Consolidated Balance Sheet Data (end of period):					
Cash, cash equivalents and marketable securities(1)	$ 702.2	$ 1,100.7	$ 1,823.1	$ 2,330.9	$ 2,444.2
Working capital(5)	443.5	855.1	398.5	372.5	555.4
Total assets	5,445.7	6,434.0	7,930.3	11,880.5	10,797.5
Short-term debt (including current portion of long-term debt)	424.6	191.2	123.2	141.6	129.3
Long-term debt (excluding current portion)(1)	356.4	755.8	1,348.5	2,700.5	2,771.5
Shareholders' equity(1)	3,307.4	4,083.3	4,563.9	6,124.6	6,074.7
Capital stock(6)	2,004.9	2,232.3	2,508.0	2,823.6	2,978.3
Consolidated Operating Data:					
Capital expenditures(7)	$ 1,035.4	$ 947.3	$ 1,347.5	$ 3,327.5	$ 1,699.8
Net cash provided by operating activities	983.8	1,012.5	1,469.3	2,422.8	2,052.0
Depreciation and amortization(7)	608.1	704.0	806.8	1,108.2	1,320.2

(1) On November 16, 2000, we issued $1,480.0 million initial aggregate principal amount of zero-coupon unsubordinated convertible notes, due 2010, for net proceeds of $1,457.8 million. On September 22, 1999, we completed an equity offering of 8,970,000 shares of capital stock at $24.88 per share (adjusted for the 3-for-1 stock split) for net proceeds of $216.8 million. On September 22, 1999, we also completed a debt offering of $720.9 million initial aggregate principal amount of zero-coupon convertible Liquid Yield Option™ Notes, due 2009, for net proceeds of $708.3 million. On June 10, 1998, we completed an equity offering of 18,000,000 shares of capital stock at $12.03 per share (adjusted for the 2-for-1 stock split in June 1999 and 3-for-1 stock split in May 2000) for net proceeds of $208.8 million. On June 10, 1998, we also completed a debt offering of $431.7 million initial aggregate principal amount of zero-coupon convertible Liquid Yield Option™ Notes (LYONs), due 2008, for net proceeds of $421.8 million. On April 27, 2001, we issued a redemption notice for the remaining outstanding LYONs, due 2008, which were redeemed and converted into common shares in May and June 2001; the residual aggregate principal amount converted into common shares was $51.7 million. In 2001, we repurchased 9,400,000 common shares for $233.3 million and we have reflected these purchases at cost as a reduction of shareholders' equity. The repurchased shares have been designated to fund our most recent employee stock option plan.

(2) Other income and expenses includes, among other things, funds received through government agencies for research and development expenses, the cost of new plant start-ups, foreign currency gains and losses, gains on sales of marketable securities, the costs of certain activities relating to intellectual property and goodwill amortization. Our reported research and development expenses do not include design center, process engineering, pre-production or industrialization costs.

(3) All share information has been adjusted to reflect the 2-for-1 stock split effected in June 1999 and the 3-for-1 stock split effected in May 2000. See Notes 2.10, 2.20 and 13 to the Consolidated Financial Statements.

(4) For purposes of calculating the ratio of earnings to fixed charges, earnings consist of income before income taxes and minority interests, plus fixed charges. Fixed charges consist of interest expenses.

(5) Working capital is calculated as current assets (excluding cash, cash equivalents and marketable securities) less current liabilities (excluding bank overdrafts and current portion of long-term debt).

(6) Capital stock consists of common stock and capital surplus.

(7) Capital expenditures are net of certain funds received through government agencies, the effect of which is to decrease depreciation.

RISK FACTORS

Risks related to the semiconductor industry

The semiconductor industry is highly cyclical, and severe downturns have had a negative impact on our results of operations

The semiconductor industry is highly cyclical and has been subject to significant economic downturns at various times. In 2001, the industry experienced the most severe downturn in its history. These downturns are typically characterized by production overcapacity, accelerated erosion of average selling prices and reduced revenues. When these downturns occur, such as in 1991 and 1996 through 1998, as well as during the current downturn, which started in the third quarter of 2000, our results of operations are adversely affected. In addition, the markets for semiconductors and electronic systems that use semiconductor products are characterized by rapid technological change, leading to more complex and powerful products, evolving industry standards, intense competition, and fluctuations in end-user demand.

Overall, the semiconductor market expanded significantly from 1983 through 2000. According to trade association data, annual worldwide sales of all semiconductor products, referred to as the total available market, or "TAM," grew from 1983 through 2000 at an average compound annual growth rate of approximately 15.4%. During the upward industry cycle in the first half of the 1990s, the semiconductor industry experienced significantly increased demand and production capacity constraints, with the TAM growth rate reaching over 40% in 1995. Reflecting the current downturn in the industry, the TAM decreased by approximately 32.0% in 2001 compared to 2000 following an increase of approximately 36.8% in 2000 compared to 1999. In addition, the serviceable available market, or SAM (redefined in 2001 to cover approximately 56% of total TAM and excluding PC motherboard major devices such as microprocessors and their peripherals, random access memories ("RAMs"), read-only memories ("ROMs") and semicustom ICs and discrete segments such as the small signal transistor market and optoelectronics devices) decreased by approximately 24% over 2000 following an increase in 2000 of 44.5% compared with 1999. In the face of weakening economic conditions, the addition of new capacity and excess inventory held by end-users has given rise to overcapacity and competitive pricing which affected margins. We cannot guarantee that the current downturn will not continue to be severe or that it will not be followed by one or more future downturns or that any future downturns will not also have an even more severe material adverse effect on our results of operations.

Changes in industry capacity have led to overcapacity and have exacerbated the current industry downturn and may exacerbate future downturns

In the last ten years, many companies invested in building or improving semiconductor manufacturing capacity. According to published industry data and other industry sources, investment in worldwide semiconductor fabrication capacity totaled approximately $38 billion in 1997, $28 billion in 1998, $33 billion in 1999, $59 billion in 2000 and $35 billion in 2001 or approximately 28%, 22%, 22%, 29% and 25%, respectively, of the total available market for such years. In addition to international semiconductor companies, companies specializing in operating semiconductor foundries (companies providing outsourcing capacity on a third party basis) such as Chartered, TSMC or UMC have added significant capacity, particularly in Asia. These capacity additions contributed to an increase of supply over demand during 1997, 1998 and 2001 and to declines in average selling prices and the downturn in the industry during these periods. Recent investments in 2000 and 2001 further increased overcapacity in 2001 and contributed to inventory surpluses, which exacerbated the current downturn. There has also been a shift in existing industry capacity to production of products that compete with our products. We believe that future fluctuations in the rate of industry capacity additions relative to the growth rate in demand for semiconductor products or the transformation of manufacturing facilities to produce products that compete with our products could continue to contribute to fluctuations in average selling prices and affect our results of operations.

During industry downturns, our high fixed costs adversely impact our results

In less favorable industry environments, we are driven to reduce prices in response to competitive pressures and we are also faced with a decline in the utilization rates of our manufacturing facilities due to decreases in product demand. Since the semiconductor industry is characterized by high fixed costs, we are not always able to reduce our total costs in line with revenue declines. Reduced average selling prices for our products therefore adversely affect our results of operations. Furthermore, in periods of reduced customer demand for our products, such as in 2001, our fabrication facilities, or fabs, do not operate at full capacity, thereby increasing our fixed costs. Our gross profit margin declined from 38.9% in 1997 to 38.3% in 1998 during difficult market conditions. Our gross profit margin was 39.6% in 1999, 46.0% in 2000 and 36.3% in 2001. In the difficult market conditions encountered during 2001, our gross profit margin was 44.5% in the first quarter, 33.6% in the second quarter, 33.0% in the third quarter and 31.7% in the fourth quarter. Gross profit margin for the first quarter of 2002 was 33.4%, 170 basis points above fourth quarter 2001, but well below the comparable first quarter 2001 period. We cannot guarantee that the current downturn will not continue to affect the loading of our fabs, particularly our more mature plants and consequently our future gross margins. We cannot guarantee that increased competition in our core product markets will not lead to further price erosion, lower revenue growth rates and lower margins in the future.

Competitive factors in our industry make the competitive environment intense

We compete on the basis of a variety of factors, and our success depends on our ability to compete successfully in all of the relevant areas. We compete in different product lines to various degrees on the following bases:

- price
- technical performance
- product features
- product system compatibility

- product design
- availability
- quality
- sales and technical support.

Our ability to compete successfully also depends on factors partially outside of our control, including:

- successful and timely development of new products and manufacturing processes
- manufacturing yields
- product availability
- industry and general economic trends
- performance of our key customers in the markets they serve.

Our results may be adversely impacted by worldwide economic downturns

Our results are increasingly linked to worldwide economic trends, especially in the United States, the European Union, Japan and Asia. The economic situation in Asia in 1998 had a negative effect on the worldwide semiconductor market and made semiconductor and end-user market requirements more difficult to predict. The deteriorated economic conditions in the United States, the recession in Japan and the slow-down in other markets in which we operate, linked to a declining GDP growth rate and to inventory build-ups by certain customers for semiconductor products, negatively impacted the semiconductor market in 2001 which, following growth of 36.8% in 2000, declined by over 32% in 2001, according to industry sources. We believe that these market conditions have created additional pressures on unit demand and on semiconductor prices in general. The current economic uncertainties have caused our customers to experience reduced demand for their products that include our products and our results of operations have been adversely affected.

Because we operate in an industry where technology changes rapidly, our products may become obsolete and we may not be able to develop new ones in a timely manner

The market for our products is characterized by rapidly changing technology. Therefore, our success is highly dependent upon our ability to develop and manufacture increasingly complex new products on a cost-effective basis, to introduce them in the marketplace on a timely basis, and to have them selected for design into future products of leading systems manufacturers. We have committed and intend to continue to commit substantial resources to the development of new products. Because new product development commitments must be made well in advance of sales, however, our new product decisions must anticipate both future demand and the technology that will be available to supply such demand. Delays in developing new products with anticipated technological advances, failure to win new design projects for customers or in commencing volume shipments of new products, may have an adverse effect on our business. In addition, there can be no assurance that new products, if introduced, will gain market acceptance or will not be adversely affected by new technological changes or new product announcements by others.

Our future success depends in part upon our ability to develop and implement new design and process technologies

Semiconductor design and process technologies are subject to rapid technological change and require large expenditures for capital investment and research and development. We are developing advanced and standardized design tools for our processes as well as libraries of macrofunctions and megafunctions for many of our products. We are also focusing on improving our concurrent engineering practices to better coordinate design activities and reduce overall time-to-market. If we experience substantial delays in developing new design or process technologies or inefficiently implement production increases or transitions, our results of operations could be adversely affected.

Loss of key employees could hurt our competitive position

As is common in the semiconductor industry, success depends to a significant extent upon our key senior executives and research and development, engineering, marketing, sales, manufacturing, support and other personnel. Our success also depends upon our ability to continue to attract, retain and motivate qualified personnel. The competition for such employees is intense, and the loss of the services of any of these key personnel without adequate replacement or the inability to attract new qualified personnel could have a material adverse effect on us. Mr. Pasquale Pistorio, age 66, has been the sole member of our Managing Board and our president and chief executive officer since our formation in 1987. Mr. Pistorio was reappointed at our 2002 annual shareholders' meeting for a three-year term expiring at our annual general meeting to be held in 2005. We do not maintain insurance with respect to the loss of any of our key personnel.

Some of our production processes and materials are environmentally sensitive, which could lead to increased costs due to environmental regulations or to damage to the environment

We are subject to a variety of governmental regulations relating to the use, storage, discharge and disposal of chemicals, gases and other hazardous substances used in our manufacturing processes. We have established proactive environmental policies with respect to the handling of chemicals, gases, emissions and waste disposals from our manufacturing operations, and we have not suffered material environmental claims in the past. We believe that our activities comply with presently applicable environmental regulations in all material respects. All of our facilities have been approved as being in compliance with the EU Eco-Management and Audit Scheme regulations, and have also obtained ISO 14001 certification. We are participating in various working groups set up by the European Commission to propose new legislation regarding the collection, recovery and disposal of electronic equipment, as well as banning the use of lead and some flame retardants in manufacturing electronic components. We intend to proactively implement such new legislation when enacted, in line with our commitment towards environmental protection.

The implementation of any such legislation could adversely affect our manufacturing costs or product sales by requiring us to acquire costly equipment or materials, or to incur other significant expenses in adapting our manufacturing processes or waste and emission disposal processes. Furthermore, environmental claims or our failure to comply with present or future regulations could result in the assessment of damages or imposition of fines against us, suspension of production or a cessation of operations and, as with other companies engaged in similar activities, any failure by us to control the use of, or adequately restrict the discharge of hazardous substances could subject us to future liabilities.

Because we depend on a limited number of suppliers for raw materials, we may experience supply disruptions or pricing pressure

Our manufacturing operations depend upon obtaining adequate supplies of quality raw materials on a timely basis. Thus, our results of operations would be adversely affected if we were unable to obtain adequate supplies of raw materials in a timely manner or if there were significant increases in the costs of raw materials or problems with the quality of these raw materials. A number of materials are available only from a limited number of suppliers, or only from a limited number of suppliers in a particular region. In addition, we purchase raw materials such as silicon wafers, lead frames, mold compounds, ceramic packages and chemicals and gases from a number of suppliers on a just-in-time basis. Although supplies for the raw materials we use are currently adequate, shortages could occur in various essential materials due to interruption of supply or increased demand in the industry. In addition, suppliers may extend lead times, limit our supply or increase prices due to capacity constraints or other factors. Any such supply limitations or price increases could adversely affect our quarterly or annual results of operations.

Risk factors related to our operations

Our operating results may vary significantly from quarter to quarter and annually

Our operating results are affected by a wide variety of factors that could materially and adversely affect revenues and profitability or lead to significant variability of operating results. These factors include, among others, the cyclicality of the semiconductor and electronic systems industries, capital requirements, inventory management and the availability of funding, competition, new product development and technological change, and manufacturing problems. In addition, a number of other factors could lead to fluctuations in quarterly and annual operating results, including:

- order cancellations or reschedulings by customers
- excess inventory held by customers leading to reduced bookings or product returns by key customers
- manufacturing capacity and utilization rates
- restructuring and impairment charges
- changes in distribution and sales arrangements
- intellectual property developments
- failure to win new design projects
- problems with product quality
- litigation
- possible acquisitions
- problems in obtaining adequate raw materials on a timely basis
- the loss of key personnel
- inability to secure sufficient insurance coverage at acceptable terms, in light of current conditions on the insurance market.

Unfavorable changes in the above and other factors have in the past and may in the future adversely affect our operating results. In addition, during periods of industry overcapacity and declining selling prices, customer orders are not generally made as far in advance of the scheduled shipment date as during periods of capacity constraints, and we have experienced an increasing reliance on orders placed and shipped within the same month. During the current industry downturn, as in those in the past, we are experiencing lower levels of backlog, which in turn reduce our management’s ability to forecast production levels, revenues and margins.

We face intense competition in our core product lines as well as in emerging applications from both large integrated manufacturers and smaller niche companies

The semiconductor industry is intensely competitive and we face significant competition in each of our product lines. Some of our competitors are large integrated manufacturing groups that compete with us in most of our product lines. A few of these large companies have substantially greater financial and other resources than we do. As a result, these companies may be able to invest more than us in research and development, in the construction of large-scale, advanced, cost-effective manufacturing plants and in the marketing of products, and this may adversely affect our ability to take advantage of potentially profitable business opportunities. Such large competitors include:

- Advanced Micro Devices
- Agere Systems
- Analog Devices
- Atmel
- Broadcom
- Fairchild
- Fujitsu
- Hitachi

- IBM
- Infineon Technologies
- Intel
- LSI Logic
- Matsushita
- Mitsubishi Electric Corporation
- Motorola
- National Semiconductor
- Nippon Electric Company
- ON Semiconductor
- Philips Semiconductors
- Samsung
- Texas Instruments
- Toshiba

In addition, we are facing increased competition from some of the above companies as well as from smaller niche companies, especially design companies, that specialize in certain product lines and may decide to invest more than we do in research and development and marketing of selected products. These competitors may also use semiconductor foundry companies that produce high volume products and may offer competitive pricing. Such foundry companies such as Chartered, TSMC and UMC have expanded significantly in recent years, particularly in Asia. Other smaller niche competitors include manufacturers of standard semiconductors, integrated circuits for specific applications and fully customized integrated circuits, including both chip and board-level products. In addition, some of our customers have developed their own integrated circuit products and foundry operations.

Certain of our competitors have increased their focus on products that compete with our products

In recent years, some of our competitors have redirected their research and development activities, marketing focus and manufacturing capacity toward products that compete with our products. We believe increased focus by our competitors in our core product markets is generating greater pricing pressure, increased competition for market share in the serviceable available market, and a generally more challenging market environment for us. In addition, as new products are developed, we will face significant competition in each of these markets. We may not be able to establish or maintain a strong market position in all of our product markets.

Because we have our own manufacturing facilities, our capital needs are high compared to competitors who do not produce their own products, and they remain high during industry downturns

As a result of our strategic choice to maintain control of our advanced proprietary manufacturing technologies to serve our customer base and develop our strategic alliances, we require significant amounts of capital to build, expand, modernize and maintain our facilities. Some of our competitors, however, do not manufacture their own products, and therefore do not require significant capital expenditures for their facilities. Our capital expenditures totaled $0.9 billion in 1998, $1.3 billion in 1999 and $3.3 billion in 2000. Due to market conditions, we reduced our capital expenditure for 2001 from an initial plan of $2.5 billion to $1.7 billion. For 2002, we forecast capital expenditures to total approximately $1.2 billion. We seek to modulate such investments in line with market requirements although we may continue to invest significantly in the coming years as the requirements of new technologies increase the cost of production equipment. We will continue to monitor our level of capital spending taking into consideration factors such as trends in the semiconductor market and capacity utilization.

The semiconductor industry also requires heavy commitments of funds for research and development necessary to keep up with the rapid pace of technological change and to consistently develop innovative, well performing and cost-effective products. We intend to continue to increase research and development expenditures in the future, although not necessarily as a percentage of net revenues.

Our research and development efforts in the field of CMOS process development are dependant on alliances and our business, results of operations and prospects could be materially adversely affected by the failure of such alliances in developing new process technologies in line with market requirements

On April 12, 2002, we announced that Motorola’s semiconductor unit had signed a memorandum of understanding proposing to join a comprehensive research and development alliance among us and Philips to provide 90-namometer to 32-namometer chip technologies on 300mm wafers in our Crolles, France research and development center. This announcement followed a previous announcement in March 2002 of an agreement among us, Philips and TSMC which completed an existing agreement between Philips and us concerning joint research and development and the operation of a 300mm pilot line in Crolles. Joint investment is intended to reach $1.4 billion by 2005 with the stated goal of accelerating the development of future technologies and their proliferation throughout the semiconductor industry. See “Item 4. Information on the Company—Research and Development”. We expect to finalize the terms of this new alliance with Motorola shortly. However, there can be no assurance that we will be able to achieve this objective on satisfactory terms, that our alliances with Philips, Motorola and/or TSMC will enable us to effectively develop new technologies which meet customer demands, or that our operations will not be adversely affected by unforeseen events and the sizeable risks related to the development of new technologies, including unforeseen extra costs, which could materially adversely affect our business, results of operations and prospects.

We could need additional funding in the coming years

At December 31, 2001, we had a negative net financial position (total debt net of cash, cash equivalents and marketable securities) of $456.6 million. The cost of new manufacturing facilities is increasing due to the requirements of advanced sub-micron facilities and technologies as well as the migration from 200mm wafer to the new, more complex 300mm wafer manufacturing equipment. In addition, if we proceed with acquisitions, we may incur additional indebtedness, which could increase our interest costs and adversely affect our results. In such circumstances, we may need to issue additional debt or equity, or both.

Our manufacturing processes are highly complex, costly and potentially vulnerable to impurities and disruptions that can significantly increase our costs and delay product shipments to our customers

Our manufacturing processes are highly complex, require advanced and increasingly costly equipment and are continuously being modified in an effort to improve yields and product performance. Impurities or other difficulties in the manufacturing process can lower yields, interrupt production or result in losses of products in process. As system complexity has increased and sub-micron technology has become more advanced, manufacturing tolerances have been reduced and requirements for precision have become even more demanding. Although in the past few years we have significantly enhanced our manufacturing capability in terms of efficiency, precision and capacity, we have from time to time experienced production difficulties that have caused delivery delays and quality control problems, as is common in the semiconductor industry. We cannot guarantee that we will be able to increase the capacity, efficiency or precision of our manufacturing capabilities in the future to the same extent as in the past. We might also experience production difficulties in the future. In addition, during past periods of high revenue growth for us, our manufacturing facilities have operated at high capacity, which has led to production constraints.

As is common in the semiconductor industry, we have, from time to time, experienced difficulty in ramping up production at new facilities or effecting transitions to new manufacturing processes. As a result, we have suffered delays in product deliveries or reduced yields. In the future, we might face:

- construction delays
- delays in ramping up production at our new facilities or on our new lines, in upgrading or expanding our existing facilities, or in changing our process technologies
- interruptions in production
- delivery delays

- manufacturing problems in achieving acceptable yields
- capacity constraints
- contamination or fires, storms, earthquakes or other acts of nature, for which we may be unable to obtain sufficient insurance coverage on acceptable terms and conditions,

the impact of which is exacerbated during a period of industry constraint.

In addition, our development of fabrication facilities that include 200mm or 300mm capabilities, or which require advanced technologies, has increased the potential for losses associated with production difficulties, imperfections, or other causes of defects. If production is interrupted at a manufacturing facility, we may not be able to shift production to other facilities on a timely basis or customers may decide to purchase products from another supplier. In either case the loss of revenues and impact on our relationships with our customers could be significant. Our operating results could also be adversely affected by the increase in fixed costs and operating expenses related to increases in production capacity if revenues do not increase commensurately.

We may face overcapacity and obsolescence in some of our older fabrication facilities that may lead to plant closures, impairments and inventory write-offs

In a period of market downturn, we may face overcapacity issues, particularly in our older fabrication facilities that use mature process technologies. Like other semiconductor manufacturers, we could have mature fabrication facility capacity being only partially used, which may affect our cost of operations. These considerations led us to record an asset impairment and restructuring charge of $296.3 million in the second quarter 2001, with respect to certain of our more mature 150mm wafer fabs as well as to announce and complete the closing in 2001 of our wafer fab manufacturing facility in Ottawa, Canada. During the third quarter of 2001, we also initiated a plan for the closure of our plant in Rancho Bernado, California, which was completed in April 2002, resulting in an additional asset impairment charge of $23.3 million recorded in 2001. We are continuously reviewing our strategy with respect to our more mature 150mm wafer fabs in order to maintain flexibility and efficiency through difficult market conditions. We announced on January 22, 2002 that without the expected pickup in demand and/or pricing during 2002, we could incur further impairment and restructuring charges with respect to our more mature 150mm fabs in 2002. Further actions may include the sale, wafer production curtailment or closure of other similar facilities. In addition, in the second quarter 2001, we recorded a special inventory charge for obsolescence of $70.7 million in cost of sales due to significant cancellations of customer orders that resulted in unuseable quantities of work in process and finished goods inventories. If we are unable to simultaneously and proportionately cut our manufacturing costs, or make other necessary savings in due time, our cost of operations could be adversely affected in the future.

If our outside wafer suppliers fail to perform, this could adversely affect our ability to exploit growth opportunities

In order to meet anticipated requirements for high-speed complementary metal-oxide silicon (“HCMOS”) wafers, we have used outside suppliers, or foundries, for the supply of up to 15% of our requirements for these wafers. We do not intend to increase our reliance on front-end manufacturing through external foundries beyond this level. In fact, in 2001, in a period of market downturn, our reliance on such suppliers significantly decreased. However, when our markets grow, we may face capacity constraints and we expect to continue to rely on third-party wafer suppliers without having the same degree of management control and supervision over their operations as we do over our own. If these suppliers experience manufacturing difficulties, delays, or reduced yields, our results of operations and ability to satisfy customer demand could suffer. In addition, purchasing rather than manufacturing these products may adversely affect our gross profit margin if the purchase costs of these products are higher than our own manufacturing costs.

Our common share price and operating results may be negatively affected by potential acquisitions

Our growth to date has primarily been organic. In 1999, however, we made three acquisitions: the Peripheral Technology Solutions group from Adaptec for a purchase price of approximately $72 million, Vision Group plc for a purchase price of approximately $41 million and Arithmos for a purchase price of approximately $42 million. In 2000, we acquired from Nortel Networks its semiconductor business including a 150mm manufacturing facility located in Ottawa, Canada, for a purchase price of approximately $60 million. In May 2001, we announced the closure of this facility, which was completed by the end of 2001. In September 2000, we acquired the assets and business of Waferscale Integration, Inc. for approximately $78 million. In December 2000, we acquired Portland Group Inc. (PGI), a vendor of compilers and software development tools to the high-performance parallel computing market, for approximately $18 million. In March 2001, we acquired Ravisent’s consumer electronics business for approximately $56 million. In July 2001, we closed the purchase of a software design center in Prague, Czech Republic from Veridicom Inc., involving the acquisition and licensing of intellectual property for fingerprint biometric security products, for approximately $4 million. On April 15, 2002, we announced the acquisition of Alcatel Microelectronics SA, an affiliate of Alcatel SA, for approximately €390 million (approximately $351 million) and a cooperation agreement for the joint development of DSL chip-sets that will also be made available on the open markets. The acquisition announcement was followed by the announcement of an agreement with AMI Semiconductors Inc. (“AMIS”) for the sale by us to AMIS of Alcatel Microelectronics’ mixed-signal business for approximately €70 million (approximately $63 million). Both transactions remain subject to regulatory approvals and customary conditions to closing of corporate transactions. As a result of the adoption of a new statement by the Financial Accounting Standards Board regarding the accounting to be applied to goodwill and intangible assets subsequent to their initial recognition (FAS 142), to become effective for fiscal years beginning after December 15, 2001, goodwill resulting from certain of these acquisitions may no longer be amortized but may be subject to annual impairment tests to determine their appropriate carrying value.

We may, from time to time, consider making selected additional acquisitions that we believe would complement or expand our existing business. We may pay for these acquisitions with cash, our common shares or both. These acquisitions, if they occur, may have a dilutive effect for existing shareholders and, whether they are paid for in cash or common shares, may negatively affect our common share price. Announcements concerning potential acquisitions could be made at any time.

Acquisitions involve a number of risks that could adversely affect our operating results, including:

- the diversion of management’s attention
- the assimilation of the operations and personnel of the acquired companies
- the assumption of potential liabilities, disclosed or undisclosed, associated with the business acquired, which liabilities may exceed the amount of indemnification available from the seller
- the risk that the financial and accounting systems utilized by the business acquired will not meet our standards
- the risk that the businesses acquired will not maintain the quality of products and services that we have historically provided
- the inability to attract and retain qualified management for the acquired business
- our inability to retain customers of the acquired entity
- the risk of goodwill impairment.

There can be no assurance that (a) we will be able to consummate future acquisitions on satisfactory terms, if at all, (b) adequate financing will be available for future acquisitions on terms acceptable to us, if at all, or (c) any operations acquired will be successfully integrated or that such operations will ultimately have a positive impact on our business.

Our business can be adversely affected by changes in the value of the U.S. dollar

A material variation in the value of the U.S. dollar against the principal European and Asian currencies which have a material impact on us could result in a favorable impact on our net income in the case of an appreciation of the U.S. dollar, or a negative impact on our net income if the U.S. dollar depreciates relative to these currencies. For example, the appreciation registered by the U.S. dollar in 2000 and 2001 against the principal European and Asian currencies (excluding the Japanese yen, which appreciated compared to the U.S. dollar) resulted in a negative impact on revenues and a favorable impact on operating income for 2001, because of the favorable impact on cost of sales and operating expenses which exceeded the negative impact on net revenues. Isn addition, the balance sheet impact of translation adjustments has been, and may be expected to continue to be, material from period to period. Our policy is to monitor and cover a portion of our exchange rate exposure, and we manage our operations to mitigate, but not eliminate, the positive or negative impact of exchange rate fluctuations.

Our controlling shareholders' interests may conflict with investors' interests

ST Microelectronics Holding II B.V. ("ST Holding II"), a wholly owned subsidiary of STMicroelectronics Holding N.V. ("ST Holding"), currently owns approximately 36.2% of our issued and outstanding common shares and is effectively in a position to control actions that require shareholder approval, including corporate actions, the election of our Supervisory Board and our Managing Board and the issuance of new shares or other securities. As permitted by our articles of association, the Supervisory Board has specified further selected actions by the Managing Board that require the approval of the Supervisory Board.

ST Holding is currently jointly and directly owned by a French shareholder that is indirectly controlled by the French government and an Italian shareholder in whom the Italian government holds approximately 34.2% of the share capital and retains special powers to approve or determine certain corporate actions. The French shareholder, FT1CI, is a holding company for two of our indirect shareholders, Areva Group and France Telecom, each of which are ultimately controlled by the French government. Finmeccanica is an Italian holding company owned by both the Italian Ministry of Treasury, which controls important actions of Finmeccanica due to its significant holding in it, Istituto per la Ricostruzione Industriale-IRI S.p.A. *in liquidazione* ("I.R.I.", the holding company for Italian state-owned industrial and commercial interests) and the public. The Italian Ministry of Treasury has appointed a majority of the members of Finmeccanica's Board of Directors and pursuant to the provisions of its articles of association and Italian law, retains veto rights over certain major transactions involving Finmeccanica. These French and Italian shareholder groups of ST Holding have entered into a shareholders agreement which enables each of them to designate three members of the Supervisory Board and includes provisions requiring the approval of the Supervisory Board of ST Holding for actions by ST Holding, us and our subsidiaries. In December 2001, the French and Italian shareholder groups of ST Holding (Areva Group, Finmeccanica S.p.A. and France Telecom) signed a new shareholders agreement to facilitate the offering of our common shares by France Telecom and Finmeccanica as well as the offering by France Telecom of exchangeable notes, exchangeable into our common shares. The new shareholders agreement provides that for a two-year period, FT1CI (the holding company for the two indirect French shareholders of ST Holding) and Finmeccanica will share equal voting rights with respect to ST Holding and us despite their difference in indirect economic interest in us resulting from the December 2001 common share offering by France Telecom and Finmeccanica and exchangeable note offering by France Telecom. See "Item 7. Major Shareholders and Related Party Transactions—Shareholders Agreements—New Shareholders Agreement".

Furthermore, the new shareholders agreement provides, among other things, that France Telecom intends to dispose of its entire interest in our common shares following the expiration of a 180-day lock-up period which expires in May 2002. It also provides that Areva has both the freedom to dispose of its stake after a 24-month period following the agreement, as well as the possibility of rebalancing its stake to equal Finmeccanica's stake. Finmeccanica sold certain amounts of common shares held, initially at the same time as France Telecom, and has the right to have additional common shares sold during such 24-month period so that it may sell a total number of common shares equal to the amount sold during such 24-month period by France Telecom.

Finally, the new ST Holding shareholders agreement continues the requirement that unanimous approval of the ST Holding shareholders be obtained before the Supervisory Board members can take certain actions notwithstanding the reduction in their indirect ownership interest in us. The actions covered by these provisions include, among other things, any alteration in our authorized share capital, any new issue of shares by us, any merger, acquisition or joint venture agreement to which we are to be a party, and any items on the agenda for our general shareholders meeting. In addition, as is the case with other companies controlled by the French government, certain ministries of the Republic of France may veto any decision taken by the board of directors of FT1CI.

France Telecom and Areva, the shareholders of FT1CI, are parties to a separate shareholders agreement that requires the approval of the board of directors of each such company before members of the Supervisory Board appointed by the group of French shareholders may approve specified actions to be taken by ST Holding, ST Holding II, us or our subsidiaries. See "Item 7. Major Shareholders and Related Party Transactions—Shareholders Agreements—New Shareholders Agreement".

These various requirements for the prior approval of various actions to be taken by us and our subsidiaries may give rise to a conflict of interest between our interests and investors’ interests, on the one hand, and the interests of the individual shareholders approving such actions, on the other, and may result in a delay in the ability of our Managing Board to respond as quickly as may be necessary in the rapidly changing environment of the semiconductor industry. In particular, our ability to issue new shares or other securities may be limited by the existing shareholders’ desire to maintain their proportionate shareholding, and aggregate shareholding level, at a certain minimum level, such as the 30% percentage threshold that applies to the option agreement relating to preference shares discussed below. Such approval process is, however, subject to the provisions of Dutch law requiring members of our Supervisory Board to act independently in supervising our management.

In addition, France Telecom issued exchangeable notes redeemable by way of exchange for our common shares after January 2, 2004, representing 3.37% of our issued and outstanding common shares in December 2001. The interests of France Telecom as the issuer of the exchangeable notes may not necessarily coincide with our interests.

We may also have contractual and other business relationships with our indirect shareholders and/or their affiliates and may engage in significant transactions from time to time. Although it is anticipated that any such transactions and agreements will be on terms no less favorable to us than we could obtain in comparable contracts with unaffiliated third parties, conflicts of interest may arise between us and our indirect shareholders and their affiliates in a number of circumstances.

Our shareholder structure and our preference shares may deter a change of control

On May 31, 1999, our shareholders at the annual general meeting approved the creation of up to 180,000,000 preference shares. Pursuant to the 3-for-1 stock split effected in May 2000, the number of such preference shares has increased to 540,000,000. These preference shares entitle a holder to full voting rights at any meeting of shareholders and to a preferential right to dividends and distributions upon liquidation. On May 31, 1999, in order to protect ourselves from a hostile takeover or other similar action, we entered into an option agreement with ST Holding II, which provides that (taking into account the 3-for-1 stock split of May 2000) up to 540,000,000 preference shares shall be issued to ST Holding II upon its request and subject to the adoption of a resolution of our Supervisory Board giving our consent to the exercise of the option and upon payment of at least 25% of the par value of the preference shares to be issued. Following the most recent decision of our Supervisory Board, the option is contingent upon ST Holding II retaining at least 30% of our issued share capital at the time of exercise. No preference shares have been issued to date. The preference shares, if issued, would have priority with respect to dividends and distributions upon liquidation over the common shares. The effect of the preference shares may be to deter potential acquirers from effecting an unsolicited acquisition resulting in a change of control. In addition, any issuance of additional capital within the limits of our authorized share capital, as approved by our shareholders, is subject to the approval of our Supervisory Board and of the Supervisory Board of ST Holding.

Substantial sales of our common shares into the market could cause the market price of our common shares to drop significantly

As of December 31, 2001, 889,699,181 of our common shares were issued and outstanding, not including (i) common shares issuable under our various employee stock option plans or employee share purchase plans, (ii) common shares issuable upon conversion of our outstanding convertible debt securities and (iii) 9.4 million shares repurchased in 2001. Substantial sales of existing shares of our common shares or securities exchangeable into our existing shares, or newly issued shares or convertible debt securities by us, could cause the market price of our common shares to drop significantly. The timing and size of any future primary or secondary offerings will depend upon market conditions as well as a variety of factors.

The shareholders of ST Holding signed a new shareholders agreement on December 10, 2001 that states that France Telecom intends to dispose as soon as possible of its indirect interest in our common shares, while Areva has obtained its freedom to dispose of its stake after a 24-month period from the date of such agreement, as well as the possibility of rebalancing its stake to equal Finmeccanica’s stake. The new shareholders agreement provides that Finmeccanica will have the right to sell additional common shares during such 24-month period so that it may sell a total number of shares equal to the amount sold by France Telecom. For a description of these provisions, see “Item 7. Major Shareholders and Related Party Transactions—Shareholders Agreements—New Shareholders Agreement—Disposals of Our Common Shares”. Under the new shareholders agreement, sales of additional amounts of our common shares by ST Holding II on behalf of its indirect shareholders will not necessarily affect its relative voting rights as shareholders. It is highly likely that additional sales of our common shares will occur. Any such transaction, or publicity concerning such a potential transaction, could negatively affect the market price of our common shares. See “Item 7. Major Shareholders and Related Party Transactions—Shareholders Agreements—New Shareholders Agreement—Disposals of Our Common Shares”.

Disruptions in our relationships with any one of our key customers could adversely affect our results of operations

We have several large customers, some of whom have entered into strategic alliances with us. As of December 31, 2001, our largest customer was Nokia, which accounted for 19.3% of net revenues, and our top ten customers accounted for approximately 50% of net revenues. We cannot guarantee that our largest customers will continue to book the same level of sales with us that they have in the past. Many of our key customers operate in cyclical businesses that are also highly competitive, and their own demands and market positions may vary considerably. Our customers have in the past, and may in the future, vary order levels significantly from period to period. In addition, approximately 16% of our net revenues were made through distributors in 2001 compared to 18% in each of 2000 and 1999. We cannot guarantee that distributors, or any other customers, will continue to place orders with us in the future at the same levels as in prior periods. If we were to lose one or more of our customers or distributors, or if any other key customer were to reduce its bookings, increase its product returns or fail to meet its payment obligations, our operating results could be adversely affected. If orders are cancelled, we may not be able to resell products previously made or require the customers who have ordered these products to pay for them.

We depend on patents to protect our rights to our technology

We depend in part on patents and other intellectual property rights covering our products and their design and manufacturing processes. We intend to continue to seek patents on our inventions relating to product designs and manufacturing processes. The process of seeking patent protection can be long and expensive, however, and we cannot guarantee that we will receive patents from currently pending or future applications. Even if patents are issued, they may not be of sufficient scope or strength to provide meaningful protection or any commercial advantage. In addition, effective patent, copyright and trade secret protection may be unavailable or limited in some countries. Competitors may also develop technologies that are protected by patents and other intellectual property and therefore either be unavailable to us or be made available to us subject to adverse terms and conditions. We may not be able to obtain licenses or other rights to necessary intellectual property on acceptable terms.

Because patent and other intellectual property litigation is costly and unpredictable, our attempts to protect our rights or to defend ourselves against claims made by others could impose high costs and risks on our business

Litigation that could demand financial and management resources may be necessary to enforce our patents or other intellectual property rights. Also, we may become involved in costly litigation brought against us regarding patents, mask works, copyrights, trademarks or trade secrets. If we cannot obtain licenses or other intellectual property rights, or if we have litigation expenses or judgments that are contrary to us, our results of operations or financial condition could be hurt. We have from time to time received, and may in the future receive, communications alleging possible infringement of patents and other intellectual property rights of others. We have in the past negotiated broad patent cross-licenses with many of our competitors enabling us to design, manufacture and sell semiconductor products, without fear of infringing patents held by such competitors. As our sales increase compared to those of our competitors, the strength of our patent portfolio may not be sufficient to guarantee the conclusion or renewal of broad patent cross-licenses on terms which do not affect our results of operations. Furthermore, regardless of the validity or the successful assertion of any third-party patent or other intellectual property claims, we could incur significant costs with respect to the defense thereof that could have a material adverse affect our results of operations or financial condition.

We have benefited from state funding in France and Italy which might become unavailable, and as a result our costs could increase

Like many other semiconductor manufacturers operating in Europe, we have had the benefit of governmental funding for research and development expenses, industrialization costs (which include some of the costs incurred to bring prototype products to the production stage) and capital investment as well as low-interest financing. As a result of our history, our research and development facilities and manufacturing activities are concentrated mainly in France and Italy, and the substantial majority of our state funding has been derived from national and European Union programs in these countries. We have entered into funding agreements with France and Italy, which set forth the parameters for state support to us under selected national programs. These funding agreements require compliance with European Union (“EU”) regulations and approval by EU authorities and annual and project-by-project reviews and approvals.

The EU adopted guidelines in 1995 seeking to limit state aid for research and development activities routinely performed in the normal course of business. We cannot guarantee that we will continue to benefit from state aid for research and development, that such aid will not be revoked or discontinued, or that material aid granted by a government for research and development will not be reviewed or challenged by the EU.

We rely on receiving funds allocated by state governments on a timely basis. However, funding of programs in France and Italy is subject to annual appropriation. If these governments were unable to provide anticipated funding on a timely basis or if existing government-funded programs were curtailed or discontinued, this could have a material adverse effect on our business, operating results and financial condition. From time to time we have experienced delays in the receipt of funding under these programs. As the availability and timing of such funding are substantially outside its control, we may not continue to benefit from such government support, and funding may be delayed from time to time, or sufficient alternative funding may not be available if necessary or any such alternative funding may not be provided on terms as favorable to us as those previously provided. In addition, funding granted to us may be revoked or challenged or discontinued in whole or in part by any competent state or European authority, or competent administrative or judicial body, until the legal time period for challenging or revoking such funding has elapsed.

Because we are a Dutch company subject to the corporate law of The Netherlands, investors might have difficulty protecting their interests in a court of law or otherwise

Our corporate affairs are governed by our articles of association and by the laws governing corporations incorporated in The Netherlands. The corporate affairs of each of our consolidated subsidiaries are governed by the articles of association and by the laws governing such corporations in the jurisdiction in which such consolidated subsidiary is incorporated. The rights of the investors and the responsibilities of members of our Supervisory Board and Managing Board under Dutch law are not as clearly established as under the rules of some U.S. jurisdictions. Therefore, investors may have more difficulty in protecting their interests in the face of actions by our management, members of our Supervisory Board or our controlling shareholders than investors would have if we were incorporated in the United States. Under our articles of association, when our annual accounts are adopted by the general meeting of shareholders, the members of our Managing Board and Supervisory Board are discharged from liability for their actions during the financial year concerned, unless an express reservation is made by the general meeting of shareholders. This is without prejudice to the provisions of Dutch law, including provisions relating to liability of members of Supervisory Boards and Managing Boards upon bankruptcy of a company pursuant to articles 2:138 and 2:149 of the Dutch Civil Code. Notwithstanding the language in our articles of association, effective the financial year commencing on January 1, 2002, Dutch law no longer allows the automatic discharge of the members of our Supervisory Board and of our Managing Board when our annual accounts are adopted by our shareholders. Therefore, for the financial year commencing on January 1, 2002 and for subsequent financial years, in order to obtain such a discharge, the discharge will be introduced as a separate item on the agenda for our annual general meetings of shareholders.

Our executive offices and a substantial portion of our assets are located outside the United States. In addition, ST Holding II and most members of our Managing and Supervisory Boards are residents of jurisdictions other than the United States and Canada. As a result, it may be difficult or impossible for shareholders to effect service within the United States or Canada upon us, ST Holding II, or members of our Managing or Supervisory Boards. It may also be difficult or impossible for shareholders to enforce outside the United States or Canada judgments obtained against such persons in U.S. or Canadian courts, or to enforce in U.S. or Canadian courts judgments obtained against such persons in courts in jurisdictions outside the United States or Canada. This could be true in any legal action, including actions predicated upon the civil liability provisions of the U.S. securities laws. In addition, it may be difficult for shareholders to enforce, in original actions brought in courts in jurisdictions located outside the United States, rights predicated upon the U.S. securities laws.

We have been advised by our Dutch counsel, De Brauw Blackstone Westbroek N.V., that the United States and The Netherlands do not currently have a treaty providing for reciprocal recognition and enforcement of