10-Q 1 d10q.txt QUARTERLY REPORT PERIOD ENDED OCTOBER 28, 2001 ---------- ---------- ---------- SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 ---------- FORM 10-Q ---------- (Mark One) [X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934. For the quarterly period ended October 28, 2001 OR [_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934. For the transition period from to . Commission file number: 0-23985 NVIDIA CORPORATION (Exact Name of Registrant as Specified in Its Charter) Delaware 94-3177549 (State or Other Jurisdiction of (I.R.S. Employer Incorporation or Organization) Identification No.) 2701 San Tomas Expressway Santa Clara, California 95050 (408) 486-2000 (Address, including Zip Code, of Registrant's Principal Executive Offices and Registrant's Telephone Number, including Area Code) ---------- Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [_] The number of shares of the registrant's common stock outstanding as of November 9, 2001 was 144,573,828 shares. ---------- ---------- NVIDIA CORPORATION TABLE OF CONTENTS

2 PART I. FINANCIAL INFORMATION ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) NVIDIA CORPORATION AND SUBSIDIARIES CONDENSED CONSOLIDATED BALANCE SHEETS (In thousands) (Unaudited)

	October 28, 2001	January 28, 2001
~~ASSETS~~		
~~Current assets:~~		
~~Cash and cash equivalents~~	~~$ 398,491~~	~~$ 674,275~~
~~Restricted cash~~	~~7,050~~	~~24,500~~
~~Marketable securities~~	~~318,674~~	~~--~~
~~Total cash, cash equivalents, restricted cash and marketable securities~~	~~724,215~~	~~698,775~~
~~Accounts receivable, less allowances of $14,276 at October 28, 2001 and $8,403 at January 28, 2001~~	~~117,664~~	~~104,988~~
~~Inventory, net~~	~~120,488~~	~~89,905~~
~~Prepaid expenses and other current assets~~	~~9,536~~	~~8,355~~
~~Prepaid and deferred taxes~~	~~35,034~~	~~28,386~~
~~Total current assets~~	~~1,006,937~~	~~930,409~~
~~Property and equipment, net~~	~~108,695~~	~~47,280~~
~~Deposits and other assets~~	~~11,210~~	~~10,909~~
~~Prepaid and deferred taxes~~	~~35,298~~	~~4,034~~
~~Goodwill and purchased intangible assets, net~~	~~85,210~~	~~23,795~~
	~~$1,247,350~~	~~$1,016,427~~
~~LIABILITIES AND STOCKHOLDERS' EQUITY~~		
~~Current liabilities:~~		
~~Accounts payable~~	~~$ 108,953~~	~~$ 72,241~~
~~Accrued liabilities~~	~~73,625~~	~~37,506~~
~~Current portion of capital lease obligations~~	~~4,014~~	~~588~~
~~Deferred revenue~~	~~143,181~~	~~200,000~~
~~Total current liabilities~~	~~329,773~~	~~310,335~~
~~Capital lease obligations, less current portion~~	~~6,941~~	~~378~~
~~Long-term debt~~	~~300,000~~	~~300,000~~
~~Stockholders' equity:~~		
~~Common stock~~	~~72~~	~~68~~
~~Additional paid-in capital~~	~~377,019~~	~~277,029~~
~~Deferred compensation~~	~~--~~	~~(6)~~
~~Accumulated other comprehensive income~~	~~818~~	~~--~~
~~Retained earnings~~	~~232,727~~	~~128,623~~
~~Total stockholders' equity~~	~~610,636~~	~~405,714~~
	~~$1,247,350~~	~~$1,016,427~~

See accompanying notes to condensed consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME (In thousands, except per share data) (Unaudited)

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
~~Net revenues~~	~~$370,241~~	~~$198,165~~	~~$871,432~~	~~$517,046~~
~~Cost of revenues~~	~~231,698~~	~~124,643~~	~~537,564~~	~~324,249~~
~~Gross profit~~	~~138,543~~	~~73,522~~	~~333,868~~	~~192,797~~
~~Operating expenses: Research and development~~	~~44,387~~	~~22,023~~	~~109,392~~	~~59,994~~
~~Sales, general and administrative~~	~~24,786~~	~~14,852~~	~~63,361~~	~~41,569~~
~~Amortization of goodwill and purchased intangible assets~~	~~4,020~~	~~--~~	~~8,687~~	~~--~~
~~Acquisition related charges~~	~~--~~	~~--~~	~~10,337~~	~~--~~
~~Discontinued use of property~~	~~3,230~~	~~--~~	~~3,230~~	~~--~~
~~Total operating expenses~~	~~76,423~~	~~36,875~~	~~195,007~~	~~101,563~~
~~Operating income~~	~~62,120~~	~~36,647~~	~~138,861~~	~~91,234~~
~~Interest and other income, net~~	~~1,682~~	~~4,630~~	~~9,860~~	~~10,056~~
~~Income before tax expense~~	~~63,802~~	~~41,277~~	~~148,721~~	~~101,290~~
~~Income tax expense~~	~~19,141~~	~~13,209~~	~~44,617~~	~~32,413~~
~~Net income~~	~~$ 44,661~~	~~$ 28,068~~	~~$104,104~~	~~$ 68,877~~
~~Basic net income per share~~	~~$ 0.31~~	~~$ 0.21~~	~~$ 0.74~~	~~$ 0.53~~
~~Diluted net income per share~~	~~$ 0.26~~	~~$ 0.17~~	~~$ 0.62~~	~~$ 0.43~~
~~Shares used in basic per share computation~~	~~144,017~~	~~132,005~~	~~141,512~~	~~129,319~~
~~Shares used in diluted per share computation~~	~~170,159~~	~~160,870~~	~~168,854~~	~~158,467~~

See accompanying notes to condensed consolidated financial statements. 4 NVIDIA CORPORATION AND SUBSIDIARIES CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (In thousands) (Unaudited)

	Nine Months Ended	
	October 28, 2001	October 29, 2000

Nine Months Ended	October 28, 2001	October 29, 2000
Cash flows from operating activities: Net income	$ 104,104	$ 68,877
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	28,732	10,721
Deferred income taxes	(10,592)	--
Amortization of deferred compensation	6	103
Stock based compensation	364	--
Tax benefit from employee stock plans	58,299	53,424
Common stock issued in exchange for assets and services	--	1,382
Changes in operating assets and liabilities: Accounts receivable	(12,676)	(37,128)
Inventory	(30,583)	(55,561)
Prepaid income taxes	(27,320)	(23,818)
Prepaid expenses and other current assets	(1,181)	(2,735)
Deposits and other assets	(11,362)	(8,496)
Accounts payable	36,712	21,306
Accrued liabilities	35,573	24,299
Deferred revenue	(56,819)	--
Net cash provided by operating activities	113,257	52,374
Cash flows used in investing activities: Purchases of marketable securities	(316,812)	--
Purchase of property and equipment	(76,815)	(21,594)
Purchase of certain assets from various businesses	(64,109)	--
Release of restricted cash	17,450	--
Net cash used in investing activities	(440,286)	(21,594)
Cash flows from financing activities: Convertible notes--net of issuance costs	(75)	290,838
Sale of common stock under public offering, net of issuance costs	(75)	96,611
Common stock issued under employee stock plans	41,406	16,513
Advance in connection with Microsoft agreement	--	200,000
Equipment lease financing	11,246	--
Payments under capital leases	(1,257)	(1,419)
Net cash provided by financing activities	51,245	602,543
Change in cash and cash		

~~equivalents..... (275,784) 633,323 Cash and cash equivalents at beginning of period..... 674,275 61,560 ---------- ---------- Cash and cash equivalents at end of period..... $ 398,491 $694,883 ========== ========== Cash paid for interest..... $ 14,601 $ 121 ========== ========== Cash paid for taxes..... $ 34,219 $ 233 ========== ==========~~

See accompanying notes to condensed consolidated financial statements. 5 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (1) Basis of presentation The accompanying condensed consolidated unaudited financial statements were prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments except as otherwise noted, considered necessary for a fair presentation have been included. The results for the interim periods presented are not necessarily indicative of the results expected for any future period. The following information should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended January 28, 2001. Reclassifications Certain prior year balances were reclassified to conform to the current period presentation. (2) Recent Pronouncements On June 29, 2001, the Financial Accounting Standards Board ("FASB"), voted unanimously to approve Statement of Financial Accounting Standards No. ("SFAS") 141, "Business Combinations" and SFAS 142, "Goodwill and Other Intangible Assets". SFAS 141 will require the purchase method of accounting on all transactions initiated after June 30, 2001 and the pooling of interests method will no longer be allowed. SFAS 142 will require that goodwill and all identifiable intangible assets that have an indeterminable life, be recognized as assets, but not amortized. These assets will be assessed for impairment at least on an annual basis. Identifiable intangible assets that have a determinable life will continue to be segregated from goodwill and amortized over their useful lives. These assets will be assessed for impairment pursuant to guidance in SFAS 121. Companies will be required to maintain documentation of their impairment testing activities and include significant disclosure in filings in the event of an impairment charge. Goodwill and other intangible assets arising from acquisitions completed before July 1, 2001 (previously recognized goodwill and intangible assets) will be accounted for in accordance with the provisions of SFAS 142 beginning January 28, 2002. The Company has not determined the impact of these pronouncements on its financial position and results of operations. Any acquisitions consummated between July 1, 2001 and January 27, 2002 will be accounted for in accordance with the provisions of SFAS 141 and 142. In October 2001, the FASB issued SFAS 143, "Accounting for Asset Retirement Obligations". SFAS 143 requires that the fair value of retirement obligations be recognized as a liability when they are incurred and that the associated retirement costs be capitalized as a long-term asset and expensed over its useful life. The provisions of SFAS 143 will be effective for fiscal years beginning after June 15, 2002. The Company does not expect that the adoption of SFAS 143 will have a significant effect on its financial position or results of operations. In October 2001, the FASB issued SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". SFAS 144 supercedes SFAS 121, "Accounting for the Impairment of Long-lived Assets and Assets to be Disposed of" and the accounting and reporting provisions of Accounting Principles Board Opinion No. 30, "Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions". SFAS 144 establishes a single accounting model for impairment or disposal by sale of long-lived assets. The provisions of SFAS 144 will be effective for fiscal years beginning after December 15, 2001. The Company does not expect that the adoption of SFAS 144 will have a significant effect on its financial position or results of operations. 6 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued) (Unaudited) (3) Business Combination During the first nine months of fiscal year 2002, the Company completed the purchase of certain assets from various businesses, including 3dfx Interactive, Inc. ("3dfx") and other acquisitions, for an aggregate purchase price of approximately $78.7 million. These acquisitions have been accounted for under the purchase method of accounting. Excluding the 3dfx transaction, the aggregate purchase price for all other acquisitions are immaterial to the financials of the Company. On April 18, 2001, the Company completed the purchase of certain assets of 3dfx, including patents and patent applications. Under the terms of the Asset Purchase Agreement, the cash consideration due at the closing was $70.0 million, less $15.0 million that was loaned to 3dfx pursuant to a Credit Agreement dated December 15, 2000, between the Company and 3dfx. Pursuant to the Asset Purchase Agreement, following the closing, the Company is to pay 3dfx additional consideration in the form of stock equal to two million shares of the Company's common stock, subject to 3dfx satisfying certain conditions. If the debts and liabilities of 3dfx cannot be satisfied, under some circumstances, 3dfx could receive a post-closing advance from the Company of up to $25.0 million and this advance would reduce the number of shares of the Company's common stock receivable by 3dfx by up to one million shares. Consequently, due to the possibility of contingent consideration, the components of the estimated purchase price could differ from that presented below. In addition, following the closing, the Company and 3dfx filed a stipulation to dismiss with prejudice the patent litigation between the parties. The litigation was dismissed on April 26, 2001, pursuant to a judicial order. As of October 28, 2001, the 3dfx asset purchase price of $70.0 million and direct transaction costs of $4.1 million were allocated based on fair values as follows:

	Straight-Line Amortization 3dfx Period
	(In thousands) (Years)
~~Property and equipment~~	~~$ 2,433~~ ~~1-2~~
~~Workforce in place....~~	~~3,010~~ ~~2~~
~~Patents and trademarks~~	~~11,510~~ ~~5~~
~~Goodwill.....~~	~~57,208~~ ~~5~~
~~Total.....~~	~~$74,161~~

The final allocation will depend upon the composition of 3dfx assets acquired and the Company's evaluation of the fair value of the net assets. Consequently, the actual allocation of the purchase price could differ from that presented above. 7 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued) (Unaudited) Pro Forma Results of Operations The following summary, prepared on a pro forma basis, presents the results of operations as if 3dfx assets were purchased as of the beginning of the periods presented. Pro forma net income for the three and nine months ending October 28, 2001 includes the impact of amortization of goodwill and intangible assets of $4.0 million and $12.2 million, respectively. Excluded are acquisition related charges $10.3 million for the nine months ending October 28, 2001, and assumed tax benefits of $2.0 million for the same period. For the three and nine months ending October 29, 2000, pro forma net income includes the same amount of amortization of goodwill and intangible assets. Also included are assumed salary related expenses of $4.2 million and $12.5 million and tax benefits of $2.6 million and $7.9 million for the three and nine months ending October 29, 2000.

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
	(In thousands)		(In thousands)	
~~Pro forma revenue.....~~	~~$370,241~~	~~$198,165~~	~~$871,432~~	~~$517,046~~
~~Pro forma net income.....~~	~~$ 44,661~~	~~$ 22,500~~	~~$108,883~~	~~$ 52,079~~
~~Pro forma basic net income per share..~~	~~$ 0.31~~	~~$ 0.17~~	~~$ 0.77~~	~~$ 0.40~~
~~Pro forma diluted net income per share~~	~~$ 0.26~~	~~$ 0.14~~	~~$ 0.64~~	~~$ 0.33~~

(4) Discontinued Use of Property The Company moved into its new headquarters in June 2001 and is still obligated to pay rent for a portion of its previous office space. Since relocating, the Company has been unable to secure a subtenant for its previous office space due to the decrease in demand for commercial rental space as a result of the declining economy. The Company recorded approximately $3.2 million during the current quarter ended October 28, 2001 for the remaining cost related to the preexisting lease, including rental payments, capitalized leasehold improvements, and furniture and fixtures as the leased property or improvements have no substantive future use or benefit. (5) Comprehensive Income (Loss) Other comprehensive income consists of unrealized gains or losses on available-for-sale securities. The components of comprehensive income (loss), net of tax, were as follows:

	Three Months Ended	
	October 28, 2001	January 28, 2001
	(In thousands)	
Net income	$44,661	$31,056
Increase in net unrealized gains on available-for-sale securities, net of tax	818	--
Comprehensive income	$45,479	$31,056

The Company commenced investing activities beginning August 2001 and therefore there were no unrealized gains or losses in prior periods. (6) Net Income Per Share Basic net income per share is computed using the weighted average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period, using the as-if-converted method for convertible debt and the treasury stock method for options. The common-equivalent shares which were antidilutive for the three and nine months ended October 28, 2001 were 8,376,996.

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
	(In thousands)		(In thousands)	
Denominator:				
Denominator for basic net income per share, weighted average shares	144,017	132,005	141,512	129,319
Effect of dilutive securities: Stock options outstanding	26,142	28,865	27,342	29,148
Denominator for diluted net income per share	170,159	160,870	168,854	158,467

(7) Marketable Securities The Company accounts for its investment instruments in accordance with Statement of Financial Accounting Standards No. 115. Cash equivalents consist of financial instruments which are readily convertible into cash and have original maturities of three months or less at the time of acquisition. The Company classifies its marketable debt securities at the date of acquisition in the available-for-sale category. These securities are reported at fair value with the related unrealized gains and losses included in other comprehensive income, net of tax, a component of stockholders' equity. As of October 28, 2001 the average holding period until maturity of the Company's cash equivalents and marketable securities were approximately 14 and 616 days, respectively. The principal amount and related weighted-average interest rates for its investment portfolio was $236.9 million and 2.7% for the cash equivalents, and $317.7 million and 3.5% for the marketable securities as of October 28, 2001. (8) Inventory

	October 28, 2001	January 28, 2001
	(In thousands)	
Raw material.....	$ 6,471	$22,906
Work-in-process....	44,051	11,815
Finished goods.....	69,966	55,184
Total inventory.	$120,488	$89,905

At October 28, 2001, the Company had non-cancelable inventory purchase commitments totaling $360.7 million. (9) Accrued Liabilities

	October 28, 2001	January 28, 2001
	(In thousands)	
Accrued sales and marketing allowances	$43,553	$11,303
Taxes payable.....	10,180	10,369
Accrued payroll and related expenses..	15,597	11,026
Other.....	4,295	4,808
Total accrued liabilities.....	$73,625	$37,506

9 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued) (Unaudited) (10) Segment Information The Company operates in a single industry segment: the design, development and marketing of 3D graphics processors for the PC market. The Company's chief operating decision maker, the Chief Executive Officer, reviews financial information presented on a consolidated basis for purposes of making operating decisions and assessing financial performance. Enterprise-wide information provided on geographic sales is based upon the billing location of the customer. The following table summarizes geographic information on net sales:

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
	(In thousands)		(In thousands)	
~~Revenue:~~				
~~U.S.~~	~~$ 83,919~~	~~$ 13,491~~	~~$128,845~~	~~$ 51,638~~
~~Asia Pacific~~	~~272,327~~	~~156,894~~	~~705,518~~	~~388,215~~
~~Europe~~	~~13,995~~	~~27,780~~	~~37,069~~	~~77,193~~
~~Total revenue~~	~~$370,241~~	~~$198,165~~	~~$871,432~~	~~$517,046~~

Revenues to significant customers, those representing approximately 10% or more of total revenue for the respective periods and the related accounts receivable, are summarized as follows:

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
~~Revenue:~~				
~~Customer A.~~	~~19%~~	~~13%~~	~~5%~~	~~3%~~
~~Customer B.~~	~~15%~~	~~7%~~	~~--~~	~~--~~
~~Customer C.~~	~~14%~~	~~21%~~	~~24%~~	~~23%~~
~~Customer D.~~	~~9%~~	~~11%~~	~~6%~~	~~6%~~
~~Customer E.~~	~~6%~~	~~7%~~	~~11%~~	~~10%~~
~~Customer F.~~	~~3%~~	~~3%~~	~~11%~~	~~6%~~
~~Customer G.~~	~~5%~~	~~8%~~	~~10%~~	~~10%~~

	As of October 28, 2001	As of January 28, 2001
~~Accounts Receivable:~~		
~~Customer A....~~	~~26%~~	~~4%~~
~~Customer B....~~	~~--~~	~~1%~~
~~Customer C....~~	~~16%~~	~~18%~~
~~Customer D....~~	~~8%~~	~~3%~~
~~Customer E....~~	~~7%~~	~~7%~~
~~Customer F....~~	~~2%~~	~~6%~~
~~Customer G....~~	~~8%~~	~~16%~~

10 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued) (Unaudited) (11) Microsoft Agreement On March 5, 2000, the Company entered into an agreement with Microsoft in which the Company agreed to develop and sell graphics chips and to license certain technology to Microsoft and its licensees for use in the Xbox video game console under development by Microsoft. In April 2000, Microsoft paid the Company $200.0 million as an advance against graphics chip purchases. Microsoft may terminate the agreement at any time. If termination occurs prior to offset in full of the advance payments, the Company would be required to return to Microsoft up to $100.0 million of the prepayment and to convert the remainder into its preferred stock at a 30% premium to the 30-day average trading price of its common stock preceding Microsoft's termination of the agreement. In addition, in the event that an individual or corporation makes an offer to purchase shares equal to or greater than thirty percent (30%) of the outstanding shares of its common stock, Microsoft has first and last rights of refusal to purchase the stock. The graphics chip contemplated by the agreement is highly complex, and the development and release of the Microsoft Xbox video game console and its commercial success are dependent upon a number of parties, such as hardware and software developers, and a number of factors, many of which are outside of the Company's control. On February 14, 2001, the Company announced that the Xbox integrated graphic processor and Xbox media communications processor were released to Taiwan Semiconductor Manufacturing Company for prototype fabrication. In July 2001, the Company began to ship production units to Microsoft. The $200.0 million advance has been drawn down by $56.8 million in relation to the shipments made to date. On November 15, 2001, Microsoft released the Xbox to retailers in the U.S. (12) Litigation On February 22, 2000, Graphiques Matrox, Inc. and Systemes Electroniques Matrox Ltd. (collectively "Matrox") filed suit against the Company in the Superior Court, Judicial District of Montreal, Province of Quebec, Canada. The suit alleged that the Company improperly solicited and recruited Matrox employees and encouraged Matrox employees to breach their Matrox confidentiality and/or non-competition agreements. The suit by Matrox sought, among other things, certain injunctive relief. The trial of this matter occurred during April 2001. On July 12, 2001, the court issued its ruling in favor of the Company and dismissed all of Matrox' claims. Matrox has not appealed this ruling and the time for appeal passed on August 13, 2001. On February 2, 2001, the Company was served with a complaint from Sunonwealth Electric Machine Industry Co., Ltd. The complaint was filed against the Company in the United States District Court for the Central District of California, for infringement of US Patent Nos. 6,109,892 and 6,114,785. The underlying case is Sunonwealth v. Adda Corporation, et al, filed in the United States District Court for the Central District on October 19, 2000. Both cases have been consolidated. The patents are for a positioning device for a sensor element of a miniature fan. The Company purchased these fans from Adda. Adda has agreed to defend the Company and to pay any judgment rendered against the Company as well as the cost of any settlement to the extent that the Company's liability in such settlement arises from patent infringement resulting from its purchase of products from Adda. On August 3, 2001 the Court of Appeals for the Federal Circuit issued its decision in a patent infringement action originally brought in 1998 by S3 Incorporated (now SONICblue Incorporated). The decision vacated the district court's summary judgment in favor of the Company and dismissal of the action relative to certain disputed claims and remanded the matter back to the district court. Under a previous settlement agreement with S3, the Company agreed to pay up to $2.0 million if S3's appeal of the district court judgment was decided in favor of S3. The Company made a payment of $1.9 million to S3 in August 2001 to fully satisfy its obligation under the settlement. 11 NVIDIA CORPORATION AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued) (Unaudited) (13) Stockholders' Equity and Stock Split In

August 2001, the Company's Board of Directors approved a two-for-one stock split of the Company's common stock for stockholders of record on August 28, 2001, to be effected in the form of a 100% stock dividend. The transfer agent distributed the shares resulting from the split on September 17, 2001. All share and per-share numbers contained herein reflect this stock split. 12 ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS The following discussion contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which are subject to the "safe harbor" created by those sections. These forward-looking statements include but are not limited to: statements related to industry trends and future growth in the markets for 3D graphics processors; our product development efforts; the timing of our introduction of new products; industry and consumer acceptance of our products; and future profitability. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those in the forward-looking statements. We undertake no obligation to publicly release any revisions to the forward-looking statements or reflect events or circumstances after the date of this document. The "Business Risks" section, among other things, should be considered in evaluating our prospects and future financial performance. Overview We design, develop and market graphics processors and related software for personal computers, or PCs, workstations and digital entertainment platforms. We provide an architecturally compatible "top-to-bottom" family of award-winning performance 3D graphics processors and graphics processing units, or GPUs, that set the standard for performance, quality and features for a broad range of desktop PCs, from professional workstations to low-cost PCs and mobile PCs, from performance laptops to thin-and-light notebooks. Our 3D graphics processors are used for a wide variety of applications, including games, digital image editing, business productivity, the Internet and industrial design. Our graphics processors were the first to incorporate a 128-bit multi-texturing graphics architecture designed to deliver to users of our products a highly immersive, interactive 3D experience with compelling visual quality, realistic imagery and motion, stunning effects and complex object and scene interaction at real-time frame rates. The NVIDIA TNT2 family of graphics processors delivers high performance 3D and 2D graphics at affordable prices, making them the graphics hardware of choice for a wide range of applications for both consumer and commercial use. Our graphics processors are designed to be architecturally compatible backward and forward between generations, giving our original equipment manufacturers, or OEMs, customers and end users a low cost of ownership. We are recognized for developing the world's first GPU, the GeForce 256, which incorporates independent hardware transform and lighting processing units along with a complete rendering pipeline into a single-chip architecture. The GeForce3, GeForce2 and Quadro2 family of desktop and laptop GPUs are the first to incorporate pixel and vertex shaders, enabling the creation of interactive, cinematic-quality images through the use of highly programmable processing elements. The nForce and Xbox integrated graphics processor (IGP) and media and communications processor (MCP) are the industry's first highly-integrated platform processors to incorporate a comprehensive set of multimedia capabilities, such as 2D, 3D, DVD, HDTV, Dolby Digital audio playback and fast broadband and networking communications. Our entire product family provides superior processing and rendering power at competitive prices and are architected to deliver the maximum performance from industry standards such as Microsoft's Direct3D Application Programming Interface (API) and Silicon Graphics, Inc.'s (SGI's) OpenGL API on Windows operating systems and Linux platforms. We recognize revenue from product sales to customers when a contract is in place, the price is determined, shipment is made and collectability is reasonably assured. Our policy on sales to distributors and stocking representatives is to defer recognition of sales and related cost of sales until the distributors and representatives resell the product. Royalty revenue is recognized upon shipment of product by the licensee to its customers. We believe that the software sold with our products is incidental to the product as a whole. Currently, all of our product sales and our arrangements with third-party manufacturers provide for pricing and payment in U.S. dollars. We have not engaged in any foreign currency hedging activities, although we may do so in the future. Since we have no other product line, our business would suffer if for any reason our graphics processors do not achieve widespread acceptance in the PC market. 13 A majority of our sales have been to a limited number of customers and sales are highly concentrated. We sell graphics processors to add-in board and motherboard manufacturers and contract equipment manufacturers, or CEMs. These manufacturers incorporate our processors into the boards they sell to PC OEMs, retail outlets and system integrators. The average selling prices for our products, as well as our customers' products, vary by distribution channel. Our four largest customers accounted for approximately 57% of revenues for the third quarter of fiscal 2002 and 52% of revenues for the first nine months of fiscal 2002. The same four customers accounted for approximately 35% of revenues for the third quarter of fiscal 2001 and 32% of revenues for the first nine months of fiscal 2001. The number of potential customers for our products is limited, and we expect sales to be concentrated to a few major customers for the foreseeable future. As markets for our 3D graphics processors develop and competition increases, we anticipate that product life cycles in the high end will remain short and average selling prices will continue to decline. In particular, average selling prices and gross margins are expected to decline as each product matures. Our add-in board and motherboard manufacturers and major OEM customers typically introduce new system configurations as often as twice per year for the high end, typically based on spring and fall design cycles. In order to maintain average selling prices and gross margins, our existing and new products must achieve competitive performance levels to be designed into new system configurations and must be produced at low costs, in sufficient volumes and on a timely basis, especially with respect to our new products. We currently utilize Taiwan Semiconductor Manufacturing Company, or TSMC, to produce semiconductor wafers, and utilize independent contractors to perform assembly, test and packaging. On April 18, 2001, we completed the purchase of certain assets of 3dfx Interactive, Inc., including patents and patent applications. Under the terms of the Asset Purchase Agreement, the cash consideration due at the closing was $70.0 million, less $15.0 million that was loaned to 3dfx pursuant to a Credit Agreement dated December 15, 2000, between us and 3dfx. Pursuant to the Asset Purchase Agreement, following the closing, we are to pay 3dfx additional consideration in the form of stock equal to two million shares of NVIDIA common stock, subject to 3dfx satisfying certain conditions. In addition, following the closing, we and 3dfx filed a stipulation to dismiss with prejudice the patent litigation between us. The litigation was dismissed on April 26, 2001, pursuant to a judicial order. The transaction is accounted for under the purchase method of accounting. See Note 3 of Notes to Condensed Consolidated Financial Statements. 14 Results of Operations The following table sets forth, for the periods indicated, certain items in our condensed consolidated statements of income expressed as a percentage of total revenue.

	Three Months Ended		Nine Months Ended	
	October 28, 2001	October 29, 2000	October 28, 2001	October 29, 2000
Revenue	100.0%	100.0%	100.0%	100.0%
Cost of revenue	62.6	62.9	61.7	62.7
Gross profit	37.4	37.1	38.3	37.3
Operating expenses:				
Research and development	12.0	11.1	12.6	11.6
Sales, general and administrative	6.7	7.5	7.2	8.0
Amortization of goodwill and purchased intangible assets	1.1	--	1.0	--
Acquisition related charges	--	--	1.2	--
Discontinued use of property	0.9	--	0.4	--
Total operating expenses	20.7	18.6	22.4	19.6
Operating income	16.7	18.5	15.9	17.7
Interest and other income, net	0.5	2.3	1.1	1.9
Income before income tax expense	17.2	20.8	17.0	19.6
Income tax expense	5.2	6.7	5.1	6.3
Net income	12.0%	14.1%	11.9%	13.3%

Three months and nine months ended October 28, 2001, and October 29, 2000 Revenue Revenue increased 87% to $370.2 million in the third quarter ended October 28, 2001 from $198.2 million in the third quarter ended October 29, 2000. Revenue of $871.4 million for the first nine months of fiscal 2002 grew 69% over the first nine months of fiscal 2001. The growth was primarily the result of increased sales of our graphics processors and the strong demand for new products at higher unit average selling prices. Revenue from sales outside of the United States accounted for 77% of total revenue for the third quarter ended October 28, 2001 and 85% of total revenue for the first nine months of fiscal 2002. Revenue from sales outside of the United States represented 93% of total revenue in the third quarter ended October 29, 2000 and 90% in the first nine months of fiscal 2001. Geographic sales are based on bill to address and this decrease in revenue from sales outside of the United States is primarily attributable to sales of the graphic processor used in the Microsoft Xbox product billed to Microsoft in the United States. Revenue by geographical region is allocated to individual countries based on the location to which the products are initially billed. The portion of revenue derived from foreign contract equipment manufacturers, or CEMs, and add-in board and motherboard manufacturers that are attributable to end customers in the United States is not separately disclosed. Although we achieved substantial growth in product revenue for the first nine months of 2002 from the same period in fiscal 2001, we do not expect to sustain this rate of growth in future periods. In addition, we expect that the average selling prices of our products will decline over the lives of the products. The declines in average selling prices of 3D graphics processors in general may also accelerate as the market develops and competition increases. Gross Profit Gross profit consists of total revenue, net of allowances, less cost of revenue. Cost of revenue consists primarily of the costs of semiconductors purchased from contract manufacturers (including assembly, test and packaging), manufacturing support costs (labor and overhead associated with such purchases), inventory 15 provisions and shipping costs. Our gross profit margin can vary in any period depending on the mix of types of graphics processors sold. Gross profit increased 88% from the third quarter of fiscal 2001 to the same period of fiscal 2002, and 73% from the first nine months of fiscal 2001 to the same period of fiscal 2002, primarily due to significant increases in unit shipments and the favorable impact of the higher margin GeForce graphics processors, partially offset by increased sales of the lower margin Xbox graphic processors. Although we achieved substantial growth in gross profit and margin from the first nine months of fiscal 2001 to the same period of fiscal 2002, we do not expect to sustain these rates of growth in future periods. Operating Expenses Research and Development. Research and development expenses consist of salaries and

benefits, cost of development tools and software, costs of prototypes of new products and consultant costs. Research and development expenses increased by 102% from the third quarter of fiscal 2001 to the same period of fiscal 2002, and 82% from the first nine months of fiscal 2001 to the first nine months of fiscal 2002, primarily due to new employees from 3dfx, the move to new headquarters, the addition of personnel and related engineering costs to support our next generation products, such as depreciation charges incurred on capital expenditures and software license and maintenance fees. We anticipate that we will continue to devote substantial resources to research and development, and we expect these expenses to increase in absolute dollars in the foreseeable future due to the increased complexity and the greater number of products under development. Research and development expenses are likely to fluctuate from time to time to the extent we make periodic incremental investments in research and development and these investments may be independent of our level of revenues. Sales, General and Administrative. Sales, general and administrative expenses consist primarily of salaries, commissions and bonuses, promotional tradeshow and advertising expenses, travel and entertainment expenses and legal and accounting expenses. Sales, general and administrative expenses increased by 67% from the third quarter of fiscal 2001 to the same period of fiscal 2002, and 52% from the first nine months of fiscal 2001 to the first nine months of fiscal 2002, primarily due to costs associated with additional personnel and commissions, bonuses on sales of the GeForce families of graphic processors, the move to new headquarters, and a donation to the American Red Cross. We expect sales and marketing expenses to continue to increase in absolute dollars as we continue to expand our operations and our sales. General and administrative expenses are also likely to increase in absolute dollars as we continue to expand our operations. However, we do not expect significant changes in these expenses as a percentage of revenue in future periods. Discontinued use of property. Discontinued use of property consists of write-offs of a portion of our previous office space. Since we relocated in June 2001, we have been unable to secure a subtenant for our previous office space due to the decrease in demand for commercial rental space as a result of the declining economy. We have completed write-offs consisting of the remaining cost related to the preexisting lease, including rental payments, capitalized leasehold improvements, and furniture and fixtures. Amortization of goodwill and purchased intangible assets. Amortization of goodwill and purchased intangible assets consist primarily of goodwill and intangible assets from the asset purchase of 3dfx. The initial allocation of the purchase price was to (a) workforce in place, amortized over two years, (b) patents and trademarks, amortized over five years and (c) goodwill, amortized over five years. The final allocation will depend upon the additional consideration given to 3dfx, subject to 3dfx satisfying certain conditions. Consequently, the actual allocation of the purchase price could differ from that presented in Note 3 of Notes to Condensed Consolidated Financial Statements. Acquisition related charges. Acquisition related charges are attributable to expenses related to the acquisition of 3dfx. These charges primarily consisted of bonuses for employees. 16 Interest and Other Income (Expense), Net Interest expense increased for the third quarter and the first nine months of fiscal 2002 compared to the same periods in fiscal 2001 due to the issuance of $300.0 million of convertible debt in October 2000. Interest income increased 12% and 103% during the third quarter and the first nine months of fiscal 2002 from the same periods in fiscal 2001, respectively, due to higher average cash balances as a result of the $200.0 million advance received from Microsoft in connection with our agreement with Microsoft and the receipt of $387.4 million from our combined convertible debt and common stock offerings that closed in October 2000. Income Taxes Income taxes as a percentage of pretax income was 30% for the first nine months of fiscal 2002 and 32% for the same period in fiscal 2001. Foreign income which is taxed at rates lower than the United States statutory rates contributed to the lower tax rate for the first nine months of fiscal 2002. Amortization of Stock-Based Compensation With respect to stock options granted to employees, we recorded deferred compensation of $4.3 million in 1997 and $361,000 in the one month ended January 31, 1998. These amounts are being amortized over the vesting period of the individual options, generally four years. We amortized approximately $6,000 in the first six months of fiscal 2002 and $103,000 in the first nine months of fiscal 2001. Deferred compensation was fully amortized by the first half of fiscal 2002. Liquidity and Capital Resources As of October 28, 2001, we had $398.5 million in cash and cash equivalents, a decrease of $275.8 million from the end of fiscal 2001. We historically have held our cash balances in cash equivalents such as money market funds or as cash. In August 2001, we began to invest in marketable securities. We place our marketable securities investments with high-quality financial institutions and limit the amount of exposure with any one financial institution and investment instrument. We had $360.7 million of non-cancelable manufacturing commitments outstanding at October 28, 2001. Operating activities generated cash of $113.3 million during the first nine months of fiscal 2002 and $52.4 million during the first nine months of fiscal 2001. The increase from the first nine months of fiscal 2001 to the same period in fiscal 2002 was due to a substantial increase in net income and changes in operating assets and liabilities. Our accounts receivable are highly concentrated. At October 28, 2001, three large customers accounted for approximately 50% of accounts receivable. We may be required to write off bad debts in the future, which could harm our business. Our investing activities have consisted primarily of the purchase of certain assets from various businesses, investments in marketable securities, and purchases of property and equipment and leasehold improvements for our new facility under construction. We incurred acquisition costs of $64.1 million during the first nine months of fiscal 2002, primarily due to the closing of 3dfx asset purchase. There were no acquisitions during the same period a year ago. We began to purchase marketable securities equal to approximately $316.8 million during the first nine months of fiscal 2002. Our capital expenditures increased from $21.6 million in the first nine months of fiscal 2001 to $76.8 million in the first nine months of fiscal 2002. The increase was primarily attributable to the construction of our new facility as well as for purchases of computer and emulation equipment to support increased research and development activities. We expect capital expenditures to increase as we further expand research and development initiatives and as our employee base grows. The timing and amount of future capital expenditures will depend primarily on our future growth. We expect to spend approximately $90.0 million for capital expenditures in fiscal 2002, primarily for software licenses, emulation equipment, purchase of computer and engineering workstations, future phases of enterprise resource planning system implementation and tenant and leasehold improvements in our new headquarters facility. 17 In April 2000, we entered into leases for our new headquarters complex in Santa Clara, California. Our new complex comprises four buildings, representing approximately 500,000 total square feet. The first phase of two buildings consisting of approximately 250,000 square feet was completed in June 2001, and the second phase of one building consisting of approximately 125,000 square feet was completed in July 2001. Restricted cash deposits of $17.5 million were released upon completion of the first and second phase. We expect the last phase consisting of approximately 125,000 square feet to be completed in March 2002. The leases expire in 2012 and include two seven-year renewals at our option. The future minimum lease payments under these operating leases total approximately $221.4 million over the terms of the leases. Financing activities provided cash of $51.2 million in the first nine months of fiscal 2002 compared to $602.5 million in the same period of fiscal 2001. On March 5, 2000, we entered into an agreement with Microsoft in which we agreed to develop and sell graphics chips and to license certain technology to Microsoft and its licensees for use in the Xbox product then under development by Microsoft. In April 2000, Microsoft paid us $200.0 million as an advance against graphics chip

purchases. Microsoft may terminate the agreement at any time. If termination occurs prior to offset in full of the advance payments, we would be required to return to Microsoft up to $100.0 million of the prepayment and to convert the remainder into shares of our preferred stock a 30% premium to the 30-day average trading price of our common stock preceding Microsoft's termination of the agreement. In July 2001, we began to ship production units to Microsoft, and the $200.0 million advance was drawn down by $56.8 million in relation to the shipments made to date. On November 15, 2001, Microsoft released the Xbox to retailers in the U.S. We believe that our existing cash balances and anticipated cash flows from operations will be sufficient to meet our operating and capital requirements for at least the next 12 months. However, there is no assurance that we will not need to raise additional equity or debt financing within this time frame. Additional financing may not be available on favorable terms or at all and may be dilutive to our then-current stockholders. We also may require additional capital for other purposes not presently contemplated. If we are unable to obtain sufficient capital, we could be required to curtail capital equipment purchases or research and development expenditures, which could harm our business. ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK Interest Rate Risk We invest in a variety of financial instruments, consisting principally of investments in commercial paper, money market funds and highly liquid debt securities of corporations, municipalities and the U.S. Government. These investments are denominated in U.S. dollars. We account for our investment instruments in accordance with SFAS 115. All of the cash equivalents and marketable securities are treated as "available-for-sale" under SFAS 115. Investments in both fixed rate and floating rate interest earning instruments carry a degree of interest rate risk. Fixed rate securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if forced to sell securities that decline in market value due to changes in interest rates. However, we reduce our interest rate risk by investing cash primarily in instruments with short maturities. Our exposure to changes in short term interest rates on our portfolio of marketable securities is insignificant as of October 28, 2001 given that the average holding periods until maturity of our cash equivalents and marketable securities were approximately 14 and 616 days, respectively. The principal amount and related weighted-average interest rates for our investment portfolio were $236.9 million and 2.7% for the cash equivalents, and $317.7 million and 3.5% for the marketable securities as of October 28, 2001. Our convertible subordinated notes due 2007 are at a fixed interest rate of 4 3/4% and are not subject to interest rate fluctuations. 18 Exchange Rate Risk We consider our exposure to foreign exchange rate fluctuations to be minimal. Currently, sales and arrangements with third-party manufacturers provide for pricing and payment in U.S. dollars, and therefore are not subject to exchange rate fluctuations. To date, we have not engaged in any currency hedging activities, although we may do so in the future. Fluctuations in currency exchange rates could harm our business in the future. Business Risks In addition to the risks discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations," our business is subject to the risks set forth below. Our operating results are unpredictable and may fluctuate. Many of our revenue components fluctuate and are difficult to predict, and our operating expenses are largely independent of revenue in any particular period. It is therefore difficult for us to accurately forecast revenue and profits or losses. As a result, it is possible that in some quarters our operating results could be below the expectations of securities analysts and investors, which could cause the trading price of our common stock to decline, perhaps substantially. We believe that our quarterly and annual results of operations will be affected by a variety of factors that could adversely affect our revenue, gross profit and results of operations. Factors that have affected our results of operations in the past, and that could affect our results of operations in the future, include the following: . demand and market acceptance for our products and/or our customers' products; . the successful development and volume production of next-generation products; . new product announcements or product introductions by our competitors; . our ability to introduce new products in accordance with OEM design requirements and design cycles; . changes in the timing of product orders due to unexpected delays in the introduction of our customers' products; . fluctuations in the availability of manufacturing capacity or manufacturing yields; . declines in spending by corporations and consumers related to perceptions regarding an economic downturn in the U.S. and international economies; . competitive pressures resulting in lower than expected average selling prices; . rates of return in excess of that forecasted or expected due to quality issues; . the rescheduling of shipments or cancellation of customer orders; . the loss of a key customer or the termination of a strategic relationship; . seasonal fluctuations associated with the PC market; . substantial disruption in our or our suppliers' operations, either as a result of a natural disaster, equipment failure, terrorism or other cause; . supply constraints for and changes in the cost of the other components incorporated into our customers' products, including memory devices; . our ability to reduce the manufacturing costs of our products; . legal and other costs related to defending intellectual property; 19 . bad debt write-offs; . costs associated with the repair and replacement of defective products; . unexpected inventory write-downs; and . introductions of enabling technologies to keep pace with faster generations of processors and controllers. Any one or more of the factors discussed above could prevent us from achieving our expected future revenue or net income. Because most operating expenses are relatively fixed in the short term, we may be unable to adjust spending sufficiently in a timely manner to compensate for any unexpected sales shortfall. We may be required to reduce prices in response to competition or to pursue new market opportunities. If new competitors, technological advances by existing competitors or other competitive factors require us to invest significantly greater resources than anticipated in research and development or sales and marketing efforts, our business could suffer. Accordingly, we believe that period-to-period comparisons of our results of operations should not be relied upon as an indication of future performance. In addition, the results of any quarterly period are not indicative of results to be expected for a full fiscal year. Our 3D graphics solution may not continue to be accepted by the PC market. Our success will depend in part upon continued broad adoption of our 3D graphics processors for high performance 3D graphics in PC applications. The market for 3D graphics processors has been characterized by unpredictable and sometimes rapid shifts in the popularity of products, often caused by the publication of competitive industry benchmark results, changes in dynamic random memory devices pricing and other changes in the total system cost of add-in boards, as well as by severe price competition and by frequent new technology and product introductions. Only a small number of products have achieved broad market acceptance and such market acceptance, if achieved, is difficult to sustain due to intense competition. Since we have no other product lines, our business would suffer if for any reason our current or future 3D graphics processors do not continue to achieve widespread acceptance in the PC market. If we are unable to complete the timely development of or successfully and cost-effectively manufacture and deliver products that meet the requirements of the PC market, our business would be harmed. Our integrated graphics product may not be accepted by the PC market. We expect that integrated graphics chipset products will become an increasing part of the lower cost segment of the PC graphics market. We recently announced an integrated chipset product and are currently developing future products. The integrated chipset market is dominated by Intel. If these products are not competitive in this segment and the integrated chipset segment continues to account for an increasing percentage of

the units sold in the PC market, our business may suffer. We need to develop new products and to manage product transitions in order to succeed. Our business will depend to a significant extent on our ability to successfully develop new products for the 3D graphics market. Our add-in board and motherboard manufacturers and major OEM customers typically introduce new system configurations as often as twice per year, typically based on spring and fall design cycles. Accordingly, our existing products must have competitive performance levels or we must timely introduce new products with such performance characteristics in order to be included in new system configurations. This requires that we do the following: . anticipate the features and functionality that consumers will demand; . incorporate those features and functionality into products that meet the exacting design requirements of PC OEMs, or add-in board and motherboard manufacturers and CEMs; 20 . price our products competitively; and . introduce the products to the market within the limited window for PC OEMs and add-in board and motherboard manufacturers. As a result, we believe that significant expenditures for research and development will continue to be required in the future. The success of new product introductions will depend on several factors, including the following: . proper new product definition; . timely completion and introduction of new product designs; . the ability of TSMC and any additional third-party manufacturers to effectively manufacture our new products in a timely manner; . the quality of any new products; . differentiation of new products from those of our competitors; . market acceptance of our products and our customers' products; and . availability of adequate quantity and configurations of various types of memory products. Our strategy is to utilize the most advanced semiconductor process technology appropriate for our products and available from commercial third-party foundries. Use of advanced processes has in the past resulted in initial yield problems. New products that we introduce may not incorporate the features and functionality demanded by PC OEMs, add-in board and motherboard manufacturers and consumers of 3D graphics. In addition, we may not successfully develop or introduce new products in sufficient volumes within the appropriate time to meet both the PC OEMs' design cycles and market demand. We have in the past experienced delays in the development of some new products. Our failure to successfully develop, introduce or achieve market acceptance for new 3D graphics products would harm our business. Our failure to identify new product opportunities or develop new products could harm our business. As markets for our 3D graphics processors develop and competition increases, we anticipate that product life cycles at the high end will remain short and average selling prices will continue to decline. In particular, we expect average selling prices and gross margins for our 3D graphics processors to decline as each product matures and as unit volume increases. As a result, we will need to introduce new products and enhancements to existing products to maintain overall average selling prices and gross margins. In order for our 3D graphics processors to achieve high volumes, leading PC OEMs and add-in board and motherboard manufacturers must select our 3D graphics processor for design into their products, and then successfully complete the designs of their products and sell them. We may be unable to successfully identify new product opportunities or to develop and bring to market in a timely fashion any new products. In addition, we cannot guarantee that any new products we develop will be selected for design into PC OEMs' and add-in board and motherboard manufacturers' products, that any new designs will be successfully completed or that any new products will be sold. As the complexity of our products and the manufacturing process for products increases, there is an increasing risk that we will experience problems with the performance of products and that there will be delays in the development, introduction or volume shipment of our products. We may experience difficulties related to the production of current or future products or other factors may delay the introduction or volume sale of new products we developed. In addition, we may be unable to successfully manage the production transition risks with respect to future products. Failure to achieve any of the foregoing with respect to future products or product enhancements could result in rapidly declining average selling prices, reduced margins, and reduced demand for products or loss of market share. In addition, technologies developed by others may render our 3D graphics products non-competitive or obsolete or result in our holding excess inventory, any of which would harm our business. 21 We rely on third-party vendors to supply us tools for the development of our new products and we may be unable to obtain the tools necessary to develop these products. In the design and development of new products and product enhancements, we rely on third-party software development tools. While we currently are not dependent on any one vendor for the supply of these tools, some or all of these tools may not be readily available in the future. For example, we have experienced delays in the introduction of products in the past as a result of the inability of then available software development tools to fully simulate the complex features and functionalities of our products. The design requirements necessary to meet consumer demands for more features and greater functionality from 3D graphics products in the future may exceed the capabilities of the software development tools available to us. If the software development tools we use become unavailable or fail to produce designs that meet consumer demands, our business could suffer. Our industry is characterized by vigorous protection and pursuit of intellectual property rights or positions that could result in substantial costs to us. The semiconductor industry is characterized by vigorous protection and pursuit of intellectual property rights and positions, which has resulted in protracted and expensive litigation. The 3D graphics market in particular has been characterized recently by the aggressive pursuit of intellectual property positions, and we expect our competitors to continue to pursue aggressive intellectual property positions. In addition, from time to time we receive notices alleging that we have infringed patents or other intellectual property rights owned by third parties. We expect that, as the number of issued hardware and software patents increases, and as competition in our markets intensifies, the volume of intellectual property infringement claims may increase. If infringement claims are made against us, we may seek licenses under the claimants' patents or other intellectual property rights. However, licenses may not be offered at all or on terms acceptable to us, particularly by competitors. The failure to obtain a license from a third party for technology used by us could cause us to incur substantial liabilities and to suspend the manufacture of and sale of one or more products, which could reduce our revenues and harm our business. Furthermore, we may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. We have agreed to indemnify certain customers for claims of infringement arising out of sale of our products. Litigation by or against us or our customers concerning infringement would likely result in significant expense to us and divert the efforts of our technical and management personnel, whether or not the litigation results in a favorable determination for us. We have in the past been subject to patent infringement suits, and we may be subject to patent infringement suits brought by other parties in the future. These future lawsuits could divert our resources and result in the payment of substantial damages. We may be unable to adequately protect our intellectual property. We rely primarily on a combination of patents, trademarks, trade secrets, employee and third-party nondisclosure agreements and licensing arrangements to protect our intellectual property. As of October 31, 2001, we owned 66 issued United States patents and 6 issued foreign patents, and have 124 United States patent applications pending. Our issued patents have expiration dates from June 9, 2012 to December 6, 2019. As of October 31, 2001, our patents and pending patent applications related to technology used by us in connection with our products, including our graphics processors. Our pending patent applications and any future applications may not be approved. In addition, any issued patents may not provide us with competitive advantages or may be challenged by third parties. The enforcement of patents by

others may harm our ability to conduct our business. Others may independently develop substantially equivalent intellectual property or otherwise gain access to our trade secrets or intellectual property. Our failure to effectively protect our intellectual property could harm our business. We have licensed technology from third parties for incorporation in our graphics processors, and expect to continue to enter into license agreements for future products. These licenses may result in royalty payments to third parties, the cross licensing of technology by us or payment of other consideration. If these arrangements are not concluded on commercially reasonable terms, our business could suffer. 22 Our failure to achieve one or more design wins would harm our business. Our future success will depend in large part on achieving design wins, which entails having our existing and future products chosen as the 3D graphics processors for hardware components or subassemblies designed by PC OEMs and add-in board and motherboard manufacturers. Our add-in board and motherboard manufacturers and major OEM customers typically introduce new system configurations as often as twice per year, generally based on spring and fall design cycles. Accordingly, our existing products must have competitive performance levels or we must timely introduce new products with such performance characteristics in order to be included in new system configurations. Our failure to achieve one or more design wins would harm our business. The process of being qualified for inclusion in a PC OEM's product can be lengthy and could cause us to miss a cycle in the demand of end users for a particular product feature, which also could harm our business. Our ability to achieve design wins also depends in part on our ability to identify and ensure compliance with evolving industry standards. Unanticipated changes in industry standards could render our products incompatible with products developed by major hardware manufacturers and software developers, including Intel and Microsoft. This would require us to invest significant time and resources to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards for a significant period of time, our ability to achieve design wins could suffer. We are dependent on the PC market and the slowdown in its growth may have a negative impact on our business. During the first nine months of fiscal 2002, we derived most of our revenue from the sale of products for use in the entire desktop PC market, from professional workstations to low-cost PCs. We expect to continue to derive most of our revenue from the sale or license of products for use in the entire desktop PC market in the next several years. The PC market is characterized by rapidly changing technology, evolving industry standards, frequent new product introductions and significant price competition. These factors result in short product life cycles and regular reductions of average selling prices over the life of a specific product. A reduction in sales of PCs, or a reduction in the growth rate of PC sales, could reduce demand for our products. Moreover, changes in demand could be large and sudden. Since PC manufacturers often build inventories during periods of anticipated growth, they may be left with excess inventories if growth slows or if they have incorrectly forecast product transitions. In these cases, PC manufacturers may abruptly suspend substantially all purchases of additional inventory from suppliers like us until the excess inventory has been absorbed. It is possible that the recent slowing of the economy in the U.S. and international regions, which has negatively impacted some PC manufacturers and led to some reductions in the demand for PCs, could lead to reductions in inventory purchases by PC manufacturers. Any reduction in the demand for PCs generally, or for a particular product that incorporates our 3D graphic processors, could harm our business. The acceptance of next generation products in business PC 3D graphics may not continue to develop. Our success will depend in part upon the demand for performance 3D graphics for business PC applications. The market for performance 3D graphics in business PCs has only recently begun to emerge and is dependent on the future development of, and substantial end-user and OEM demand for, 3D graphics functionality. As a result, the market for business PC 3D graphics computing may not continue to develop or may not grow at a rate sufficient to support our business. The development of the market for performance 3D graphics on business PCs will in turn depend on the development and availability of a large number of business PC software applications that support or take advantage of performance 3D graphics capabilities. Currently, there are only a limited number of software applications like this, most of which are games, and a broader base of software applications may not develop in the near term or at all. Consequently, a broad market for full function performance 3D graphics on business PCs may not develop. Our business prospects will suffer if the market for business PC 3D graphics fails to develop or develops more slowly than expected. 23 We are dependent on a small number of customers and we are subject to order and shipment uncertainties. We have only a limited number of customers and our sales are highly concentrated. We primarily sell our products to add-in board and motherboard manufacturers and CEMs, which incorporate graphics products in the boards they sell to PC OEMs and system builders. Sales to add-in board and motherboard manufacturers and CEMs are primarily dependent on achieving design wins with leading PC OEMs. The number of add-in board and motherboard manufacturers, CEMs and leading PC OEMs is limited. We expect that a small number of add-in board and motherboard manufacturers and CEMs directly, and a small number of PC OEMs indirectly, will continue to account for a substantial portion of our revenue for the foreseeable future. As a result, our business could be harmed by the loss of business from PC OEMs or add-in board and motherboard manufacturers and CEMs. In addition, revenue from add-in board and motherboard manufacturers, CEMs and PC OEMs that have directly or indirectly accounted for significant revenue in past periods, individually or as a group, may not continue, or may not reach or exceed historical levels in any future period. Our business may be harmed by instability in Asia due to the concentration of customers who are located or have substantial operations in Asia, including Taiwan. The People's Republic of China and Taiwan have in the past experienced and currently are experiencing strained relations. A worsening of these relationships or the development of hostilities between the two could result in disruptions in Taiwan and possibly other areas of Asia, which could harm our business. In addition, if relations between the U.S. and The People's Republic of China become strained, our business could be adversely affected. While we believe political instability in Asia has not adversely affected our business, because of our reliance on companies with operations in Asia, continued economic and political instability in Asia might harm it. We may not be successful in producing the processors in volumes required for the Microsoft Xbox product and, even if we do successfully produce these processors in the volumes required, we may not achieve profit margins consistent with those of our other products. Our Xbox IGP and MCP are new, complicated processors. Both processors have increased in complexity and features from what was contemplated at the time we entered into the agreement with Microsoft. There can be no assurance that we will be able to produce these processors in the volume necessary and within the required time frames or that the payments for these processors will be consistent with profit margins achieved on our other products. Finally, there can be no assurance that the Xbox program will be commercially successful, given the high level of competition in the game console market. If any of these risks occur, our business may be harmed. We may be unable to manage our growth and, as a result, may be unable to successfully implement our strategy. Our rapid growth has placed, and is expected to continue to place, a significant strain on our managerial, operational and financial resources. As of October 28, 2001, we had 1,005 employees as compared to 796 employees as of January 28, 2001. We expect that the number of our employees will increase substantially over the next 12 months. Our future growth, if any, will depend on our ability to continue to implement and improve operational, financial and management information and control systems on a timely basis, as well as our ability to maintain effective cost controls.

Further, we will be required to manage multiple relationships with various customers and other third parties. Our systems, procedures or controls may not be adequate to support our operations and our management may be unable to achieve the rapid execution necessary to successfully implement our strategy. We are dependent on key personnel and the loss of these employees could harm our business. Our performance is substantially dependent on the performance of our executive officers and key employees. None of our officers or employees is bound by an employment agreement, and our relationships with these officers and employees are, therefore, at will. We do not have "key person" life insurance policies on any 24 of our employees. The loss of the services of any of our executive officers, technical personnel or other key employees, particularly Jen-Hsun Huang, our President and Chief Executive Officer, would harm our business. Our success will depend on our ability to identify, hire, train and retain highly qualified technical and managerial personnel. Our failure to attract and retain the necessary technical and managerial personnel would harm our business. We depend on third-party fabrications to produce our products. We do not manufacture the semiconductor wafers used for our products and do not own or operate a wafer fabrication facility. Our products require wafers manufactured with state-of-the-art fabrication equipment and techniques. We utilize TSMC to produce our semiconductor wafers and utilize independent contractors to perform assembly, test and packaging. We depend on these suppliers to allocate to us a portion of their manufacturing capacity sufficient to meet our needs, to produce products of acceptable quality and at acceptable manufacturing yields, and to deliver those products to us on a timely basis. These manufacturers may be unable to meet our near-term or long-term manufacturing requirements. We obtain manufacturing services on a purchase order basis and TSMC has no obligation to provide us with any specified minimum quantities of product. TSMC fabricates wafers for other companies, including certain of our competitors, and could choose to prioritize capacity for other users or reduce or eliminate deliveries to us on short notice. Because the lead-time needed to establish a strategic relationship with a new manufacturing partner could be several quarters, there is no readily available alternative source of supply for any specific product. We believe that long-term market acceptance for our products will depend on reliable relationships with TSMC and any other manufacturers used by us to ensure adequate product supply to respond to customer demand. Because of our reliance on TSMC, our business may be harmed by political instability in Taiwan, including the worsening of the strained relations between The People's Republic of China and Taiwan, or if relations between the U.S. and The People's Republic of China are strained due to foreign relations events. Furthermore, any substantial disruption in our suppliers' operations, either as a result of a natural disaster, political unrest, economic instability, equipment failure or other cause, could harm our business. We are dependent primarily on TSMC and we expect in the future to continue to be dependent upon third-party manufacturers to do the following: . produce wafers of acceptable quality and with acceptable manufacturing yields; . deliver those wafers to us and our independent assembly and testing subcontractors on a timely basis; and . allocate to us a portion of their manufacturing capacity sufficient to meet our needs. Our wafer requirements represent a significant portion of the total production capacity of TSMC. Although our products are designed using TSMC's process design rules, TSMC may be unable to achieve or maintain acceptable yields or deliver sufficient quantities of wafers on a timely basis and/or at an acceptable cost. Additionally, TSMC may not continue to devote resources to the production of our products, or to advance the process design technologies on which the manufacturing of our products are based. Any difficulties like these would harm our business. Failure to achieve expected manufacturing yields for existing and/or new products would reduce our product supply and harm our business. Semiconductor manufacturing yields are a function both of product design, which is developed largely by us, and process technology, which typically is proprietary to the manufacturer. Since low yields may result from either design or process technology failures, yield problems may not be effectively determined or resolved until an actual product exists that can be analyzed and tested to identify process sensitivities relating to the design rules that are used. As a result, yield problems may not be identified until well into the production process, and resolution of yield problems would require cooperation by and communication between us and the manufacturer. 25 The risk of low yields is compounded by the offshore location of most of our manufacturers, increasing the effort and time required to identify, communicate and resolve manufacturing yield problems. Because of our potentially limited access to wafer fabrication capacity from our manufacturers, any decrease in manufacturing yields could result in an increase in our per unit costs and force us to allocate our available product supply among our customers. This could potentially harm customer relationships as well as revenue and gross profit. Our wafer manufacturers may be unable to achieve or maintain acceptable manufacturing yields in the future. Our inability to achieve planned yields from our wafer manufacturers could harm our business. We also face the risk of product recalls or product returns resulting from design or manufacturing defects that are not discovered during the manufacturing and testing process. In the event of a significant number of product returns due to a defect or recall, our business could suffer. Failure to transition to new manufacturing process technologies could affect our ability to compete effectively. Our strategy is to utilize the most advanced process technology appropriate for our products and available from commercial third-party foundries. Use of advanced processes may have greater risk of initial yield problems. Manufacturing process technologies are subject to rapid change and require significant expenditures for research and development. We continuously evaluate the benefits of migrating to smaller geometry process technologies in order to improve performance and reduce costs. We have migrated to the .15-micron technology with the GeForce3, Xbox and nForce families of graphics processors, and we believe that the transition of our products to increasingly smaller geometries will be important to our competitive position. Other companies in the industry have experienced difficulty in migrating to new manufacturing processes and, consequently, have suffered reduced yields, delays in product deliveries and increased expense levels. We may experience similar difficulties and the corresponding negative effects. Moreover, we are dependent on our relationships with our third-party manufacturers to migrate to smaller geometry processes successfully. We may be unable to migrate to new manufacturing process technologies successfully or on a timely basis. The 3D graphics industry is highly competitive and we may be unable to compete. The market for 3D graphics processors for PCs in which we compete is intensely competitive and is characterized by rapid technological change, evolving industry standards and declining average selling prices. We believe that the principal competitive factors in this market are performance, breadth of product offerings, access to customers and distribution channels, backward-forward software support, conformity to industry standard APIs, manufacturing capabilities, price of graphics processors and total system costs of add-in boards and motherboards. We expect competition to increase both from existing competitors and new market entrants with products that may be less costly than our 3D graphics processors, or may provide better performance or additional features not provided by our products. We may be unable to compete successfully in the emerging PC graphics market. Our primary source of competition is from companies that provide or intend to provide 3D graphics solutions for the PC market. Our competitors include the following: . suppliers of integrated core logic chipsets that incorporate 2D and 3D graphics functionality as part of their existing solutions, such as Intel, Silicon Integrated Systems and Via Technologies, Inc. ("Via"); . suppliers of graphics add-in boards that utilize their internally developed graphics chips, such as ATI Technologies Inc. and Matrox Electronics Systems Ltd.; . suppliers of mobile graphics processors that incorporate 2D or 3D graphics functionality as

part of their existing solutions, such as ATI, Trident Microsystems, Inc. and the joint venture of a division of SONICblue Incorporated (formerly S3 Incorporated) and Via; . companies that have traditionally focused on the professional market and provide high end 3D solutions for PCs and workstations, including 3Dlabs, SGI and ATI; and 26 . companies that focus on the video game market, such as Imagination Technologies and ST Microelectronics. If and to the extent we offer products outside of the 3D graphics processor market, we may face competition from some of our existing competitors as well as from companies with which we currently do not compete. We cannot accurately predict if we will compete successfully in any new markets we may enter. We may not successfully compete with Intel in the integrated chipset market. It is projected by analysts that integrated chipsets are likely to become a majority share of the PC graphics market. We have recently introduced the nForce chipset, an integrated 3D graphics chipset. The nForce graphics chipset is designed to support microprocessors produced by AMD. Intel is the dominant supplier of integrated 3D graphics chipsets. Intel has significantly greater resources than we do, and the nForce processor, or other 3D graphics products that we may introduce, may not compete effectively against Intel's current chipset products or future products introduced by Intel, either in terms of price or performance. In addition, due to the widespread industry acceptance of Intel's microprocessor architecture and interface architecture, including its accelerated graphics port architecture, or AGP, Intel exercises significant influence over the PC industry and over companies developing products for such architecture. Any significant modifications by Intel to the AGP, the microprocessor or core logic components or other aspects of the PC microprocessor architecture could result in incompatibility with our technology, which would harm our business. In addition, any delay in the public release of information relating to modifications like this could harm our business. In addition to its influence over the PC architecture, Intel has asserted intellectual property rights in various PC architecture interfaces. For example, as a result of patents held by Intel, it has asserted that companies wishing to develop a chipset compatible with the Pentium 4 microprocessor or similar microprocessors obtain a license from Intel. In September 2001 Intel filed a patent infringement suit against Via with respect to a Via chipset for the Pentium 4. We do not have a license from Intel for such a chipset. We expect Intel to continue to do the following: . invest heavily in research and development and continue development of integrated 3D graphics products; . maintain its position as the largest manufacturer of PC microprocessors; . use its intellectual property position with respect to the PC microprocessor and architecture to defend its position in 3D graphics, including the filing of patent infringement suits against competitors; . follow business practices in its PC business which strongly encourage use of Intel integrated chipsets; . increasingly dominate the PC platform; and . promote its product offerings through advertising campaigns designed to engender brand loyalty among PC users. We are dependent on third parties for assembly, testing and packaging of our products. Our graphics processors are assembled and tested by Siliconware Precision Industries Company Ltd., ChipPAC Incorporated and Advanced Semiconductor Engineering. We do not have long-term agreements with any of these subcontractors. As a result of our dependence on third-party subcontractors for assembly, testing and packaging of our products, we do not directly control product delivery schedules or product quality. Any product shortages or quality assurance problems could increase the costs of manufacture, assembly or testing of our products and could harm our business. Due to the amount of time typically required to qualify assemblers and testers, we could experience significant delays in the shipment of our products if we are required to find alternative third parties to assemble or test our products or components. Any delays in delivery of our products could harm our business. 27 We are subject to risks associated with product defects and incompatibilities. Products as complex as those offered by us may contain defects or failures when introduced or when new versions or enhancements to existing products are released. We have in the past discovered software defects and incompatibilities with customers' hardware in certain of our products and may experience delays or lost revenue to correct any new defects in the future. Errors in new products or releases after commencement of commercial shipments could result in loss of market share or failure to achieve market acceptance. Our products typically go through only one verification cycle prior to beginning volume production and distribution. As a result, our products may contain defects or flaws that are undetected prior to volume production and distribution. If these defects or flaws exist and are not detected prior to volume production and distribution, we may be required to reimburse customers for costs to repair or replace the affected products in the field. These costs could be significant and could adversely affect our business and operating results. The production and distribution of defective products could harm our business. We are subject to risks associated with international operations. Our reliance on foreign third-party manufacturing, assembly, testing and packaging operations subjects us to a number of risks associated with conducting business outside of the United States, including the following: . unexpected changes in, or impositions of, legislative or regulatory requirements; . delays resulting from difficulty in obtaining export licenses for certain technology, tariffs, quotas and other trade barriers and restrictions; . longer payment cycles; . imposition of additional taxes and penalties; . the burdens of complying with a variety of foreign laws; and . other factors beyond our control, including terrorism which may delay the shipment of our products. We also are subject to general political risks in connection with our international trade relationships. In addition, the laws of certain foreign countries in which our products are or may be manufactured or sold, including various countries in Asia, may not protect our products or intellectual property rights to the same extent as do the laws of the United States. This makes the possibility of piracy of our technology and products more likely. Currently, all of our arrangements with third-party manufacturers provide for pricing and payment in U.S. dollars, and to date we have not engaged in any currency hedging activities, although we may do so in the future. Fluctuations in currency exchange rates could harm our business in the future. The semiconductor industry is cyclical in nature. The semiconductor industry historically has been characterized by the following factors: . rapid technological change; . cyclical market patterns; . significant average selling price erosion; . fluctuating inventory levels; . alternating periods of overcapacity and capacity constraints; and . variations in manufacturing costs and yields and significant expenditures for capital equipment and product development. 28 In addition, the industry has experienced significant economic downturns at various times, characterized by diminished product demand and accelerated erosion of average selling prices. We may experience substantial period-to-period fluctuations in results of operations due to general semiconductor industry conditions. Failure in operation or future implementation of our enterprise resource planning system could adversely affect our operations. In December 1999, we began the implementation of an SAP A.G. system as our enterprise resource planning or ERP system to replace our information systems in business, finance, operations and service. The first phase of the implementation was successfully completed in June 2000 and our operations are fully functioning under the new ERP system. Future phases of the implementation are expected to occur throughout fiscal 2002. We are heavily dependent upon the proper functioning of our internal systems to conduct our business. System failure or malfunctioning may result in disruptions of operations and inability to process transactions. Our results of operations and financial position could be adversely affected if we encounter unforeseen problems with respect to system operations or future implementations. Some provisions in our certificate of incorporation, our bylaws and our agreement with Microsoft could delay or prevent a change in control. Our certificate of incorporation and bylaws contain provisions that could make it more difficult for a third party to acquire a majority of our outstanding voting stock.

These provisions include the following: . the ability of the board of directors to create and issue preferred stock without prior shareholder approval; . the prohibition of shareholder action by written consent; . a classified board of directors; and . advance notice requirements for director nominations and shareholder proposals. On March 5, 2000, we entered into a licensing and development agreement with Microsoft that included a grant to Microsoft of first and last rights of refusal over any offer we receive to purchase 30% or more of the outstanding shares of our common stock. The provision could also delay or prevent a change in control of our company. We are exposed to fluctuations in the market values of our portfolio investments and in interest rates. For additional information regarding the sensitivity of and risks associated with the market value of portfolio investments and interest rates, see Item 3 "Quantitative and Qualitative Disclosures About Market Risk--Interest Rate Risk". Our stock price may continue to experience significant short-term fluctuations. The price of our common stock has fluctuated greatly. These price fluctuations have been rapid and severe. The price of our common stock may continue to fluctuate greatly in the future due to factors non-company specific, such as the decline in the U.S. economy, or due to a variety of company specific factors, including quarter to quarter variations in our operating results, shortfalls in revenue or earnings from levels expected by securities analysts and the other factors discussed above in these risk factors. In the past, following periods of volatility in the market price of a company's stock, securities class action litigation has been initiated against the issuing company. This type of litigation could result in substantial cost and a diversion of management's attention and resources, which could have an adverse effect on our revenues and earnings. Any adverse determination in this type of litigation could also subject us to significant liabilities. See "Business Risks--Our operating results are unpredictable and may fluctuate." 29 We may not be able to realize the potential financial or strategic benefits of business acquisitions that could hurt our ability to grow our business and sell our products. In the past we have acquired and invested in other businesses that offered products, services and technologies that we believed would help expand or enhance our products and services or help expand our distribution channels. In the future, if we were to make such an acquisition or investment, the following risks could impair our ability to grow our business and develop new products and, ultimately, could impair our ability to sell our products: . difficulty in combining the technology, operations or work force of the acquired business; . disruption of our on-going businesses; . difficulty in realizing the potential financial or strategic benefits of the transaction; . difficulty in maintaining uniform standards, controls, procedures and policies; and . possible impairment of relationships with employees and customers as a result of any integration of new businesses and management personnel. In addition, the consideration for any future acquisition could be paid in cash, shares of our common stock, or a combination of cash and common stock. If the consideration is paid with our common stock, existing stockholders would be further diluted. 30 PART II: OTHER INFORMATION ITEM 1. LEGAL PROCEEDINGS On February 22, 2000, Graphiques Matrox, Inc. and Systemes Electroniques Matrox Ltd. (collectively "Matrox") filed suit against us in the Superior Court, Judicial District of Montreal, Province of Quebec, Canada. The suit alleged that we improperly solicited and recruited Matrox employees and encouraged Matrox employees to breach their Matrox confidentiality and/or non-competition agreements. The suit by Matrox sought, among other things, certain injunctive relief. The trial of this matter occurred during April, 2001. On July 12, 2001, the court issued its ruling in favor of us and dismissed all of Matrox' claims. Matrox has not appealed this ruling and the time for appeal passed August 13, 2001. On February 2, 2001, we were served with a complaint from Sunonwealth Electric Machine Industry Co., Ltd. The complaint was filed against us in the United States District Court for the Central District of California for infringement of US Patent Nos. 6,109,892 and 6,114,785. The underlying case is Sunonwealth v. Adda Corporation, et al, filed in the United States District Court for the Central District on October 19, 2000. Both cases have been consolidated. The patents are for a positioning device for a sensor element of a miniature fan. We purchased these fans from Adda. Adda has agreed to defend us and to pay any judgment rendered against us as well as the cost of any settlement to the extent that our liability in such settlement arises from patent infringement resulting from its purchase of products from Adda. On August 3, 2001 the Court of Appeals for the Federal Circuit issued its decision in a patent infringement action originally brought in 1998 by S3 Incorporated (now SONICblue Incorporated). The decision vacated the district court's summary judgment in favor of us and dismissal of the action relative to certain disputed claims and remanded the matter back to the district court. Under a previous settlement agreement with S3, we agreed to pay up to $2.0 million if S3's appeal of the district court judgment was decided in favor of S3. We made a payment of $1.9 million to S3 in August 2001 to fully satisfy our obligation under the settlement. In addition, we may be subject to litigation in the future. See "Business Risks--Litigation by or against us or our customers concerning infringement would likely result in significant expense to us and divert the efforts of our technical and management personnel, whether or not the litigation results in a favorable determination for us." From time to time, we are also subject to claims in the ordinary course of business, none of which in our view would have a material adverse impact on our business or financial position if resolved unfavorably. ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS At the Annual Meeting of Stockholders held on August 15, 2001, the following proposals were adopted by the margin indicated. As the Annual Meeting was held prior to the effective date of the two-for-one stock split, the following results are presented on a pre-split basis. Proxies for the Annual Meeting were solicited pursuant section 14(a) of the Securities Exchange Act of 1934, as amended, and there was no solicitation in opposition of managements' solicitation. (a) To elect three directors, James C. Gaither, Jen-Hsun Huang, and A. Brooke Seawell to hold office until the 2004 Annual Meeting of Stockholders.

Nominee For Withheld -- ----- ------ ---- ------- -- James C. Gaither.... 59,044,859 748,649 Jen-Hsun Huang..... 50,751,181 9,042,327 A. Brooke Seawell... 59,094,912 698,596

31 (b) To approve an amendment to the Company's Amended and Restated Certificate of Incorporation to increase the authorized number of shares of Common Stock from 200,000,000 to 500,000,000. For.... 45,991,308 Against 13,780,853 Abstain 21,347

(c) To ratify the selection of KPMG LLP as independent accountants of the Company for its fiscal year ended January 27, 2002. For.... 59,577,318 Against 198,973 Abstain 17,217

ITEM 5. OTHER INFORMATION On November 19, 2001, the U.S. Securities and Exchange Commission charged ten of our employees with civil violations of insider trading laws. The United States Attorney's Office separately charged four of these employees with criminal violations of insider trading laws. The charges relate to alleged insider trading of our common stock in March 2000 based on information regarding the Xbox contract with Microsoft Corporation. We have been cooperating fully with the investigations by the SEC and the U.S. Attorney's Office for more than a year and we have placed those employees who were named as defendants by the SEC and the U.S. Attorney on a leave of absence. Neither the SEC nor the U.S. Attorney's Office has indicated to us that any action is contemplated against NVIDIA or any of our key employees, directors or officers. ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K (a) Exhibits None (b) Reports on Form 8-K No reports were filed on Form 8-K during the quarter ended October 28, 2001. 32 SIGNATURE Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, on November 21, 2001. NVIDIA CORPORATION /s/ CHRISTINE B. HOBERG By: _____ Christine B. Hoberg Chief Financial Officer 33