

AMBARELLA INC
Form 10-Q
June 12, 2013
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended April 30, 2013

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: 001-35667

AMBARELLA, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: AMBARELLA INC - Form 10-Q

Cayman Islands
(State or other jurisdiction of
incorporation or organization)

3101 Jay Street

Santa Clara, California
(Address of principal executive offices)

98-0459628
(I.R.S. Employer
Identification No.)

95054
(Zip Code)

(408) 734-8888
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of ordinary shares, \$0.00045 par value, of the Registrant, outstanding as of April 30, 2013 was 27,258,434 shares.

Table of Contents

AMBARELLA, INC.

QUARTERLY REPORT ON FORM 10-Q

TABLE OF CONTENTS

| | Page |
|---|-------------|
| <u>PART I. FINANCIAL INFORMATION</u> | 3 |
| Item 1. <u>Financial Statements</u> | 3 |
| <u>Unaudited Condensed Consolidated Balance Sheets at April 30, 2013 and January 31, 2013</u> | 3 |
| <u>Unaudited Condensed Consolidated Statements of Operations for the three months ended April 30, 2013 and 2012</u> | 4 |
| <u>Unaudited Condensed Consolidated Statements of Cash Flows for the three months ended April 30, 2013 and 2012</u> | 5 |
| <u>Notes to Unaudited Condensed Consolidated Financial Statements</u> | 6 |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 23 |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 34 |
| Item 4. <u>Controls and Procedures</u> | 34 |
| <u>PART II. OTHER INFORMATION</u> | 35 |
| Item 1. <u>Legal Proceedings</u> | 35 |
| Item 1A. <u>Risk Factors</u> | 35 |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 64 |
| Item 6. <u>Exhibits</u> | 64 |
| <u>Signatures</u> | 65 |

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. Financial Statements****AMBARELLA, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(in thousands, except share and per share data)****(unaudited)**

| | April 30, 2013 | January 31, 2013 |
|--|-------------------|---------------------|
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 104,277 | \$ 100,494 |
| Accounts receivable, net | 23,467 | 20,153 |
| Inventories | 9,325 | 8,918 |
| Restricted cash | 3 | 3 |
| Deferred tax assets, current | 1,219 | 1,220 |
| Prepaid expenses and other current assets | 1,839 | 2,360 |
| Total current assets | 140,130 | 133,148 |
| Property and equipment, net | 2,976 | 2,536 |
| Deferred tax assets, non-current | 1,079 | 938 |
| Other assets | 2,054 | 1,981 |
| Total assets | \$ 146,239 | \$ 138,603 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable | 9,987 | 6,674 |
| Accrued liabilities | 11,184 | 14,419 |
| Income taxes payable | 171 | 286 |
| Deferred revenue, current | 4,024 | 3,451 |
| Total current liabilities | 25,366 | 24,830 |
| Other long-term liabilities | 1,470 | 1,441 |
| Total liabilities | 26,836 | 26,271 |
| Commitments and contingencies (Note 10) | | |
| Shareholders equity: | | |
| Preference shares, \$0.00045 par value per share, 20,000,000 shares authorized and no shares issued and outstanding at April 30, 2013 and January 31, 2013, respectively | | |
| Ordinary shares, \$0.00045 par value per share, 200,000,000 shares authorized at April 30, 2013 and January 31, 2013, respectively; 27,258,434 shares issued and outstanding at April 30, 2013; 27,035,074 shares issued and outstanding at January 31, 2013 | 12 | 12 |

Edgar Filing: AMBARELLA INC - Form 10-Q

| | | |
|--|----------------|----------------|
| Additional paid-in capital | 94,241 | 91,911 |
| Retained earnings | 25,150 | 20,409 |
| Total shareholders' equity | 119,403 | 112,332 |
| | | |
| Total liabilities and shareholders' equity | \$ 146,239 | \$ 138,603 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents**AMBARELLA, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(in thousands, except share and per share data)****(unaudited)**

| | Three Months Ended April 30, | |
|---|---|-----------------|
| | 2013 | 2012 |
| Revenue | \$ 33,941 | \$ 25,921 |
| Cost of revenue | 12,248 | 7,516 |
| Gross profit | 21,693 | 18,405 |
| Operating expenses: | | |
| Research and development | 11,317 | 11,473 |
| Selling, general and administrative | 5,157 | 4,025 |
| Total operating expenses | 16,474 | 15,498 |
| Income from operations | 5,219 | 2,907 |
| Other expense | (5) | (2) |
| Income before income taxes | 5,214 | 2,905 |
| Provision for income taxes | 473 | 303 |
| Net income | \$ 4,741 | \$ 2,602 |
| Net income per share attributable to ordinary shareholders: | | |
| Basic | \$ 0.17 | \$ 0.08 |
| Diluted | \$ 0.16 | \$ 0.07 |
| Weighted-average shares used to compute net income per share attributable to ordinary shareholders: | | |
| Basic | 27,056,932 | 7,519,360 |
| Diluted | 29,066,062 | 9,031,710 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents**AMBARELLA, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(unaudited, in thousands)**

| | Three Months Ended April 30, | |
|---|---|---------------|
| | 2013 | 2012 |
| Cash flows from operating activities: | | |
| Net income | \$ 4,741 | \$ 2,602 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation of property and equipment | 194 | 176 |
| Loss on disposal of long-lived assets | 3 | |
| Amortization of other intangible assets | | 135 |
| Stock-based compensation | 1,606 | 943 |
| Net excess income tax benefits associated with stock-based compensation | (91) | |
| Change in value of warrants | | (10) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (3,314) | 555 |
| Inventories | (407) | (830) |
| Prepaid expenses and other current assets | 521 | 110 |
| Deferred tax assets | (139) | 1 |
| Other assets | (73) | 22 |
| Accounts payable | 3,313 | (808) |
| Accrued liabilities | (3,687) | 319 |
| Income taxes payable | (24) | 205 |
| Deferred revenue | 573 | (2,640) |
| Net cash provided by operating activities | 3,216 | 780 |
| Cash flows from investing activities: | | |
| Restricted Cash | | (8) |
| Purchase of property and equipment | (579) | (147) |
| Net cash used in investing activities | (579) | (155) |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options, warrants, and employee stock purchase plan withholding, net of repurchase of stock options | 1,080 | 125 |
| Payment for initial public offering cost | (25) | |
| Net excess income tax benefits associated with stock-based compensation | 91 | |
| Net cash provided by financing activities | 1,146 | 125 |
| Net increase in cash and cash equivalents | 3,783 | 750 |
| Cash and cash equivalents at beginning of period | 100,494 | 58,944 |
| Cash and cash equivalents at end of period | \$ 104,277 | \$ 59,694 |

Supplemental disclosure of cash flow information:

Edgar Filing: AMBARELLA INC - Form 10-Q

| | | | | |
|--|----|-----|----|----|
| Cash paid for income taxes | \$ | 157 | \$ | 99 |
| Supplemental disclosure of noncash investing activities: | | | | |
| Increase in accrued liabilities related to non-monetary assets purchases | \$ | 181 | \$ | 48 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

AMBARELLA, INC.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Organization and Summary of Significant Accounting Policies

Organization

Ambarella, Inc. (the Company) was incorporated in the Cayman Islands on January 15, 2004. The Company is a developer of semiconductor processing solutions for video that enable high-definition video capture, sharing and display. The Company combines its processor design capabilities with its expertise in video and image processing, algorithms and software to provide a technology platform that is designed to be easily scalable across multiple applications and enable rapid and efficient product development. The Company's system-on-a-chip, or SoC, designs fully integrate high-definition video processing, image processing, audio processing and system functions onto a single chip, delivering exceptional video and image quality, differentiated functionality and low power consumption.

The Company sells its solutions to leading original design manufacturers, or ODMs, and original equipment manufacturers, or OEMs, globally.

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company in accordance with the instructions to Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and, therefore, do not include all information and notes normally provided in audited financial statements. The accounting policies are described in the Notes to Consolidated Financial Statements in the Annual Report on Form 10-K for the 2013 fiscal year filed with the SEC on April 4, 2013 (the Form 10-K) and updated, as necessary, in this Form 10-Q. The year-end condensed consolidated balance sheet data presented for comparative purposes was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles in the United States (U.S. GAAP). In the opinion of management, all adjustments (consisting of normal recurring accruals and other adjustments) considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of, nor comparable to, the results of operations for any other interim period or for a full fiscal year. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes contained in the Form 10-K.

Basis of Consolidation

The Company's fiscal year ends on January 31. The condensed consolidated financial statements of the Company and its subsidiaries have been prepared in conformity with U.S. GAAP. All intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reported periods. Actual results could differ from those estimates.

Table of Contents

On an ongoing basis, management evaluates its estimates and assumptions, including those related to (i) the collectability of accounts receivable; (ii) write down for excess and obsolete inventories; (iii) the estimated useful lives of long-lived assets; (iv) impairment of long-lived assets and financial instruments; (v) warranty obligations; (vi) the valuation of equity instruments; (vii) the realization of tax assets and estimates of tax liabilities, including reserves for uncertain tax positions; and (viii) the recognition and disclosure of contingent liabilities. These estimates and assumptions are based on historical experience and on various other factors which the Company believes to be reasonable under the circumstances. The company may engage third-party valuation specialists to assist with estimates related to the valuation of financial instruments and assets associated with various contractual arrangements, and the valuation of preference and ordinary shares. Such estimates often require the selection of appropriate valuation methodologies and significant judgment. Actual results could differ from these estimates under different assumptions or circumstances.

Concentration of Risk

The Company's products are manufactured, assembled and tested by third-party contractors located primarily in Asia. The Company does not have long-term agreements with these contractors. A significant disruption in the operations of one or more of these contractors would impact the production of the Company's products which could have a material adverse effect on its business, financial condition and results of operations.

A substantial portion of the Company's revenue is derived from sales through its logistics provider, Wintech Microelectronics Co., Ltd., or Wintech, which serves as the Company's non-exclusive sales representative in all of Asia other than Japan, and through one large direct ODM customer, Chicony Electronics Co., Ltd., or Chicony. Termination of the relationships with these two customers could result in a temporary or permanent loss of revenue and obligation to repurchase unsold product. Furthermore, any credit issues from these two customers could impair their abilities to make timely payment to the Company. See Note 11 for additional information regarding concentration with these two customers.

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and accounts receivable. The Company places its cash primarily in checking and money market accounts with reputable financial institutions. Deposits held with these financial institutions may exceed the amount of insurance provided on such deposits. The Company has not experienced any material losses on deposits of its cash. The Company does not hold or issue financial instruments for trading purposes.

The Company performs ongoing credit evaluations of each of its customers and adjusts credit limits based upon payment history and the customer's credit worthiness. The Company regularly monitors collections and payments from its customers.

Table of Contents

Foreign Currency Transactions

The U.S. dollar is the functional currency for the Company and its subsidiaries. Monetary assets and liabilities denominated in non-U.S. currencies are re-measured to U.S. dollars using current exchange rates in effect at the balance sheet date. Nonmonetary assets and liabilities are re-measured to U.S. dollars using historical exchange rates. Monetary and other accounts are re-measured to U.S. dollars using average exchange rates in effect during each period. Gains or losses from foreign currency remeasurement are included in other expense in the condensed consolidated statements of operations, and, to date, have not been material.

Cash, Cash Equivalents and Short-Term Investments

The Company considers all highly liquid investments with maturities of less than three months at the time of purchase to be cash equivalents. Investments with maturities at the time of acquisition greater than three months are classified as short-term investments as these are considered as available-for-sale in current operations. There were no cash equivalents or short-term investments as of April 30, 2013 and January 31, 2013, respectively.

Cost Method Investment

The Company accounts for its investment in a privately held company under the cost method and reports the investment in other assets in the condensed consolidated balance sheets. The Company monitors the carrying value of the investment and records a reduction in carrying value when a decline in value is deemed to be other than temporary. To date, the Company has not recognized any impairment losses related to this investment.

Trade Accounts Receivable and Allowances for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount and do not include finance charges. The Company performs ongoing credit evaluation of its customers and generally requires no collateral. The Company assesses the need for allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments by considering factors such as historical collection experience, credit quality, aging of the accounts receivable balances and current economic conditions that may affect a customer's ability to pay. There were no write-offs of accounts receivable for the three months ended April 30, 2013 and 2012, respectively. There was no allowance for doubtful accounts recorded as of April 30, 2013 and January 31, 2013, respectively.

Fair Market Value of Financial Instruments

The carrying amounts reflected in the condensed consolidated balance sheets for cash, accounts receivable, accounts payable, accrued liabilities and other current liabilities, approximate fair value due to the short-term nature. The fair value of outstanding warrants to purchase redeemable convertible preference shares converted into warrants to purchase ordinary shares is described in Note 6.

Inventories

The Company records inventories at the lower of cost or market. The cost includes materials and other production costs and is computed using standard cost on a first-in, first-out basis. Inventory reserves are recorded for estimated obsolescence or unmarketable inventories based on forecast of future demand and market conditions. If actual market conditions are less favorable than projected, or if future demand for the Company's products decrease, additional inventory write-downs may be required. Once inventory is written down, a new accounting basis has been established and, accordingly, any associated reserve is not reversed until the inventory sold or scrapped. The Company has not recognized any material inventory loss to date.

Table of Contents

Property and Equipment

Property and equipment are stated at cost and depreciated using the straight-line method over the estimated useful life of three years for computer equipment, computer software, machinery, equipment and furniture and fixtures. Leasehold improvements are amortized over the shorter of the lease term or their estimated useful lives. Repairs and maintenance are charged to expense as incurred.

Intangible Assets

Technology licenses purchased from third parties and that can be used in alternative research and development projects are capitalized as intangible assets. Capitalized costs are amortized over an estimated economic useful life under a straight-line method and recorded as research and development expenses.

Impairment of Long-Lived Assets

The Company records long-lived assets at cost and evaluates them for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Events or changes in circumstances that may indicate that an asset is impaired include significant decreases in the market value of an asset, significant underperformance relative to expected historical or projected future results of operations, a change in the extent or manner in which an asset is utilized, significant declines in the estimated fair value of the overall Company for a sustained period, shifts in technology, loss of key management or personnel, changes in the Company's operating model or strategy and competitive forces. When the sum of the expected future undiscounted cash flows expected to be generated by the related asset group is less than its carrying amount, an impairment loss would be recognized. Should impairment exist, the impairment loss would be measured based on the excess of the carrying amount of the asset over the asset's estimated fair value. There has been no occurrence of events to date that would trigger an impairment analysis. As such, no impairment charge has been recognized as of April 30, 2013.

Revenue Recognition

The Company generates revenue from the sale of its SoCs to OEMs or ODMs, either directly or through logistics providers. Revenue from sales directly to OEMs and ODMs is recognized upon shipment provided persuasive evidence of an arrangement exists, legal title to the products and risk of ownership have transferred, the fee is fixed or determinable, and collection of the resulting receivable is reasonably assured. The Company provides its logistics providers with the right to return excess levels of inventory and to future price adjustments. Given the inability to reasonably estimate these price changes and returns, revenue and costs related to shipments to logistics providers are deferred until the Company has received notification from its logistics providers that they have sold the Company's products. Information reported by the Company's logistics providers includes product resale price, quantity and end customer shipment information as well as remaining inventory on hand. At the time of shipment to a logistics provider, the Company records a trade receivable as there is a legally enforceable right to receive payment, reduces inventory for the value of goods shipped as legal title has passed to the logistics provider and defers the related margin as deferred revenue in the condensed consolidated balance sheets. Any price adjustments are recorded as a reduction to deferred revenue at the time the adjustments are agreed upon.

Table of Contents

Arrangements with certain OEM customers provide for pricing that is dependent upon the end products into which the Company's SoCs are used. These arrangements may also entitle the Company to a share of the product margin ultimately realized by the OEM. The minimum guaranteed amount of revenue related to the sale of products subject to these arrangements is recognized when all other elements of revenue recognition are met. Any amounts at the date of shipment invoiced in excess of the minimum guaranteed contract price are deferred until the additional amounts the Company is entitled to are fixed or determinable. Additional amounts earned by the Company resulting from margin sharing arrangements and determination of the end products into which the products are ultimately incorporated are recognized when end customer sales volume is reported to the Company.

The Company also sells a limited amount of software under perpetual licenses that include post-contract customer support, or PCS. The Company does not have evidence of fair value for the PCS and, accordingly, license revenue is recognized ratably over the estimated supporting period in accordance with ASC 985, Software Revenue Recognition. The revenue from those licenses comprised 1% and 3% of the Company's total revenue for the three months ended April 30, 2013 and 2012, respectively.

Cost of Revenue

Cost of revenue includes cost of materials, cost associated with packaging and assembly, testing and shipping, cost of personnel, stock-based compensation, logistics and quality assurance, warranty cost, royalty expense, write-downs of inventories and allocation of overhead.

Warranty Costs

The Company typically provides warranty on its products. The Company accrues for the estimated warranty costs at the time when revenue is recognized. The warranty accruals are regularly monitored by management based upon historical experience and any specifically identified failures. While the Company engages in extensive product quality assessment, actual product failure rates, material usage or service delivery costs could differ from estimates and revisions to the estimated warranty liability would be required. The Company's warranty accruals have not been material to date.

Research and Development

Research and development costs are expensed as incurred and consist primarily of personnel costs, product development costs, which include engineering services, development software and hardware tools, license fees, cost of fabrication of masks for prototype products, other development materials costs, depreciation of equipment used in research and development and allocation of facilities costs.

Selling, General and Administrative

Selling, general and administrative expense consists of personnel costs, travel and trade show costs, legal expenses, other professional services and occupancy costs. Advertising expenses have not been material to date.

Operating Leases

The Company recognizes rent expense on a straight-line basis over the term of the lease. The difference between rent expense and rent paid is recorded as deferred rent and is included in accrued liabilities in the condensed consolidated balance sheets.

Table of Contents

Income Taxes

The Company records income taxes using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in its financial statements or tax returns. In estimating future tax consequences, generally all expected future events other than enactments or changes in the tax law or rates are considered. Valuation allowances are provided when necessary to reduce deferred tax assets to the amount expected to be realized.

The Company applies authoritative guidance for the accounting for uncertainty in income taxes. The guidance requires that tax effects of a position be recognized only if it is more likely than not to be sustained based solely on its technical merits as of the reporting date. Upon estimating the Company's tax positions and tax benefits, the Company considered and evaluated numerous factors, which may require periodic adjustments and which may not reflect the final tax liabilities. The Company adjusts its financial statements to reflect only those tax positions that are more likely than not to be sustained under examination.

As part of the process of preparing condensed consolidated financial statements, the Company is required to estimate its taxes in each of the jurisdictions in which it operates. The Company estimates actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as accruals and allowances not currently deductible for tax purposes. These differences result in deferred tax assets, which are included in the condensed consolidated balance sheets. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in the condensed consolidated statements of operations become deductible expenses under applicable income tax laws, or loss or credit carryforwards are utilized.

In assessing whether deferred tax assets may be realized, management considers whether it is more likely than not that some portion or all of deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income.

The Company makes estimates and judgments about its future taxable income based on assumptions that are consistent with its plans and estimates. Should the actual amounts differ from estimates, the amount of valuation allowance could be materially impacted. Any adjustment to the deferred tax asset valuation allowance would be recorded in the income statement for the periods in which the adjustment is determined to be required.

Stock-Based Compensation

The Company measures stock-based compensation for equity awards granted to employees and directors based on the estimated fair value on the grant date, and recognizes that compensation as expense using the straight-line attribution method for service condition awards or using the graded-vesting attribution method for awards with performance conditions over the requisite service period, which is typically the vesting period of each award. The Company estimates the fair value of awards of restricted stock units, or RSUs, based on the fair market value of its ordinary shares on the date of grant. The Company uses the Black-Scholes option pricing model to determine the fair value of stock option grants and shares issuance pursuant to its employee stock purchase plan, or ESPP. Determining the fair value of stock option awards on the grant date or the fair value of ESPP shares on the offering date requires the input of various assumptions, including stock price of the underlying ordinary share, the exercise price of the stock option or the offering price of the ESPP share, expected volatility, expected term, risk-free interest rate and dividend rate. The expected term for stock option is calculated using the simplified method as prescribed by the guidance provided by the Securities and Exchange Commission, as neither relevant historical experience nor other relevant data are available to estimate future exercise behavior. The expected term for shares issuance pursuant to the ESPP is the offering period. The expected volatility is based on the historical volatilities of similar companies whose share prices are publicly available for a period commensurate with the expected term. The risk-free interest rate is derived from the average U.S. Treasury constant maturity rates during the respective periods commensurate with the expected term. The expected dividend yield is zero because the Company has not historically paid dividends and has no present intention to pay dividends. The Company uses historical data to estimate pre-vesting award forfeitures and records stock-based compensation only for those awards that are expected to vest. Forfeitures are estimated at the time of grant and revised if necessary in subsequent periods if actual forfeitures differ from estimates.

Table of Contents

The Company recognizes non-employee stock-based compensation expense based on the estimated fair value of the equity instrument determined by the Black-Scholes option pricing model. The fair value of the non-employee awards is remeasured at each reporting period until services required under the arrangement are completed, which is the vesting date.

Prior to the initial public offering, or IPO, the Company engaged an independent appraiser to assist in the valuation of its ordinary share price. The board of directors directed these regular valuations and had input into determining the relevant objective and subjective factors accounted for and relevant approaches in each valuation. After the IPO, the exercise price of stock option awards is determined based on the closing price of the Company's ordinary shares traded on NASDAQ on the grant date.

Net Income Per Ordinary Share

The Company applies the two-class method to calculate and present net income per ordinary share. Under the two-class method, net income is allocated between ordinary shares and other participating securities based on their participating rights. Participating securities are defined as securities that may participate in undistributed earnings with ordinary shares, whether that participation is conditioned upon the occurrence of a specified event or not. Basic net income per ordinary share is computed by dividing net income allocable to ordinary shares by the weighted-average number of ordinary shares outstanding for the period. Diluted net income per ordinary share is computed by dividing net income allocable to ordinary shares and income allocable to participating securities, to the extent they are dilutive, by the weighted-average number of ordinary shares outstanding, including the dilutive effects of participating securities on an if-converted basis plus the dilutive effects of ordinary shares. The Company's potential dilutive ordinary share equivalents consist of incremental ordinary shares issuable upon the exercise of options, upon the issuance of shares pursuant to the ESPP, upon the release of vested restricted stock units, upon the conversion of its redeemable convertible preference shares and upon the exercise of warrants.

The Company performs an assessment as to whether instruments granted in stock-based payment transactions are participating securities. Stock-based payment awards that have not yet vested meet the definition of a participating security provided the right to receive the dividend is non-forfeitable and non-contingent. These participating securities should be included in the computation of basic net income per share under the two-class method. The Company has concluded that its non-vested early-exercised options meet the definition of a participating security and should be included in the Company's computation of basic earnings per ordinary share.

Comprehensive Income

There are no differences between comprehensive income as defined by ASC 220, Comprehensive Income, and net income as reported in the Company's condensed consolidated statements of operations.

Table of Contents**Recent Accounting Pronouncements**

In February 2013, the FASB issued ASU No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (AOCI). This new guidance requires that the Company present either in a single note or parenthetically on the face of the financial statements, the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and the income statement line items affected by the reclassification. If a component is not required to be reclassified to net income in its entirety, the Company would instead cross reference to the related footnote for additional information. This guidance only impacts disclosures within the Company's consolidated financial statements and notes to the consolidated financial statements and does not result in a change to the accounting treatment of AOCI. This new guidance became effective prospectively for fiscal years, and interim periods with those years, beginning after December 15, 2012. The Company adopted this guidance and the adoption did not have an impact on its financial position, results of operations or disclosures.

2. Inventories

Inventory at April 30, 2013 and January 31, 2013 consisted of the following:

| | As of April 30, 2013 | As of January 31, 2013 (in thousands) |
|------------------|-------------------------|---|
| Work-in-progress | \$ 4,845 | \$ 4,044 |
| Finished goods | 4,480 | 4,874 |
| Total | \$ 9,325 | \$ 8,918 |

3. Property and Equipment, Net

Depreciation expense was approximately \$0.2 million for the three months ended April 30, 2013 and 2012, respectively. Property and equipment at April 30, 2013 and January 31, 2013 consisted of the following:

| | As of April 30, 2013 | As of January 31, 2013 (in thousands) |
|---|-------------------------|---|
| Computer equipment and software | \$ 2,867 | \$ 2,810 |
| Machinery and equipment | 2,063 | 2,050 |
| Furniture and fixtures | 397 | 397 |
| Leasehold improvements | 642 | 642 |
| Construction in progress | 1,370 | 827 |
| | 7,339 | 6,726 |
| Less: accumulated depreciation and amortization | (4,363) | (4,190) |
| Total property and equipment, net | \$ 2,976 | \$ 2,536 |

Table of Contents**4. Accrued Liabilities**

Accrued liabilities at April 30, 2013 and January 31, 2013 consisted of the following:

| | As of April 30, 2013 | As of January 31, 2013 |
|---------------------------------------|-------------------------|---------------------------|
| | (in thousands) | |
| Accrued employee compensation | \$ 5,259 | \$ 8,599 |
| Refundable exercised unvested options | 161 | 210 |
| Accrued warranty | 335 | 352 |
| Accrued rebates | 192 | 272 |
| Accrued product development costs | 3,920 | 2,875 |
| Other accrued liabilities | 1,317 | 2,111 |
| Total accrued liabilities | \$ 11,184 | \$ 14,419 |

5. Deferred Revenue and Deferred Cost

Deferred revenue and related cost at April 30, 2013 and January 31, 2013 consisted of the following:

| | As of April 30, 2013 | As of January 31, 2013 |
|---|-------------------------|---------------------------|
| | (in thousands) | |
| Deferred revenue on product shipments | \$ 5,051 | \$ 3,827 |
| Deferred revenue from licenses | 300 | 485 |
| Deferred cost of revenue on product shipments | (1,327) | (861) |
| Total deferred income | \$ 4,024 | \$ 3,451 |

6. Capital Stock***Preference shares***

After completion of the IPO, a total of 20,000,000 preference shares, with a \$0.00045 par value per share, were authorized. There were no shares issued and outstanding as of April 30, 2013 and January 31, 2013, respectively.

Warrants

In connection with a financing agreement in 2004, the Company issued warrants to purchase 36,292 Series B redeemable convertible preference shares at an exercise price of \$3.582 per share. The warrants are fully vested and are exercisable through December 2014.

In June 2005, the FASB issued authoritative guidance on the classification of freestanding warrants and other similar instruments on shares that are redeemable (either puttable or mandatorily redeemable). The guidance requires liability classification for warrants issued that are exercisable into convertible preferred stock. Liability classification requires the warrants to be remeasured to their fair value for each reporting period.

Prior to the closing of IPO, the Company utilized the Black-Scholes option pricing model to determine the fair value of the warrants to purchase redeemable convertible preference shares, including the consideration of underlying ordinary share price, a risk-free interest rate, the expected term and expected volatilities. The warrants were revalued up to the closing of IPO and any change in fair value has been recorded in other expense.

Edgar Filing: AMBARELLA INC - Form 10-Q

Upon the completion of the IPO, the warrants to purchase redeemable convertible preference shares converted to warrants to purchase ordinary shares. During the three months ended April 30, 2013, a total of 25,125 warrants were exercised. A total of 11,167 and 36,292 warrants were outstanding at April 30, 2013 and January 31, 2013, respectively.

Table of Contents**Ordinary shares**

At April 30, 2013 and January 31, 2013, a total of 200,000,000 ordinary shares were authorized. As of April 30, 2013 and January 31, 2013, the following ordinary shares were reserved for future issuance:

| | As of April 30, 2013 | As of January 31, 2013 |
|--|-------------------------|---------------------------|
| Shares reserved for options and restricted stock units | 6,836,469 | 5,818,126 |
| Shares reserved for employee stock purchase plan | 798,383 | 460,445 |
| Shares reserved for warrants | 11,167 | 36,292 |

7. Employee Benefits and Stock-based Compensation**401(k) Plan**

The Company maintains a defined contribution 401(k) plan (the "401(k) Plan") for all of its eligible U.S. employees. Under the 401(k) Plan, eligible employees may contribute up to the Internal Revenue Service annual contribution limitation. The Company is responsible for administrative costs of the Plan. The Company has not had any matching contributions to date.

Stock Option Plans

2004 Stock Plan. The board of directors adopted, and the shareholders approved, the 2004 Stock Plan, as amended, (the "2004 Plan"). The 2004 Plan was last amended on August 28, 2012. The 2004 Plan provides for the grant of incentive stock options ("ISOs") within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), nonstatutory stock options ("NSOs"), stock purchase rights to acquire restricted stock and restricted stock units. Upon the completion of the IPO, no additional awards will be granted under the 2004 Plan and the 2004 Plan was terminated. However, all outstanding stock options and other awards previously granted under the 2004 Plan will remain subject to the terms of the 2004 Plan.

2012 Equity Incentive Plan. The board of directors has adopted, and the shareholders have approved, the 2012 Equity Incentive Plan, (the "EIP"). The EIP became effective on October 8, 2012. The EIP permits the grant of ISOs, within the meaning of Section 422 of the Code, to employees of the Company and any of the Company's subsidiary corporations, and the grant of NSOs, stock appreciation rights, restricted stock, restricted stock units, performance units, performance shares, deferred stock units and dividend equivalents to employees, directors and consultants of the Company and any of the Company's subsidiary corporations' employees and consultants.

The exercise price of ISOs granted to a holder of more than 10% of the voting power of all classes of the Company's shares shall be no less than 110% of the estimated fair market value on the grant date. The exercise price of ISOs granted to other employees and NSOs shall be no less than 100% of estimated fair market value on the grant date. Options granted under the Plans have a term of up to 10 years from grant date. Options granted to new employees generally vest 25% on the first anniversary date of the grant and the remainder ratably over the following 36 months. Vesting schedules for other grants to employees vary and are subject to approval by the board of directors.

Table of Contents

The fair value of restricted stock units, or RSUs, is determined on the grant date. Prior to the Company's IPO, 1/16th of the RSUs were to vest each three months following the vesting commencement date, so as to be 100% vested on the fourth anniversary of the vesting commencement date (the Time-Based Vesting Schedule); provided, however, that the RSUs did not vest at all until a Liquidity Event has occurred, at which time the Time-Based Vesting Schedule would apply, subject to the RSU holder continuing to provide services to the Company through such vesting dates. For purpose of those RSUs, Liquidity Event means either (i) the expiration of the lock-up period that commenced on October 10, 2012 and ended on April 8, 2013 applicable in connection with the Company's IPO, or (ii) a change in control of the Company. After the Company's IPO, RSUs granted to new employees generally vest 25% on the first anniversary of the vesting commencement date and 1/16th of the RSUs vest each 3 months thereafter. Vesting schedules for other RSUs to employees vary and are subject to approval by the board of directors.

2012 Employee Stock Purchase Plan. The board of directors has adopted, and the shareholders have approved, the 2012 Employee Stock Purchase Plan, or ESPP, which became effective upon the completion of IPO. The ESPP permits eligible participants to purchase ordinary shares at a discount through contributions of up to 10% of their eligible compensation, subject to any IRS limitations. The ESPP provides for offering and purchase periods of six months in duration, except for the first offering period that commenced on the occurrence of the IPO and will end on September 16, 2013. The purchase price of ordinary shares is 85% of the lower of the closing market price of the Company's ordinary shares on the first trading day of each offering period or on the purchase date.

Early exercise rights. Certain employees have the right to early exercise unvested options, subject to repurchase rights held by the Company at their original purchase price upon termination of employment until vested. As of April 30, 2013 and January 31, 2013, a total of 86,005 and 84,377 shares of unvested early exercised options were repurchased, respectively. There were 39,242 and 53,151 unvested shares subject to the Company's repurchase rights as of April 30, 2013 and January 31, 2013, respectively.

Stock-based Compensation

The following table presents the classification of stock-based compensation for the periods indicated:

| | Three Months Ended April 30, | |
|---------------------------------------|---|---------------|
| | 2013 | 2012 |
| | (in thousands) | |
| Stock-based compensation: | | |
| Cost of revenue | \$ 34 | \$ 14 |
| Research and development | 974 | 532 |
| Selling, general and administrative | 598 | 397 |
| Total stock-based compensation | \$ 1,606 | \$ 943 |

As of April 30, 2013, total unrecognized compensation cost related to unvested stock options and unvested restricted stock units was \$6.7 million and \$2.0 million, respectively, and is expected to be recognized over a weighted-average period of 2.15 years and 1.83 years, respectively. As of January 31, 2013, total unrecognized compensation cost related to unvested stock options and unvested restricted stock units was \$7.3 million and \$2.4 million, respectively, and is expected to be recognized over a weighted-average period of 2.26 years and 1.77 years, respectively.

Table of Contents

The income tax benefit on stock-based compensation recognized for the three months ended April 30, 2013 and 2012 was not material.

The following table sets forth the weighted-average assumptions used to estimate the fair value of the stock options for the periods indicated:

| | Three Months Ended April 30, | |
|-------------------------|---------------------------------|-------|
| | 2013 | 2012 |
| Stock Options: | | |
| Volatility | 65% | 66% |
| Risk-free interest rate | 1.17% | 1.10% |
| Expected term (years) | 6.05 | 6.05 |
| Dividend yield | 0% | 0% |

The following table summarizes stock option activities for the three months ended April 30, 2013:

| | Shares | Weighted-Average Exercise Price | Option Outstanding | | Weighted-Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (in thousands) |
|---|-----------|---------------------------------|--|---|--|--|
| | | | Weighted-Average Grant-date Fair Value | Total Intrinsic Value of options Exercised (in thousands) | | |
| Outstanding at January 31, 2013 | 4,344,535 | 6.07 | | | | |
| Granted | 60,000 | 13.74 | \$ 8.15 | | | |
| Exercised | (158,871) | 3.11 | | \$ 1,689 | | |
| Forfeited | (31,561) | 8.45 | | | | |
| Outstanding at April 30, 2013 | 4,214,103 | 6.27 | | | 6.67 | \$ 31,311 |
| Exercisable at April 30, 2013 | 3,084,125 | 5.42 | | | 6.07 | \$ 25,522 |
| Vested and expected to vest at April 30, 2013 | 4,140,490 | 6.23 | | | 6.64 | \$ 30,940 |

Exercisable shares include options with early exercise rights. The vested and expected-to-vest options are calculated based on vesting schedule of each grant as of the reporting date.

The intrinsic value of options outstanding, exercisable and vested and expected-to-vest are calculated based on the difference between the fair market value of the Company's ordinary shares on the reporting date and the exercise price. The closing price of the Company's ordinary shares was \$13.70 on April 30, 2013, as reported by the NASDAQ Global Market. The intrinsic value of exercised options is calculated based on the difference between the fair market value of the Company's ordinary shares on the exercise date and the exercise price.

Table of Contents

The following table summarizes restricted stock units activities for the three months ended April 30, 2013:

| | Shares | Weighted-Average Grant-Date Fair Value |
|------------------------------|----------|--|
| Unvested at January 31, 2013 | 339,217 | \$ 9.99 |
| Granted | 11,000 | 13.74 |
| Released | (39,364) | 9.99 |
| Forfeited | (5,464) | 9.99 |
| Unvested at April 30, 2013 | 305,389 | \$ 10.13 |

As of April 30, 2013, the aggregate intrinsic value of unvested restricted stock units was \$4.2 million.

Non-employee Stock-based Compensation

The fair value of awards granted to non-employees is determined on the date of grant and remeasured at the end of each reporting period until such awards vest. The non-employee stock-based compensation was not material for the three months ended April 30, 2013 and 2012, respectively.

8. Net Income Per Ordinary Share

The following table sets forth the computation of basic and diluted net income per ordinary share for the periods indicated:

| | Three Months Ended April 30, | |
|---|---|-----------|
| | 2013 | 2012 |
| | (in thousands, except share and per share data) | |
| Numerator: | | |
| Net income | \$ 4,741 | \$ 2,602 |
| Less: amount allocable to preference shareholders | | (2,028) |
| Less: amount allocable to unvested early exercised options | (9) | (8) |
| Net income allocable to ordinary shareholders - basic | \$ 4,732 | \$ 566 |
| Undistributed earnings reallocated to ordinary shareholders | 1 | 68 |
| Net income allocable to ordinary shareholders - diluted | \$ 4,733 | \$ 634 |
| Denominator: | | |
| Weighted-average ordinary shares outstanding | 27,103,129 | 7,622,621 |
| Less: weighted-average unvested early exercised options subject to repurchase | (46,197) | (103,261) |
| Weighted-average ordinary shares - basic | 27,056,932 | 7,519,360 |

Edgar Filing: AMBARELLA INC - Form 10-Q

Effect of potentially dilutive securities:

| | | |
|--|------------|-----------|
| Employee stock options | 1,688,768 | 1,512,350 |
| Restricted stock units | 141,647 | |
| Employee stock purchase plan | 170,817 | |
| Warrants to purchase ordinary shares | 7,898 | |
| Weighted-average ordinary shares - diluted | 29,066,062 | 9,031,710 |

Net income per ordinary share:

| | | |
|---------|---------|---------|
| Basic | \$ 0.17 | \$ 0.08 |
| Diluted | \$ 0.16 | \$ 0.07 |

Table of Contents

Earnings per share (EPS) of ordinary shares was calculated using the two-class method required for participating securities. Prior to the date of the IPO, all series of redeemable convertible preference shares were considered to be participating securities due to their non-cumulative dividend rights. In connection with the Company's IPO in October 2012, all outstanding redeemable convertible preference shares converted to ordinary shares. Net income has been allocated to the ordinary shares, redeemable convertible preference shares and unvested early exercised options based on their respective rights to share in net income and weighted-average outstanding during the periods.

The following weighted-average potentially dilutive securities were excluded from the computation of diluted net income per ordinary share as their effect would have been antidilutive:

| | Three Months Ended April 30, | |
|--|-------------------------------------|-------------|
| | 2013 | 2012 |
| Options to purchase ordinary shares | 390,928 | 2,046,941 |
| Restricted stock units | 6,303 | |
| Employee stock purchase plan | | |
| Early exercised options subject to repurchase | 46,197 | 103,261 |
| Redeemable convertible preference shares (if-converted basis) | | 13,315,727 |
| Warrants to purchase redeemable convertible preference shares (if-converted basis) | | 36,292 |
| Warrants to purchase ordinary shares | | |
| | 443,428 | 15,502,221 |

9. Income Taxes

The Company reported the following income tax for the periods indicated:

| | Three Months Ended April 30, | |
|--------------------|-------------------------------------|-------------|
| | 2013 | 2012 |
| | (in thousands) | |
| Income tax expense | \$ 473 | \$ 303 |

The Company recognized income tax expense of approximately \$0.5 million and \$0.3 million for the three months ended April 30, 2013 and 2012, respectively. The estimated effective tax rate was 9.1% and 10.4% for the three months ended April 30, 2013 and 2012, respectively. The effective tax rate for the three months ended April 30, 2013 was lower than the effective tax rate for the three months ended April 30, 2012 primarily due to tax benefits resulting from the reinstatement of the U.S. federal research credit in January 2013.

The Company files federal and state income tax returns in the United States and in various foreign jurisdictions. The tax years 2007 to 2009 and 2011 to 2013 remain open to examination by U.S. federal tax authorities. The tax years 2004 to 2013 remain open to examination by U.S. state tax authorities. The tax years 2010 to 2013 remain open to examination by material foreign tax authorities.

The Company regularly assesses the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of its provision for income taxes. These assessments can require considerable estimates and judgments. As of April 30, 2013, the gross amount of unrecognized tax benefits was approximately \$3 million. If the estimates of income tax liabilities prove to be less than the ultimate assessment, then a further charge to expense would be required. If events occur and the payment of these amounts ultimately proves to be unnecessary, the reversal of the liabilities would result in tax benefits being recognized in the period in which the Company determines the liabilities are no longer necessary. The Company does not anticipate any material changes to its uncertain tax positions during the next twelve months.

Table of Contents**10. Commitments and Contingencies**

The Company leases its principal facilities and time-based software licenses under operating agreements with various expiration dates through February 2018. In March 2013, the Company entered into a lease agreement for approximately 35,000 square feet for its new Santa Clara, California headquarters. The lease has an initial five-year term and terminates in April 2018. The monthly basic rent obligation for this facility initially will be approximately \$44,550, increasing annually to approximately \$65,400 in 2017. The average monthly basic rent expense over the term of the lease will be approximately \$59,800. Net rental expenses for the three months ended April 30, 2013 and 2012 were approximately \$1.1 million for both periods. Future annual minimum lease payments under these operating leases with initial lease terms in excess of one year are as follows:

| Fiscal Year | As of April 30, 2013 (in thousands) |
|-------------|---|
| 2014 | \$ 2,718 |
| 2015 | 1,498 |
| 2016 | 1,346 |
| 2017 | 933 |
| 2018 | 955 |
| | \$ 7,450 |

Contract Manufacturer Commitments

The Company's components and products are procured and built by independent contract manufacturers based on sales forecasts. These forecasts include estimates of future demand, historical trends, analysis of sales and marketing activities, and adjustment of overall market conditions. The Company regularly issues purchase orders to independent contract manufacturers which are cancelable only upon the agreement between the Company and the third-party. As of April 30, 2013 and January 31, 2013, total manufacturing purchase commitments were approximately \$13.1 million and \$15.1 million, respectively.

Indemnification

The Company, from time to time, in the normal course of business, indemnifies certain vendors with whom it enters into contractual relationships. The Company has agreed to hold the other party harmless against third-party claims in connection with the Company's future products. The Company also indemnifies certain customers against third party claims related to certain intellectual property matters. It is not possible to determine the maximum potential amount of liability under these indemnification obligations due to the limited history of prior indemnification claims and the unique facts and circumstances that are likely to be involved in each particular claim. The Company has not made payments under these obligations and no liabilities have been recorded for these obligations on the condensed consolidated balance sheets as of April 30, 2013 and January 31, 2013.

Table of Contents**11. Segment Reporting**

The Company operates in one reportable segment related to the development and sales of low-power, high-definition video products. The Chief Executive Officer of the Company has been identified as the Chief Operating Decision Maker (the CODM) and manages the Company's operations as a whole and for the purpose of evaluating financial performance and allocating resources, the CODM reviews financial information presented on a consolidated basis accompanied by information by customer and geographic region.

Geographic Revenue

The following table sets forth the Company's revenue by geographic region for the periods indicated:

| | Three Months Ended April 30, | |
|---------------|-------------------------------------|-------------|
| | 2013 | 2012 |
| | (in thousands) | |
| Hong Kong | \$ 28,774 | \$ 21,200 |
| Asia Pacific | 256 | 177 |
| United States | 2,605 | 3,036 |
| North America | 962 | 320 |
| Europe | 1,344 | 1,188 |
| | | |
| Total revenue | \$ 33,941 | \$ 25,921 |

As of April 30, 2013, substantially all of the Company's long-lived tangible assets are located in the Asia Pacific region.

Major Customers

The customers representing 10% or more of revenue and accounts receivable were customer A, a logistic provider, and customer B, a direct ODM customer, that combined accounted for approximately 82% of total revenue for the three months ended April 30, 2013. The customer representing 10% or more of revenue and accounts receivable for the three months ended April 30, 2012 was only customer A, a logistic provider, which accounted for approximately 75% of total revenue. Accounts receivable with these two customers combined accounted for approximately \$21.7 million and \$17.6 million as of April 30, 2013 and January 31, 2013, respectively.

12. Related-Party Transactions

The Company considers an entity to be a related party if it owns more than 10% of its total voting stock at the end of each reporting period or if an officer or employee of an entity also serves on the board of directors or if it is a significant shareholder and has material business transactions with the Company.

Starting from the fiscal year 2008, the Company entered into several software license agreements with Cadence Design Systems, Inc. (Cadence). A member of the Company's board of directors is also the Chief Executive Officer, President and a Director of Cadence. Under these license agreements, the Company committed to pay an aggregate amount of \$10.2 million payable through January 2014. The Company paid \$0.4 million and \$0.5 million in license fees for the three months ended April 30, 2013 and 2012, respectively. Operating lease expenses related to these agreements included in research and development cost were approximately \$0.4 million for the three months ended April 30, 2013 and 2012, respectively.

Table of Contents

In addition to the related party transactions noted above, the Company recognized revenue from sales to Wintech Microelectronics Co., Ltd, or Wintech, the Company's logistics provider. Wintech, along with an affiliate, is a shareholder of the Company owning approximately 4.6% of the voting stock as of January 31, 2013. The Company recognized revenue from sales to Wintech of approximately \$13.4 million and \$19.4 million for the three months ended April 30, 2013 and 2012, respectively. As of April 30, 2013 and January 31, 2013, the Company had receivables from Wintech of approximately \$7.6 million and \$8.2 million, respectively.

Table of Contents

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q, and the consolidated financial statements and notes thereto for the year ended January 31, 2013 and management's discussion and analysis of our financial condition and results of operations included in our Annual Report on Form 10-K for the 2013 fiscal year filed with the SEC on April 4, 2013.

This Quarterly Report on Form 10-Q, including this Management's discussion and analysis of financial condition and results of operations, includes a number of forward-looking statements that involve many risks and uncertainties. Forward-looking statements are identified by the use of the words would, could, will, may, expect, believe, should, anticipate, outlook, if, future, intend, plan, estimate, predict, potential, targets, seek or continue and similar words and phrases, including the negatives of these terms, or other variations of these terms, that denote future events. Such statements include, but are not limited to, statements concerning our market opportunity, our ability to develop new solutions, our future financial and operating performance, sales and marketing strategy, investment strategy, research and development, customer and supplier relationships, industry trends, our cash needs and capital requirements, expectations about seasonality, taxes, and operating expenses. These statements reflect our current views with respect to future events and our potential financial performance and are subject to risks and uncertainties that could cause our actual results and financial position to differ materially and adversely from what is projected or implied in any forward-looking statements included in this Quarterly Report on Form 10-Q. These factors include, but are not limited to, the risks described under Item 1A of Part II Risk Factors, Item 2 of Part I Management's Discussion and Analysis of Financial Condition and Results of Operations, elsewhere in this Quarterly Report on Form 10-Q and those discussed in other documents we file with the SEC. We make these forward-looking statements based upon information available on the date of this Quarterly Report on Form 10-Q, and we have no obligation (and expressly disclaim any such obligation) to update or alter any forward-looking statements, whether as a result of new information or otherwise except as otherwise required by securities regulations.

Overview

We are a leading developer of semiconductor processing solutions for video that enable high-definition, or HD, video capture, sharing and display. We combine our processor design capabilities with our expertise in video and image processing algorithms and software to provide a technology platform that is designed to be easily scalable across multiple applications and enable rapid and efficient product development. Our system-on-a-chip, or SoC, designs fully integrate HD video processing, image processing, audio processing and system functions onto a single chip, delivering exceptional video and image quality, differentiated functionality and low power consumption.

We sell our solutions to leading original design manufacturers, or ODMs, and original equipment manufacturers, or OEMs, globally. We refer to ODMs as our customers and OEMs as our end customers, except as otherwise indicated or as the context otherwise requires. In the camera market, our solutions enable the creation of high-quality video content for wearable sports cameras, automotive aftermarket cameras, Internet Protocol, or IP, security cameras, telepresence cameras and camcorders. In the infrastructure market, our solutions efficiently manage IP video traffic, broadcast encoding and IP video delivery applications.

Table of Contents

Our sales cycles typically require a significant investment of time and a substantial expenditure of resources before we can realize revenue from the sale of our solutions, if any. Our typical sales cycle consists of a multi-month sales and development process involving our customers' system designers and management along with our sales personnel and software engineers. If successful, this process culminates in a customer's decision to use our solutions in its system, which we refer to as a design win. Our sales efforts are typically directed to the OEM of the product that will incorporate our video and image processing solution, but the eventual design and incorporation of our SoC into the product may be handled by an ODM on behalf of the OEM. Volume production may begin within six to 18 months after a design win, depending on the complexity of our customer's product and other factors upon which we may have little or no influence. Once one of our solutions has been incorporated into a customer's design, we believe that our solution is likely to remain a component of the customer's product for its life cycle because of the time and expense associated with redesigning a product or substituting an alternative solution. Conversely, a design loss to a competitor will likely preclude any opportunity for future revenue from such customer's product.

Financial Highlights and Trends for the Three Months Ended April 30, 2013

We recorded revenue of \$33.9 million for the three months ended April 30, 2013, an increase of 31% as compared to the three months ended April 30, 2012. The increase was primarily due to higher demand for our A7 SoC in the wearable sports camera market, as well as continuing growth in the automotive aftermarket and IP security camera end markets. The increase was partially offset by decreased revenue in the infrastructure market as a result of weak macro market conditions in the United States and Europe resulting in lower capital expenditures for video encoding capital equipment. The same period in the prior fiscal year was affected by renegotiation of an infrastructure customer contract that resulted in an additional \$1.6 million of deferred revenue released for the three months ended April 30, 2012, which was not repeated in the first quarter of fiscal year 2014.

We recorded operating income of \$5.2 million for the three months ended April 30, 2013, an increase of 80% as compared to the three months ended April 30, 2012, primarily due to an increase in revenue and as well as efficient control of operating expenses.

We generated cash flows from operating activities of \$3.2 million for the three months ended April 30, 2013, as compared to \$0.8 million for the three months ended April 30, 2012. The increase was primarily attributable to increased net income, adjusted for increased non-cash stock-based compensation expense. The increase was partially offset by additional inventory purchased to support growing sales as well as increased accounts receivable resulting from the shifting of sales through a logistics customer to direct sales to a large ODM customer with longer payment terms.

In March 2013, we entered into a lease agreement for approximately 35,000 square feet for our new Santa Clara, California headquarters. The lease has an initial five-year term and terminates in April 2018. The monthly basic rent obligation for this facility initially will be approximately \$44,550, increasing annually to approximately \$65,400 in 2017. The average monthly basic rent expense over the term of the lease will be approximately \$59,800.

Factors Affecting Our Performance

Design Wins. We closely monitor design wins by customer and end market. We consider design wins to be critical to our future success, although the revenue generated by each design win can vary significantly. Our long-term sales expectations are based on forecasts from customers and internal estimations of customer demand factoring in the expected time to market for end customer products incorporating our solutions and associated revenue potential.

Table of Contents

Pricing, Product Cost and Margins. Our pricing and margins depend on the volumes and the features of the solutions we provide to our customers. Additionally, we make significant investments in new solutions for both cost improvements and new features that we expect to drive revenue and maintain margins. In general, solutions incorporated into more complex configurations, such as those used in the infrastructure market, have higher prices and higher gross margins as compared to solutions sold into the camera market. Our average selling price, or ASP, can vary by market and application due to market-specific supply and demand, the maturation of products launched in previous years and the launch of new products.

We continually monitor the cost of our solutions. As we rely on third-party manufacturers for the production of our products, we maintain a close relationship with these suppliers to continually monitor production yields, component costs and design efficiencies.

Shifting Consumer Preferences. Our revenue is subject to consumer preferences, regarding form factor and functionality, and how those preferences impact the video and image capture electronics that we support. For example, improved smartphone video capture capabilities, and rapid adoption by consumers, has led to the decline of pocket video cameras aimed at the video and image capture market over the past couple of years. The current video and image capture market is now characterized by a greater volume of more specialized video and image capture devices that are less likely to be replaced with smartphones, such as wearable sports cameras, automotive aftermarket cameras, IP security cameras, high-end DSCs and enterprise telepresence cameras. This increasing specialization of video capture devices has changed our customer base and end markets and has impacted our revenue. In the future, we expect further changes in the market to continue to impact our business performance.

Continued Concentration of Revenue by End Market. Historically, our revenue has been significantly concentrated in a small number of end markets. In fiscal year 2010, the majority of our revenue came from the pocket video, camcorder and infrastructure markets. Over the last three years, we have continued to provide solutions for the camcorder and infrastructure markets, but also have expanded our focus to include the wearable sports, automotive aftermarket, IP security, and telepresence camera markets. We believe our entry into these new markets will continue to facilitate revenue growth and customer diversification. While we will continue to expand our end market exposure, we anticipate that sales to a limited number of end markets will continue to account for a significant percentage of our total revenue for the foreseeable future. Our end market concentration may cause our financial performance to fluctuate significantly from period to period based on the success or failure of video capture markets in which we compete. In addition, we derive a significant portion of our revenue from a limited number of ODMs who build products on behalf of a limited number of OEMs and from a limited number of OEMs to whom we ship directly. We believe that our operating results for the foreseeable future will continue to depend on sales to a relatively small number of customers.

Ability to Capitalize on Connectivity Trends. Mobile connected devices are ubiquitous today and play an increasingly prominent role in consumers' lives. The constant connectivity provided by these devices has created a demand for connected electronic peripherals such as video and image capture devices. Our ability to capitalize on these trends by supporting our end customers in the development of connected peripherals that seamlessly cooperate with other connected devices and allow consumers to distribute and share video and images with online media platforms is critical for our success. We have added wireless communication functionality into our solutions for wearable sports cameras, IP security cameras and DSCs. The combination of our compression technology with wireless connectivity enables wireless video streaming and the uploading of videos and images to the Internet. Our solutions enable IP security camera systems to stream video content to either cloud infrastructure or connected mobile devices, and our solutions for wearable sports cameras allow consumers to quickly stream or upload video and images to social media platforms.

Table of Contents

Sales Volume. A typical design win can generate a wide range of sales volumes for our solutions, depending on the end market demand for our customers' products. This can depend on several factors, including the reputation of the end customer, market penetration, product capabilities, size of the end market that the product addresses and our end customers' ability to sell their products. In certain cases, we may provide volume discounts on sales of our solutions, which may be offset by lower manufacturing costs related to higher volumes. In general, our customers with greater market penetration and better branding tend to develop products that generate larger volumes over the product life cycle.

Customer Product Life Cycle. We estimate our customers' product life cycles based on the customer, type of product and end market. In general, products launched in the camera market have shorter life cycles than those sold into the infrastructure market. We typically commence commercial shipments from six to 15 months following a design win; however, in some markets, more lengthy product and development cycles are possible, depending on the scope and nature of the project. A portable consumer device typically has a product life cycle of six to 18 months. In the infrastructure market, the product life cycle can range from 24 to 60 months.

Results of Operations

The following table sets forth a summary of our statement of operations for the periods indicated:

| | Three Months Ended April 30, | |
|-------------------------------------|-------------------------------------|-------------|
| | 2013 | 2012 |
| | (dollars in thousands) | |
| Revenue | \$ 33,941 | \$ 25,921 |
| Cost of revenue | 12,248 | 7,516 |
| Gross profit | 21,693 | 18,405 |
| Operating expenses: | | |
| Research and development | 11,317 | 11,473 |
| Selling, general and administrative | 5,157 | 4,025 |
| Total operating expenses | 16,474 | 15,498 |
| Income from operations | 5,219 | 2,907 |
| Other expense | (5) | (2) |
| Income before income taxes | 5,214 | 2,905 |
| Provision for income taxes | 473 | 303 |
| Net income | \$ 4,741 | \$ 2,602 |

Table of Contents

The following table sets forth operating results as a percentage of revenue of each line item for the periods indicated:

| | Three Months Ended April 30, | |
|-------------------------------------|-------------------------------------|-------------|
| | 2013 | 2012 |
| Revenue | 100% | 100% |
| Cost of revenue | 36 | 29 |
| Gross profit | 64 | 71 |
| Operating expenses: | | |
| Research and development | 33 | 44 |
| Selling, general and administrative | 15 | 16 |
| Total operating expenses | 48 | 60 |
| Income from operations | 16 | 11 |
| Other expense | | |
| Income before income taxes | 16 | 11 |
| Provision for income taxes | 1 | 1 |
| Net income | 15% | 10% |

Revenue

We derive substantially all of our revenue from the sale of HD video and image processing SoC solutions to OEMs and ODMs, either directly or through our logistics providers. Our SoC solutions have been used in the camera and infrastructure markets, and we expect these will be the primary markets for our solutions for the foreseeable future. We derive a substantial portion of our revenue from sales made indirectly through our logistics provider, Wintech Microelectronics Co., Ltd., or Wintech.

We typically experience seasonal fluctuations in our quarterly revenue with our third fiscal quarter normally being the highest revenue quarter. This fluctuation has been driven primarily by increased sales into the camera market as our customers build inventory in preparation for the holiday shopping season. More generally, our average selling prices fluctuate based on the mix of our solutions sold in a period which reflects the impact of both changes in unit sales of existing solutions as well as the introduction and sales of new solutions. Our solutions are typically characterized by a life cycle that begins with higher average selling prices and lower volumes, followed by broader market adoption, higher volumes and average selling prices that are lower than initial levels.

The end markets into which we sell our products have seen significant changes as consumer preferences have evolved in response to new technologies. As a result, the composition of our revenue may differ meaningfully during periods of technology or consumer preference changes. We expect shifts in consumer use of video capture to continue to change over time, as more specialized use cases emerge and video capture continues to proliferate.

Cost of Revenue and Gross Margin

Cost of revenue includes the cost of materials such as wafers processed by third-party foundries, costs associated with packaging, assembly and test, and our manufacturing support operations such as logistics, planning and quality assurance. Cost of revenue also includes indirect costs such as warranty, inventory valuation reserves and other general overhead costs.

Table of Contents

We expect that our gross margin may fluctuate from period to period as a result of changes in average selling price, product mix and the introduction of new products by us or our competitors. In general, solutions incorporated into more complex configurations, such as those used in the infrastructure market, have higher prices and higher gross margins, as compared to solutions sold into the camera market. As semiconductor products mature and unit volumes sold to customers increase, their average selling prices typically decline. These declines may be paired with improvements in manufacturing yields and lower wafer, packaging and test costs, which offset some of the margin reduction that could result from lower selling prices. We believe that our gross margin will decline in the future as we continue to penetrate the highly competitive camera market and as we launch our solutions into new markets.

Research and Development

Research and development expense consists primarily of personnel costs, including salaries, stock-based compensation and employee benefits. The expense also includes costs of development incurred in connection with our collaborations with our foundry vendors, costs of licensing intellectual property from third parties for product development, costs of development for software and hardware tools, cost of fabrication of mask sets for prototype products, and allocated depreciation and facility expenses. All research and development costs are expensed as incurred. We expect our research and development expense to increase in absolute dollars as we continue to enhance and expand our product features and offerings.

Selling, General and Administrative

Selling, general and administrative expense consists primarily of personnel costs, including salaries, stock-based compensation and employee benefits for our sales, marketing, finance, human resources, information technology and administrative personnel. The expense also includes professional service costs related to accounting, tax, legal services, and allocated depreciation and facility expenses. We expect our selling expense to increase in absolute dollars as we expand the size of our sales and marketing organization to support our anticipated growth. We expect our general and administrative expense to increase in absolute dollars and as a percent of revenue as we develop the infrastructure necessary to operate as a public company, which includes increased audit and legal fees, costs to comply with the Sarbanes-Oxley Act of 2002 and the rules and regulations applicable to companies listed on The NASDAQ Stock Market, investor relations costs, and higher insurance premiums.

Other Expense

Other expense consists primarily of gain and loss from foreign currency transactions and remeasurements.

Provision for Income Taxes

We are incorporated in the Cayman Islands and conduct business in several countries such as the United States, China, Taiwan, Hong Kong, South Korea and Japan, and we are subject to taxation in those jurisdictions. As such, our worldwide operating income is subject to varying tax rates and our effective tax rate is highly dependent upon the geographic distribution of our earnings or losses and the tax laws and regulations in each geographical region. Consequently, we have experienced lower effective tax rates as a substantial percentage of our operations are conducted in lower-tax jurisdictions. If our operational structure was to change in such a manner that would increase the amount of operating income subject to taxation in higher-tax jurisdictions, or if we were to commence operations in jurisdictions assessing relatively higher tax rates, our effective tax rate could fluctuate significantly on a quarterly basis and/or be adversely affected.

Table of Contents**Comparison of the Three Months Ended April 30, 2013 and 2012****Revenue**

| | Three Months Ended April 30, 2013 | Three Months Ended April 30, 2012 | Change Amount | % |
|---------|--------------------------------------|--------------------------------------|------------------|-----|
| Revenue | \$ 33,941 | \$ 25,921 | \$ 8,020 | 31% |

Revenue increased for the three months ended April 30, 2013 compared to the same period in the prior fiscal year primarily due to higher demand for our A7 SoC in the wearable sports camera market, as well as continuing growth in the automotive aftermarket and IP security camera end markets. The increase was partially offset by decreased revenue in the infrastructure market as a result of weak macro market conditions in the United States and Europe resulting in lower capital expenditures for video encoding capital equipment. In addition, the infrastructure market revenue was higher than the current period primarily due to the renegotiation of an infrastructure customer contract that resulted in an additional \$1.6 million of deferred revenue being released in the three months ended April 30, 2012. This similar release of deferred revenue was not repeated in the first quarter of fiscal year 2014.

Cost of Revenue and Gross Margin

| | Three Months Ended April 30, 2013 | Three Months Ended April 30, 2012 | Change Amount | % |
|-----------------|--------------------------------------|--------------------------------------|------------------|-----|
| Cost of revenue | \$ 12,248 | \$ 7,516 | \$ 4,732 | 63% |
| Gross profit | 21,693 | 18,405 | 3,288 | 18% |
| Gross margin | 64% | 71% | (7)% | |

Cost of revenue increased for the three months ended April 30, 2013 primarily due to an increase in the number of SoCs sold into the camera markets and to increased sales of our higher cost A7 SoCs. The increase was partially offset by cost reductions received from suppliers for certain SoCs due to purchase volume increases.

Gross margin decreased for the three months ended April 30, 2013 as compared to the same period in the prior fiscal year primarily due to the decline in higher gross margin infrastructure revenue as a percentage of total revenue discussed above. The decline in infrastructure revenue also resulted from the release of \$1.6 million of deferred revenue as a result of the renegotiation of a customer contract that contributed approximately 2% to the gross margin in the three months ended April 30, 2012. This additional contribution to gross margin was not repeated in the first quarter of fiscal year 2014. To a lesser extent, gross margin declined due to a change in revenue mix within the camera markets, as we recorded higher consumer product revenues at lower gross margin in the three months ended April 30, 2013 compared to the three months ended April 30, 2012.

Table of Contents**Research and Development**

| | Three Months Ended April 30, 2013 | 2012 | Change Amount | % |
|--------------------------|--------------------------------------|-----------|------------------|------|
| Research and development | \$ 11,317 | \$ 11,473 | \$ (156) | (1)% |

Research and development expense decreased for the three months ended April 30, 2013 primarily due to decreased product development costs of approximately \$1.1 million associated with the timing of new product development efforts. The decrease was partially offset by an increase in engineering headcount and additional bonus and stock-based compensation. Our research and development engineering headcount increased to 340 at April 30, 2013 compared to 311 at April 30, 2012, resulting in an increase in salary related expenses of approximately \$0.5 million. In the third quarter of fiscal year 2013, we granted restricted stock units and offered participation in our employee stock purchase plan upon completion of our IPO, resulting in an increase in stock-based compensation expense of approximately \$0.5 million for the three months ended April 30, 2013.

Selling, General and Administrative

| | Three Months Ended April 30, 2013 | 2012 | Change Amount | % |
|-------------------------------------|--------------------------------------|----------|------------------|-----|
| Selling, general and administrative | \$ 5,157 | \$ 4,025 | \$ 1,132 | 28% |

Selling, general and administrative expense increased for the three months ended April 30, 2013 compared to the same period in the prior fiscal year primarily due to an additional \$0.5 million in personnel costs as a result of increased headcount to 105 at April 30, 2013 compared to 89 at April 30, 2012 and an additional \$0.2 million of stock-based compensation expense from the issuance of restricted stock units and offering of employee stock purchase plan. The increase was also attributable to approximately \$0.3 million of additional expenditures on outside professional services to support our expanding business and operations as a public company.

Other Expense

| | Three Months Ended April 30, 2013 | 2012 | Change Amount | % |
|---------------|--------------------------------------|--------|------------------|--------|
| Other expense | \$ (5) | \$ (2) | \$ (3) | (150)% |

Other expense for the three months ended April 30, 2013 included the revaluation of foreign currency. In the same period in the prior fiscal year, other expense included the impact of the revaluation of warrants to purchase redeemable convertible preference shares as well as foreign currency changes. The warrants to purchase redeemable convertible preference shares converted into warrants to purchase ordinary shares upon our IPO in the third quarter of fiscal year 2013 and as a result, there will be no future impact to net income from the revaluation of such warrants.

Table of Contents*Provision for Income Taxes*

| | Three Months Ended April 30, | | Change | |
|----------------------------|------------------------------|--------|--------|--------|
| | 2013 | 2012 | Amount | % |
| | (dollars in thousands) | | | |
| Provision for income taxes | \$ 473 | \$ 303 | \$ 170 | 56% |
| Effective tax rate | 9.1% | 10.4% | | (1.3)% |

Our quarterly income taxes reflect an estimation of the corresponding fiscal year's annual effective tax rate and include, when applicable, adjustments for discrete tax items. For the three months ended April 30, 2013, our overall estimation of the current fiscal year's annual effective tax rate reflected the favorable impact from the extended U.S. federal R&D credits, the change in increase in pretax earnings and a change in mix of earnings to lower tax jurisdictions.

Table of Contents**Liquidity and Capital Resources**

We had cash of \$104.3 million and \$100.5 million as of April 30, 2013 and January 31, 2013, respectively.

Cash Flows

The following table summarizes our cash flows for the periods indicated:

| | Three Months Ended April 30, | |
|---|-------------------------------------|-------------|
| | 2013 | 2012 |
| | (in thousands) | |
| Net cash provided by operating activities | \$ 3,216 | \$ 780 |
| Net cash used in investing activities | (579) | (155) |
| Net cash provided by financing activities | 1,146 | 125 |
| | | |
| Net increase in cash | \$ 3,783 | \$ 750 |

Net Cash Provided by Operating Activities

The increase in cash flow from operating activities for the three months ended April 30, 2013 compared to the same period in fiscal year 2012 was primarily due to increased net income, adjusted for increased non-cash stock-based compensation expense. The increase was partially offset by additional inventory purchased to support growing sales, as well as increased accounts receivable resulting from longer payment terms associated with direct sales to a large ODM customer rather than sales to the customers that previously purchased through our logistics partner.

Net Cash Used in Investing Activities

Net cash used in investing activities increased primarily due to approximately \$0.4 million of leasehold improvements for our new headquarters located in Santa Clara, California for the three months ended April 30, 2013 compared to the three months ended April 30, 2012.

Net Cash Provided by Financing Activities

Net cash provided by financing activities increased for the three months ended April 30, 2013 compared to the same period in prior fiscal year primarily due to cash proceeds from employee exercises of stock options and cash withholding contributed by employees under our employee stock purchase plan.

Operating and Capital Expenditure Requirements

We have generated net income in each quarter beginning with the first quarter of fiscal year 2010, and we have generated cash from operations in each of fiscal years 2009 to 2013. We believe that our anticipated cash generated from operations and our existing cash balances will be sufficient to meet our anticipated cash requirements through at least the next 12 months. In the future, we expect our operating and capital expenditures to increase as we increase headcount, expand our business activities and implement and enhance our information technology and enterprise resource planning systems. We expect our accounts receivable and inventory balances to increase, and to be partially offset by increases in accounts payable, which will result in a greater need for working capital. If our available cash balances are insufficient to satisfy our future liquidity requirements, we may in the future seek to sell equity or convertible debt securities or borrow funds commercially. The sale of equity and convertible debt securities may result in dilution to our shareholders and those securities may have rights senior to those of our ordinary shares. If we raise additional funds through the issuance of convertible debt securities, these securities could contain covenants that would restrict our operations. We may require additional capital beyond our currently anticipated amounts. Additional capital may not be available to us on reasonable terms, or at all.

Table of Contents

Our short- and long-term capital requirements will depend on many factors, including the following:

our ability to generate cash from operations;

our ability to control our costs;

the emergence of competing or complementary technologies or products;

the costs of filing, prosecuting, defending and enforcing any patent claims and other intellectual property rights, or participating in litigation-related activities; and

our acquisition of complementary businesses, products and technologies.

Contractual Obligations, Commitments and Contingencies

The following table summarizes our outstanding contractual obligations as of April 30, 2013:

| | Payment Due by Period as of April 30, 2013 (in thousands) | | | | | |
|--|--|---------------------|-----------------|-----------------|----------------------|-----------------|
| | Total | Less than 1 Year | 1-3 Years | 3-5 Years | More than 5 Years | All Other |
| Contractual Obligations | | | | | | |
| Facilities under operating leases | \$ 5,489 | \$ 954 | \$ 2,667 | \$ 1,868 | \$ | \$ |
| Technology license or other obligations under operating leases | 1,961 | 1,764 | 177 | 20 | | |
| Noncancellable purchase obligations | 13,140 | 13,140 | | | | |
| Uncertain tax liabilities | 1,394 | | | | | 1,394 |
| Total | \$ 21,984 | \$ 15,858 | \$ 2,844 | \$ 1,888 | \$ | \$ 1,394 |

As of April 30, 2013, we had purchase obligations with our independent contract manufacturers of \$13.1 million.

Uncertain tax liabilities represent our liabilities for uncertain tax positions as of April 30, 2013. We are unable to reasonably estimate the timing of payments in individual years due to uncertainties in the timing of the effective settlement of tax positions.

Table of Contents

Off-Balance Sheet Arrangements

As of April 30, 2013, we did not engage in any off-balance sheet arrangements, including the use of structured finance, special purpose entities or variable interest entities.

Recent Authoritative Accounting Guidance

See Note 1 to our unaudited condensed consolidated financial statements for information regarding recently issued accounting pronouncements.

Critical Accounting Policies and Significant Management Estimates

There have been no material changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates described in our Annual Report on Form 10-K for the 2013 fiscal year filed with the SEC on April 4, 2013.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

We had cash totaling \$104.3 million and \$100.5 million at April 30, 2013 and January 31, 2013, respectively. Our cash consists of cash in standard bank accounts and are held for working capital purposes. We do not enter into investments for trading or speculative purposes.

Foreign Currency Risk

To date, all of our product sales and inventory purchases have been denominated in U.S. dollars. We therefore have not had any foreign currency risk associated with these two activities. The functional currency of all of our entities is the U.S. dollar. Our operations outside of the United States incur operating expenses and hold assets and liabilities denominated in foreign currencies, principally the New Taiwan Dollar and the Chinese Yuan Renminbi. Our results of operations and cash flows are, therefore, subject to fluctuations due to changes in foreign currency exchange rates. However, we believe that the exposure to foreign currency fluctuation from operating expenses is immaterial at this time as the related costs do not constitute a significant portion of our total expenses. As we grow our operations, our exposure to foreign currency risk could become more significant. To date, we have not entered into any foreign currency exchange contracts and currently do not expect to enter into foreign currency exchange contracts for trading or speculative purposes.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer (our principal executive officer) and Chief Financial Officer (our principal financial officer), has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a- 15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange Act)), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that as of such date, our disclosure controls and procedures were effective.

Table of Contents***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting identified in management's evaluation pursuant to Rules 13a-15(d) or 15d-15(d) of the Exchange Act during the period covered by this Quarterly Report on Form 10-Q that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on the Effectiveness of Controls

Control systems, no matter how well conceived and operated, are designed to provide a reasonable, but not an absolute, level of assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Because of the inherent limitations in any control system, misstatements due to error or fraud may occur and not be detected.

PART II OTHER INFORMATION**ITEM 1. Legal Proceedings**

We are not engaged in any material legal proceedings at this time.

ITEM 1A. Risk Factors

Certain factors may have a material adverse effect on our business, financial condition and results of operations. You should consider carefully the risks and uncertainties described below, in addition to other information contained in this Quarterly Report on Form 10-Q, including our unaudited condensed consolidated financial statements and related notes. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that adversely affect our business. If any of the following risks actually occurs, our business, financial condition, results of operations, and future prospects could be materially and adversely affected. In that event, the trading price of our ordinary share could decline, and you could lose part or all of your investment.

Risks Related to Our Business and Our Industry

If our customers do not design our solutions into their product offerings, or if our customers' product offerings are not commercially successful, our business would suffer.

We sell our video and image processing system-on-a-chip, or SoC, solutions to original equipment manufacturers, or OEMs, who include our SoCs in their products, and to original design manufacturers, or ODMs, who include our SoCs in the products that they supply to OEMs. We refer to ODMs as our customers and OEMs as our end customers, except as otherwise indicated or as the context otherwise requires. Our video and image processing SoCs are generally incorporated into our customers' products at the design stage, which is referred to as a design win. As a result, we rely on OEMs to design our solutions into the products that they design and sell. Without these design wins, our business would be harmed. We often incur significant expenditures developing a new SoC solution without any assurance that an OEM will select our solution for design into its own product. Once an OEM designs a competitor's device into its product, it becomes significantly more difficult for us to sell our SoC solutions to that OEM because changing suppliers involves significant cost, time, effort and risk for the OEM. Furthermore, even if an OEM designs one of our SoC solutions into its product, we cannot be assured that the OEM's product will be commercially successful over time or at all or that we will receive or continue to receive any revenue from that OEM. For example, improved smartphone video capture capabilities, and rapid adoption of smartphones by consumers, led to the decline of an entire category of pocket video cameras aimed at the casual video capture market. In fiscal year 2011, pocket video revenue represented approximately 40% of our total revenue. The proliferation of smartphones and their ability to capture high-quality video and still images significantly impacted this market, decreasing pocket video cameras contribution to approximately 15% of our total revenue in fiscal year 2012 and approximately 1.2% of our total revenue in fiscal year 2013. If other product categories incorporating our SoC solutions are not commercially successful or experience rapid decline, our revenue and business will suffer.

Table of Contents

We depend on a limited number of customers and end customers for a significant portion of our revenue. If we fail to retain or expand our customer relationships, our revenue could decline.

We derive a significant portion of our revenue from a limited number of ODMs who build products on behalf of a limited number of OEMs and from a limited number of OEMs to whom we ship directly. We anticipate that this customer concentration will continue for the foreseeable future. For the three months ended April 30, 2013, sales directly and through our logistics providers to our five largest customers collectively was estimated to be 58.2% of our revenue, and sales to our 10 largest customers collectively was estimated to be 71.7% of our revenue. For the three months ended April 30, 2013, our largest ODM customer was estimated to be 42.3% of our revenue and built products for several OEM customers as well as for its own brand. We believe that our operating results for the foreseeable future will continue to depend on sales to a relatively small number of customers and end-customers. In the future, these customers may decide not to purchase our SoC solutions at all, may purchase fewer solutions than they did in the past or may alter their purchasing patterns. As substantially all of our sales to date have been made on a purchase order basis, these customers may cancel, change or delay product purchase commitments with little or no notice to us and without penalty and may make our revenue volatile from period to period. For example, our largest OEM end customer in fiscal year 2011, Eastman Kodak Company, or Kodak, closed its camera division in January 2012. The loss of a significant customer like Kodak could happen again at any time and without notice, and such loss would likely harm our financial condition and results of operations.

In addition, our relationships with some customers may deter other potential customers who compete with these customers from buying our solutions. To attract new customers or retain existing customers, we may have to offer these customers favorable prices on our solutions. In that event, our average selling prices and gross margins would decline. The loss of a key customer, a reduction in sales to any key customer or our inability to attract new customers could seriously impact our revenue and harm our results of operations.

Achieving design wins is subject to lengthy competitive selection processes that require us to incur significant costs. Even if we begin a product design, a customer may decide to cancel or change its product plans, resulting in no revenue from such expenditures.

We are focused on selling our video and image processing solutions to ODMs and OEMs for incorporation into their products at the design stage. These efforts to achieve design wins typically are lengthy, especially in new markets we intend to address, and in any case can require us to both incur design and development costs and dedicate scarce engineering resources in pursuit of a single customer opportunity. We may not prevail in the competitive selection process and, even when we do achieve a design win, we may never generate any revenue despite incurring development expenditures. For example, in the past we had achieved a significant design win and projected substantial future revenue from that end customer as a result of that design win. Subsequently, based on changes in that end customer's assessment of the consumer market, among other factors, the end customer abruptly shut down its business unit with which we achieved the design win, with no notice to us.

Table of Contents

These risks are exacerbated by the fact that some of our end customers' products, particularly in the camera market, likely will have short life cycles. Further, even after securing a design win, we have experienced and may again experience delays in generating revenue from our solutions as a result of the lengthy product development cycle typically required, if we generate any revenue at all as a result of any such design win.

Our customers generally take a considerable amount of time to evaluate our solutions. The typical time from early engagement by our sales force to actual product introduction runs from nine to 12 months for the camera market, and 12 to 24 months for the infrastructure market, though it may take longer in new markets we intend to address. The delays inherent in these lengthy sales cycles increase the risk that a customer will decide to cancel, curtail, reduce or delay its product plans, causing us to lose anticipated sales. In addition, any delay or cancellation of a customer's plans could harm our financial results, as we may have incurred significant expense and generated no revenue. Finally, our customers' failure to successfully market and sell their products could reduce demand for our SoC solutions and harm our business, financial condition and results of operations. If we were unable to generate revenue after incurring substantial expenses to develop any of our solutions, our business would suffer.

We do not have long-term supply contracts with our third-party manufacturing vendors, and they may not allocate sufficient capacity to us at reasonable prices to meet future demands for our solutions.

The semiconductor industry is subject to intense competitive pricing pressure from customers and competitors. Accordingly, any increase in the cost of our solutions, whether by adverse purchase price variances or adverse manufacturing cost variances, will reduce our gross margins and operating profit. We currently do not have long-term supply contracts with any of our third-party vendors, and we typically negotiate pricing on a purchase order-by-purchase order basis. Therefore, they are not obligated to perform services or supply product to us for any specific period, in any specific quantities, or at any specific price, except as may be provided in a particular purchase order. Availability of foundry capacity has in the recent past been limited due to strong demand. The ability of our foundry vendors to provide us with product, which is sole sourced at each foundry, is limited by their available capacity, existing obligations and technological capabilities. Foundry capacity may not be available when we need it or at reasonable prices. None of our third-party foundry or assembly and test vendors has provided contractual assurances to us that adequate capacity will be available to us to meet our anticipated future demand for our solutions. Our foundry and assembly and test vendors may allocate capacity to the production of other companies' products while reducing deliveries to us on short notice. In particular, other customers that are larger and better financed than we are or that have long-term agreements with our foundry or assembly and test vendors may cause our foundry or assembly and test vendors to reallocate capacity to those customers, decreasing the capacity available to us. Converting or transferring manufacturing from a primary location or supplier to a backup foundry vendor could be expensive and could take two or more quarters. As we transition to more advanced process nodes beyond 32 nanometer, or nm, we will be increasingly dependent upon Samsung Electronics Co., Ltd., or Samsung, Taiwan Semiconductor Manufacturing Co., Ltd., or TSMC, who are two of the only three foundries currently available for certain advanced process technologies that we may utilize.

If, in the future, we enter into arrangements with suppliers that include additional fees to expedite delivery, nonrefundable deposits or loans in exchange for capacity commitments or commitments to purchase specified quantities over extended periods, such arrangements may be costly, reduce our financial flexibility and be on terms unfavorable to us, if we are able to secure such arrangements at all. Moreover, if we are able to secure foundry capacity, we may be obligated to use all of that capacity or incur penalties. These penalties could harm our financial results. To date, we have not entered into any such arrangements with our suppliers. If we need additional foundry or assembly and test subcontractors because of increased demand or the inability to obtain timely and adequate deliveries from our current vendors, we may not be able to do so cost-effectively, if at all.

Table of Contents

Our customers may cancel their orders, change production quantities or delay production. If we fail to accurately forecast demand for our solutions, revenue shortfalls, or excess, obsolete or insufficient inventory could result.

Our customers typically do not provide us with firm, long-term purchase commitments. Substantially all of our sales are made on a purchase order basis, which permits our customers to cancel, change or delay their product purchase commitments with little or no notice to us and without penalty to them. Because production lead times often exceed the amount of time required by our customers to fill their orders, we often must build SoCs in advance of orders, relying on an imperfect demand forecast to project volumes and product mix.

Our SoCs are incorporated into products manufactured by or for our end customers, and as a result, demand for our solutions is influenced by the demand for our customers' products. Our ability to accurately forecast demand can be adversely affected by a number of factors, including inaccurate forecasting by our customers, miscalculations by our customers of their inventory requirements, changes in market conditions, adverse changes in our product order mix and fluctuating demand for our customers' products. Even after an order is received, our customers may cancel these orders or request a decrease in production quantities. Any such cancellation or decrease subjects us to a number of risks, most notably that our projected sales will not materialize on schedule or at all, leading to unanticipated revenue shortfalls and excess or obsolete inventory that we may be unable to sell to other customers.

Alternatively, if we are unable to project customer requirements accurately, we may not build enough SoCs, which could lead to delays in product shipments and lost sales opportunities in the near term, as well as force our customers to identify alternative sources, which could affect our ongoing relationships with these customers. We have in the past had customers significantly increase their requested production quantities with little or no advance notice. If we do not fulfill customer demands in a timely manner, our customers may cancel their orders and we may be subject to customer claims for cost of replacement. In addition, the rapid pace of innovation in our industry could render portions of our inventory obsolete. Excess or obsolete inventory levels could result in unexpected expenses or increases in our reserves that could adversely affect our business, operating results and financial condition. In addition, any significant future cancellations or deferrals of product orders could harm our margins, increase our write-offs due to product obsolescence and restrict our ability to fund our operations.

Our target markets may not grow or develop as we currently expect and are subject to market risks, any of which could harm our business, revenue and operating results.

To date, our revenue has been attributable to demand for our video and image processing SoCs in the camera and infrastructure markets and the growth of these overall markets. We initially focused on the infrastructure market, and then leveraged our knowledge and experience to design solutions for the camera market. We derive the majority of our revenue from the camera market, and our operating results are increasingly affected by trends in the camera market. These trends include demand for higher resolution, increasing functionality and greater storage and connectivity requirements, while accommodating more sophisticated standards for video compression. We may be unable to predict the timing or development of these markets with accuracy. For example, the proliferation of smartphones having the ability to capture high-quality video and still images has significantly impacted this market in a relatively short period of time and continues to impact this market. In the Internet Protocol, or IP, security camera market, a slower than expected adoption rate for digital technology in place of analog solutions could slow the demand for our solutions. If our target markets, such as wearable sports cameras, automotive aftermarket cameras, IP security cameras, digital still cameras, or DSCs, and telepresence cameras, do not grow or develop in ways that we currently expect, demand for our video and image processing SoCs may not materialize as expected and our business and operating results could suffer.

Table of Contents

We are dependent on sales of a limited number of video and image processing solutions, and a decline in market adoption of these solutions could harm our business.

From inception through April 30, 2013, our revenue has been generated primarily from the sale of a limited number of high-definition, or HD, video and image processing SoC solutions in the camera and infrastructure markets. Moreover, we currently derive a significant amount of our revenue from the sale of our SoCs for use in the camera market and we expect to do so for the next several years. As a result, continued market adoption of our SoC solutions in the camera market is critical to our future success. If demand for our SoC solutions were to decline, or demand for products incorporating our solutions declines, does not continue to grow or does not grow as expected, our revenue would decline and our business would be harmed.

If we fail to develop and introduce new or enhanced solutions on a timely basis, our ability to attract and retain customers could be impaired and our competitive position could be harmed.

We operate in a dynamic environment characterized by rapidly changing technologies and technological obsolescence. To compete successfully, we must design, develop, market and sell enhanced solutions that provide increasingly higher levels of performance and functionality and that meet the cost expectations of our customers. Our existing or future solutions could be rendered obsolete by the introduction of new products by our competitors; convergence of other markets, such as smartphones, with or into the camera market; the market adoption of products based on new or alternative technologies; or the emergence of new industry standards for video compression. In addition, the markets for our solutions are characterized by frequent introduction of next-generation and new products, short product life cycles, increasing demand for added functionality and significant price competition. If we or our customers are unable to manage product transitions in a timely and cost-effective manner, our business and results of operations would suffer.

Our failure to anticipate or timely develop new or enhanced solutions in response to technological shifts could result in decreased revenue and our competitors achieving design wins that we sought. In particular, we may experience difficulties with product design, development of new software, manufacturing, marketing or qualification that could delay or prevent our development, introduction or marketing of new or enhanced solutions. In addition, delays in development could impair our relationships with our customers and negatively impact sales of our solutions under development. Moreover, it is possible that our customers may develop their own product or adopt a competitor's solution for products that they currently buy from us. If we fail to introduce new or enhanced solutions that meet the needs of our customers or penetrate new markets in a timely fashion, we will lose market share and our operating results will be adversely affected.

If we fail to penetrate new markets, our revenue and financial condition could be harmed.

In the past several years, a significant amount of our revenue was generated from sales of our products to OEMs and ODMs of high definition, or HD, video cameras and broadcasting infrastructure equipment. Our future revenue growth, if any, will depend in part on our ability to expand within these markets with our video and image processing SoC solutions, particularly for wearable sports cameras, automotive aftermarket cameras and DSCs, and to enter new markets. Each of these markets presents distinct and substantial risks and, in many cases, requires us to develop new software to address the particular requirements of that market. If any of these markets do not develop as we currently anticipate or if we are unable to penetrate them successfully, our revenue could decline.

Table of Contents

Some of these markets are primarily served by only a few large, multinational OEMs with substantial negotiating power relative to us and, in some instances, with internal solutions that are competitive to our products. Meeting the technical requirements and securing design wins with any of these companies will require a substantial investment of our time and resources. We cannot assure you that we will secure design wins from these or other companies or that we will achieve meaningful revenue from the sales of our solutions into these markets.

If we fail to penetrate these or other new markets we are targeting, our revenue likely will decrease over time and our financial condition could suffer.

The average selling prices of video and image processing solutions in our target markets have historically decreased over time and will likely do so in the future, which could harm our revenue and gross margins.

Average selling prices of semiconductor products in the markets we serve have historically decreased over time, and we expect such declines to continue to occur for our solutions over time. Our gross margins and financial results will suffer if we are unable to offset reductions in our average selling prices by reducing our costs, developing new or enhanced SoC solutions on a timely basis with higher selling prices or gross margins, or increasing our sales volumes. Additionally, because we do not operate our own manufacturing, assembly or testing facilities, we may not be able to reduce our costs as rapidly as companies that operate their own facilities, and our costs may even increase, which could also reduce our gross margins. In the past, we have reduced the prices of our SoC solutions in anticipation of future competitive pricing pressures, new product introductions by us or our competitors and other factors. We expect that we will have to do so again in the future.

We expect competition to increase in the future, which could have an adverse effect on our revenue and market share.

The global semiconductor market in general, and the video and image processing markets in particular, are highly competitive. We compete in different target markets to various degrees on the basis of a number of competitive factors, including our solutions performance, features, functionality, energy efficiency, size, ease with which our solution may be integrated into our customers products, customer support, reliability and price, as well as on the basis of our reputation. We expect competition to increase and intensify as more and larger semiconductor companies enter our markets, and as the internal resources of large OEMs grow. Increased competition could result in price pressure, reduced profitability and loss of market share, any of which could harm our business, revenue and operating results.

Our competitors range from large, international companies offering a wide range of semiconductor products to smaller companies specializing in narrow markets. Our primary competitors in the camera market include CSR plc (who acquired Zoran Corporation in August 2011), Fujitsu Limited, HiSilicon Technologies Co., Ltd. and Texas Instruments Incorporated, as well as vertically integrated divisions of consumer device OEMs, including Canon Inc., Panasonic Corporation and Sony Corporation. In the market for automotive aftermarket cameras, we compete against Core Logic, Inc., Novatek Microelectronics Corp. and Sunplus Technology Co. Ltd. Our primary competitors in the infrastructure market include Intel Corporation, Magnum Semiconductor, Inc. and Texas Instruments Incorporated. Certain of our customers and suppliers also have divisions that produce products competitive with ours. We expect competition in our current markets to increase in the future as existing competitors improve or expand their product offerings and as potential new competitors, such as Broadcom Corporation, NVIDIA Corporation, Qualcomm Incorporated and Samsung, enter these markets.

Table of Contents

Our ability to compete successfully depends on elements both within and outside of our control, including industry and general economic trends. Many of our competitors are substantially larger, have greater financial, technical, marketing, distribution, customer support and other resources, are more established than we are and have significantly better brand recognition and broader product offerings which may enable them to better withstand adverse economic or market conditions in the future. Our ability to compete will depend on a number of factors, including:

our ability to anticipate market and technology trends and successfully develop solutions that meet market needs;

our success in identifying and penetrating new markets, applications and customers;

our ability to understand the price points and performance metrics of competing products in the marketplace;

our solutions' performance and cost-effectiveness relative to that of competing products;

our ability to gain access to leading design tools and product specifications at the same time as our competitors;

our ability to develop and maintain relationships with key OEMs and ODMs;

our products' effective implementation of video processing standards;

our ability to protect our intellectual property;

our ability to expand international operations in a timely and cost-efficient manner;

our ability to deliver products in volume on a timely basis at competitive prices;

our ability to support our customers' incorporation of our solutions into their products; and

our ability to recruit design and application engineers with expertise in image video and image processing technologies and sales and marketing personnel.

Our competitors may also establish cooperative relationships among themselves or with third parties or acquire companies that provide similar products to ours. As a result, new competitors or alliances may emerge that could acquire significant market share. Any of these factors, alone or in combination with others, could harm our business and result in a loss of market share and an increase in pricing pressure.

If we are unable to manage any future growth, we may not be able to execute our business plan and our operating results could suffer.

Our business has grown rapidly. Our future operating results depend to a large extent on our ability to successfully manage any expansion and growth, including the challenges of managing a company with headquarters in the United States and the majority of its employees in Asia. To manage our growth successfully and handle the responsibilities of being a public company, we believe we must effectively, among other things:

recruit, hire, train and manage additional qualified engineers for our research and development activities, particularly in our offices in Asia and especially for the positions of semiconductor design and systems and applications engineering;

Table of Contents

add additional sales personnel;

add additional finance and accounting personnel;

implement and improve our administrative, financial and operational systems, procedures and controls; and

enhance our information technology support for enterprise resource planning and design engineering by adapting and expanding our systems and tool capabilities, and properly training new hires as to their use.

We are increasing our investment in research and development and other functions to grow our business. We are likely to incur the costs associated with these increased investments earlier than some of the anticipated benefits, and the return on these investments, if any, may be lower, may develop more slowly than we expect or may not materialize.

If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities or develop new solutions, and we may fail to satisfy customer product or support requirements, maintain product quality, execute our business plan or respond to competitive pressures.

A substantial portion of our revenue is processed through a single logistics provider and the loss of this logistics provider may cause disruptions in our shipments, which may adversely affect our operations and financial condition.

We sell most of our solutions through a single logistics provider, Wintech Microelectronics Co., Ltd., or Wintech, which serves as our non-exclusive sales representative in all of Asia other than Japan. Approximately 40% and 75% of our revenue was derived from sales through Wintech for the three months ended April 30, 2013 and 2012, respectively. We anticipate that a significant portion of our revenue will continue to be derived from sales through Wintech in the foreseeable future. Our current agreement with Wintech is effective until September 2015, unless it is terminated earlier by either party for any or no reason with 90 days written notice or by failure of the breaching party to cure a material breach within 30 days following written notice of such material breach by the non-breaching party. Our agreement with Wintech will automatically renew for additional successive 12-month terms unless at least 60 days before the end of the then-current term either party provides written notice to the other party that it elects not to renew the agreement. Termination of the relationship with Wintech, either by us or by Wintech, could result in a temporary or permanent loss of revenue. We may not be successful in finding suitable alternative logistics providers on satisfactory terms, or at all, and this could adversely affect our ability to effectively sell our solutions in certain geographical locations or to certain end customers. Additionally, if we terminate our relationship with Wintech, we may be obligated to repurchase unsold product, which could be difficult or impossible to sell to other end customers. Furthermore, Wintech, or any successor or other logistics providers we do business with, may face issues obtaining credit, which could impair their ability to make timely payments to us.

Fluctuations in our operating results on a quarterly and annual basis could cause the market price of our ordinary shares to decline.

Our revenue and operating results have fluctuated significantly from period to period in the past and are likely to do so in the future. In particular, our business tends to be seasonal with higher revenue in our third quarter as our customers typically increase their production to meet year-end demand for their products. As a result, you should not rely on period-to-period comparisons of our operating results as an indication of our future performance. In future periods, our revenue and results of operations may be below the expectations of analysts and investors, which could cause the market price of our ordinary shares to decline.

Table of Contents

Factors that may affect our operating results include:

shifts in consumer preferences and any resultant change in demand for video and image capture devices into which our solutions are incorporated;

changes in the competitive dynamics of our markets, including new entrants or pricing pressures;

variances in order patterns by our customers, particularly any of our significant customers;

our ability to successfully define, design and release new solutions in a timely manner that meet our customers' needs;

changes in manufacturing costs, including wafer, test and assembly costs, mask costs, manufacturing yields and product quality and reliability;

timely availability of adequate manufacturing capacity from our manufacturing subcontractors;

the timing of product announcements by our competitors or by us;

future accounting pronouncements and changes in accounting policies;

volatility in our share price, which may lead to higher stock-based compensation expense;

general socioeconomic and political conditions in the countries where we operate or where our products are sold or used; and

costs associated with litigation, especially related to intellectual property.

Moreover, the semiconductor industry has historically been cyclical in nature, reflecting overall economic conditions as well as budgeting and buying patterns of consumers. We expect these cyclical conditions to continue. As a result, our quarterly operating results are difficult to predict, even in the near term. Our expense levels are relatively fixed in the short term and are based, in part, on our expectations of future revenue. If revenue levels are below our expectations, we may experience declines in margins and profitability or incur losses.

If we do not sustain our growth rate, we may not be able to execute our business plan and our operating results could suffer.

We have experienced significant growth in a short period of time. Our revenue increased from \$21.5 million in fiscal year 2008 to \$121.1 million in fiscal year 2013. Compared to the three months ended April 30, 2012, our revenue increased by 31% from \$25.9 million to \$33.9 million for the three months ended April 30, 2013. We may not achieve similar growth rates in future periods. You should not rely on our revenue growth, gross margins or operating results for any prior quarterly or annual periods as an indication of our future operating performance. If we are unable to maintain adequate revenue growth, our financial results could suffer and our stock price could decline.

Table of Contents

Due to our limited operating history, we may have difficulty accurately predicting our future revenue and appropriately budgeting our expenses.

We were incorporated in 2004 and first generated product revenue in the third quarter of fiscal year 2006. As a result, we have a limited operating history from which to predict future revenue. This limited operating experience, combined with the rapidly evolving nature of the markets in which we sell our solutions, substantial uncertainty concerning how these markets may develop and other factors beyond our control, limits our ability to accurately forecast quarterly or annual revenue. In addition, because we record a significant portion of our revenue from sales when we have received notification from our logistics providers that they have sold our products, some of the revenue we record in a quarter may be derived from sales of products shipped to our logistics providers during previous quarters. This revenue recognition methodology limits our ability to forecast quarterly or annual revenue accurately. We are currently expanding our staffing and increasing our expenditures in anticipation of future revenue growth. If our revenue does not increase as anticipated, we could incur significant losses due to our higher expense levels if we are not able to decrease our expenses in a timely manner to offset any shortfall in future revenue.

While we intend to continue to invest in research and development, we may be unable to make the substantial investments that are required to remain competitive in our business.

The semiconductor industry requires substantial investment in research and development in order to bring to market new and enhanced solutions. Our research and development expense was \$11.3 million and \$11.5 million for the three months ended April 30, 2013 and 2012, respectively. We expect to increase our research and development expenditures as compared to prior periods as part of our strategy of focusing on the development of innovative and sustainable video and image processing solutions. We do not know whether we will have sufficient resources to maintain the level of investment in research and development required to remain competitive. In addition, we cannot assure you that the technologies which are the focus of our research and development expenditures will become commercially successful or generate any revenue.

We may experience difficulties demonstrating the value to customers of newer, higher priced and higher margin solutions if they believe existing solutions are adequate to meet end customer expectations.

As we develop and introduce new solutions, we face the risk that customers may not value or be willing to bear the cost of incorporating these newer solutions into their products, particularly if they believe end customers are satisfied with current solutions. Regardless of the improved features or superior performance of the newer solutions, customers may be unwilling to adopt our new solutions due to design or pricing constraints. Owing to the extensive time and resources that we invest in developing new solutions, if we are unable to sell customers new generations of our solutions, our revenue could decline and our business, financial condition, operating results and cash flows could be negatively affected.

The complexity of our solutions could result in unforeseen delays or expenses from undetected defects, errors or bugs in hardware or software which could reduce the market adoption of our new solutions, damage our reputation with current or prospective customers and adversely affect our operating costs.

Highly complex SoC solutions such as ours frequently contain defects, errors and bugs when they are first introduced or as new versions are released. We have in the past and may in the future experience these defects, errors and bugs. If any of our solutions have reliability, quality or compatibility problems, we may not be able to successfully correct these problems in a timely manner or at all. In addition, if any of our proprietary features contain defects, errors or bugs when first introduced or as new versions of our solutions are released, we may be unable to timely correct these problems. Consequently, our reputation may be damaged and customers may be reluctant to buy our solutions, which could harm our ability to retain existing customers and attract new customers, and could adversely affect our financial results. In addition, these defects, errors or bugs could interrupt or delay sales to our customers. If any of these problems are not found until after we have commenced commercial production of a new product, we may incur significant additional development costs and product recall, repair or replacement costs. These problems may also result in claims against us by our customers or others.

Table of Contents

The loss of any of our key personnel could seriously harm our business, and our failure to attract or retain qualified management, engineering, sales and marketing talent could impair our ability to grow our business.

We believe our future success will depend in large part upon our ability to attract, retain and motivate highly skilled management, engineering and sales and marketing personnel. The loss of any key employees or the inability to attract, retain or motivate qualified personnel, including engineers and sales and marketing personnel, could delay the development and introduction of, and harm our ability to sell, our solutions. We believe that our future success is dependent on the contributions of Fermi Wang, our co-founder, Chairman of the Board of Directors, President and Chief Executive Officer, Les Kohn, our co-founder and Chief Technology Officer, George Laplante, our Chief Financial Officer, Didier LeGall, our Executive Vice President, and Christopher Day, our Vice President, Marketing and Business Development. Each of these executive officers is an at-will employee. The loss of the services of Dr. Wang, Mr. Kohn, Mr. Laplante, Dr. LeGall, Mr. Day or certain other key personnel could harm our business, financial condition and results of operations. For example, if any of these individuals were to leave unexpectedly, we could face substantial difficulty in hiring qualified successors and could experience a loss in productivity during the search for any such successor and while any successor is integrated into our business and operations.

Our key technical and engineering personnel represent a significant asset and serve as the source of our technological and product innovations. We plan to recruit software and system engineers with expertise in video processing technologies, primarily in Taiwan and China. We may not be successful in attracting, retaining and motivating sufficient numbers of technical and engineering personnel to support our anticipated growth. The competition for qualified engineering personnel in our industry, and particularly in Asia, is very intense. If we are unable to hire, train and retain qualified engineering personnel in a timely manner, our ability to grow our business will be impaired. In addition, if we are unable to retain our existing engineering personnel, our ability to maintain or grow our revenue will be adversely affected.

Camera manufacturers incorporate components supplied by multiple third parties, and a supply shortage or delay in delivery of these components could delay orders for our solutions by our customers.

Our customers purchase components used in the manufacture of their cameras from various sources of supply, often involving several specialized components, including lenses and sensors. Any supply shortage or delay in delivery by third-party component suppliers, or a third-party supplier's cessation or shut down of its business, may prevent or delay production of our customers' products. For example, in the camera market, the unavailability of complementary metal-oxide semiconductor, or CMOS, sensors could slow adoption of our solutions in the DSC market. In addition, replacement or substitute components may not be available on commercially reasonable terms, or at all. As a result of delays in delivery or supply shortages of third-party components, orders for our solutions may be delayed or canceled and our business may be harmed. Similarly, errors or defects within a camera system or in the manner in which the various components interact could prevent or delay production of our customers' products, which could harm our business.

Table of Contents

We outsource our wafer fabrication, assembly and testing operations to third parties, and if these parties fail to produce and deliver our products according to requested demands in specification, quantity, cost and time, our reputation, customer relationships and operating results could suffer.

We rely on third parties for substantially all of our manufacturing operations, including wafer fabrication, assembly and testing. Currently, the majority of our SoCs are supplied by Samsung in South Korea, from whom we have the option to purchase both fully assembled and tested products as well as tested die in wafer form for assembly. Samsung subcontracts the assembly and initial testing of the assembled chips it supplies to us to Signetics Corporation and STATS ChipPAC Ltd. In the case of purchases of tested die from Samsung, we contract the assembly to Advanced Semiconductor Engineering, Inc., or ASE. We also have products supplied by Global UniChip Corporation, or GUC, in Taiwan, from whom we purchase fully assembled and tested products. The wafers used by GUC in the assembly of our products are manufactured by TSMC in Taiwan. The assembly is done by GUC subcontracted assembly suppliers ASE, and Powertech Technology Inc, or PTI. Final testing of all of our products is handled by King Yuan Electronics Co., Ltd. or Sigurd Corporation under the supervision of our engineers. We depend on these third parties to supply us with material of a requested quantity in a timely manner that meets our standards for yield, cost and manufacturing quality. We do not have any long-term supply agreements with any of our manufacturing suppliers. If one or more of these vendors terminates its relationship with us, or if we encounter any problems with our manufacturing supply chain, our ability to ship our solutions to our customers on time and in the quantity required would be adversely affected, which in turn could cause an unanticipated decline in our sales and damage our customer relationships.

If our foundry vendors do not achieve satisfactory yields or quality, our reputation and customer relationships could be harmed.

The fabrication of our video and image processing SoC solutions is a complex and technically demanding process. Minor deviations in the manufacturing process can cause substantial decreases in yields, and in some cases, cause production to be suspended. Our foundry vendors, from time to time, experience manufacturing defects and reduced manufacturing yields, including in the fabrication of our SoCs. Changes in manufacturing processes or the inadvertent use of defective or contaminated materials by our foundry vendors could result in lower than anticipated manufacturing yields or unacceptable performance of our SoCs. Many of these problems are difficult to detect at an early stage of the manufacturing process and may be time consuming and expensive to correct. Poor yields from our foundry vendors, or defects, integration issues or other performance problems in our solutions, could cause us significant customer relations and business reputation problems, harm our financial results and give rise to financial or other damages to our customers. Our customers might consequently seek damages from us for their losses. A product liability claim brought against us, even if unsuccessful, would likely be time consuming and costly to defend.

Each of our SoC solutions is manufactured at a single location. If we experience manufacturing problems at a particular location, we would be required to transfer manufacturing to a new location or supplier. Converting or transferring manufacturing from a primary location or supplier to a backup fabrication facility could be expensive and could take two or more quarters. During such a transition, we would be required to meet customer demand from our then-existing inventory, as well as any partially finished goods that could be modified to the required product specifications. We do not seek to maintain sufficient inventory to address a lengthy transition period because we believe it is uneconomical to keep more than minimal inventory on hand. As a result, we may not be able to meet customer needs during such a transition, which could delay shipments, cause production delays, result in a decline in our sales and damage our customer relationships.

Table of Contents

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

We aim to use the most advanced manufacturing process technology appropriate for our products that is available from our third-party foundries. As a result, we periodically evaluate the benefits of migrating our solutions to smaller geometry process technologies in order to improve performance and reduce costs. We believe this strategy will help us remain competitive. These ongoing efforts require us from time to time to modify the manufacturing processes for our products and to redesign some products, which in turn may result in delays in product deliveries. We may face difficulties, delays and increased expense as we transition our products to new processes and potentially to new foundries. We depend on Samsung and TSMC, as the principal foundries for our products, to transition to new processes successfully. We cannot assure you that Samsung or TSMC will be able to effectively manage such transitions or that we will be able to maintain our relationship with Samsung or TSMC or develop relationships with new foundries. Moreover, as we transition to more advanced process nodes beyond 32nm, we will be increasingly dependent upon Samsung and TSMC, who are two of the only three foundries currently available for certain advanced process technologies. If we or our foundry vendors experience significant delays in transitioning to smaller geometries or fail to efficiently implement transitions, we could experience reduced manufacturing yields, delays in product deliveries and increased costs, all of which could harm our relationships with our customers and our operating results. As new processes become more prevalent, we expect to continue to integrate greater levels of functionality, as well as more end-customer and third-party intellectual property, into our solutions. We may not be able to achieve higher levels of design integration or deliver new integrated solutions on a timely basis.

We rely on third-party vendors to supply software development tools to us for the development of our new products, and we may be unable to obtain the tools necessary to develop or enhance new or existing products.

We rely on third-party software development tools to assist us in the design, simulation and verification of new products or product enhancements. To bring new products or product enhancements to market in a timely manner, or at all, we need software development tools that are sophisticated enough or technologically advanced enough to complete our design, simulations and verifications. In the future, the design requirements necessary to meet consumer demands for more features and greater functionality from our solutions may exceed the capabilities of available software development tools. Unavailability of software development tools may result in our missing design cycles or losing design wins, either of which could result in a loss of market share or negatively impact our operating results.

Because of the importance of software development tools to the development and enhancement of our solutions, our relationships with leaders in the computer-aided design industry, including Cadence Design Systems, Inc., Mentor Graphics Corporation and Synopsys, Inc., are critical to us. We have invested significant resources to develop relationships with these industry leaders. We believe that utilizing next-generation development tools to design, simulate and verify our products will help us remain at the forefront of the video compression market, and develop solutions that utilize leading-edge technology on a rapid basis. If these relationships are not successful, we may be unable to develop new products or product enhancements in a timely manner, which could result in a loss of market share, a decrease in revenue or negatively impact our operating results.

Table of Contents

Our failure to adequately protect our intellectual property rights could impair our ability to compete effectively or defend ourselves from litigation, which could harm our business, financial condition and results of operations.

Our success depends, in part, on our ability to protect our intellectual property. We rely primarily on patent, copyright, trademark and trade secret laws, as well as confidentiality and non-disclosure agreements and other contractual protections, to protect our proprietary technologies and know-how, all of which offer only limited protection. The steps we have taken to protect our intellectual property rights may not be adequate to prevent misappropriation of our proprietary information or infringement of our intellectual property rights, and our ability to prevent such misappropriation or infringement is uncertain, particularly in countries outside of the United States. As of April 30, 2013, we had twenty issued and allowed patents in the United States plus nine additional continuation patents, three issued patents in China, two issued patent in Japan and thirty-two pending and provisional patent applications in the United States. Even if the pending patent applications are granted, the rights granted to us may not be meaningful or provide us with any commercial advantage. For example, these patents could be opposed, contested, circumvented, designed around by our competitors or be declared invalid or unenforceable in judicial or administrative proceedings. The failure of our patents to adequately protect our technology might make it easier for our competitors to offer similar products or technologies. Our foreign patent protection is generally not as comprehensive as our U.S. patent protection and may not protect our intellectual property in some countries where our products are sold or may be sold in the future. Many U.S.-based companies have encountered substantial intellectual property infringement in foreign countries, including countries where we sell products. Even if foreign patents are granted, effective enforcement in foreign countries may not be available. For example, the legal environment relating to intellectual property protection in China is relatively weak, often making it difficult to create and enforce such rights. We may not be able to effectively protect our intellectual property rights in China or elsewhere. If such an impermissible use of our intellectual property or trade secrets were to occur, our ability to sell our solutions at competitive prices may be adversely affected and our business, financial condition, operating results and cash flows could be materially and adversely affected.

The legal standards relating to the validity, enforceability and scope of protection of intellectual property rights are uncertain