MARVELL TECHNOLOGY GROUP LTD
Form 10-Q
September 04, 2014
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended August 2, 2014

or

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

For the transition period from ______ to ______

Commission file number: 000-30877

Marvell Technology Group Ltd.

(Exact name of registrant as specified in its charter)

Bermuda	**77-0481679**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

Canon s Court, 22 Victoria Street, Hamilton HM 12, Bermuda

(441) 296-6395

(Address of principal executive offices, Zip Code and registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

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	x	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

The number of common shares of the registrant outstanding as of August 28, 2014 was 514.4 million shares.

TABLE OF CONTENTS

Table of Contents

PART I: FINANCIAL INFORMATION

Item 1. ***Financial Statements***

MARVELL TECHNOLOGY GROUP LTD.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	August 2, 2014	February 1, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,332,535	$ 965,750
Short-term investments	967,469	1,003,655
Accounts receivable, net	498,484	453,496
Inventories	393,957	347,861
Prepaid expenses and other current assets	79,276	56,952
Deferred income taxes	17,285	11,506
Total current assets	3,289,006	2,839,220
Property and equipment, net	344,836	356,165
Long-term investments	13,422	16,279
Goodwill	2,029,945	2,029,945
Acquired intangible assets, net	38,072	49,035
Other non-current assets	150,413	160,366
Total assets	$ 5,865,694	$ 5,451,010
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 415,718	$ 316,389
Accrued liabilities	159,420	161,762
Accrued employee compensation	133,958	111,408
Deferred income	82,887	61,747
Total current liabilities	791,983	651,306
Non-current income taxes payable	72,019	81,325
Other non-current liabilities	40,158	42,469
Total liabilities	904,160	775,100
Commitments and contingencies (Note 10)		
Shareholders equity:		
Common shares, $0.002 par value	1,028	1,005
Additional paid-in capital	3,049,864	2,941,650
Accumulated other comprehensive income	627	597
Retained earnings	1,910,015	1,732,658
Total shareholders equity	4,961,534	4,675,910
Total liabilities and shareholders equity	$ 5,865,694	$ 5,451,010

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Net revenue	$ 961,545	$ 807,056	$ 1,919,375	$ 1,541,425
Operating costs and expenses:				
Cost of goods sold	477,741	386,059	971,601	721,497
Research and development	294,764	292,642	590,127	571,694
Selling and marketing	33,949	38,548	72,307	78,537
General and administrative	31,333	27,192	61,906	53,515
Amortization and write-off of acquired intangible assets	3,304	10,638	9,993	21,324
Total operating costs and expenses	841,091	755,079	1,705,934	1,446,567
Operating income	120,454	51,977	213,441	94,858
Interest and other income, net	12,263	8,253	14,188	11,413
Income before income taxes	132,717	60,230	227,629	106,271
Benefit for income taxes	(6,153)	(1,596)	(10,720)	(8,764)
Net income	$ 138,870	$ 61,826	$ 238,349	$ 115,035
Net income per share:				
Basic	$ 0.27	$ 0.13	$ 0.47	$ 0.23
Diluted	$ 0.27	$ 0.12	$ 0.46	$ 0.23
Weighted average shares:				
Basic	511,821	494,293	508,463	498,237
Diluted	520,269	500,625	520,510	503,006
Cash dividend declared per share	$ 0.06	$ 0.06	$ 0.12	$ 0.12

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Net income	$ 138,870	$ 61,826	$ 238,349	$ 115,035
Other comprehensive income, net of tax:				
Net change in unrealized gain/loss on marketable securities	(221)	(3,586)	157	(2,534)
Net change in unrealized gain/loss on auction rate securities	(34)	(251)	143	(170)
Net change in unrealized gain/loss on cash flow hedges	473	89	(270)	(16)
Other comprehensive income (loss), net	218	(3,748)	30	(2,720)
Comprehensive income	$ 139,088	$ 58,078	$ 238,379	$ 112,315

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	August 2, 2014	August 3, 2013
Cash flows from operating activities:		
Net income	$ 238,349	$ 115,035
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	53,269	50,663
Share-based compensation	64,989	74,604
Amortization and write-off of acquired intangible assets	10,963	21,324
Other expense (income), net	(6,126)	4,339
Excess tax benefits from share-based compensation	(76)	(32)
Changes in assets and liabilities:		
Accounts receivable	(30,159)	(100,636)
Inventories	(46,299)	(84,293)
Prepaid expenses and other assets	(27,157)	19,305
Accounts payable	87,686	83,869
Accrued liabilities and other non-current liabilities	2,962	(33,094)
Accrued employee compensation	22,550	3,952
Deferred income	21,140	15,315
Net cash provided by operating activities	392,091	170,351
Cash flows from investing activities:		
Purchases of available-for-sale securities	(335,770)	(471,469)
Sales and maturities of available-for-sale securities	372,410	498,680
Investments in privately-held companies	(441)	(750)
Cash paid for acquisition, net		(2,551)
Purchases of technology licenses	(9,409)	(7,610)
Purchases of property and equipment	(31,954)	(39,061)
Net cash used in investing activities	(5,164)	(22,761)
Cash flows from financing activities:		
Repurchase of common stock		(304,808)
Proceeds from employee stock plans	68,374	73,121
Minimum tax withholding paid on behalf of employees for net share settlement	(24,923)	(9,888)
Dividend payments to shareholders	(60,992)	(60,044)
Payments on technology license obligations	(2,677)	(6,301)
Excess tax benefits from share-based compensation	76	32
Net cash used in financing activities	(20,142)	(307,888)
Net increase (decrease) in cash and cash equivalents	366,785	(160,298)
Cash and cash equivalents at beginning of period	965,750	751,953
Cash and cash equivalents at end of period	$ 1,332,535	$ 591,655

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. The Company and Basis of Presentation

The Company

Marvell Technology Group Ltd., a Bermuda company (the Company), is a leading global semiconductor provider of high-performance application-specific standard products. The Company s core strength of expertise is the development of complex System-on-a-Chip devices leveraging its extensive technology portfolio of intellectual property in the areas of analog, mixed-signal, digital signal processing, and embedded and stand alone integrated circuits. The majority of the Company s product portfolio leverages the ARM technology portfolio. The Company also develops platforms that it defines as integrated hardware along with software that incorporates digital computing technologies designed and configured to provide an optimized computing solution compared to individual components. The Company s broad product portfolio includes devices for data storage, enterprise-class Ethernet data switching, Ethernet physical-layer transceivers, mobile handsets, connectivity and other consumer electronics.

Basis of Presentation

The Company s fiscal year is the 52- or 53-week period ending on the Saturday closest to January 31. In a 52-week year, each fiscal quarter consists of 13 weeks. The additional week in a 53-week year is added to the fourth quarter, making such quarter consist of 14 weeks. Fiscal 2015 and 2014 each have a 52-week period.

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for annual financial statements. In the opinion of management, all adjustments consisting of normal and recurring entries considered necessary for a fair statement of the results for the interim periods have been included in the Company s balance sheet as of August 2, 2014, the results of its operations for the three and six months ended August 2, 2014 and August 3, 2013, its comprehensive income for the three and six months ended August 2, 2014 and August 3, 2013, and its cash flows for the six months ended August 2, 2014 and August 3, 2013. The February 1, 2014 condensed consolidated balance sheet data was derived from the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended February 1, 2014, but does not include all disclosures required for annual periods.

These condensed consolidated financial statements and related notes are unaudited and should be read in conjunction with the Company s audited financial statements and related notes included in the Company s Annual Report on Form 10-K for the fiscal year ended February 1, 2014 as filed on March 27, 2014 with the Securities and Exchange Commission. The results of operations for the three and six months ended August 2, 2014 are not necessarily indicative of the results that may be expected for any other interim period or for the full fiscal year.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, the Company evaluates its estimates, including those related to performance-based compensation, revenue recognition, provisions for sales returns and allowances, inventory excess and obsolescence, investment fair values, goodwill and other intangible assets, restructuring, income taxes, litigation and other contingencies. In addition, the Company uses assumptions when employing the Black-Scholes valuation model to calculate the fair value of share-based awards that are granted. Actual results could differ from these estimates, and such differences could affect the results of operations reported in future periods.

Principles of Consolidation

The unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated. The functional currency of the Company and its subsidiaries is the U.S. dollar.

6

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 2. Recent Accounting Pronouncements

Accounting Pronouncements Not Yet Effective

In April 2014, the Financial Accounting Standards Board (FASB) issued an amendment to its guidance regarding the reporting requirements of discontinued operations. Under this amended guidance, a discontinued operation is defined as a disposal of a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has (or will have) a major effect on an entity s operations and financial results. In addition, this amendment requires an entity to present, for each comparative period, the assets and liabilities of a disposal group that includes a discontinued operation separately in the asset and liability sections, respectively, of the statement of financial position and additional disclosures about discontinued operations. This amended guidance is effective for annual and interim reporting periods beginning after December 15, 2014. The Company expects this guidance to have an impact on its financial statements only in the event of a future disposition which meets the criteria.

In May 2014, the FASB issued a new standard on the recognition of revenue from contracts with customers, which will supersede nearly all existing revenue recognition guidance under GAAP. The core principal of the standard is that an entity should recognize revenue when a customer has control of promised goods or services in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. It also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, and assets recognized from costs incurred to obtain or fulfill a contract, including significant judgments and changes in judgments. This standard is effective for annual and interim reporting periods beginning after December 15, 2016 and will be effective for the Company s first quarter of fiscal 2018. Early adoption is not permitted. The standard allows for either full retrospective or modified retrospective adoption. We are evaluating the transition method that will be elected and the potential effects of its adoption on our financial statements.

Note 3. Investments

The following tables summarize the Company s investments (in thousands):

	August 2, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Short-term investments:				
Available-for-sale:				
Corporate debt securities	$ 600,495	$ 2,754	$ (187)	$ 603,062
U.S. government and agency debt	250,395	103	(37)	250,461
Asset backed securities	73,401	60	(48)	73,413
Foreign government and agency debt	25,427	25	(22)	25,430
Municipal debt securities	15,060	44	(1)	15,103
Total short-term investments	964,778	2,986	(295)	967,469
Long-term investments:				
Available-for-sale:				
Auction rate securities	16,150		(2,728)	13,422
Total long-term investments	16,150		(2,728)	13,422
Total investments	$ 980,928	$ 2,986	$ (3,023)	$ 980,891

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	February 1, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Short-term investments:				
Available-for-sale:				
Corporate debt securities	$ 587,095	$ 2,789	$ (370)	$ 589,514
U.S. government and agency debt	301,423	128	(72)	301,479
Asset backed securities	76,220	89	(38)	76,271
Foreign government and agency debt	20,324	12	(44)	20,292
Municipal debt securities	16,059	44	(4)	16,099
Total short-term investments	1,001,121	3,062	(528)	1,003,655
Long-term investments:				
Available-for-sale:				
Auction rate securities	19,150		(2,871)	16,279
Total long-term investments	19,150		(2,871)	16,279
Total investments	$ 1,020,271	$ 3,062	$ (3,399)	$ 1,019,934

As of August 2, 2014, the Company s investment portfolio included auction rate securities with an aggregate par value of $16.2 million. Although these securities have continued to pay interest, there is currently limited trading volume. To estimate the fair value of the auction rate securities, the Company uses a discounted cash flow model based on estimated timing and amount of future interest and principal payments. In developing the cash flow model, the Company considers the credit quality and liquidity of the underlying securities and related issuer, the collateralization of underlying security investments and other considerations. The fair value of the auction rate securities as of August 2, 2014 was $2.7 million less than the par value and was recorded in long-term investments. Based on the Company s balance of approximately $2.3 billion in cash, cash equivalents and short-term investments, and the fact that the Company continues to generate positive cash flow from operations on a quarterly basis, the Company does not anticipate having to sell these securities below par value and does not have the intent to sell these auction rate securities until recovery. Since the Company considers the impairment to be temporary, the Company recorded the unrealized loss to accumulated other comprehensive income, a component of shareholders equity.

Gross realized gains and gross realized losses on sales of available-for-sales securities are presented in the following tables (in thousands):

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Gross realized gains	$ 480	$ 232	$ 952	$ 792
Gross realized losses		(14)	(25)	(37)
Total net realized gains	$ 480	$ 218	$ 927	$ 755

The contractual maturities of available-for-sale securities are presented in the following table (in thousands):

	August 2, 2014	February 1, 2014

	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 285,659	$ 286,045	$ 309,543	$ 309,861
Due between one and five years	674,803	677,119	686,062	688,280
Due over five years	20,466	17,727	24,666	21,793
	$ 980,928	$ 980,891	$ 1,020,271	$ 1,019,934

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For individual securities that have been in a continuous unrealized loss position, the fair value and gross unrealized loss for these securities aggregated by investment category and length of time in an unrealized position are presented in the following tables (in thousands):

	August 2, 2014					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Corporate debt securities	$ 82,399	$ (142)	$ 7,807	$ (45)	$ 90,206	$ (187)
U.S. government and agency debt	74,931	(37)			74,931	(37)
Asset backed securities	19,927	(48)			19,927	(48)
Foreign government and agency debt	19,420	(22)			19,420	(22)
Municipal debt securities	702	(1)			702	(1)
Auction rate securities			13,422	(2,728)	13,422	(2,728)
Total securities	$ 197,379	$ (250)	$ 21,229	$ (2,773)	$ 218,608	$ (3,023)

	February 1, 2014					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Corporate debt securities	$ 110,903	$ (366)	$ 2,105	$ (4)	$ 113,008	$ (370)
U.S. government and agency debt	93,118	(72)			93,118	(72)
Asset backed securities	18,865	(19)	1,912	(19)	20,777	(38)
Foreign government and agency debt	14,299	(44)			14,299	(44)
Municipal debt securities	723	(4)			723	(4)
Auction rate securities			16,279	(2,871)	16,279	(2,871)
Total securities	$ 237,908	$ (505)	$ 20,296	$ (2,894)	$ 258,204	$ (3,399)

Note 4. Supplemental Financial Information (in thousands)

	August 2, 2014	February 1, 2014
Inventories:		
Work-in-process	$ 250,615	$ 195,495
Finished goods	143,342	152,366
Total inventories	$ 393,957	$ 347,861

	August 2, 2014	February 1, 2014
Property and equipment, net:		
Machinery and equipment	$ 584,492	$ 562,038
Buildings	144,320	144,320
Computer software	96,619	96,096
Land	53,373	53,373
Building improvements	49,687	49,645
Leasehold improvements	49,830	49,060
Furniture and fixtures	27,577	27,621
Construction in progress	1,046	2,911
	1,006,944	985,064
Less: Accumulated depreciation and amortization	(662,108)	(628,899)
Total property and equipment, net	$ 344,836	$ 356,165

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	August 2, 2014	February 1, 2014
Other non-current assets:		
Technology and other licenses	$ 70,841	$ 83,521
Deferred tax assets	23,442	19,282
Investments in privately-held companies	9,006	14,565
Prepaid land use rights	13,588	13,744
Deposits	12,119	12,433
Other	21,417	16,821
Total other non-current assets	$ 150,413	$ 160,366

	August 2, 2014	February 1, 2014
Accrued liabilities:		
Accrued rebates	$ 69,199	$ 61,616
Accrued royalties	26,459	36,568
Technology license obligations	14,452	18,482
Accrued legal expense	17,522	14,589
Other	31,788	30,507
Total accrued liabilities	$ 159,420	$ 161,762

	August 2, 2014	February 1, 2014
Other non-current liabilities:		
Technology license obligations	$ 21,654	$ 28,959
Long-term accrued employee compensation	4,664	4,370
Other	13,840	9,140
Other non-current liabilities	$ 40,158	$ 42,469

Accumulated other comprehensive income

The changes in accumulated other comprehensive income by component are presented in the following tables (in thousands):

	Unrealized Gain (Loss) on Marketable Securities	Unrealized Gain (Loss) on Auction Rate Securities	Unrealized Gain (Loss) on Cash Flow Hedges	Total
Balance at February 1, 2014	$ 2,534	$ (2,871)	$ 934	$ 597
Other comprehensive income before reclassifications	1,012	143	734	1,889
	(855)		(1,004)	(1,859)

Amounts reclassified from accumulated other comprehensive income								
Other comprehensive income (loss)		157		143		(270)		30
Balance at August 2, 2014	$	2,691	$	(2,728)	$	664	$	627

10

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Unrealized Gain (Loss) on Marketable Securities	Unrealized Gain (Loss) on Auction Rate Securities	Unrealized Gain (Loss) on Cash Flow Hedges	Total
Balance at February 2, 2013	$ 2,742	$ (2,681)	$ 1,087	$ 1,148
Other comprehensive income before reclassifications	(1,991)	(170)	1,921	(240)
Amounts reclassified from accumulated other comprehensive income	(543)		(1,937)	(2,480)
Other comprehensive income (loss)	(2,534)	(170)	(16)	(2,720)
Balance at August 3, 2013	$ 208	$ (2,851)	$ 1,071	$ (1,572)

The amounts reclassified from accumulated other comprehensive income by components are presented in the following table (in thousands):

Affected Line Item in the Statement of Operations	Three Months Ended August 2, 2014	Three Months Ended August 3, 2013	Six Months Ended August 2, 2014	Six Months Ended August 3, 2013
Available-for-sale securities:				
Interest and other income, net	$ 435	$ 167	$ 855	$ 543
Cash flow hedges:				
Cost of goods sold	17	47	63	108
Research and development	183	726	858	1,671
Selling and marketing	19	63	81	145
General and administrative		5	2	13
Total	$ 654	$ 1,008	$ 1,859	$ 2,480

Net income per share

The Company reports both basic net income per share, which is based on the weighted average number of common shares outstanding, and diluted net income per share, which is based on the weighted average number of common shares outstanding and potentially dilutive common shares. The computations of basic and diluted net income per share are presented in the following table (in thousands, except per share amounts):

	Three Months Ended August 2, 2014	Three Months Ended August 3, 2013	Six Months Ended August 2, 2014	Six Months Ended August 3, 2013
Numerator:				
Net income	$ 138,870	$ 61,826	$ 238,349	$ 115,035
Denominator:				
Weighted average shares basic	511,821	494,293	508,463	498,237
Effect of dilutive securities:				
Share-based awards	8,448	6,332	12,047	4,769

Weighted average shares diluted		520,269		500,625		520,510		503,006
Net income per share:								
Basic	$	0.27	$	0.13	$	0.47	$	0.23
Diluted	$	0.27	$	0.12	$	0.46	$	0.23

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Anti-dilutive potential shares:				
Weighted average shares outstanding from stock options:				
Time-based options	23,203	41,923	21,285	30,660
Market-based options	2,289	2,738	2,336	2,753
	25,492	44,661	23,621	33,413
Weighted average exercise price:				
Time-based options	$ 17.55	$ 14.66	$ 17.81	$ 13.30
Market-based options	$ 15.43	$ 15.43	$ 15.43	$ 15.43
Total	$ 17.36	$ 14.71	$ 17.57	$ 13.48

Anti-dilutive potential shares for stock options are excluded from the calculation of diluted earnings per share for the periods reported above because either their exercise price exceeded the average market price during the period or certain stock options with exercise prices less than the average market price were determined to be anti-dilutive based on applying the treasury stock method.

Note 5. Derivative Financial Instruments

The Company manages some of its foreign currency exchange rate risk through the purchase of foreign currency exchange contracts that hedge against the short-term effect of currency fluctuations. Beginning in fiscal 2015, the Company entered into contracts to hedge the Chinese yuan in addition to the Israeli shekel as operating expenses in China continue to grow. The Company s policy is to enter into foreign currency forward contracts with maturities generally less than 12 months that mitigate the effect of rate fluctuations on certain local currency denominated operating expenses. All derivative instruments are recorded at fair value in either prepaid expenses and other current assets or accrued liabilities. The Company reports cash flows from derivative instruments in cash flows from operating activities. The Company uses quoted prices to value its derivative instruments.

The notional amounts of outstanding forward contracts were as follows (in thousands):

	Buy Contracts	
	August 2, 2014	February 1, 2014
Israeli shekel	$ 39,372	$ 39,670
Chinese yuan	34,319	
Euro	5,821	5,718
Swedish krona		3,709
	$ 79,512	$ 49,097

Cash Flow Hedges. The Company designates and documents its foreign currency forward exchange contracts as cash flow hedges for certain operating expenses denominated in Israeli shekels, Chinese yuan and Swedish krona. The Company evaluates and calculates the effectiveness of each hedge at least quarterly. The effective change is recorded in accumulated other comprehensive income and is subsequently reclassified to operating expense when the hedged expense is recognized. Ineffectiveness is recorded in interest and other income, net.

Other Foreign Currency Forward Contracts. The Company enters into foreign currency forward exchange contracts to hedge certain assets and liabilities denominated in various foreign currencies that it does not designate as hedges for accounting purposes. The maturities of these contracts are generally less than 12 months. Gains or losses arising from the remeasurement of these contracts to fair value each period are recorded in interest and other income, net.

The fair value of foreign currency exchange contracts was not significant as of any period presented.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 6. Fair Value Measurements

Fair value is an exit price representing the amount that would be received in the sale of an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. As a basis for considering such assumptions, the accounting guidance establishes a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1 Observable inputs that reflect quoted prices for identical assets or liabilities in active markets.

Level 2 Include other inputs that are directly or indirectly observable in the marketplace.

Level 3 Unobservable inputs that are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company s Level 1 assets include institutional money-market funds that are classified as cash equivalents and marketable investments in U.S. government and agency debt, which are valued primarily using quoted market prices. The Company s Level 2 assets include its marketable investments in time deposits, corporate debt securities, foreign government and agency debt, municipal debt securities and asset backed securities as the market inputs to value these instruments consist of market yields, reported trades and broker/dealer quotes, which are corroborated with observable market data. In addition, forward contracts and the severance pay fund are classified within Level 2 as the valuation inputs are based on quoted prices and market observable data of similar instruments. The Company s Level 3 assets include its investments in auction rate securities, which are classified within Level 3 because there are currently no active markets for the auction rate securities and consequently the Company is unable to obtain independent valuations from market sources. Therefore, the auction rate securities are valued using a discounted cash flow model. Some of the inputs to the cash flow model are unobservable in the market. The total amount of assets measured using Level 3 valuation methodologies represented 0.2% of total assets as of August 2, 2014.

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below set forth, by level, the Company s assets that were accounted for at fair value as of August 2, 2014 and February 1, 2014. The tables do not include assets and liabilities that are measured at historical cost or any basis other than fair value (in thousands):

	Level 1	Level 2	Level 3	Portion of Carrying Value Measured at Fair Value at August 2, 2014
Items measured at fair value on a recurring basis:				
Assets				
Cash equivalents:				
U.S. government and agency debt	$ 43,846	$	$	$ 43,846
Money market funds	19,981			19,981
Time deposits		181,163		181,163
Municipal debt securities		2,300		2,300
Corporate debt securities		1,450		1,450
Short-term investments:				
U.S. government and agency debt	250,461			250,461
Corporate debt securities		603,062		603,062
Asset backed securities		73,413		73,413
Foreign government and agency debt		25,430		25,430
Municipal debt securities		15,103		15,103
Prepaid expenses and other current assets:				
Foreign currency forward contracts		673		673
Long-term investments:				
Auction rate securities			13,422	13,422
Other non-current assets:				
Severance pay fund		1,976		1,976
Total assets	$ 314,288	$ 904,570	$ 13,422	$ 1,232,280
Liabilities				
Accrued liabilities:				
Foreign currency forward contracts	$	$ 194	$	$ 194

14

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Level 1	Level 2	Level 3	Portion of Carrying Value Measured at Fair Value at February 1, 2014
Items measured at fair value on a recurring basis:				
Assets				
Cash equivalents:				
U.S. government and agency debt	$ 11,999	$	$	$ 11,999
Money market funds	2,804			2,804
Time deposits		247,958		247,958
Municipal debt securities		4,800		4,800
Corporate debt securities		3,400		3,400
Short-term investments:				
U.S. government and agency debt	301,479			301,479
Corporate debt securities		589,514		589,514
Asset backed securities		76,271		76,271
Foreign government and agency debt		20,292		20,292
Municipal debt securities		16,099		16,099
Prepaid expenses and other current assets:				
Foreign currency forward contracts		1,012		1,012
Long-term investments:				
Auction rate securities			16,279	16,279
Other non-current assets:				
Severance pay fund		2,193		2,193
Total assets	$ 316,282	$ 961,539	$ 16,279	$ 1,294,100
Liabilities				
Accrued liabilities:				
Foreign currency forward contracts	$	$ 26	$	$ 26

The following table summarizes the change in fair value for Level 3 assets (in thousands):

	Six Months Ended	
	August 2, 2014	August 3, 2013
Beginning balance	$ 16,279	$ 16,769
Sales and redemptions	(3,000)	(300)
Unrealized losses included in accumulated other comprehensive income	143	(170)
Ending balance	$ 13,422	$ 16,299

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 7. Acquired Intangible Assets, Net

The carrying amount of acquired intangible assets, net, are as follows (in thousands):

		August 2, 2014			February 1, 2014		
	Range of Useful Lives	Gross Carrying Amounts	Accumulated Amortization and Write-Offs	Net Carrying Amount	Gross Carrying Amounts	Accumulated Amortization and Write-Offs	Net Carrying Amount
Purchased technology	4 - 6 years	$ 49,240	$ (25,124)	$ 24,116	$ 49,240	$ (20,634)	$ 28,606
Core technology	5 - 8 years	2,350	(1,761)	589	2,350	(1,583)	767
Trade names	5 years	1,300	(698)	602	1,300	(568)	732
Customer intangibles	5 - 6 years	28,600	(15,835)	12,765	28,600	(13,056)	15,544
IPR&D					3,386		3,386
Total intangible assets, net		$ 81,490	$ (43,418)	$ 38,072	$ 84,876	$ (35,841)	$ 49,035

The Company recorded a charge to write-off $3.4 million of IPR&D in the six months ended August 2, 2014, upon the Company s decision to discontinue the related project.

Based on the identified intangible assets recorded at August 2, 2014, the future amortization expense for the next five fiscal years is as follows (in thousands):

Fiscal Year	
Remainder of fiscal 2015	$ 7,374
2016	12,212
2017	11,027
2018	5,599
2019	1,860
Thereafter	
	$ 38,072

Note 8. Restructuring

In connection with ongoing evaluations of its business, the Company decided to streamline its operations, primarily in Israel to align with its overall strategic plan and to discontinue the development of a product it originally acquired from a business that it previously purchased. As a result, the Company recorded the following restructuring charges in the three and six months ended August 2, 2014 (in thousands):

	August 2, 2014	
	Three Months Ended	Six Months Ended
Severance and related costs	$ 418	$ 5,035

Facilities and related costs	254	698
Other exit-related costs	63	73
	735	5,806
Write-off of assets:		
Equipment		17
Acquired intangible asset		3,386
	$ 735	$ 9,209

The write-off of an acquired intangible asset in the six months ended August 2, 2014 was due to the Company s decision to discontinue the related project. Other exit-related costs are primarily associated with ongoing operating expenses related to vacated facilities under restructure actions in previous fiscal years.

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents details of restructuring charges by functional line item (in thousands):

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Research and development	$ 412	$	$ 5,094	$
Selling and marketing	(48)			
General and administrative	371	178	729	406
Write-off of acquired intangible assets			3,386	
	$ 735	$ 178	$ 9,209	$ 406

The following table sets forth a reconciliation of the beginning and ending restructuring liability balances by each major type of costs associated with the restructuring charges (in thousands):

	Severance and Related Costs	Facilities and Related Costs	Other Exit-Related Costs	Total
Balance at February 1, 2014	$ 51	$ 2,383	$ 19	$ 2,453
Restructuring charges	5,035	698	73	5,806
Net cash payments	(4,237)	(958)	(92)	(5,287)
Balance at August 2, 2014	$ 849	$ 2,123	$	$ 2,972

The severance costs included in the table above are expected to be paid by the end of the calendar year. The facility and related costs primarily represent an adjustment to the estimated sublease rentals related to the lease obligation of a vacated facility. The balance at August 2, 2014 for facility and related costs includes remaining payments under lease obligations related to vacated facilities under previous restructure actions which are expected to be paid through fiscal 2018.

Note 9. Income Tax

The income tax benefit for the three months ended August 2, 2014 included the current income tax liability of $4.9 million, which was more than offset by tax benefits of $7.3 million from a net reduction in unrecognized tax benefits and $3.7 million from an increase in the net deferred tax assets because of a tax rate change in Singapore. The Company finalized its agreement with the Singapore Economic Development Board for the remaining portion of pre-tax income subject to the Development and Expansion Incentive, which was extended through June 2019. The net reduction in unrecognized tax benefits primarily arose from the release of the expiration of statutes of limitation in non-U.S. jurisdictions. The income tax benefit for the six months ended August 2, 2014 included the current income tax liability of $10.6 million which was offset by a net reduction in unrecognized tax benefits of $9.8 million and $11.5 million from an increase in the net deferred tax assets because of the tax rate change in Singapore. The net reduction in unrecognized tax benefits arose from the release of $13.2 million due to the expiration of statutes of limitation, which was reduced by a $3.4 million increase in current unrecognized tax benefit estimates in various non-U.S. jurisdictions.

The income tax benefit for the three months ended August 3, 2013 included the current income tax liability of $5.2 million, which was offset by a net reduction in unrecognized tax benefits of $6.8 million. The net reduction in unrecognized tax benefits primarily arose from the expiration of statutes of limitation. The income tax benefit for the six months ended August 3, 2013 included the current income tax liability of $7.0 million plus $0.7 million in settlements of audits in non-U.S. jurisdictions, which were offset by a net reduction in unrecognized tax benefits of $16.5 million. The net reduction in unrecognized tax benefits primarily arose from the expiration of statutes of limitation in non-U.S. jurisdictions and from the settlement of two audits in non-U.S. jurisdictions (one for $3.5 million and the other for $4.1 million), less an increase in current unrecognized tax estimates.

It is reasonably possible that the amount of unrecognized tax benefits could increase or decrease significantly due to changes in tax law in various jurisdictions, new tax audits and changes in the U.S. dollar as compared to foreign currencies within the next 12 months. Excluding these factors, uncertain tax positions may decrease by as much as $17 million from the lapse of statutes of limitation in various jurisdictions during the next 12 months. Government tax authorities from several non-U.S. jurisdictions are also examining returns. The Company believes that it has adequately provided for any reasonably foreseeable outcomes related to its tax audits and that any settlement will not have a material effect on its results at this time.

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company operates under tax incentives in certain countries, which may be extended if certain additional requirements are satisfied. The tax incentives are conditional upon meeting certain employment and investment thresholds. The impact of these tax incentives decreased foreign taxes by $7.1 million and $10.4 million for the three and six months ended August 2, 2014, respectively, and $7.1 million and $9.2 million for the three and six months ended August 3, 2013, respectively. The benefit of the tax incentives on net income per share was $0.01 per share for the three months ended August 2, 2014 and $0.02 per share for the six months ended August 2, 2014, compared to less than $0.01 per share for the three months ended August 3, 2013 and $0.02 per share for the six months ended August 3, 2013.

Our principal source of liquidity as of August 2, 2014 consisted of approximately $2.3 billion of cash, cash equivalents and short-term investments, of which approximately $850 million was held by foreign subsidiaries (outside Bermuda). Approximately $500 million of this amount held by foreign subsidiaries is related to undistributed earnings, which have been indefinitely reinvested outside of Bermuda. These funds are primarily held in Israel, the United States and Switzerland. We have plans to use such amounts to fund various activities outside of Bermuda including working capital requirements, capital expenditures for expansion, funding of future acquisitions, or other financing activities. If such funds were needed by the parent company in Bermuda or if the amounts were otherwise no longer considered indefinitely reinvested, we would incur a tax expense of approximately $150 million.

Note 10. Commitments and Contingencies

Purchase Commitments

Under the Company s manufacturing relationships with its foundry partners, cancellation of all outstanding purchase orders are allowed but require payment of all costs and expenses incurred through the date of cancellation. As of August 2, 2014, these foundries had incurred approximately $228.9 million of manufacturing costs and expenses relating to the Company s outstanding purchase orders.

Intellectual Property Indemnification

The Company has agreed to indemnify certain customers for claims made against the Company s products, where such claims allege infringement of third party intellectual property rights, including, but not limited to, patents, registered trademarks, and/or copyrights. Under the aforementioned indemnification clauses, the Company may be obligated to defend the customer and pay for the damages awarded against the customer under an infringement claim as well as the attorneys fees and costs. The Company s indemnification obligations generally do not expire after termination or expiration of the agreement containing the indemnification obligation. Generally, there are limits on and exceptions to the Company s potential liability for indemnification. The Company cannot estimate the amount of potential future payments, if any, that it might be required to make as a result of these agreements. The maximum potential amount of any future payments that the Company could be required to make under these indemnification obligations could be significant.

Contingencies

The Company and certain of its subsidiaries are currently parties to various legal proceedings, including those noted in this section. The legal proceedings and claims described below could result in substantial costs and could divert the attention and resources of the Company s management. The Company is also engaged in other legal proceedings and claims not described below, which arise in the ordinary course of its business. Litigation is subject to inherent uncertainties and unfavorable rulings could occur. An unfavorable ruling in litigation could require the Company to pay damages, one-time license fees or ongoing royalty payments, and could prevent the Company from manufacturing or selling some of its products or limit or restrict the type of work that employees involved in such litigation may perform for the Company, any of which could adversely affect financial results in future periods. The Company believes that its products do not infringe valid and enforceable claims and it will continue to conduct a vigorous defense in these proceedings. However, there can be no assurance that these matters will be resolved in a manner that is not adverse to the Company s business, financial condition, results of operations or cash flows.

As of August 2, 2014, the Company has a $9.1 million accrued liability related to certain legal proceedings described below in this section. The amount recorded does not relate to the litigation with Carnegie Mellon University (CMU). Other than for the matters that the Company has recognized in the consolidated financial statements, it has not recorded any amounts for contingent losses associated with the matters described below based on its belief that losses, while reasonably possible, are not probable. Unless otherwise stated, the Company is currently unable to predict the final outcome of these lawsuits and therefore cannot determine the likelihood of loss nor estimate a range of possible loss.

Carnegie Mellon University Litigation. On March 6, 2009, CMU filed a complaint in the U.S. District Court for the Western District of Pennsylvania naming Marvell Semiconductor, Inc. (MSI) and the Company as defendants and alleging patent infringement. CMU has asserted U.S. Patent Nos. 6,201,839 and 6,438,180 (collectively, the CMU patents in suit), which relate to read-channel integrated circuit devices and the hard disk drive (HDD) incorporating such devices. A jury trial began on November 26, 2012. On December 26,

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2012, a jury delivered a verdict that found the CMU patents in suit were literally and willfully infringed and valid, and awarded past damages in the amount of $1.17 billion. CMU sought in its post-trial motions enhanced damages up to three times the jury verdict, pre-judgment interest up to $322 million, post-judgment interest, supplemental damages, attorneys fees, and an injunction and/or ongoing royalties. Post-trial motions were heard on May 1 and 2, 2013. On June 26, 2013, the District Court denied CMU s post-trial motion for attorney fees without prejudice. On August 23, 2013, the District Court denied the Company s motion for mistrial. On September 23, 2013, the District Court denied the Company s motion for judgment as a matter of law or a new trial on non-infringement, invalidity and other non-damages issue as well as the Company s motion for reduced damages. On the same day, the District Court granted-in-part CMU s motion for a finding of willful infringement and enhanced damages, reserving its further rulings on any enhancement of the verdict for a separate opinion. On December 6, 2013, CMU filed a motion to permit registration of judgment and a motion for supplemental relief including a request to enjoin future share repurchases, any leveraged buyout or similar asset leveraging transaction, and dividends (including the dividend scheduled for December 23, 2013), in the absence of a court approved bond or other security. On December 23, 2013, the District Court denied the motions. On January 8, 2014, CMU filed a motion for telephonic status conference, which was denied on January 28, 2014. On January 14, 2014, the District Court denied the Company s post-trial motion on laches. On March 31, 2014, the District Court rejected CMU s motion for an injunction. The District Court also denied CMU s request for pre-judgment interest, and substantially scaled back CMU s request for enhanced damages. Based on these decisions, the Court calculated the damages including enhancement to total approximately $1.54 billion, and held that, under its decision, CMU is entitled to post judgment interest and an ongoing royalty. On May 7, 2014, the District Court entered final judgment, from which the Company filed a notice of appeal on May 14, 2014. The Company filed its opening appeal brief on August 4, 2014. The Court has required us to report ongoing royalties under the current judgment. Based on the royalty rate assessed by the District Court, such additional royalties through August 2, 2014 could be as much as $300 million. If we are required to further secure all or some additional portion of ongoing royalties, we may be required to post cash or other Company assets as collateral.

The Company and MSI believe that the evidence and the law do not support the jury s findings of infringement, validity and the award of damages and do not believe a material loss is probable. The Company believes that there are strong grounds for appeal and the Company and MSI are currently pursuing an appeal before the U.S. Court of Appeals for the Federal Circuit in Washington, D.C. The Company believes the low end of the possible range of loss is zero, but it cannot reasonably estimate the upper range of the possible loss, as a number of factors could significantly change the assessment of damages.

USEI Litigation. On October 9, 2009, U.S. Ethernet Innovations, LLC (USEI) filed a complaint in the U.S. District Court for the Eastern District of Texas, in which USEI has accused a number of system manufacturers, including the Company s customers, of patent infringement (the USEI litigation). Specifically, USEI has asserted that these customers infringe U.S. Patent Nos. 5,307,459, 5,434,872, 5,732,094 and 5,299,313, which relate to Ethernet technologies. The complaint seeks unspecified damages and an injunction.

On May 4, 2010, MSI filed a motion to intervene in the USEI litigation, which was granted on May 19, 2010. On July 13, 2010, the District Court issued an order granting the defendants motion to transfer the action to the U.S. District Court for the Northern District of California; the case was formally transferred on August 23, 2010. On September 14, 2011, USEI withdrew its allegations against MSI for the 459 patent. The court issued a first claim construction ruling on January 31, 2012 and a supplemental claim construction ruling on August 29, 2012. On August 16, 2013, the District Court granted defendants summary judgment motion to preclude the plaintiff from recovering certain pre-suit damages. Trial is scheduled for January 5, 2015.

Lake Cherokee Patent Litigation. On June 30, 2010, Lake Cherokee Hard Drive Technologies, L.L.C. (Lake Cherokee) filed a complaint in the U.S. District Court for the Eastern District of Texas. The complaint alleged infringement of U.S. Patent Nos. 5,844,738 and 5,978,162 (collectively, the Lake Cherokee patents) which purportedly relate to read-channel integrated circuit devices and to certain HDD products incorporating such devices. Lake Cherokee s damages claim was approximately $193 million at the start of trial. The case proceeded to trial on August 12, 2013. On August 16, 2013, an Eastern District of Texas jury returned a verdict which unanimously found that MSI did not infringe the Lake Cherokee patents and the Court entered judgment in MSI s favor. Lake Cherokee then moved for a new trial and the briefing was concluded on October 28, 2013.

On September 5, 2013, Lake Cherokee filed a second suit in the U.S. District Court for the Eastern District of Texas against Marvell Asia Pte., Ltd. and several of the Company s storage customers, alleging infringement of the Lake Cherokee patents.

On September 25, 2013, Lake Cherokee filed a third suit in the U.S. District Court for the Eastern District of Texas against MSI, MAPL and two of the Company s customers, alleging infringement of U.S. Patent No. 5,583,706, which purportedly relates to certain HDD related technologies.

All the parties involved in the three cases reached settlement in August 2014 and motions to dismiss were filed. The settlement did not have a significant impact on the Company s financial statements.

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Azure Networks Litigation. On March 22, 2011, Azure Networks, LLC and Tri-County Excelsior Foundation filed suit in the U.S. District Court for the Eastern District of Texas against MSI and eight other companies. The Complaint asserts U.S. Patent No. 7,756,129 against MSI s Bluetooth products. MSI filed its answer and counterclaims on July 20, 2011. On November 2, 2012, MSI and the other defendants filed a motion for summary judgment of invalidity, which was denied. A claim construction hearing was held on December 20, 2012. On January 15, 2013, the magistrate judge issued a claim construction ruling. On May 20, 2013, the District Court issued an order denying plaintiff s motion for reconsideration and adopted the magistrate judge s claim construction ruling. On May 30, 2013, the District Court entered a judgment of non-infringement. On June 24, 2013, Azure appealed, and the appeal has been briefed. Oral argument before a Federal Circuit panel was held on April 11, 2014.

Power Management Systems Litigation. On August 22, 2011, Power Management Systems LLC (PMS), a subsidiary of Acacia Research Corp., filed a complaint against the Company s subsidiary Marvell Semiconductor, Ltd. (MSL) and other defendants, in the U.S. District Court for the District of Delaware. The complaint asserts U.S. Patent No. 5,504,909, which relates to a power management apparatus, against various products. The complaint seeks unspecified damages. On October 17, 2011, PMS amended its complaint by substituting MSL with MSI. MSI filed its answer and counterclaims on November 4, 2011. A claim construction hearing was held on January 18, 2013, and a ruling was issued on May 30, 2013. On June 14, 2013, the District Court entered a judgment of non-infringement. On June 17, 2013, PMS appealed, and the appeal has been briefed. The Federal Circuit Court of Appeals heard oral argument on January 10, 2014, and affirmed the district court s rulings on January 14, 2014. The deadline for PMS to appeal to the United States Supreme Court passed in mid-April 2014 without PMS taking any further action.

France Telecom Litigation. On June 26, 2012, France Telecom S.A. filed a complaint against MSI in the U.S. District Court for the Southern District of New York. The complaint asserts U.S. Patent No.5,446,747 against MSI s communications processors and thin modems. The complaint seeks unspecified damages as well as injunctive relief. MSI answered the complaint on July 18, 2012 and August 1, 2012. On July 30, 2012, MSI filed a motion to transfer the lawsuit to the U.S. District Court for the Northern District of California. On September 17, 2012, the Court granted MSI s motion and transferred the case to the Northern District of California. A claim construction hearing was held on December 13, 2013. On April 14, 2014, the Court denied MSI s motion for summary judgment of invalidity, and granted MSI s summary judgment motion concerning certain damages preclusion. Trial is scheduled for September 15, 2014.

Freescale Litigation. On July 6, 2012, Freescale Semiconductor, Inc. (Freescale) filed a complaint against MSI in the U.S. District Court for the Western District of Texas, and amended the complaint on February 4, 2013. On January 4, 2013, three of the Company s subsidiaries, MSI, Marvell International Ltd. and Marvell World Trade Ltd., filed a complaint against Freescale in the U.S. District Court for the Western District of Texas, and amended the compliant on January 14, 2013. On April 11, 2014, the Court dismissed both of the above two cases with prejudice pursuant to a settlement and patent license agreement. The settlement did not have a significant impact on the Company s financial statements.

Progressive Semiconductor Solutions Patent Litigation. On September 30, 2013, Progressive Semiconductor Solutions LLC (PSS) filed a complaint in the Central District of California against MSI and another defendant, alleging infringement of U.S. Patent Nos. 6,473,349 (the 349 patent) and 6,862,208 (the 208 patent). The patents purportedly relate to certain memory devices. On March 3, 2014, the District Court dismissed MSI without prejudice. On March 4, 2014, PSS filed a new complaint against MSI, alleging infringement of the 349 patent but not the 208 patent. The parties reached settlement in August 2014 and the case was dismissed with prejudice on August 21, 2014. The settlement did not have a significant impact on the Company s financial statements.

Vantage Point Technology Patent Litigation. On November 21, 2013, Vantage Point Technology, Inc. (VPT) filed suit against a third party defendant for patent infringement relating to processor technology. On February 3, 2014, VPT filed an amended complaint against the third party and added MSI as an additional defendant. The complaint seeks unspecified damages. A claim construction hearing is currently scheduled for January 27, 2015. The first trial in the series of VPT cases against various defendants is currently scheduled for July 13, 2015.

Voss Litigation and Consolidated Cases. On April 7, 2014, Lee Voss (Voss) filed an action asserting putative class action claims on behalf of the Company s shareholders and derivative claims ostensibly on behalf of the Company in the United States District Court for the Northern District of California, San Jose Division. The complaint alleges that certain officers and directors of the Company breached their fiduciary duties by causing or allowing the Company to engage in the purported willful infringement of certain patents asserted against it in litigation by CMU and by failing to institute adequate internal controls, resulting in an adverse verdict. Additionally, the complaint alleges unjust enrichment and a breach of the duty of honest services by three of the officers. The Company is named as a nominal defendant. Voss requests damages and restitution in unspecified amounts, equitable and/or injunctive relief, and the costs and fees of bringing the action. On June 2, 2014, Sebastiano D Arrigo filed a second, nearly identical complaint in the same court, which was consolidated with the Voss action. On June 13, 2014, James and Marie DiBiase filed a third, nearly identical complaint in the Superior

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Court for the County of Santa Clara Superior Court, which was removed to the United States District Court for the Northern District of California, San Jose Division and consolidated with the Voss action. The plaintiffs filed an amended consolidated complaint on August 15, 2014. The action is in the preliminary stages and the Court has permitted only limited discovery.

Bandspeed Litigation. On May 9, 2014, Bandspeed, Inc. filed suit against MSI, alleging infringement of U.S. Patent Nos. 7,027,418; 7,570,614; 7,477,624; 7,903,608; 8,542,643, purportedly related to certain Bluetooth technology. The complaint seeks unspecified damages.

Surety Bond

On May 14, 2014, the Company filed a Notice of Appeal to appeal the final judgment issued by the District Court in the CMU litigation. In order to stay the execution of the final judgment pending its appeal, the Company filed a supersedeas bond for $1.54 billion with the District Court. The bond was issued by a consortium of sureties authorized by the U.S. Treasury. If the judgment is affirmed after the completion of all appellate proceedings, and the Company does not thereafter fully satisfy the judgment within thirty days, the sureties are obligated under the bond to make payment to CMU. In support of the bond, the Company entered into separate indemnity agreements with each of the sureties to indemnify the sureties from all costs and payments made under the bond. The indemnity agreements did not require collateral to be posted at the time of the issuance of the bond. Therefore no cash or other Company assets are considered restricted as of the date of this filing. However, the indemnity agreements provide that each of the sureties have the right to demand to be placed in funds or call for collateral under pre-defined events. The indemnity agreements will remain outstanding for as long as the underlying bond remains outstanding.

Indemnities, Commitments and Guarantees

During its normal course of business, the Company has made certain indemnities, commitments and guarantees under which it may be required to make payments in relation to certain transactions. These indemnities may include intellectual property indemnities to the Company s customers in connection with the sales of its products, indemnities for liabilities associated with the infringement of other parties technology based upon the Company s products, indemnities for general commercial obligations, indemnities to various lessors in connection with facility leases for certain claims arising from such facility or lease, and indemnities to directors and officers of the Company to the maximum extent permitted under the laws of Bermuda. In addition, the Company has contractual commitments to various customers, which could require the Company to incur costs to repair an epidemic defect with respect to its products outside of the normal warranty period if such defect were to occur. The duration of these indemnities, commitments and guarantees varies, and in certain cases, is indefinite. Some of these indemnities, commitments and guarantees do not provide for any limitation of the maximum potential future payments that the Company could be obligated to make. In general, the Company does not record any liability for these indemnities, commitments and guarantees in the accompanying consolidated balance sheets as the amounts cannot be reasonably estimated and are not considered probable. The Company does, however, accrue for losses for any known contingent liability, including those that may arise from indemnification provisions, when future payment is probable.

Note 11. Shareholders Equity

Stock Plans

Activity under the Company s stock option plans for the six months ended August 2, 2014 is summarized below (in thousands, except per share amounts):

	Time-Based Options		Market-Based Options		Total	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Balance at February 1, 2014	49,156	$ 13.40	2,623	$ 15.43	51,779	$ 13.51
Granted	6,011	$ 15.37		$	6,011	$ 15.37

Exercised	(2,722)	$	10.63		$		(2,722)	$	10.63
Canceled/Forfeited	(2,987)	$	14.72	(364)	$	15.43	(3,351)	$	14.79
Balance at August 2, 2014	49,458	$	13.72	2,259	$	15.43	51,717	$	13.79
Vested or expected to vest at August 2, 2014	45,857	$	13.79						
Exercisable at August 2, 2014	23,929	$	15.14						

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For time-based stock options vested and expected to vest at August 2, 2014, the aggregate intrinsic value was $75.7 million and the weighted average remaining contractual term was 6.2 years. For time-based stock options exercisable at August 2, 2014, the aggregate intrinsic value was $38.0 million and the weighted average remaining contractual term was 3.9 years. The aggregate intrinsic value of stock options exercised during the three months ended August 2, 2014 and August 3, 2013 was $4.2 million and $5.0 million, respectively. The aggregate intrinsic value of stock options exercised during the six months ended August 2, 2014 and August 3, 2013 was $13.6 million and $16.1 million, respectively. There was no aggregate intrinsic value for market-based stock options at August 2, 2014 and the weighted average remaining contractual term of market-based stock options expected to reach the end of the vesting period at August 2, 2014 was 6.7 years. The Company s closing stock price of $13.39 as reported on the NASDAQ Global Select Market for all in-the-money options as of August 1, 2014 was used to calculate the aggregate intrinsic value.

As of August 2, 2014, the unamortized compensation expense for time-based stock options was $67.0 million and market-based stock options were fully amortized in fiscal 2014. The unamortized compensation expense for time-based stock options will be amortized on a straight-line basis and is expected to be recognized over a weighted average period of 2.8 years.

Included in the following table is activity related to the non-vested portion of the restricted stock units as follows (in thousands, except for share prices):

	Time-Based		Performance-Based		Total	
	Number of Shares	Weighted Average Grant Date Fair Value	Number of Shares	Weighted Average Grant Date Fair Value	Number of Shares	Weighted Average Grant Date Fair Value
Balance at February 1, 2014	11,254	$ 14.11	100	$ 10.52	11,354	$ 14.08
Granted	5,240	$ 15.30	1,257*	$ 15.00*	6,497	$ 15.24
Vested	(5,405)	$ 14.02	(3)	$ 10.52	(5,408)	$ 14.01
Canceled/Forfeited	(623)	$ 14.12	(99)	$ 10.63	(722)	$ 13.64
Balance at August 2, 2014	10,466	$ 14.79	1,255	$ 15.00	11,721	$ 14.81

* Amounts represent the target number of restricted stock units at grant date. For awards granted to our executive officers, up to 200% of the target restricted stock units may vest if the maximum level for financial and strategic goals is achieved.

In June 2014, the Company granted performance-based restricted stock units (PSUs) to certain members of senior management. Pursuant to the PSUs, each eligible employee is entitled to vest in a certain number of shares based on such employee s achievement of individual financial and strategic performance goals for fiscal 2015, including, for example, net revenue and operating expense targets, and other individual strategic milestones. The actual number of shares that will vest for each eligible employee based on the achievement of such performance goals will be determined at the end of fiscal 2015 and will vest over two years, with 50% vesting on April 1, 2015 and 50% on April 1, 2016. The Company recognizes expenses associated with the PSUs when it becomes probable that the performance conditions will be met. Once it becomes probable that a PSU will vest, the Company recognizes compensation expense equal to the number of shares multiplied by the fair value of the related shares measured at the grant date.

The aggregate intrinsic value of restricted stock units expected to vest as of August 2, 2014 was $142.7 million. The number of restricted stock units that are expected to vest is 10.7 million shares.

As of August 2, 2014, unamortized compensation expense related to restricted stock units was $132.9 million. The unamortized compensation expense for restricted stock units will be amortized on a straight-line basis and is expected to be recognized over a weighted average period of 1.8 years.

Executive Performance Awards

In April 2014, the Company granted performance-based equity awards to each of our executive officers which are based on their achievement of certain performance goals in fiscal 2015 and 2016. These equity awards include restricted stock units which vest based on financial performance criteria (Financial Performance RSU) and restricted stock units which vest based on both financial performance criteria and individual strategic goals (Strategic Performance Award). The Financial Performance RSUs will be earned based on the achievement of revenue and modified non-GAAP operating income that have been established at threshold, target and maximum levels. Each Financial Performance RSU will vest 50% on the first anniversary of the commencement date based on achievement of fiscal 2015 financial performance criteria and 50% on the second anniversary of the vesting commencement date based on the achievement of fiscal 2016 financial performance criteria. The Strategic Performance Awards will vest based on achievement at the threshold level of either the revenue or modified non-GAAP operating income objective established for the Financial Performance RSU, in addition to the achievement of additional individual strategic goals. Each Strategic Performance Award will vest 50% on the first anniversary of the commencement date based on achievement of fiscal 2015 individual strategic goals and 50% on second anniversary date based on the achievement of the fiscal 2016 individual strategic goals.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Employee Stock Purchase Plan

During the three and six months ended August 2, 2014, a total of 5.2 million shares were issued at a weighted-average price of $7.58 per share under the 2000 Employee Stock Purchase Plan, as amended and restated (the ESPP). During the three and six months ended August 3, 2013, a total of 5.0 million shares were issued at a weighted-average price of $7.34 per share under the ESPP. As of August 2, 2014, there was $10.9 million of unrecognized compensation cost related to the ESPP.

Share Repurchase Program

The Company had no repurchases of its common shares during the three and six months ended August 2, 2014. During the three and six months ended August 3, 2013, the Company repurchased 7.2 million of its common shares for $82.6 million in cash and 27.1 million of its common shares for $282.8 million in cash, respectively. The repurchased shares were retired immediately after the repurchases were completed. The Company records all repurchases, as well as investment purchases and sales, based on trade date. As of August 2, 2014, a total of 216.9 million cumulative shares have been repurchased under the Company s share repurchase program for a total $2.7 billion in cash and there was $258.4 million remaining available for future share repurchases.

Dividends

The Company paid the following cash dividends in the three and six months ended August 2, 2014 and August 3, 2013:

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Cash dividend per share	$ 0.06	$ 0.06	$ 0.12	$ 0.12
Total payment to shareholders (in thousands)	$ 30,820	$ 29,791	$ 60,992	$ 60,044

On August 21, 2014, the Company announced that its board of directors declared a cash dividend of $0.06 per share to be paid on October 2, 2014 to shareholders of record as of September 11, 2014.

Future payment of a regular quarterly cash dividend on the Company s common shares will be subject to, among other things, the best interests of the Company, the Company s results of operations, cash balances and future cash requirements, financial condition, statutory requirements under Bermuda law and other factors that the Company s board of directors may deem relevant. The Company s dividend payments may change from time to time, and the Company cannot provide assurance that it will continue to declare dividends at all or in any particular amounts. In addition, developments in ongoing litigation could affect the Company s ability to make a dividend payment on a declared payment date until such time as the Company can meet statutory requirements under Bermuda law.

Note 12. Share-Based Compensation

The following table presents details of share-based compensation expenses by functional line item (in thousands):

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Cost of goods sold	$ 1,733	$ 1,868	$ 4,032	$ 3,735

Research and development	24,276	28,982	44,644	52,261
Selling and marketing	2,617	3,648	5,545	7,040
General and administrative	6,394	6,593	10,768	11,568
	$ 35,020	$ 41,091	$ 64,989	$ 74,604

Share-based compensation capitalized in inventory was $1.5 million at August 2, 2014 and $1.7 million at February 1, 2014.

Table of Contents

MARVELL TECHNOLOGY GROUP LTD.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Valuation Assumptions

The following weighted average assumptions were used for each respective period to calculate the fair value of each time-based stock option award on the date of grant using the Black-Scholes valuation model:

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Time-based Stock Options:				
Weighted average fair value	$ 3.98	$ 3.63	$ 4.37	$ 3.41
Expected volatility	34%	44%	35%	45%
Expected term (in years)	5.0	5.0	5.0	5.0
Risk-free interest rate	1.7%	1.2%	1.6%	0.8%
Expected dividend yield	1.6%	2.1%	1.6%	2.4%

	Three and Six Months Ended	
	August 2, 2014	August 3, 2013
Employee Stock Purchase Plan:		
Estimated fair value	$ 4.13	$ 3.45
Volatility	32%	40%
Expected term (in years)	1.3	1.3
Risk-free interest rate	0.2%	0.2%
Dividend yield	1.6%	2.2%

Table of Contents

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 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), which are subject to the safe harbor created by those sections. These statements involve known and unknown risks, uncertainties and other factors, which may cause our actual results to differ materially from those implied by the forward-looking statements. Words such as anticipates, expects, intends, plans, believes, seeks, estimates, can, will and similar expressions identify such forward-looking statements. Examples of forward-looking statements include statements regarding:

our anticipation that the rate of new orders and shipments may vary significantly from quarter to quarter;

market acceptance of our products using our innovative solutions;

sustained investments leading to new growth opportunities;

our expectations about industry trends;

future growth of our customer s products, including the timing of any launches;

increased competition in the semiconductor industry;

the pricing of our products;

future customer concentration;

net revenue, cost of goods sold as a percentage of revenue and operating expenses for future periods;

the impact of legal proceedings and claims;

our ability to meet our capital needs for at least the next 12 months;

future growth opportunities;

the effect of recent accounting pronouncements and changes in taxation rules;

the effectiveness of our hedges of foreign currency exposures;

- *our plans regarding our investment portfolio;*
- *our expectation that quarterly operating results will fluctuate from quarter to quarter;*
- *the general economic environment;*
- *arrangements with suppliers;*
- *our ability to develop and introduce new products and achieve market acceptance of our products;*
- *demand for our products and the impact of seasonality on demand;*
- *the implementation and improvement of operational and financial systems, as well as the implementation of additional procedures and other internal management systems;*
- *gross margin and the events that may cause gross margin to fluctuate;*
- *the transition of our semiconductor products to increasingly smaller line width geometries;*
- *our operations and sales outside of the United States, including future sales in Asia; and*
- *the anticipated features and benefits of our technology solutions.*

These forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those indicated in the forward-looking statements. Factors that could cause actual results to differ materially from those predicted, include, but are not limited to:

- *our dependence upon the hard disk drive and mobile and wireless markets, which are highly cyclical and intensely competitive;*
- *the outcome of pending or future litigation and legal proceedings, including our patent litigation action involving Carnegie Mellon University;*

- *our dependence on a small number of customers;*
- *our ability and the ability of our customers to successfully compete in the markets in which we serve;*
- *our reliance on independent foundries and subcontractors for the manufacture, assembly and testing of our products;*
- *our ability and our customers ability to develop new and enhanced products and the adoption of those products in the market;*
- *decreases in our gross margin and results of operations in the future due to a number of factors;*
- *our ability to estimate customer demand and future sales accurately, including the impact of lengthy and expensive product sales cycles;*
- *our ability to scale our operations in response to changes in demand for existing or new products and services;*
- *the impact of international conflict and continued economic volatility in either domestic or foreign markets;*
- *our ability to transition to smaller geometry process technologies or higher levels of design integration;*
- *the risks associated with manufacturing and selling a majority of our products and our customers products outside of the United States;*
- *the impact of any change in our application of the United States federal income tax laws and the loss of any beneficial tax treatment that we currently enjoy;*
- *our success in integrating businesses we acquire and the impact such acquisitions may have on our operating results;*
- *our ability to protect our intellectual property;*
- *the impact and costs associated with changes in international financial and regulatory conditions; and*
- *our maintenance of an effective system of internal controls;*

Additional factors which could cause actual results to differ materially include those set forth in the following discussion, as well as the risks discussed in Part II, Item 1A, Risk Factors, and other sections of this Quarterly Report on Form 10-Q. These forward-looking statements speak only as of the date hereof. Unless required by law, we undertake no obligation to update any forward-looking statements.

Overview

We are a fabless semiconductor provider of high-performance application-specific standard products. Our core strength of expertise is the development of complex Systems-on-a-Chip devices, leveraging our extensive technology portfolio of intellectual property in the areas of analog, mixed-signal, digital signal processing, and embedded and standalone integrated circuits. The majority of our product portfolio leverages the ARM technology portfolio. We also develop platforms that we define as integrated hardware along with software that incorporates digital computing technologies designed and configured to provide an optimized computing solution. Our broad product portfolio includes devices for data storage, enterprise-class Ethernet data switching, Ethernet physical-layer transceivers, mobile handsets, connectivity and other consumer electronics. Our products serve diverse applications used in carrier, metropolitan, enterprise and PC-client data communications and storage systems. Additionally, we serve the consumer electronics market for the convergence of voice, video and data applications. As a fabless integrated circuit company, we rely on independent, third party contractors to perform manufacturing, assembly and test functions. This approach allows us to focus on designing, developing and marketing our products and significantly reduces the amount of capital we need to invest in manufacturing products.

A significant number of our products are being incorporated into consumer electronics products, including gaming devices and personal computers, which are subject to significant seasonality and fluctuations in demand. Holiday and back-to-school buying trends may at times negatively impact our results in the first and fourth quarter and positively impact our results in the second and third quarter of our fiscal years. In addition, consumer electronics sales are heavily dependent on new product launch timelines and product refreshes. For example, our sales of wireless connectivity products may increase significantly during a period when one of our consumers launches a new gaming console, and these sales may taper significantly after the initial launch period.

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

Table of Contents

In this Quarterly Report on Form 10-Q, we refer to the fiscal year ended February 2, 2008 as fiscal 2008, the fiscal year ended January 30, 2010 as fiscal 2010, the fiscal year ended January 29, 2011 as fiscal 2011, the fiscal year ended January 28, 2012 as fiscal 2012, the fiscal year ended February 2, 2013 as fiscal 2013, the fiscal year ending February 1, 2014 as fiscal 2014 and the fiscal year ending January 31, 2015 as fiscal 2015.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. Actual results could differ from these estimates, and such differences could affect the results of operations reported in future periods. For a description of our critical accounting policies and estimates, please refer to the Critical Accounting Policies and Estimates section of our Management s Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended February 1, 2014.

Results of Operations

Net revenue for the three months ended August 2, 2014 was higher by approximately19% compared to the three months ended August 3, 2013, led by year over year growth in the mobile and wireless end markets, together with stable growth in the storage market. On a sequential basis, net revenue was essentially flat as revenue in the mobile and wireless end markets declined by approximately 9% as we experienced weaker than expected 3G demand from one of our major Asian smartphone OEM partners. We continue to see unit growth across our customer base in 4G LTE and in the coming months, we expect our customers to launch new smartphones powered by our LTE solutions. Overall, many of our customers have introduced new devices using our innovative solutions, which we believe will drive success across all of our end markets. Our future growth is expected to be driven by areas such as mobile handsets, tablets, connectivity, smart home devices and solid state drive (SSD) controllers.

In the mobile market, we continued to make steady progress with our LTE solutions. We have focused initially on the LTE market in China where we are seeing more OEM partners start new 4G LTE smart phone, tablet and mobile broadband device projects with our chipsets. We are now also expanding into multiple geographies and have recently seen good expansion of our 4G LTE products outside of China with a leading OEM launching our LTE solution in the European market. Samsung recently launched the new Galaxy Mini 4G smartphone and its multi-mode LTE mobile hotspot. We are on track to powering more multimode LTE devices from leading OEMs for deployment around the world later this year.

In the wireless connectivity market, we experienced growth in the gaming market where our wireless connectivity solutions are being used in new game consoles that were launched for the past holiday season. We expect wireless connectivity and other advanced features in these new game consoles to help drive growth for us this year in this industry. We are seeing new opportunities for our connectivity solutions across multiple market segments. We are also seeing increased momentum for both our 1x1 and our 2x2 combo solutions in mobile computing, dongles, set-top boxes and home automation. Our WiFi and Zigbee devices are gaining strong adoption in new IoT-type devices, home automation and smart lighting applications, and we expect volume to ramp up later this year. Our connectivity products have superior RF performance which helps accelerate customer on-boarding and reduce their time-to-market.

In the storage market, we continued to execute well as the overall industry appears to have stabilized. Our revenue has continued to grow within the SSD market and our strategy of partnering with top tier OEMs has resulted in excellent traction for our advanced SSD solutions. During the second quarter of fiscal 2015, we announced multiple new products that we believe enhanced and expanded our SSD offerings. They included our 5th generation SATA product with LDPC technology to support 3D NAND, as well as 15nm 2D NAND, and a low-cost PCIe-based SSD solution priced similar to our SATA solution but with much higher performance. Within the hard disk drive (HDD) market, we continue to experience strong demand for our 500 gigabyte per platter products. We have continued to see increased demand for our products used in enterprise drives at a top North America based HDD customer. In addition, we are continuing to accelerate our investment in next generation HDD technologies. We are also leveraging our technology leadership in HDD and SSD to help our customer migrate to hybrid storage devices by developing a single-chip solution that we believe will drive lower price points and allow the market to grow. We believe all of these efforts will allow us to further increase our share and solidify our leadership position in the market over the next few years.

In the networking market, revenue grew in the second quarter of fiscal 2015 as we saw growth from our Ethernet product lines across enterprise, datacenter and service provider networks, with the latter also driving growth in our PON product line. Design win momentum continued this quarter, with new programs that cover low-end fixed solutions to high-end modular platforms in the enterprise and service provider markets, driving new opportunities with our latest family of network processing solutions.

Table of Contents

Our cost of goods sold as a percentage of net revenue for the three months ended August 2, 2014 was higher compared to both the three months ended May 3, 2014 and August 3, 2013. As we expand our presence and grow revenue in the mobile and wireless end markets, we expect our gross margin to face downward pressure, as these end markets generally have lower average gross margins than the rest of our business. However, we expect this growth will result in improvement to total gross margin dollars and operating profit. In addition, we are focused on efforts to improve both aspects of our gross profit, including through cost improvement and pricing.

Our financial position is strong and we continue to generate significant positive cash flows. Our cash, cash equivalents and short-term investments were $2.3 billion at August 2, 2014 and we generated cash flow from operations of $392.1 million through the second quarter of fiscal 2015. We paid a cash dividend of $0.06 per share for a total of $30.8 million in the second quarter of fiscal 2015 and we recently announced a dividend of $0.06 per share to be paid during the third quarter of fiscal 2015.

We are currently involved in a patent litigation action with Carnegie Mellon University (CMU) (See Risk Factors under Part II, Item 1A of this Quarterly Report on Form 10-Q and Note 10 Commitments and Contingencies in the Notes to Unaudited Condensed Consolidated Financial Statements for a further discussion of the risks associated with this matter and other patent litigation matters). A jury has awarded past damages of $1.17 billion, and the Court calculated damages, including enhancement, to total approximately $1.54 billion, and held that, under its decision, CMU is entitled to post judgment interest and an ongoing royalty. Based on the royalty rate assessed by the District Court, such additional royalties through August 2, 2014 could be as much as $300 million. If we are required to further secure all or some additional portion of ongoing royalties, we may be required to post cash or other Company assets as collateral. On May 7, 2014, the District Court entered final judgment and on May 14, 2014, we filed a notice of appeal and posted a bond to stay execution of judgment pending the appeal. We filed our opening appeal brief on August 4, 2014. We strongly believe that we do not infringe on the methods described in the CMU patents and that our products use our own internally developed patented read channel technology.

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

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
Net revenue	100.0%	100.0%	100.0%	100.0%
Operating costs and expenses:				
Cost of goods sold	49.7	47.8	50.6	46.8
Research and development	30.7	36.3	30.7	37.1
Selling and marketing	3.5	4.8	3.8	5.1
General and administrative	3.3	3.4	3.3	3.4
Amortization and write-off of acquired intangible assets	0.3	1.3	0.5	1.4
Total operating costs and expenses	87.5	93.6	88.9	93.8
Operating income	12.5	6.4	11.1	6.2
Interest and other income, net	1.3	1.1	0.6	0.7
Income before income taxes	13.8	7.5	11.7	6.9
Benefit for income taxes	(0.6)	(0.2)	(0.7)	(0.6)
Net income	14.4%	7.7%	12.4%	7.5%

Three and six months ended August 2, 2014 and August 3, 2013

Net Revenue

	Three Months Ended	Six Months Ended

	August 2, 2014	August 3, 2013	% Change	August 2, 2014	August 3, 2013	% Change
	(in thousands, except percentage)					
Net revenue	$ 961,545	$ 807,056	19.1%	$ 1,919,375	$ 1,541,425	24.5%

Net revenue for the three and six months ended August 2, 2014 increased by $154.5 million and $378.0 million compared to the three and six months ended August 3, 2013. The increase was led by sales of our mobile and wireless products where we saw strong growth from multiple customers who have launched their 4G LTE smart phones based on our solutions. Sales of our 3G products in the three and six months ended August 2, 2014 were also higher compared to the three and six months ended August 3, 2013. In our storage market, we saw higher HDD revenue, which was mostly driven by continued growth for our 500 gigabyte per platter products and increased demand for our products used in enterprise drives at a top North America based HDD customer. In addition, revenue for SSD controllers increased significantly compared to the prior year. Our networking revenue increased during the quarter led by strong demand for enterprise switches and routers.

We currently expect overall net revenue for the three months ending November 1, 2014 to be in the range of $960 million to $1.0 billion. We expect revenue from our mobile and wireless end markets to increase modestly while sales from our storage and networking customers is anticipated to be flat to slightly up.

Historically, a relatively small number of customers have accounted for a significant portion of our net revenue. We had two end customers who each represented greater than 10% of our total net revenue for the three and six months ended August 2, 2014 and August 3, 2013. Net revenue from one of these two customers was 20% and 19% of total net revenue for the three and six months ended August 2, 2014, respectively, compared to 25% and 26% for the three and six months ended August 3, 2013, respectively. Net revenue from the other customer was 12% and 11% of total net revenue for the three and six months ended August 2, 2014, respectively, compared to 12% for each of the three and six months ended August 3, 2013. We also had net revenue from one distributor of 17% and 12% of total net revenue for the three and six months ended August 2, 2014. No distributors accounted for more than 10% of our net revenue for the three and six months ended August 3, 2013. We expect to continue to experience similar customer concentration in future periods.

Most of our sales are expected to continue to be made to customers located outside of the United States, primarily in Asia. Sales to customers located in Asia represented 97% and 96% of our net revenue for the three and six months ended August 2, 2014 compared to 95% and 94% of our net revenue for the three and six months ended August 3, 2013. Because many manufacturers and manufacturing subcontractors of our customers are located in Asia, we expect that most of our net revenue will continue to be represented by sales to our customers in that region.

Cost of Goods Sold

	Three Months Ended			Six Months Ended		
	August 2, 2014	August 3, 2013	% Change	August 2, 2014	August 3, 2013	% Change
	(in thousands, except percentage)					
Cost of goods sold	$ 477,741	$ 386,059	23.7%	$ 971,601	$ 721,497	34.7%
% of net revenue	49.7%	47.8%		50.6%	46.8%	

Cost of goods sold as a percentage of net revenue was higher for the three and six months ended August 2, 2014 compared to the three and six months ended August 3, 2013 due to a shift in the mix of our revenue towards our mobile and wireless products which have a higher average cost of goods sold as a percentage of revenue, in addition to increased royalty expense. We also had higher inventory write downs in the six months ended August 2, 2014. Our cost of goods sold as a percentage of net revenue may fluctuate in future periods due to, among other things, changes in the mix of products sold; the timing of production ramps of new products; increased pricing pressures from our customers and competitors, particularly in the consumer product markets that we are targeting; charges for obsolete or potentially excess inventory; changes in the costs charged by our foundry; assembly and test subcontractors; product warranty costs; changes in commodity prices such as gold; and the margin profiles of our new product introductions.

We currently expect cost of goods sold as a percentage of net revenue for the three months ending November 1, 2014 to be slightly higher compared to the three months ended August 2, 2014.

Share-Based Compensation Expense

	Three Months Ended		Six Months Ended	
	August 2, 2014	August 3, 2013	August 2, 2014	August 3, 2013
	(in thousands)			
Cost of goods sold	$ 1,733	$ 1,868	$ 4,032	$ 3,735
Research and development	24,276	28,982	44,644	52,261
Selling and marketing	2,617	3,648	5,545	7,040

General and administrative	6,394	6,593	10,768	11,568