



PHOENIX TECHNOLOGIES LTD.

FORM 10-Q

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PHOENIX TECHNOLOGIES LTD.  
CONDENSED CONSOLIDATED BALANCE SHEETS

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(in thousands, except per share amounts)

		December 31, 2000
Assets		----- (unaudited)
Current Assets:		
Cash and cash equivalents	\$	58,883
Short-term investments		35,126
Accounts receivable, net of allowance of \$931 at December 31, 2000 and \$790 at September 30, 2000		37,172
Deferred income taxes		3,926
Other current assets		5,738
		-----
Total current assets		140,845
Investments		4,973
Property and equipment, net		12,871
Computer software cost, net		6,967
Goodwill and other intangible assets, net		18,713
Other assets		11,894
		-----
Total assets	\$	196,263 =====
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable	\$	3,867
Accrued compensation and related liabilities		8,835
Deferred revenue		4,771
Other accrued liabilities		5,882
Income taxes payable		5,037
		-----
Total current liabilities		28,392
Long-term obligations		1,368
Long-term deferred tax liabilities		4,181
		-----
Total liabilities		33,941
Minority Interest		15,889
Stockholders' equity:		
Preferred stock, \$.10 par value, 500 shares authorized, none issued or outstanding		--
Common stock, \$.001 par value, 60,000 shares authorized, 24,863 and 25,608 issued and outstanding at December 31, 2000 and September 30, 2000		25
Additional paid-in capital		163,019
Retained earnings		59,401
Accumulated other comprehensive loss		(1,347)
Less: Cost of treasury stock (4,405 shares at December 31, 2000 and 3,377 shares at September 30, 2000)		(74,665)
		-----
Total shareholders' equity		146,433
		-----
Total liabilities and shareholders' equity	\$	196,263 =====

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SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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PHOENIX TECHNOLOGIES LTD.  
 CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
 (in thousands, except per share amounts)  
 (unaudited)

	Three months ended December 31,	
	2000	
Revenue:		
License fees	\$ 33,877	\$ 2
Services	4,898	
Total revenue	38,775	3
Cost of revenue:		
License fees	417	
Services	3,633	
Amortization of purchased technology	314	
Total cost of revenue	4,364	
Gross margin	34,411	2
Operating expenses:		
Research and development	10,934	1
Sales and marketing	9,763	
General and administrative	5,490	
Amortization of goodwill and acquired intangible assets	555	
Stock-based compensation	444	
Total operating expenses	27,186	2
Income from operations	7,225	
Interest and other income, net	590	
Minority interest	108	
Income before income taxes	7,923	
Provision for income taxes	2,412	
Net income	\$ 5,511	\$
Earnings per share:		
Basic	\$ 0.22	\$
Diluted	\$ 0.21	\$

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Weighted average number of shares used in computations:

Basic	25,096	2
Diluted	26,636	2

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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PHOENIX TECHNOLOGIES LTD.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands)  
(unaudited)

	Three months December
	2000
Cash flows from operating activities:	
Net income	\$ 5,511
Reconciliation to net cash provided by operating activities:	
Depreciation and amortization	2,103
Minority interest	(108)
Deferred income tax	316
Change in operating assets and liabilities:	
Accounts receivable	2,696
Other assets	(1,451)
Accounts payable	(78)
Accrued compensation and related liabilities	(1,719)
Other accrued liabilities	(1,068)
Income taxes payable	(217)
Net cash provided by operating activities	5,985
Cash flows from investing activities:	
Proceeds from sales of investments	109,740
Purchases of investments	(92,665)
Purchases of property and equipment	(1,008)
Additions to computer software costs	(1,898)
Acquisition of Xentec, Inc., net of cash acquired	(2,933)
Net cash provided by investing activities	11,236
Cash flows from financing activities:	
Proceeds from common stock issuance under stock option and stock purchase plans	3,554
Repurchases of common stock	(15,895)
Repayment of notes payable	(47)

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Net cash used in financing activities	(12,388)
Effect of exchange rate changes on cash and cash equivalents	(967)
Net increase in cash and cash equivalents	3,866
Cash and cash equivalents at beginning of period	55,017
Cash and cash equivalents at end of period	\$ 58,883

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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PHOENIX TECHNOLOGIES LTD.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1. DESCRIPTION OF BUSINESS

Phoenix Technologies Ltd. (together with its subsidiaries, "Phoenix" or the "Company") is a global leader in system-enabling software solutions for PCs and connected digital devices. Its software provides compatibility, connectivity, security and manageability of the various components and technologies used in such devices. Phoenix provides these products primarily to platform and peripheral manufacturers (collectively, "OEMs") that range from large PC manufacturers to small system integrators. Phoenix also provides training, consulting, maintenance and engineering services to its customers. It markets and licenses its products and services primarily through a direct sales force, as well as through regional distributors and sales representatives. The Company has three business units (one of which, inSilicon Corporation ("inSilicon"), is a majority-owned subsidiary), each of which delivers leading products and professional services that enable connected computing.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements as of December 31, 2000 and for the three months ended December 31, 2000 and 1999 have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). All intercompany accounts and transactions have been eliminated. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The consolidated balance sheet as of September 30, 2000 was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2000.

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In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary to summarize fairly the Company's financial position, results of operations and cash flows for the interim periods presented. The operating results for the three months period ended December 31, 2000 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2001, or for any other future period.

### EARNINGS PER SHARE

Basic earnings per share is computed using the weighted-average number of common shares outstanding during each period. Diluted earnings per share is computed using the weighted-average number of common and dilutive common-equivalent shares outstanding during the period. Dilutive common-equivalent shares primarily consist of employee stock options, computed using the treasury stock method.

### RECLASSIFICATIONS

Certain prior year amounts have been reclassified to conform to the current year presentation.

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PHOENIX TECHNOLOGIES LTD.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(UNAUDITED)

### NEW ACCOUNTING PRONOUNCEMENTS

In the first quarter of fiscal year 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended by Statement of Financial Accounting Standards No. 138, (the Statements) which establish accounting and reporting standards for derivative instruments and for hedging activities. The Statements require that an entity recognize all derivatives as either assets or liabilities on the balance sheet and measure those instruments at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. The Company does not hold any derivative financial instrument and does not engage in hedging activities. Accordingly, the adoption of the Statements does not have a material impact on the Company's financial position, results of operations or cash flows.

### NOTE 3 PURCHASE COMBINATIONS

In December 2000, inSilicon Corporation ("inSilicon"), a majority owned subsidiary of the Company acquired Xentec, Inc. and HD Lab, K.K. for a total purchase price of \$12.6 million, paid in inSilicon common stock and cash.

The condensed consolidated financial statements include the operating results of each business from the date of acquisition. Pro forma results of operations have not been presented because the effects of these acquisitions were not material on either an individual or an aggregate basis.

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### NOTE 4. EARNINGS PER SHARE

The following table presents the calculations of basic and diluted earnings per share under Statement of Financial Accounting Standards No. 128 ("SFAS 128"), "Earnings per Share" (in thousands, except per share amounts):

	Three Months Ended December 31,	
	2000	1999
Net income	\$ 5,511	\$ 2,749
Weighted average common shares outstanding	25,096	24,128
Effect of dilutive securities (using the treasury stock method):		
Stock options	1,366	2,002
Warrants	174	202
Total dilutive securities	1,540	2,204
Weighted average diluted common and equivalent shares outstanding	26,636	26,332
Earnings per share:		
Basic	\$ 0.22	\$ 0.11
Diluted	\$ 0.21	\$ 0.10

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PHOENIX TECHNOLOGIES LTD.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(UNAUDITED)

### NOTE 5. COMPREHENSIVE INCOME

Following are the components of comprehensive income (in thousands):

Three Months Ended December 31,	
2000	1999



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Net income	\$ 5,511	\$
Change in accumulated translation and foreign currency adjustments	(967)	
Comprehensive income	\$ 4,544	\$

NOTE 6. SEGMENT REPORTING

Segment information is presented in accordance with Statement of Financial Account Standards No. 131 ("SFAS 131"), "Disclosures about Segments of an Enterprise and Related Information." This standard requires segmentation based upon the Company's internal organization and disclosure of revenue and operating income based upon internal accounting methods. The Company has three reportable segments: Platform Enabling, inSilicon and PhoenixNet-TM-.

PLATFORM ENABLING: Provides system-enabling software that is used in the design, deployment and ongoing operation of PCs, internet appliances, embedded systems, and other connected digital devices. The Platform Enabling's flagship software products provide support for current technologies and industry standards, allowing systems and device manufacturers to base new product designs on a range of microprocessors, chipsets and operating systems combinations.

INSILICON: Provides communications technology that is used by semiconductor and systems companies to design complex semiconductors called systems-on-a-chip that are critical components of digital devices. inSilicon provides cores, related silicon subsystems and firmware to customers that use its technologies in hundreds of different digital devices ranging from network routers to cellular phones.

PHOENIXNET-TM-: Provides worldwide PC users with a solution to configure their web browsers and desktops, directs users to web destinations, offers software download tools through a graphical launch screen, and provides the licensing of machine profile data.

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PHOENIX TECHNOLOGIES LTD.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(UNAUDITED)

The Company evaluates operating segment performance based on revenue and operating income (in thousands):

	Three Months Ended December 31,	
	2000	1999
Revenue:		
Platform Enabling	\$32,858	\$27,114

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inSilicon	5,055	5,257
PhoenixNet	862	--
	-----	-----
Total	\$38,775	\$ 32,371
	=====	=====

	Three Months Ended December 31,	
	2000	1999
	-----	-----
Income (loss) from operations before restructuring charges:		
Platform Enabling	\$11,023	\$7,640
inSilicon	(937)	(1,058)
PhoenixNet	(2,861)	(3,077)
	-----	-----
Total	\$ 7,225	\$ 3,505
	=====	=====

The Company also reports revenue by geographic area, which is categorized into three regions: North America, Asia and Europe (in thousands):

	Three Months Ended December 31,	
	2000	1999
	-----	-----
Revenue:		
North America	\$10,381	\$ 7,616
Asia	26,626	22,108
Europe	1,768	2,647
	-----	-----
Total	\$38,775	\$32,371
	=====	=====

NOTE 7. STOCK REPURCHASE PROGRAM

In fiscal 2000, the Board of Directors authorized a program to utilize approximately \$30 million of the Company's cash to repurchase outstanding shares of its common stock over a 24-month period. Under this program, the Company repurchased approximately 1,011,000 shares during fiscal 2000 at a cost of \$16.6 million. The Company has repurchased an additional 1,028,400 shares during the three months ended December 31, 2000 at a cost of \$15.9 million. As of December 31, 2000, the fiscal 2000 repurchase program was completed and terminated.

NOTE 8. SUBSEQUENT EVENT

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In February 2001, the Board of Directors authorized a program to repurchase up to \$30 million of outstanding shares of common stock over a 12-month period.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Report on Form 10-Q, including without limitation the Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21 (E) of the Securities Exchange Act 1934, as amended. These statements include, but are not limited to, statements concerning increases in research and development activities, future liquidity and financing requirements, expected price erosion, plans to make acquisitions, dispositions or strategic investments, expectation of increased sales to original equipment manufacturers, and plans to improve and enhance existing products and develop new products.

These forward-looking statements of the Company are subject to risks and uncertainties. Some of the factors that could cause future results to materially differ from the recent results or those projected in the forward-looking statements include, but are not limited to, significant increases or decreases in demand for Phoenix's products, increased competition, lower prices and margins, failure to successfully develop and market new product and technologies, competitor introductions of superior products, continued industry consolidation, instability and currency fluctuations in international markets, product defects, failure to secure intellectual property rights, results of litigation, and failure to retain and recruit key employees. For a more detailed discussion of certain risks associated with the Company's business, see the "Business Risks" section of the Company's Annual Report on Form 10-K for the year ended September 30, 2000.

#### COMPANY OVERVIEW

Phoenix Technologies Ltd. (together with its subsidiaries, "Phoenix" or the "Company") is a global leader in system-enabling software solutions for PCs and connected digital devices. Its software provides compatibility, connectivity, security and manageability of the various components and technologies used in such devices. Phoenix provides these products primarily to platform and peripheral manufacturers (collectively, "OEMs") that range from large PC manufacturers to small system integrators. Phoenix also provides training, consulting, maintenance and engineering services to its customers. It markets and licenses its products and services primarily through a direct sales force, as well as through regional distributors and sales representatives. The Company has three business units (one of which, inSilicon Corporation ("inSilicon"), is a majority-owned subsidiary), each of which delivers leading products and professional services that enable connected computing.

The Company's operations include the following:

**PLATFORM ENABLING:** Provides system-enabling software that is used in the design, deployment and ongoing operation of PCs, internet appliances, embedded systems, and other connected digital devices. The Platform Enabling's flagship software products provide support for current technologies and industry standards, allowing systems and device manufacturers to base new product designs on a range of microprocessors, chipsets and operating systems combinations.

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INSILICON: Provides communications technology that is used by semiconductor and systems companies to design complex semiconductors called systems-on-a-chip that are critical components of digital devices. inSilicon provides cores, related silicon subsystems and firmware to customers that use its technologies in hundreds of different digital devices ranging from network routers to cellular phones.

PHOENIXNET-TM-: Provides worldwide PC users with a solution to configure their web browsers and desktops, directs users to web destinations, offers software download tools through a graphical launch screen, and provides the licensing of machine profile data.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### REVENUE

The Company's products are generally designed into personal computer systems, information appliances and semiconductors. License fee and service revenue by segment for the three month periods ended December 31, 2000 and 1999, were as follows (dollars in thousands):

Three months ended December 31:	Amount			% of Conso Reve
	2000	1999	% CHANGE	2000
Platform Enabling	\$32,858	\$27,114	21.2%	84.7%
inSilicon	5,055	5,257	-3.8%	13.1%
PhoenixNet	862	--	N/A	2.2%
Total revenue	\$38,775	\$32,371	19.8%	100%

The increase in Platform Enabling revenue in the first quarter of fiscal 2001 of 21.2% over the comparable period of fiscal 2000 was primarily due to increased sales of system enabling software used primarily in personal computers. inSilicon revenue, net of intercompany transactions, declined due largely to a decrease in non-recurring engineering work for a significant customer. PhoenixNet first generated revenues in the second quarter of fiscal 2000.

Revenue by geographic region for the quarter ended December 31, 2000 and 1999, was as follows (dollars in thousands):

% of Conso

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Three months ended December 31:	Amount			Reve
	2000	1999	% CHANGE	2000
North America	\$10,381	\$7,616	36.3%	26.8%
Asia	26,626	22,108	20.4%	68.7%
Europe	1,768	2,647	-33.2%	4.5%
Total revenue	\$38,775	\$32,371	19.8%	100%

During the three months ended December 31, 2000, North American and Asian revenue increased while European revenue declined. This was due primarily to the outsourcing of system design and manufacturing to Asian personal computer and motherboard manufacturers, growth in Japanese personal computer shipments in the Platform enabling segment and a shift in revenue from the European market to the Asian market.

One customer accounted for 20% of total revenue during the three-month period ended December 31, 2000. One customer accounted for more than 11% of revenue during the three-month period ended December 31, 1999.

GROSS MARGIN

Gross margin as a percentage of revenue for the three-month period ended December 31, 2000 increased to 88.7% from 82.0% in the comparable period of fiscal 2000. Included in the costs of revenue was \$0.3 million of amortization of purchased technology arising from the acquisition of Sand Microelectronics, Inc. for both three-month periods ended December 31, 2000 and 1999. Also included in the costs of revenue in the quarter ended December 31, 1999 was \$0.6 million of non-recurring Year 2000 ("Y2K") support cost. Gross margin as a percentage of revenue before the amortization of purchased technology and Y2K support costs was 89.6% and 84.8% for the three months ended December 31, 2000 and 1999, respectively. The increase in gross margin was due primarily to shifts in license revenue mix.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses for the three-month period ended December 31, 2000 increased by \$0.4 million over the prior year quarter, but as a percentage of revenue fell to 28.2% from

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

32.4%. The percentage decrease was primarily due to improvement in product and resource management resulting in lower headcount and the relocation of research and development centers to Asia and Japan where costs are lower.

SALES AND MARKETING EXPENSES

Sales and marketing expenses for the three-month period ended December 31, 2000 increased by \$2.8 million from the comparable period in fiscal 2000. As a percentage of revenue, sales and marketing expenses

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increased from 21.5% in the three-month period ended December 31, 1999 to 25.2% in the current quarter. The increase in sales and marketing expense was principally due to an increase in the size of the Company's direct sales force and related commissions and the expansion of our distribution channels to position the Company for growth in markets beyond the PC market. Management has made a conscious effort to increase sales and marketing efforts through the reallocation of resources.

### GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses for the three-month period ended December 31, 2000, increased by \$0.8 million from the comparable period in fiscal 2000. As a percentage of revenue, general and administrative expenses decreased from 14.5% to 14.2% in the three-month period ended December 31, 2000 compared to the quarter ended December 31, 1999. The slight percentage decrease was due to efficiency improvement in infrastructure costs.

### AMORTIZATION OF GOODWILL AND ACQUIRED INTANGIBLE ASSETS

Amortization of goodwill and acquired intangible assets included in operating expense was \$0.6 million for both the first quarters of fiscal 2001 and 2000. Amortization of goodwill and acquired intangible asset relates primarily to the acquisition of Sand Microelectronics, Inc. in September 1998.

### STOCK-BASED COMPENSATION

The stock-based compensation charges in both quarters presented were mostly due to the granting of options to purchase inSilicon stock at exercise prices less than the fair market value of inSilicon common stock on the grant date.

### INTEREST AND OTHER INCOME, NET

Interest and other income, net, for the three month period ended December 31, 2000 increased 10.3% from the comparable period in fiscal 2000 primarily due to improved interest income related to higher cash balances as a result of the proceeds inSilicon received from the initial public offering of inSilicon stock in the second quarter of fiscal 2000, offset by foreign currency exchange losses.

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### PROVISION FOR INCOME TAXES

The Company recorded an income tax provision of \$2.4 million for three-month period ended December 31, 2000, as compared to \$1.3 million in the comparable period in fiscal 2000. The provisions for income taxes reflect effective tax rates of 30.9% and 32.0%, respectively. The decrease in the effective tax rate is immaterial. For federal income tax purposes, the Company does not file a consolidated return with inSilicon as the Company owns less than 80% of the voting stock issued and outstanding as of December 31, 2000.

### LIQUIDITY AND CAPITAL RESOURCES

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At December 31, 2000, the Company' principal source of liquidity consisted of cash and cash equivalents, and short-term investments totaling \$94 million. Cash and cash equivalents of \$58.9 million as of December 31, 2000 included \$12.4 million restricted and owned by inSilicon. The primary sources of cash during the first three months of fiscal 2001 were \$6.0 million from operating activities, net sales of short-term investments of \$17.1 million and proceeds from issuance of stock under various stock plans of \$3.6 million. The primary uses of cash during the first three months of fiscal 2001 were \$15.9 million for the repurchase of common stock, \$2.9 million for the purchase of property, equipment and computer software and \$2.9 million for the acquisition of Xentec, Inc.

The Company believes that current cash, short-term investment balances and cash flow from operations will be sufficient to meet its operating and capital requirements on a short-term and long-term basis.

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### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For financial market risks related to changes in interest rate, foreign currency exchange rates, and investment, refer to Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in the Company's Annual Report on Form 10-K for the year ended September 30, 2000.

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## PART II. OTHER INFORMATION

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

- (a) None
- (b) Reports on Form 8-K.  
The Company filed no reports on Form 8-K during the quarter ended December 31, 2000.

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SIGNATURE

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Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

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PHOENIX TECHNOLOGIES LTD.

Date: February 14, 2001

By: /s/ JOHN M. GREELEY

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John M. Greeley  
Senior Vice President  
and Chief Financial Officer

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