NETLOGIC MICROSYSTEMS INC
Form 10-Q
August 09, 2006
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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 June 30, 2006

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: 000-50838

NETLOGIC MICROSYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**77-0455244**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1875 Charleston Rd.

Mountain View, CA 94043

(650) 961-6676

(Address and telephone number of principal executive offices)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large accelerated filer ¨	Accelerated filer x	Non-accelerated filer ¨

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at July 31, 2006
Common Stock, $0.01 par value per share	**20,306,390 shares**

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PART I: FINANCIAL INFORMATION

Item 1. ***Financial Statements***

NETLOGIC MICROSYSTEMS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS)

(UNAUDITED)

	June 30, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 76,021	$ 65,788
Accounts receivable, net	10,960	5,972
Inventory	11,144	8,822
Prepaid expenses and other current assets	1,616	832
Total current assets	99,741	81,414
Property and equipment, net	6,545	4,012
Goodwill	37,343	
Intangible asset, net	6,012	
Other assets	101	103
Total assets	$ 149,742	$ 85,529
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 8,484	$ 8,458
Accrued liabilities	8,405	7,434
Deferred revenue	135	
Capital lease and other obligations, current	1,362	360
Total current liabilities	18,386	16,252
Capital lease and other obligations, long-term	1,383	327
Other liabilities	291	294
Total liabilities	20,060	16,873
Stockholders equity:		
Common stock and additional paid-in capital	217,262	152,559
Notes receivable from stockholders	(24)	(44)
Deferred stock-based compensation	(484)	(1,114)
Accumulated other comprehensive income	59	
Accumulated deficit	(87,131)	(82,745)
Total stockholders equity	129,682	68,656
Total liabilities and stockholders equity	$ 149,742	$ 85,529

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

NETLOGIC MICROSYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(IN THOUSANDS, EXCEPT FOR PER SHARE AMOUNTS)

(UNAUDITED)

	Three months ended		**Six months ended**	
	June 30, 2006	**June 30, 2005**	**June 30, 2006**	**June 30, 2005**
Revenue	$ 25,831	$ 18,707	$ 49,155	$ 40,509
Cost of revenue	10,094	8,220	19,030	17,704
Gross profit	15,737	10,487	30,125	22,805
Operating expenses:				
Research and development	9,703	5,719	17,764	9,813
In-process research and development			10,700	
Selling, general and administrative	3,996	2,479	7,603	5,271
Total operating expenses	13,699	8,198	36,067	15,084
Income (loss) from operations	2,038	2,289	(5,942)	7,721
Interest and other income, net	923	248	1,604	407
Income (loss) before income taxes	2,961	2,537	(4,338)	8,128
Provision for income taxes	23	112	48	280
Net income (loss)	$ 2,938	$ 2,425	$ (4,386)	$ 7,848
Net income (loss) per share - Basic	$ 0.15	$ 0.14	$ (0.23)	$ 0.45
Net income (loss) per share - Diluted	$ 0.14	$ 0.13	$ (0.23)	$ 0.42
Shares used in calculation - Basic	19,923	17,619	19,393	17,564
Shares used in calculation - Diluted	21,508	18,773	19,393	18,661

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

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NETLOGIC MICROSYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN THOUSANDS)

(UNAUDITED)

	Six months ended June 30, 2006	Six months ended June 30, 2005
Cash flows from operating activities:		
Net income (loss)	$ (4,386)	$ 7,848
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	2,438	918
Non-cash interest expense		136
Stock-based compensation	5,591	1,143
Provision for allowance for doubtful accounts	45	(185)
Provision for inventory reserves	1,400	2,147
In-process research and development	10,700	
Changes in assets and liabilities, net of effect of NSE assets acquired:		
Accounts receivable	(5,033)	79
Inventory	(2,858)	488
Prepaid expenses and other assets	(580)	(1,006)
Accounts payable	26	(1,230)
Accrued liabilities	997	347
Deferred revenue	307	
Other long-term liabilities	(3)	119
Net cash provided by operating activities	8,644	10,804
Cash flows from investing activities:		
Purchase of property and equipment	(947)	(863)
Cash paid for acquisition	(1)	
Net cash used in investing activities	(948)	(863)
Cash flows from financing activities:		
Proceeds from issuance of common stock	3,327	859
Payments of software license and capital lease obligations	(800)	(1,558)
Repurchase of common stock		(8)
Proceeds from payment of notes receivable from stockholders	20	340
Net cash provided by (used in) financing activities	2,547	(367)
Effects of exchange rate on cash and cash equivalents	(10)	
Net increase in cash and cash equivalents	10,233	9,574
Cash and cash equivalents at the beginning of period	65,788	41,411
Cash and cash equivalents at the end of period	$ 76,021	$ 50,985
Supplemental disclosure of cash flow information:		

Cash paid for interest	$	$ 1
Supplemental disclosure of non-cash investing and financing activities:		
Software license obligations	$ 3,233	$ 1,089
Issuance of common stock in connection with the acquisition of Cypress NSE assets	$ 56,201	$

The accompanying notes are an integral part of these unaudited condensed financial statements.

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NetLogic Microsystems, Inc.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of NetLogic Microsystems, Inc. (we , us , our and the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America and with the instructions for Form 10-Q and Regulation S-X statements. Accordingly, they do not include all of the information and notes required for complete financial statements. In the opinion of management, all adjustments, consisting of only normal recurring items, considered necessary for a fair statement of the results of operations for the periods shown.

These unaudited financial statements should be read in conjunction with the audited financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2005. Operating results for the three and six-month period ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

Stock-Based Compensation Expense

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment, (SFAS 123(R)) which requires the measurement and recognition of compensation expense for all share-based payment awards, including employee stock options and employee stock purchases, based on estimated fair values. SFAS 123(R) supersedes the Company s previous accounting under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) for periods beginning in fiscal 2006. In March 2005, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 (SAB 107) relating to SFAS 123(R). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R). The Company adopted SFAS 123(R) using the modified prospective transition method, which requires the application of the accounting standard as of January 1, 2006, the first day of the Company s fiscal year 2006. The Company s Condensed Consolidated Financial Statements as of and for the three and six months ended June 30, 2006 reflect the adoption of SFAS 123(R).

Stock-based compensation expense recognized under SFAS 123(R) for the three and six months ended June 30, 2006 was $3.1 million and $5.6 million, respectively, related to employee stock options and employee stock purchase rights. Under the modified prospective transition method, the Company s Consolidated Financial Statements for prior periods need not be restated to reflect or include the effect of SFAS 123(R). Accordingly, there was no stock-based compensation expense related to employee stock options and employee stock purchase rights recognized in prior periods presented, other than stock-based compensation expense recognized and disclosed previously.

SFAS 123(R) requires companies to estimate the fair value of option and ESPP awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in the Company s Consolidated Statement of Operations. Prior to the adoption of SFAS 123(R), the Company accounted for stock-based awards using the intrinsic value method in accordance with APB 25 as allowed under Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (SFAS 123). Under the intrinsic value method, no stock-based compensation expense for options had been recognized in the Company s Consolidated Statement of Operations if the exercise price of the Company s stock options granted to employees and directors equaled the fair market value of the underlying stock at the date of grant.

Stock-based compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest. Stock-based compensation expense recognized in the Company s Unaudited Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2006 included compensation expense for share-based payment awards granted prior to, but not yet vested as of December 31, 2005 based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123 and compensation expense for the share-based payment awards granted subsequent to December 31, 2005 based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). The Company attributes the value of stock-based compensation to expense on a straight-line single option method for the awards granted subsequent to December 31, 2005, while the accelerated method is being used for awards granted on or prior to December 31, 2005. As stock-based compensation expense recognized in the Unaudited Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2006 is based on awards ultimately expected to vest, it has been reduced for estimated

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forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In the Company s pro forma information required under SFAS 123 for the periods prior to fiscal 2006, the Company accounted for forfeitures as they occurred.

The Company uses the Black-Scholes-Merton option-pricing model (Black-Scholes model) as its method of valuation for share-based awards granted beginning in fiscal 2006, the same model used for the Company s pro forma information required under SFAS 123. The Company s determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company s stock price as well as assumptions regarding a number of subjective variables. These variables include, but are not limited to, the Company s expected stock price volatility over the term of the awards as well as actual and projected employee stock option exercise behaviors.

Critical Accounting Policies and Estimates

The preparation of our unaudited condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base these estimates and assumptions on historical experience and evaluate them on an on-going basis to ensure they remain reasonable under current conditions. Actual results could differ from these estimates. There were no changes to our critical accounting policies and estimates except as noted below.

Stock-based Compensation: We estimate the fair value of stock options using the Black-Scholes-Merton valuation model (the Black-Scholes model), consistent with the provisions of SFAS 123(R), SAB 107 and our prior period pro forma disclosures of net income, including stock-based compensation (determined under a fair value method as prescribed by SFAS 123). Option-pricing model requires the input of highly subjective assumptions, including the option s expected life and the price volatility of the underlying stock. The expected stock price volatility assumption was determined using the historical volatility of the Company s common stock. Changes in the subjective assumptions required in the valuation models may significantly affect the estimated value of the awards, the related stock-based compensation expense and, consequently, our results of operations.

Revenue Recognition: We derive revenue mainly from product sales and, to a lesser extent, from engineering services. Revenue from product sales is recognized upon shipment (except for shipments to a distributor) when persuasive evidence of an arrangement exists, legal title and risk of ownership has transferred, the price is fixed or determinable, and collection of the resulting receivables is reasonably assured. Our sales agreements do not provide for any customer acceptance provisions or return rights. We have no obligation to provide any modification or customization, upgrades, enhancements, post-contract customer support, additional products or enhancements. Customers, other than the distributor discussed below, have no rights of return unless the product does not perform according to specifications. Provisions for warranty expenses are recorded when revenue is recognized.

From time to time we perform engineering services for third parties. Engineering service revenue is recognized as services are performed, agreed-upon milestones are achieved and customer acceptance, if required, is received from the customer.

As a consequence of the acquisition of NSE business assets from Cypress, we began selling our products to a distributor in February 2006. We offer price protection and limited stock rotation rights to the distributor. Given the uncertainties associated with the levels of returns and price protection and other credits potentially issuable to the distributor, revenues and costs relating to the distributor sales are deferred, on a gross basis, until such rights lapse, which is generally upon receiving notification from the distributor that it has resold the products to our end customer.

2. Basic and Diluted Net Income (Loss) Per Share

We compute net income (loss) per share in accordance with SFAS 128, Earnings per Share . Basic net income (loss) per share is computed by dividing net income attributable to common stockholders (numerator) by the weighted average number of common shares outstanding (denominator) during the period. Diluted net income per share gives effect to all dilutive potential common shares outstanding during the period including stock options and warrants using the treasury stock method.

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The following is a reconciliation of the weighted average common shares used to calculate basic net income (loss) per share to the weighted average common and potential common shares used to calculate diluted net income (loss) per share for the three and six months ended June 30, 2006 and 2005 (in thousands, except per share data):

	Three months ended		Six months ended	
	June 30,		June 30,	
	2006	2005	2006	2005
Numerator:				
Net income (loss)	$ 2,938	$		