Item 7. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion of our financial condition and results of operations should be read in conjunction with the financial statements and related notes included in this Annual Report on Form 10-K. This discussion may contain forward-looking statements based upon current expectations that involve risks and uncertainties including those discussed under Part I, Item 1A, "Risk Factors." These risks and uncertainties may cause actual results to differ materially from those discussed in the forward-looking statements.

Overview

We are a leading global semiconductor provider of high-performance application-specific standard products. Our core strength of expertise is the development of complex SoC devices leveraging our extensive portfolio of technology intellectual property in the areas of analog, mixed-signal, digital signal processing and embedded ARM-based microprocessor integrated circuits. We also develop platforms that we define as integrated hardware along with software that incorporates digital computing technologies designed and configured to provide an optimized computing solution compared to individual components. Our broad product portfolio includes devices for data storage, enterprise-class Ethernet data switching, Ethernet PHY, mobile handsets and other consumer electronics, wireless networking, personal area networking, Ethernet-based PC connectivity, control plane communications controllers, video-image processing and power management solutions. Our products serve diverse applications used in carrier, metropolitan, enterprise and PC-client data communications and storage systems. Additionally, we serve the consumer electronics market for the convergence of voice, video and data applications. We are a fabless integrated circuit company, which means that we rely on independent, third party contractors to perform manufacturing, assembly and test functions. This approach allows us to focus on designing, developing and marketing our products and significantly reduces the amount of capital we need to invest in manufacturing products.

Historically, a small number of customers have accounted for a significant portion of our net revenue. One customer, Western Digital, accounted for more than 10% of our net revenue in fiscal 2012, and two customers represented more than 10% of our net revenue in fiscal 2011 and 2010. Western Digital represented 19%, 21%, and 24% of our net revenue in fiscal 2012, 2011 and 2010, respectively. Research in Motion represented 14% of net revenue in fiscal 2011. Toshiba represented 15% of net revenue in fiscal 2010. Subsequent to our fiscal 2012, Western Digital acquired Hitachi's HDD unit. If this acquisition had occurred at the beginning of fiscal 2012, Western Digital would have represented 24% of net revenue. During fiscal 2012, Seagate acquired the HDD operations of Samsung. If this acquisition had occurred at the beginning of fiscal 2012, Seagate would have represented 11% of total revenue. Also, in fiscal 2012, one distributor accounted for more than 10% of our net revenue. In fiscal 2011 and 2010, no distributor accounted for more than 10% of our net revenue. We expect to continue to experience significant customer concentration in future periods. In addition, most of our sales are made to customers located outside of the United States, primarily in Asia. Sales to customers in Asia represented approximately 88%, 81% and 89% of our net revenue for fiscal 2012, 2011 and 2010, respectively. Because many manufacturers and manufacturing subcontractors of our customers are located in Asia, we expect that most of our net revenue will continue to be represented by sales to our customers in that region. All of our sales to date have been denominated in U.S. dollars.

An increasing number of our products are being incorporated into consumer electronics products, including gaming devices, which are subject to significant seasonality and fluctuations in demand. Due to holiday and back to school buying trends, these seasonal demand patterns generally will negatively impact our results in the first and fourth quarter and positively impact our results in the second and third quarter of our fiscal years.

A relatively large portion of our sales have historically been made on the basis of purchase orders rather than long-term agreements. In addition, the sales cycle for our products is long, which may cause us to experience a delay between the time we incur expenses and the time revenue is generated from these expenditures. We anticipate that the rate of new orders may vary significantly from quarter to quarter. Consequently, if anticipated sales and shipments in any quarter do not occur when expected, expenses and inventory levels could be disproportionately high, and our operating results for that quarter and future quarters may be adversely affected.

Our fiscal year is the 52- or 53-week period ending on the Saturday closest to January 31. In a 52-week year, each fiscal quarter consists of 13 weeks. The additional week in a 53-week year is added to the fourth quarter, making such quarter consist of 14 weeks. Fiscal 2012, 2011 and 2010 were comprised of 52-week periods. Fiscal 2013 will be comprised of a 53-week period.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with GAAP in the United States requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to performance-based compensation, revenue recognition, provisions for sales returns and allowances, inventory excess and obsolescence, investment fair values, goodwill and other intangible assets, income taxes, litigation and other contingencies. In addition, we use assumptions when employing the Monte Carlo simulation and Black-Scholes valuation models to calculate the fair value of stock-based awards granted. We base our estimates of the carrying value of certain assets and liabilities on historical experience and on various other assumptions that are believed to be reasonable under the circumstances when these carrying values are not readily available from other sources. Actual results could differ from these estimates, and such differences could affect the results of operations reported in future periods. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue Recognition. We recognize revenues when there is persuasive evidence of an arrangement, delivery has occurred, the fee is fixed or determinable, and collection is reasonably assured.

Product revenue is generally recognized upon shipment of product to customers, net of accruals for estimated sales returns and rebates. However, some of our sales are made through distributors under agreements allowing for price protection, shipped from stock pricing adjustment rights, and limited rights of return on product unsold by the distributors. Although title passes to the distributor upon shipment terms and payment by our distributors is not contingent on resale of the product, product revenue on sales made through distributors with price protection, shipped from stock pricing adjustment rights and stock rotation rights are deferred until the distributors sell the product to end customers. Deferred revenue less the related cost of the inventories is reported as deferred income. We do not believe that there is any significant exposure related to impairment of deferred cost of sales, as our historical returns have been minimal and inventory turnover for our distributors generally ranges from 60 to 90 days. Our sales to direct customers are made primarily pursuant to standard purchase orders for delivery of products.

A portion of our revenue is derived from sales through third party logistics providers, who maintain warehouses in close proximity to, and may be located directly in our customer’s facilities. Revenue from sales through these third party logistics providers is not recognized until the product is pulled from stock by the customer.

The provision for estimated sales returns and allowances on product sales is recorded in the same period the related revenues are recorded. These estimates are based on historical sales returns, analysis of credit memo data and other known factors. Actual returns could differ from these estimates. We account for rebates by recording reductions to revenue in the same period that the related revenue is recorded. The amount of these reductions is based upon the terms included in our various rebate agreements.

Stock-Based Compensation. Stock-based compensation is measured at the grant date, based on the fair value of the award, and is recognized as expense over the requisite service period. We amortize stock-based compensation expense under the straight-line attribution method over the vest term, which is generally four years for annual grants to employees and five years for new hire grants.

The fair value of restricted stock units is based on the fair market value of our common shares on the date of grant. We estimate the fair value of time-based stock option awards on the date of grant using the Black Scholes option-pricing model. The fair value of market-based option awards is estimated on the date of grant using a Monte Carlo simulation model. The value of the portion of the awards that is ultimately expected to vest is recognized as expense over the requisite service periods. The Black-Scholes and Monte Carlo models incorporate various highly subjective assumptions including expected term of awards, expected future stock price volatility and expected forfeiture rates.

In developing estimates used to calculate assumptions, we establish the expected term for employee options, as well as expected forfeiture rates, based on the historical settlement experience and after giving consideration to vesting schedules. Assumptions for option exercises and pre-vesting terminations of options were stratified by employee groups with sufficiently distinct behavior patterns. Expected volatility was developed based on an equally weighted combination of historical price volatility and implied volatility derived from traded options on our stock in the marketplace.

Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates. Stock-based compensation expense is recorded net of estimated forfeitures such that expense is recorded only for those stock-based awards that are expected to vest. Previously recognized expense is reversed for the portion of awards forfeited prior to vesting as and when forfeitures occurred.

In addition, for both stock options and restricted stock units, we are required to estimate forfeiture rates, and true up these forfeiture rates when actual results are different from our estimates. Assumptions for forfeitures are stratified by employee groups with sufficiently distinct behavior patterns. Changes in the estimated forfeiture rate can have a significant effect on reported stock-based compensation expense, as the effect of adjusting the rate for all expense amortization is recognized in the period the forfeiture estimate is changed. If the actual forfeiture rate is higher than the estimated forfeiture rate, then an adjustment will be made to increase the estimated forfeiture rate, which will result in a decrease to the expense recognized in the financial statements. If the actual forfeiture rate is lower than the estimated forfeiture rate, then an adjustment will be made to lower the estimated forfeiture rate, which will result in an increase to the expense recognized in the financial statements. The expense we recognize in future periods could be affected by changes in the estimated forfeiture rate and may differ significantly from amounts recognized in the current period and/or our forecasts.

Additionally, for certain of our performance-based awards, we must make subjective assumptions regarding the likelihood that the related performance metrics will be met. These assumptions are based on various revenue and operating performance criteria. Changes in our actual performance could cause a significant adjustment in future periods for these performance-based awards.

Accounting for Income Taxes. To prepare our consolidated financial statements, we estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual tax exposure together with assessing temporary differences resulting from the differing treatment of certain items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets.

In accordance with Accounting Standards Codification (“ASC”) Topic 740, “Income Taxes” (“ASC 740”), we recognize income taxes using an asset and liability approach. This approach requires the recognition of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in our consolidated financial statements or tax returns. The measurement of current and deferred taxes is based on provisions of the enacted tax law and the effects of future changes in tax laws or rates are not anticipated.

Evaluating the need for an amount of a valuation allowance for deferred tax assets often requires judgment and analysis of all the positive and negative evidence available to determine whether all or some portion of the deferred tax assets will not be realized. A valuation allowance must be established for deferred tax assets when it is more likely than not that they will not be realized. Based on the available evidence and judgment, we have determined that it is more likely than not that U.S. research credits and certain acquired net operating losses will not be realized and therefore we have provided a full valuation allowance against these credits. If there is a change in our ability to realize our deferred tax assets, then our tax provision may decrease in the period in which we determine that realization is more likely than not.

As a multinational corporation, we conduct our business in many countries and are subject to taxation in many jurisdictions. The taxation of our business is subject to the application of various and sometimes conflicting tax laws and regulations as well as multinational tax conventions. Our effective tax rate is highly dependent upon the geographic distribution of our worldwide earnings or losses, the tax regulations and tax holidays in each geographic region, the availability of tax credits and carryforwards, and the effectiveness of our tax planning strategies. The application of tax laws and regulations is subject to legal and factual interpretation, judgment and uncertainty. Tax laws themselves are subject to change as a result of changes in fiscal policy, changes in legislation, and the evolution of regulations and court rulings. Consequently, taxing authorities may impose tax assessments or judgments against us that could materially impact our tax liability and/or our effective income tax rate.

We are subject to income tax audits by the respective tax authorities in all of the jurisdictions in which we operate. We recognize the effect of income tax positions only if these positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is more than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. We record interest and penalties related to unrecognized tax benefits in income tax expense. The calculation of our tax liabilities involves the inherent uncertainty associated with the application of U.S. GAAP and complex tax laws. We believe we have adequately provided in our financial statements for additional taxes that we estimate may be required to be paid as a result of such examinations. While we believe that we have adequately provided for all tax positions, amounts asserted by tax authorities could be greater or less than our accrued position. These tax liabilities, including the interest and penalties, are released pursuant to a settlement with tax authorities, completion of audit or expiration of various statutes of limitation. The material jurisdictions in which we may be subject to potential examination by tax authorities throughout the world include China, Israel, Singapore, Switzerland and the United States.

The recognition and measurement of current taxes payable or refundable and deferred tax assets and liabilities require that we make certain estimates and judgments. Changes to these estimates or a change in judgment may have a material impact on our tax provision in a future period.

Inventories. We value our inventory at the lower of cost or market, cost being determined under the first-in, first-out method. We regularly review inventory quantities on hand and record a provision for excess and obsolete inventory based primarily on our estimated forecast of product demand and production requirements. The valuation of inventory requires us to estimate the future demand for our products. The estimate of future demand is compared to our inventory levels, including open purchase commitments, to determine the amount, if any, of obsolete or excess inventory. Demand for our products can fluctuate significantly from period to period. A significant decrease in demand could result in an increase in the amount of excess inventory on hand. In addition, our industry is characterized by rapid technological change, frequent new product development and rapid product obsolescence that could result in an increase in the amount of obsolete inventory quantities on hand. Additionally, our estimates of future product demand may prove to be inaccurate, in which case we may have understated or overstated the provision required for excess and obsolete inventory. In the future, if our inventory is determined to be overvalued, we would be required to recognize such costs in our cost of goods sold at the time of such determination. Likewise, if our inventory is determined to be undervalued, we may have over-reported our cost of goods sold in previous periods and would be required to recognize additional gross margin at the time the related inventory is sold. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product demand, any significant unanticipated changes in demand or technological developments could have a significant impact on the value of our inventory and our results of operations.

Long-lived Assets and Intangible Assets. We assess the impairment of long-lived assets and intangible assets whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Circumstances which could trigger a review include, but are not limited to the following: significant decreases in the market price of the asset; significant adverse changes in the business climate or legal factors; accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of the asset; current period cash flow or operating losses combined with a history of losses or a forecast of continuing losses associated with the use of the asset; and current expectation that the asset will more likely than not be sold or disposed of significantly before the end of its estimated useful life. Whenever events or changes in circumstances suggest that the carrying amount of long-lived assets may not be recoverable, we estimate the future cash flows expected to be generated by the asset from its use or eventual disposition. If the sum of the expected future cash flows, which includes revenue, is less than the carrying amount of those assets, we recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets. Significant management judgment is required in the forecasts of future operating results that are used in the discounted cash flow method of valuation.

As of January 28, 2012, we had a total of $141.5 million in acquired intangible assets. Of this amount, $10.5 million of in-process research and development (“IPR&D”) was evaluated based on an annual impairment test at the beginning of the fourth quarter by comparing the current fair value of the IPR&D asset to its carrying value. No impairment was recorded in fiscal 2012 on our IPR&D.

Goodwill. We perform an annual impairment assessment of goodwill at the beginning of our fiscal fourth quarter, and whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Factors we consider important which could trigger a goodwill impairment review include (i) significant underperformance relative to historical or projected future operating results, (ii) significant changes in the manner of our use of the acquired assets or the strategy for our overall business, (iii) significant negative industry or economic trends, (iv) a significant decline in our stock price for a sustained period and (v) a significant change in our market capitalization relative to our net book value. When performing our assessment, we include a control premium, in addition to our fair value to reflect the full value and amount that a buyer would be willing to pay for the company. Since our inception, we have not recognized any impairment of goodwill.

Litigation Costs. From time to time, we are involved in legal actions arising in the ordinary course of business. There can be no assurance these actions or other third party assertions will be resolved without costly litigation, in a manner that does not adversely impact our financial position, results of operations or cash flows or without requiring royalty payments in the future, which may adversely impact gross margins. We are aggressively defending these litigation matters and believe no material adverse outcome will result. However, given uncertainties associated with any litigation, if our assessments prove to be wrong, or if additional information becomes available such that we estimate that there is a probable loss or probable range of loss associated with these contingencies, then we would be required to record liabilities to cover those losses, which could materially impact our results of operations, financial position and cash flows.

Results of Operations

Despite the challenges we faced during fiscal 2012, we finished the year with net income of $615 million, or $0.99 per share, and generated $771 million in cash from operations. We finished the year with more than $2.2 billion in cash, cash equivalents and short-term investments, even after repurchasing $1.34 billion of our common shares during the year.

Net revenue declined by 6% in fiscal 2012 compared to fiscal 2011, from $3.61 billion to $3.39 billion. The supply chain for our HDD products faced both the effects of a major earthquake in Japan early in the year, and significant flooding in Thailand later in the year. In addition, one of our major cellular customers faced product transitions and significant competitive headwinds. We believe these combined factors impacted our net revenue by approximately 10%. Somewhat offsetting these impacts, we saw good growth in several new products and initiatives, including our products for the TD-SCDMA market for smartphones in China. We currently have a significant market share in this market, and we believe the market will continue to grow as users transition to smartphones in China. In addition, our net revenue for the SSD market more than doubled during the year, and we remain well-positioned to benefit from the growth in popularity of SSD.

In addition to the decline in net revenue, our gross margins declined during the year, from 59.2% in fiscal 2011, to 56.8% in fiscal 2012. Although the average selling price of semiconductor products normally declines over time, the decline in average selling prices of our products in fiscal 2012 outpaced the cost reductions received from our manufacturing partners. In addition, the volume and costs of new product tapeouts in advanced technology nodes has increased, and we were impacted by the significant increase in the cost of gold, which is used in the packaging of our products.

Looking forward, we expect the HDD industry to recover during the first half of fiscal 2013 from the impacts of the floods in Thailand. However, we expect that the normal seasonal impacts to net revenue, primarily to mobile and wireless, will somewhat offset the increase in net revenue from the HDD industry. Taken together, we expect net revenue in the first quarter of fiscal 2013 to be flat to up 6% from the fourth quarter of fiscal 2012. Looking further into the year, we expect to begin to realize net revenue growth in various new product initiatives. In addition to the growth in TD-SCDMA smartphones in China, we have introduced a related WCDMA product that we expect to generate further growth in the coming year. We recently introduced our Armada 1500 applications processor that will be used in the latest version of Google TV. We are also currently shipping the industry's only next-generation 500 gigabyte per platter SoC HDD solution, and we believe this technological advantage will benefit us in fiscal 2013. We have begun working with multiple foundry partners to ensure that our products are qualified and can be manufactured in multiple locations, which we believe will ensure favorable wafer pricing. In addition, we are designing all new products as well as redesigning some existing products with packaging that uses copper wiring, rather than gold wiring.

The following table sets forth information derived from our consolidated statements of operations expressed as a percentage of net revenue.

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	January 30, 2010
Net revenue	100%	100%	100%
Operating costs and expenses:			
Cost of goods sold	43.2	40.8	43.7
Research and development	29.9	24.9	29.5
Selling and marketing	4.7	4.3	5.0
General and administrative	3.0	2.9	6.1
Amortization and write-off of acquired intangible assets	1.4	2.2	3.8
Total operating costs and expenses	82.2	75.1	88.1
Operating income	17.8	24.9	11.9
Interest and other income, net	0.4	0.3	0.3
Income before income taxes	18.2	25.2	12.2
Provision (benefit) for income taxes	0.1	0.2	(0.4)
Net income	18.1%	25.0%	12.6%

Years Ended January 28, 2012 and January 29, 2011

Net Revenue

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Net revenue	$3,393,040	$3,611,893	(6.1)%

Net revenue is gross revenue, net of accruals for estimated sales returns and rebates. The revenue decline during fiscal 2012 was primarily driven by challenges within our mobile and wireless end markets as well as the impact of natural disasters on our storage end markets. Within our mobile and wireless end markets, our leading handset customer faced challenges against their competition. Our mobile and wireless revenues were negatively impacted as our leading handset customer shifted their product volumes to more 2G and 2.5G devices that address several of the emerging markets around the world. This shift has significantly impacted the demand for our 3G solutions. This decline was partially offset by the ramp of our mobile SoC products for the TD handset market in China, which were introduced during the first quarter of fiscal 2012 and ramped up over the course of the year. Within our storage end markets, our net revenue was negatively impacted by both the earthquakes in Japan at the tail end of the first quarter of fiscal 2012 as well as the floods in Thailand during the later part of our fiscal third quarter, which also impacted the fourth quarter of fiscal 2012. These natural disasters caused serious restrictions on our HDD customers' ability to build drives, which in turn affected demand for our SoC solutions for these customers. Over the course of the year, we did experience the ramp up of a significant new customer and the growth in our SSD business, helping to partially offset the negative effects described above. Within our networking end markets, our net revenue increased moderately as demand increased with our largest customer along with the ramp of our EPON and GPON products during fiscal 2012.

In the first quarter of fiscal 2013, we expect net revenue to be in the range of flat to up 6% as compared to fourth quarter of fiscal 2012 as the HDD industry continues its recovery from the floods in Thailand, partially offset by seasonal declines in the wireless consumer markets.

Cost of Goods Sold

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Cost of goods sold	$1,465,805	$1,473,274	(0.5)%
% of net revenue	43.2%	40.8%	

Cost of goods sold as a percentage of net revenue in fiscal 2012 increased by 240 basis points, from 40.8% in fiscal 2011 to 43.2% in fiscal 2012. The increase during fiscal 2012 was primarily driven by declines in the average selling prices of our products, which outpaced the cost reductions received from our manufacturing partners, the volume and costs of new product tapeouts in advanced technology nodes and higher commodity costs in the assembly of our products. Specifically, the cost of gold has increased significantly over the past year.

Our cost of goods sold as a percentage of net revenue may fluctuate in future periods due to, among other things, changes in the mix of products sold, the timing of production ramps and margin structures of new products, increased pricing pressures from our customers and competitors, particularly in the consumer product end markets we serve, the pricing of certain commodities such as gold along with our ability to transition new and existing designs away from gold to copper wiring, charges for obsolete or potentially excess inventory, changes in the costs charged by our foundry, assembly and test subcontractors including our ability to implement our strategy to utilize multiple foundries.

We currently expect that cost of goods sold as a percentage of net revenue in the first quarter of fiscal 2013 will be flat compared to the fourth quarter of fiscal 2012.

Research and Development

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Research and development	$1,013,678	$ 897,578	12.9%
% of net revenue	29.9%	24.9%	

Research and development expenses increased by $116.1 million in fiscal 2012 compared to fiscal 2011, primarily due to a $105.7 million increase in personnel-related costs as a result of increased headcount, contractor services and other professional services. The impact of the higher headcount was slightly offset by lower incentive compensation, as a result of lower profitability. In addition, third party intellectual property costs increased by $4.0 million and we had a $13.2 million increase in various other research and development expenses to support our larger organization. The overall increase was partially offset by a $6.8 million decrease in depreciation expense.

We currently expect that research and development expenses will be approximately flat in the first quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012, as the impact of the reset of calendar 2012 payroll taxes is mostly offset by lower share-based compensation as a result of the completion of vesting of prior grants.

Selling and Marketing

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Selling and marketing	$ 159,434	$ 155,481	2.5%
% of net revenue	4.7%	4.3%	

Selling and marketing expense increased by $4.0 million in fiscal 2012 compared to fiscal 2011 primarily due to a $6.6 million increase in personnel-related costs, including contractor services and other professional services. The increase was partially offset by a $2.6 million decrease in general selling and marketing expense, as we reduced trade show and public relations expenses.

We currently expect that selling and marketing expenses will be slightly higher in the first quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012.

General and Administrative

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
General and administrative	$ 100,620	$ 104,830	(4.0)%
% of net revenue	3.0%	2.9%	

General and administrative expense decreased by $4.2 million in fiscal 2012 compared to fiscal 2011. This included a $1.6 million decrease in legal expenses, primarily due to the conclusion of a significant legal case in the prior fiscal year, and a $2.6 million decrease in stock-based compensation, as a result of adjustments recorded on certain grants connected to performance targets that were not achieved. In addition, incentive compensation expenses were slightly lower due to lower profitability.

We currently expect that general and administrative expenses will be slightly higher in the first quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012.

Amortization and Write-Off of Acquired Intangible Assets

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Amortization and write-off of acquired intangible assets	$ 49,357	$ 79,538	(37.9)%
% of net revenue	1.4%	2.2%	

The decrease in amortization and write-off of acquired intangible assets of $30.2 million in fiscal 2012 compared to fiscal 2011 is primarily due to certain intangible assets becoming fully amortized during the year.

Interest and Other Income, net

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Interest and other income, net	$ 14,913	$ 9,270	60.9%
% of net revenue	0.4%	0.3%	

Interest and other income, net consists primarily of interest earned on cash, cash equivalents and short-term investment balances, gains and losses on the sale of marketable and equity securities and foreign currency impacts, net of interest paid. The increase in interest and other income, net in fiscal 2012 compared to fiscal 2011 was primarily due to higher interest income on our investments due to a slightly higher rate of return and lower currency translation losses. These increases were partially offset by net gains in fiscal 2011 on sales of investments in privately held companies of $5.9 million.

Provision for Income Taxes

	Fiscal Years Ended		
	January 28, 2012	January 29, 2011	% Change in 2012
	(in thousands, except percentage)		
Provision for income taxes	$ 3,968	$ 6,333	(37.3)%
% of net revenue	0.1%	0.2%	

During fiscal 2012, the provision for income taxes consisted of the current income tax liability of $12.4 million a reduction of unrecognized tax benefits of $14.1 million due to the expiration of the statutes of limitations in multiple jurisdictions, an increase in unrecognized tax benefits of $8.0 million including accrual of interest and penalty, an increase of $0.9 million tax expense primarily resulted from tax provision-to-tax return adjustments in various countries; and a decrease in deferred tax expense of $3.2 million due to the increase in the corporate tax rate of a foreign subsidiary. During fiscal 2011, the provision for income taxes was impacted by the current income tax liability of $13.8 million, a reduction of unrecognized tax benefits of $13.8 million due to the expiration of the statutes of limitations in multiple jurisdictions, an increase in unrecognized tax benefits of $8.4 million including accrual of interest and penalty, an increase in deferred tax asset of $1.0 million related to employee stock options for a non-U.S. subsidiary, $2.3 million withholding taxes on dispositions of investments, $3.4 million income tax benefit due to release of valuation allowance from the completion of a non-U.S. audit, $1.5 million benefit for a ruling denial related to our supply chain structure, and a $1.9 million tax expense in a U.S. subsidiary due to the defeat of a state proposition.

Years Ended January 29, 2011 and January 30, 2010

Net Revenue

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Net revenue	$3,611,893	$2,807,687	28.6%

Our net revenue in fiscal 2011 increased by $804 million or 28.6%, from $2.81 billion in fiscal 2010, to $3.61 billion in fiscal 2011. Mobile and wireless revenue more than doubled as a result of the significant growth in demand for our cellular communications products, along with increased demand for our embedded wireless LAN products. Our networking revenue grew 15% during fiscal 2011 compared to fiscal 2010, primarily due to a combination of increased demand for both our client and enterprise Ethernet products, along with an improved macroeconomic environment for capital intensive networking equipment. Despite a challenging first few quarters, overall storage revenue grew 5% in fiscal 2011 as compared to fiscal 2010, due to improved industry demand for hard drives as well as company specific market share gains. The growth in our overall net revenue of approximately 28.6% reflected a combination of increased demand for our newer products, and an improvement in overall economic conditions.

Cost of Goods Sold

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Cost of goods sold	$1,473,274	$1,227,096	20.1%
% of net revenue	40.8%	43.7%	

Cost of goods sold as a percentage of net revenue in fiscal 2011 decreased by 290 basis points, from 43.7% in fiscal 2010 to 40.8% in fiscal 2011. The improvement was primarily driven by the improved cost structure of our newer products as we have continued to benefit from the cost focus during the engineering design phase of our products, continued focus on efficiency and yield improvements. The increases were partially offset by a higher amount of period costs related to production tapeouts for newer products, and rising costs of gold.

Research and Development

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Research and development	$ 897,578	$ 828,176	8.4%
% of net revenue	24.9%	29.5%	

Research and development expenses increased by $69.4 million in fiscal 2011 compared to fiscal 2010, primarily due to a $71.1 million increase in compensation and benefits expense related to headcount increases and temporary help in fiscal 2011. Tools for research and development activities increased by $11.5 million. Amortization expense of technology licenses increased by $9.1 million due to the increases in acquired licenses compared to fiscal 2010. Expenses for outside professional services and other services increased by $4.9 million. These increases were partially offset by a decrease of $13.1 million in restructuring costs, a decrease of $7.2 million in stock-based compensation expense, and a decrease of $6.8 million in depreciation expense due to certain assets being fully depreciated. In addition, legal expenses related to patent filings decreased by $2.6 million due to lower legal activity, while general facility expenses, including software and hardware expenses, decreased by $2.1 million.

Selling and Marketing

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Selling and marketing	$ 155,481	$ 139,404	11.5%
% of net revenue	4.3%	5.0%	

Selling and marketing expense increased $16.1 million in fiscal 2011 compared to fiscal 2010 primarily due to a $10.6 million increase in trade shows and public relations activities as we increased our involvement in these areas in fiscal 2011. Compensation and benefits expenses increased by $12.1 million, primarily due to higher headcount. These increases were partially offset by a decrease of $3.5 million in stock-based compensation expense, a decrease of $1.8 million in restructuring expense, and a decrease of $1.6 million in general facility expense.

General and Administrative

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
General and administrative	$ 104,830	$ 171,362	(38.8)%
% of net revenue	2.9%	6.1%	

General and administrative expense decreased by $66.5 million in fiscal 2011 compared to fiscal 2010 primarily due to the one-time $72.0 million legal settlement recorded during fiscal 2010 in connection with the settlement of the class action securities litigation related to our historical stock option granting practices. Legal fees, on a net basis, decreased by $8.6 million due to lower overall legal activity as a result of the settlement of various litigation matters. Depreciation expense decreased by $8.1 million due to certain assets being fully depreciated. Restructuring costs decreased by $3.6 million due to lower restructuring activity in fiscal 2011. These decreases were partially offset by an increase of $10.8 million in employee-related benefits expense and temporary help. General facility expenses increased by $6.6 million, stock-based compensation expense increased by $5.8 million, outside professional services increased by $1.5 million, and charitable contributions increased by $1.2 million.

Amortization and Write-Off of Acquired Intangible Assets

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Amortization and write-off of acquired intangible assets	$ 79,538	$ 107,534	(26.0)%
% of net revenue	2.2%	3.8%	

The decrease in amortization and write-off of acquired intangible assets of $28.0 million in fiscal 2011 compared to fiscal 2010 is primarily due to certain intangible assets being fully amortized. In addition, no write-off was made in fiscal 2011, while a write-off occurred in fiscal 2010. In fiscal 2010, we determined that certain acquisition-related intangibles associated with the acquisition of the ICAP Business were partially impaired. The primary reason for the partial write-off of certain purchased intangibles from the ICAP Business was due to the transition to a newer product by a large customer. The amount of the purchased intangibles written-off in fiscal 2010 due to impairment was $1.0 million.

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Interest and Other Income, Net

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Interest and other income, net	$ 9,270	$ 8,995	3.1%
% of net revenue	0.3%	0.3%	

Interest and other income, net consists primarily of interest earned on cash, cash equivalents and short-term investment balances, gains and losses on the sale of marketable and equity securities and foreign currency impacts, net of interest paid. The slight increase in interest and other income, net during fiscal 2011, as compared to fiscal 2010, was primarily due to a $8.0 million gain on our severance fund assets in a foreign jurisdiction. Gains on equity investments in privately held companies were slightly higher at $5.9 million in fiscal 2011, compared to gains of $4.9 million in fiscal 2010. During fiscal 2011, we also had $5.4 million of higher interest income due to higher cash and investment balances, as well as slightly higher interest rates on invested balances as compared to fiscal 2010.

Provision (Benefit) for Income Taxes

	Fiscal Years Ended		
	January 29, 2011	January 30, 2010	% Change in 2011
	(in thousands, except percentage)		
Provision (benefit) for income taxes	$ 6,333	$ (10,346)	(161.2)%
% of net revenue	0.2%	(0.4)%	

Our effective tax rate was an expense of 0.7% for fiscal 2011 compared to a benefit of 3.0% for fiscal 2010. The increase in the provision for taxes in 2011 was primarily due to releases of tax contingency reserves in fiscal 2010. During fiscal 2010, we released $34.1 million in uncertain tax positions (including interest and penalties) due to the expiration of the statute of limitations in multiple jurisdictions, compared to $13.8 million in fiscal 2011. In fiscal 2011, the tax rate also benefited from a reduction in our valuation allowance of $3.4 million due to the completion of a non-US audit. We continued to incur significant non-tax deductible expenses such as stock-based compensation expenses and intangible amortization resulting in lower profit before tax in jurisdictions where we are not able to utilize the tax benefits. In addition, the tax benefits associated with our tax incentives vary from year to year based on the relative profitability in Israel, Singapore and Switzerland.

Liquidity and Capital Resources

Our principal source of liquidity as of January 28, 2012 consisted of approximately $2.2 billion of cash, cash equivalents and short-term investments. We believe that our existing cash, cash equivalents and investments, together with cash generated from operations, will be sufficient to cover our working capital needs, capital expenditures, investment requirements and commitments for at least the next 12 months.

Net Cash Provided by Operating Activities

Net cash provided by operating activities was $771.2 million for fiscal 2012 compared to $1.2 billion for fiscal 2011 and $811.5 million for fiscal 2010. The cash inflows from operating activities during fiscal 2012 were primarily due to $884.5 million of net income adjusted for non-cash items, as compared to $1.2 billion during fiscal 2011.

Within working capital during fiscal 2012, accounts receivable decreased by $52.1 million due to lower levels of revenue in the fourth quarter of fiscal 2012 compared to the fourth quarter of fiscal 2011. Inventories increased by $108.7 million due primarily to two factors: (1) the floods in Thailand which increased our inventories of hard drive products at the end of fiscal 2012, and (2) the increased use of "hubs" managed by third party logistics providers. When products are shipped to these third party managed locations, the inventory remains on our books until pulled by the customer. Accounts payable decreased by $27.3 million due to lower levels of purchasing activities near the end of fiscal 2012.

The cash inflows from operating activities in fiscal 2011 were primarily due to $1.2 billion of net income adjusted for non-cash items. Within working capital during fiscal 2011, accounts payable increased by $48.6 million due to higher levels of purchasing to support our business. Deferred income increased by $16.8 million as the inventory levels at our distributors were higher at the end of fiscal 2011. Accrued employee compensation increased by $20.7 million due to higher accruals for incentive compensation programs due to the higher levels of revenue and operating income in fiscal 2011 compared to fiscal 2010. Accounts receivable increased $102.6 million due to higher levels of revenue. During fiscal 2011, other non-current assets and other long-term liabilities both decreased significantly compared to fiscal 2010, primarily as a result of the conversion of our severance plan for our employees in Israel.

The cash inflow from operating activities in fiscal 2010 were due to net income of $684.7 million adjusted for non-cash items changes in working capital items. Within working capital during fiscal 2010, accounts payable increased $144.3 million due to our on-going efforts to manage payment terms with vendors. In addition, inventories decreased by $69.1 million as we reduced our inventory levels earlier in fiscal 2010 in light of the economic downturn and have experienced capacity constraints as we have attempted to restore the levels to support our anticipated revenues. Accrued employee compensation increased by $33.8 million due primarily to the reinstatement of the performance bonus program in fiscal 2010. Significant working capital changes offsetting cash inflows in fiscal 2010 included an increase in accounts receivable of $134.7 million due primarily to the timing of revenue whereby more revenue was recorded toward the end of the fourth quarter of fiscal 2010 compared to fiscal 2009.

Net Cash Used in Investing Activities

Net cash used in investing activities was $590.1 million for fiscal 2012 compared to $529.3 million for fiscal 2011 and $744.0 million for fiscal 2010. The net cash used in investing activities in fiscal 2012 was primarily due to net purchases of investments of $393.5 million. In addition, we paid $93.9 million for acquisitions, purchased $88.8 million of property and equipment mainly to support additional capacity, and purchased $13.8 million of technology licenses in fiscal 2012. The net cash used in investing activities in fiscal 2011 was primarily due to net purchases of investments of $395.8 million. In addition, we purchased $90.2 million of property and equipment mainly to support additional capacity, paid $29.4 million for acquisitions and purchased $23.1 million of technology licenses in fiscal 2011. The net cash used in investing activities in fiscal 2010 was primarily due to net purchases of short-term investments of $686.6 million as we began to ramp up our new investment strategy, purchases of property and equipment of $39.8 million mainly to support additional capacity and purchases of technology licenses of $15.6 million to help accelerate product development in certain applications.

Net Cash Provided by (Used In) Financing Activities

Net cash used in financing activities was $1.24 billion for fiscal 2012 compared to net cash provided by financing activities of $77.4 million for fiscal 2011 and net cash provided by financing activities of $110.5 million for fiscal 2010. For fiscal 2012, net cash used in financing activities was primarily attributable to repurchases under our share repurchase program of 87.8 million shares of our outstanding common shares for a total of $1.3 billion. The cash outflow was partially offset by $97.9 million of proceeds from the issuance of common shares under our stock option and employee stock purchase plans. In fiscal 2011, net cash provided by financing activities was attributable to proceeds from the issuance of common shares under our stock option plan and employee stock purchase plan of $166.0 million, which was partially offset by share repurchases under our share repurchase program. We repurchased 4.9 million common shares for a total of $87.5 million in fiscal 2011.

In fiscal 2010, net cash provided by financing activities was attributable to proceeds from the issuance of common shares under our stock option plan and employee stock purchase plan of $111.6 million, which was partially offset by payments on capital leases of $1.8 million.

Contractual Obligations and Commitments

Under our manufacturing relationships with our foundry partners, cancellation of outstanding purchase orders are allowed but require repayment of all expenses incurred through the date of cancellation. As of January 28, 2012, these foundries had incurred approximately $226.6 million of manufacturing costs and expenses relating to our outstanding purchase orders.

We entered into an agreement with a foundry to secure foundry fabrication capacity for a fixed number of wafers at agreed upon prices. In return, we paid the foundry $174.2 million. As of January 28, 2012, approximately $5.9 million of the prepayment remained. At January 28, 2012, there were no outstanding commitments under the agreement.

The following table summarizes our contractual obligations as of January 28, 2012 and the effect that such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

	Fiscal 2013	Fiscal 2014	Fiscal 2015	Fiscal 2016	Fiscal 2017	Thereafter	Total
Contractual obligations:							
Facilities operating leases, net	$ 19,564	$ 11,470	$ 9,378	$ 5,871	$ 4,384	$ 968	$ 51,635
CAD and other operating leases	48,473	16,078	12,518	4,498	1,934	3414	86,915
Purchase commitments to foundries	226,630	—	—	—	—	—	226,630
Capital purchase obligations	18,976	—	—	—	—	—	18,976
Other long-term obligations (1)	—	14,426	5,985	4,803	402	1,840	27,456
Total contractual cash obligations	$ 313,643	$ 41,974	$ 27,881	$ 15,172	$ 6,720	$ 6,222	$411,612

(1) Amounts represent anticipated future cash payments, including anticipated interest payments not recorded on the consolidated balance sheet.

In addition to the above commitments and contingencies, as of January 28, 2012, we had recorded $78.8 million of unrecognized tax benefits as liabilities. We also had recorded a liability for potential interest and penalties of $28.3 million and $7.0 million, respectively, as of January 28, 2012. During the next 12 months, it is reasonably possible that the amount of unrecognized tax benefits could decrease due to potential settlement with tax authorities and the expiration of applicable statutes of limitations. However, the amount cannot be reasonably estimated as we will have negotiations with various tax authorities throughout the year. At this time, we are unable to make a reasonably reliable estimate of the amount of payments in individual years beyond 12 months due to uncertainties in the timing of tax audit outcomes.

Off-balance sheet arrangements: As part of our ongoing business, we do not participate in transactions that generate relationships with unconsolidated entities of financial partnerships, such as entities often referred to as structured finance or special purpose entities ("SPEs"), which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of January 28, 2012, we were not involved in any unconsolidated SPE transactions.

Prospective capital needs: We believe that our existing cash, cash equivalents and short-term investments, together with cash generated from operations, from exercise of employee stock options and purchases under our employee stock purchase plan will be sufficient to cover our working capital needs, capital expenditures, investment requirements and commitments for at least the next 12 months. Our capital requirements will depend on many factors, including our rate of sales growth, market acceptance of our products, costs of securing access to adequate manufacturing capacity, the timing and extent of research and development projects, costs of making improvements to facilities and increases in operating expenses, which are all subject to uncertainty. However, we are named as defendants to several litigation actions and an unfavorable outcome in such actions could have a material adverse effect on our cash flows.

To the extent that our existing cash, cash equivalents and investment balances and cash generated by operations are insufficient to fund our future activities, we may need to raise additional funds through public or private debt or equity financing. We may enter into additional acquisitions of businesses, assets, products, technologies or other strategic arrangements in the future, which could also require us to seek debt or equity financing. Additional equity financing or convertible debt financing may be dilutive to our current shareholders. If we elect to raise additional funds, we may not be able to obtain such funds on a timely basis or on acceptable terms, if at all. If we raise additional funds by issuing additional equity or convertible debt securities, the ownership percentages of existing shareholders would be reduced. In addition, the equity or debt securities that we issue may have rights, preferences or privileges senior to our common shares.

Recent Accounting Pronouncements

Please see “Note 1 — The Company and its Significant Accounting Policies — Recent Accounting Pronouncements” for further details in our notes to the Consolidated Financial Statements set forth in Part II, Item 8 of this Form 10-K.

Related Party Transactions

Please see “Note 14 — Related Party Transactions” for further details in our notes to the Consolidated Financial Statements set forth in Part II, Item 8 of this Form 10-K.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rate Risk. Our interest rate risk relates primarily to our fixed income short-term investment portfolio as we did not have any outstanding debt as of January 28, 2012. We maintain an investment policy that requires minimum credit ratings, diversification of credit risk and limits the long-term interest rate risk by requiring maturities of less than five years. We invest our excess cash primarily in highly liquid debt instruments of the U.S. government and its agencies, time deposits, money market mutual funds, and corporate debt securities. These investments are generally classified as available-for-sale and, consequently, are recorded on our balance sheets at fair market value with their related unrealized gain or loss reflected as a component of accumulated other comprehensive income in shareholders’ equity. Investments in both fixed rate and floating rate interest earning securities carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than predicted if interest rates fall.

To provide an assessment of the interest rate risk associated with our investment portfolio, we performed a sensitivity analysis to determine the impact that an adverse change in interest rates would have on the value of the investment portfolio. Based on investment positions as of January 28, 2012, a hypothetical 100 basis point increase in interest rates across all maturities would result in a $14.5 million incremental decline in the fair market value of the portfolio. Due to our positive cash flow from operations, the relatively short-term nature of our investment portfolio and our ability to hold investments to maturity, such change in fair market value would likely not have resulted in any cash flow impact.

As of January 28, 2012, our investment portfolio included $24.5 million in par value of auction rate securities. Beginning in February 2008, liquidity issues in the global credit markets resulted in a failure of auction rate securities, as the amount of securities submitted for sale in those auctions exceeded the amount of bids. To estimate the fair value of the auction rate securities since that time, we have used a discounted cash flow model based on estimated timing and amount of future interest and principal payments, credit quality of the