DSP GROUP INC /DE/
Form 10-Q
August 09, 2010
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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, 2010

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 0-23006

DSP GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-2683643**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. employer identification number)**
2580 North First Street, Suite 460	
San Jose, California	**95131**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number, including area code: (408) 986-4300

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 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). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

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

As of August 4, 2010, there were 23,349,634 shares of Common Stock ($.001 par value per share) outstanding.

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PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DSP GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share and per share data)

	June 30, 2010 Unaudited	December 31, 2009 Audited
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 31,409	$ 37,986
Restricted deposit	120	120
Marketable securities and short-term deposits	34,977	19,567
Trade receivables, net	43,848	28,352
Deferred income taxes		178
Other accounts receivable and prepaid expenses	9,396	12,162
Inventories	15,473	12,427
TOTAL CURRENT ASSETS	135,223	110,792
PROPERTY AND EQUIPMENT, NET	9,303	10,090
LONG-TERM ASSETS:		
Long-term marketable securities and deposits	54,678	65,392
Long-term prepaid expenses and lease deposits	633	1,286
Deferred income taxes	148	15
Severance pay fund	9,535	9,521
Intangible assets, net	15,370	20,473
Investment in other companies	2,200	2,200
	82,564	98,887
TOTAL ASSETS	$ 227,090	$ 219,769

Note: The balance sheet at December 31, 2009 has been derived from the audited financial statements on that date.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share and per share data)

	June 30, 2010 Unaudited	December 31, 2009 Audited
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Trade payables	$ 26,019	$ 18,309
Accrued compensation and benefits	8,652	9,900
Income tax accruals and payables	3,098	2,939
Accrued expenses and other accounts payable	8,793	11,631
Total current liabilities	46,562	42,779
LONG-TERM LIABILITIES:		
Accrued severance pay	10,681	10,572
Accrued pensions	847	929
Total long-term liabilities	11,528	11,501
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Capital stock:		
Preferred stock, $ 0.001 par value - Authorized shares: 5,000,000 at June 30, 2010 and December 31, 2009; Issued and outstanding shares: none at June 30, 2010 and December 31, 2009		
Common stock, $ 0.001 par value -		
Authorized shares: 50,000,000 shares at June 30, 2010 and December 31, 2009; Issued and outstanding shares: 23,154,928 and 22,901,051 shares at June 30, 2010 and December 31, 2009, respectively	23	23
Additional paid-in capital	330,656	325,579
Treasury stock	(120,644)	(123,350)
Accumulated other comprehensive income	(38)	2,174
Accumulated deficit	(40,997)	(38,937)
Total stockholders equity	169,000	165,489
Total liabilities and stockholders equity	$ 227,090	$ 219,769

Note: The balance sheet at December 31, 2009 has been derived from the audited financial statements on that date.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(U.S. dollars in thousands, except per share amounts)

(U.S. dollars in thousands, except share and per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Revenues	$ 60,846	$ 52,020	$ 116,956	$ 91,934
Cost of revenues (1) (2)	37,592	32,940	70,113	59,444
Gross profit	23,254	19,080	46,843	32,490
Operating expenses:				
Research and development (3)	13,541	13,632	27,032	27,368
Sales and marketing (4)	4,226	4,284	8,671	8,801
General and administrative (5)	3,615	3,926	7,377	7,740
Intangible assets amortization	2,488	3,058	4,985	6,105
Total operating expenses	23,870	24,900	48,065	50,014
Operating loss	(616)	(5,820)	(1,222)	(17,524)
Interest and other income, net	263	582	688	1,184
Loss before taxes on income	(353)	(5,238)	(534)	(16,340)
Taxes on income (income tax benefit)	14	(3,561)	17	(3,972)
Net loss	$ (367)	$ (1,677)	$ (551)	$ (12,368)
Net loss per share:				
Basic	$ (0.02)	$ (0.07)	$ (0.02)	$ (0.51)
Diluted	$ (0.02)	$ (0.07)	$ (0.02)	$ (0.51)
Weighted average number of shares used in per share computations of net loss:				
Basic	23,149	22,734	23,128	24,408
Diluted	23,149	22,734	23,128	24,408

(1) Includes an amount of $0 and $8,013 with a related party for the six months ended June 30, 2010 and 2009, respectively; and $0 for the three months ended June 30, 2010 and 2009, respectively.

(2) Includes equity-based compensation expense in the amount of $167 and $195 for the three months ended June 30, 2010 and 2009, respectively; and $369 and $403 for the six months ended June 30, 2010 and 2009, respectively.

(3) Includes equity-based compensation expense in the amount of $1,119 and $1,403 for the three months ended June 30, 2010 and 2009, respectively; and $2,502 and $2,977 for the six months ended June 30, 2010 and 2009, respectively.

(4) Includes equity-based compensation expense in the amount of $325 and $468 for the three months ended June 30, 2010 and 2009, respectively; and $768 and $926 for the six months ended June 30, 2010 and 2009, respectively.

(5) Includes equity-based compensation expense in the amount of $622 and $759 for the three months ended June 30, 2010 and 2009, respectively; and $1,438 and $1,539 for the six months ended June 30, 2010 and 2009, respectively.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(U.S. dollars in thousands)

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Net cash provided by operating activities	$ 1,309	$ 11,507
Investing activities		
Purchase of marketable securities and deposits	(45,499)	(33,466)
Proceeds from maturity and sale of marketable securities and deposits	39,769	22,437
Proceeds from sales of property and equipment	41	
Purchases of property and equipment	(2,271)	(3,044)
Net cash used in investing activities	(7,960)	(14,073)
Financial activities		
Purchase of treasury stock		(20,028)
Issuance of treasury stock for cash upon exercise of options	269	
Net cash provided by (used in) financing activities	269	(20,028)
Decrease in cash and cash equivalents	$ (6,382)	$ (22,594)
Cash erosion due to exchange rate differences	(195)	(63)
Cash and cash equivalents at the beginning of the period	$ 37,986	$ 68,887
Cash and cash equivalents at the end of the period	$ 31,409	$ 46,230

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED STATEMENTS OF STOCKHOLDERS EQUITY

(UNAUDITED)

(U.S. dollars in thousands)

Three Months Ended June 30, 2009	**Number of Common Stock**	**Common Stock**	**Additional Paid-In Capital**	**Treasury Stock**	**Retained Earnings (accumulated deficit)**	**Other Comprehensive Income (Loss)**	**Total Comprehensive Income (Loss)**	**Total Stockholders Equity**
Balance at March 31, 2009	22,734	$ 23	$ 317,509	$ (125,142)	$ (40,369)	$ (1,680)		$ 150,341
Net loss					(1,677)		$ (1,677)	(1,677)
Change in unrealized gain from hedging activities, net						1,204	1,204	1,204
Change in unrealized gain from marketable securities, net						1,545	1,545	1,545
Change in foreign currency translation adjustments, net						256	256	256
Total comprehensive income							$ 1,328	
Equity-based compensation			2,825					2,825
Balance at June 30, 2009	**22,734**	**$ 23**	**$ 320,334**	**$ (125,142)**	**$ (42,046)**	**$ 1,325**		**$ 154,494**
Three Months Ended June 30, 2010								
Balance at March 31, 2010	23,134	$ 23	$ 328,423	$ (120,871)	$ (40,509)	$ 2,084		$ 169,150
Net loss					(367)		$ (367)	(367)
Change in unrealized loss from hedging activities, net						(555)	(555)	(555)
Change in unrealized gain from marketable securities, net						(1,014)	(1,014)	(1,014)_
Change in realized gain from pensions, net						(8)	(8)	(8)
Change in foreign currency translation adjustments, net						(545)	(545)	(545)
Total comprehensive income							$ (2,489)	
Issuance of treasury stock upon exercise of stock options and SARs by employees	21			227	(121)			106
Equity-based compensation			2,233					2,233
Balance at June 30, 2010	**23,155**	**$ 23**	**$ 330,656**	**$ (120,644)**	**$ (40,997)**	**$ (38)**		**$ 169,000**

(*) Represents an amount lower than $1.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED STATEMENTS OF STOCKHOLDERS EQUITY

(UNAUDITED)

(U.S. dollars in thousands)

	Number of Common Stock	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings (accumulated deficit)	Other Comprehensive Income (Loss)	Total Comprehensive Income	Total Stockholders Equity
Six Months Ended June 30, 2009								
Balance at December 31, 2008	26,731	$ 27	$ 314,484	$ (107,749)	$ (28,186)	$ 51		$ 178,627
Net loss					(12,368)		$ (12,368)	(12,368)
Change in unrealized gain from hedging activities, net						128	128	128
Change in unrealized gain from marketable securities, net						1,146	1,146	1,146
Total comprehensive loss							$ (11,094)	
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	190			2,635	(1,492)			1,143
Purchase of treasury stock	(4,187)	(4)	4	(20,028)				(20,028)
Equity-based compensation			5,846					5,846
Balance at June 30, 2009	**22,734**	**$ 23**	**$ 320,334**	**$ (125,142)**	**$ (42,046)**	**$ 1,325**		**$ 154,494**
Six Months Ended June 30, 2010								
Balance at December 31, 2009	22,901	$ 23	$ 325,579	$ (123,350)	$ (38,937)	$ 2,174		$ 165,489
Net loss					(551)		$ (551)	(551)
Change in unrealized loss from hedging activities, net						(505)	(505)	(505)
Change in unrealized gain from marketable securities, net						(899)	(899)	(899)
Change in unrealized gain from pensions, net						(15)	(15)	(15)
Change in foreign currency translation adjustments, net						(793)	(793)	(793)

Total comprehensive loss							$ (2,763)	
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	194	*)		2,064	(1,136)			928
Issuance of treasury stock upon exercise of stock options and SARs by employees	60	*)		642	(373)			269
Equity-based compensation			5,077					5,077
Balance at June 30, 2010	**23,155**	**$ 23**	**$ 330,656**	**$ (120,644)**	**$ (40,997)**	**$ (38)**		**$ 169,000**

(*) Represents an amount lower than $1.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2010

(UNAUDITED)

(U.S. dollars in thousands, except share and per share data)

NOTE A BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, The FASB Accounting Standards Codification TM and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162 (the ASC). The ASC is effective for interim and annual periods ending after September 15, 2009 and became the single official source of authoritative, nongovernmental U.S. generally accepted accounting principles (U.S. GAAP), other than guidance issued by the Securities and Exchange Commission. All other literature will become non-authoritative. The standard does not have an impact on the Company s consolidated financial statements and notes. Where applicable, references to pre-codification accounting standards will include an initial parenthetical reference to the ASC and subsequent references will use the ASC reference only.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States 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 footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. For further information, reference is made to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K of DSP Group, Inc. (the Company) for the year ended December 31, 2009.

NOTE B INVENTORIES

Inventories are stated at the lower of cost or market value. The Company periodically evaluates the quantities on hand relative to current and historical selling prices, and historical and projected sales volume. Based on these evaluations, provisions are made in each period to write inventory down to its net realizable value. Inventories are composed of the following:

	June 30, 2010 (Unaudited)	December 31, 2009 (Audited)
Work-in-process	$ 7,991	$ 2,654
Finished goods (*)	7,482	9,773
	$ 15,473	$ 12,427

(*) The finished products inventory includes $283 and $613 of inventory held in consignment by other parties as of June 30, 2010 and December 31, 2009, respectively.

Write-off of inventory amounted to $189 and $0 for the six months ended June 30, 2010 and 2009, respectively.

NOTE C NET LOSS PER SHARE

Basic net loss per share is computed based on the weighted average number of shares of common stock outstanding during the period. For the same periods, diluted net loss per share further includes the effect of dilutive stock options and stock appreciation rights outstanding during the period, all in accordance with FASB ASC No. 260 Earnings per Share. The following table sets forth the computation of basic and diluted net loss per share:

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	Three months ended June 30, 2010	2009	Six months ended June 30, 2010	2009
	Unaudited			
Net loss	$ (367)	$ (1,677)	$ (551)	$ (12,368)
Loss per share:				
Basic	$ (0.02)	$ (0.07)	$ (0.02)	$ (0.51)
Diluted	$ (0.02)	$ (0.07)	$ (0.02)	$ (0.51)
Weighted average number of shares of common stock outstanding during the period used to compute basic net earnings per share	23,149	22,734	23,128	24,408
Incremental shares attributable to exercise of outstanding options (assuming proceeds would be used to purchase treasury stock)				
Weighted average number of shares of common stock used to compute diluted net earnings per share	23,149	22,734	23,128	24,408

NOTE D MARKETABLE SECURITIES AND TIME DEPOSITS

The Company accounts for investments in marketable securities in accordance with FASB ASC No.320-10 Investments in Debt and Equity Securities. Management determines the appropriate classification of its investments in government and corporate marketable debt securities at the time of purchase and reevaluates such determinations at each balance sheet date.

The Company classifies marketable securities as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses, net of taxes, reported in other comprehensive income. The amortized cost of marketable securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and interest are included in financial income, net. Interest and dividends on securities are included in financial income, net. The following is a summary of available-for-sale securities at June 30, 2010 and December 31, 2009:

	Amortized cost June 30, 2010 (Unaudited)	December 31, 2009 (Audited)	Unrealized gains (losses), net June 30, 2010 (Unaudited)	December 31, 2009 (Audited)	Estimated fair value June 30, 2010 (Unaudited)	December 31, 2009 (Audited)
Short and long-term deposits	$ 22,826	$ 25,258	$	$	$ 22,826	$ 25,258
U.S. government obligations and political subdivisions	25,565	14,703	(93)	(88)	25,472	14,615
Corporate obligations	40,973	43,808	384	1,278	41,357	45,086
	$ 89,364	$ 83,769	$ 291	$ 1,190	$ 89,655	$ 84,959

The amortized cost of short and long-term deposit and available-for-sale debt securities at June 30, 2010, by contractual maturities, is shown below:

	Amortized cost	Unrealized gains (losses) Gains	Losses	Estimated fair value
Due in one year or less	$ 24,740	$ 114	$ (5)	$ 24,849
Due after one year to five years	64,624	395	(213)	64,806
	$ 89,364	$ 509	$ (218)	$ 89,655

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The actual maturity dates may differ from the contractual maturities because debtors may have the right to call or prepay obligations without penalties.

As of June 30, 2010, the unrealized losses in the Company s investments in all types of marketable securities were temporary and no impairment loss was realized in the Company s condensed consolidated statement of operation.

Marketable securities are periodically reviewed for impairment. If management concludes that any marketable security is impaired, management determines whether such impairment is other-than-temporary. Factors considered in making such a determination include the duration and severity of the impairment, the reason for the decline in value and the potential recovery period, and the Company s intent to sell, or whether it is more likely than not that the Company will be required to sell the marketable security before recovery of cost basis. If any impairment is considered other-than-temporary, the marketable security is written down to its fair value through a corresponding charge to financial income, net.

NOTE E TAXES ON INCOME

The effective tax rate used in computing the provision for income taxes is based on projected fiscal year income before taxes, including estimated income by tax jurisdiction. Tax provision for the three months and six month ended June 30, 2010 and June 30, 2009 does not include tax benefit associated with equity-based compensation expenses. During the three and six months ended June 30, 2010 the Company did not record any deferred tax assets due to its current estimation of future taxable income primarily as a result of general adverse market conditions.

The total amount of net unrecognized tax benefits that, if recognized, would affect the effective tax rate was $3,140 and $3,107 at June 30, 2010 and December 31, 2009, respectively. The Company accrues interest and penalties, relating to unrecognized tax benefits, in its provision for income taxes. At June 30, 2010 and December 31, 2009, the Company had accrued interest and penalties relating to unrecognized tax benefits of $522 and $489, respectively.

NOTE F SIGNIFICANT CUSTOMERS

The Company sells its products primarily through distributors and directly to original equipment manufacturers (OEMs) and original design manufacturers (ODMs) who incorporate the Company s products into consumer products. The Company s future performance will depend, in part, on the continued success of its distributors in marketing and selling its products. The loss of the Company s distributors and the Company s inability to obtain satisfactory replacements in a timely manner may harm the Company s sales and results of operations. In addition, the Company expects that a limited number of customers, varying in identity from period-to-period, will account for a substantial portion of its revenues in any period. The loss of, or reduced demand for products from, any of the Company s major customers could have a material adverse effect on the Company s business, financial condition and results of operations.

Sales to Hong Kong-based VTech Holdings Ltd. (VTech) represented 32% and 33% of the Company s total revenues for the three months ended June 30, 2010 and 2009, respectively. Sales to VTech represented 34% and 31% of the Company s total revenues for the six months ended June 30, 2010 and 2009, respectively.

Sales to CCT Telecom Holdings Ltd. (CCT) represented 10% and 7% of the Company s total revenues for the three and six months ended June 30, 2010 and 2009, respectively

Revenues derived from sales through one distributor, Tomen Electronics Corporation (Tomen Electronics), accounted for 23% and 21% of the Company s total revenues for the three months ended June 30, 2010 and 2009, respectively. Additionally, Tomen Electronics accounted for 21% and 23% of the Company s total revenues for the six months ended June 30, 2010 and 2009, respectively. The Japanese market and the OEMs that operate in that market are among the largest suppliers in the world with significant market share in the U.S. market for residential wireless products. Tomen Electronics sells the Company s products to a limited number of customers. One customer, Panasonic Communications Co., Ltd. (Panasonic), has continually accounted for a majority of the sales of Tomen Electronics. Sales to Panasonic through Tomen Electronics generated 16% and 15% of the Company s total revenues for the three months ended June 30, 2010 and 2009, respectively. Sales to Panasonic through Tomen Electronics generated 15% of the Company s revenues for both the six months ended June 30, 2010 and 2009. Additionally, sales to Uniden America Corp. (Uniden) through

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Tomen Electronics or directly to Uniden represented 11% and 13% of the Company s total revenues for the three months ended June 30, 2010 and 2009, respectively. Sales to Uniden represented 12% and 13% of the Company s total revenues for the six months ended June 30, 2010 and 2009, respectively.

NOTE G DERIVATIVE INSTRUMENTS

The Company accounts for derivative instruments in accordance with FASB. ASC No. 815 Derivatives and Hedging . Due to the Company s global operations, it is exposed to foreign currency exchange rate fluctuations in the normal course of its business. The Company s treasury policy allows it to offset the risks associated with the effects of certain foreign currency exposures through the purchase of foreign exchange forward contracts and put options (collectively, hedging contracts). The policy, however, prohibits the Company from speculating on hedging contracts for profit.

To protect against the increase in value of forecasted foreign currency cash flows resulting from salary and lease payments of its Israeli facilities denominated in the Israeli currency, the New Israeli Shekels (NIS), during the year, the Company instituted a foreign currency cash flow hedging program. The Company hedges portions of the anticipated payroll and lease payments denominated in NIS for a period of one to twelve months with hedging contracts. Accordingly, when the dollar strengthens against the foreign currencies, the decline in present value of future foreign currency expenses is offset by losses in the fair value of the hedging contracts. Conversely, when the dollar weakens, the increase in the present value of future foreign currency cash flows is offset by gains in the fair value of the hedging contracts. These hedging contracts are designated as cash flow hedges, as defined by FASB ASC No. 815 Derivatives and Hedging (ASC 815) and are all effective hedges of these expenses.

In accordance with ASC 815, for derivative instruments that are designated and qualify as a cash flow hedge (i.e. hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Any gain or loss on a derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item is recognized in current earnings during the period of change. As of June 30, 2010, the Company had outstanding forward contracts in the amount of $11,225 and outstanding option contract in the amount of $1,400. These hedging contracts do not contain any credit-risk-related contingency features. See Note K for information on the fair value of these hedging contracts.

The fair value of derivative assets and derivative liabilities were $11 and $289, respectively, at June 30, 2010. The Company recorded a net amount of $278 in other accounts payable and accrued expenses in the condensed consolidated balance sheets at June 30, 2010.

The amount recorded as an income in research and development expenses, sales and marketing expenses and general and administrative expenses in the condensed consolidated statements of income for the six months ended June 30, 2010 that resulted from the above referenced hedging transactions was $171, $29 and $21, respectively. The amount recorded as an income in research and development expenses, sales and marketing expenses and general and administrative expenses in the condensed consolidated statements of income for the three months ended June 30, 2010 that resulted from the above referenced hedging transactions was $56, $10 and $7, respectively.

The fair value of the outstanding derivative instruments at June 30, 2010 and December 31, 2009 is summarized below:

		Fair Value of Derivative Instruments	
	Balance Sheet Location	**As of June 30, 2010**	**As of December 31, 2009**
Derivative Assets			
Foreign exchange forward contracts and put options	Other accounts receivable and prepaid expenses (*)		227
Total		$	$ 227
Derivative Liabilities			
		$ 278	$

Foreign exchange forward contracts and put options	Other accounts payable and accrued expenses (*)				
Total		$	278	$	

*) Estimated to be reclassified into earnings during 2010 and 2011.

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The effect of derivative instruments in cash flow hedging transactions on income and other comprehensive income (OCI) for the three and six months ended June 31, 2010 and 2009 is summarized below:

	Gains (Losses) on Derivatives Recognized in OCI			
	for the three months ended June 30,		for the six months ended June 30,	
	2010	2009	2010	2009
Foreign exchange forward contracts	$ (482)	969	(285)	(829)

		Gains (Losses) Reclassified from OCI into Income			
		for the three months ended June 30		for the six months ended June 30,	
	Location	2010	2009	2010	2009
Foreign exchange forward contracts	Operating expenses	73	(235)	220	(957)

NOTE H CONTINGENCIES

From time to time, the Company may become involved in litigation relating to claims arising from its ordinary course of business. Also, as is typical in the semiconductor industry, the Company has been and may from time to time be notified of claims that the Company may be infringing patents or intellectual property rights owned by third parties. The Company currently believes that there are no claims or actions pending or threatened against it, the ultimate disposition of which would have a material adverse effect on the Company.

NOTE I ACCOUNTING FOR EQUITY-BASED COMPENSATION

Grants for Three Months Ended June 30, 2010 and June 30, 2009:

The weighted average estimated fair value of employee stock options and share appreciation rights (SARs) granted during the three months ended June 30, 2010 was $3.37 per share. During the three months ended June 30, 2009, no stock options and SARs were granted. The weighted average estimated fair value for grants during the three months ended June 30, 2010 was calculated using the binomial model, with the following weighted average assumptions (annualized percentages):

	Three months ended June 30, 2010
Volatility	62.22%
Risk-free interest rate	2.32%
Dividend yield	0%
Pre-vest cancellation rate	6.72%
Post-vest cancellation rate	3.87%
Suboptimal exercise factor	1.52

The expected life of employee stock options and SARs is impacted by all of the underlying assumptions used in the Company s model. The binomial model assumes that employees exercise behavior is a function of the remaining contractual life of the stock option or SAR and the extent to which the stock option or SAR is in-the-money (*i.e.*, the average stock price during the period is above the exercise price of the stock option or SAR). The binomial model estimates the probability of exercise as a function of these two variables based on the history of exercises and cancellations of past option and SAR grants made by the Company. The expected life for options and SARs granted during the three months ended June 30, 2010 derived from the binomial model was 4.00 years.

Employee Stock Benefit Plans

As of June 30, 2010, the Company had four equity incentive plans and one employee stock purchase plan. As of June 30, 2010, approximately 652,000 shares of common stock remain available for grant under the Company s employee stock purchase plan and approximately 1,199,994 shares of common stock remain available for grant under the Company s equity incentive plans.

The table below presents a summary of information relating to the Company s stock option and SAR grants pursuant to its equity incentive plans:

	Number of Options/SAR Units in thousands	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Value (*) in thousands
Outstanding at March 31, 2010	12,724	$ 13,64		
Options granted	43	$ 8.47		
SAR units granted (1)	37	$ 8.47		
Options / SAR units cancelled/forfeited/expired	(537)	$ 14.16		
Options / SAR units exercised	(40)	$ 5.97		
Outstanding at June 30, 2010 (2)	12,228	$ 13.61	4.48	$ 1,113
Exercisable at June 30, 2010 (3)	6,751	$ 18.18	3.28	$ 366

(*) Calculation of aggregate intrinsic value is based on the share price of the Company s common stock on June 30, 2010 ($6.39 per share).

(1) The SAR units in the above table, which were granted subsequent to January 1, 2010, are convertible for a maximum number of shares of the Company s common stock equal to 66.67% of the SAR units subject to the grant.

(2) Due to the ceiling imposed on the SAR grants, the outstanding amount equals to a maximum of 8,870 shares of the Company s common stock outstanding. SAR grants made prior to January 1, 2009 are convertible for a maximum number of shares of the Company s common stock equal to 50% of the SAR units subject to the grant. SAR grants made on or after January 1, 2009 and before January 1, 2010 are convertible for a maximum number of shares of the Company s common stock equal to 75% of the SAR units subject to the grant. SAR grants made on or after January 1, 2010 are convertible for a maximum number of shares of the Company s common stock equal to 66.67% of the SAR units subject to the grant.

(3) Due to the ceiling imposed on the SAR grants, the currently exercisable amount equals to a maximum of 4,971 shares of the Company s common stock exercisable.

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Additional information about stock options and SAR units outstanding and exercisable at June 30, 2010 with exercise prices above $6.39 per share (the closing price of the Company s common stock on June 30, 2010) is as follows (in thousands):

	Exercisable		Unexercisable		Total	
Exercise Prices	Number of Options/SAR Units	Weighted Average Exercise Price	Number of Options/ SAR Units	Weighted Average Exercise Price	Number of Options/ SAR Units	Weighted Average Exercise Price
Above $6.39	5,883	$ 19.98	3,806	$ 8.87	9,690	$ 15.61
Less than $6.39	868	$ 5.97	1,670	$ 5.94	2,538	$ 5.95
Total	6,751	$ 18.18	5,477	$ 7.97	12,228	$ 13.61

The Company s aggregate compensation expense for the three months ended June 30, 2010 and 2009 totaled $2,233 and $2,825, respectively. The Company did not recognize any income tax benefit relating to its equity-based compensation expense for the three months ended June 30, 2010 and 2009.

The Company s aggregate compensation expense for the six months ended June 30, 2010 and 2009 totaled $5,077 and $5,846, respectively. The Company did not recognize any income tax benefit relating to its equity-based compensation expense for the six months ended June 30, 2010 and 2009.

As of June 30, 2010, there was $10,027 of total unrecognized equity-based compensation expense related to unvested equity-based compensation awards granted under the Company s equity incentive plans. This amount is expected to be recognized during the period from 2010 through 2014.

NOTE J PENSION LIABILITY

The information in this note represents the net periodic pension and post-retirement benefit costs and related components in accordance with FASB ASC No. 715 Employers Disclosures about Pensions and Other Postretirement Benefits. The components of net pension and post-retirement periodic benefit cost (income) for the six months ended June 30, 2010 and 2009 are as follows (in thousands):

	June 30, 2010	June 30, 2009
Components of net periodic benefit cost		
Service cost	$ 147	$ 94
Interest cost	70	95
Expected return on plan assets	(53)	(78)
Exchange rate expenses	(139)	44
Net periodic benefit cost	**$ 25**	**$ 67**

The net pension liability as of June 30, 2010 amounted to $847.

NOTE K FAIR VALUE MEASUREMENTS

Assets and Liabilities Measured at Fair Value on a Recurring Basis:

The Company measures its cash equivalents, short-term deposits, marketable securities and foreign currency derivative contracts at fair value. Cash equivalents, short-term deposits and marketable securities are classified within Level 1 or Level 2 value hierarchies as they are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs. Foreign currency derivative contracts are classified within Level 2 value hierarchy as the valuation inputs are based on quoted prices and market observable data of similar instruments.

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The following table provides information by value level for assets and liabilities that are measured at fair value on a recurring basis as of June 30, 2010.

	Balance as of June 30, 2010	Fair Value Measurements Level 1	Level 2	Level 3
Description				
Assets:				
Cash equivalents:				
Time deposits	$ 2,894		$ 2,894	
Money market mutual funds	$ 6,385	$ 6,385		
Short-term marketable securities and cash deposits:				
Corporate debt securities	$ 12,151		$ 12,151	
U.S. government securities				
Time deposits	$ 12,697		$ 12,697	
Long-term marketable securities:				
U.S. government securities	$ 25,472		$ 25,472	
Corporate debt securities	$ 29,206		$ 29,206	
Time deposits	$ 10,129		$ 10,129	
Derivative liabilities	$ 278		$ 278	

The following table provides information by value level for assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2009.

	Balance as of December 31, 2009	Fair Value Measurements Level 1	Level 2	Level 3
Description				
Assets:				
Cash equivalents:				
Time deposits	$ 14,691		$ 14,691	
Money market mutual funds	$ 2,100	$ 2,100		
Short-term marketable securities and cash deposits:				
Corporate debt securities	$ 4,360		$ 4,360	
Time deposits	$ 15,208		$ 15,208	
Long-term marketable securities:				
U.S. government securities	$ 14,615		$ 14,615	
Corporate debt securities	$ 40,727		$ 40,727	
Time deposits	$ 10,050		$ 10,050	
Derivative assets	$ 227		$ 227	

In addition to the assets and liabilities described above, the Company s financial instruments also include cash and cash equivalents, restricted and short-term deposits, trade receivables, other accounts receivable, trade payables, accrued expenses and other payables. The fair value of these financial instruments was not materially different from their carrying values at June 30, 2010 due to the short-term maturity of these instruments.

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NOTE L STOCKHOLDERS EQUITY

No shares were repurchased under the Company s board authorized share repurchase program during the first six months of 2010. As of June 30, 2010, 255,488 shares of the Company s common stock remain authorized for repurchase under the share repurchase program.

During the first quarter of 2009, in accordance with the Stock Repurchase Agreement executed by the Company and NXP B.V. (NXP) on January 27, 2009, the Company repurchased 4,186,603 shares of its common stock that were issued to NXP in connection with the acquisition of the cordless and VoIP terminals business of NXP at the purchase price of $4.78 per share for approximately $20,028.

Repurchases of common stock are accounted for as treasury stock, and result in a reduction of stockholders equity. When treasury shares are reissued, the Company accounts for the reissuance in accordance with Accounting Principles Board Opinion No. 6, Status of Accounting Research Bulletins (ASC 505-30) and charges the excess of the repurchase cost over issuance price using the weighted average method to accumulated deficit. In the case where the repurchase cost over issuance price using the weighted average method is lower than the issuance price, the Company credits the difference to additional paid-in capital.

During the first six months of 2010, the Company issued 253,877 shares of common stock out of treasury stock to employees who exercised their stock options or purchased shares from the Company s 1993 Employee Stock Purchase Plan.

NOTE M NEW ACCOUNTING PRONOUNCEMENTS

In January 2010, the FASB issued Accounting Standards Update ASU No. 2010-06, Improving Disclosures about Fair Value Measurements, which requires disclosures about inputs and valuation techniques used to measure fair value, as well as disclosures about significant transfers, beginning in the first quarter of 2010. Additionally, these amended standards require presentation of disaggregated activity within the reconciliation for fair value measurements using significant unobservable inputs (Level 3) beginning in the first quarter of 2011. The adoption of the effective portions of this ASU did not have a material impact on the Company s consolidated financial position, results of operations or cash flows. The Company does not anticipate that the adoption of the remaining portions of this ASU will have a material impact to its consolidated financial position, results of operations or cash flows.

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

This report and certain information incorporated herein by reference contain forward-looking statements, which are provided under the safe harbor protection of the Private Securities Litigation Reform Act of 1995. All statements included or incorporated by reference in this report, other than statements that are purely historical in nature, are forward-looking statements. Forward-looking statements are generally written in the future tense and/or are preceded by words such as will, may, should, could, expect, suggest, believe, anticipate, intend, plan, or other similar words. Forward-looking statements include statements regarding:

Our belief that CAT-iq, which has been widely embraced by all leading European operators, will also proliferate into other regions that have adopted DECT telephony, such as the U.S., and that this new standard will enable the introduction of new cordless products into the market;

Our belief that the XpandR platform will present unique opportunities for us to expand the domain of applications and add new customers served by our products;

We believe that revenues from our DECT 6.0 products will grow in the second half of 2010 as compared to the same period of 2009;

Our belief that the rapid deployment of new communication access methods, as well as the projected lack of growth in fixed-line telephony, will reduce our total revenues derived from, and unit sales of, cordless telephony products, including our DECT and 2.4GHz products, for the long term;

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Our belief that the market will remain price sensitive for the remainder of 2010 and that price erosion will continue;

Our belief that our available cash and cash equivalents should be sufficient to finance our operations for both the short and long term.

All forward-looking statements included in this Quarterly Report on Form 10-Q are made as of the date hereof, based on information available to us as of the date hereof, and we assume no obligation to update any forward-looking statement. Many factors may cause actual results to differ materially from those expressed or implied by the forward-looking statements contained in this report. These factors include, but are not limited to, our dependence on one primary distributor, our OEM relationships and competition, as well as those risks described in Part II Item 1A Risk Factors of this Form 10-Q.

Overview

The following discussion and analysis is intended to provide investors with a narrative of our financial results and an evaluation of our financial condition and results of operations. The discussion should be read in conjunction with our condensed consolidated financial statements and notes thereto.

Business Overview

DSP Group is a leading global provider of wireless chipset solutions for converged communications at home, delivering system solutions that combine semiconductors and software with reference designs. We provide a broad portfolio of wireless chipsets integrating DECT, Wi-Fi, PSTN and VoIP technologies with state-of-the-art application processors. We also enable converged voice, audio, video and data connectivity across diverse consumer products from cordless and VoIP phones to home gateways and connected multimedia screens. Our current primary focus is digital cordless telephony with sales of our in-house developed DECT, CoIP, 2.4GHz and 5.8GHz chipsets representing approximately 93% of our total revenues for the first half of 2010.

In September 2007, we acquired the cordless and VoIP terminals business (the CIPT Business) of NXP B.V. (NXP) (the Acquisition). In connection with the Acquisition, we paid NXP approximately $200 million in cash and issued 4,186,603 shares of our common stock to NXP. On March 12, 2009, we repurchased the shares of common stock issued to NXP in connection with the Acquisition for an aggregate consideration of approximately $20 million.

Our business operates in a highly competitive environment. Our revenues were $117.0 million for the first half of 2010, an increase of 27.2% in comparison to the same period of 2009. Sales of our DECT 6.0 products in the U.S. market increased from $39.7 million for the first half of 2009 to $48.7 million for the first half of 2010. Revenues derived from the sale of DECT products represented 79% of our total revenues for the first half of 2010, as compared to 78% of our total revenues for the half year of 2009. We believe that revenues from our DECT 6.0 products will grow in the second half of 2010 as compared to the same period of 2009. Competition has historically increased pricing pressures for our products and decreased our average selling prices, and we believe this trend will continue for the remainder of 2010. Our gross margin increased to 40.0% of total revenues for the first half of 2010 from 35.3% for the first half of 2009, primarily due to (i) the increase in overall revenues, (ii) increased sales of products during the six months of 2010 with higher gross margins, and (iii) reversal of a reserve amounting to $2.5 million regarding a potential patent infringement claim that was determined to be no longer needed due to the expiration of the applicable statute of limitations.

In addition to general market competitiveness of our business, the cordless telephony market is undergoing a challenging period of transition characterized by stagnation due to the lack of new model launches and market anticipation of next generation products. As a result, we expect the market to remain price sensitive and expect price erosion to continue. Moreover, various other factors, including increases in the cost of raw materials and commodities and our suppliers passing such increases onto us, increases in silicon wafer costs and increases in production, assembly and testing costs, and shortage of capacity to fulfill our fabrication, assembly and testing needs, all may decrease our gross profit in future periods. Moreover, the continued uncertainty about the sustainability of the global economic recovery and outlook has resulted in accelerated erosion of prices, longer product cycles and decision-making processes at our customers organizations, and general adverse business conditions.

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In addition to the highly competitive environment in which we operate, we believe there are also several emerging market trends that challenge our continued business growth potential. For example, the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, as well as the lack of growth in products using fixed-line telephony, may reduce our revenues derived from, and unit sales of, cordless telephony products, which are currently our primary focus. Our business also may be affected by the outcome of the competition between cellular phone operators and fixed-line operators for the provision of residential communication. A significant majority of our revenues are currently generated from sales of chipsets used in cordless phones that are based on fixed-line telephony.

Nonetheless, we recognize the competitive landscape and are actively engaged in addressing these market challenges and trends. Our operating expenses decreased by 4% to $48.1 million for the first half of 2010, as compared to $50.0 million for the first half of 2009. Our operating loss also decreased to $1.2 million for the first half of 2010, as compared to $17.5 million for the first half of 2009. We are also concentrating our development efforts on a new cordless telephony DECT standard, the CAT-iq protocol, which stands for Cordless Advanced Technology: Internet and Quality. CAT-iq has been widely embraced by all leading European operators, and we believe that this technology will also proliferate into other regions that have adopted DECT telephony, such as the U.S. This new standard is anticipated to enable the introduction of new cordless products into the market as telecom operators have begun deploying home gateways and mobile handsets with CAT-iq in the market. In addition to DECT technologies, we are investing in developing CoIP (Cordless over IP) technologies in-house. Our goal is to leverage the Wi-Fi technology acquired in 2004 from Bermai Inc. to further develop and offer products for residential communication that integrate voice, data and video with broadband offerings. We have already introduced to the market the XpandR platform that integrates DECT and Wi-Fi capabilities to enable multimedia and web-related applications in our future products. We believe that the XpandR platform will present unique opportunities for us to expand the domain of applications and add new customers served by our products. In 2010, our second generation XpandR platform is expected to be sold by some of our customers. However, our success in introducing new products and penetrating new markets may not occur and may require us to substantially increase our operating expenses. As a result, our past operating results should not be relied upon as an indication of future performance.

As of June 30, 2010, our principal source of liquidity consisted of cash and cash equivalents of $31.4 million and marketable securities and short and long term deposits of $89.7 million, totaling $121.1 million.

RESULTS OF OPERATIONS

Total Revenues. Our total revenues were $60.8 million for the second quarter of 2010, as compared to $52.0 million for the same period in 2009. Our total revenues were $117.0 million for the first six months of 2010, as compared to $91.9 million for the same period in 2009. The increase for both periods was primarily a result of increased sales of our DECT products. Sales of DECT products for the second quarter of 2010 and 2009 were $49.1 million and $42.6 million, respectively, representing approximately 81% and 82%, respectively, of total revenues, an increase of 15% in absolute dollars when comparing sales for the second quarter of 2010 to sales for the second quarter of 2009. Sales of DECT products for the first half of 2010 and 2009 were $92.8 million and $71.5 million, respectively, representing approximately 79% and 78%, respectively, of total revenues, an increase of 30% in absolute dollars when comparing sales for the first half of 2010 to sales for the first half of 2009. Sales of 2.4GHz products were $6.5 million and $4.6 million for the second quarter of 2010 and 2009, respectively, representing 11% and 9%, respectively, of our total revenues for the second quarter of 2010 and 2009, representing an increase of 41% in absolute dollars when comparing sales for the second quarter of 2010 to sales for the second quarter of 2009. Sales of 2.4GHz products for the first half of 2010 and 2009 were $13.7 million and $11.4 million, respectively, representing approximately 12% of our total revenues for both periods and an increase of 20% in absolute dollars when comparing sales for the first half of 2010 to the first half of 2009.

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The following table shows the breakdown of revenues for the periods indicated by geographic location (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
United States	$ 1,276	$ 558	$ 2,661	$ 946
Japan	20,596	17,544	39,947	33,351
Europe	2,289	3,856	5,965	7,269
Hong-Kong	31,757	24,256	60,191	41,473
Other	4,928	5,806	8,192	8,895
Total revenues	$ 60,846	$ 52,020	$ 116,956	$ 91,934

Sales to our customers in Hong Kong increased for the second quarter and the first six months of 2010 as compared to the same periods of 2009, representing an increase of 31% and 45%, respectively, in absolute dollars. The increase in our sales to Hong Kong for the comparable periods resulted from (i) an increase in sales to VTech Holdings Ltd. (VTech), representing an increase of 16% and 39% in absolute dollars for the second quarter and the first six months of 2010, respectively, as compared to the same periods of 2009 , and (ii) an increase in sales to CCT Telecom Holdings Ltd. (CCT Telecom), representing an increase of 66% and 81% in absolute dollars for the second quarter and the first six months of 2010, respectively, as compared to the same periods of 2009. Sales to our customers in Japan increased for the second quarter and the first six months of 2010 as compared to the same period of 2009, representing an increase of 17% and 20%, respectively, in absolute dollars. The increase in our sales to Japan for the comparable periods resulted from (i) an increase in sales to Panasonic Communications Co., Ltd. (Panasonic), representing a 24% increase in absolute dollars for both the second quarter and the first six months of 2010, as compared to the same periods of 2009, and (ii) an increase in sales to the Japanese domestic market and to Uniden American Corp. (Uniden), representing an increase of 21% and 15%, respectively, in absolute dollars for the six months of 2010 as compared to the same periods of 2009. Sales to Uniden for the second quarter of 2010 as compared to the same period of 2009 decreased by 2% in absolute dollars and sales to the Japanese domestic market for the same comparable periods increased by 48% in absolute dollars.

As our products are generally incorporated into consumer products sold by our OEM customers, our revenues are affected by seasonal buying patterns of consumer products sold by our OEM customers that incorporate our products. The fourth quarter in any given year is usually the strongest quarter of sales for our OEM customers and, as a result, the third quarter in any given year is usually the strongest quarter for our revenues as our OEM customers request increased shipments of our products in anticipation of the fourth quarter holiday season. By contrast, the first quarter in any given year is usually the weakest quarter for us. This trend can be generally observed from reviewing our quarterly information and results of operations. However, the magnitude of this trend varies annually, and this seasonality trend for the first half of 2010 was positively impacted by the improvement in business conditions.

Significant Customers. VTech is a significant OEM customer based in Hong Kong. Sales to VTech represented 32% and 33% of total revenues for the three months ended June 30, 2010 and 2009, respectively. Sales to VTech represented 34% and 31% of total revenues for the six months ended June 30, 2010 and 2009, respectively.

Sales to CCT Telecom represented 10% and 7% of our total revenues for the three and six months ended June 30, 2010 and 2009, respectively.

The Japanese market and the OEMs that operate in that market are among the largest suppliers of residential wireless products with significant market share in the U.S. market. Revenues derived from sales through our largest distributor, Tomen Electronics Corporation (Tomen Electronics), accounted for 23% and 21% of our total revenues for the three months ended June 30, 2010 and 2009, respectively. Revenues derived from sales through Tomen Electronics accounted for 21% and 23% of our total revenues for the six months ended June 30, 2010 and 2009, respectively.

Tomen Electronics sells our products to a limited number of customers. One customer, Panasonic, has continually accounted for a majority of sales through Tomen Electronics. Sales to Panasonic through Tomen Electronics generated approximately 16% and 15% for the three months ended June 30, 2010 and 2009, respectively. Sales to Panasonic through Tomen Electronics generated approximately 15% of our revenues for both the six months ended June 30, 2010 and 2009. Sales to Uniden through Tomen Electronics or directly to Uniden represented 11% and 13% of our total revenues for the three months ended June 30, 2010 and 2009, respectively. Sales to Uniden represented 12% and 13% of our total revenues for the six months ended June 30, 2010 and 2009, respectively. The loss of Tomen Electronics as a distributor and our inability to obtain a satisfactory replacement in a timely manner would harm our sales and results of operations. Additionally, the loss of Panasonic and/or Uniden and Tomen Electronics inability to thereafter effectively market our products would also harm our sales and results of operations.

In addition to Tomen Electronics and Panasonic, the loss of any of our other significant customers or distributors, including VTech and CCT, or reduced demand for products from, or the reduction in purchasing capability of, one of our other significant customers, could have a material adverse effect on our business, financial condition and results of operations.

Significant Products. Revenues from our DECT products represented 81% and 79% of our total revenues for the three and six months ended June 30, 2010, respectively. Revenues from our DECT products represented 82% and 78% of our total revenues for the three and six months ended June 30, 2009, respectively. Revenues from our 2.4GHz digital products represented 11% and 12% of our total revenues for the three and six months ended June 30, 2010, respectively. Revenues from our 2.4GHz digital products represented 9% and 12% of our total revenues for the three and six months ended June 30, 2009, respectively. We believe that sales of DECT and 2.4GHz products will continue to represent a substantial percentage of our revenues for 2010. We believe that the rapid deployment of new communication access methods, as well as the lack of growth in fixed-line telephony, will reduce our total revenues derived from, and unit sales of, cordless telephony products, including our DECT and 2.4GHz products, for the long term.

Gross Profit. Gross profit as a percentage of revenues was 38.2% for the second quarter of 2010 and 36.7% for the second quarter of 2009. Gross profit as a percentage of revenues was 40.1% for the first half of 2010 and 35.3% for the first half of 2009. The increase in our gross profit for the first six months of 2010 as compared to the same period of 2009 was primarily due to (i) the reversal of a reserve amounting to $2.5 million regarding a potential patent infringement claim that was determined to be no longer needed due to the expiration of the applicable statute of limitations, (ii) an increase in overall revenues, and (iii) increased sales of products with higher gross margins. As gross profit reflects the sale of chips and chipsets that have different margins, changes in the mix of products sold have impacted and will continue to impact our gross profit in future periods. Our gross profit may decrease in the future due to a variety of factors, including the continued decline in the average selling prices of our products, changes in the mix of products sold, our failure to achieve cost reductions, roll-out of new products in any given period, our success in introducing new engineering processes to reduce manufacturing costs, increases in the cost of raw materials such as gold, oil and silicon wafers, and increases in production, assembly and testing costs. Moreover, our suppliers may pass the increase in the cost of raw materials and commodities onto us which would further reduce the gross margins of our products. We cannot guarantee that our ongoing efforts in cost reduction and yield improvements will be successful or that they will keep pace with the anticipated continuing decline in average selling prices of our products. One approach we are using to offset the expected decrease in gross profit is offering our customers bare-die chips that eliminate assembly and testing services in return for lower selling prices to our customers. Other steps we are taking include the implementation of cost improvement plans to reduce testing costs and offering our customers more cost effective products. However, we can provide no assurance that any alternative solutions we provide to our customers will be acceptable to them or that these steps will help us offset the continued decrease in gross margins of our products.

Cost of goods sold consists primarily of costs of wafer manufacturing and fabrication, assembly and testing of integrated circuit devices and related overhead costs, and compensation and associated expenses related to manufacturing and testing support and logistics personnel.

Research and Development Expenses. Our research and development expenses decreased to $13.5 million for the second quarter of 2010 from $13.6 million for the second quarter of 2009. Research and development expenses decreased to $27.0 million for the first six months of 2010 from $27.4 million for the first six months of 2009. The decrease for the first three and six months of 2010 in research and development expenses, as compared to comparable periods during 2009, was mainly due to a decrease in equity-based compensation expenses by $0.3 million and $0.5 million , respectively, for the first three and six months of 2010, as compared to comparable periods during 2009.

Our research and development expenses as a percentage of total revenues were 22% and 26% for the three months ended June 30, 2010 and 2009, respectively, and 23% and 30% for the six months ended June 30, 2010 and 2009, respectively. This decrease in research and development expenses as a percentage of total revenues was due to the increase in absolute dollars of our total revenues.

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Research and development expenses consist mainly of payroll expenses to employees involved in research and development activities, expenses related to tapeout and mask work, subcontracting, labor contractors and engineering expenses, depreciation and maintenance fees related to equipment and software tools used in research and development, and facilities expenses associated with and allocated to research and development activities.

Sales and Marketing Expenses. Our sales and marketing expenses decreased to $4.2 million for the second quarter of 2010 from $4.3 million for the second quarter of 2009. Sales and marketing expenses decreased to $8.7 million for the first six months of 2010 from $8.8 million for the first six months of 2009. The decrease in sales and marketing expenses was mainly attributed to a decrease in payroll expenses due to a lower number of sales and marketing employees in the first six months of 2010, as compared to the same period in 2009.

Our sales and marketing expenses as a percentage of total revenues were 7% and 8% for the three months ended June 30, 2010 and 2009, respectively, and 7% and 10% for the six months ended June 30, 2010 and 2009, respectively. This decrease in sales and marketing expenses as a percentage of total revenues was due to the increase in absolute dollars of our total revenues.

Sales and marketing expenses consist mainly of sales commissions, payroll expenses to direct sales and marketing employees, travel, trade show expenses, and facilities expenses associated with and allocated to sales and marketing activities.

General and Administrative Expenses. Our general and administrative expenses decreased to $3.6 million for the second quarter of 2010 from $3.9 million for the second quarter of 2009. General and administrative expenses decreased to $7.4 million for the first six months of 2010 from $7.7 million for the first six months of 2009. The decrease in general and administrative expenses was mainly attributed to a decrease in legal and accounting expenses in the first six months of 2010, as compared to the same period in 2009 and a decrease in equity-based compensation expenses by $0.1 million for both the three and six months ended June 30 in 2010, as compared to the same periods in 2009.

General and administrative expenses as a percentage of total revenues were 6% and 8% for the three and six months ended June 30, 2010 and 2009, respectively. This decrease in general and administrative expenses as a percentage of total revenues was due to the decrease of those expenses along with the increase in absolute dollars of our total revenues.

Our general and administrative expenses consist mainly of payroll expenses for management and administrative employees, accounting and legal fees, expenses related to investor relations as well as facilities expenses associated with general and administrative activities.

Amortization of Intangible Assets. During the second quarter of 2010, we recorded an expense of approximately $2.5 million, as compared to $3.0 million for the three month ended June 30, 2009, relating to the amortization of intangible assets associated with the Acquisition. During the six months ended June 30, 2010, we recorded an expense of approximately $5.0 million, as compared to $6.0 million for the six month ended June 30, 2009 relating to the amortization of intangible assets associated with the Acquisition. The decrease is consistent with, and is based on, the original amortization schedule determined following the impairment of goodwill and other intangible assets that took place in 2008.

Financial and Other Income, net. Financial and other income, net, for the three months ended June 30, 2010 decreased to $0.3 million from $0.6 million for the three months ended June 30, 2009. Financial and other income, net, for the six months ended June 30, 2010 decreased to $0.7 million from $1.2 million for the six months ended June 30, 2009. The decrease was mainly due to the devaluation of the Euro against the U.S. dollar, which resulted in expenses associated with the exchange rate differences.

Our total cash, cash equivalents and marketable securities were $121.1 million as of June 30, 2010, compared to $110.7 million as of June 30, 2009.

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Provision for Income Taxes. We had no income tax benefit for the first six months of 2010, as compared to income tax benefit of $4.0 million for the first six months of 2009. The income tax benefit for the first six month of 2009 was mainly due to (i) a settlement with the Internal Revenues Service relating to an audit of our U.S. federal income tax returns for 2003 and 2004, and (ii) our ability to carry back our U.S. losses against taxes paid during prior years. Pursuant to the IRS settlement, we recorded a tax benefit of $3.5 million during the three months ended June 30, 2009 as a result of the partial reversal of the tax reserves associated with the 2003 and 2004 tax audit.

During the three and six months ended June 30, 2010, we did not record any net deferred tax assets due to our current estimation of future taxable income, primarily as a result of general adverse market conditions.

DSP Group Ltd., our Israeli subsidiary, was granted Approved Enterprise status by the Israeli government with respect to six separate investment plans. Approved Enterprise status allows our Israeli subsidiary to enjoy a tax holiday for a period of two or four years**,** and a reduced corporate tax rate of 10%-25% (based on the percentage of foreign ownership) for an additional six or eight years, on each investment plan s proportionate share of taxable income. The tax benefits under these investment plans are scheduled to gradually expire by 2015.

On April 1, 2005, an amendment to the Israeli Investment Law came into effect. The amendment revised the criteria for investments qualified to receive tax benefits. An eligible investment program under the amendment qualifies for benefits as a Privileged Enterprise (rather than the previous terminology of Approved Enterprise). Among other things, the amendment provides tax benefits to both local and foreign investors and simplified the approval process. The amendment does not apply to investment programs approved prior to December 31, 2004. The new tax regime applies to new investment programs only. We believe that we are currently in compliance with these requirements. However, if we fail to meet these requirements, we would be subject to corporate tax in Israel at the regular statutory rate (25% for 2010). We also could be required to refund tax benefits, with interest and adjustments for inflation based on the Israeli consumer price index.

As of December 31, 2006, DSP Group Ltd. has elected the status of a Privileged Enterprise under the amendment to the Israeli Investment Law for its seventh plan. The seventh plan entitles DSP Group Ltd. to a corporate tax exemption for a period of two years and to a reduced corporate tax rate of 10%-25% (based on the percentage of foreign ownership) for an additional period of eight years from the first year it has taxable income.

Recently, proposed amendments to the Law for the Encouragement of Capital Investments were submitted to the Israeli government. The proposed amendments recommended, among other things, the cancellation of existing tax benefits mechanism and establishment of a uniform corporate tax that would apply to the entire approved income of an industrial enterprise that would not be contingent on making a qualified investment and make irrelevant the percentage of foreign investment. The implementation of the proposed amendments requires legislative authorization. However, should such legislative changes be approved, these changes may affect our effective tax rate.

In connection with the Acquisition, we received a tax ruling from the Swiss tax authorities with respect to the taxable income generated by our Swiss subsidiary, including the amortization period for tax purposes of goodwill and all other intangible assets acquired in the Acquisition by our Swiss subsidiary. Pursuant to the tax ruling, our Swiss subsidiary is entitled to reduced tax rates of approximately 10% to 15%, depending on the source of income, and tax amortization period of up to 10 years for the goodwill and other intangible assets acquired in the Acquisition by our Swiss subsidiary.

LIQUIDITY AND CAPITAL RESOURCES

Operating Activities. For the first six months of 2010, we generated $1.3 million of cash and cash equivalents from our operating activities. Cash generated from operating activities amounted to $11.5 million for the first six months of 2009. The decrease in cash generated from operating activities for the first six months of 2010, as compared to cash generated by operating activities for the same period in 2009 was mainly as a result of (i) an increase in accounts receivable by $16.0 million during the first six months of 2010, as compared to a decrease in accounts receivable of $8.1 million during the first six months of 2009, and (ii) an increase in inventories by $3.2 million during the first six months of 2010, as compared to a decrease in inventories of $1.5 million during the first six months of 2009. The amount of cash generated from operating activities when comparing the respective periods was offset to some extent by an increase in accounts payables by $7.7 million during the first six months of 2010, as compared to an increase in accounts payables of $1.0 million during the first six months of 2009 and an increase in net profit for the first six months of 2010, as compared to the same period in 2009.

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Investing Activities. We invest excess cash in marketable securities of varying maturity, depending on our projected cash needs for operations, capital expenditures and other business purposes. During the first six months of 2010, we purchased $45.5 million of marketable securities, and short and long term deposits, as compared to $33.5 million during the first six months of 2009. During the first six months of 2010 and 2009, $39.8 million and $22.4 million, respectively, of marketable securities matured, were called by the issuer or were sold.

As of June 30, 2010, the amortized cost of our marketable securities, and short and long term deposits was $89.4 million and their stated market value was $89.7 million, representing an unrealized gain of $0.3 million, which was caused mainly by overall market conditions and interest rate changes.

Our capital equipment purchases for the first six months of 2010, consisting primarily of research and development software tools, computers and other peripheral equipment, engineering test and lab equipment, leasehold improvements, furniture and fixtures, totaled $2.3 million, as compared to $3.0 million for the first six months of 2009.

Financing Activities. During the first six months of 2010, we made no share repurchases. During the first quarter of 2009, we repurchased 4,186,603 shares of our common stock that were issued to NXP in connection with the Acquisition at a purchase price of $4.78 per share for approximately $20,028,000.

We received $0.3 million and nil upon the exercise of employee stock options during the first six months of 2010 and 2009, respectively. We cannot predict cash flows from option exercises for future periods.

As of June 30, 2010, we had cash and cash equivalents totaling approximately $31.4 million and marketable securities of approximately $89.7 million.

Our working capital at June 30, 2010 was approximately $88.7 million, compared to $77.4 as of June 30, 2009. The increase in working capital was mainly due to (i) an increase in accounts receivable as of June 30, 2010, (ii) the reversal of a reserve amounting to $2.5 million regarding a potential patent infringement claim that was determined to be no longer needed due to the expiration of the applicable statute of limitations as of March 31, 2010, and (iii) the reversal of $7.6 million of income tax contingency reserve that was determined to be no longer needed due to the expiration of applicable statute of limitations as of September 30, 2009. We believe that our current cash, cash equivalents, cash deposits and marketable securities will be sufficient to meet our cash requirements for both the short and long term.

Pursuant to authorizations in March 1999, July 2003, October 2004, January 2007 and January 2008, our board of directors authorized a share repurchase program for the repurchase of an aggregate of 14.9 million shares of our common stock. Also in January 2008, our board approved the company s entry into a share repurchase plan, in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934, for the repurchase of 5.0 million of the aggregate shares of our common stock authorized for repurchase, which plan has since expired. As of June 30, 2010, 255,488 shares of our common stock remained authorized for repurchase pursuant to our share repurchase program.

In addition, as part of our business strategy, we may evaluate potential acquisitions of businesses, products and technologies. Accordingly, a portion of our available cash may be used at any time for the acquisition of complementary products or businesses. Such potential transactions may require substantial capital resources, which may require us to seek additional debt or equity financing. We cannot assure you that we will be able to successfully identify suitable acquisition candidates, complete acquisitions, integrate acquired businesses into our current operations, or expand into new markets. Furthermore, we cannot assure you that additional financing will be available to us in any required time frame and on commercially reasonable terms, if at all. See the section of the risk factors entitled We may engage in future acquisitions that could dilute our stockholders equity and harm our business, results of operations and financial condition. for more detailed information.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, as such term is defined in recently enacted rules by the Securities and Exchange Commission, that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk. It is our policy not to enter into interest rate derivative financial instruments, except for hedging of foreign currency exposures discussed below. We do not currently have any significant interest rate risk since we do not have any financial obligations.

The majority of our cash and cash equivalents are invested in high grade certificates of deposits with major U.S., European and Israeli banks. Generally, cash and cash equivalents and short term deposits may be redeemed and therefore minimal credit risk exists with respect to them. Nonetheless, cash deposits with these banks exceed the Federal Deposit Insurance Corporation (FDIC) insurance limits in the U.S. or similar limits in foreign jurisdictions, to the extent such deposits are even insured in such foreign jurisdictions. While we monitor on a systematic basis the cash balances and adjust the balances as appropriate, these balances could be impacted if one or more of the financial institutions with which we deposit our funds fails or is subject to other adverse conditions in the financial or credit markets. To date we have experienced no loss of principal or lack of access to our cash; however, we can provide no assurance that access to our cash will not be affected if the financial institutions that we hold our cash fail or the financial and credit markets fail to recover fully.

We hold an investment portfolio of marketable securities consisting principally of debentures of U.S. corporations, and state and political subdivisions of the U.S. government. We intend, and have the ability, to hold such investments until recovery of any temporary declines in market value or maturity.

Interest rate fluctuations relating to our cash and cash equivalents and within our investment portfolio have not had, and are not currently anticipated to have, a material effect on our financial position on an annual or quarterly basis.

Foreign Currency Exchange Rate Risk. A significant part of our sales and expenses are denominated in U.S. dollars. Part of our expenses in Israel is paid in NIS, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the NIS. Our primary expenses paid in NIS are employee salaries and lease payments on our Israeli facilities. Furthermore, due to the Acquisition, a portion of our expenses for our European operations are paid in the Euro and Swiss Franc, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the Euro and Swiss Franc. Our primary expenses paid in Euro and Swiss Franc are employee salaries, lease and operational payments on our European facilities. To partially protect the company against an increase in value of forecasted foreign currency cash flows resulting from salary and lease payments denominated in NIS during 2010, we instituted a foreign currency cash flow hedging program. The option and forward contracts used are designated as cash flow hedges, as defined by FASB ASC No. 815, Derivatives and Hedging, and are all effective as hedges of these expenses. For more information about our hedging activity, see Note G to the attached Notes to the Condensed Consolidated Financial Statement for the period ended June 30, 2010. An increase in the value of the NIS, Euro and Swiss Franc in comparison to the U.S. dollar could increase the cost of our research and development expenses and general and administrative expenses, all of which could harm our operating profit. Although we currently are using a hedging program to minimize the effects of currency fluctuations relating to the NIS, our hedging position is partial, may not exist at all in the future and may not succeed in minimizing our foreign currency fluctuation risks.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See Management s Discussion and Analysis of Financial Condition and Results of Operations Quantitative and Qualitative Disclosures about Market Risk.

ITEM 4. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 30, 2010.

There has been no change in our internal control over financial reporting that occurred during our most recent fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

From time to time, we may become involved in litigation relating to claims arising from our ordinary course of business. Also, as is typical in the semiconductor industry, we have been and may from time to time be notified of claims that we may be infringing patents or intellectual property rights owned by third parties. We currently believe that there are no claims or actions pending or threatened against us, the ultimate disposition of which would have a material adverse effect on our company.

ITEM 1A. RISK FACTORS.

This Form 10-Q contains forward-looking statements concerning our future products, expenses, revenue, liquidity and cash needs as well as our plans and strategies. These forward-looking statements are based on current expectations and we assume no obligation to update this information. Numerous factors could cause our actual results to differ significantly from the results described in these forward-looking statements, including the following risk factors.

There are no material changes to the Risk Factors described under the title Factors That May Affect Future Performance in our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 other than (1) changes to the Risk Factor below entitled We generate a significant amount of our total revenues from the sale of digital cordless telephony products and our business and operating results may be materially adversely affected if we do not continue to succeed in this highly competitive market or if sales within the overall cordless digital market decreases; (2) changes to the Risk Factor below entitled We rely significantly on revenue derived from a limited number of customers; (3) changes to the Risk Factor below entitled Because our products are components of end products, if OEMs do not incorporate our products into their end products or if the end products of our OEM customers do not achieve market acceptance, we may not be able to generate adequate sales of our products; (4) changes to the Risk Factor below entitled We rely on a primary distributor for a significant portion of our total revenues and the failure of this distributor to perform as expected would materially reduce our future sales and revenues; (5) changes to the Risk Factor below entitled Because our quarterly operating results may fluctuate significantly, the price of our common stock may decline; (6) changes to the Risk Factor below entitled Our revenues, gross margins and profitability may be materially adversely affected by the continued decline in average selling prices of our products and other factors, including increases in assembly and testing expenses, and raw material and commodity costs; (7) changes to the Risk Factor below entitled Because we depend on independent foundries and other third party suppliers to manufacture and test all of our integrated circuit products, we are subject to additional risks that may materially disrupt our business; (8) changes to the Risk Factor below entitled Because we have significant international operations, we may be subject to political, economic and other conditions relating to our international operations that could increase our operating expenses and disrupt our business; (9) changes to the Risk Factor below entitled Our operating results are affected by general economic conditions and the highly cyclical nature of the semiconductor industry; (10) changes to the Risk Factor below entitled Because we have significant operations in Israel, we may be subject to political, economic and other conditions affecting Israel that could increase our operating expenses and disrupt our business; (11) changes to Risk Factor below entitled: The tax benefits available to us under Israeli law require us to meet several conditions, and may be terminated or reduced in the future, which could increase our taxes; (12) changes to the Risk Factor below entitled: Third party claims of infringement or other claims against us could adversely affect our ability to market our products, require us to redesign our products or seek licenses from third parties, and seriously harm our operating results and disrupt our business and (13) changes to the Risk Factor below entitled: We are exposed to fluctuations in currency exchange rates.

We generate a significant amount of our total revenues from the sale of digital cordless telephony products and our business and operating results may be materially adversely affected if we do not continue to succeed in this highly competitive market or if sales within the overall cordless digital market decreases.

Sales of our digital cordless telephony products comprised a majority of our total revenues for the first six months of 2010. Specifically, sales of our DECT, 2.4GHz, 5.8GHz and CoIP products comprised 93% and 92% of our total revenues for the first half of 2010 and 2009, respectively. Revenues from our DECT products represented 79% and 78% of our total revenues for the first half of 2010 and 2009, respectively.

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Any adverse change in the digital cordless market or in our ability to compete and maintain our competitive position in that market would harm our business, financial condition and results of operations. The digital cordless telephony market is extremely competitive and is facing intensive pricing pressures, and we expect that competition and pricing pressures will only increase. Our existing and potential competitors in this market include large and emerging domestic and foreign companies, many of whom have significantly greater financial, technical, manufacturing, marketing, sale and distribution resources and management expertise than we do. It is possible that we may one day be unable to respond to increased pricing competition for digital cordless telephony processors or other products through the introduction of new products or reduction of manufacturing costs. This inability to compete would have a material adverse effect on our business, financial condition and results of operations. Likewise, any significant delays by us in developing, manufacturing or shipping new or enhanced products in this market also would have a material adverse effect on our business, financial condition and results of operations.

In addition, we believe new developments in the residential connectivity market may adversely affect the revenues we derive from our digital cordless telephony products. For example, the projected decline in fixed-line telephony together with the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, may compound the decrease in sales of products using fixed-line telephony. This decrease in demand would reduce our revenues derived from, and unit sales of, our digital cordless telephony products.

We rely significantly on revenue derived from a limited number of customers.

We expect that a limited number of customers, varying in identity from period-to-period, will account for a substantial portion of our revenues in any period. Our four largest customers VTech, Panasonic, Uniden and CCT Telecom accounted for approximately 70% and 66% of our total revenues for the first half of 2010 and 2009, respectively. Sales to VTech represented 34% and 31% of our total revenues for the first half of 2010 and 2009, respectively. Sales to Panasonic represented 15% of our total revenues for both the first half of 2010 and 2009. Sales to Uniden represented 12% and 13% of our total revenues for the first half of 2010 and 2009, respectively. Sales to CCT Telecom represented 10% and 7% of our total revenues for the first half of 2010 and 2009, respectively. Typically, our sales are made on a purchase order basis, and none of our customers has entered into a long-term agreement requiring it to purchase our products. Moreover, we do not typically require our customers to purchase a minimum quantity of our products, and our customers can generally cancel or significantly reduce their orders on short notice without significant penalties. A significant amount of our revenues will continue to be derived from a limited number of large customers. Furthermore, the primary customers for our products are original equipment manufacturers (OEMs) and original design manufacturers (ODMs) in the cordless digital market. This industry is highly cyclical and has been subject to significant economic downturns at various times, particularly in recent periods. These downturns are characterized by production overcapacity and reduced revenues, which at times may affect the financial stability of our customers. Therefore, the loss of one of our major customers, or reduced demand for products from, or the reduction in purchasing capability of, one of our major customers, could have a material adverse effect on our business, financial condition and results of operations.

Because our products are components of end products, if OEMs do not incorporate our products into their end products or if the end products of our OEM customers do not achieve market acceptance, we may not be able to generate adequate sales of our products.

Our products are not sold directly to the end-user; rather, they are components of end products. As a result, we rely upon OEMs to incorporate our products into their end products at the design stage. Once an OEM designs a competitor s product into its end product, it becomes significantly more difficult for us to sell our products to that customer because changing suppliers involves significant cost, time, effort and risk for the customer. As a result, we may incur significant expenditures on the development of a new product without any assurance that an OEM will select our product for design into its own product and without this design win it becomes significantly difficult to sell our products. Moreover, even after an OEM agrees to design our products into its end products, the design cycle is long and may be delayed due to factors beyond our control which may result in the end product incorporating our products not to reach the market until long after the initial design win with the OEM. From initial product design-in to volume production, many factors could impact the timing and/or amount of sales actually realized from the design-in. These factors include, but are not limited to, changes in the competitive position of our technology, our customers financial stability, and our ability to ship products according to our customers schedule. Moreover, the continued uncertainty about the sustainability of the global economic recovery and outlook may further prolong an OEM customer s decision-making process and design cycle.

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Furthermore, we rely on the end products of our OEM customers that incorporate our products to achieve market acceptance. Many of our OEM customers face intense competition in their markets. If end products that incorporate our products are not accepted in the marketplace, we may not achieve adequate sales volume of our products, which would have a negative effect on our results of operations.

We rely on a primary distributor for a significant portion of our total revenues and the failure of this distributor to perform as expected would materially reduce our future sales and revenues.

We sell our products to customers primarily through a network of distributors. Particularly, revenues derived from sales through our Japanese distributor, Tomen Electronics, accounted for 21% and 23% of our total revenues for the first half of 2010 and 2009, respectively. Our future performance will depend, in part, on this distributor to continue to successfully market and sell our products. Furthermore, Tomen Electronics sells our products to a limited number of customers. One customer, Panasonic, has continually accounted for a majority of the sales through Tomen Electronics. Sales to Panasonic through Tomen Electronics generated approximately 15% of our total revenues for both the first half of 2010 and 2009. The loss of Tomen Electronics as our distributor and our inability to obtain a satisfactory replacement in a timely manner would materially harm our sales and results of operations. Additionally, the loss of Panasonic and/or Uniden and Tomen Electronics inability to thereafter effectively market our products would also materially harm our sales.

Because our quarterly operating results may fluctuate significantly, the price of our common stock may decline.

Our quarterly results of operations may vary significantly in the future for a variety of reasons, many of which are outside our control, including the following:

- fluctuations in volume and timing of product orders;
- timing, rescheduling or cancellation of significant customer orders and our ability, as well as the ability of our customers, to manage inventory;
- changes in demand for our products due to seasonal consumer buying patterns and other factors;
- timing of new product introductions by us, including our DECT and XpandR products, and by our customers or competitors;
- changes in the mix of products sold by us or our competitors;
- fluctuations in the level of sales by our OEM customers and other vendors of end products incorporating our products;
- timing and size of expenses, including expenses to develop new products and product improvements and expenses resulting from restructuring activities;
- entry into new markets, including China, Korea and South America;
- our ability to scale our operations in response to changes in demand for our existing products and services or demand for new products requested by our customers;

- mergers and acquisitions by us, our competitors and our existing and potential customers; and

- general economic conditions, including current economic conditions in the United States and worldwide, and the adverse effects on the semiconductor and consumer electronics industries.

Each of the above factors is difficult to forecast and could harm our business, financial condition and results of operations. Also, we sell our products to OEM customers that operate in consumer markets. As a result, our revenues are affected by seasonal buying patterns of consumer products sold by our OEM customers that incorporate our products and the market acceptance of such products supplied by our OEM customers. The fourth quarter in any given year is usually the strongest quarter for sales by our OEM customers in the consumer markets, and thus, our third quarter in any given year is usually the strongest quarter for revenues as our OEM customers request increased shipments of our products in anticipation of the increased activity in the fourth quarter. By contrast, the first quarter in any given year is usually the weakest quarter for us. However, the magnitude of this trend varies annually and this seasonality trend for the first quarter of 2010 was positively impacted by the improvement in business conditions.

Our revenues, gross margins and profitability may be materially adversely affected by the continued decline in average selling prices of our products and other factors, including increases in assembly and testing expenses, and raw material and commodity costs.

We have experienced and will continue to experience a decrease in the average selling prices of our products. Decreasing average selling prices could result in decreased revenues even if the volume of products sold increases. Decreasing average selling prices may also require us to sell our products at much lower gross margin than in the past and reduce profitability. Although we have to date been able to partially offset on an annual basis the declining average selling prices through general operational efficiencies and manufacturing cost reductions by achieving a higher level of product integration and improving our yield percentages, there is no guarantee that our ongoing efforts will be successful or that they will keep pace with the anticipated, continued decline in average selling prices of our products. In addition to the continued decline in the average selling prices of our products, our gross profit may decrease in the future due to other factors, including the roll-out of new products in any given period and the penetration of new markets which may require us to sell products at a lower margin, our failure to introduce new engineering processes and mix of products sold.

Our gross margins also are affected by the product mix. For example, DECT products have lower average gross margins than 2.4GHz products and the increased sales of DECT products lower our gross margins. We anticipate that the shift to DECT 6.0 products in the U.S. market will continue in 2010. This trend will continue to put pressure on our gross margins.

Furthermore, increases in the price of silicon wafers, increases in testing costs and increases in gold, oil and other commodities which may result in increased production costs, mainly assembly and packaging costs may result in a decrease to our gross margins. Moreover, our suppliers may pass the increase in raw materials and commodity costs onto us which would further reduce the gross margin of our products. In addition, as we are a fabless company, global market trends such as over-capacity problems so that there is a shortage of capacity to fulfill our fabrication needs also may increase our raw material costs and thus decrease our gross margin.

Because we have significant international operations, we may be subject to political, economic and other conditions relating to our international operations that could increase our operating expenses and disrupt our business.

Although the majority of end users of the consumer products that incorporate our products are located in the U.S., we are dependent on sales to OEM customers, located outside of the U.S., that manufacture these consumer products. Also, we depend on a network of distributors to sell our products that also are primarily located outside of the U.S. Export sales, primarily consisting of digital cordless telephony products shipped to manufacturers in Europe and Asia, including Japan and Asia Pacific, represented 98% and 99% of our total revenues for the first half of 2010 and 2009, respectively. Furthermore, pursuant to the acquisition of the CIPT Business from NXP, we established new foreign subsidiaries, and currently have material operations, in Germany, Switzerland, Hong Kong and India and employ a number of individuals within those foreign operations. As a result, the occurrence of any negative international political, economic or geographic events, as well as our failure to mitigate the challenges in managing an organization operating in various countries, could result in significant revenue shortfalls and disrupt our workforce within our foreign operations. These shortfalls and disruptions could cause our business, financial condition and results of operations to be harmed. Some of the risks of doing business internationally include:

- unexpected changes in foreign government regulatory requirements;
- fluctuations in the exchange rate for the United States dollar;
- import and export license requirements;
- imposition of tariffs and other barriers and restrictions;

burdens of complying with a variety of foreign laws, treaties and technical standards;

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- uncertainty of laws and enforcement in certain countries relating to the protection of intellectual property;
- difficulty in collecting accounts receivable and longer payment cycles for international customers than existing customers;
- difficulty in staffing and managing foreign operations and maintaining the morale and productivity of employees within foreign operations;
- multiple and possibly overlapping tax structures and potentially adverse tax consequences;
- political and economic instability; and
- changes in diplomatic and trade relationships.

One or more of these factors may have a material adverse effect on our future operations and consequently, on our business, financial conditions and operating results.

Because we depend on independent foundries and other third party suppliers to manufacture and test all of our integrated circuit products, we are subject to additional risks that may materially disrupt our business.

All of our integrated circuit products are manufactured and tested by independent foundries and other third party suppliers. While these foundries and other third party suppliers have been able to adequately meet the demands of our increasing business, we are and will continue to be dependent upon these foundries and third party suppliers to achieve acceptable manufacturing yields, quality levels and costs, and to allocate to us a sufficient portion of their foundry, assembly and test capacity to meet our needs in a timely manner.

While we currently believe we have adequate capacity to support our current sales levels pursuant to our arrangement with our foundries and other third party suppliers, we may encounter capacity shortage issues in the future. In the event of a worldwide shortage in foundry, assembly and/or test capacity, we may not be able to obtain a sufficient allocation of such capacity to meet our product needs or we may incur additional costs to ensure specified quantities of products and services. Over-capacity at the current foundries and other third party suppliers we use, or future foundries or other third party suppliers we may use, to manufacture and test our integrated circuit products may lead to increased operating costs and lower gross margins. In addition, such a shortage could lengthen our products manufacturing and testing cycle and cause a delay in the shipment of our products to our customers. This could ultimately lead to a loss of sales of our products, harm our reputation and competitive position, and our revenues could be materially reduced. Our business could also be harmed if our current foundries or other third party suppliers terminate their relationship with us and we are unable to obtain satisfactory replacements to fulfill customer orders on a timely basis and in a cost-effective manner. Moreover, we do not have long term capacity guarantee agreements with our foundries and with other third party suppliers.

In addition, as TSMC produces a significant portion of our integrated circuit products and ASE tests and assembles a significant portion of them, earthquakes, aftershocks or other natural disasters in Asia, or adverse changes in the political situation in Taiwan, could preclude us from obtaining an adequate supply of wafers to fill customer orders. Such events could harm our reputation, business, financial condition, and results of operations.

Because we depend on NXP to manufacture all of our products for the CIPT Business, we are subject to additional risks that may materially disrupt our business.

As part of the acquisition of the CIPT Business, we entered into a Manufacturing Services Collaboration Agreement (MSCA), as amended, with NXP pursuant to which NXP agreed to provide us with specified manufacturing, pre-testing, assembling and final-testing services relating to the CIPT Business products for up to seven years following the closing of the Acquisition at predetermined costs. Products from the CIPT Business (e.g., DECT and Voice-over-Internet Protocol (VoIP) products) currently represent a substantial portion of our total revenues and are anticipated to continue to generate significant revenues for the company in future periods. While NXP has been able to generally meet our manufacturing demands to date, in some cases NXP has failed to meet its required delivery schedule and may be subject to late delivery penalties as a result. These late deliveries have not adversely impacted our ability to satisfy our customers requirements in a timely manner. Our business also could be materially harmed if NXP fails to achieve acceptable manufacturing yields, quality levels or allocate to us a sufficient portion of its foundry, and assembly and testing capacities to meet our needs for the CIPT Business products due to its capacity constraints, including as a result of the provision of manufacturing services to NXP s internal business units or other third parties. We also may encounter capacity shortage issues in the future if sales for the CIPT Business products continue to increase as we anticipate and NXP cannot sufficiently meet our increasing demands. A capacity shortage could lengthen our CIPT Business products manufacturing cycle, cause a delay in the shipment of our products to our customers, lead to a loss of sales of our products, harm our reputation and competitive position with customers, some of whom we recently established relationships as a result of the acquisition, and our revenues could be materially reduced. Our business would be materially harmed if NXP cannot for any reason fulfill its manufacturing obligations to us under the manufacturing agreement, including due to financial or operational hardships within NXP as a result of the cyclical nature of the semiconductors industry or otherwise, and we are unable to obtain a satisfactory replacement to fulfill customer orders on a timely basis and in a cost-effective manner.

Additionally, in order to enable NXP to provide the specified manufacturing, pre-testing, assembling and final-testing services relating to the CIPT Business products to us, we provide binding capacity commitments to NXP based on a periodic rolling forecast. The manufacturing agreement with NXP provides that we may be subject to monetary penalties if we fail to meet our capacity commitments to NXP that we previously provided to them. If we fail to meet our capacity commitments due to errors in planning logistics, a decrease in forecast from our customers or other reasons, we may be subject to such monetary penalties.

Moreover, in accordance with the MSCA, NXP s manufacturing of certain CIPT Business products would expire in 2010, subject to our ability to extend the period for two consecutive one-year terms under specified circumstances. Upon expiration as a result of our inability to extend the manufacturing period by NXP, we may experience difficulty in finding a suitable replacement manufacturer for these CIPT Business products, which may result in a disruption in product shipments, harm our customer relationships and generally disrupt our business. Even in the event we are able to find a suitable replacement manufacturer, transitioning of manufacturing processes, including re-qualification of CIPT Business Products, may be a difficult process. There are inherent and unforeseen risks and delays associated with the transfer of manufacturing capacities from one facility to another, including production and shipment delays, capacity constraints with the replacement manufacturer, IP incompatibility, logistical and administrative concerns or general difficulties associated with starting a new manufacturing process. Therefore, even with a suitable replacement manufacturer, we may experience a significant disruption in product shipments, harm to our customer relationships and generally a disruption of our business. In addition, we may incur higher manufacturing costs with the replacement manufacturer which may decrease our gross margins and generally adversely affect our results of operations.

Our operating results are affected by general economic conditions and the highly cyclical nature of the semiconductor industry.

During the global downturn that started in the second half of 2008 and continued throughout 2009, general worldwide economic conditions significantly deteriorated, and resulted in decreased consumer confidence and spending, reduced corporate profits and capital spending, adverse business conditions and liquidity concerns. Notwithstanding the improvement in business conditions since the second half of 2009, the current uncertainty about the sustainability of the global economic recovery and outlook continue to make it extremely difficult for our customers, the end-product customers, our vendors and us to accurately forecast and plan future business activities and make reliable projections.

Moreover, we operate within the semiconductor industry which experiences significant fluctuations in sales and profitability. The industry was materially adversely affected by the 2008-2009 global downturn. Downturns in the semiconductor industry are characterized by diminished product demand, excess customer inventories, accelerated erosion of prices and excess production capacity. These factors could cause substantial fluctuations in our revenues and in our results of operations.

If global economic and market conditions remain uncertain or deteriorate, we could experience a material adverse impact on our business and results of operations.

Because the manufacture of our products is complex, the foundries on which we depend may not achieve the necessary yields or product reliability that our business requires.

The manufacture of our products is a highly complex and precise process, requiring production in a highly controlled environment. Changes in manufacturing processes or the inadvertent use of defective or contaminated

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materials by a foundry could adversely affect the foundry s ability to achieve acceptable manufacturing yields and product reliability. If the foundries we currently use do not achieve the necessary yields or product reliability, our ability to fulfill our customers needs could suffer. This could ultimately lead to a loss of sales of our products and have a negative effect on our gross margins and results of operations.

Furthermore, there are other significant risks associated with relying on these third-party foundries, including:

- risks due to the fact that we have reduced control over production cost, delivery schedules and product quality;
- less recourse if problems occur as the warranties on wafers or products supplied to us are limited; and
- increased exposure to potential misappropriation of our intellectual property.

As we depend on independent subcontractors, located in Asia, to assemble and test our semiconductor products, we are subject to additional risks that may materially disrupt our business.

Independent subcontractors, located in Asia, assemble and test our semiconductor products. Because we rely on independent subcontractors to perform these services, we cannot directly control our product delivery schedules or quality levels. We are dependent on these subcontractors to allocate to us a sufficient portion of their capacity to meet our needs in a timely manner. Our future success also depends on the financial viability of our independent subcontractors. If the capital structures of our independent subcontractors weaken, we may experience product shortages, production delays, quality assurance problems, increased manufacturing costs, and/or supply chain disruption. All of this could ultimately lead to a loss of sales of our products, harm our reputation and competitive position, and our revenues could be materially harmed.

Moreover, the economic, market, social, and political situations in countries where some of our independent subcontractors are located are unpredictable, can be volatile, and can have a significant impact on our business because we may not be able to obtain product in a timely manner. Market and political conditions, including currency fluctuation, terrorism, political strife, war, labor disruption, and other factors, including natural or man-made disasters, adverse changes in tax laws, tariff, import or export quotas, power and water shortages, or interruption in air transportation, in areas where our independent subcontractors are located also could have a severe negative impact on our operating capabilities.

In order to sustain the future growth of our business, we must penetrate new markets and our new products must achieve widespread market acceptance.

In order to increase our sales volume and expand our business, we must penetrate new markets and introduce new products. We are exploring opportunities to expand sales of our products to China, Korea and South America. However, there are no assurances that we will gain significant market share in those competitive markets. In addition, many North American, European and Japanese OEMs are moving their manufacturing sites to Southeast Asia as a result of the cyclical nature of manufacturing capacity issues and cost of silicon integrated circuits, the continued decline of average selling prices of chipsets and other industry-wide factors. This trend may cause the mix of our OEM customers to change in the future, thereby further necessitating our need to penetrate new markets. Furthermore, to sustain the future growth of our business, we need to introduce new products as sales of our older products taper off. Moreover, the penetration of new competitive markets and introduction of new products could require us to reduce the sale prices of our products or increase the cost per product and thus reducing our total gross profit in future periods. As an example, we introduced to the market the XpandR platform that integrates DECT and Wi-Fi capabilities to enable multimedia and web-related applications in our future products. Our future growth is dependent on market acceptance and penetration of the XpandR-based products, for which we can provide no assurances. Our inability to penetrate the market or lack of customer acceptance of these products may harm our business and potential growth.

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We are subject to order and shipment uncertainties and if we are unable to accurately predict customer demand, our business may be harmed.

We typically sell products pursuant to purchase orders rather than long-term purchase commitments. Customers can generally cancel, change or defer purchase orders on short notice without incurring a significant penalty. Given current market conditions, we have less ability to accurately predict what or how many products our customers will need in the future. In addition, we have little visibility into and no control of the demand by our customer s customers generally consumer electronics retailers. A decrease in the consumer electronics retailers demand or a build up of their inventory, both of which are out of our control, may cause a cancellation, change or deferral of purchase orders on at short notice by our customers. Anticipating demand is difficult because our customers and their customers face volatile pricing and unpredictable demand for their own products, and are increasingly focused on cash preservation and tighter inventory management. We place orders with our suppliers based on forecasts of our customers demand and, in some instances, may establish buffer inventories to accommodate anticipated demand. Our forecasts are based on multiple assumptions, each of which may introduce error into our estimates. If we overestimate our customers demand or our customers overestimate their demand, we may allocate resources to manufacturing products that we may not be able to sell when we expect to, if at all. As a result, we could hold excess or obsolete inventory, which would reduce our profit margins and adversely affect our financial results. Conversely, if we underestimate our customers demand or our customers underestimate their demand and insufficient manufacturing capacity is available, we could forego revenue opportunities and potentially lose market share and damage our customer relationships.

As a result of the acquisition of NXP s CIPT Business, we now maintain inventory, or hubbing, arrangements with certain of our customers. Pursuant to these arrangements, we deliver products to a customer or a designated third party warehouse based upon the customer s projected needs, but do not recognize product revenue unless and until the customer reports that it has removed our product from the warehouse to incorporate into its end products. Since we own inventory that is physically located in a third party s warehouse, our ability to effectively manage inventory levels may be impaired, causing our total inventory turns to decrease, which could increase expenses associated with excess and obsolete product and negatively impact our cash flow.

We are dependent on a small number of OEM customers, and our business could be harmed by the loss of any of these customers or reductions in their purchasing volumes.

We sell our products to a limited number of OEM customers directly or through a network of distributors. Moreover, many North American, European and Japanese OEMs are moving their manufacturing sites to Southeast Asia, as a result of the cyclical nature of manufacturing capacity issues and cost of silicon integrated circuits, the continued decline of average selling prices of chipsets and other industry-wide factors. In addition, OEMs located in Southeast Asia are growing and gaining competitive strength. As a result, the mix of our OEM customers may change in the future. However, we may not succeed in attracting new customers as these potential customers may have pre-existing relationships with our current or potential competitors. This trend also may promote the consolidation of OEMs located in North America, Europe and Japan with OEMs located in Southeast Asia, which may reduce the number of our potential customers and reduce the volume of chipsets the combined OEM customer may purchase from us. However, as is common in our industry, we typically do not enter into long term contracts with our customers in which they commit to purchase products from us. The loss of any of our OEM customers may have a material adverse effect on our results of operations. To attract new customers, we may be faced with intense price competition, which may affect our revenues and gross margins.

There are several emerging market trends that may challenge our ability to continue to grow our business.

We believe new technological developments in the home connectivity market may adversely affect our operating results. For example, the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, as well as the projected lack of growth in products using fixed-line telephony would reduce our total revenues derived from, and unit sales of, cordless fixed-line telephony products. Our ability to maintain our growth will depend on the expansion of our product lines to capitalize on the emerging access methods and on our success in developing and selling a portfolio of system-on-a-chip solutions that integrate video, voice, data and communication technologies in a wider multimedia market, as well as on our success in developing and selling DECT, XpandR and video products. We cannot assure you that we will succeed in expanding our product lines or portfolio of system-on-a-chip solutions, or that they would receive market acceptance.

Furthermore, there is a growing threat from alternative technologies accelerating the decline of the fixed-line telephony market. This competition comes from mobile telephony, including emerging dual-mode mobile Wi-Fi phones, and other innovative applications, such as Skype and iChat. Given that we derive a significant amount of revenues from chipsets incorporated into fixed-line telephony products, if we are unable to develop new technologies in the face of the decline of this market, our business could be materially adversely affected.

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The possible emerging trend of our OEM customers outsourcing their production may cause our revenue to decline.

We believe there may be an emerging trend of our OEM customers outsourcing their production to third parties. We have invested substantial resources to build relationships with our OEM customers. However the outsourcing companies whom our OEM customers may choose to outsource production may not have prior business relationship with us or may instead have prior or ongoing relationships with our competitors. The emergence of this trend may require us to expend substantial additional resources to build relationships with these outsourcing companies, which would increase our operating expenses. Even if we do expend such resources, there are no assurances that these outsourcing companies will choose to incorporate our chipsets rather than chipsets of our competitors. Our inability to retain an OEM customer once such customer chooses to outsource production would have a material adverse effect on our future revenue.

Because we have significant operations in Israel, we may be subject to political, economic and other conditions affecting Israel that could increase our operating expenses and disrupt our business.

Our principal research and development facilities are located in the State of Israel and, as a result, at June 30, 2010, 270 of our 406 employees were located in Israel, including 185 out of 255 of our research and development personnel. In addition, although we are incorporated in Delaware, a majority of our directors and executive officers are residents of Israel. Although substantially all of our sales currently are being made to customers outside of Israel, we are nonetheless directly influenced by the political, economic and military conditions affecting Israel. Any major hostilities involving Israel, or the interruption or curtailment of trade between Israel and its present trading partners, could significantly harm our business, operating results and financial condition.

Israel s economy has been subject to numerous destabilizing factors, including a period of rampant inflation in the early to mid-1980s, low foreign exchange reserves, fluctuations in world commodity prices, military conflicts and civil unrest. In addition, Israel and companies doing business with Israel have been the subject of an economic boycott by the Arab countries since Israel s establishment. Although they have not done so to date, these restrictive laws and policies may have an adverse impact on our operating results, financial condition or expansion of our business.

Since the establishment of the State of Israel in 1948, a state of hostility has existed, varying in degree and intensity, between Israel and the Arab countries. Although Israel has entered into various agreements with certain Arab countries and the Palestinian Authority, and various declarations have been signed in connection with efforts to resolve some of the economic and political problems in the Middle East, hostilities between Israel and some of its Arab neighbors have recently escalated and intensified. We cannot predict whether or in what manner these conflicts will be resolved. Our results of operations may be negatively affected by the obligation of key personnel to perform military service. In addition, certain of our officers and employees are currently obligated to perform annual reserve duty in the Israel Defense Forces and are subject to being called for active military duty at any time. Although we have operated effectively under these requirements since our inception, we cannot predict the effect of these obligations on the company in the future. Our operations could be disrupted by the absence, for a significant period, of one or more of our officers or key employees due to military service.

The tax benefits available to us under Israeli law require us to meet several conditions, and may be terminated or reduced in the future, which would increase our taxes.

Our facilities in Israel have been granted Approved Enterprise and Beneficiary Enterprise status under the Law for the Encouragement of Capital Investments, 1959, commonly referred to as the Investment Law, and as amended. The Investment Law provides that capital investments in a production facility (or other eligible assets) may be designated as an Approved Enterprise. Under that law, we receive certain tax benefits in Israel. To be eligible for tax benefits, we must meet certain conditions, relating principally to adherence to the investment program filed with the Investment Center of the Israeli Ministry of Industry and Trade and to periodic reporting obligations. Although we believe we have met such conditions in the past, should we fail to meet such conditions in the future, we would be subject to corporate tax in Israel at the standard corporate tax rate (25% for 2010) and could be required to refund tax benefits already received. We cannot assure you that such grants and tax benefits will be continued in the future at their current levels, if at all. The tax benefits under these investment plans are scheduled to gradually expire by 2015. The termination or reduction of certain programs and tax benefits (particularly benefits available to us as a result of the Approved Enterprise status of our facilities and programs) or a requirement to refund tax benefits already received may have a material adverse effect on our business, operating results and financial condition.

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On April 1, 2005, an amendment to the Investment Law came into effect. The amendment revised the criteria for investments qualified to receive tax benefits. An eligible investment program under the amendment will qualify for benefits as a Beneficiary Enterprise (rather than the previous terminology of Approved Enterprise). Among other things, the amendment provides tax benefits to both local and foreign investors and simplifies the approval process. The amendment does not apply to investment programs approved prior to December 31, 2004. The new tax regime applies to new investment programs only. We believe that we are currently in compliance with these requirements. However, if we fail to meet these requirements, we would be subject to corporate tax in Israel at the regular statutory rate (25% for 2010). We also could be required to refund tax benefits, with interest and adjustments for inflation based on the Israeli consumer price index.

Recently, proposed amendments to the Law for the Encouragement of Capital Investments were submitted to the Israeli government. The proposed amendments recommended, among other things, the cancellation of existing tax benefits mechanism and establishment of a uniform corporate tax that would apply to the entire approved income of an industrial enterprise that would not be contingent on making a qualified investment and make irrelevant the percentage of foreign investment. The implementation of the proposed amendments requires legislative authorization. However, should such legislative changes be approved, these changes may affect the Company s effective tax rate.

We may engage in future acquisitions that could dilute our stockholders equity and harm our business, results of operations and financial condition.

We have pursued, and will continue to pursue, growth opportunities through internal development and acquisition of complementary businesses, products and technologies. We are unable to predict whether or when any other prospective acquisition will be completed. The process of integrating an acquired business may be prolonged due to unforeseen difficulties and may require a disproportionate amount of our resources and management s attention. We cannot assure you that we will be able to successfully identify suitable acquisition candidates, complete acquisitions, integrate acquired businesses into our operations, or expand into new markets. Further, once integrated, acquisitions may not achieve comparable levels of revenues, profitability or productivity as our existing business or otherwise perform as expected. The occurrence of any of these events could harm our business, financial condition or results of operations. Future acquisitions may require substantial capital resources, which may require us to seek additional debt or equity financing.

Future acquisitions by us could result in the following, any of which could seriously harm our results of operations or the price of our stock:

- issuance of equity securities that would dilute our current stockholders percentages of ownership;
- large one-time write-offs;
- the incurrence of debt and contingent liabilities;
- difficulties in the assimilation and integration of operations, personnel, technologies, products and information systems of the acquired companies;
- diversion of management s attention from other business concerns;
- contractual disputes;
- risks of entering geographic and business markets in which we have no or only limited prior experience; and
- potential loss of key employees of acquired organizations.

Third party claims of infringement or other claims against us could adversely affect our ability to market our products, require us to redesign our products or seek licenses from third parties, and seriously harm our operating results and disrupt our business.

As is typical in the semiconductor industry, we and our customers have been and may from time to time be notified of claims that we may be infringing patents or intellectual property rights owned by third parties. In addition, patent infringement claims are increasingly being asserted by patent holding companies (so-called patent trolls), which

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do not use technology and whose sole business is to enforce patents against companies, such as us, for monetary gain. Because such patent holding companies do not provide services or use technology, the assertion of our own patents by way of counter-claim may be ineffective. We have received claims that our products infringe upon the proprietary rights of such patent holding companies. In addition, third parties have asserted and may in the future assert intellectual property infringement claims against our customers, which we have agreed in certain circumstances to indemnify and defend against such claims. If litigation becomes necessary to determine the validity of any third party claims, it could result in significant expense to us and could divert the efforts of our technical and management personnel, whether or not the claim has merit and notwithstanding that the litigation is determined in our favor.

If it appears necessary or desirable, we may try to obtain licenses for those patents or intellectual property rights that we are allegedly infringing. Although holders of these types of intellectual property rights commonly offer these licenses, we cannot assure you that licenses will be offered or that the terms of any offered licenses will be acceptable to us. Our failure to obtain a license for key intellectual property rights from a third party for technology used by us could cause us to incur substantial liabilities, suspend the manufacturing of products utilizing the technology or damage the relationship with our customers. Alternatively, we could be required to expend significant resources to develop non-infringing technology. We cannot assure you that we would be successful in developing non-infringing technology. The occurrence of any of these events could harm our business, financial condition or results of operations.

We may not be able to adequately protect or enforce our intellectual property rights, which could harm our competitive position.

Our success and ability to compete is in part dependent upon our internally-developed technology and other proprietary rights, which we protect through a combination of copyright, trademark and trade secret laws, as well as through confidentiality agreements and licensing arrangements with our customers, suppliers, employees and consultants. In addition, we have filed a number of patents in the United States and in other foreign countries with respect to new or improved technology that we have developed. However, the status of any patent involves complex legal and factual questions, and the breadth of claims allowed is uncertain. Accordingly, we cannot assure you that any patent application filed by us will result in a patent being issued, or that the patents issued to us will not be infringed by others. Also, our competitors and potential competitors may develop products with similar technology or functionality as our products, or they may attempt to copy or reverse engineer aspects of our product line or to obtain and use information that we regard as proprietary. Moreover, the laws of certain countries in which our products are or may be developed, manufactured or sold, including Hong Kong, Japan, Korea and Taiwan, may not protect our products and intellectual property rights to the same extent as the laws of the United States. Policing the unauthorized use of our products is difficult and may result in significant expense to us and could divert the efforts of our technical and management personnel. Even if we spend significant resources and efforts to protect our intellectual property, we cannot assure you that we will be able to prevent misappropriation of our technology. Use by others of our proprietary rights could materially harm our business and expensive litigation may be necessary in the future to enforce our intellectual property rights.

Because our products are complex, the detection of errors in our products may be delayed, and if we deliver products with defects, our credibility will be harmed, the sales and market acceptance of our products may decrease and product liability claims may be made against us.

Our products are complex and may contain errors, defects and bugs when introduced. If we deliver products with errors, defects or bugs, our credibility and the market acceptance and sales of our products could be significantly harmed. Furthermore, the nature of our products may also delay the detection of any such error or defect. If our products contain errors, defects and bugs, then we may be required to expend significant capital and resources to alleviate these problems. This could result in the diversion of technical and other resources from our other development efforts. Any actual or perceived problems or delays may also adversely affect our ability to attract or retain customers. Furthermore, the existence of any defects, errors or failures in our products could lead to product liability claims or lawsuits against us or against our customers. We generally provide our customers with a standard warranty for our products, generally lasting one year from the date of purchase. Although we attempt to limit our liability for product defects to product replacements, we may not be successful, and customers may sue us or claim liability for the defective products. A successful product liability claim could result in substantial cost and divert management s attention and resources, which would have a negative impact on our financial condition and results of operations.

We are exposed to the credit risk of our customers and to credit exposures in weakened markets, which could result in material losses.

Most of our sales are on an open credit basis. Because of current conditions in the global economy, our exposure to credit risks relating to sales on an open credit basis has increased. We expect demand for enhanced open credit terms, for example, longer payment terms, to continue and believe that such arrangements are a competitive factor in obtaining business. Although we monitor and attempt to mitigate credit risks, including through insurance coverage from time to time, there can be no assurance that our efforts will be effective. Moreover, even if we attempt to mitigate credit risks through insurance coverage, such coverage may not be sufficient to cover all of our losses and we would be subject to a deductible under any insurance coverage. Furthermore, as part of the acquisition of the CIPT Business from NXP, we increased our customer base with new customers in Europe and Asia. As a result, our future credit risk exposure may increase. Although any losses to date relating to credit exposure of our customers have not been material, future losses, if incurred, could harm our business and have a material adverse effect on our operating results and financial condition. Moreover, the loss of a customer due to its financial default also could harm our future business and potential growth.

Our executive officers and key personnel are critical to our business, and because there is significant competition for personnel in our industry, we may not be able to attract and retain such qualified personnel.

Our success depends to a significant degree upon the continued contributions of our executive management team, and our technical, marketing, sales customer support and product development personnel. The loss of significant numbers of such personnel could significantly harm our business, financial condition and results of operations. We do not have any life insurance or other insurance covering the loss of any of our key employees. Because our products are specialized and complex, our success depends upon our ability to attract, train and retain qualified personnel, including qualified technical, marketing and sales personnel. However, the competition for personnel is intense and we may have difficulty attracting and retaining such personnel.

We may have exposure to additional tax liabilities as a result of our foreign operations.

We are subject to income taxes in both the United States and various foreign jurisdictions. In addition to our significant operations in Israel, pursuant to the acquisition of the CIPT Business from NXP, we currently have operations in Germany, Switzerland, Hong Kong and India. Significant judgment is required in determining our worldwide provision for income taxes and other tax liabilities. In the ordinary course of a global business, there are many intercompany transactions and calculations where the ultimate tax determination is uncertain. We are regularly under audit by tax authorities. Our intercompany transfer pricing may be reviewed by the U.S. Internal Revenue Service and by foreign tax jurisdictions. Although we believe that our tax estimates are reasonable, due to the complexity of our corporate structure, the multiple intercompany transactions and the various tax regimes, we cannot assure you that a tax audit or tax dispute to which we may be subject will result in a favorable outcome for us. If taxing authorities do not accept our tax positions and impose higher tax rates on our foreign operations, our overall tax expenses could increase.

Legislative action in the United States could materially and adversely affect us from a tax perspective.

Legislative action may be taken by the U.S. Congress which, if ultimately enacted, would adversely affect our effective tax rate and/or require us to take further action, at potentially significant expense, to seek to preserve our effective tax rate. In 2009 and 2010, President Obama s administration announced budgets, which included proposed future tax legislation that could substantially modify the rules governing the U.S. taxation of certain non-U.S. affiliates. These potential changes include, but are not limited to, curbing the deferral of U.S. taxation of certain foreign earnings and limiting the ability to use foreign tax credits. Many details of the proposal remain unknown, and any legislation enacting such modifications would require Congressional support and approval. We cannot predict the outcome of any specific legislative proposals. However, if any of these proposals are enacted into law, they could significantly impact our effective tax rate.

We are exposed to fluctuations in currency exchange rates.

A significant portion of our business is conducted outside the United States. Export sales to manufacturers in Europe and Asia, including Japan and Asia Pacific, represented 98% of our total revenues for the first half of 2010. Although most of our revenue and expenses are transacted in U.S. dollars, we may be exposed to currency exchange fluctuations in the future as business practices evolve and we are forced to transact business in local currencies.

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Moreover, part of our expenses in Israel are paid in Israeli currency, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the New Israeli Shekel (NIS) and to economic pressures resulting from Israel s general rate of inflation. Our primary expenses paid in NIS are employee salaries and lease payments on our Israeli facilities. Furthermore, due to the acquisition of the CIPT Business from NXP, a portion of our expenses for our European operations are paid in the Euro and Swiss Franc, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the Euro and Swiss Franc. Our primary expenses paid in the Euro and Swiss Franc are employee salaries, lease and operational payments on our European facilities. As a result, an increase in the value of the NIS, Euro and Swiss Franc in comparison to the U.S. dollar, which has been the trend in most of the year due to the devaluation of the U.S. dollar, could increase the cost of our technology development, research and development expenses and general and administrative expenses, all of which could harm our operating profit. From time to time, we use derivative instruments in order to minimize the effects of currency fluctuations, but our hedging positions may be partial, may not exist at all in the future or may not succeed in minimizing our foreign currency fluctuation risks. Our financial results may be harmed if the trend relating to the devaluation of the U.S. dollars continues for an extended period.

Because the markets in which we compete are subject to rapid changes, our products may become obsolete or unmarketable.

The markets for our products and services are characterized by rapidly changing technology, short product life cycles, evolving industry standards, changes in customer needs, demand for higher levels of integration, growing competition and new product introductions. Our future growth is dependent not only on the continued success of our existing products but also successful introduction of new products. Our ability to adapt to changing technology and anticipate future standards, and the rate of adoption and acceptance of those standards, will be a significant factor in maintaining or improving our competitive position and prospects for growth. If new industry standards emerge, our products or our customers products could become unmarketable or obsolete, and we could lose market share. We may also have to incur substantial unanticipated costs to comply with these new standards. If our product development and improvements take longer than planned, the availability of our products would be delayed. Any such delay may render our products obsolete or unmarketable, which would have a negative impact on our ability to sell our products and our results of operations.

Because of changing customer requirements and emerging industry standards, we may not be able to achieve broad market acceptance of our products. Our success is dependent, in part, on our ability to:

- successfully develop, introduce and market new and enhanced products at competitive prices and in a timely manner in order to meet changing customer needs;
- convince leading OEMs to select our new and enhanced products for design into their own new products;
- respond effectively to new technological changes or new product announcements by others;
- effectively use and offer leading technologies; and
- maintain close working relationships with our key customers.

There are no assurances that we will be successful in these pursuits, that the demand for our products will continue or that our products will achieve market acceptance. Our failure to develop and introduce new products that are compatible with industry standards and that satisfy customer requirements, and the failure of our products to achieve broad market acceptance, could have a negative impact on our ability to sell our products and our results of operations.

Because the markets in which we compete are highly competitive, and many of our competitors have greater resources than we do, we cannot be certain that our products will be accepted in the marketplace or capture market share.

The markets in which we operate are extremely competitive and characterized by rapid technological change, evolving standards, short product life cycles and price erosion. We expect competition to intensify as current competitors expand their product offerings and new competitors enter the market. Given the highly competitive environment in which we operate, we cannot be sure that any competitive advantages enjoyed by our current products would be sufficient to establish and sustain our new products in the market. Any increase in price or competition could result in the erosion of our market share, to the extent we have obtained market share, and would have a negative impact on our financial condition and results of operations.

In each of our business activities, we face current and potential competition from competitors that have significantly greater financial, technical, manufacturing, marketing, sales and distribution resources and management expertise than we do. These competitors may also have pre-existing relationships with our customers or potential customers. Further, in the event of a manufacturing capacity shortage, these competitors may be able to manufacture products when we are unable to do so. Our principal competitors in the cordless market include Lantiq (formerly Infineon) and SiTel (formerly the DECT division of National Semiconductor). Our principal competitors in the VoIP market include Broadcom, Lantiq, SiTel, Texas Instruments and new Taiwanese IC vendors. Our principal competitors in the multimedia market include Wi-Fi and multimedia application processor IC vendors like Atheros, Broadcom, CSR, Freescale, Intel, Marvel, Ralink, Samsung and Texas Instruments.

As discussed above, various new developments in the home residential market may require us to enter into new markets with competitors that have more established presence, and significantly greater financial, technical, manufacturing, marketing, sales and distribution resources and management expertise than we do. The expenditure of greater resources to expand our current product lines and develop a portfolio of system-on-a-chip solutions that integrate video, voice, data and communication technologies in a wider multimedia market may increase our operating expenses and reduce our gross profit. We cannot assure you that we will succeed in developing and introducing new products that are responsive to market demands.

An unfavorable government review of our federal income tax returns or changes in our effective tax rates could adversely affect our operating results.

Our future effective tax rates could be adversely affected by earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws, regulations, accounting principles or interpretations thereof. In addition, we are subject to the periodic examination of our income tax returns by the IRS and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. The outcomes from these examinations may have an adverse effect on our operating results and financial condition.

We may experience difficulties in transitioning to smaller geometry process technologies or in achieving higher levels of design integration, which may result in reduced manufacturing yields, delays in product deliveries and increased expenses.

A growing trend in our industry is the integration of greater semiconductor content into a single chip to achieve higher levels of functionality. In order to remain competitive, we must achieve higher levels of design integration and deliver new integrated products on a timely basis. This will require us to expend greater research and development resources, and may require us to modify the manufacturing processes for some of our products, to achieve greater integration. We periodically evaluate the benefits, on a product-by-product basis, of migrating to smaller geometry process technologies to reduce our costs. Although this migration to smaller geometry process technologies has helped us to offset the declining average selling prices of our products, this effort may not continue to be successful. Also, because we are a fabless semiconductor company, we depend on our foundries to transition to smaller geometry processes successfully. We cannot assure you that our foundries will be able to effectively manage the transition. In case our foundries or we experience significant delays in this transition or fail to efficiently implement this transition, our business, financial condition and results of operations could be materially and adversely affected.

Our certificate of incorporation and bylaws contain anti-takeover provisions that could prevent or discourage a third party from acquiring us.

Our certificate of incorporation and bylaws contain provisions that may prevent or discourage a third party from acquiring us, even if the acquisition would be beneficial to our stockholders. We have a staggered board, which means it will generally take two years to change the composition of our board. Our board of directors also has the authority to fix the rights and preferences of shares of our preferred stock and to issue such shares without a stockholder vote. It is possible that these provisions may prevent or discourage third parties from acquiring us, even if the acquisition would be beneficial to our stockholders. In addition, these factors may also adversely affect the market price of our common stock, and the voting and other rights of the holders of our common stock.

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Our stock price may be volatile so you may not be able to resell your shares of our common stock at or above the price you paid for them.

Announcements of developments related to our business, announcements by competitors, quarterly fluctuations in our financial results, changes in the general conditions of the highly dynamic industry in which we compete or the national economies in which we do business, and other factors could cause the price of our common stock to fluctuate, perhaps substantially. In addition, in recent years, the stock market has experienced extreme price fluctuations, which have often been unrelated to the operating performance of affected companies. These factors and fluctuations could have a material adverse effect on the market price of our common stock.

ITEM 6. EXHIBITS.

Exhibit 10.36	Amendment to Employment Agreement by and among DSP Group, Inc., DSP Group, Ltd. and Eli Ayalon, as amended, effective as of May 24, 2010 (filed as Exhibit 10.1 to Registrant s Current Report on 8-K filed on May 28, 2010, and incorporated herein by reference).
Exhibit 10.37	Amendment to Employment Agreement by and between DSP Group, Ltd. and Eli Fogel, effective as of July 8, 2010. (filed as Exhibit 10.1 to Registrant s Current Report on 8-K filed on July 9, 2010, and incorporated herein by reference).
Exhibit 31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 31.2	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.1	Certification of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.2	Certification of the Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

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.

	DSP GROUP, INC.
	(Registrant)
Date: August 9, 2010	By: /s/ Dror Levy Dror Levy, Chief Financial Officer and Secretary
	(Principal Financial Officer and Principal Accounting Officer)