a material adverse effect on our business or results of operations.

CHINA'S GOVERNMENT POLICIES COULD IMPACT OUR BUSINESS

Since 1978, China's government has been and is expected to continue reforming its economic and political systems. These reforms have resulted in and are expected to continue to result in significant economic and social development in China. Many of the reforms are unprecedented or experimental and may be subject to change or readjustment due to a number of political, economic and social factors. We believe that the basic principles underlying the political and economic reforms will continue to be implemented and provide the framework for China's political and economic system. New reforms or the readjustment of previously implemented reforms could have a significant negative effect on our operations. Changes in China's political, economic and social conditions and governmental policies which could have a substantial impact on our business include:

new laws and regulations or the interpretation of those laws and regulations;

the introduction of measures to control inflation or stimulate growth;

changes in the rate or method of taxation;

the imposition of additional restrictions on currency conversion and remittances abroad; and

any actions which limit our ability to develop, manufacture, import or sell our products in China, or to finance and operate our business in China.

CHINA'S ECONOMIC POLICIES COULD IMPACT OUR BUSINESS

The economy of China differs from the economies of most countries belonging to the Organization for Economic Cooperation and Development in various respects such as structure, government involvement, level of development, growth rate, capital reinvestment, allocation of resources, self-sufficiency, rate of inflation and balance of payments position. In the past, the economy of China has been primarily a planned economy subject to one- and five-year state plans adopted by central government authorities and largely implemented by provincial and local authorities which set production and development targets.

Since 1978, increasing emphasis had been placed on decentralization and the utilization of market forces in the development of China's economy. Economic reform measures adopted by China's government may be inconsistent or ineffectual, and we may not in all cases be able to capitalize on any reforms. Further, these measures may be adjusted or modified in ways which could result in economic liberalization measures that are inconsistent from time to time or from industry to industry or across different regions of the country. China's economy has experienced significant growth in the past

decade. This growth, however, has been accompanied by imbalances in China's economy and has resulted in significant fluctuations in general price levels, including periods of inflation. China's government has implemented policies from time to time to increase or restrain the rate of economic growth, control periods of inflation or otherwise regulate economic expansion. While we may be able to benefit from the effects of some of these policies, these policies and other measures taken by China's government to regulate the economy could also have a significant overall impact on economic conditions in China with a resulting negative impact on our business.

CHINA'S EXPECTED ENTRY INTO THE WTO CREATES UNCERTAINTY AS TO THE FUTURE ECONOMIC AND BUSINESS ENVIRONMENTS IN CHINA

China is expected to enter the World Trade Organization some time in 2001. Although China has been reducing tariff levels over the past several years, entry into the WTO will require China to further reduce tariffs and eliminate other trade restrictions. While China's entry into the WTO and related relaxation of trade restrictions may lead to increased foreign investment, it may also lead to increased competition in China's markets from international companies. Whether or not China is accepted into the WTO, the impact on China's economy and our business is uncertain.

IF TAX BENEFITS AVAILABLE TO OUR SUBSIDIARIES LOCATED IN CHINA ARE REDUCED OR REPEALED, OUR BUSINESS COULD SUFFER

Our subsidiaries and joint ventures located in China enjoy tax benefits in China which are generally available to foreign investment enterprises, including full exemption from national enterprise income tax for two years starting from the first profit-making year and/or a 50% reduction in national income tax rate for the following three years. In addition, local enterprise income tax is often waived or reduced during this tax holiday/incentive period. Under current regulations in China, foreign investment enterprises that have been accredited as technologically advanced enterprises are entitled to additional tax incentives. These tax incentives vary in different locales and could include preferential national enterprise income tax treatment at 50% of the usual rates for different periods of time. All of our active subsidiaries in China were accredited as technologically advanced enterprises. These tax incentives may be repealed or reduced in the future. If these tax incentives are abolished before our subsidiaries in China can take full advantage of them, the tax liability of these subsidiaries will increase, which will negatively impact our financial condition and results of operations.

CHINA'S LEGAL SYSTEM EMBODIES UNCERTAINTIES THAT COULD NEGATIVELY IMPACT OUR BUSINESS

China has a civil law legal system. Although often used by judges for guidance, decided court cases do not have binding legal effect on future decisions. Since 1979, many new laws and regulations covering general economic matters have been promulgated in China. Despite this activity to develop the legal system, China's system of laws is not yet complete. Even where adequate law exists in China, enforcement of existing laws or contracts based on existing law may be uncertain and sporadic and it may be difficult to obtain swift and equitable enforcement, or to obtain enforcement of a judgment by a court of another jurisdiction. The relative inexperience of China's judiciary in many cases creates additional uncertainty as to the outcome of any litigation. Further, interpretation of statutes and regulations may be subject to government policies reflecting domestic political changes.

China has adopted a broad range of related laws, administrative rules and regulations that govern the conduct and operations of foreign investment enterprises and restrict the ability of foreign companies to conduct business in China. These laws, rules and regulations provide some incentives to encourage the flow of investment into China, but also subject foreign companies, and foreign investment enterprises including our subsidiaries in China, to a set of restrictions which may not always apply to domestic companies in China. Although China is increasingly according foreign companies and

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foreign investment enterprises established in China the same rights and privileges as Chinese domestic companies in anticipation of China's entry into the WTO, these special laws, administrative rules and regulations governing foreign companies and foreign investment enterprises may still place us and our subsidiaries at a disadvantage in relation to Chinese domestic companies and may adversely affect our competitive position. Moreover, as China's legal system develops, the promulgation of new laws, changes to existing laws and the pre-emption of local regulations by national laws may adversely affect foreign investors and companies.

Many of our activities and products in China are subject to administrative review and approval by various national and local agencies of China's government. Because of the changes occurring in China's legal and regulatory structure, there can be no assurance that we will be able to secure the requisite governmental approval for our activities and products. Failure to obtain the requisite government approval for any of our activities or products could substantially harm our business.

STOCK PERFORMANCE

OUR STOCK PRICE IS HIGHLY VOLATILE

The trading price of our common stock has fluctuated significantly since our initial public offering in March 2000. Our stock price could be subject to wide fluctuations in the future in response to many events or factors, including those discussed in the preceding risk factors relating to our operations, as well as:

actual or anticipated fluctuations in operating results;

changes in expectations as to future financial performance or changes in financial estimates or buy/sell recommendations of securities analysts;

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our, or a competitor's, announcement of new products, services or technological innovations; and

the operating and stock price performance of other comparable companies.

General market conditions and domestic or international macroeconomic factors unrelated to our performance may also affect our stock price. For these reasons, investors should not rely on recent trends to predict future stock prices or financial results. In addition, following periods of volatility in a company's securities, securities class action litigation against a company is sometimes instituted. This type of litigation could result in substantial costs and the diversion of management time and resources.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

UTStarcom is exposed to the impact of interest rate changes and changes in foreign currency exchange rates.

Interest Rate Risk. Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio. The fair value of our investment portfolio would not be significantly affected by either a 10% increase or decrease in interest rates due mainly to the short term nature of our investment portfolio. However, our interest income can be sensitive to changes in the general level of U.S. interest rates since the majority of our funds are invested instruments with maturities less than one year. Our policy is to limit the risk of principal loss and ensure the safety of invested funds by limiting market risk. Funds in excess of current operating requirements are invested in government sponsored entities notes, commercial paper, floating rate corporate bonds and fixed income corporate bonds.

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The table below represents carrying amounts and related weighted-average interest rates of maturity of our investment portfolio at March 31, 2001:

(In thousands, except interest rates)

| | | |
|-----------------------------|----|---------|
| Cash and cash equivalents | \$ | 175,535 |
| Average interest rate | | 2.9% |
| Short-term investments | | 32,949 |
| Average interest rate | | 5.7% |
| Total investment securities | | 208,485 |
| Average interest rate | | 3.3% |

Foreign Exchange Rate Risk. We are exposed to foreign exchange rate risk because our sales to China are denominated in Renminbi and portions of our accounts payable are denominated in Japanese Yen. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China. Although the impact of currency fluctuations of Renminbi to date has been insignificant, fluctuations in currency exchange rates in the future may have a material adverse effect on our results of operations. We have a multi-currency bank account in Japanese Yen for purchasing portions of our inventories and supplies. The balance of this Japanese Yen account as of March 31, 2001 is approximately \$7.0 million.

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PART II OTHER INFORMATION

ITEM 2 CHANGES IN SECURITIES AND USE OF PROCEEDS

We completed our initial public offering ("IPO") on March 3, 2000 pursuant to a Registration Statement on Form S-1 (File No. 333-93069). In the IPO, we sold an aggregate of 11,500,000 shares of common stock (including an over-allotment option of 1,500,000 shares) at \$18.00 per share.

The managing underwriters of the offering were Merrill Lynch & Co., Banc of America Securities LLC, U.S. Bancorp Piper Jaffray, Merrill Lynch Japan Inc., and E-TRADE Securities Co., Ltd. The sale of the shares of common stock generated aggregate gross proceeds of approximately \$207.0 million. The aggregate net proceeds were approximately \$189.4 million, after deducting underwriting discounts and

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commissions of approximately \$14.5 million and expenses of the offering of approximately \$3.1 million. None of such amounts were direct or indirect payments to our directors or officers or their associates, to persons owning 10 percent or more of any class of our equity securities or to our affiliates.

The net proceeds are expected to be used for general corporate purposes, including working capital and capital expenditures. The amounts actually expended for such purposes may vary significantly and will depend on a number of factors, including our future revenues and cash generated by operations and the other factors described under "Factors Affecting Future Operating Results". Accordingly, we retain broad discretion in the allocation of the net proceeds of the offering. A portion of the net proceeds may also be used to acquire or invest in complementary businesses, technologies or product offerings. As of March 31, 2001 we have not used any of the net proceeds and the entire amounts of net proceeds remains in our cash and cash equivalents and short-term investments accounts. In addition, at March 31, 2001, there are no material agreements or commitments with respect to any acquisition or investment activities.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5 OTHER INFORMATION

From time to time, our directors, officers, or employees may enter into good faith trading plans pursuant to SEC Rule 10b5-1(c) (effective October 23, 2000).

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a)

Exhibits:

| NUMBER | EXHIBIT DESCRIPTION |
|-----------|--|
| 10.56 (1) | Assignment Agreement between UTStarcom, Inc. and Stable Gain International Limited dated July 24, 2000. |
| 10.57 (1) | Amendment No.1 to July 24, 2000 Assignment Agreement between UTStarcom, Inc. and Stable Gain International Limited, dated March 2, 2001. |
| 10.58 (1) | Loan Agreement between China Merchant Bank and UTStarcom (China) Co., Ltd., dated March 14, 2001. |
| 10.59 (1) | Technical Service Agreement between UTStarcom (China) Co., Ltd. and Hainan Xinhuangpu Investment Co., Ltd., dated August 18, 2000. |
| 10.60 (1) | Assets Transfer Agreement between Hainan Xinhuangpu Investment Co., Ltd. and UTStarcom (China) Co., Ltd., dated August 18, 2000. |
| 10.61 (1) | Equity Transferring Agreement between Zhe Jiang Nantian Telecommunication Development Group Share Company and UTStarcom, Inc., dated February 5, 2001. |
| 10.62 (1) | Sales Contract between Zhejiang Telecom Co. and UTStarcom (China) Co., Ltd., dated March 23, 2001. |
| 10.63 (1) | Manufacturing License Agreement between Himachal Futuristic Communications Ltd. and |

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| NUMBER | EXHIBIT DESCRIPTION |
|--------|---------------------|
|--------|---------------------|

| | |
|--|---------------------------------------|
| | UTStarcom, Inc., dated March 6, 2001. |
|--|---------------------------------------|

- (1) Certain information in this Exhibit has been omitted and filed separately with the Commission. Confidential treatment has been requested with respect to the omitted portions.
- (b) Reports on Form 8-K:
- No reports on Form 8-K were filed during the quarter.

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UTSTARCOM, 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.

Date: May 11, 2001

UTSTARCOM, INC.
(Registrant)

BY:

/s/ Hong Liang Lu

Hong Liang Lu
President, Chief Executive Officer and Director

/s/ Michael J. Sophie

Michael J. Sophie
Chief Financial Officer and Assistant Secretary

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