

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 1997.

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: 0-21184  
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MICROCHIP TECHNOLOGY INCORPORATED  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of  
Incorporation or Organization)

86-0629024  
(I.R.S. Employer  
Identification No.)

2355 W. Chandler Blvd., Chandler, AZ 85224-6199  
(602) 786-7200  
(Address, Including Zip Code, and Telephone Number,  
Including Area Code, of Registrant's  
Principal Executive Offices)

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 the filing requirements for the past 90 days.

Yes X No  
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The number of shares outstanding of the issuer's common stock, as of July 25, 1997:

Common Stock, \$.001 Par Value: 53,384,555 shares  
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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES  
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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands except share amounts)

ASSETS

|                                  | June 30,<br>1997 | March 31,<br>1997 |
|----------------------------------|------------------|-------------------|
|                                  | -----            | -----             |
|                                  | (Unaudited)      |                   |
| Cash and cash equivalents        | \$ 67,645        | \$ 42,999         |
| Accounts receivable, net         | 62,587           | 61,102            |
| Inventories                      | 59,330           | 56,813            |
| Prepaid expenses                 | 1,389            | 1,715             |
| Deferred tax asset               | 24,240           | 24,251            |
| Other current assets             | 2,614            | 2,656             |
|                                  | -----            | -----             |
| Total current assets             | 217,805          | 189,536           |
| Property, plant & equipment, net | 252,331          | 234,058           |
| Other assets                     | 4,558            | 4,498             |
|                                  | -----            | -----             |
| Total assets                     | \$ 474,694       | \$ 428,092        |
|                                  | =====            | =====             |

LIABILITIES AND STOCKHOLDERS' EQUITY

|  |            |            |
|--|------------|------------|
| Accounts payable   | \$ 45,670  | \$ 35,281  |
| Current maturities of long-term debt   | 2,435      | 2,470      |
| Current maturities of capital lease obligations  | 3,672      | 3,776      |
| Accrued liabilities  | 46,337     | 36,392     |
| Deferred income on shipments to distributors   | 27,390     | 20,441     |
|  | -----      | -----      |
| Total current liabilities  | 125,504    | 98,360     |
| Long-term debt, less current maturities  | 2,926      | 3,616      |
| Capital lease obligations, less current maturities   | 1,746      | 2,383      |
| Long-term pension accrual  | 1,048      | 980        |
| Deferred tax liability   | 6,169      | 6,169      |
| Stockholders' equity:  |            |            |
| Preferred stock, \$.001 par value; authorized 5,000,000 shares; no shares issued or outstanding                          | --         | --         |
| Common stock, \$.001 par value; authorized 65,000,000 shares; issued and outstanding 53,355,414 shares at June 30, 1997; | 53         | 53         |
| 53,196,037 shares at March 31, 1997  |            |            |
| Additional paid-in capital   | 169,591    | 168,185    |
| Retained earnings  | 167,657    | 149,825    |
| Less shares of common stock held in treasury   | --         | (1,479)    |
|  | -----      | -----      |
| Net stockholders' equity   | 337,301    | 316,584    |
| Total liabilities and stockholders' equity   | \$ 474,694 | \$ 428,092 |
|  | =====      | =====      |

See accompanying notes to condensed consolidated financial statements

MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands except per share amounts)

|  | Three Months Ended June 30, |           |
|--|-----------------------------|-----------|
|  | 1997                        | 1996      |
|  | (Unaudited)                 |           |
| Net sales  | \$ 97,228                   | \$ 74,161 |
| Cost of sales  | 47,835                      | 37,525    |
| Gross profit   | 49,393                      | 36,636    |
| Operating expenses:                                  |                             |           |
| Research and development                             | 9,210                       | 6,920     |
| Selling, general and administrative                  | 16,228                      | 12,627    |
| Restructuring cost                                   | --                          | 5,969     |
| Write-off of in-process technology                   | --                          | 1,575     |
|  | 25,438                      | 27,091    |
| Operating income                                     | 23,955                      | 9,545     |
| Other income (expense):                              |                             |           |
| Interest income                                      | 740                         | 414       |
| Interest expense                                     | (281)                       | (759)     |
| Other, net   | 13                          | (39)      |
| Income before income taxes                           | 24,427                      | 9,161     |
| Income taxes   | 6,595                       | 2,475     |
| Net income   | \$ 17,832                   | \$ 6,686  |
|  | =====                       | =====     |
| Net income per common and<br>common equivalent share | \$ 0.32                     | \$ 0.12   |
|  | =====                       | =====     |
| Shares used in per share calculation                 | 56,432                      | 54,423    |
|  | =====                       | =====     |

See accompanying notes to condensed consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

|   | Three Months Ended June 30, |          |
|---|-----------------------------|----------|
|   | 1997                        | 1996     |
|   | (Unaudited)                 |          |
| Cash flows from operating activities:   |                             |          |
| Net income  | \$ 17,832                   | \$ 6,686 |
| Adjustments to reconcile net income to<br>net cash provided by operating<br>activities: |                             |          |
| Provision for doubtful accounts   | 144                         | 171      |
| Provision for inventory valuation   | (400)                       | 2,761    |
| Provision for pension accrual   | 296                         | 305      |
| Provision for restructuring cost  | --                          | 5,211    |
| Depreciation and amortization   | 12,095                      | 9,710    |
| Amortization of purchased technology  | 75                          | 75       |
| Deferred income taxes   | 11                          | 2        |
| Compensation expense on stock options   | --                          | 15       |
| (Increase)/decrease in accounts receivable  | (1,629)                     | 1,685    |
| Increase in inventories   | (2,117)                     | (6,437)  |
| Increase in accounts payable and accrued liabilities                                    | 20,334                      | 2,369    |
| Change in other assets and liabilities  | 6,953                       | (7,672)  |

|  |           |           |
|--|-----------|-----------|
| Net cash provided by operating activities            | 53,594    | 14,881    |
| Cash flows from investing activities:                |           |           |
| Capital expenditures                                 | (30,367)  | (26,756)  |
| Net cash used in investing activities                | (30,367)  | (26,756)  |
| Cash flows from financing activities:                |           |           |
| Net proceeds from lines of credit                    | --        | 8,100     |
| Payments on long-term debt                           | (725)     | (798)     |
| Payments on capital lease obligations                | (741)     | (748)     |
| Repurchase of common stock                           | --        | (4,100)   |
| Proceeds from sale of stock and put options          | 2,885     | 935       |
| Net cash provided by financing activities            | 1,419     | 3,389     |
| Net increase (decrease) in cash and cash equivalents | 24,646    | (8,486)   |
| Cash and cash equivalents at beginning of period     | 42,999    | 31,059    |
| Cash and cash equivalents at end of period           | \$ 67,645 | \$ 22,573 |

See accompanying notes to condensed consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation

The accompanying condensed consolidated financial statements include the accounts of Microchip Technology Incorporated and its wholly-owned subsidiaries (the "Company"). All intercompany balances and transactions have been eliminated in consolidation.

In the quarter ended June 30, 1997, the Company changed its method of accounting for inventories from the last-in, first-out (LIFO) method to the first-in, first-out (FIFO) method. The change did not have a material effect on the results of operations for the quarter. The FIFO method is the predominant accounting method used in the semiconductor industry. Prior to this change, the Company's inventory costs did not differ significantly under the two methods. Prior period results of operations will not be restated for this change as the impact is not material.

The accompanying financial statements have been prepared in accordance with generally accepted accounting principles, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of the Company, the accompanying financial statements include all adjustments of a normal recurring nature which are necessary for a fair presentation of the results for the interim periods presented. Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to such rules and regulations. It is suggested that these financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended March 31, 1997. The results of operations for the three months ended June 30, 1997 are not necessarily indicative of the results to be expected for the full fiscal year.

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(2) Accounts Receivable

Accounts receivable consists of the following (amounts in thousands):

|                                      | June 30,<br>1997 | March 31,<br>1997 |
|--------------------------------------|------------------|-------------------|
| Trade accounts receivable            | \$64,153         | \$62,165          |
| Other                                | 672              | 1,031             |
|                                      | 64,825           | 63,196            |
| Less allowance for doubtful accounts | 2,238            | 2,094             |
|                                      | \$62,587         | \$61,102          |

(3) Inventories

The components of inventories are as follows (amounts in thousands):

|  | June 30,<br>1997 | March 31,<br>1997 |
|--|------------------|-------------------|
| Raw materials                          | \$ 3,172         | \$ 2,310          |
| Work in process                        | 41,702           | 44,813            |
| Finished goods                         | 22,044           | 18,021            |
|  | -----            | -----             |
|  | 66,918           | 65,144            |
| Less allowance for inventory valuation | 7,588            | 8,331             |
|  | -----            | -----             |
|  | \$59,330         | \$56,813          |
|  | =====            | =====             |

(4) Property, Plant and Equipment

Property, plant and equipment consists of the following (amounts in thousands):

|   | June 30,<br>1997 | March 31,<br>1997 |
|---|------------------|-------------------|
| Land  | \$ 11,178        | \$ 10,837         |
| Building and building improvements                | 55,025           | 51,796            |
| Machinery and equipment                           | 262,175          | 218,284           |
| Projects in process                               | 34,974           | 52,608            |
|   | -----            | -----             |
|   | 363,352          | 333,525           |
| Less accumulated depreciation<br>and amortization | 111,021          | 99,467            |
|   | -----            | -----             |
|   | \$252,331        | \$234,058         |
|   | =====            | =====             |

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(5) Lines of Credit

The Company has an unsecured line of credit with a syndicate of U.S. banks for up to \$90,000,000, bearing interest at the Prime Rate (8.50% at June 30, 1997) and expiring in October, 1998. At March 31, 1997 and June 30, 1997 there were no borrowings against the line of credit. The agreement between the Company and the syndicate of banks requires the Company to achieve certain financial ratios and operating results. The Company was in compliance with these covenants as of June 30, 1997.

(6) Stockholders' Equity

Stock Repurchase Activity. In connection with a stock repurchase program, during the year ended March 31, 1997, the Company purchased a total of 1,326,477 shares of the Company's Common Stock in open market activities at a total cost of \$19,463,000. As of June 30, 1997, the Company had reissued all of these shares through stock option exercises and the Company's employee stock purchase plan. Also, in connection with a stock repurchase program, during the quarter ended June 30, 1997, the Company sold put options for 350,000 shares of Common Stock at pricing per share ranging from \$29.50 to \$30.86. The net proceeds from the sale of these options, in the amount of \$1,606,100 for the period ended June 30, 1997, has been credited to additional paid-in capital. As of June 30, 1997, the Company had outstanding put options for 550,000 shares which have expiration dates ranging from July 8, 1997 to June 16, 1998 at prices ranging from \$15.08 to \$30.86 per share.

Increase to the Number of Authorized Shares. In April, 1997, the Board of Directors approved an amendment to the Company's Restated Certificate of Incorporation, as amended, to increase the number of authorized shares of Common Stock from 65,000,000 to 100,000,000. This matter was approved by the stockholders at the 1997 annual stockholders' meeting held on July 28, 1997, and became effective upon the filing of a certificate of amendment to the Restated Certificate of Incorporation with the Delaware Secretary of State on July 28, 1997.

(7) Subsequent Events

Microchip Technology Incorporated v. Lucent Technologies Inc. On July 16, 1997, the Company filed an action for declaratory relief against Lucent Technologies Inc. ("Lucent") requesting that the Court declare, among other matters, that Microchip does not infringe certain of Lucent's semiconductor patents (District of Arizona, CIV97-1502 PHX EHC). The Company initiated legal action so that a determination could be made relating to the validity, enforceability and alleged

infringement of the asserted patents. Prior to filing suit, Microchip had engaged in good faith license negotiations with Lucent for over four years regarding alleged infringement of certain of Lucent's semiconductor patents. The Company investigated Lucent's claims and believes that it does not infringe any of the asserted Lucent patents. Despite the filing, the Company intends to continue negotiations with Lucent with the goal of obtaining a resolution of this matter, which could include a license on commercially reasonable terms. However, no assurances can be given that a mutually satisfactory conclusion will be achieved and that protracted litigation will not ensue. Litigation could result in substantial cost to the Company and diversion of management effort. If unsuccessful, the Company could be forced to pay royalties on past and future sales. Such litigation and/or royalty payments could have a material adverse impact on the Company's business and operating results.

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

The following table sets forth certain operational data as a percentage of net sales for the periods indicated:

|                                     | Three Months Ended June 30, |        |
|-------------------------------------|-----------------------------|--------|
|                                     | 1997                        | 1996   |
|                                     | -----                       |        |
| Net sales .....                     | 100.0%                      | 100.0% |
| Cost of sales .....                 | 49.2                        | 50.6   |
|                                     | -----                       | -----  |
| Gross profit .....                  | 50.8                        | 49.4   |
| Research and development .....      | 9.5                         | 9.3    |
| Selling, general and administrative | 16.7                        | 17.0   |
| Restructuring cost .....            | --                          | 8.1    |
| Write-off of in-process technology  | --                          | 2.1    |
|                                     | -----                       | -----  |
| Operating income .....              | 24.6%                       | 12.9%  |
|                                     | =====                       | =====  |

Net Sales. The Company's net sales for the quarter ended June 30, 1997 were \$97.2 million, an increase of 31.1% over sales of \$74.2 million for the corresponding quarter of the previous fiscal year, and an increase of 4.0% from the previous quarter's sales of \$93.5 million. The Company's family of 8-bit microcontrollers represents the largest component of Microchip's total net sales. Microcontrollers and associated application development systems accounted for 69.8% and 61.0% of total net sales in the three months ended June 30, 1997 and 1996, respectively. A related component of the Company's product sales consists primarily of serial EEPROMs, along with smaller quantities of parallel EEPROM memories and high-speed and low-voltage EPROMs. These products accounted for 28.2% and 33.0% of net sales in the three months ended June 30, 1997 and 1996, respectively. In the three months ended June 30, 1997, as compared to the same period in the previous fiscal year, the Company increased the percentage of net sales attributable to 8-bit microcontrollers as a result of the Company's focus in this area. It is anticipated that this trend will continue for the foreseeable future.

The Company's net sales in any given quarter are dependent upon a combination of orders received in that quarter for shipment in that quarter ("turns orders") and shipments from backlog. The Company has emphasized its ability to respond quickly to customer orders as part of its competitive strategy. This strategy, combined with current industry conditions, is resulting in customers placing orders with relatively short delivery schedules. This has had the effect of increasing turns orders as a portion of the Company's business in the three months ended June 30, 1997, as compared to the similar period of the previous fiscal year. During the quarter, however, the Company began to see improved customer order backlog placement after many quarters of declining order visibility. Because turns orders are more difficult to predict, there can be no assurance that the combination of turns orders and backlog in any quarter will be sufficient to achieve growth in net sales. If the Company does not achieve a sufficient level of turns orders in a particular quarter, the Company's revenues and operating results would be materially adversely affected.

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In the quarter ended June 30, 1997, the Company was unable to ship \$4 million of product for which it had firm scheduled orders, approximately the same as shipment delinquencies at the end of the prior fiscal quarter. These shipment delinquencies were a result of inventory mix issues which have been exacerbated by the rapid growth in the Company's product offerings and the low long-term order visibility. While the Company experienced an improvement in customer order backlog during the quarter, it is anticipated that low long-term order visibility will continue for the foreseeable future and, as a result, the Company expects it may have shipment delinquencies at the end of each quarter which could adversely affect quarterly operating results.

The Company's overall average selling prices for its microcontroller products have remained relatively constant while average selling prices of its non-volatile memory products have declined gradually over time. During fiscal 1997, and for the three months ended June 30, 1997, the Company experienced increased pricing pressure on its non-volatile memory products due primarily to a worldwide industry inventory correction and the less proprietary nature of these products. There can be no assurance that average selling prices for the Company's microcontroller or other products will not experience increased pricing pressure in the future. An increase in pricing pressure could adversely affect the Company's operating results.

The foregoing statements regarding product mix, turns orders, shipment delinquencies and pricing pressures are forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are subject to the safe harbors created thereby. Actual results could differ materially because of the following factors, among others: the level of orders that are received and can be shipped in a quarter; inventory mix and timing of customer orders; competition and competitive pressures on pricing and product availability; customers' inventory levels, order patterns and seasonality; the cyclical nature of both the semiconductor industry and the markets addressed by the Company's products; market acceptance of the products of both the Company and its customers; demand for the Company's products; fluctuations in production yields, production efficiencies and overall capacity utilization; changes in product mix; and absorption of fixed costs, labor and other fixed manufacturing costs.

Foreign sales represented 70.0% of net sales in the current quarter and 67.0% of net sales in the corresponding quarter of the previous fiscal year and 66.0% of net sales in the previous quarter. The Company's foreign sales have been predominantly in Asia, Europe and Japan, which the Company attributes to the manufacturing strength in those areas for consumer, automotive, office automation, communications and industrial products. The majority of foreign sales are U.S. Dollar denominated. The Company has entered into and, from time to time, will enter into hedging transactions in order to minimize exposure to currency rate fluctuations. Although none of the countries in which the Company conducts significant foreign operations have had a highly inflationary economy in the last five years, there is no assurance that inflation rates or fluctuations in foreign currency rates in countries where the Company conducts operations will not adversely affect the Company's operating results in the future.

Additional Factors Affecting Operating Results. The Company believes that future growth in net sales of its 8-bit family of microcontroller products and related memory products will depend largely upon the Company's success in having its current and new products designed into high-volume customer applications. Design wins typically precede the Company's volume shipment of products for such applications by 15 months or more. The Company also believes that shipment levels of its proprietary application development systems are an indicator of potential future design wins and microcontroller sales. The Company continued to achieve a high volume of design wins and shipped increased numbers

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of application development systems in the three months ended June 30, 1997 compared to previous fiscal periods. There can be no assurance that any particular development system shipment will result in a product design win or that any particular design win will result in future product sales.

The Company's operating results are affected by a wide variety of other factors that could adversely impact its net sales and profitability, many of which are beyond the Company's control. These factors include the Company's ability to design and introduce new products on a timely basis, market acceptance of products of both the Company and its customers, customer order patterns and seasonality, changes in product mix, whether the Company's customers buy from a distributor or directly from the Company, product performance and reliability, product obsolescence, the amount of any product returns, availability and utilization of manufacturing capacity, fluctuations in manufacturing yield, the availability and cost of raw materials, equipment and other supplies, the cyclical nature of both the semiconductor industry and the markets addressed by the Company's products, technological changes, competition and competitive pressures on prices, and economic, political or other conditions in the United States, and other worldwide markets served by the Company. The Company believes its ability to continue to increase its manufacturing capacity to meet customer demand and maintain satisfactory delivery schedules will be an important competitive factor. As a result of the increase in fixed costs and operating expenses related to expanding its manufacturing capacity, the Company's operating results may be adversely affected if net sales do not increase sufficiently to offset the increased costs. The Company's products are incorporated into a wide variety of consumer, automotive, office automation, communications and industrial products. A slowdown in demand for products which utilize the Company's products as a result of economic or other conditions in the worldwide markets served by the Company could adversely affect the Company's operating results.

Gross Profit. The Company's gross profit was \$49.4 million in the three months ended June 30, 1997, as compared to \$36.6 million in the corresponding quarter of the prior fiscal year, and \$47.0 million in the previous quarter. Gross

profit as a percent of sales was 50.8% in the current quarter, 49.4% in the corresponding quarter of the prior fiscal year and 50.3% in the previous quarter. The Company anticipates that its cost of sales will fluctuate over time, driven primarily by the product mix of 8-bit microcontroller products and related memory products manufacturing yields, wafer fab loading levels and competitive and economic conditions. Gross profit percentage increased from the prior period levels, primarily as a result of the percentage of net sales attributable to 8-bit microcontrollers and improved wafer fabrication utilization. The Company anticipates that its gross profit percentage will fluctuate over time, driven primarily by product mix, manufacturing costs and yields, and competitive and economic conditions. The Company is continuing the process of transitioning products to smaller geometries and to larger wafer sizes to reduce future manufacturing costs. Eight-inch wafer production commenced at the Company's Tempe wafer fabrication facility in early fiscal 1998, and the Company is continuing the transition of products to its 0.7 micron process. The foregoing statements relating to anticipated gross margins, cost of sales, and the transition to higher yielding manufacturing processes are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are subject to the safe harbors created thereby. Actual results could differ materially because of the following factors, among others: fluctuations in production yields, production efficiency and overall capacity utilization; cost and availability of raw materials; absorption of fixed costs, labor and other direct manufacturing costs; the timing and success of manufacturing process transition; changes in product mix; competitive pressures on prices; and other economic conditions in the United States and other worldwide markets.

All of Microchip's assembly operations and a portion of its product final test requirements are performed by third-party contractors in order to meet product shipment requirements. Reliance on third parties

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involves some reduction in the Company's level of control over these portions of its business. While the Company reviews the quality, delivery and cost performance of these third-party contractors, there can be no assurance that reliance on third-party contractors will not adversely impact results in future reporting periods if any third-party contractor is unable to maintain assembly and test yields and costs at approximately their current levels.

The Company owns product final test facilities in Kaohsiung, Taiwan, Republic of China and Chachoengsao, Thailand. The Company also uses various third-party contractors in Thailand, Taiwan, the Philippines, China and other locations in Asia for product assembly and test. The Company's reliance on facilities in these countries, and maintenance of substantially all of its finished goods inventory overseas, entails certain political and economic risks, including political instability and expropriation, labor disruption, supply disruption, currency controls and exchange fluctuations, as well as changes in tax laws, tariff and freight rates. Microchip currently employs the Alphatec Electronics PCL group of companies ("Alphatec") headquartered in Bangkok, Thailand, for a portion of its product assembly volume and product final test capacity. While Alphatec's assembly and test operations have performed reliably for the Company for several years, Alphatec has recently experienced difficulty in obtaining financing in connection with some of its unrelated joint ventures involving semiconductor fabrication facilities in Thailand. Alphatec has also recently released information concerning a report from their independent auditors resulting in the Alphatec Board of Directors requesting the Stock Exchange of Thailand to immediately suspend trading in Alphatec shares. Microchip currently has multiple sources for product assembly and test for most of its package types and is in the process of shifting its assembly and test requirements to other factories. Despite these actions, there can be no assurance that Microchip may not experience short-term disruption, including possible temporary product shortages and increased assembly and test costs, compared to those received from the current subcontract relationship with Alphatec. The Company has not experienced any significant interruptions in its foreign business operations to date. Nonetheless, the Company's business and operating results could be adversely affected if foreign operations or international air transportation were disrupted.

During the fourth quarter of fiscal 1997, the Company commenced construction of an additional 20,000 square foot wafer fabrication module at its Tempe, Arizona, facility. It is anticipated that the construction will be completed during the second quarter of fiscal 1998 and that the new wafer fabrication module will begin 8-inch wafer production in the fourth quarter of fiscal 1998. In addition, the Company is also expanding capacity at its Chandler wafer fabrication facility and expects to have an additional 3,000 square feet of capacity available in Chandler during the second quarter of fiscal 1998. The foregoing statements regarding completion of construction and additional available capacity are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are subject to the safe harbors created thereby. Actual results could differ materially because of the following factors, among others: delays in facilitation of the expanded Tempe and Chandler wafer fabrication facilities; production yields and efficiencies; factory absorption rates; capacity loading; supply disruption; operating cost levels; and the rate of revenue growth.

Research and Development. The Company is committed to continued investment in new and enhanced products, including its development systems software and its design and manufacturing process technology, which are significant factors in maintaining the Company's competitive position. The dollar investment in research and development increased 33.1% in the current quarter as compared to the corresponding quarter of the previous fiscal year and by 2.0% from the previous quarter. The Company will continue to invest in research and development in the future, including an investment in process and product development associated with the capacity expansion of the Company's fabrication facilities.

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The Company's future operating results will depend to a significant extent on its ability to continue to develop and introduce new products on a timely basis which can compete effectively on the basis of price and performance and which address customer requirements. The success of new product introductions depends on various factors, including proper new product selection, timely completion and introduction of new product designs, development of support tools and collateral literature that make complex new products easy for engineers to understand and use and market acceptance of customers' end products. Because of the complexity of its products, the Company has experienced delays from time to time in completing the development of new products. In addition, there can be no assurance that any new products will receive or maintain substantial market acceptance. If the Company were unable to design, develop and introduce competitive products on a timely basis, its future operating results would be adversely affected.

The Company's future success will also depend upon its ability to develop and implement new design and process technologies. Semiconductor design and process technologies are subject to rapid technological change, requiring large expenditures for research and development. Other companies in the industry have experienced difficulty in effecting transitions to smaller geometry processes and to larger wafers and, consequently, have suffered reduced manufacturing yields or delays in product deliveries. The Company believes that its transition to smaller geometries and to larger wafers will be important for the Company to remain competitive, and operating results could be adversely affected if the transition is substantially delayed or inefficiently implemented.

Selling, General and Administrative. Through expense controls and operating efficiencies, the Company has reduced selling, general and administrative expenses in the current fiscal quarter to 16.7% of sales, as compared to 17.0% of sales in the corresponding period of the previous fiscal year, and compared to 16.8% in the previous quarter. This has been achieved while the Company has continued to invest significantly in incremental worldwide sales and technical support resources to promote the Company's embedded control products. However, there can be no assurance that revenue growth in the future will be sufficient to continue to reduce the current level of selling, general and administrative expenses as a percentage of sales.

Other Income (Expense). Interest expense in the three months ended June 30, 1997 decreased over the same period of the previous fiscal year due to lower borrowings associated with the Company's capital equipment additions. Interest income in the three months ended June 30, 1997 increased from the same period of the previous fiscal year, primarily as a result of investing the proceeds of the Company's equity offering completed in the fourth quarter of fiscal 1997. Other income represents numerous immaterial non-operating items. The Company's interest expense could increase in fiscal 1998 if the Company increases its borrowings and interest expense would be adversely impacted by increased interest rates.

Provision for Income Taxes. Provisions for income taxes reflect tax on foreign earnings and federal and state tax on U.S. earnings. The Company had an effective tax rate of 27.0% for each of the three months ended June 30, 1997 and 1996, due primarily to lower tax rates at its foreign locations. The Company believes that its tax rate for the foreseeable future will be approximately 27.0%. The foregoing statement regarding the Company's anticipated future tax rate is a forward-looking statement within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and is subject to the safe harbors created thereby. Actual results could differ materially because of the following factors, among others: taxation rates in geographic regions where the Company has significant operations; and current tax holidays available in foreign locations.

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#### Liquidity and Capital Resources

The Company had \$67.6 million in cash and cash equivalents at June 30, 1997, an increase of \$24.6 million from the June 30, 1996 balance. The Company has an unsecured line of credit with a syndicate of domestic banks totaling \$90.0 million. There were no borrowings under the domestic line of credit as of June 30, 1997. The domestic line of credit requires the Company to achieve certain financial ratios and operating results. The Company was in compliance with these covenants at June 30, 1997. The Company also has an unsecured short term line of credit totaling \$24.9 million with certain foreign banks. There were no borrowings under the foreign line of credit as of June 30, 1997. There are no covenants related to the foreign line of credit.

At June 30, 1997, an aggregate of \$114.9 million of these facilities was available, subject to financial covenants and ratios with which the Company was in compliance. The Company's ability to fully utilize these facilities is dependent on the Company remaining in compliance with such covenants and ratios.

During the three months ended June 30, 1997, the Company generated \$53.6 million of cash from operating activities, an improvement of \$38.7 million from the three months ended June 30, 1996. The improvement in cash flow from operations was primarily due to increased profitability, the impact of increases in accounts payable and accrued expenses and an increase in depreciation expense.

The Company's level of capital expenditures varies from time to time as a result of actual and anticipated business conditions. Capital expenditures in the three months ended June 30, 1997 and 1996, were \$30.4 million and \$26.8 million, respectively. Capital expenditures were primarily for the expansion of production capacity and the addition of research and development equipment in each of these periods. The Company currently intends to spend approximately \$135.0 million during the next 12 months for additional capital equipment to increase capacity at its existing wafer fabrication facilities, to construct additional facilities and to expand product test operations. The Company expects capital expenditures will be financed by cash flow from operations, available debt arrangements and other sources of financing. The Company believes that the capital expenditures anticipated to be incurred over the next 12 months will provide sufficient additional manufacturing capacity to meet its currently anticipated needs.

Net cash provided by financing activities was \$1.4 million and \$3.4 million for the three months ended June 30, 1997 and 1996 respectively. Proceeds from sale of stock and put options were \$2.9 million and \$0.9 million for the three months ended June 30, 1997 and 1996, respectively. Payments on long term debt and capital lease obligations were \$1.5 million for each of the three months ended June 30, 1997 and 1996. Proceeds from lines of credit were \$8.1 million for the three months ended June 30, 1996. Cash expended for the purchase of the Company's Common Stock was \$4.1 million for the three months ended June 30, 1996.

On July 26, 1996, the Company's Board of Directors authorized a share repurchase plan which permits the Company to purchase up to 1,500,000 shares of its Common Stock and to sell up to 750,000 put options. Based on the price of Microchip's stock and other pertinent factors, the Company may from time to time purchase shares on the open market or sell put options. See Footnote 6 to the Company's Condensed Consolidated Financial Statements.

The Company believes that its existing sources of liquidity combined with cash generated from operations will be sufficient to meet the Company's currently anticipated cash requirements for at least the next 12 months. However, the semiconductor industry is capital intensive. In order to remain competitive, the Company must continue to make significant investments in capital equipment, for both

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production and research and development. The Company may seek additional equity or debt financing during the next 12 months for the capital expenditures required to maintain or expand the Company's wafer fabrication and product test facilities. The timing and amount of any such capital requirements will depend on a number of factors, including demand for the Company's products, product mix, changes in industry conditions and competitive factors. There can be no assurance that such financing will be available on acceptable terms, and any additional equity financing could result in additional dilution to existing investors.

Recent Accounting Pronouncements. In February, 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 128, "Earnings per Share" ("Statement 128"). Statement 128 establishes standards for computing and presenting earnings per share ("EPS"), and supersedes APB Opinion No. 15. Statement 128 replaces primary EPS with basic EPS and requires dual presentation of basic and diluted EPS. Statement 128 is effective for annual and interim periods ending after December 15, 1997. Earlier adoption is not permitted. After adoption, all prior period EPS data shall be restated to conform to Statement 128. Basic and diluted EPS, as calculated under Statement 128 would have been \$0.33 and \$0.32 for the three months ended June 30, 1997.

## PART II. OTHER INFORMATION

### Item 1. LEGAL PROCEEDINGS

Microchip Technology Incorporated v. Lucent Technologies Inc. On July 16, 1997, the Company filed an action for declaratory relief against Lucent Technologies Inc. ("Lucent") requesting that the Court declare, among other matters, that Microchip does not infringe certain of Lucent's semiconductor patents (District of Arizona, CIV 97-1502 PHX EHC). The Company initiated legal action so that a determination could be made relating to the validity, enforceability and alleged infringement of the asserted patents. Prior to filing suit, Microchip had engaged in good faith license negotiations with Lucent for over four years regarding alleged infringement of certain of Lucent's semiconductor patents. The

Company investigated Lucent's claims and believes that it does not infringe any of the asserted Lucent patents. Despite the filing, the Company intends to continue negotiations with Lucent with the goal of obtaining a resolution of this matter, which could include a license on commercially reasonable terms. However, no assurances can be given that a mutually satisfactory conclusion will be achieved and that protracted litigation will not ensue. Litigation could result in substantial cost to the Company and diversion of management effort. If unsuccessful, the Company could be forced to pay royalties on past and future sales. Such litigation and/or royalty payments could have a material adverse impact on the Company's business and operating results.

Item 5. OTHER INFORMATION

On July 28, 1997, the Company held its annual meeting of stockholders (the "Meeting"). Among other matters acted upon at the Meeting, the stockholders approved an amendment to the Company's Restated Certificate of Incorporation, as amended, to increase the authorized Common Stock of the Company from 65,000,000 shares, \$0.001 par value per share, to 100,000,000 shares. The amendment became effective upon the filing of a certificate of amendment to the Restated Certificate of Incorporation with the Delaware Secretary of State on July 28, 1997.

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Item 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

- Exhibit 3.1. Certificate of Amendment to Registrant's Restated Certificate of Incorporation, as amended
- Exhibit 11 Computation of Net Income Per Share
- Exhibit 18.1 Letter from KPMG Peat Marwick LLP re: Change in Accounting Principles

(b) Reports on Form 8-K.

The registrant did not file any reports on Form 8-K during the quarter ended June 30, 1997.

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SIGNATURES

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

MICROCHIP TECHNOLOGY INCORPORATED

Date: August 11, 1997  
-----

By: /s/ C. Philip Chapman  
-----  
C. Philip Chapman  
Vice President, Chief Financial  
Officer and Secretary (Duly  
Authorized Officer, and Principal  
Financial and Accounting Officer)

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EXHIBIT INDEX

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CERTIFICATE OF AMENDMENT  
TO THE  
RESTATED CERTIFICATE OF INCORPORATION  
OF MICROCHIP TECHNOLOGY INCORPORATED

Microchip Technology Incorporated, a corporation organized and existing under any by virtue of the General Corporation Law of the State of Delaware (the "Corporation") does hereby certify:

FIRST: That at a meeting of the Corporation's Board of Directors, resolutions were duly adopted proposing and declaring advisable a proposed amendment to the Corporation's Restated Certificate of Incorporation, amending Article IV(A) thereto to read as follows:

(A) Classes of Stock. This corporation is authorized to issue two classes of stock to be designated, respectively, "Common Stock" and "Preferred Stock." The total number of shares which the corporation is authorized to issue is one hundred and five million (105,000,000) shares. One hundred million (100,000,000) shares shall be Common Stock, par value \$0.001 per share and five million (5,000,000) shares shall be Preferred Stock, par value \$0.001 per share.

SECOND: That upon notice given in accordance with Section 222 of the General Corporation Law of the State of Delaware, and pursuant to a resolution of the Board of Directors, a meeting of the stockholders of the Corporation was duly called and held, at which meeting the stockholders approved said amendment.

THIRD: That the aforesaid amendment was duly adopted in accordance with the applicable provisions of Section 242 of the General Corporation Law of the State of Delaware.

IN WITNESS WHEREOF, Microchip Technology Incorporated has caused this Certificate of Amendment to be signed by Steve Sanghi, its President and attested by C. Philip Chapman, its Secretary as of the 28th day of July, 1997.

MICROCHIP TECHNOLOGY INCORPORATED

By /s/ Steve Sanghi  
Steve Sanghi, President

ATTEST:

By: /s/ C. Philip Chapman  
C. Philip Chapman, Secretary

MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES

EXHIBIT 11 - COMPUTATION OF NET INCOME PER SHARE

(in thousands, except per share amounts)

|  | Three Months Ended June 30, |          |
|--|-----------------------------|----------|
|  | 1997                        | 1996     |
|  | -----                       | -----    |
| Net income   | \$17,832                    | \$ 6,686 |
|  | =====                       | =====    |
| Weighted average shares:   |                             |          |
| Common shares outstanding  | 53,291                      | 51,723   |
| Common equivalent shares<br>representing shares issuable<br>upon exercise of stock options(1)                            | 3,141                       | 2,700    |
|  | -----                       | -----    |
| Total weighted average<br>shares - primary   | 56,432                      | 54,423   |
|  | =====                       | =====    |
| Incremental common equivalent<br>shares (calculated using the<br>higher of end of period or<br>average market value) (2) | --                          | --       |
|  | -----                       | -----    |
| Total weighted average<br>shares - fully diluted   | 56,432                      | 54,423   |
|  | =====                       | =====    |
| Primary net income per common and<br>common equivalent share   | \$ 0.32                     | \$ 0.12  |
|  | =====                       | =====    |
| Fully diluted net income per common<br>and common equivalent share   | \$ 0.32                     | \$ 0.12  |
|  | =====                       | =====    |

(1) Amount calculated using the treasury stock method and fair market values for stock.

(2) This calculation is submitted in accordance with Regulation S-K Item 601(b)(11) although not required by footnote 2 to paragraph 14 of APB Opinion No. 15 because it results in dilution of less than 3%.

KPMG Peat Marwick LLP

One Arizona Center            Telephone 602 253 2000  
400 E. Van Buren Street  
Suite 1100  
Phoenix, AZ 85004

August 4, 1997

Microchip Technology Incorporated  
Chandler, Arizona

Ladies and Gentlemen:

We have been furnished with a copy of Form 10-Q of Microchip Technology Incorporated (Microchip or Company) for the three months ended June 30, 1997, and have read the Company's statements contained in Note 1 to the condensed consolidated financial statements included therein. As stated in Note 1, the Company changed its method of accounting for inventories from the last-in, first-out (LIFO) method to the first-in, first-out (FIFO) method and states that the newly adopted accounting principle is preferable in the circumstances because the FIFO method is the predominant accounting method used in the semiconductor industry. In accordance with your request, we have reviewed and discussed with Company officials the circumstances and business judgment and planning upon which the decision to make this change in the method of accounting was based.

We have not audited any financial statements of Microchip Technology Incorporated as of any date or for any period subsequent to March 31, 1997, nor have we audited the information set forth in the aforementioned Note 1 to the condensed consolidated financial statements; accordingly, we do not express an opinion concerning the factual information contained therein.

With regard to the aforementioned accounting change, authoritative criteria have not been established for evaluating the preferability of one acceptable method of accounting over another acceptable method. However, for purposes of Microchip Technology Incorporated's compliance with the requirements of the Securities and Exchange Commission, we are furnishing this letter.

Based on our review and discussion, with reliance on management's business judgment and planning, we concur that the newly adopted method of accounting is preferable in the Company's circumstances.

Very truly yours,  
/s/ KPMG Peat Marwick LLP

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