OCLARO, INC.
Form 10-Q
November 10, 2010

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended October 2, 2010

OR

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

For the transition period from ________________ to ________________

Commission file number 000-30684

OCLARO, INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-1303994**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

2584 Junction Avenue, San Jose, California 95134

(Address of principal executive offices, zip code)

(408) 383-1400

(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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes o No þ

Number of shares of common stock outstanding as of November 5, 2010: 49,822,870

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PART I. FINANCIAL INFORMATION

Item 1. ***Financial Statements (Unaudited)***

OCLARO, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	October 2, 2010	July 3, 2010
	(Thousands, except par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 91,117	$ 107,176
Restricted cash	2,835	4,458
Accounts receivable, net	101,909	93,412
Inventories	72,557	62,570
Prepaid expenses and other current assets	16,251	14,905
Total current assets	284,669	282,521
Property and equipment, net	45,453	37,516
Other intangible assets, net	21,873	10,610
Goodwill	30,904	20,000
Other non-current assets	10,107	10,148
Total assets	$ 393,006	$ 360,795
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 60,007	$ 50,103
Accrued expenses and other liabilities	39,855	35,404
Total current liabilities	99,862	85,507
Deferred gain on sale-leaseback	13,406	12,969
Other non-current liabilities	18,992	9,785
Total liabilities	132,260	108,261
Commitments and contingencies (Note 9)		
Stockholders equity:		
Preferred stock: 1,000 shares authorized; none issued and outstanding		
Common stock: $0.01 par value per share; 90,000 shares authorized; 49,812 and 49,396 shares issued and outstanding at October 2, 2010 and July 3, 2010, respectively	498	494
Additional paid-in capital	1,306,695	1,304,779
Accumulated other comprehensive income	32,843	26,907
Accumulated deficit	(1,079,290)	(1,079,646)

Total stockholders equity	260,746	252,534
Total liabilities and stockholders equity	$ 393,006	$ 360,795

The accompanying notes form an integral part of these condensed consolidated financial statements.

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OCLARO, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended	
	October 2, 2010	**September 26, 2009**
	(Thousands, except per share amounts)	
Revenues	$ 121,347	$ 85,110
Cost of revenues	86,521	63,119
Gross profit	34,826	21,991
Operating expenses:		
Research and development	13,711	9,014
Selling, general and administrative	14,813	12,963
Amortization of intangible assets	619	125
Restructuring, merger and related costs	670	1,499
Gain on sale of property and equipment	(21)	(532)
Total operating expenses	29,792	23,069
Operating income (loss)	5,034	(1,078)
Other income (expense):		
Interest income	7	23
Interest expense	(573)	(88)
Loss on foreign currency translation	(3,587)	(1,276)
Other income		5,267
Total other income (expense)	(4,153)	3,926
Income from continuing operations before income taxes	881	2,848
Income tax provision	525	223
Income from continuing operations	356	2,625
Income from discontinued operations, net of tax		1,420
Net income	$ 356	$ 4,045
Basic net income per share:		
Income per share from continuing operations	$ 0.01	$ 0.07
Income per share from discontinued operations		0.04
Basic net income per share	$ 0.01	$ 0.11
Diluted net income per share:		
Income per share from continuing operations	$ 0.01	$ 0.07

Income per share from discontinued operations				0.04
Diluted net income per share	$	0.01	$	0.11
Shares used in computing net income per share:				
Basic		48,115		37,240
Diluted		50,984		38,100

The accompanying notes form an integral part of these condensed consolidated financial statements.

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OCLARO, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Cash flows from operating activities:		
Net income	$ 356	$ 4,045
Adjustments to reconcile net income to net cash used in operating activities:		
Amortization of deferred gain on sale-leaseback	(231)	(238)
Depreciation and amortization	3,833	2,789
Gain on bargain purchase		(5,267)
Gain on sale of discontinued operations		(1,420)
Stock-based compensation expense	1,358	920
Other non-cash adjustments	(21)	(513)
Changes in operating assets and liabilities:		
Accounts receivable, net	(583)	(9,550)
Inventories	(4,902)	2,587
Prepaid expenses and other current assets	(258)	(553)
Other non-current assets	86	809
Accounts payable	6,252	1,372
Accrued expenses and other liabilities	(6,896)	(4,122)
Net cash used in operating activities	(1,006)	(9,141)
Cash flows from investing activities:		
Purchases of property and equipment	(6,882)	(744)
Proceeds from sales of property and equipment	21	620
Sales and maturities of available-for-sale investments		8,150
Transfer (to) from restricted cash	1,696	(30)
Cash (paid for) received from business combinations	(10,482)	3,000
Net cash provided by (used in) investing activities	(15,647)	10,996
Cash flows from financing activities:		
Proceeds from issuance of common stock, net	516	
Repayment of other loans		(16)
Net cash provided by (used in) financing activities	516	(16)
Effect of exchange rate on cash and cash equivalents	78	784
Net increase (decrease) in cash and cash equivalents	(16,059)	2,623
Cash and cash equivalents at beginning of period	107,176	44,561
Cash and cash equivalents at end of period	$ 91,117	$ 47,184

The accompanying notes form an integral part of these condensed consolidated financial statements.

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OCLARO, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Preparation

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Oclaro, Inc., a Delaware corporation, (Oclaro, we, us or our) as of October 2, 2010 and for the three months ended October 2, 2010 and September 26, 2 have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with the instructions to Article 10 of Securities and Exchange Commission (SEC) Regulation S-X, and include the accounts of Oclaro and all of our subsidiaries. Accordingly, they do not include all of the information and footnotes required by such accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of our consolidated financial position and results of operations have been included. The condensed consolidated results of operations for the three months ended October 2, 2010 are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year ending July 2, 2011.

The condensed consolidated balance sheet as of July 3, 2010 has been derived from our audited financial statements as of such date, but does not include all disclosures required by U.S. GAAP. These unaudited condensed consolidated financial statements should be read in conjunction with our audited financial statements included in our Annual Report on Form 10-K for the year ended July 3, 2010 (2010 Form 10-K).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenue and expenses during the reported periods. These judgments can be subjective and complex, and consequently, actual results could differ materially from those estimates and assumptions. Descriptions of some of the key estimates and assumptions are included in our 2010 Form 10-K.

Reclassifications

For presentation purposes, we have reclassified certain prior period amounts to conform to the current period financial statement presentation. With the exception of those discussed below, these reclassifications did not affect our consolidated net income, cash flows, cash and cash equivalents or stockholders equity, as previously reported.

During the second quarter of fiscal year 2010, we finalized the purchase accounting with respect to our acquisition of Newport Corporation s (Newport) high power laser diodes business. Our final assessment resulted in the gain on bargain purchase increasing from $0.7 million as originally reported to $5.3 million and the income from discontinued operations increasing from $1.3 million as originally reported to $1.4 million during the second quarter of fiscal year 2010.

Recent Accounting Pronouncements

There have been no recent accounting pronouncements or changes in accounting pronouncements during the three months ended October 2, 2010 that are of significance, or potential significance, to us.

Comprehensive Income

For the three months ended October 2, 2010 and September 26, 2009, comprehensive income is primarily comprised of our net income, changes in the unrealized gain (loss) on currency instruments designated as cash flow hedges, unrealized loss on short-term investments and currency translation adjustments.

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The components of comprehensive income were as follows for the periods indicated:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Net income	$ 356	$ 4,045
Other comprehensive income (loss):		
Unrealized gain (loss) on currency instruments designated as cash flow hedges	323	(23)
Currency translation adjustments	5,613	1,547
Unrealized loss on short-term investments		(7)
Comprehensive income	$ 6,292	$ 5,562

Note 2. Fair Value

We define fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining fair value measurements for assets and liabilities which are required to be recorded at fair value, we consider the principal or most advantageous market in which we would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions and credit risk. We apply the following fair value hierarchy, which ranks the quality and reliability of the information used to determine fair values:

Level 1 quoted prices in active markets for identical assets or liabilities;

Level 2 inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices of identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets), or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

Our cash equivalents and short-term investment instruments are generally classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. The types of instruments valued based on quoted market prices in active markets include most U.S. government and agency securities and money market securities. Such instruments are generally classified within Level 1 of the fair value hierarchy. The types of instruments valued based on other observable inputs include investment-grade corporate bonds, mortgage-backed and asset-backed securities and foreign currency forward exchange contracts. Such instruments are generally classified within Level 2 of the fair value hierarchy.

We have classified an escrow liability issued in connection with our acquisition of Xtellus Inc. (Xtellus) within Level 2 of the fair value hierarchy, as its value was derived by discounting the total liability of $7.0 million due 18 months after the acquisition to its present value using our incremental borrowing cost. During the first quarter of fiscal year 2011, we classified $15.3 million in earnout liabilities arising from our acquisition of Mintera Corporation (Mintera) within Level 3 of the fair value hierarchy because their values were primarily derived from management estimates of future operating results. See Note 3, *Business Combinations*, for additional details regarding these liabilities.

We have a defined benefit pension plan in Switzerland whose assets are classified within Level 1 of the fair value hierarchy for plan assets of cash, equity investments and fixed income investments, and Level 3 of the fair value

hierarchy for plan assets of real estate and alternative investments. These pension plan assets are not reflected in the accompanying condensed consolidated balance sheets, and are thus not included in the tables below.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Assets and liabilities measured at fair value are shown in the table below by their corresponding balance sheet caption and consisted of the following types of instruments at October 2, 2010:

	Fair Value Measurement at Reporting Date Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(Thousands)			
Assets:				
Cash and cash equivalents (1):				
Money market funds	$ 58,194	$	$	$ 58,194
Prepaid expenses and other current assets:				
Unrealized gain on currency instruments designated as cash flow hedges		372		372
Total assets measured at fair value	$ 58,194	$ 372	$	$ 58,566
Liabilities:				
Accrued expenses and other liabilities:				
Escrow liability for Xtellus acquisition (2)	$	$ 6,662	$	$ 6,662
Other non-current liabilities:				
Earnout liabilities for Mintera acquisition (2)			15,328	15,328
Total liabilities measured at fair value	$	$ 6,662	$ 15,328	$ 21,990

(1) Excludes $32.9 million in cash held in our bank accounts at October 2, 2010.

(2) Includes interest expense accrued during the three months ended October 2, 2010.

The following table provides details regarding the changes in assets and liabilities classified within Level 3 from July 3, 2010 to October 2, 2010:

	Fair Value Measured and Recorded Using Significant Unobservable Inputs (Level 3)

		Other Non-Current Liabilities (Thousands)
Balance at July 3, 2010	$	
Earnout liabilities from Mintera acquisition		15,148
Interest expense on Mintera earnout liabilities		180
Balance at October 2, 2010	$	15,328

Derivative Financial Instruments

At the end of each accounting period, we mark-to-market all foreign currency forward exchange contracts that have been designated as cash flow hedges and changes in fair value are recorded in accumulated other comprehensive

income until the underlying cash flow is settled and the contract is recognized in other income (expense) in our condensed consolidated statements of operations. As of October 2, 2010, we held eleven outstanding foreign currency forward exchange contracts to sell U.S. dollars and buy U.K. pounds sterling. All of these contracts have been designated as cash flow hedges. These contracts had an aggregate notional value of approximately $11.3 million of put and call options which expire, or expired, at various dates ranging from October 2010 through May 2011. To date, we have not entered into any such contracts for longer than 12 months and, accordingly, all amounts included in accumulated other comprehensive income as of October 2, 2010 will generally be reclassified into other income (expense) within the next 12 months. As of October 2, 2010, each of the eleven designated cash flow hedges was determined to be fully effective; therefore, we recorded an unrealized gain of $0.4 million to accumulated other comprehensive income related to recording the fair value of these foreign currency forward exchange contracts for accounting purposes.

Note 3. Business Combinations

During the three months ended October 2, 2010 and September 26, 2009, we recorded $0.1 million and $0.3 million, respectively, in legal and other direct merger-related costs in connection with business combinations. These costs are recorded within restructuring, merger and related costs in our condensed consolidated statement of operations.

As of June 27, 2009, we had capitalized $0.3 million in legal and other deal-related costs associated with the acquisition of the high-power laser diodes business from Newport. On June 28, 2009, we wrote-off these deferred assets to retained earnings as a cumulative effect of a change in accounting principle upon adoption of new accounting guidance.

Sale of the New Focus Business and Acquisition of Newport s High Power Laser Diodes Business

On July 4, 2009, we sold the net assets of our New Focus business to Newport in exchange for the net assets of Newport s high power laser diodes business and $3.0 million in cash proceeds. This transaction resulted in the recording of $1.4 million in income from discontinued operations from the sale of the New Focus business and a $5.3 million gain on bargain purchase of Newport s high power laser diodes business during the quarter ended September 26, 2009.

Acquisition of Xtellus

On December 17, 2009, we acquired Xtellus and accounted for the assets acquired and liabilities assumed from this acquisition using the purchase method of accounting. During the first quarter of fiscal year 2011, we completed our fair value assessment of the Xtellus acquisition, which resulted in no change to the estimated fair values of the assets acquired and liabilities assumed from the amounts we previously reported in our 2010 Form 10-K.

During the current quarter, we recorded $0.3 million in interest expense related to the Xtellus escrow liability and reclassified this liability from other non-current liabilities to accrued expenses and other liabilities. In addition, we also reassessed the fair value of the Xtellus valuation protection guarantee determining that its value should remain at nil as of October 2, 2010. Any subsequent change to the fair value of the value protection guarantee will result in an adjustment to our results of operations in the period of adjustment, up to a potential maximum of $7.0 million.

Further description of the Xtellus acquisition is included in Note 3, *Business Combinations*, of our 2010 Form 10-K.

Acquisition of Mintera

On July 21, 2010, we acquired Mintera, a privately-held company providing high-performance optical transport sub-systems solutions. We accounted for the assets acquired and liabilities assumed from our acquisition of Mintera using the purchase method of accounting. Under the terms of this agreement, we paid $10.5 million in cash to the former security holders and creditors of Mintera at the time of close and assumed $1.5 million in liabilities due by the security holders of Mintera, which we paid during the three months ended October 2, 2010. We also agreed to pay additional revenue-based consideration whereby former security holders of Mintera are entitled to receive up to $20.0 million, determined based on a set of sliding scale formulas, to the extent revenue from Mintera products is more than $29.0 million in the 12 months following the acquisition and/or more than $40.0 million in the 18 months

following the acquisition. The earnout consideration, if any, will be payable in cash or, at our option, newly issued shares of our common stock, or a combination of cash and stock. Achieving cumulative revenues of $40.0 million over the next 12 month period and $70.0 million over the next 18 month period would lead to the maximum $20.0 million in additional consideration. The estimated fair value of this obligation was determined using management estimates of the total amounts expected to be paid based on estimated future operating results, discounted to its present value using our incremental borrowing cost. The estimated fair value of this obligation is $15.1 million at the acquisition date, and has been recorded in other non-current liabilities in our condensed consolidated balance sheet at October 2, 2010. During the three months ended October 2, 2010, we recorded $0.2 million in interest expense related to this liability.

For accounting purposes, the total fair value of consideration given in connection with the acquisition of Mintera was $25.6 million, consisting of the following:

		Total Consideration
		(Thousands)
Consideration to security holders and creditors of Mintera	$	12,000
Less: Unpaid liabilities of Mintera security holders assumed by Oclaro		(1,518)
Net cash paid to security holders and creditors of Mintera		10,482
Estimated fair value for the 12-month earnout liability		4,338
Estimated fair value for the 18-month earnout liability		10,810
Total estimated fair value for the earnouts		15,148
Total consideration	$	25,630

Our preliminary allocation of the purchase price of Mintera, based on the estimated fair values of the assets acquired and liabilities assumed as of the acquisition date, is as follows:

		Preliminary Purchase Price
		(Thousands)
Restricted cash	$	41
Accounts receivable, net		3,053
Inventories		2,592
Prepaid expenses and other current assets		130
Property and equipment, net		3,202
Other intangible assets		11,740
Accounts payable		(1,947)
Accrued expenses and other current liabilities		(4,085)
Fair value of assets acquired and liabilities assumed		14,726
Goodwill		10,904
Total purchase price	$	25,630

We intend to finalize our purchase accounting with respect to the Mintera acquisition by the second quarter of fiscal year 2011. Any adjustments recorded will be retrospectively presented in our consolidated financial statements as

though they had been recorded as of the acquisition date.

Unaudited Pro Forma Financial Information

The following unaudited pro forma consolidated results of operations have been prepared as if the acquisition of Mintera had occurred as of June 28, 2009, the first day of our fiscal year 2010:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Revenues	$ 121,815	$ 91,972
Income (loss) from continuing operations	$ (2,002)	$ 1,178
Net income (loss)	$ (2,002)	$ 2,598
Net income (loss) per share basic	$ (0.04)	$ 0.07
Net income (loss) per share diluted	$ (0.04)	$ 0.07
Shares used in computing net income (loss) per share basic	48,115	37,240
Shares used in computing net income (loss) per share diluted	48,115	38,100

This unaudited pro forma financial information is presented for informational purposes only and is not necessarily indicative of the results of operations that actually would have been achieved had the acquisition been consummated as of that time, nor is it intended to be a projection of future results.

Note 4. Balance Sheet Details

The following table provides details regarding our cash and cash equivalents at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Cash and cash equivalents:		
Cash-in-bank	$ 32,923	$ 23,962
Money market funds	58,194	83,214
	$ 91,117	$ 107,176

The following table provides details regarding our inventories at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Inventories:		
Raw materials	$ 29,138	$ 17,732
Work-in-process	28,784	32,491
Finished goods	14,635	12,347
	$ 72,557	$ 62,570

The following table provides details regarding our property and equipment, net at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Property and equipment, net:		
Buildings	$ 16,615	$ 16,104
Plant and machinery	106,991	97,186
Fixtures, fittings and equipment	1,334	1,142
Computer equipment	12,889	12,232

	137,829	126,664
Less: Accumulated depreciation	(92,376)	(89,148)
	$ 45,453	$ 37,516

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The following table presents details regarding our accrued expenses and other liabilities at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Accrued expenses and other liabilities:		
Trade payables	$ 5,482	$ 4,464
Compensation and benefits related accruals	7,442	8,688
Warranty accrual	2,736	2,437
Restructuring accrual	2,187	4,338
Escrow liability for Xtellus acquisition (1)	6,662	
Other accruals	15,346	15,477
	$ 39,855	$ 35,404

(1) Includes interest expense accrued during the three months ended October 2, 2010. During the first quarter of fiscal year 2011, we reclassified this escrow liability from non-current liabilities to current liabilities.

The following table presents details regarding our other non-current liabilities at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Other non-current liabilities		
Escrow liability for Xtellus acquisition (1)	$	$ 6,324
Earnout liabilities for Mintera acquisition (2)	15,328	
Other non-current liabilities	3,664	3,461
	$ 18,992	$ 9,785

(1) During the first quarter of fiscal year 2011, we reclassified this escrow liability from non-current liabilities to current liabilities.

(2) Includes interest expense accrued during the three months ended October 2, 2010.

The following table presents the components of accumulated other comprehensive income at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Accumulated other comprehensive income:		
Unrealized gain on currency instruments designated as cash flow hedges	$ 372	$ 49
Currency translation adjustments	33,624	28,011
Swiss defined benefit plan	(1,153)	(1,153)
	$ 32,843	$ 26,907

Note 5. Goodwill and Other Intangible Assets

In connection with our acquisition of Mintera on July 21, 2010, we recorded $10.9 million in goodwill and $11.7 million in other intangible assets. The other intangible assets acquired from Mintera consist of core and current technology assets of $6.0 million with a weighted-average life of 6 years, a development agreement of $3.4 million with a weighted-average life of 7 years, customer relationships of $1.4 million with a weighted-average life of 8.5 years, manufacturing software of $0.7 million with a weighted-average life of 6 years, patents of $0.1 million with a weighted-average life of 5.5 years, trade names of $80,000 with a weighted-average life of 1.5 years and backlog of $30,000 with a weighted-average life of 1.5 years. These amounts are subject to change upon the finalization of our purchase accounting for the Mintera acquisition.

The following table provides details regarding the changes in our goodwill and other intangible assets from July 3, 2010 to October 2, 2010:

	Goodwill	Other Intangible Assets Cost	Accumulated Amortization	Net Book Value
		(Thousands)		
Balance at July 3, 2010	$ 20,000	$ 12,815	$ (2,205)	$ 10,610
Acquired	10,904	11,740		11,740
Amortization			(619)	(619)
Exchange rate adjustment		142		142
Balance at October 2, 2010	$ 30,904	$ 24,697	$ (2,824)	$ 21,873

The following table reflects the components of other intangible assets, net at the dates indicated:

	October 2, 2010	July 3, 2010
	(Thousands)	
Other intangible assets, net		
Supply agreements	$ 3,198	$ 3,056
Customer relationships	3,200	1,760
Core and current technology	10,939	4,909
Patent portfolio	2,910	2,780
Development agreement	3,350	
Manufacturing software	680	
Backlog	140	110
Tradename	280	200
	24,697	12,815
Less: Accumulated amortization	(2,824)	(2,205)
	$ 21,873	$ 10,610

Amortization of other intangible assets for the three months ended October 2, 2010 and September 26, 2009 was $0.6 million and $0.1 million, respectively. Amortization is recorded as an operating expense within our condensed consolidated statements of operations. Estimated future amortization expense of other intangible assets is $2.2 million for the remaining nine months of fiscal year 2011, $3.3 million for each of the fiscal years 2012 to 2015 and $3.0 million for fiscal year 2016. Estimated future amortization expense is subject to the finalization of our purchase accounting for the Mintera acquisition.

Note 6. Restructuring Liabilities

The following table summarizes activities related to our restructuring liabilities for the three months ended October 2, 2010:

	Accrued Restructuring Costs at July 3, 2010	Amounts Charged to Restructuring Costs	Amounts Paid or Written-off	Adjustments	Accrued Restructuring Costs at October 2, 2010
			(Thousands)		

Lease cancellations and commitments and other charges	$ 4,107	$		$	(2,279)	$	(100)	$	1,728
Termination payments to employees and related costs	231		646		(446)		28		459
Total accrued restructuring charges	$ 4,338	$	646	$	(2,725)	$	(72)	$	2,187

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In connection with earlier cost reduction and restructuring plans, we accrued $0.3 million in additional employee separation costs during the three months ended October 2, 2010. During the three months ended October 2, 2010, we initiated a new restructuring plan in connection with our acquisition of Mintera. We incurred $0.3 million in employee separation charges under the Mintera plan during the three months ended October 2, 2010 and do not expect to incur significant additional restructuring costs under this plan.

Note 7. Credit Facility

As of October 2, 2010, we had a $25.0 million senior secured revolving credit facility with Wells Fargo Capital Finance, Inc. and other lenders with an expiration date of August 1, 2012. As of October 2, 2010 and July 3, 2010, there were no amounts outstanding under the credit facility. At October 2, 2010, there was a $1.5 million outstanding standby letter of credit with a vendor secured under the credit facility. This letter of credit expires in November 2010.

Note 8. Post-Retirement Benefits

Switzerland Defined Benefit Plan (Swiss Plan)

Net periodic pension costs associated with our Swiss Plan for the three months ended October 2, 2010 included the following components:

	Three Months Ended October 2, 2010
	(Thousands)
Service cost	$ 419
Interest cost	176
Expected return on plan assets	(232)
Net periodic pension costs	$ 363

During the three months ended October 2, 2010, we contributed $0.4 million to our Swiss Plan. We currently anticipate contributing an additional $1.0 million to this pension plan in the remainder of fiscal year 2011.

Note 9. Commitments and Contingencies

Guarantees

We indemnify our directors and certain employees as permitted by law, and have entered into indemnification agreements with our directors and executive officers. We have not recorded a liability associated with these indemnification arrangements, as we historically have not incurred any material costs associated with such indemnification obligations. Costs associated with such indemnification obligations may be mitigated by insurance coverage that we maintain, however, such insurance may not cover any, or may cover only a portion of, the amounts we may be required to pay. In addition, we may not be able to maintain such insurance coverage in the future.

We also have indemnification clauses in various contracts that we enter into in the normal course of business, such as those issued by our bankers in favor of certain suppliers or indemnification in favor of customers in respect of liabilities they may incur as a result of purchasing our products should such products infringe the intellectual property rights of a third party. We have not historically paid out any material amounts related to these indemnifications, therefore, no accrual has been made for these indemnifications.

Warranty accrual

We accrue for the estimated costs to provide warranty services at the time revenue is recognized. Our estimate of costs to service our warranty obligations is based on historical experience and expectation of future conditions. To

the extent we experience increased warranty claim activity or increased costs associated with servicing those claims, our warranty costs would increase, resulting in a decrease in gross profit.
The following table summarizes movements in the warranty accrual for the periods indicated:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Warranty provision beginning of period	$ 2,437	$ 2,228
Warranties assumed in acquisitions	357	155
Warranties issued	432	772
Warranties utilized or expired	(564)	(843)
Currency translation adjustment	74	5
Warranty provision end of period	$ 2,736	$ 2,317

Litigation

On June 26, 2001, the first of a number of securities class actions was filed in the United States District Court for the Southern District of New York against New Focus, Inc., now known as Oclaro Photonics, Inc. (New Focus), certain of its officers and directors, and certain underwriters for New Focus initial and secondary public offerings. A consolidated amended class action complaint, captioned *In re New Focus, Inc. Initial Public Offering Securities Litigation*, No. 01 Civ. 5822, was filed on April 20, 2002. The complaint generally alleges that various underwriters engaged in improper and undisclosed activities related to the allocation of shares in New Focus initial public offering and seeks unspecified damages for claims under the Exchange Act on behalf of a purported class of purchasers of common stock from May 17, 2000 to December 6, 2000.

The lawsuit against New Focus is coordinated for pretrial proceedings with a number of other pending litigations challenging underwriter practices in over 300 cases, as *In re Initial Public Offering Securities Litigation*, 21 MC 92 (SAS), including actions against Bookham Technology plc, now known as Oclaro Technology Ltd (Bookham Technology) and Avanex Corporation, now known as Oclaro (North America), Inc. (Avanex), and certain of each entity s respective officers and directors, and certain of the underwriters of their public offerings. In October 2002, the claims against the directors and officers of New Focus, Bookham Technology and Avanex were dismissed, without prejudice, subject to the directors and officers execution of tolling agreements.

The parties have reached a global settlement of the litigation. On October 5, 2009, the Court entered an order certifying a settlement class and granting final approval of the settlement. Under the settlement, the insurers will pay the full amount of the settlement share allocated to New Focus, Bookham Technology and Avanex, and New Focus, Bookham Technology and Avanex will bear no financial liability. New Focus, Bookham Technology and Avanex, as well as the officer and director defendants who were previously dismissed from the action pursuant to tolling agreements, will receive complete dismissals from the case. Certain objectors have appealed the Court s October 5, 2009 order to the Second Circuit Court of Appeals. If for any reason the settlement does not become effective, we believe that Bookham Technology, New Focus and Avanex have meritorious defenses to the claims and therefore believe that such claims will not have a material effect on our financial position, results of operations or cash flows.

On February 13, 2009, Bijan Badihian filed a complaint against Avanex Corporation and certain of its employees in the Superior Court for the State of California, Los Angeles County. On August 6, 2010, the parties entered into a confidential settlement agreement. On September 10, 2010 the litigation was dismissed with prejudice. Consistent with the terms of the settlement agreement, the Defendants denied any wrongdoing.

On May 27, 2009, a patent infringement action captioned *QinetiQ Limited v. Oclaro, Inc.*, Civil Action No. 1:09-cv-00372 was filed in the United States District Court for the District of Delaware. QinetiQ s original complaint alleged infringement of United States Patent Nos. 5,410,625 and 5,428,698, and sought a permanent

injunction, money damages, costs, and attorneys fees. Oclaro filed an answer to the complaint and stated counterclaims against

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QinetiQ for judgments that the patents-in-suit are invalid and unenforceable. Additionally, we filed a motion to transfer venue to the Northern District of California, which was granted on December 18, 2009. After transfer, the litigation was assigned Civil Action No. 4:10-cv-00080-SBA by the Northern District Court. On June 21, 2010, QinetiQ amended its complaint to allege infringement of a third patent, U.S. Patent No. 5,379,354. We answered QinetiQ s amended complaint and asserted fraud counterclaims against QinetiQ. A trial in this matter has not yet been set. We believe the claims asserted against us by QinetiQ are without merit and will continue to defend ourselves vigorously.

Note 10. Employee Stock Plans

Our Amended and Restated 2004 Stock Incentive Plan (Plan) was amended by stockholder approval on October 27, 2010. The primary changes to the Plan resulting from this amendment include: (1) an increase in the number of shares available under the Plan from 3,800,000 shares to 7,800,000 shares, (2) issuance of full value awards being counted as 1.25 share of common stock for purposes of the share limit, and (3) a prohibition on recycling of repurchased shares in cases where shares are used to exercise an award or shares are withheld for taxes. As amended, the Plan now expires on October 26, 2020.

As of October 2, 2010, there were approximately 0.2 million shares of our common stock available for grant under the Plan. We generally grant stock options that vest over a four year service period, and restricted stock awards and units that vest over a one to four year service period, and in certain cases each may vest earlier based upon the achievement of specific performance-based objectives as set by our board of directors.

The following table summarizes the combined activity under all of our equity incentive plans for the three months ended October 2, 2010:

	Shares Available For Grant	Stock Options Outstanding	Weighted-Average Exercise Price	Restricted Stock Awards / Units Outstanding	Weighted-Average Grant Date Fair Value
	(Thousands)	(Thousands)		(Thousands)	
Balances at July 3, 2010	1,089	3,186	$ 8.78	703	$ 6.42
Granted	(867)	606	10.93	261	10.43
Exercised or released		(49)	4.10	(114)	3.18
Cancelled or forfeited	18	(55)	6.56	(30)	6.60
Balances at October 2, 2010	240	3,688	9.23	820	8.14

Supplemental disclosure information about our stock options outstanding as of October 2, 2010 is as follows:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life	Aggregate Intrinsic Value
	(Thousands)		(Years)	(Thousands)
Options exercisable at October 2, 2010	1,266	$ 13.93	6.7	$ 10,300
Options outstanding at October 2, 2010	3,688	9.23	7.9	32,194

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value, based on the closing price of our common stock of $15.82 on October 1, 2010, which would have been received by the option holders had all option holders exercised their options as of that date (our closing stock price was $9.97 on November 5, 2010). There were approximately 1.0 million shares of common stock subject to in-the-money options which were exercisable as of

October 2, 2010. We settle employee stock option exercises with newly issued shares of common stock.

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Note 11. Stock-based Compensation

We recognize compensation expense in our statement of operations related to all share-based awards, including grants of stock options, based on the grant date fair value of such share-based awards. Estimating the grant date fair value of such share-based awards requires us to make judgments in the determination of inputs into the Black-Scholes stock option pricing model which we use to arrive at an estimate of the grant date fair value for such awards. The assumptions used in this model to value stock option grants for the three months ended October 2, 2010 and September 26, 2009 were as follows:

	Three Months Ended	
	October 2, 2010	September 26, 2009
Expected life	4.5 years	4.5 years
Risk-free interest rate	1.3%	2.3%
Volatility	96.6%	101.3%
Dividend yield		

The amounts included in cost of revenues and operating expenses for stock-based compensation for the three months ended October 2, 2010 and September 26, 2009 were as follows:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Stock-based compensation by category of expense:		
Cost of revenues	$ 310	$ 195
Research and development	318	209
Selling, general and administrative	730	516
	$ 1,358	$ 920
Stock-based compensation by type of award:		
Stock options	$ 763	$ 790
Restricted stock awards	642	179
Inventory adjustment to cost of revenues	(47)	(49)
	$ 1,358	$ 920

As of October 2, 2010 and July 3, 2010, we had capitalized approximately $0.3 million and $0.2 million, respectively, of stock-based compensation as inventory.

Note 12. Income Taxes

The total amount of our unrecognized tax benefits as of October 2, 2010 and July 3, 2010 was approximately $8.4 million. For the three months ended October 2, 2010, we had $0.5 million in unrecognized tax benefits that, if recognized, would affect our effective tax rate. While it is often difficult to predict the final outcome of any particular uncertain tax position, management does not expect that changes to our unrecognized tax benefits will be significant in the next twelve months. We are currently under audit in France and Canada. We do not anticipate any significant adjustment to our financial position or results of operations as a result of these examinations.

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Note 13. Net Income Per Share

The following table presents the calculation of basic and diluted net income per share:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands,except per share amounts)	
Net income	$ 356	$ 4,045
Weighted-average shares basic	48,115	37,240
Effect of dilutive potential common shares from:		
Stock options	1,657	512
Restricted stock awards	770	348
Obligations under escrow agreement	442	
Weighted-average shares diluted	50,984	38,100
Basic net income per share	$ 0.01	$ 0.11
Diluted net income per share	$ 0.01	$ 0.11

Basic net income per share is computed using only the weighted-average number of shares of common stock outstanding for the applicable period, while diluted net income per share is computed assuming conversion of all potentially dilutive securities, such as stock options, unvested restricted stock awards, warrants and obligations under escrow agreements during such period.

For the three months ended October 2, 2010 and September 26, 2009, respectively, we excluded 1.8 million and 6.4 million of outstanding stock options and warrants from the calculation of diluted net income per share because their effect would have been anti-dilutive.

Note 14. Operating Segments and Related Information

We are organized and operate as two operating segments: (i) telecom and (ii) advanced photonics solutions. Our telecom segment is responsible for the design, development, chip and filter level manufacturing, marketing and selling of high performance core optical network components, module and subsystem products to telecommunications systems vendors. Our advanced photonics solutions segment is responsible for the design, manufacture, marketing and selling of optics and photonics solutions for markets including material processing, printing, medical and consumer applications.

Our Chief Executive Officer is our chief operating decision maker, and as such, evaluates the performance of these segments and makes resource allocation decisions based on segment revenues. We previously reported segment operating income (loss) for each of our segments. Beginning in fiscal year 2011, we are no longer presenting this information. Due to our integration of the activities of recent acquisitions into our existing operations and our recent efforts to streamline certain existing operations along geographic lines, the discrete financial information necessary to present segment operating income (loss) is no longer available.

Segment revenues for the three months ended October 2, 2010 and September 26, 2009 were as follows:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
Revenues:		

Telecom	$	107,822	$	74,266
Advanced photonics solutions		13,525		10,844
Consolidated revenues	$	121,347	$	85,110

The following table shows revenues by geographic area based on the delivery locations of our products:

	Three Months Ended	
	October 2, 2010	September 26, 2009
	(Thousands)	
United States	$ 19,664	$ 17,525
Canada	3,401	4,991
Europe	35,424	20,153
Asia	54,329	35,560
Rest of world	8,529	6,881
	$ 121,347	$ 85,110

Significant Customers and Concentration of Credit Risk

For the three months ended October 2, 2010, Huawei Technologies Co., Ltd. (Huawei) accounted for 15 percent and Alcatel-Lucent accounted for 13 percent of our revenues. For the three months ended September 26, 2009, Huawei accounted for 13 percent of our revenues.

As of October 2, 2010, Huawei accounted for 17 percent and Alcatel-Lucent accounted for 14 percent of our accounts receivable. As of July 3, 2010, Alcatel-Lucent accounted for 15 percent and Huawei accounted for 14 percent of our accounts receivable.

Note 15. Subsequent Events

Our Amended and Restated 2004 Stock Incentive Plan (Plan) was amended by stockholder approval on October 27, 2010. The primary changes to the Plan resulting from this amendment include: (1) an increase in the number of shares available under the Plan from 3,800,000 shares to 7,800,000 shares, (2) issuance of full value awards being counted as 1.25 share of common stock for purposes of the share limit, and (3) a prohibition on recycling of repurchased shares in cases where shares are used to exercise an award or shares are withheld for taxes. As amended, the Plan now expires on October 26, 2020.

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

This Quarterly Report on Form 10-Q contains forward-looking statements, within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, about our future expectations, plans or prospects and our business. These forward-looking statements include statements concerning (i) potential future financial results, (ii) the impact of mergers or acquisitions on our financial results, including without limitation, accretion or dilution, gross margin, operating income and cash usage, (iii) future expense levels and sources for improvement of gross margin and operating expenses, including supply chain synergies, optimizing mix of product offerings, transition to higher margin product offerings, benefits of combined research and development and sales organizations and single public company costs, (iv) the expected financial opportunities after mergers or acquisitions and the expected synergies related thereto, (v) opportunities to grow in adjacent markets, (vi) statements containing the words target, believe, plan, anticipate, expect, estimate, will, should, similar expressions and (vii) the assumptions underlying such statements. There are a number of important factors that could cause our actual results or events to differ materially from those indicated by such forward-looking statements, including the impact of continued uncertainty in world financial markets and any resulting or other reduction in demand for our products, the effect of fluctuating product mix, currency prices and consumer demand on our financial results, the future performance of Oclaro, Inc. following the closing of mergers or acquisitions, the potential inability to realize the expected benefits and synergies as a result of mergers or acquisitions, increased costs related to downsizing and compliance with regulatory requirements in connection with such downsizing, and the potential lack of availability of credit or opportunity for equity-based financing. You should not place undue reliance on forward-looking statements. We cannot guarantee any future results, levels of activity, performance or achievements. Moreover, we assume no obligation to update forward-looking statements or update the reasons actual results could differ materially from those anticipated in forward-looking statements. The factors discussed in the sections captioned Management s Discussion and Analysis of Financial Condition and Results of Operations and Risk Factors in this Quarterly Report on Form 10-Q also identify important factors that may cause our actual results to differ materially from the expectations we describe in our forward-looking statements.

Overview

We are a leading provider of high-performance core optical network components, modules and subsystems to global telecom equipment manufacturers. We leverage our proprietary core technologies and vertically integrated product development to provide our customers with cost-effective and innovative optical solutions in metro and long-haul network applications. In addition, we utilize our optical expertise to address new and emerging optical product opportunities in selective non-telecom markets, such as materials processing, consumer, medical, industrial, printing and biotechnology, which we refer to as our advanced photonics solutions segment. We offer our customers a differentiated solution that is designed to make it easier for our customers to do business by combining optical technology innovation, photonic integration, and a vertical approach to manufacturing and product development.

Results of Operations

The following tables set forth our condensed consolidated results of operations for the three month periods indicated, along with amounts expressed as a percentage of revenues, and comparative information regarding the absolute and percentage changes in these amounts:

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	Three Months Ended				Change	Increase (Decrease)
	October 2, 2010		September 26, 2009			
	(Thousands)	%	(Thousands)	%	(Thousands)	%
Revenues	$ 121,347	100.0	$ 85,110	100.0	$ 36,237	42.6
Cost of revenues	86,521	71.3	63,119	74.2	23,402	37.1
Gross profit	34,826	28.7	21,991	25.8	12,835	58.4
Operating expenses:						
Research and development	13,711	11.3	9,014	10.6	4,697	52.1
Selling, general and administrative	14,813	12.2	12,963	15.2	1,850	14.3
Amortization of intangible assets	619	0.5	125	0.1	494	395.2
Restructuring, merger and related costs	670	0.6	1,499	1.8	(829)	(55.3)
Gain on sale of property and equipment	(21)		(532)	(0.6)	511	(96.1)
Total operating expenses	29,792	24.6	23,069	27.1	6,723	29.1
Operating income (loss)	5,034	4.1	(1,078)	(1.3)	6,112	n/m(1)
Other income (expense):						
Interest income	7		23		(16)	(69.6)
Interest expense	(573)	(0.5)	(88)	(0.1)	(485)	551.1
Loss on foreign currency translation	(3,587)	(2.9)	(1,276)	(1.5)	(2,311)	181.1
Other income			5,267	6.2	(5,267)	n/m(1)
Total other income (expense)	(4,153)	(3.4)	3,926	4.6	(8,079)	n/m(1)
Income from continuing operations before income taxes	881	0.7	2,848	3.3	(1,967)	(69.1)
Income tax provision	525	0.4	223	0.2	302	135.4
Income from continuing operations	356	0.3	2,625	3.1	(2,269)	(86.4)
Income from discontinued operations, net of tax			1,420	1.7	(1,420)	n/m(1)
Net income	$ 356	0.3	$ 4,045	4.8	$ (3,689)	(91.2)

(1) Not meaningful.

Revenues

Revenues for the three months ended October 2, 2010 increased by $36.2 million, or 43 percent, compared to the three months ended September 26, 2009. Revenues by operating segments increased by $33.5 million in our telecom segment and $2.7 million in our advanced photonics segment during the three months ended October 2, 2010, compared to the three months ended September 26, 2009. The increases were primarily from improvements in market conditions, as compared to the calendar year 2009 economic downturn, in both of our operating segments, and, to some extent, a result of our ability to effectively integrate and realize synergies from our recent mergers and acquisitions, offset in part by certain deferrals and cancellations of orders we experienced towards the end of the current quarter.

For the three months ended October 2, 2010, Huawei Technologies Co., Ltd. (Huawei) accounted for $18.3 million, or 15 percent, of our revenues, and Alcatel-Lucent accounted for $16.0 million, or 13 percent, of our revenues. For the three months ended September 26, 2009, Huawei accounted for $11.1 million, or 13 percent, of our revenues.

Cost of Revenues

Our cost of revenues consists of the costs associated with manufacturing our products, and includes the purchase of raw materials, labor costs and related overhead, including stock-based compensation charges, and the costs charged by our contract manufacturers on the products they manufacture for us. Charges for excess and obsolete inventory, including inventories procured by contract manufacturers on our behalf, the cost of product returns and warranty costs are also included in cost of revenues. Costs and expenses related to our manufacturing resources incurred in connection with the development of new products are included in research and development expense.

Our cost of revenues for the three months ended October 2, 2010 increased by $23.4 million, or 37 percent, from the three months ended September 26, 2009. The increase was primarily related to costs associated with higher volumes of revenue resulting from improved market conditions subsequent to the economic downturn of calendar year 2009, offset in part by decreases from merger-related synergies and realizing the benefits of previous cost reduction efforts described more fully in Note 6, *Restructuring Liabilities*.

Gross Profit

Gross profit is calculated as revenues less cost of revenues. Gross margin rate is gross profit reflected as a percentage of revenues.

Our gross margin rate increased to 29 percent for the three months ended October 2, 2010, compared to 26 percent for the three months ended September 26, 2009. The increase in gross margin rate was primarily due to operating leverage from higher revenue volumes, synergies from the Avanex merger, including related cost reductions and the internal sourcing of Oclaro components into Avanex products, as well as the impact of other cost reduction efforts during the first quarter of fiscal year 2011 and earlier.

Research and Development Expenses

Research and development expenses consist primarily of salaries and related costs of employees engaged in research and design activities, including stock-based compensation charges related to those employees, costs of design tools and computer hardware, costs related to prototyping and facilities costs for certain research and development focused sites.

Research and development expenses increased to $13.7 million for the three months ended October 2, 2010 from $9.0 million for the three months ended September 26, 2009. The increase was primarily due to increased investment in research and development resources, primarily personnel-related, as we are investing to match the rate of our recent revenue growth. Personnel-related costs increased to $8.2 million for the three months ended October 2, 2010, compared with $5.8 million for the three months ended September 26, 2009. Other costs, including the costs of design tools and facilities-related costs increased to $5.5 million for the three months ended October 2, 2010, compared with $3.2 million for the three months ended September 26, 2009. Research and development expenses were favorably impacted by approximately $0.5 million as a result of the U.K. pound sterling weakening relative to the U.S. dollar.

Over the coming year, we intend to increase our research and development expenditures consistent with the rate of any actual revenue growth, with a bias towards investing in low cost regions where practical.

Selling, General and Administrative Expenses

Selling, general and administrative expenses consist primarily of personnel-related expenses, including stock-based compensation charges related to employees engaged in sales, general and administrative functions, legal and professional fees, facilities expenses, insurance expenses and certain information technology costs.

Selling, general and administrative expenses increased to $14.8 million for the three months ended October 2, 2010, from $13.0 million for the three months ended September 26, 2009. The increase was primarily due to the increase in costs incurred in connection with recent mergers and acquisitions, offset in part by merger-related synergies. Personnel-related costs increased to $7.8 million for the three months ended October 2, 2010, compared with $6.7

million for the three months ended September 26, 2009. Other costs, including legal and professional fees, facilities expenses and other miscellaneous expenses, increased to $7.0 million for the three months ended October 2, 2010, compared with $6.3 million for the three months ended September 26, 2009. Selling, general and administrative expenses were favorably impacted by approximately $0.5 million as a result of the U.K. pound sterling weakening relative to the U.S. dollar.

Restructuring, Merger and Related Costs

In connection with earlier cost reduction and restructuring plans, we accrued $0.3 million in additional employee separation costs, net of adjustments, during the three months ended October 2, 2010. During this period, we initiated a new restructuring plan resulting from our acquisition of Mintera Corporation (Mintera). We incurred $0.3 million in employee separation charges under the Mintera plan during the three months ended October 2, 2010 and do not expect to incur significant additional restructuring costs in connection with this plan. During the three months ended October 2, 2010, we also recorded $0.1 million in merger-related professional fees.

During the three months ended September 26, 2009, in connection with earlier cost reduction and restructuring plans, we accrued $0.2 million in additional expenses, net of adjustments, for revised estimates related to lease cancellations and commitments and $1.0 million in additional employee separation costs. During this period we also recorded $0.3 million in merger-related professional fees.

Gain on Sale of Property and Equipment

For the three months ended September 26, 2009, we recorded a net gain of $0.5 million, primarily related to the sale of certain fixed assets in Villebon, France made surplus in connection with the closing of that facility.

Other Income (Expense)

Other income (expense) for the three months ended October 2, 2010 decreased by $8.1 million compared to the three months ended September 26, 2009. This decrease was primarily due to $5.3 million in gain from the bargain purchase of Newport s high power laser diodes business being recorded during the three months ended September 26, 2009. There was also a $2.3 million increase in loss from the re-measurement of short term receivables and payables among certain of our wholly-owned international subsidiaries for fluctuations in the U.S. dollar relative to our other local functional currencies during the corresponding periods. This decrease was also due to a $0.5 million increase in interest expense related to liabilities recognized in the acquisitions of Xtellus, Inc. (Xtellus) and Mintera.

Income Tax Provision (Benefit)

For the three months ended October 2, 2010, our income tax provision of $0.5 million primarily related to our foreign operations. For the three months ended September 26, 2009, our income tax provision of $0.2 million primarily related to income taxes on our operations in the United States, Italy and China.

In the fourth quarter of fiscal year 2010, we determined that it is more-likely-than-not that we will utilize net operating losses in one of our foreign jurisdictions due to current earnings and projections of future profitability. Accordingly, we released $1.3 million of our valuation allowance against $1.3 million of previously unrecognized deferred tax assets during the fourth quarter of fiscal year 2010. This amount represented the entire remaining deferred tax asset related to the accumulated net operating losses of the foreign jurisdiction. Due to the uncertainty surrounding the realization of the tax attributes in other jurisdictions, we have recorded a full valuation allowance against our remaining foreign and domestic deferred tax assets as of October 2, 2010.

Income from Discontinued Operations

During the three months ended September 26, 2009, we recorded income of $1.4 million from discontinued operations from the sale of our New Focus business. For further details, refer to Note 3, *Business Combinations*.

Recent Accounting Pronouncements

See Note 1, *Basis of Preparation*, to our condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q for information regarding the effect of new accounting pronouncements on our financial statements.

Application of Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements contained elsewhere in this Quarterly Report on Form 10-Q, which have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The preparation of our financial statements requires us to make estimates and judgments that affect our reported assets and liabilities, revenues and expenses and other financial information. Actual results may differ significantly from those based on our estimates and judgments or could be materially different if we used different assumptions, estimates or conditions. In addition, our financial condition and results of operations could vary due to a change in the application of a particular accounting standard.

We identified our critical accounting policies in our Annual Report on Form 10-K for the year ended July 3, 2010 (2010 Form 10-K) related to revenue recognition and sales returns, inventory valuation, business combinations, impairment of goodwill and other intangible assets, accounting for share-based payments and income taxes. It is important that the discussion of our operating results be read in conjunction with the critical accounting policies discussed in our 2010 Form 10-K.

Liquidity and Capital Resources

Cash Flows from Operating Activities

Net cash used by operating activities for the three months ended October 2, 2010 was $1.0 million, primarily resulting from a $6.3 million decrease in cash due to changes in operating assets and liabilities, partially offset by net income of $0.4 million and non-cash adjustments of $4.9 million. The $6.3 million decrease in cash due to changes in operating assets and liabilities was comprised of a $6.9 million decrease in accrued expenses and other liabilities, a $4.9 million increase in inventory, a $0.6 million increase in accounts receivable and a $0.3 million increase in prepaid expense and other current assets, offset in part by cash generated from a $6.3 million increase in accounts payable and a $0.1 million decrease in other non-current assets. The $4.9 million increase in cash resulting from non-cash adjustments primarily consisted of $3.8 million of expense related to depreciation and amortization and $1.4 million of expense related to stock-based compensation, offset in part by $0.2 million from the amortization of deferred gain from a sales-leaseback transaction.

Net cash used in operating activities for the three months ended September 26, 2009 was $9.1 million, resulting from an increase in our net operating assets and liabilities of $9.4 million and non-cash adjustments of $3.7 million, partially offset by net income of $4.0 million. The $9.4 million decrease in cash due to an increase in net operating assets and liabilities was comprised of a $9.6 million increase in accounts receivable, a $4.1 million decrease in accrued expenses and other liabilities and a $0.5 million increase in prepaid expenses and other current assets, offset by cash generated from a $2.6 million decrease in inventory, a $1.4 million increase in accounts payable and a $0.8 million decrease in other non-current assets. The $3.7 million decrease in cash resulting from non-cash adjustments consisted of $5.3 million in gain from the bargain purchase of Newport s high-power laser diodes business, $1.4 million in gain from the sale of the New Focus business, $0.5 million in gain from the sale of property and equipment and $0.2 million from the amortization of deferred gain from a sales-leaseback transaction, offset in part by $2.8 million of expense related to depreciation and amortization and $0.9 million of expense related to stock-based compensation.

Cash Flows from Investing Activities

Net cash used in investing activities for the three months ended October 2, 2010 was $15.6 million, primarily consisting of $10.5 million used in the acquisition of Mintera and $6.9 million used in capital expenditures, which

were partially offset by a reduction of $1.7 million in restricted cash related to a facility lease from which we exited during the current quarter.

Net cash provided by investing activities for the three months ended September 26, 2009 was $11.0 million, primarily consisting of $8.2 million in sales and maturities of available-for-sale investments, $3.0 million in cash proceeds from the exchange of assets with Newport and $0.6 million in proceeds from the sale of certain fixed assets, which were partially offset by $0.7 million used in capital expenditures.

Cash Flows from Financing Activities

Net cash provided by financing activities of $0.5 million for the three months ended October 2, 2010 primarily resulted from $0.3 million in additional proceeds related to our May 2010 follow-on stock offering due to finalization of our previous estimates of offering related expenses and $0.2 million received from issuance of common stock, primarily through stock option exercises. There were no other significant cash flows from financing activities for the three months ended October 2, 2010 or the three months ended September 26, 2009.

Effect of Exchange Rates on Cash and Cash Equivalents for the Three Months Ended October 2, 2010 and September 26, 2009

The effect of exchange rates on cash and cash equivalents for the three months ended October 2, 2010 was an increase of $0.1 million, primarily consisting of $0.9 million in net gain due to the revaluation of foreign currency cash balances to the functional currency of the respective subsidiaries and from a loss of approximately $1.1 million related to the revaluation of U.S. dollar denominated operating intercompany payables on the books of our subsidiaries.

The effect of exchange rates on cash and cash equivalents for the three months ended September 26, 2009 was an increase of $0.8 million, primarily consisting of $0.4 million in net loss due to the revaluation of foreign currency denominated cash balances to the functional currency of the respective subsidiaries, and a loss of approximately $0.8 million related to the revaluation of foreign currency denominated operating intercompany receivables on the books of our U.S., China and Italy subsidiaries, offset by a gain of approximately $0.3 million related to the revaluation of U.S. dollar denominated operating intercompany receivables on the books of our U.K. subsidiary.

Credit Facility

As of October 2, 2010, we had a $25.0 million senior secured revolving credit facility with Wells Fargo Capital Finance, Inc. and other lenders with an expiration date of August 1, 2012. As of October 2, 2010 and July 3, 2010, there were no amounts outstanding under the credit facility. At October 2, 2010, there was $1.5 million in outstanding standby letter of credit with a vendor secured under the credit facility. This standby letter of credit expires in November 2010.

Future Cash Requirements

As of October 2, 2010, we held $91.1 million in cash and cash equivalents and $2.8 million in restricted cash. In the future, in order to strengthen our financial position, in the event of unforeseen circumstances, or in the event we need to fund our growth in future financial periods, we may need to raise additional funds by any one or a combination of the following: issuing equity securities, debt or convertible debt or the sale of certain product lines and/or portions of our business. There can be no guarantee that we will be able to raise additional funds on terms acceptable to us, or at all.

From time to time, we have engaged in discussions with third parties concerning potential acquisitions of product lines, technologies and businesses, and we continue to consider potential acquisition candidates. Any such transactions could involve the issuance of a significant number of new equity securities, debt, and/or cash consideration. We may also be required to raise additional funds to complete any such acquisition, through either the issuance of equity securities or borrowings. If we raise additional funds or acquire businesses or technologies through the issuance of equity securities, our existing stockholders may experience significant dilution.

Off-Balance Sheet Arrangements

We indemnify our directors and certain employees as permitted by law, and have entered into indemnification agreements with our directors and executive officers. We have not recorded a liability associated with these indemnification arrangements, as we historically have not incurred any material costs associated with such indemnification obligations. Costs associated with such indemnification obligations may be mitigated by insurance coverage that we maintain, however, such insurance may not cover any, or may cover only a portion of, the amounts we may be required to pay. In addition, we may not be able to maintain such insurance coverage in the future.

We also have indemnification clauses in various contracts that we enter into in the normal course of business, such as those issued by our bankers in favor of certain suppliers or indemnification in favor of customers in respect of liabilities they may incur as a result of purchasing our products should such products infringe the intellectual property rights of a third party. We have not historically paid out any material amounts related to these indemnifications; therefore, no accrual has been made for these indemnifications.

Other than as set forth above, we are not currently party to any material off-balance sheet arrangements.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rates

We finance our operations through a mixture of the issuance of equity securities, finance leases, working capital and by drawing on our Amended Credit Agreement. Our only exposure to interest rate fluctuations is on our cash deposits. We monitor our interest rate risk on cash balances primarily through cash flow forecasting. Cash that is surplus to immediate requirements is generally invested in short-term deposits with banks accessible within one day s notice and invested in overnight money market accounts. We believe our interest rate risk is immaterial.

Foreign currency

As our business is multinational in scope, we are subject to fluctuations based upon changes in the exchange rates between the currencies in which we collect revenues and pay expenses. In the future we expect that a majority of our revenues will be denominated in U.S. dollars, while a significant portion of our expenses related to our operations in the United Kingdom will be denominated in U.K. pounds sterling. Fluctuations in the exchange rate between the U.S. dollar and the U.K. pound sterling and, to a lesser extent, other currencies in which we collect revenues and pay expenses, could affect our operating results. This includes the Chinese yuan, the Korean won, the Israeli shekel, the Swiss franc and the Euro in which we pay expenses in connection with operating our facilities in Shenzhen and Shanghai, China; Daejeon, South Korea; Jerusalem, Israel; Zurich, Switzerland and San Donato, Italy. To the extent the exchange rate between the U.S. dollar and these currencies were to fluctuate more significantly than experienced to date, our exposure would increase.

As of October 2, 2010, our U.K. subsidiary had $34.5 million, net, in U.S. dollar denominated operating intercompany payables and $72.1 million in U.S. dollar denominated accounts receivable related to sales to external customers. It is estimated that a 10 percent fluctuation in the U.S. dollar relative to the U.K. pound sterling would lead to a profit of $3.8 million (U.S. dollar strengthening), or loss of $3.8 million (U.S. dollar weakening) on the translation of these receivables, which would be recorded as gain (loss) on foreign exchange in our condensed consolidated statement of operations.

Hedging Program

We enter into foreign currency forward exchange contracts in an effort to mitigate a portion of our exposure to such fluctuations between the U.S. dollar and the U.K. pound sterling. We do not currently hedge our exposure to the Chinese yuan, the Korean won, the Israeli shekel, the Swiss franc or the Euro, but we may in the future if conditions warrant. We also do not currently hedge our exposure related to our U.S. dollar denominated intercompany payables and receivables. We may be required to convert currencies to meet our obligations. Under certain circumstances, foreign currency forward exchange contracts can have an adverse effect on our financial condition. As of October 2, 2010, we held eleven outstanding foreign currency forward exchange contracts with a notional value of

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$11.3 million which include put and call options which expire, or expired, at various dates from October 2010 to May 2011 and we have recorded an unrealized gain of $0.4 million to accumulated other comprehensive income in connection with marking these contracts to fair value as of October 2, 2010. It is estimated that a 10 percent fluctuation in the dollar between October 2, 2010 and the maturity dates of the put and call instruments underlying these contracts would lead to a profit of $1.0 million dollars (U.S. dollar weakening) or loss of $0.2 million dollars (U.S. dollar strengthening) on our outstanding foreign currency forward exchange contracts, should they be held to maturity.

Item 4. ***Controls and Procedures***

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of October 2, 2010. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, or the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of October 2, 2010, our Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

There was no change in our internal control over financial reporting during the three months ended October 2, 2010 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. ***Legal Proceedings***

On June 26, 2001, the first of a number of securities class actions was filed in the United States District Court for the Southern District of New York against New Focus, Inc., now known as Oclaro Photonics, Inc. (New Focus), certain of its officers and directors, and certain underwriters for New Focus initial and secondary public offerings. A consolidated amended class action complaint, captioned *In re New Focus, Inc. Initial Public Offering Securities Litigation*, No. 01 Civ. 5822, was filed on April 20, 2002. The complaint generally alleges that various underwriters engaged in improper and undisclosed activities related to the allocation of shares in New Focus initial public offering and seeks unspecified damages for claims under the Exchange Act on behalf of a purported class of purchasers of common stock from May 17, 2000 to December 6, 2000.

The lawsuit against New Focus is coordinated for pretrial proceedings with a number of other pending litigations challenging underwriter practices in over 300 cases, as *In re Initial Public Offering Securities Litigation*, 21 MC 92 (SAS), including actions against Bookham Technology plc, now known as Oclaro Technology Ltd (Bookham Technology) and Avanex Corporation, now known as Oclaro (North America), Inc. (Avanex), and certain of each entity s respective officers and directors, and certain of the underwriters of their public offerings. In October 2002, the claims against the directors and officers of New Focus, Bookham Technology and Avanex were dismissed, without prejudice, subject to the directors and officers execution of tolling agreements.

The parties have reached a global settlement of the litigation. On October 5, 2009, the Court entered an order certifying a settlement class and granting final approval of the settlement. Under the settlement, the insurers will pay the full amount of the settlement share allocated to New Focus, Bookham Technology and Avanex, and New Focus, Bookham Technology and Avanex will bear no financial liability. New Focus, Bookham Technology and Avanex, as well as the officer and director defendants who were previously dismissed from the action pursuant to tolling

agreements, will receive complete dismissals from the case. Certain objectors have appealed the Court s October 5, 2009 order to the Second Circuit Court of Appeals. If for any reason the settlement does not become effective, we believe that Bookham Technology, New Focus and Avanex have meritorious defenses to the claims and therefore believe that such claims will not have a material effect on our financial position, results of operations or cash flows.

On February 13, 2009, Bijan Badihian filed a complaint against Avanex Corporation and certain of its employees in the Superior Court for the State of California, Los Angeles County. On August 6, 2010, the parties entered into a confidential settlement agreement. On September 10, 2010 the litigation was dismissed with prejudice. Consistent with the terms of the settlement agreement, the Defendants denied any wrongdoing.

On May 27, 2009, a patent infringement action captioned *QinetiQ Limited v. Oclaro, Inc.*, Civil Action No. 1:09-cv-00372, was filed in the United States District Court for the District of Delaware. QinetiQ s original complaint alleged infringement of United States Patent Nos. 5,410,625 and 5,428,698, and sought a permanent injunction, money damages, costs, and attorneys fees. We filed an answer to the complaint and stated counterclaims against QinetiQ for judgments that the patents-in-suit are invalid and unenforceable. Additionally, we filed a motion to transfer venue to the Northern District of California, which was granted on December 18, 2009. After transfer, the litigation was assigned Civil Action No. 4:10-cv-00080-SBA by the Northern District Court. On June 21, 2010, QinetiQ amended its complaint to allege infringement of a third patent, U.S. Patent No. 5,379,354. We answered QinetiQ s amended complaint and asserted fraud counterclaims against QinetiQ. A trial in this matter has not yet been set. We believe the claims asserted against us by QinetiQ are without merit and will continue to defend ourselves vigorously.

Item 1A. ***Risk Factors***

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below in addition to the other information included or incorporated by reference in this Quarterly Report on Form 10-Q. If any of the following risks actually occur, our business, financial condition or results of operations would likely suffer. In that case, the trading price of our common stock could fall and you could lose all or part of your investment.

Risks Related to Our Business

Prior to the year ended July 3, 2010, we had a history of large operating losses and we may not be able to sustain profitability in the future.

We have historically incurred losses and negative cash flows from operations since our inception. As of October 2, 2010, we had an accumulated deficit of $1,079.3 million. Although we generated income from continuing operations for the quarter ended October 2, 2010 and the year ended July 3, 2010 of $0.4 million and $11.0 million, respectively, we incurred losses from continuing operations for the years ended June 27, 2009 and June 28, 2008 of $25.8 million and $23.3 million, respectively. We may not be able to achieve profitability in any future periods. If we are unable to do so, we may need additional financing, which may not be available to us on commercially acceptable terms or at all, to execute on our current or future business strategies.

We may not be able to maintain gross margin levels.

We may not be able to maintain or improve our gross margins, to the extent that current economic uncertainty, changes in customer demand, including a change in product mix between different areas of our business, or other factors, affects our overall revenue, and we are unable to adjust our expenses as necessary. We attempt to reduce our product costs and improve our product mix to offset price competition and erosion expected in most product categories, but there is no assurance that we will be successful. Our gross margins can also be adversely impacted for reasons including, but not limited to, unfavorable production variances, increases in costs of input parts and materials, the timing of movements in our inventory balances, warranty costs and related returns, and possible exposure to inventory valuation reserves. Any failure to maintain, or improve, our gross margins will adversely affect our financial results, including our goal to achieve sustainable cash flow positive operations.

Our business and results of operations may be negatively impacted by general economic and financial market conditions and such conditions may increase the other risks that affect our business.

Over the past two years, the world s financial markets have experienced significant turmoil, resulting in reductions in available credit, increased costs of credit, extreme volatility in security prices, potential changes to existing credit terms, rating downgrades of investments and reduced valuations of securities generally. In light of these economic conditions, many of our customers reduced their spending plans, leading them to draw down their existing inventory and reduce orders for optical components. While we have seen a short-term improvement in customer demand, and improvements in the economic conditions contributing to that improved customer demand, it is possible that economic conditions could result in further setbacks, and that these customers, or others, could as a result significantly reduce their capital expenditures, draw down their inventories, reduce production levels of existing products, defer introduction of new products or place orders and accept delivery for products for which they do not pay us due to their economic difficulties or other reasons. Prior to the recent improvement in customer demand, these actions had, and in future quarters could have, an adverse impact on our own revenues. In addition, the financial downturn affected the financial strength of certain of our customers, and could adversely affect others. Our suppliers may also be adversely affected by economic conditions that may impact their ability to provide important components used in our manufacturing processes on a timely basis, or at all. In our most recent three months ended October 2, 2010, we experienced order cancellations and delays which, given the recent economic history discussed above, we cannot be certain are short term in nature.

These conditions could also result in reduced capital resources because of the potential lack of credit availability, higher costs of credit and the stretching of payables by creditors seeking to preserve their own cash resources. We are unable to predict the likely duration, severity and potential continuation of the recent disruption in financial markets and adverse economic conditions in the U.S. and other countries, but the longer the duration the greater the risks we face in operating our business.

Our success will depend on our ability to anticipate and respond to evolving technologies and customer requirements.

The market for telecommunications equipment is characterized by substantial capital investment and diverse and evolving technologies. For example, the market for optical components is currently characterized by a trend toward the adoption of pluggable components and tunable transmitters that do not require the customized interconnections of traditional fixed wavelength gold box devices and the increased integration of components on subsystems. Our ability to anticipate and respond to these and other changes in technology, industry standards, customer requirements and product offerings and to develop and introduce new and enhanced products will be significant factors in our ability to succeed. We expect that new technologies will continue to emerge as competition in the telecommunications industry increases and the need for higher and more cost efficient bandwidth expands. The introduction of new products embodying new technologies or the emergence of new industry standards could render our existing products or products in development uncompetitive from a pricing standpoint, obsolete or unmarketable.

We depend on a limited number of customers for a significant percentage of our revenues.

Historically, we have generated most of our revenues from a limited number of customers. Our dependence on a limited number of customers is due to the fact that the optical telecommunications systems industry is dominated by a small number of large companies. These companies in turn depend primarily on a limited number of major telecommunications carrier customers to purchase their products that incorporate our optical components. For example, in the years ended July 3, 2010, June 27, 2009 and June 28, 2008, our three largest customers accounted for 29 percent, 38 percent and 38 percent of our revenues, respectively. Revenues from any of our major customers may fluctuate significantly in the future, which could have an adverse impact on our business and results of operations.

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The majority of our long-term customer contracts do not commit customers to specified buying levels, and our customers may decrease, cancel or delay their buying levels at any time with little or no advance notice to us.

The majority of our customers typically purchase our products pursuant to individual purchase orders or contracts that do not contain purchase commitments. Some customers provide us with their expected forecasts for our products several months in advance, but many of these customers may decrease, cancel or delay purchase orders already in place, and the impact of any such actions may be intensified given our dependence on a small number of large customers. If any of our major customers decrease, stop or delay purchasing our products for any reason, our business and results of operations would be harmed. Cancellation or delays of such orders may cause us to fail to achieve our short-term and long-term financial and operating goals and result in excess and obsolete inventory. For example, in mid-September 2010, we did experience certain deferrals and cancellation of orders which adversely impacted our financial results.

We may undertake mergers or acquisitions that do not prove successful.

From time to time we consider mergers or acquisitions, collectively referred to as acquisitions, of other businesses, assets or companies. We may not be able to identify suitable acquisition candidates at prices we consider appropriate. If we do identify an appropriate acquisition candidate, we may not be able to successfully and satisfactorily negotiate the terms of the acquisition. Our management may not be able to effectively implement our acquisition plans and internal growth strategy simultaneously. We are also in an industry that is actively consolidating and there is no guarantee that we will successfully bid against third parties, including competitors, when we identify a critical target we want to acquire.

The integration of acquisitions involves a number of risks and presents financial, managerial and operational challenges. We may have difficulty, and may incur unanticipated expenses related to, integrating management and personnel from these acquired entities with our management and personnel. Our failure to identify, consummate or integrate suitable acquisitions could adversely affect our business and results of operations. We cannot readily predict the timing, size or success of our future acquisitions. Failure to successfully implement our acquisition plans could have a material adverse effect on our business, prospects, financial condition and results of operations. Even successful acquisitions could have the effect of reducing our cash balances, diluting the ownership interests of existing stockholders or increasing our indebtedness. For example, our recent acquisition of Xtellus required an immediate issuance of a significant number of newly issued shares of our common stock and we may choose to issue a significant number of additional newly issued shares of our common stock in connection with the value protection guarantee provided to Xtellus shareholders in the acquisition. We could also choose to use shares of our common stock to settle the Mintera earnouts, should all, or portions, of these earnouts be achieved in the twelve and/or eighteen month periods subsequent to the acquisition date. We cannot predict with certainty which strategic, financial or operating synergies or other benefits, if any, will actually be achieved from any transaction we undertake, the timing of any such benefits, or whether those benefits which have been achieved will be sustainable on a long-term basis.

Acquisitions could involve a number of other potential risks to our business, including the following, any of which could harm our business:

- failure to realize the potential financial or strategic benefits of the acquisition;
- declines in the revenue of the combined company;
- economic dilution to gross and operating profit and earnings (loss) per share;
- failure to successfully further develop the combined, acquired or remaining technology, resulting in the impairment of amounts recorded as goodwill or other intangible assets;
- unanticipated costs and liabilities and unforeseen accounting charges;
- difficulty in integrating product offerings;

- difficulty in coordinating and rationalizing research and development activities to enhance introduction of new products and technologies with reduced cost;
- difficulty in coordinating and integrating the manufacturing activities of our acquired businesses, including with respect to third-party manufacturers, including executing a production capacity ramp up of our South Korea facility and our contract manufacturers to support the potential revenue demand for the WSS-related products of Xtellus, including managing the manufacturing activities of the laser diode business acquired from Newport while these activities are being transferred from Tucson, Arizona to Europe and Asia, and including transferring certain production of Mintera products to our internal facilities;
- delays and difficulties in delivery of products and services;
- failure to effectively integrate or separate management information systems, personnel, research and development, marketing, sales and support operations;
- difficulty in maintaining controls and procedures;
- difficulty in preserving important relationships of our acquired businesses and resolving potential conflicts between business cultures;
- uncertainty on the part of our existing customers, or the customers of an acquired company, about our ability to operate effectively after a transaction, and the potential loss of such customers;
- loss of key employees;
- difficulty in coordinating the international activities of our acquired businesses;
- the effect of tax laws due to increasing complexities of our global operating structure;
- the effect of employment law or regulations or other limitations in foreign jurisdictions that could have an impact on timing, amounts or costs of achieving expected synergies; and
- substantial demands on our management as a result of these transactions that may limit their time to attend to other operational, financial, business and strategic issues.

Our integration with merged and acquired businesses has been and will continue to be a complex, time-consuming and expensive process. We cannot assure you that we will be able to successfully integrate these businesses in a timely manner, or at all, or that any of the anticipated benefits from our acquisition of these businesses will be realized. Our failure to achieve the strategic objectives of our mergers and acquisitions could have a material adverse effect on our revenues, expenses and our other operating results and cash resources and could result in us not achieving the anticipated potential benefits of these transactions. In addition, we cannot assure you that the growth rate of the combined company will equal the historical growth rate experienced by any of the companies that we have acquired or merged with. Comparable risks would accompany any divestiture of business or assets we might undertake.

Sales of our products could decline if customer and/or supplier relationships are disrupted by our recent merger and acquisition activities.

The customers of acquired or merged businesses, and/or of predecessor companies, may not continue their historical buying patterns. Customers may defer purchasing decisions as they evaluate the likelihood of successful integration of our products and our future product strategy, or consider purchasing products of our competitors.

Customers may also seek to modify or terminate existing agreements, or prospective customers may delay entering into new agreements or purchasing our products or may decide not to purchase any products from us. In addition, by

increasing the breadth of our business, the transactions may make it more difficult for us to enter into relationships, including customer relationships, with strategic partners, some of whom may view us as a more direct competitor than any of the predecessor and/or acquired and merged businesses as independent companies.

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Competitive positions in the market, including relative to suppliers who are also competitors, could change as a result of an acquisition or merger of a new business into Oclaro, and this could impact supplier relationships, including the terms under which we do business with such suppliers.

As a result of our recent business combinations, we have become a larger and more geographically diverse organization, and if our management is unable to manage the combined organization efficiently, our operating results will suffer.

As of October 2, 2010, we had approximately 2,926 employees in a total of 15 facilities around the world. As a result, we face challenges inherent in efficiently managing an increased number of employees over large geographic distances, including the need to implement appropriate systems, policies, benefits and compliance programs. Our inability to manage successfully the geographically more diverse (including from a cultural perspective) and substantially larger combined organization could have a material adverse effect on our operating results and, as a result, on the market price of our common stock.

We may not successfully transfer the wafer production from the Tucson, Arizona manufacturing operations we acquired from Newport to our European fabrication facilities and realize the anticipated benefits of the acquisition.

Achieving the potential benefits of our July 4, 2009 acquisition from Newport of the laser diodes manufacturing operations in Tucson, Arizona will depend in substantial part on the successful transfer of those manufacturing operations to our European fabrication facilities. We face significant challenges in transferring these operations in a timely and efficient manner. As a result of certain of these challenges, our opportunities to increase revenues in the corresponding business were limited in the quarter ended October 2, 2010, and we expect these limitations to continue into the second quarter of fiscal year 2011. Some of the challenges involved in this transfer include:

transferring operations is placing substantial demands on our management that may limit their time to attend to other operational, financial and strategic issues;

it may take longer than anticipated to complete the transfer of wafer manufacturing operations from Tucson, Arizona to our European fabs, the results may not deliver desired yields and costs savings, any delay may cause us not to achieve expected synergies from leveraging our existing global manufacturing infrastructure, and our ability to grow related revenues could be limited by the levels of inventory built to sustain customer demand during the period of transfer;

the costs of transferring manufacturing operations from Tucson, Arizona to our European fabs may exceed our current estimates;

delays in qualifying production of the laser diodes in our European fabs could cause disruption to our customers and have an adverse impact on our operating results; and

we may experience difficulty in the integration of operational, financial and administrative functions and systems to permit effective management, and may experience a lack of control if such integration is not implemented or delayed.

Our products are complex and may take longer to develop than anticipated and we may not recognize revenues from new products until after long field testing and customer acceptance periods.

Many of our new products must be tailored to customer specifications. As a result, we are developing new products and using new technologies in those products. For example, while we currently manufacture and sell discrete gold box technology, we expect that many of our sales of gold box technology will soon be replaced by pluggable modules. New products or modifications to existing products often take many quarters or even years to develop because of their complexity and because customer specifications sometimes change during the development cycle. We often incur substantial costs associated with the research and development and sales and marketing activities in connection with products that may be purchased long after we have incurred the costs associated with designing, creating and selling such products. In addition, due to the rapid technological changes in our market, a

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customer may cancel or modify a design project before we begin large-scale manufacture of the product and receive revenues from the customer. It is unlikely that we would be able to recover the expenses for cancelled or unutilized design projects. It is difficult to predict with any certainty, particularly in the present economic climate, the frequency with which customers will cancel or modify their projects, or the effect that any cancellation or modification would have on our results of operations.

As a result of our global operations, our business is subject to currency fluctuations that have adversely affected our results of operations in recent quarters and may continue to do so in the future.

Our financial results have been and will continue to be materially impacted by foreign currency fluctuations. At certain times in our history, declines in the value of the U.S. dollar versus the U.K. pound sterling have had a major negative effect on our margins and our cash flow. A significant portion of our expenses are denominated in U.K. pounds sterling and substantially all of our revenues are denominated in U.S. dollars.

Fluctuations in the exchange rate between these two currencies and, to a lesser extent, other currencies in which we collect revenues and/or pay expenses could have a material effect on our future operating results. From the end of our year ended June 27, 2009 to the end of our year ended July 3, 2010, the U.S. dollar appreciated 8 percent relative to the U.K. pound sterling, which favorably impacted our operating results for fiscal year 2010. If the U.S. dollar stays the same or depreciates relative to the U.K. pound sterling in the future, our future operating results may be materially impacted. Additional exposure could also result should the exchange rate between the U.S. dollar and the Chinese yuan, the South Korean won, the Israeli shekel, the Swiss franc or the Euro vary more significantly than they have to date.

We engage in currency hedging transactions in an effort to cover some of our exposure to U.S. dollar to U.K. pound sterling currency fluctuations, and we may be required to convert currencies to meet our obligations. These transactions may not operate to fully hedge our exposure to currency fluctuations, and under certain circumstances, these transactions could have an adverse effect on our financial condition.

We have significant manufacturing operations in China, which exposes us to risks inherent in doing business in China.

The majority of our assembly and test operations, chip-on-carrier operations and manufacturing and supply chain management operations are concentrated in our facility in Shenzhen, China. We have substantial research and development related activities in Shenzhen and Shanghai, China. To be successful in China we will need to:

- qualify our manufacturing lines and the products we produce in Shenzhen, as required by our customers;
- attract and retain qualified personnel to operate our Shenzhen facility; and
- attract and retain research and development employees at our Shenzhen and Shanghai facilities.

We cannot assure you that we will be able to do any of these.

Employee turnover in China is high due to the intensely competitive and fluid market for skilled labor. To operate our Shenzhen facility under these conditions, we will need to continue to hire direct manufacturing personnel, administrative personnel and technical personnel; obtain and retain required legal authorization to hire such personnel and incur the time and expense to hire and train such personnel. We are currently seeing a return of customer demand which had decreased as a result of adverse economic conditions in the preceding two years. Our ability to respond to this demand will, among other things, be a function of our ability to attract, train and retain skilled labor in China.

Operations in China are subject to greater political, legal and economic risks than our operations in other countries. In particular, the political, legal and economic climate in China, both nationally and regionally, is fluid and unpredictable. Our ability to operate in China may be adversely affected by changes in Chinese laws and regulations such as those related to, among other things, taxation, import and export tariffs, environmental regulations, land use rights, intellectual property, employee benefits and other matters. In addition, we may not

obtain or retain the requisite legal permits to continue to operate in China, and costs or operational limitations may be imposed in connection with obtaining and complying with such permits.

We have, in the past, been advised that power may be rationed in the location of our Shenzhen facility, and were power rationing to be implemented, it could have an adverse impact on our ability to complete manufacturing commitments on a timely basis or, alternatively, could require significant investment in generating capacity to sustain uninterrupted operations at the facility, which we may not be able to do successfully.

We intend to continue to export the majority of the products manufactured at our Shenzhen facility. Under current regulations, upon application and approval by the relevant governmental authorities, we will not be subject to certain Chinese taxes and will be exempt from certain duties on imported materials that are used in the manufacturing process and subsequently exported from China as finished products. However, Chinese trade regulations are in a state of flux, and we may become subject to other forms of taxation and duties in China or may be required to pay export fees in the future. In the event that we become subject to new forms of taxation or export fees in China, our business and results of operations could be materially adversely affected. We may also be required to expend greater amounts than we currently anticipate in connection with increasing production at our Shenzhen facility. Any one of the factors cited above, or a combination of them, could result in unanticipated costs or interruptions in production, which could materially and adversely affect our business.

Our results of operations may suffer if we do not effectively manage our inventory, and we may incur inventory-related charges.

We need to manage our inventory of component parts and finished goods effectively to meet changing customer requirements. Accurately forecasting customers product needs is difficult. Some of our products and supplies have in the past, and may in the future, become obsolete while in inventory due to rapidly changing customer specifications or a decrease in customer demand. We also have exposure to contractual liabilities to our contract manufacturers for inventories purchased by them on our behalf, based on our forecasted requirements, which may become excess or obsolete. If we are not able to manage our inventory effectively, we may need to write down the value of some of our existing inventory or write off non-saleable or obsolete inventory, which would adversely affect our results of operations. We have from time to time incurred significant inventory-related charges. Any such charges we incur in future periods could materially and adversely affect our results of operations.

We depend on a limited number of suppliers who could disrupt our business if they stopped, decreased, delayed or were unable to meet our demand for shipments of their products.

We depend on a limited number of suppliers of raw materials and equipment used to manufacture our products. We also depend on a limited number of contract manufacturers, principally Fabrinet in Thailand, to manufacture certain of our products. Some of these suppliers are sole sources. We typically have not entered into long-term agreements with our suppliers other than Fabrinet and, therefore, these suppliers generally may stop supplying us materials and equipment at any time. Our reliance on a sole supplier or limited number of suppliers could result in delivery problems, reduced control over product pricing and quality, and an inability to identify and qualify another supplier in a timely manner. Given the recent macroeconomic downturn, some of our suppliers that may be small or undercapitalized may experience financial difficulties that could prevent them from supplying us materials and equipment.

Any supply deficiencies relating to the quality or quantities of materials or equipment we use to manufacture our products could materially adversely affect our ability to fulfill customer orders and our results of operations. Lead times for the purchase of certain materials and equipment from suppliers have increased and in some cases have limited our ability to rapidly respond to increased demand, and may continue to do so in the future. These conditions have been exacerbated by suppliers, customers and companies reducing their inventory levels in response to the economic conditions described above.

In addition, Fabrinet s manufacturing operations are located in Thailand. Thailand has been subject to political unrest in the recent past, including the temporary interruption of service at one of its international airports, and may again experience such political unrest in the future. If Fabrinet is unable to supply us with materials or equipment, or

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if they are unable to ship our materials or equipment out of Thailand due to political unrest, this could materially adversely affect our ability to fulfill customer orders and our results of operations.

We may record additional impairment charges that will adversely impact our results of operations.

We review our goodwill, intangible assets and long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be recoverable, and also review goodwill annually. During the year ended June 27, 2009, we determined that the goodwill related to our New Focus and Avalon reporting units was fully impaired. Impairment of goodwill and other intangible assets for fiscal year 2009, net of $2.8 million associated with the discontinued operations of the New Focus business, amounted to $9.1 million.

During year ended July 3, 2010, we recorded goodwill of $20.0 million and other intangible assets of $9.8 million primarily in connection with our acquisitions of the Newport high-power laser diodes business and Xtellus. During the first quarter of fiscal year 2011, we also recorded goodwill of $10.9 million and other intangible assets of $11.7 million in connection with our acquisition of Mintera. In the event that we determine in a future period that impairment of our goodwill, intangible assets or long-lived assets exists for any reason, we would record additional impairment charges in the period such determination is made, which would adversely impact our financial position and results of operations.

We may incur additional significant restructuring charges that will adversely affect our results of operations.

We have previously enacted a series of restructuring plans and cost reduction plans designed to reduce our manufacturing overhead and our operating expenses. Such charges have adversely affected, and will continue to adversely affect, our results of operations for the periods in which such charges have been, or will be, incurred. Additionally, actual costs have in the past, and may in the future, exceed the amounts estimated and provided for in our financial statements. Significant additional charges could materially and adversely affect our results of operations in the periods that they are incurred and recognized.

For instance, we accrued $5.4 million and $2.2 million in restructuring charges during fiscal year 2009 and 2010, respectively, in connection with our merger with Avanex. On July 4, 2009, we completed the exchange of our New Focus business to Newport in exchange for Newport s high powered laser diode business, which resulted in us incurring $0.5 million in restructuring charges in fiscal year 2010 in connection with the transfer of the Tucson manufacturing operations to our European facilities, an activity which has inherent risk as to the ability to execute and timing to completion. While restructuring activities associated with our acquisitions of Xtellus and Mintera are expected to be more limited, the costs and execution risk of the corresponding actions could be significant.

If our customers do not qualify our manufacturing lines or the manufacturing lines of our subcontractors for volume shipments, our operating results could suffer.

Most of our customers do not purchase products, other than limited numbers of evaluation units, prior to qualification of the manufacturing line for volume production. Our existing manufacturing lines, as well as each new manufacturing line, must pass through varying levels of qualification with our customers. Our manufacturing lines have passed our qualification standards, as well as our technical standards. However, our customers also require that our manufacturing lines pass their specific qualification standards and that we, and any subcontractors that we may use, be registered under international quality standards. In addition, we have in the past, and may in the future, encounter quality control issues as a result of relocating our manufacturing lines or introducing new products to fill production. We may be unable to obtain customer qualification of our manufacturing lines or we may experience delays in obtaining customer qualification of our manufacturing lines. Such delays or failure to obtain qualifications would harm our operating results and customer relationships.

Delays, disruptions or quality control problems in manufacturing could result in delays in product shipments to customers and could adversely affect our business.

We may experience delays, disruptions or quality control problems in our manufacturing operations or the manufacturing operations of our subcontractors. As a result, we could incur additional costs that would adversely

affect our gross margins, and our product shipments to our customers could be delayed beyond the shipment schedules requested by our customers, which would negatively affect our revenues, competitive position and reputation. Furthermore, even if we are able to deliver products to our customers on a timely basis, we may be unable to recognize revenues at the time of delivery based on our revenue recognition policies.

We may experience low manufacturing yields.

Manufacturing yields depend on a number of factors, including the volume of production due to customer demand and the nature and extent of changes in specifications required by customers for which we perform design-in work. Higher volumes due to demand for a fixed, rather than continually changing, design generally results in higher manufacturing yields, whereas lower volume production generally results in lower yields. In addition, lower yields may result, and have in the past resulted, from commercial shipments of products prior to full manufacturing qualification to the applicable specifications. Changes in manufacturing processes required as a result of changes in product specifications, changing customer needs and the introduction of new product lines have historically caused, and may in the future cause, significantly reduced manufacturing yields, resulting in low or negative margins on those products. Moreover, an increase in the rejection rate of products during the quality control process, before, during or after manufacture, results in lower yields and margins. Finally, manufacturing yields and margins can also be lower if we receive or inadvertently use defective or contaminated materials from our suppliers. Any reduction in our manufacturing yields will adversely affect our gross margins and could have a material impact on our operating results.

Our intellectual property rights may not be adequately protected.

Our future success will depend, in large part, upon our intellectual property rights, including patents, copyrights, design rights, trade secrets, trademarks, know-how and continuing technological innovation. We maintain an active program of identifying technology appropriate for patent protection. Our practice is to require employees and consultants to execute non-disclosure and proprietary rights agreements upon commencement of employment or consulting arrangements. These agreements acknowledge our exclusive ownership of all intellectual property developed by the individuals during their work for us and require that all proprietary information disclosed will remain confidential. Although such agreements may be binding, they may not be enforceable in full or in part in all jurisdictions and any breach of a confidentiality obligation could have a very serious effect on our business and our remedy for such breach may be limited.

Our intellectual property portfolio is an important corporate asset. The steps we have taken and may take in the future to protect our intellectual property may not adequately prevent misappropriation or ensure that others will not develop competitive technologies or products. We cannot assure you that our competitors will not successfully challenge the validity of our patents or design products that avoid infringement of our proprietary rights with respect to our technology. There can be no assurance that other companies are not investigating or developing other similar technologies, that any patents will be issued from any application pending or filed by us or that, if patents are issued, that the claims allowed will be sufficiently broad to deter or prohibit others from marketing similar products. In addition, we cannot assure you that any patents issued to us will not be challenged, invalidated or circumvented, or that the rights under those patents will provide a competitive advantage to us or that our products and technology will be adequately covered by our patents and other intellectual property. Further, the laws of certain regions in which our products are or may be developed, manufactured or sold, including Asia-Pacific, Southeast Asia and Latin America, may not be enforced to protect our products and intellectual property rights to the same extent as the laws of the United States, the U.K. and continental European countries. This is especially relevant now that we have transferred certain advanced photonics solution manufacturing activities from our San Jose, California facility to Shenzhen, China and transferred all of our assembly and test operations and chip-on-carrier operations, including certain engineering-related functions, from our facilities in the U.K. to Shenzhen, China. Also relevant is that our competitors and new Chinese companies are establishing manufacturing operations in China to take advantage of comparatively low manufacturing costs.

Our products may infringe the intellectual property rights of others which could result in expensive litigation or require us to obtain a license to use the technology from third parties, or we may be prohibited from selling certain products in the future.

Companies in the industry in which we operate frequently are sued or receive informal claims of patent infringement or infringement of other intellectual property rights. We have, from time to time, received such claims, including from competitors and from companies that have substantially more resources than us.

For example, on May 27, 2009, a patent infringement action captioned *QinetiQ Limited v. Oclaro, Inc*., Civil Action No. 1:09-cv-00372, was filed in the United States District Court for the District of Delaware. QinetiQ s original complaint alleged infringement of United States Patent Nos. 5,410,625 and 5,428,698, and sought a permanent injunction, money damages, costs, and attorneys fees. We filed an answer to the complaint and stated counterclaims against QinetiQ for judgments that the patents-in-suit are invalid and unenforceable. Additionally, we filed a motion to transfer venue to the Northern District of California, which was granted on December 18, 2009. After transfer, the litigation was assigned Civil Action No. 4:10-cv-00080-SBA by the Northern District Court. On June 21, 2010, QinetiQ amended its complaint to allege infringement of a third patent, U.S. Patent No. 5,379,354. We answered QinetiQ s amended complaint and asserted fraud counterclaims against QinetiQ. A trial in this matter has not yet been set. We believe the claims asserted against us by QinetiQ are without merit and will continue to defend ourselves vigorously, but litigation is inherently uncertain and accordingly we cannot assure you of a positive outcome.

Third parties may in the future assert claims against us concerning our existing products or with respect to future products under development, or with respect to products that we may acquire through a merger, acquisition or asset purchase. We have entered into and may in the future enter into indemnification obligations in favor of some customers that could be triggered upon an allegation or finding that we are infringing other parties proprietary rights. If we do infringe a third-party s rights, we may need to negotiate with holders of those rights relevant to our business. We have from time to time received notices from third parties alleging infringement of their intellectual property and where appropriate have entered into license agreements with those third parties with respect to that intellectual property. We may not in all cases be able to resolve allegations of infringement through licensing arrangements, settlement, alternative designs or otherwise. We may take legal action to determine the validity and scope of the third-party rights or to defend against any allegations of infringement. The recent economic downturn could result in holders of intellectual property rights becoming more aggressive in alleging infringement of their intellectual property rights and we may be the subject of such claims asserted by a third-party. In the course of pursuing any of these means or defending against any lawsuits filed against us, we could incur significant costs and diversion of our resources and our management s attention. Due to the competitive nature of our industry, it is unlikely that we could increase our prices to cover such costs. In addition, such claims could result in significant penalties or injunctions that could prevent us from selling some of our products in certain markets or result in settlements or judgments that require payment of significant royalties or damages.

If we fail to obtain the right to use the intellectual property rights of others necessary to operate our business, our ability to succeed will be adversely affected.

Certain companies in the telecommunications and optical components markets in which we sell our products have experienced frequent litigation regarding patent and other intellectual property rights. Numerous patents in these industries are held by others, including academic institutions and our competitors. Optical component suppliers may seek to gain a competitive advantage or other third parties, inside or outside our market, may seek an economic return on their intellectual property portfolios by making infringement claims against us. We currently in-license certain intellectual property of third-parties, and in the future, we may need to obtain license rights to patents or other intellectual property held by others to the extent necessary for our business. Unless we are able to obtain such licenses on commercially reasonable terms, patents or other intellectual property held by others could be used to inhibit or prohibit our production and sale of existing products and our development of new products for our markets. Licenses granting us the right to use third-party technology may not be available on commercially reasonable terms, or at all. Generally, a license, if granted, would include payments of up-front fees, ongoing royalties or both. These payments or other terms could have a significant adverse impact on our operating results. In addition, in the event we are granted such a license, it is likely such license would be non-exclusive and other parties, including competitors, may

be able to utilize such technology. Our larger competitors may be able to obtain

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licenses or cross-license their technology on better terms than we can, which could put us at a competitive disadvantage. In addition, our larger competitors may be able to buy such technology and preclude us from licensing or using such technology.

The inability to obtain government licenses and approvals for desired international trading activities or technology transfers may prevent the profitable operation of our business.

Many of our present and future business activities are subject to licensing by the United States government under the Export Administration Act, the Export Administration Regulations and other laws, regulations and requirements governing international trade and technology transfer. We presently manufacture products in China and Thailand that require such licenses. The profitable operations of our business may require the continuity of these licenses and may require further licenses and approvals for future products in these and other countries. However, there is no certainty to the continuity of these licenses, nor that further desired licenses and approvals may be obtained.

The markets in which we operate are highly competitive, which could result in lost sales and lower revenues.

The market for optical components and modules is highly competitive and such competition could result in our existing customers moving their orders to competitors. We are aware of a number of companies that have developed or are developing optical component products, including tunable lasers, pluggables, wavelength selective switches and thin film filter products, among others, that compete directly with our current and proposed product offerings.

Certain of our competitors may be able to more quickly and effectively:

- develop or respond to new technologies or technical standards;
- react to changing customer requirements and expectations;
- devote needed resources to the development, production, promotion and sale of products; and
- deliver competitive products at lower prices.

Some of our current competitors, as well as some of our potential competitors, have longer operating histories, greater name recognition, broader customer relationships and industry alliances and substantially greater financial, technical and marketing resources than we do. In addition, market leaders in industries such as semiconductor and data communications, who may also have significantly more resources than we do, may in the future enter our market with competing products. All of these risks may be increased if the market were to further consolidate through mergers or other business combinations between competitors.

We may not be able to compete successfully with our competitors and aggressive competition in the market may result in lower prices for our products and/or decreased gross margins. Any such development could have a material adverse effect on our business, financial condition and results of operations.

We generate a significant portion of our revenues internationally and therefore are subject to additional risks associated with the extent of our international operations.

For fiscal years ended July 3, 2010, June 27, 2009 and June 28, 2008, 19 percent, 20 percent and 18 percent of our revenues, respectively, were derived from sales to customers located in the United States and 81 percent, 80 percent and 82 percent of our revenues, respectively, were derived from sales to customers located outside the United States. We are subject to additional risks related to operating in foreign countries, including:

- currency fluctuations, which could result in increased operating expenses and reduced revenues;
- greater difficulty in accounts receivable collection and longer collection periods;
- difficulty in enforcing or adequately protecting our intellectual property;

ability to hire qualified candidates;

foreign taxes;

political, legal and economic instability in foreign markets; and

foreign regulations.

Any of these risks, or any other risks related to our foreign operations, could materially adversely affect our business, financial condition and results of operations.

We may face product liability claims.

Despite quality assurance measures, defects may occur in our products. The occurrence of any defects in our products could give rise to liability for damages caused by such defects, including consequential damages. Such defects could, moreover, impair market acceptance of our products. Both could have a material adverse effect on our business and financial condition. In addition, we may assume product warranty liabilities related to companies we acquire, which could have a material adverse effect on our business and financial condition. In order to mitigate the risk of liability for damages, we carry product liability insurance with a $25.0 million aggregate annual limit and errors and omissions insurance with a $5.0 million annual limit. We cannot assure you that this insurance would adequately cover any or a portion of our costs arising from any defects in our products or otherwise.

If we fail to attract and retain key personnel, our business could suffer.

Our future success depends, in part, on our ability to attract and retain key personnel. Competition for highly skilled technical people is extremely intense and we continue to face difficulty identifying and hiring qualified engineers in many areas of our business. We may not be able to hire and retain such personnel at compensation levels consistent with our existing compensation and salary structure. Our future success also depends on the continued contributions of our executive management team and other key management and technical personnel, each of whom would be difficult to replace. The loss of services of these or other executive officers or key personnel or the inability to continue to attract qualified personnel could have a material adverse effect on our business.

In addition, certain former employees from prior mergers or acquisitions that are now employed by us may decide to no longer work for us with little or no notice for a number of reasons, including dissatisfaction with our corporate culture, compensation, and new roles or responsibilities, among others.

Risks Related to Regulatory Compliance and Litigation

Our business involves the use of hazardous materials, and we are subject to environmental and import/export laws and regulations that may expose us to liability and increase our costs.

We historically handled hazardous materials as part of our manufacturing activities. Consequently, our operations are subject to environmental laws and regulations governing, among other things, the use and handling of hazardous substances and waste disposal. We may incur costs to comply with current or future environmental laws. As with other companies engaged in manufacturing activities that involve hazardous materials, a risk of environmental liability is inherent in our manufacturing activities, as is the risk that our facilities will be shut down in the event of a release of hazardous waste, or that we would be subject to extensive monetary liability. The costs associated with environmental compliance or remediation efforts or other environmental liabilities could adversely affect our business. Under applicable EU regulations, we, along with other electronics component manufacturers, are prohibited from using lead and certain other hazardous materials in our products. We could lose business or face product returns if we fail to maintain these requirements properly.

In addition, the sale and manufacture of certain of our products require on-going compliance with governmental security and import/export regulations. We may, in the future, be subject to investigation which may result in fines for violations of security and import/export regulations. Furthermore, any disruptions of our product shipments in

the future, including disruptions as a result of efforts to comply with governmental regulations, could adversely affect our revenues, gross margins and results of operations.

We have in the past, and may in the future, merge with or acquire companies that have either experienced material weaknesses in their internal controls over financial reporting or have had no previous reporting obligations under Sarbanes-Oxley. A lack of effective internal control over our financial reporting could result in an inability to report our financial results accurately, which could lead to a loss of investor confidence in our financial reports and have an adverse effect on our stock price.

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports. If we cannot provide reliable financial reports or prevent fraud, our business and operating results could be harmed. Our failure to implement and maintain effective internal control over financial reporting could result in a material misstatement of our financial statements or otherwise cause us to fail to meet our financial reporting obligations. This, in turn, could result in a loss of investor confidence in the accuracy and completeness of our financial reports, which could have an adverse effect on our business, financial condition, operating results and our stock price, and we could be subject to stockholder litigation. Even if we are able to implement and maintain effective internal control over financial reporting, the costs of doing business may increase and our management may be required to dedicate greater time and resources to that effort.

Litigation may substantially increase our costs and harm our business.

On June 26, 2001, the first of a number of securities class actions was filed in the United States District Court for the Southern District of New York against New Focus, Inc., now known as Oclaro Photonics, Inc. (New Focus), certain of its officers and directors, and certain underwriters for New Focus initial and secondary public offerings. A consolidated amended class action complaint, captioned *In re New Focus, Inc. Initial Public Offering Securities Litigation*, No. 01 Civ. 5822, was filed on April 20, 2002. The complaint generally alleges that various underwriters engaged in improper and undisclosed activities related to the allocation of shares in New Focus initial public offering and seeks unspecified damages for claims under the Exchange Act on behalf of a purported class of purchasers of common stock from May 17, 2000 to December 6, 2000.

The lawsuit against New Focus is coordinated for pretrial proceedings with a number of other pending litigations challenging underwriter practices in over 300 cases, as *In re Initial Public Offering Securities Litigation*, 21 MC 92 (SAS), including actions against Bookham Technology plc, now known as Oclaro Technology Ltd (Bookham Technology) and Avanex Corporation, now known as Oclaro (North America), Inc. (Avanex), and certain of each entity s respective officers and directors, and certain of the underwriters of their public offerings. In October 2002, the claims against the directors and officers of New Focus, Bookham Technology and Avanex were dismissed, without prejudice, subject to the directors and officers execution of tolling agreements.

The parties have reached a global settlement of the litigation. On October 5, 2009, the Court entered an order certifying a settlement class and granting final approval of the settlement. Under the settlement, the insurers will pay the full amount of the settlement share allocated to New Focus, Bookham Technology and Avanex, and New Focus, Bookham Technology and Avanex will bear no financial liability. New Focus, Bookham Technology and Avanex, as well as the officer and director defendants who were previously dismissed from the action pursuant to tolling agreements, will receive complete dismissals from the case. Certain objectors have appealed the Court s October 5, 2009 order to the Second Circuit Court of Appeals. If for any reason the settlement does not become effective, we believe that Bookham Technology, New Focus and Avanex have meritorious defenses to the claims, but litigation is inherently uncertain and we cannot assure you of a positive outcome.

In addition, we are party to certain intellectual property infringement litigation as more fully described above under Risks Related to Our Business *Our products may infringe the intellectual property rights of others which could result in expensive litigation or require us to obtain a license to use the technology from third parties, or we may be prohibited from selling certain products in the future*.

Litigation is subject to inherent uncertainties, and an adverse result in these or other matters that may arise from time to time could have a material adverse effect on our business, results of operations and financial condition. Any

litigation to which we are subject may be costly and, further, could require significant involvement of our senior management and may divert management s attention from our business and operations.

Risks Related to Our Common Stock

A variety of factors could cause the trading price of our common stock to be volatile or to decline and we may incur significant costs from class action litigation due to our expected stock volatility.

The trading price of our common stock has been, and is likely to continue to be, highly volatile. Many factors could cause the market price of our common stock to rise and fall. In addition to the matters discussed in other risk factors included herein, some of the reasons for the fluctuations in our stock price are:

- fluctuations in our results of operations;
- changes in our business, operations or prospects;
- hiring or departure of key personnel;
- new contractual relationships with key suppliers or customers by us or our competitors;
- proposed acquisitions by us or our competitors;
- financial results or projections that fail to meet public market analysts expectations and changes in stock market analysts recommendations regarding us, other optical technology companies or the telecommunication industry in general;
- future sales of common stock, or securities convertible into or exercisable for common stock;
- adverse judgments or settlements obligating us to pay damages;
- future issuances of common stock in connection with acquisitions or other transactions;
- acts of war, terrorism, or natural disasters;
- industry, domestic and international market and economic conditions, including the global macroeconomic downturn over the last two years;
- low trading volume in our stock;
- developments relating to patents or property rights; and
- government regulatory changes.

In connection with our acquisition of Xtellus in December 2009, approximately 3.7 million of the shares of our common stock that we issued to Xtellus stockholders are or were subject to sale, transfer and other disposition restrictions. The restrictions lapsed on half of such shares six months after the closing date of the transaction and lapse on the remainder of such shares 12 months after the closing date of the transaction. The sale of these shares after the restrictions lapse could negatively impact our stock price. In addition, in connection with our recent acquisition of Mintera in July 2010, we may pay up to $20.0 million in additional revenue-based consideration to former stockholders of Mintera, determined based on a set of sliding scale formulas, to the extent revenue from Mintera products is more than $29.0 million in the twelve months following the acquisition and/or more than $40.0 million in the 18 months following the acquisition. Achieving cumulative revenues of $40 million over the next 12 months and $70.0 million over the next 18 month period would lead to the maximum $20.0 million in additional consideration. This earnout consideration, if any, will be payable in cash or, at our option, newly issued shares of our common stock,

or a combination of cash and stock. The issuance, if any, and subsequent sale of these shares could also negatively impact our stock price.

Our shares of common stock and the shares of our customers and competitors have experienced substantial price and volume fluctuations, in many cases without any direct relationship to the affected company s operating performance. An outgrowth of this market volatility is the significant vulnerability of our stock price and the stock prices of our customers and competitors to any actual or perceived fluctuation in the strength of the markets we serve, regardless of the actual consequence of such fluctuations. As a result, the market prices for stock in these companies are highly volatile. These broad market and industry factors have caused the market price of our common stock to fluctuate, and may in the future cause the market price of our common stock to fluctuate, regardless of our actual operating performance or the operating performance of our customers.

When the market price of a stock has been volatile, as our stock price may be, holders of that stock have occasionally brought securities class action litigation against the company that issued the stock. If any of our stockholders were to bring a lawsuit of this type against us, even if the lawsuit were without merit, we could incur substantial costs defending the lawsuit. The lawsuit could also divert the time and attention of our management. In addition, if the suit were resolved in a manner adverse to us, the damages we could be required to pay may be substantial and would have an adverse impact on our ability to operate our business.

Fluctuations in our operating results could adversely affect the market price of our common stock.

Our revenues and other operating results are likely to fluctuate significantly in the future. The timing of order placement, size of orders and satisfaction of contractual customer acceptance criteria, as well as order or shipment delays or deferrals, with respect to our products, may cause material fluctuations in revenues. Our lengthy sales cycle in both of our segments, which may extend to more than one year, may cause our revenues and operating results to vary from period to period and it may be difficult to predict the timing and amount of any variation. Delays or deferrals in purchasing decisions by our customers may increase as we develop new or enhanced products for new markets, including data communications, industrial, research, military, consumer and biotechnology markets. Our current and anticipated future dependence on a small number of customers increases the revenue impact of each such customer s decision to delay or defer purchases from us, or decision not to purchase products from us. Our expense levels in the future will be based, in large part, on our expectations regarding future revenue sources and, as a result, operating results for any quarterly period in which material orders fail to occur, or are delayed or deferred could vary significantly.

Because of these and other factors, quarter-to-quarter comparisons of our results of operations may not be indicative of our future performance. In future periods, our results of operations may differ, in some cases materially, from the estimates of public market analysts and investors. Such a discrepancy, or our failure to meet published financial projections, could cause the market price of our common stock to decline.

We may not be able to raise capital when desired on favorable terms without dilution to our stockholders, or at all.

The rapidly changing industry in which we operate, the length of time between developing and introducing a product to market and frequent changing customer specifications for products, among other things, makes our prospects difficult to evaluate. It is possible that we may not generate sufficient cash flow from operations, or be able to draw down on the $25.0 million senior secured revolving credit facility with Wells Fargo Capital Finance, Inc. and other lenders, or otherwise have sufficient capital resources to meet our future capital needs. If this occurs, we may need additional financing to execute on our current or future business strategies.

If we raise funds through the issuance of equity, equity-linked or convertible debt securities, our stockholders may be significantly diluted, and these newly-issued securities may have rights, preferences or privileges senior to those of securities held by existing stockholders. If we raise funds through the issuance of debt instruments, the agreements governing such debt instruments may contain covenant restrictions that limit our ability to, among other things: (i) incur additional debt, assume obligations in connection with letters of credit, or issue guarantees; (ii) create liens; (iii) make certain investments or acquisitions; (iv) enter into transactions with our affiliates; (v) sell certain assets; (vi) redeem capital stock or make other restricted payments; (vii) declare or pay dividends or make other distributions to stockholders; and (viii) merge or consolidate with any entity. We cannot assure you that additional financing will be available on terms favorable to us, or at all. If adequate funds are not available or are not

available on acceptable terms, if and when needed, our ability to fund our operations, develop or enhance our products, or otherwise respond to competitive pressures and operate effectively could be significantly limited.

Because we do not intend to pay dividends, stockholders will benefit from an investment in our common stock only if it appreciates in value.

We have never declared or paid any dividends on our common stock. We anticipate that we will retain any future earnings to support operations and to finance the development of our business and do not expect to pay cash dividends in the foreseeable future. As a result, the success of an investment in our common stock will depend entirely upon any future appreciation in its value. There is no guarantee that our common stock will appreciate in value or even maintain the price at which stockholders have purchased their shares.

We can issue shares of preferred stock that may adversely affect your rights as a stockholder of our common stock.

Our certificate of incorporation authorizes us to issue up to 1,000,000 shares of preferred stock with designations, rights and preferences determined from time-to-time by our board of directors. Accordingly, our board of directors is empowered, without stockholder approval, to issue preferred stock with dividend, liquidation, conversion, voting or other rights superior to those of holders of our common stock. For example, an issuance of shares of preferred stock could:

- adversely affect the voting power of the holders of our common stock;
- make it more difficult for a third-party to gain control of us;
- discourage bids for our common stock at a premium;
- limit or eliminate any payments that the holders of our common stock could expect to receive upon our liquidation; or
- otherwise adversely affect the market price of our common stock.

We may in the future issue shares of authorized preferred stock at any time.

Delaware law and our charter documents contain provisions that could discourage or prevent a potential takeover, even if such a transaction would be beneficial to our stockholders.

Some provisions of our certificate of incorporation and bylaws, as well as provisions of Delaware law, may discourage, delay or prevent a merger or acquisition that a stockholder may consider favorable. These include provisions:

- authorizing the board of directors to issue preferred stock;
- prohibiting cumulative voting in the election of directors;
- limiting the persons who may call special meetings of stockholders;
- prohibiting stockholder actions by written consent;
- creating a classified board of directors pursuant to which our directors are elected for staggered three-year terms;
- permitting the board of directors to increase the size of the board and to fill vacancies;
- requiring a super-majority vote of our stockholders to amend our bylaws and certain provisions of our certificate of incorporation; and
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted on by stockholders at stockholder meetings.

We are subject to the provisions of Section 203 of the Delaware General Corporation Law which limit the right of a corporation to engage in a business combination with a holder of 15 percent or more of the corporation s outstanding voting securities, or certain affiliated persons. We do not currently have a stockholder rights plan in place.

Although we believe that these charter and bylaw provisions, and provisions of Delaware law provide an opportunity for the board to assure that our stockholders realize full value for their investment, they could have the effect of delaying or preventing a change of control, even under circumstances that some stockholders may consider beneficial.

Item 6. ***Exhibits***

See the Exhibit Index on the page immediately preceding the exhibits for a list of exhibits filed as part of this Quarterly Report on Form 10-Q, which Exhibit Index is incorporated herein by reference.

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.

OCLARO, INC.

Date: November 10, 2010

By: **/s/ Jerry Turin**

Jerry Turin
Chief Financial Officer
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX

Exhibit Number	Description of Exhibit
2.1	Agreement of Merger, dated as of July 20, 2010, by and among Oclaro, Inc., Nikko Acquisition Corp., Mintera Corporation and Shareholder Representative Services LLC (previously filed as Exhibit 2.1 to our current report on Form 8-K, filed with the SEC on July 26, 2010, and incorporated herein by reference).
10.1	Variable Pay Program (previously filed as Exhibit 5.02 to our current report on Form 8-K, filed with the SEC on August 2, 2010, and incorporated herein by reference)
10.2	Amended and Restated Employment Agreement, dated August 4, 2010, by and between Oclaro, Inc. and Alain Couder (previously filed as Exhibit 10.1 to our current report on Form 8-K, filed with the SEC on August 10, 2010, and incorporated herein by reference).
10.3	Oclaro, Inc. Amended and Restated 2004 Stock Incentive Plan (previously filed as Exhibit 10.1 to our current report on Form 8-K, filed with the SEC on October 28, 2010, and incorporated herein by reference).
31.1	Certification of Chief Executive Officer Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350.
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.