GENESIS MICROCHIP INC
Form 10-Q
February 14, 2001

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 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 DECEMBER 31, 2000

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:
000-29592

GENESIS MICROCHIP INCORPORATED
(Exact name of registrant as specified in its charter)

NOVA SCOTIA, CANADA (State or other jurisdiction of incorporation or organization)	N/A (I.R.S. Employer Identification No.)
165 COMMERCE VALLEY DRIVE WEST THORNHILL, ONTARIO, CANADA (Address of principal executive offices)	L3T 7V8 (Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (905) 889-5400

Former name, former address and former fiscal year if changed since last report.

Former address: N/A

Former Fiscal Year: N/A

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 [_]

There were 19,405,892 shares of the registrant's common shares issued and outstanding as of December 31, 2000.

GENESIS MICROCHIP INCORPORATED
FORM 10-Q
THREE MONTHS ENDED DECEMBER 31, 2000

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Signature

* No information has been provided because this item is not applicable.

PART I: FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

GENESIS MICROCHIP INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS
(dollar amounts in thousands of U.S. dollars)

ASSETS

	December 31, 2000 (unaudited)	March 200

Current assets:		
Cash and cash equivalents	$ 38,733	$42,
Accounts receivable trade, net of allowance for doubtful accounts of $230 at December 31, 2000 and March 31, 2000	11,747	6,
Income taxes recoverable	1,659	1,
Inventory	13,487	4,
Investment held for resale	1,100	1,
Other	3,410	
Total current assets	70,136	56,
Capital assets	10,305	12,
Deferred income taxes	3,429	3,
Investment, at cost	100	
Total assets	$ 83,970	$71,

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Accounts payable	$8,337	$1
Accrued liabilities	2,598	3
Current portion of loans payable	92	
Total current liabilities	11,027	6
Long-term liabilities:		
Loans payable	418	
Total liabilities	11,445	6
Shareholders' equity:		
Special shares:		
Authorized - 1,000,000,000 shares without par value		
Issued and outstanding - no shares at December 31 or March 31 Common shares:		
Authorized - 1,000,000,000 shares without par value		
Issued and outstanding - 19,405,892 shares at December 31, 2000 and 19,140,482 shares at March 31, 2000	73,929	72
Additional paid in capital	1,293	1
Cumulative other comprehensive loss	(94)	
Deferred compensation	(207)	(
Deficit	(2,396)	(7,
Total shareholders' equity	72,525	65
Total liabilities and shareholders' equity	$ 83,970	$ 71

See accompanying notes to condensed consolidated financial statements.

GENESIS MICROCHIP INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(dollar amounts in thousands of U.S. dollars, except per share amounts)
(unaudited)

	Three Months Ended		Nine Month
	December 31, 2000	December 31, 1999	December 31, 2000
Revenues	$17,304	$10,059	$45,156
Cost of revenues	7,697	3,263	17,654
Gross profit	9,607	6,796	27,502
Operating expenses:			
Research and development	4,792	4,351	13,257
Selling, general and administrative	3,833	2,991	10,575
Merger-related costs	-	-	-
Total operating expenses	8,625	7,342	23,832
Income (loss) from operations	982	(546)	3,670
Interest and other income	642	550	1,895
Income before income taxes	1,624	4	5,565
Provision for (recovery of) income taxes	(354)	(196)	57
Net income	$ 1,978	$ 200	$ 5,508
Earnings per share:			
Basic	$ 0.10	$ 0.01	$ 0.29
Diluted	$ 0.10	$ 0.01	$ 0.28
Weighted average number of common shares outstanding (in thousands):			
Basic	19,378	18,923	19,293
Diluted	19,860	19,807	19,869

See accompanying notes to condensed consolidated financial statements.

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GENESIS MICROCHIP INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollar amounts in thousands of U.S. dollars)
(unaudited)

	Nine Months End	
	December 31, 2000	Dec 31,
Cash flows from operating activities:		
Net income	$ 5,508	$
Adjustments to reconcile net income to cash used in operating activities:		
Amortization	2,750	
Loss on sale of capital assets	106	

Stock compensation expense	66	
Gain on sale of investment	(100)	
Inventory provision	(306)	
Deferred income taxes	(405)	(
Change in operating assets and liabilities:		
Accounts receivable trade	(5,724)	
Income taxes recoverable	(548)	
Inventory	(8,467)	
Other current assets	(2,613)	
Accounts payable	6,374	
Accrued liabilities	(1,369)	(
Net cash (used in) from operating activities	(4,728)	1
Cash flows from investing activities:		
Additions to capital assets	(1,161)	(
Other	80	(
Cash used in investing activities	(1,081)	(
Cash flows from financing activities:		
Proceeds from issue of common shares, net of issue costs	1,704	
Repayment of bank indebtedness - net	-	
Repayment of loans payable	(90)	(
Net cash from financing activities	1,614	
Effect of currency translation on cash balances	(14)	
(Decrease) increase in cash and cash equivalents	(4,209)	
Cash and cash equivalents, beginning of period	42,942	3
Cash and cash equivalents, end of period	$38,733	$4

See accompanying notes to condensed consolidated financial statements.

GENESIS MICROCHIP INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of presentation

We have prepared the accompanying unaudited condensed consolidated financial statements in accordance with United States generally accepted accounting principles and according to the rules and regulations of the Securities and Exchange Commission for interim financial reporting. Consequently, they do not include all of the information and footnotes required by United States generally accepted accounting principles for complete financial statements. These condensed financial statements should be read in conjunction with our financial statements and notes thereto for the year ended March 31, 2000 that are included in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission. We believe that the accompanying financial statements reflect all adjustments, consisting solely of normal, recurring adjustments, that are necessary for fair presentation of the results for the interim periods presented. The results of operations for the period ended December 31, 2000 are not necessarily indicative of the results to be expected for the full fiscal year.

2. Earnings per share

Basic earnings per share are computed by dividing the net income in a period by the weighted average number of common shares outstanding during that period. Diluted earnings per share are calculated in order to give effect to all potential common shares issuable during the period. The weighted average number of diluted shares outstanding is calculated by assuming that any proceeds from potential common shares, such as stock options, are used to repurchase common shares at the average share price in the period.

Per share information calculated on this basis is as follows (in thousands, except per share amounts):

	Three Months Ended		D
	December 31, 2000	December 31, 1999	
Numerator:			
Net income	$ 1,978	$ 200	
Denominator for basic earnings per share-			
Weighted average common shares outstanding	19,378	18,923	
Basic earnings per share	$ 0.10	$ 0.01	
Denominator for diluted earnings per share-			
Weighted average common shares outstanding	19,378	18,923	
Stock options and warrants	482	884	
Shares used in computing diluted earnings per share	19,860	19,807	
Diluted earnings per share	$ 0.10	$ 0.01	

3. Segmented information

We operate and track our results in one operating segment. We design, develop and market integrated circuits that manipulate and process digital images.

Revenues from our unaffiliated customers by geographic region were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	December 31, 2000	December 31, 1999	December 31, 2000	December 1999
United States	$ 2,393	$ 2,663	$ 7,583	$

Japan and Asia	12,728	7,001	33,303	3
Canada	1,794	95	2,506	
Rest of World	389	300	1,764	
	$17,304	$10,059	$45,156	$4

Net long-lived assets by country of location were as follows (in thousands):

	December 31, 2000	March 20
United States	$ 4,540	$
Canada	5,765	
	$10,305	$1

The following table shows the percentage of our revenue in each period that was derived from customers who individually accounted for more than 10% of revenue in that period:

	Three Months Ended		Nine Months Ende	
	December 31, 2000	December 31, 1999	December 31, 2000	Dece 31, 19
Customer A	11%	15%	-	
Customer B	-	12%	-	

At December 31, 2000 one customer accounted for 14% of accounts receivable trade. At March 31, 2000, two customers represented 16% and 10% of accounts receivable trade, respectively.

4. Recent accounting pronouncements

In June 1998, the Financial Accounting Standards Board issued Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," or SFAS 133. SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS 133 requires an entity to recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. The impact of adopting SFAS 133, which is effective for all fiscal quarters of fiscal years beginning after June 15, 2000 is not expected to be material to Genesis' operations.

In December 1999, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 101 (SAB 101), Revenue Recognition in Financial Statements, as amended by SAB 101A, which provides guidance on the recognition, presentation, and disclosure of revenue in financial statements filed with the SEC. SAB 101 outlines the basic criteria that must be met to recognize revenue and provides guidance for disclosures related to revenue recognition policies. The Company does not expect the adoption of SAB 101 to have a material effect on its consolidated financial position or results of operations. The Company is

required to adopt SAB 101 in the fourth quarter of fiscal 2001.

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

This Quarterly Report on Form 10-Q contains numerous statements of a forward-looking nature relating to potential future events or to our future financial performance. Our actual future results may differ significantly from those forward-looking statements. You should consider the various factors identified under the caption "Factors that may affect future operating results" in evaluating those statements.

Overview

We design, develop and market integrated circuits, or chips, that process digital video and graphic images. Our chips translate source video, graphics and digital images in order to be able to show them on various display systems such as flat panel computer monitors or digital televisions. We do not manufacture our chips. We procure them from third party manufacturers, such as IBM Corporation, Taiwan Semiconductor Manufacturing Corporation, United Semiconductor Corporation, and Samsung Semiconductor, Inc.

Applications for our products include:

- flat panel computer monitors,
- digital CRT computer monitors,
- consumer electronics applications, such as digital television and DVD, . digital projection systems, and
- advanced image processing applications such as video editing, medical and security systems.

Results of operations

The following table shows unaudited statement of operations data for the three month and nine month periods ended December 31, 2000 and December 31, 1999, expressed as a percentage of revenues:

	Three Months Ended		Nine Months End	
	December 31, 2000	December 31, 1999	December 31, 2000	Decemb 19
Revenues	100.0%	100.0%	100.0%	
Cost of revenues	44.5	32.4	39.1	
Gross profit	55.5	67.6	60.9	
Operating expenses:				
Research and development	27.7	43.3	29.4	
Selling, general and administrative	22.1	29.7	23.4	
Merger-related costs	-	-	-	
Total operating expenses	49.8	73.0	52.8	
Income from operations	5.7	(5.4)	8.1	
Interest and other income	3.7	5.5	4.2	
Income before income taxes	9.4	0.1	12.3	

Provision for (recovery of) income taxes	(2.0)	(1.9)	0.1
Net income	11.4%	2.0%	12.2%

Revenues: Revenues for the three months ended December 31, 2000 increased to $17.3 from $10.1 million in the three months ended December 31, 1999, an increase of 72.0%. This resulted from an increase in units shipped offset in part by a decline in average selling prices. The company expects that its revenues in calendar 2001 will continue to be dominated by shipments of product into the flat-panel monitor market. Consequently, it expects its revenues for calendar 2001 to grow substantially as this market continues to experience rapid growth. For the March 2001 quarter, the company is targeting its revenues to grow about $1 million over the December 2000 quarter. This reflects a more conservative approach to the quarter than previously anticipated as a result of current macroeconomic conditions. For the balance of calendar 2001, the company is targeting solid double-digit sequential percentage revenue growth per quarter, with overall revenues in calendar 2001 targeted to increase in excess of 60% over calendar 2000 actual revenues of $55.8 million.

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Gross Profit. Gross profit for the three months ended December 31, 2000 increased to $9.6 million from $6.8 million in the three months ended December 31, 1999. As a percentage of revenues, gross profit represented 55.5% of revenues in the three months ended December 31, 2000, down from 67.6% of revenues in the three months ended December 31, 1999. The decrease in gross profit percentage in 2000 over 1999 was primarily attributable to a different mix of products sold, with the newer products generally having lower average gross margins, and as a result of our pricing strategy for further increasing our share of the flat panel computer monitor market. The company continues to target its gross margins to average about 50% for calendar 2001.

Research and Development. Research and development expenses include costs associated with research and development personnel, development tools and prototyping costs. Research and development expenses for the three months ended December 31, 2000 increased to $4.8 million from $4.4 million in the three months ended December 31, 1999. These expenses represented 27.7% of revenues in the 2000 period and 43.3% of revenues in the 1999 period.

The dollar increase in the 2000 period over the comparative period in 1999 reflects increased prototype and pre-production expenses for new products brought forward ahead of plan. We expect to continue to make substantial investments in our research and development activities and anticipate that the dollar amount of research and development expenses will continue to increase in the longer term, although we do expect to see a decrease in the March quarter, due to the aforementioned timing of pre-production expenses for new products . The decrease in research and development expenses as a percentage of revenues is a result of the increase in revenues from the previous period.

Selling, General and Administrative. Selling, general and administrative expenses consist of personnel and related overhead costs for selling, marketing, customer support, finance, human resources and general management functions and of commissions paid to regional sales representatives. Selling, general and administrative expenses were $3.8 million in the three months ended December 31, 2000 and $3.0 million in the three months ended December 31, 1999. These expenses represented 22.1% of revenues in the 2000 period and 29.7% of revenues in the 1999 period.

The dollar increase in 2000 from 1999 in selling, general and administrative

expenses reflects increased personnel costs related to increased administrative, marketing, selling and customer support personnel, continued expansion of our international operations, and an increase in the number of demonstration boards built as part of our marketing strategy for new product introduction. The decrease in selling, general and administrative expenses as a percentage of revenues results from the increase in revenues from the previous period.

Total Operating Expenses. Total operating expenses for the three months ended December 31, 2000 increased to $8.6 million from $7.3 million in the three months ended December 31, 1999, for the reasons described above. The company is targeting total operating expenses in the March quarter to decrease from the December quarter by 7-9%, as a result of its having accelerated product introduction costs into the December quarter. For calendar 2001 as a whole, it is targeting its total operating expenses to grow by 6-10% over its operating expenses in calendar 2000.

In the current fiscal year the company has tax losses and credits available to it such that it anticipates no meaningful tax expense for the fiscal year as a whole. The company continues to target a longer-term effective income tax rate of about 20%.

As a result of the above, the company is targeting its after-tax diluted earnings per share to grow from $0.30 in calendar 2000 to in excess of $0.60 in calendar 2001. For the March 2001 quarter, the company is targeting double-digit earnings per share percentage growth over the December quarter.

Interest and Other Income. Interest and other income in the three months ended December 31, 2000 was $642,000, compared with $550,000 in the three months ended December 31, 1999. Changes in interest income result from changes in the average amount of cash and cash equivalents on hand, and from interest earned on income taxes and tax credits recoverable. Future interest income will depend on the amount of funds available to invest and on future interest rates.

Provision for Income Taxes. The provisions for income taxes for the three months ended December 31, 2000, are calculated based on our expected effective tax rate for the entire fiscal year. We have investment tax credits and non-capital losses available to reduce taxes payable or taxable income. Future income taxes will depend on our effective tax rates and the distribution of taxable income between taxation jurisdictions. The company is targeting a longer-term effective income tax rate of approximately 20%.

Liquidity and capital resources

Cash and cash equivalents were $38.7 million at December 31, 2000. Net cash used in operations for the nine months ended December 31, 2000, was $4.7 million. Prior to changes in operating assets and liabilities, cash of $7.6 million was generated for the nine months ended December 31, 2000.

Net cash used in investing activities was $1.1 million in the nine months ended December 31, 2000, primarily due to net capital spending of $1.2 million.

Continued expansion of our business may require higher levels of capital equipment purchases. We have no significant capital spending or purchase commitments other than purchase commitments made in the ordinary course of business.

Net cash provided by financing activities in the nine months ended December 31, 2000 was $1.6 million. This was primarily a result of funds received for the purchase of shares under the terms of our stock purchase plan and stock option

plans, offset by our repayment of indebtedness of $0.1 million.

We believe that our existing cash balances together with any cash generated from our operations will be sufficient to meet our capital requirements on a short-term basis.

Longer term, we may need to raise additional capital to fund investments in operating assets to assist in the growth of our business, such as investments in accounts receivable or inventory, or to purchase capital assets, such as land, buildings or equipment. Because we do not have our own semiconductor manufacturing facility, we may be required to make deposits to secure supply in the future. Although we currently have no plans to raise additional funds, we could be required or could decide to try and raise additional capital in the future.

We periodically evaluate acquisitions of businesses, products or technologies that complement our business. If we were to enter into a transaction of this nature, we may either have to use a portion of our cash, issue debt or issue additional equity securities. If we were to issue additional equity securities, there could be further dilution to our shareholders.

Factors that may affect future operating results

The following factors may have a harmful impact on our business:

Our success will depend on the growth of the flat panel computer monitor market and other electronics markets

Our ability to generate increased revenues will depend on the growth of the flat panel computer monitor market. This market is at an early stage of development. Our continued growth will also depend upon emerging markets for digital CRT monitors, and for consumer electronics markets, such as home theater, DVD, flat screen and digital television, and HDTV. The potential size of these markets and the timing of their development is uncertain and will depend in particular upon:

- a significant reduction in the costs of products in the respective markets,
- the availability of components required by such products, and
- the emergence of competing technologies.

For the three months ended December 31, 2000, a substantial portion of our revenues were derived from sales to customers in the flat panel computer monitor market. This and other potential markets may not develop as expected, which would harm our business.

Our products may not be accepted in the flat panel computer monitor market and other emerging markets

Our success in the flat panel computer monitor market, as well as the markets for digital CRTs, home theater, DVD, flat panel and digital television, and HDTV will depend upon the extent to which manufacturers of those products incorporate our integrated circuits into their products. Our ability to sell products into these markets will depend upon demand for the functionality provided by our products. The failure of our products to be accepted in the flat panel computer monitor market in particular would harm our business.

We must develop new products and enhance our existing products to meet OEM design requirements and design cycles

We must develop new products and enhance our existing products with improved

technologies to meet rapidly evolving customer requirements and industry standards. We need to design products for customers that continually require higher functionality at lower costs. This requires us to continue to add features to our products and to include all of these features on a single chip. The development process for these advances is lengthy and will require us to accurately anticipate technological innovations and market trends. We may be unable to successfully develop new products or product enhancements. Any new products or product enhancements may not be accepted in new or existing markets. If we fail to develop and introduce new products or product enhancements, that failure will harm our business.

We face intense competition and may not be able to compete effectively

We compete with both large companies and start-up companies, including Macronix International Co., Ltd., Philips Semiconductors, a division of Philips Electronics N.V., Pixelworks, Inc., Sage, Inc., Silicon Image, Inc., and ST Microelectronics, Inc. Our business could be harmed by these existing competitors announcing or introducing new products. Also, we anticipate that as the markets for our products develop, our current customers may develop their own products and competition from diversified electronic and semiconductor companies will intensify. Some competitors are likely to include companies with greater financial and other resources than us. This increased competition could harm our business, by, for example, increasing pressure on our profit margins or causing us to lose customers.

Our semiconductor products are complex and are difficult to manufacture cost-effectively.

The manufacture of semiconductors is a complex process. It is often difficult for semiconductor foundries to achieve acceptable product yields. Product yields depend on both our product design and the manufacturing process technology unique to the semiconductor foundry. Since low yields may result from either design or process difficulties, identifying yield problems can only occur well into the production cycle, when actual product exists which can be analyzed and tested.

Defects in our products could increase our costs and delay our product shipments.

Although we test our products, they are complex and may contain defects and errors. In the past we have encountered defects and errors in our products. Delivery of products with defects or reliability, quality or compatibility problems may damage our reputation and our ability to retain existing customers and attract new customers. In addition, product defects and errors could result in additional development costs, diversion of technical resources, delayed product shipments, increased product returns, and product liability claims against us which may not be fully covered by insurance. Any of these could harm our business.

We subcontract our manufacturing, assembly and test operations.

We do not have our own fabrication facilities, assembly or testing operations. Instead, we rely on others to fabricate, assemble and test all of our products. We have our products manufactured by IBM, United Semiconductor Corporation, Taiwan Semiconductor Manufacturing Corporation and Samsung Semiconductor, Inc. No single product is purchased from more than one supplier. There are many risks associated with our dependence upon outside manufacturing, including:

- reduced control over manufacturing and delivery schedules of products,

- potential political or environmental risks in the countries where the manufacturing facilities are located, o reduced control over quality assurance,
- difficulty of management of manufacturing costs and quantities,
- potential lack of adequate capacity during periods of excess demand, and
- potential unauthorized use of intellectual property.

We depend upon outside manufacturers to fabricate silicon wafers on which our integrated circuits are imprinted. These wafers must be of acceptable quality and in sufficient quantity and the manufacturers must deliver them to assembly and testing subcontractors on time for packaging into final products. We have at times experienced delivery delays and long manufacturing lead times. These manufacturers fabricate, test and assemble products for other companies. We cannot be sure that our manufacturers will devote adequate resources to the production of our products or deliver sufficient quantities of finished products to us on time or at an acceptable cost. The lead-time necessary to establish a strategic relationship with a new manufacturing partner is considerable. We would be unable to readily obtain an alternative source of supply for any of our products if this proves necessary. Any occurrence of these manufacturing difficulties could harm our business.

Our third-party wafer foundries, third-party assembly and test subcontractors and significant customers are located in an area susceptible to earthquakes.

All of our outside foundries and most of our third party assembly and test subcontractors are located in Taiwan, which is an area susceptible to earthquakes. In addition, some of our significant customers are located in Taiwan. Damage caused by earthquakes in Taiwan may result in shortages in water or electricity or transportation which could limit the production capacity of our outside foundries and the ability of subcontractors to provide assembly and test services. Any reduction in production capacity or the ability to provide assembly and test services could cause delays or shortages in our product supply, which would harm our business. Customers located in Taiwan were responsible for 38.7% of our product revenue for the three months ended December 31, 2000. If the facilities or equipment of these customers are damaged by future earthquakes, they could reduce their purchases of our products, which would harm our business. In addition,

the operations of suppliers to our outside foundries and our Taiwanese customers could be disrupted by future earthquakes, which could in turn harm our business by resulting in shortages in our product supply or reduced purchases of our products.

A large percentage of our revenues come from sales to a small number of large customers

The markets for our products are highly concentrated. Our sales are derived from a limited number of customers. Sales to our largest five customers accounted for 33.4% of our revenues for the three months ended December 31, 2000. We expect that a small number of customers will continue to account for a large amount of our revenues. All of our sales are made on the basis of purchase orders rather than long-term agreements so that any customer could cease purchasing products at any time without penalty. The decision by any large customer to decrease or cease using our products would harm our business.

We do not have long-term commitments from our customers, and we allocate resources based on our estimates of customer demand.

Our sales are made on the basis of purchase orders rather than long-term

purchase commitments. In addition, our customers may cancel or defer purchase orders for reasons outside our control, such as supply constraints for other components incorporated into their products. We manufacture our products according to our estimates of customer demand. This process requires us to make multiple demand forecast assumptions, each of which may introduce error into our estimates. If we overestimate customer demand, we may allocate resources to manufacturing products which we may not be able to sell. As a result, we would have excess inventory, which would increase our losses. Conversely, if we underestimate customer demand or if sufficient manufacturing capacity is unavailable, we would forego revenue opportunities, lose market share and damage our customer relationships.

Our lengthy sales cycle can result in uncertainty and delays in generating revenues.

Because our products are based on new technology and standards, a lengthy sales process, typically requiring several months or more, is often required before potential customers begin the technical evaluation of our products. This technical evaluation can then exceed six months. It can take an additional six months before a customer commences volume shipments of systems that incorporate our products. However, even when a manufacturer decides to design our products into its systems, the manufacturer may never ship systems incorporating our products. Given our lengthy sales cycle, we experience a delay between the time we increase expenditures for research and development, sales and marketing efforts and inventory and the time we generate revenues, if any, from these expenditures. As a result, our business could be harmed if a significant customer reduces or delays orders or chooses not to release products incorporating our products.

Our business depends on relationships with industry leaders that are non-binding

We work closely with industry leaders in the markets we serve to design products with improved performance, cost and functionality. We typically commit significant research and development resources to such design activities. We often divert financial and personnel resources from other development projects without entering into agreements obligating these industry leaders to continue the collaborative design project or to purchase the resulting products. The failure of an industry leader to complete development of a collaborative design project or to purchase the products resulting from such projects would have an immediate and serious impact on our business, financial condition and results of operations. Our inability to establish such relationships in the future would, similarly, harm our business.

A large percentage of our revenues will come from sales outside of North America, which creates additional business risks

A large portion of our revenues will come from sales to customers outside of North America, particularly to equipment manufacturers located in Japan and other parts of Asia. For the three months ended December 31, 2000, sales to regions outside of North America amounted to 76% of revenues. These sales are subject to numerous risks, including:

- fluctuations in currency exchange rates, tariffs, import restrictions and other trade barriers,
- unexpected changes in regulatory requirements,
- longer payment periods,
- potentially adverse tax consequences,
- export license requirements,
- political and economic instability, and

- unexpected changes in diplomatic and trade relationships.

Because our sales are denominated in United States dollars, increases in the value of the United States dollar could increase the price of our products in non-U.S. markets and make our products more expensive than competitors' products denominated in local currencies.

The cyclical nature of the semiconductor industry may lead to significant variances in the demand for our products.

In the past, the semiconductor industry has been characterized by significant downturns and wide fluctuations in supply and demand. Also, the industry has experienced significant fluctuations in anticipation of changes in general economic conditions, including economic conditions in Asia. This cyclicality has led to significant variances in product demand and production capacity. It has also accelerated erosion of average selling prices per unit. We may experience periodic fluctuations in our future financial results because of changes in industry-wide conditions.

We may be unable to adequately protect our intellectual property. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as nondisclosure agreements and other methods to protect our proprietary technologies.

We have been issued patents and have a number of pending United States and foreign patent applications. However, we cannot assure you that any patent will be issued as a result of any applications or, if issued, that any claims allowed will be sufficiently broad to protect our technology. In addition, it is possible that existing or future patents may be challenged, invalidated or circumvented. It may be possible for a third party to copy or otherwise obtain and use our products, or technology without authorization, develop similar technology independently or design around our patents. Effective copyright, trademark and trade secret protection may be unavailable or limited in foreign countries.

Others may bring infringement claims against us which could be time-consuming and expensive to defend.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. This litigation is widespread in the high-technology industry and is particularly prevalent in the semiconductor industry, where a number of companies aggressively use their patent portfolios by bringing numerous infringement claims. In addition, in recent years, there has been an increase in the filing of so-called "nuisance suits" alleging infringement of intellectual property rights, which pressure defendants into entering settlement arrangements to quickly dispose of such suits, regardless of their merits. We may become a party to litigation in the future to protect our intellectual property or as a result of an alleged infringement of others' intellectual property. These lawsuits could subject us to significant liability for damages and invalidate our proprietary rights. These lawsuits, regardless of their success, would likely be time-consuming and expensive to resolve and would divert

management time and attention. Any potential intellectual property litigation also could force us to do one or more of the following:

- stop selling products or using technology that contain the allegedly infringing intellectual property;

- attempt to obtain a license to the relevant intellectual property, which license may not be available on reasonable terms or at all; and

- attempt to redesign those products that contain the allegedly infringing intellectual property.

If we are forced to take any of these actions, we may be unable to manufacture and sell some of our products, which could harm our business.

We are growing rapidly, which strains our management and resources.

We are experiencing a period of significant growth that will continue to place a great strain on our management and other resources. To manage our growth effectively, we must:

- implement and improve operational and financial systems;
- train and manage our employee base; and
- attract and retain qualified personnel with relevant experience.

We must also manage multiple relationships with customers, business partners, and other third parties, such as our foundry and test partners. Moreover, we will spend substantial amounts of time and money in connection with our rapid growth and may have unexpected costs. Our systems, procedures or controls may not be adequate to support our operations and we may not be able to expand quickly enough to exploit potential market opportunities. Our future operating results will also depend on expanding sales and marketing, research and development and administrative support. If we cannot attract qualified people or manage growth effectively, our business would be seriously harmed.

We may not be able to attract or retain the key personnel we need to succeed

Competition for qualified management, engineering and technical employees is intense. As a result, employees could leave with little or no prior notice. We cannot assure you that we will be able to attract and retain employees.

If we cannot attract and retain key employees, our business would be harmed.

We may make future acquisitions where advisable and acquisitions involve numerous risks

Our growth is dependent upon market growth and our ability to enhance our existing products and introduce new products on a timely basis. One of the ways we may address this need to develop new products is through acquisitions of other companies. Acquisitions involve numerous risks, including the following:

- We may experience difficulty in assimilating the acquired operations and employees;
- We may be unable to retain the key employees of the acquired operation;
- The acquisition may disrupt our ongoing business;
- We may not be able to incorporate successfully the acquired technology and operations into our business and maintain uniform standards, controls, policies and procedures; and
- We may lack the experience to enter into new markets, products or technologies.

Acquisitions of high-technology companies are inherently risky, and no assurance can be given that our future acquisitions, if any, will be successful and will not adversely affect our business, operating results or financial condition. We must also maintain our ability to manage any such growth effectively. Failure to manage growth effectively and successfully integrate acquisitions made by us could materially harm our business and operating results.

Other factors to consider

You should also consider the following factors:

It may be difficult for our shareholders to enforce civil liabilities under the United States federal securities laws because we are incorporated in Canada

The enforcement by our shareholders of civil liabilities under the federal securities laws of the United States may be adversely affected because:

- we are incorporated under the laws of Nova Scotia, Canada,
- some of our directors and officers are residents of Canada, and
- substantial portions of our assets are located outside the United States.

As a result, it may be difficult for holders of our common shares to effect service of a legal claim within the United States upon our directors and officers or upon other individuals who are not residents of the United States. It may also be difficult to satisfy any judgements of courts of the United States based upon civil liabilities under the federal securities laws of the United States.

Our anti-takeover defense provisions may deter potential acquirers

Our authorized capital consists of 1,000,000,000 special shares issuable in one or more series and 1,000,000,000 common shares. Our board of directors has the authority to issue special shares and to determine the price, designation, rights, preferences, privileges, restrictions and conditions of these shares without any further vote or action by our shareholders, including voting and dividend rights. The rights of holders of our common shares will be subject to, and may be adversely affected by, rights of holders of any special shares that we may issue in the future. The issuance of special shares could make it more difficult for a third party to acquire a majority of our outstanding voting shares. We have no present plans to issue any special shares. We have adopted a shareholder rights plan with respect to our common shares. This plan is specifically designed to make an unsolicited, non-negotiated takeover attempt more difficult. We also have a board of directors with three-year staggered terms, which may, in certain circumstances, make an unsolicited, non-negotiated takeover attempt more difficult.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We carry out a significant portion of our operations in Canada. Although virtually all our revenues and costs of revenues are denominated in U.S. dollars, a substantial portion of our operating expenses are denominated in Canadian dollars. Accordingly, our operating results are affected by changes in the exchange rate between the Canadian and U.S. dollars. Any future strengthening of the Canadian dollar against the US dollar could negatively impact our operating results by increasing our operating expenses. We do not presently engage in any hedging or other transactions intended to manage the risks relating to foreign currency exchange rate fluctuations, other than natural hedges that occur as a result of holding both Canadian dollar denominated assets and Canadian dollar denominated liabilities. We may in the future undertake hedging or other such transactions if management determines that it is necessary to offset exchange rate risks. To date, net exchange gains and losses on Canadian dollar denominated assets and liabilities has not been material.

PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

As of December 31, 2000, we were not a party to any material legal proceedings.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

a) The following exhibits are attached:

27.1 Financial Data Schedule

b) Reports on Form 8-K:

We filed no reports on Form 8-K in the three months ended December 31, 2000.

SIGNATURE

Our authorized representative has signed this report on our behalf as required by the Securities Exchange Act of 1934.

GENESIS MICROCHIP INCORPORATED

By: /s/ I. ERIC ERDMAN

I. Eric Erdman
Chief Financial Officer & Secretary

(Authorized Officer &
Principal Financial Officer)

Date: February 14, 2001