

ANALOG DEVICES INC
Form 10-Q
August 21, 2007

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 August 4, 2007

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 No. 1-7819

Analog Devices, Inc.

(Exact name of registrant as specified in its charter)

Massachusetts

*(State or other jurisdiction of
incorporation or organization)*

04-2348234

*(I.R.S. Employer
Identification No.)*

One Technology Way, Norwood, MA

(Address of principal executive offices)

02062-9106

(Zip Code)

(781) 329-4700

(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 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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) YES NO

As of August 4, 2007 there were 311,185,823 shares of Common Stock, \$0.16 2/3 par value per share, outstanding.

TABLE OF CONTENTS

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

ITEM 4. Controls and Procedures

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

ITEM 1A. Risk Factors

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

ITEM 6. Exhibits

SIGNATURES

Exhibit Index

EX-10.1 Form of Confirming Memorandum

EX-31.1 Section 302 Certification of CEO

EX-31.2 Section 302 Certification of CFO

EX-32.1 Section 906 Certification of CEO

EX-32.2 Section 906 Certification of CFO

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

ANALOG DEVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(thousands, except per share amounts)

| | Three Months Ended | |
|--|--------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Product revenue | \$ 680,312 | \$ 663,660 |
| Cost of sales (1) | 291,727 | 273,550 |
| Gross margin | 388,585 | 390,110 |
| Operating expenses: | | |
| Research and development (1) | 148,562 | 136,061 |
| Selling, marketing, general and administrative (1) | 102,379 | 99,663 |
| Purchased in-process research and development | | 5,500 |
| | 250,941 | 241,224 |
| Operating income | 137,644 | 148,886 |
| Nonoperating (income) expense: | | |
| Interest expense | | 4 |
| Interest income | (17,721) | (26,716) |
| Other, net | 1,272 | 435 |
| | (16,449) | (26,277) |
| Income before income taxes | 154,093 | 175,163 |
| Provision for income taxes | 33,658 | 30,478 |
| Net income | \$ 120,435 | \$ 144,685 |
| Shares used to compute earnings per share basic | 318,465 | 357,887 |
| Shares used to compute earnings per share diluted | 327,331 | 369,542 |
| Earnings per share basic | \$ 0.38 | \$ 0.40 |

Edgar Filing: ANALOG DEVICES INC - Form 10-Q

| | | |
|---|----------|----------|
| Earnings per share diluted | \$ 0.37 | \$ 0.39 |
| Dividends declared and paid per share | \$ 0.18 | \$ 0.16 |
| (1) Includes stock-based compensation expense as follows: | | |
| Cost of sales | \$ 2,477 | \$ 2,949 |
| Research and development | \$ 8,172 | \$ 8,302 |
| Selling, marketing, general and administrative | \$ 6,816 | \$ 8,055 |
| See accompanying notes. | | |

Table of ContentsANALOG DEVICES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(thousands, except per share amounts)

| | Nine Months Ended | |
|---|-------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Product revenue | \$ 2,006,058 | \$ 1,928,834 |
| Revenue from the one-time payment associated with the licensing of certain intellectual property rights | 35,000 | |
| Total revenue | 2,041,058 | 1,928,834 |
| Cost of sales (1) | 853,815 | 797,266 |
| Gross margin | 1,187,243 | 1,131,568 |
| Operating expenses: | | |
| Research and development (1) | 439,142 | 399,197 |
| Selling, marketing, general and administrative (1) | 300,105 | 293,376 |
| Purchased in-process research and development | | 5,500 |
| Special charges | 15,312 | 1,013 |
| | 754,559 | 699,086 |
| Operating income | 432,684 | 432,482 |
| Nonoperating (income) expense: | | |
| Interest expense | | 35 |
| Interest income | (63,429) | (75,868) |
| Other, net | (16,414) | (10,261) |
| | (79,843) | (86,094) |
| Income before income taxes and minority interest | 512,527 | 518,576 |
| Provision for income taxes | 113,728 | 107,513 |
| Minority interest | (219) | |
| Net income | \$ 399,018 | \$ 411,063 |
| Shares used to compute earnings per share basic | 329,050 | 362,749 |
| Shares used to compute earnings per share diluted | 338,460 | 375,563 |

| | | |
|---------------------------------------|---------|---------|
| Earnings per share basic | \$ 1.21 | \$ 1.13 |
| Earnings per share diluted | \$ 1.18 | \$ 1.09 |
| Dividends declared and paid per share | \$ 0.52 | \$ 0.40 |

(1) Includes stock-based compensation expense as follows:

| | | |
|--|-----------|-----------|
| Cost of sales | \$ 8,085 | \$ 4,893 |
| Research and development | \$ 25,437 | \$ 27,108 |
| Selling, marketing, general and administrative | \$ 21,624 | \$ 25,829 |
| See accompanying notes. | | |

Table of Contents

ANALOG DEVICES, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (Unaudited)
 (thousands)

| | August 4, 2007 | October 28, 2006 |
|--|-------------------|---------------------|
| Assets | | |
| Cash and cash equivalents | \$ 393,898 | \$ 343,947 |
| Short-term investments | 889,692 | 1,784,387 |
| Accounts receivable, net | 350,868 | 329,393 |
| Inventories (1): | | |
| Raw materials | 17,520 | 16,430 |
| Work in process | 256,497 | 264,076 |
| Finished goods | 97,756 | 98,145 |
| | 371,773 | 378,651 |
| Deferred tax assets | 110,671 | 91,045 |
| Deferred compensation plan investments | 1,181 | 1,109 |
| Prepaid expenses and other current assets | 54,331 | 82,770 |
| Total current assets | 2,172,414 | 3,011,302 |
| Property, plant and equipment, at cost: | | |
| Land and buildings | 366,351 | 353,912 |
| Machinery and equipment | 1,415,793 | 1,371,332 |
| Office equipment | 79,451 | 78,976 |
| Leasehold improvements | 61,992 | 109,028 |
| | 1,923,587 | 1,913,248 |
| Less accumulated depreciation and amortization | 1,358,627 | 1,350,623 |
| Net property, plant and equipment | 564,960 | 562,625 |
| Deferred compensation plan investments | 33,937 | 30,579 |
| Other investments | 686 | 850 |
| Goodwill | 276,972 | 256,209 |
| Intangible assets, net | 33,893 | 42,808 |
| Deferred tax assets | 54,561 | 54,734 |
| Other assets | 28,944 | 27,744 |
| Total other assets | 428,993 | 412,924 |
| | \$ 3,166,367 | \$ 3,986,851 |

- (1) Includes \$3,432 and \$3,703 related to stock-based compensation at August 4, 2007 and October 28, 2006, respectively.
See accompanying notes.

Table of ContentsANALOG DEVICES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(thousands, except share amounts)

| | August 4, 2007 | October 28, 2006 |
|--|-------------------|---------------------|
| Liabilities and Shareholders' Equity | | |
| Accounts payable | \$ 138,987 | \$ 124,566 |
| Deferred income on shipments to distributors | 149,283 | 149,543 |
| Income taxes payable | 129,274 | 60,956 |
| Deferred compensation plan liability | 1,181 | 1,109 |
| Accrued liabilities | 141,130 | 154,769 |
| Total current liabilities | 559,855 | 490,943 |
| Deferred income taxes | 7,397 | 3,414 |
| Deferred compensation plan liability | 33,968 | 30,633 |
| Other non-current liabilities | 28,541 | 25,851 |
| Total non-current liabilities | 69,906 | 59,898 |
| Minority interest | | 217 |
| Commitments and contingencies | | |
| Shareholders' Equity | | |
| Preferred stock, \$1.00 par value, 471,934 shares authorized, none outstanding | | |
| Common stock, \$0.16 2/3 par value, 1,200,000,000 shares authorized, 311,185,823 shares issued and outstanding (342,000,004 on October 28, 2006) | 51,865 | 57,001 |
| Capital in excess of par value | | |
| Retained earnings | 2,471,627 | 3,378,999 |
| Accumulated other comprehensive income (loss) | 13,114 | (207) |
| Total shareholders' equity | 2,536,606 | 3,435,793 |
| | \$ 3,166,367 | \$ 3,986,851 |

See accompanying notes.

Table of Contents

ANALOG DEVICES, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)
 (thousands)

| | Nine Months Ended | |
|---|-------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Cash flows from operating activities: | | |
| Net income | \$ 399,018 | \$ 411,063 |
| Adjustments to reconcile net income to net cash provided by operations: | | |
| Depreciation | 107,069 | 127,947 |
| Amortization of intangibles | 10,037 | 1,953 |
| Stock-based compensation expense | 55,146 | 57,830 |
| Deferred income taxes | (10,574) | (32,386) |
| Excess tax benefit-stock options | (25,053) | (155,956) |
| Non-cash portion of special charge | | 459 |
| Gain on sale of a product line | | (13,027) |
| Gain on sale of an investment | (7,919) | |
| Purchased in-process research and development | | 5,500 |
| Minority interest | (219) | |
| Other non-cash expense | 315 | 664 |
| Changes in operating assets and liabilities | 109,695 | 50,320 |
| Total adjustments | 238,497 | 43,304 |
| Net cash provided by operating activities | 637,515 | 454,367 |
| Cash flows from investing activities: | | |
| Purchases of short-term available-for-sale investments | (1,495,905) | (2,065,104) |
| Maturities of short-term available-for-sale investments | 2,397,676 | 2,158,075 |
| Additions to property, plant and equipment | (108,633) | (87,542) |
| (Increase) decrease in other assets | (18) | 4,125 |
| Payments for acquisitions | (9,160) | (14,913) |
| Proceeds from sale of a product line | | 23,070 |
| Proceeds from sale of an investment | 8,003 | |
| Net cash provided by investing activities | 791,963 | 17,711 |
| Cash flows from financing activities: | | |
| Repurchase of common stock | (1,329,521) | (667,970) |
| Net proceeds from employee stock plans | 96,196 | 79,852 |
| Excess tax benefit-stock options | 25,053 | 155,956 |
| Dividend payments to shareholders | (172,844) | (145,809) |
| Net cash used for financing activities | (1,381,116) | (577,971) |

| | | |
|--|------------|------------|
| Effect of exchange rate changes on cash | 1,589 | 1,427 |
| Net increase (decrease) in cash and cash equivalents | 49,951 | (104,466) |
| Cash and cash equivalents at beginning of period | 343,947 | 627,591 |
| Cash and cash equivalents at end of period | \$ 393,898 | \$ 523,125 |

See accompanying notes.

Table of Contents

ANALOG DEVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE AND NINE MONTHS ENDED AUGUST 4, 2007

(all tabular amounts in thousands except per share amounts and percentages)

Note 1 Basis of Presentation

In the opinion of management, the information furnished in the accompanying condensed consolidated financial statements reflects all normal recurring adjustments that are necessary to fairly state the results for these interim periods and should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended October 28, 2006 and related notes. The results of operations for the interim periods shown in this report are not necessarily indicative of the results that may be expected for the fiscal year ending November 3, 2007 or any future period.

The Company has a 52-53 week fiscal year that ends on the Saturday closest to the last day in October. Fiscal 2007 is a 53-week fiscal year and fiscal 2006 was a 52-week fiscal year. The additional week in fiscal 2007 was included in the first quarter ended February 3, 2007. Therefore, the first nine months of fiscal 2007 included an additional week of operations as compared to the first nine months of fiscal 2006.

Note 2 Stock-Based Compensation

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R). SFAS 123R supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and amends SFAS No. 95, *Statement of Cash Flows*. Generally, the approach in SFAS 123R is similar to the approach described in SFAS 123 *Accounting for Stock-Based Compensation*. However, SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement over their vesting period based on their fair values at the date of grant. Pro forma disclosure is no longer an alternative.

On October 30, 2005 (the first day of its 2006 fiscal year), the Company adopted SFAS 123R using the modified prospective method as permitted under SFAS 123R. Under this transition method, compensation cost recognized in fiscal 2006 and fiscal 2007 includes: (a) compensation cost for all share-based payments granted prior to but not yet vested as of October 29, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to October 29, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. In accordance with the modified prospective method of adoption, the Company's results of operations and financial position for prior periods were not restated.

Grant-Date Fair Value

The Company uses the Black-Scholes option pricing model to calculate the grant-date fair value of an award. Information pertaining to the Company's stock option awards and the related estimated weighted-average assumptions to calculate the fair value of stock options granted during the three- and nine-month periods ended August 4, 2007 and July 29, 2006 are as follows:

| Stock Options | Three Months Ended | | Nine Months Ended | |
|---|--------------------|------------------|-------------------|------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Options granted (in thousands) | 109 | 158 | 7,649 | 8,398 |
| Weighted-average exercise price of stock options | \$38.74 | \$33.46 | \$33.50 | \$39.29 |
| Weighted-average grant-date fair value of stock options | \$11.52 | \$ 9.84 | \$ 9.49 | \$11.58 |
| Assumptions: | | | | |
| Weighted-average expected volatility | 30.5% | 30.2% | 30.9% | 28.6% |
| Weighted-average expected term (in years) | 5.1 | 5.0 | 5.1 | 5.0 |
| Risk-free interest rate | 4.9% | 5.1% | 4.6% | 4.4% |

| | | | | |
|-------------------------|-------|-------|-------|-------|
| Expected dividend yield | 1.86% | 1.92% | 2.15% | 1.24% |
|-------------------------|-------|-------|-------|-------|

7

Table of Contents

Expected volatility - The Company is responsible for estimating volatility and has considered a number of factors, including third-party estimates, when estimating volatility. For options granted prior to fiscal 2005, the Company used historical volatility to estimate the grant-date fair value of stock options. The Company changed its method of estimating expected volatility for all stock options granted after fiscal 2004 from exclusively relying on historical volatility to exclusively relying on implied volatility. This change was the result of a thorough review the Company undertook, which included consultations with several third-party advisors. The Company currently believes that the exclusive use of implied volatility results in a more accurate estimate of the grant-date fair value of employee stock options because it more appropriately reflects the market's current expectations of future volatility. Historical volatility during the period commensurate with the expected term of the Company's stock options over the past several years included a period of time when the Company's stock price experienced unprecedented increases and subsequent declines. The Company believes that this past stock price volatility is unlikely to be indicative of future stock price behavior. Options in the Company's common stock are actively traded on several exchanges. Implied volatility is calculated for the period that is commensurate with the option's expected term assumption. Because this term often exceeds the period for which there are exchange-traded options in the Company's common stock, statistical techniques are used to derive the implied volatility for traded options with terms commensurate with the option's expected term of 5.1 years. This calculation of implied volatility is derived from the closing prices of both the Company's common stock and exchange-traded options from the most recent five trading days prior to the grant date of the employee stock option.

Expected term - The Company uses historical employee exercise and option expiration data to estimate the expected term assumption for the Black-Scholes grant-date valuation. The Company believes that this historical data is currently the best estimate of the expected term of a new option, and that generally its employees exhibit similar exercise behavior.

Risk-free interest rate - The yield on zero-coupon U.S. Treasury securities for a period that is commensurate with the expected term assumption is used as the risk-free interest rate.

Expected dividend yield - Expected dividend yield is calculated by annualizing the cash dividend declared by the Company's Board of Directors for the current quarter and dividing that result by the closing stock price on the date of grant. Until such time as the Company's Board of Directors declares a cash dividend for an amount that is different from the current quarter's cash dividend, the current dividend will be used in deriving this assumption. Cash dividends are not paid on options, restricted stock or restricted stock units.

Stock-Based Compensation Expense

The Company used the graded attribution method to recognize expense for all stock-based awards prior to the adoption of SFAS 123R. Upon adoption of SFAS 123R on October 30, 2005, the Company changed to the straight-line attribution method to recognize expense for stock-based awards granted after October 29, 2005. The change to the straight-line attribution method was made so that the expense associated with each stock-based award is recognized ratably over the vesting period. The expense associated with the unvested portion of the pre-adoption grants will continue to be expensed using the graded attribution method.

The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term "forfeitures" is distinct from cancellations or expirations and represents only the unvested portion of the surrendered stock-based award. Based on an analysis of its historical forfeitures, the Company has applied an annual forfeiture rate of 4.3% to all unvested stock-based awards as of August 4, 2007. The rate of 4.3% represents the portion that is expected to be forfeited each year over the vesting period. This analysis is re-evaluated quarterly and the forfeiture rate is adjusted as necessary. Ultimately, the actual expense recognized over the vesting period will only be for those awards that vest. The adoption of SFAS 123R had the following impact on the third quarter of fiscal 2007 results: operating profit before tax was lower by \$17.2 million, net income was lower by \$12.2 million, cash flow from operations was lower by \$3.6 million, cash flow from financing activities was higher by \$3.6 million and basic and diluted EPS were each lower by \$0.04. The adoption of SFAS 123R had the following impact on results for the nine-months ended August 4, 2007: operating profit before tax was lower by \$54.5 million, net income was lower by \$38.7 million, cash flow from

operations was lower by \$25.1 million, cash flow from financing activities was higher by \$25.1 million and basic and diluted EPS were each lower by \$0.12.

Table of Contents

The adoption of SFAS 123R had the following impact on the third quarter of fiscal 2006 results: operating profit before tax was decreased by \$19.0 million, net income was decreased by \$13.4 million, cash flow from operations was decreased by \$141.2 million, cash flow from financing activities was increased by \$141.2 million and basic and diluted EPS were each decreased by \$0.04. The adoption of SFAS 123R had the following impact on results for the nine months ended July 29, 2006: operating profit before tax was decreased by \$56.6 million, net income was decreased by \$40.3 million, cash flow from operations was decreased by \$156.0 million, cash flow from financing activities was increased by \$156.0 million and basic and diluted EPS were each decreased by \$0.11.

Stock-Based Compensation Activity

A summary of the activity under the Company's stock option plans as of August 4, 2007 and changes during the three- and nine-month periods then ended is presented below:

| Quarter-to-Date Activity | Options Outstanding | Weighted- Average Exercise Price Per Share | Weighted- Average Remaining Contractual Term in Years | Aggregate Intrinsic Value |
|---|--------------------------------|---|--|--|
| Options outstanding at May 5, 2007 | 83,187 | \$ 35.08 | | |
| Options granted | 109 | \$ 38.74 | | |
| Options exercised | (969) | \$ 18.47 | | |
| Options forfeited | (243) | \$ 35.14 | | |
| Options expired | (386) | \$ 43.84 | | |
| Options outstanding at August 4, 2007 | 81,698 | \$ 35.24 | 5.4 | \$347,045 |
| Options exercisable at August 4, 2007 | 54,670 | \$ 35.30 | 4.2 | \$286,904 |
| Options vested or expected to vest at August 4, 2007 (1) | 79,907 | \$ 35.21 | 5.4 | \$345,627 |

- (1) In addition to the vested options, the Company expects a portion of the unvested options to vest at some point in the future. Options expected to vest is calculated by applying an estimated forfeiture rate to

the unvested
options.

| Fiscal Year-to-Date Activity | Options Outstanding | Weighted- Average Exercise Price Per Share |
|--|--------------------------------|---|
| Options outstanding at October 28, 2006 | 84,461 | \$ 34.09 |
| Options granted | 7,649 | \$ 33.50 |
| Options exercised | (6,450) | \$ 14.93 |
| Options forfeited | (1,537) | \$ 35.12 |
| Options expired | (2,425) | \$ 44.00 |
| Options outstanding at August 4, 2007 | 81,698 | \$ 35.24 |

During the three and nine months ended August 4, 2007, the total intrinsic value of options exercised (i.e., the difference between the market price at exercise and the price paid by the employee to exercise the options) was \$19.8 million and \$136.2 million, respectively, and the total amount of cash received from exercise of these options was \$17.9 million and \$96.2 million, respectively. The total grant-date fair value of stock options that vested during the three and nine months ended August 4, 2007 was approximately \$1.0 million and \$39.5 million, respectively. During the three and nine months ended July 29, 2006, the total intrinsic value of options exercised was \$9.3 million and \$96.3 million, respectively, and the total amount of cash received from exercise of these options was \$8.2 million and \$68.0 million, respectively. The total grant-date fair value of stock options that vested during the three and nine months ended July 29, 2006 was approximately \$1.0 million and \$108.7 million, respectively.

Table of Contents

A summary of the Company's restricted stock and restricted stock unit awards activity as of August 4, 2007 and changes during the three- and nine- month periods then ended is presented below:

| Quarter-to-Date Activity | Restricted Shares Outstanding | Weighted- Average Grant Date Fair Value Per Share |
|--|--|--|
| Non-vested shares outstanding at May 5, 2007 | 62 | \$ 34.29 |
| Awards and/or units granted | 4 | \$ 39.13 |
| Restrictions lapsed | (3) | \$ 32.33 |
| Awards and/or units forfeited | | |
| Non-vested shares outstanding at August 4, 2007 | 63 | \$ 34.67 |

| Fiscal Year-to-Date Activity | Restricted Shares Outstanding | Weighted- Average Grant Date Fair Value Per Share |
|--|--|--|
| Non-vested shares outstanding at October 28, 2006 | 55 | \$ 35.35 |
| Awards and/or units granted | 22 | \$ 34.44 |
| Restrictions lapsed | (14) | \$ 37.01 |
| Awards and/or units forfeited | | |
| Non-vested shares outstanding at August 4, 2007 | 63 | \$ 34.67 |

As of August 4, 2007, there was \$163.9 million (before tax consideration) of total unrecognized compensation cost related to unvested share-based awards, including stock options, restricted stock and restricted stock units. That cost is expected to be recognized over a weighted-average period of 1.8 years.

Note 3 Comprehensive Income

Components of comprehensive income include net income and certain transactions that have generally been reported in the consolidated statement of shareholders' equity and consist of the following:

| | Three Months Ended | |
|---|--------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Net income | \$ 120,435 | \$ 144,685 |
| Foreign currency translation adjustments | 773 | (131) |
| Change in unrealized holding gains (net of taxes of \$510 and \$1,099, respectively) on securities classified as short-term investments | 947 | 2,040 |
| Change in unrealized holding gains (losses) (net of taxes of \$5 and \$144, respectively) on securities classified as other investments | 9 | (268) |

| | | |
|--|------------|------------|
| Change in unrealized (losses) gains on derivative instruments designated as cash flow hedges | (850) | 885 |
| Other comprehensive income | 879 | 2,526 |
| Comprehensive income | \$ 121,314 | \$ 147,211 |

Table of Contents

| | Nine Months Ended | |
|---|-------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Net income | \$ 399,018 | \$ 411,063 |
| Foreign currency translation adjustments | 5,826 | 575 |
| Change in unrealized holding gains (net of taxes of \$2,480 and \$2,645, respectively) on securities classified as short-term investments | 4,596 | 4,911 |
| Change in unrealized holding losses (net of taxes of \$75 and \$248, respectively) on securities classified as other investments | (139) | (461) |
| Change in unrealized gains on derivative instruments designated as cash flow hedges | 3,038 | 7,944 |
| Other comprehensive income | 13,321 | 12,969 |
| Comprehensive income | \$ 412,339 | \$ 424,032 |

The components of accumulated other comprehensive income (loss) at August 4, 2007 and October 28, 2006 consisted of the following:

| | August 4, 2007 | October 28, 2006 |
|---|-------------------|---------------------|
| Foreign currency translation adjustment | \$ 15,240 | \$ 9,414 |
| Unrealized losses on available-for-sale securities | (914) | (5,371) |
| Unrealized gains on derivative instruments | 3,457 | 419 |
| Minimum pension liability adjustment | (4,669) | (4,669) |
| Total accumulated other comprehensive income (loss) | \$ 13,114 | \$ (207) |

Note 4 Earnings Per Share

Basic earnings per share is computed based only on the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted-average number of common shares outstanding during the period, plus the dilutive effect of potential future issuances of common stock relating to stock option programs and other potentially dilutive securities using the treasury stock method. In calculating diluted earnings per share, the dilutive effect of stock options is computed using the average market price for the respective period. In addition, under SFAS 123R, the assumed proceeds under the treasury stock method include the average unrecognized compensation expense of stock options that are in-the-money. This results in the assumed buyback of additional shares, thereby reducing the dilutive impact of stock options. Potential shares related to certain of the Company's outstanding stock options were excluded because they were anti-dilutive. Those potential shares, determined based on the weighted-average exercise prices during the respective periods, related to the Company's outstanding stock options could be dilutive in the future. The following table sets forth the computation of basic and diluted earnings per share:

Table of Contents

| | Three Months Ended | |
|---|--------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Basic: | | |
| Net income | \$ 120,435 | \$ 144,685 |
| Weighted-average shares outstanding | 318,465 | 357,887 |
| Earnings per share | \$ 0.38 | \$ 0.40 |
| Diluted: | | |
| Net income | \$ 120,435 | \$ 144,685 |
| Weighted-average shares outstanding | 318,465 | 357,887 |
| Assumed exercise of common stock equivalents | 8,866 | 11,655 |
| Weighted-average common and common equivalent shares | 327,331 | 369,542 |
| Earnings per share | \$ 0.37 | \$ 0.39 |
| Anti-dilutive common stock equivalents related to outstanding stock options | 40,064 | 56,118 |
| | | |
| | Nine Months Ended | |
| | August 4, 2007 | July 29, 2006 |
| Basic: | | |
| Net income | \$ 399,018 | \$ 411,063 |
| Weighted-average shares outstanding | 329,050 | 362,749 |
| Earnings per share | \$ 1.21 | \$ 1.13 |
| Diluted: | | |
| Net income | \$ 399,018 | \$ 411,063 |
| Weighted-average shares outstanding | 329,050 | 362,749 |
| Assumed exercise of common stock equivalents | 9,410 | 12,814 |
| Weighted-average common and common equivalent shares | 338,460 | 375,563 |

Edgar Filing: ANALOG DEVICES INC - Form 10-Q

| | | |
|---|---------|---------|
| Earnings per share | \$ 1.18 | \$ 1.09 |
| Anti-dilutive common stock equivalents related to outstanding stock options | 49,568 | 50,813 |

12

Table of Contents**Note 5 Special Charges**

A summary of the Company's special charges is as follows:

| Income Statement | Closure of Wafer Fabrication Facility | Reorganization of Product Development and Support Programs | Total Special Charges |
|------------------------------------|--|---|--------------------------------------|
| Fiscal 2005 Charges: | | | |
| Workforce reductions | \$ 20,315 | \$ 11,165 | \$ 31,480 |
| Total Fiscal 2005 Charges | \$ 20,315 | \$ 11,165 | \$ 31,480 |
| Fiscal 2006 Charges: | | | |
| Facility closure costs | \$ | \$ 554 | \$ 554 |
| Abandonment of equipment | | 459 | 459 |
| Other items | | 462 | 462 |
| Change in estimate | (2,029) | | (2,029) |
| Workforce reductions | | 2,344 | 2,344 |
| Total Fiscal 2006 Charges | \$ (2,029) | \$ 3,819 | \$ 1,790 |
| Fiscal 2007 Charges: | | | |
| Facility closure costs | \$ 10,288 | \$ | \$ 10,288 |
| Workforce reductions | | 4,165 | 4,165 |
| Other items | | 859 | 859 |
| Total Fiscal 2007 Charges | \$ 10,288 | \$ 5,024 | \$ 15,312 |
| Accrued Restructuring | | | |
| Balance at October 28, 2006 | \$ 5,903 | \$ 4,976 | \$ 10,879 |
| Special Charges | 3,608 | 1,588 | 5,196 |
| Severance payments | (4,205) | (1,485) | (5,690) |
| Facility closure costs | (3,251) | | (3,251) |

| | | | | | | |
|------------------------------------|----|---------|----|---------|----|---------|
| Balance at February 3, 2007 | \$ | 2,055 | \$ | 5,079 | \$ | 7,134 |
| Special Charges | | 6,680 | | 3,436 | | 10,116 |
| Severance payments | | (987) | | (1,340) | | (2,327) |
| Facility closure costs | | (1,979) | | (208) | | (2,187) |
| Balance at May 5, 2007 | \$ | 5,769 | \$ | 6,967 | \$ | 12,736 |
| Severance payments | | (245) | | (1,101) | | (1,346) |
| Facility closure costs | | (789) | | (243) | | (1,032) |
| Balance at August 4, 2007 | \$ | 4,735 | \$ | 5,623 | \$ | 10,358 |

Closure of Wafer Fabrication Facility

During the fourth quarter of fiscal 2005, the Company recorded a special charge of \$20.3 million as a result of a decision to close its California wafer fabrication operations and transfer virtually all of the production of products manufactured there to the Company's facility in Wilmington, Massachusetts. The charge was for severance and fringe benefit costs that were recorded pursuant to SFAS 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits* (SFAS 88), under the Company's ongoing benefit plan for 339 manufacturing employees and 28 general and administrative employees at that site. The severance benefit was calculated based on length of past service, and employees had to continue to be employed until they were involuntarily terminated in order to receive the severance benefit. The Company completed the remaining cleanup and closure activities during the second quarter of fiscal 2007. The employment of all of the employees included in this action has been terminated by the Company.

Table of Contents

In addition to the charge recorded in the fourth quarter of fiscal 2005, the Company recorded additional expense during fiscal 2006, which consisted of \$18.3 million of non-cash cost of sales expenses for additional depreciation due to shortened useful lives of certain manufacturing equipment and \$2.0 million for stay-on bonuses. The Company reversed approximately \$2.0 million of its severance accrual during fiscal 2006 because some employees voluntarily left the Company, other employees found alternative employment within the Company, and there was an over accrual related to fringe benefits because severance payments, normally paid as income continuance, were paid as lump sum payments, which reduced the benefit costs associated with these payments.

The Company ceased production at the wafer fabrication facility on November 9, 2006. During the first quarter of fiscal 2007, the Company recorded additional expense, in accordance with SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities* (SFAS 146), which consisted of \$3.2 million for clean-up and closure costs that were charged to expense as incurred and \$0.4 million for lease obligation costs for a warehouse facility the Company ceased using during the first quarter of fiscal 2007. During the second quarter of fiscal 2007, the Company recorded a special charge, in accordance with SFAS 146, which included \$5.0 million of expense for future lease obligation costs for the wafer fabrication facility that the Company ceased using during the second quarter of fiscal 2007. Also included in the special charge was \$1.7 million for clean-up and closure costs that were charged to expense as incurred. The clean-up activity was completed during the second quarter of fiscal 2007, and the Company does not expect to incur any additional expenses related to this action.

Reorganization of Product Development and Support Programs

During the fourth quarter of fiscal 2005, the Company recorded a special charge of \$11.2 million as a result of its decision to reorganize its product development and support programs with the goal of providing greater focus on its analog and digital signal processing product programs. The charge was for severance and fringe benefit costs that were recorded pursuant to SFAS 88 under the Company's ongoing benefit plan or statutory requirements at foreign locations for 60 manufacturing employees and 154 engineering and selling, marketing, general and administrative employees.

During fiscal 2006, the Company recorded an additional special charge of \$3.8 million related to this reorganization action. Approximately \$1.5 million of this charge was for lease obligation costs for a facility the Company ceased using during the first quarter of fiscal 2006 and the write-off of property, plant and equipment and other items at this facility. The remaining \$2.3 million related to severance and fringe benefit costs that were recorded in the fourth quarter pursuant to SFAS 88 under the Company's ongoing benefit plan or statutory requirements at foreign locations for 46 engineering and selling, marketing, general and administrative employees.

During the first quarter of fiscal 2007, the Company recorded an additional special charge of \$1.6 million related to this reorganization action. Approximately \$0.6 million of this charge was for contract termination costs. The remaining \$1.0 million relates to severance and fringe benefit costs that were recorded in the first quarter pursuant to SFAS 88 under the Company's ongoing benefit plan for six engineering employees.

During the second quarter of fiscal 2007, the Company recorded an additional special charge of \$3.4 million related to this reorganization action. Approximately \$3.2 million relates to the severance and fringe benefit costs that were recorded in the second quarter pursuant to SFAS 88 under the Company's ongoing benefit plan or minimum statutory requirements at foreign locations for 20 engineering and selling, marketing, general and administrative employees. The remaining \$0.2 million of this charge was for lease obligation costs for a facility the Company ceased using during the second quarter of fiscal 2007.

As of August 4, 2007, eight of the 286 employees included in this reorganization action were still employed by the Company. These employees must continue to be employed until they are involuntarily terminated in order to receive the severance benefit.

Note 6 Segment Information

The Company operates and tracks its results in one reportable segment. The Company designs, develops, manufactures and markets a broad range of integrated circuits. The Chief Executive Officer has been identified as the Chief Operating Decision Maker as defined by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*.

Table of Contents*Revenue Trends by End Market*

The categorization of revenue by end market is determined using a variety of data points including the technical characteristics of the product, the sold to customer information, the ship to customer information and the end customer product or application into which the Company's product will be incorporated. As data systems for capturing and tracking this data evolve and improve, the categorization of products by end market can vary over time. When this occurs the Company reclassifies revenue by end market for prior periods. Such reclassifications typically do not materially change the sizing of, or the underlying trends of results within, each end market.

| | Three Months Ended August 4, 2007 | | | Three Months Ended July 29, 2006 | |
|------------------------------|--------------------------------------|-------------------------------------|-----------|-------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y% | Revenue | % of Total Product Revenue |
| Industrial | \$ 293,557 | 43% | 3% | \$ 285,334 | 43% |
| Communications | 191,082 | 28% | (4%) | 198,414 | 30% |
| Consumer | 136,577 | 20% | 24% | 110,270 | 17% |
| Computer | 59,096 | 9% | (15%) | 69,642 | 10% |
| Total Product Revenue | \$ 680,312 | 100% | 3% | \$ 663,660 | 100% |

| | Nine Months Ended August 4, 2007 | | | Nine Months Ended July 29, 2006 | |
|------------------------------|-------------------------------------|-------------------------------------|-----------|------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y% | Revenue | % of Total Product Revenue |
| Industrial | \$ 880,827 | 44% | 8% | \$ 818,728 | 43% |
| Communications | 550,960 | 27% | (5%) | 578,512 | 30% |
| Consumer | 398,597 | 20% | 27% | 314,412 | 16% |
| Computer | 175,674 | 9% | (19%) | 217,182 | 11% |
| Total Product Revenue | \$ 2,006,058 | 100% | 4% | \$ 1,928,834 | 100% |

One-time payment associated with
the licensing of IP*

35,000

Total Revenue **\$ 2,041,058** **\$ 1,928,834**

* During the first quarter of fiscal 2007, the Company recorded revenue of \$35 million

received in
exchange for
licensing of
certain
intellectual
property rights
to a third party.

Table of Contents*Revenue Trends by Product*

The following table summarizes revenue by product categories. The categorization of the Company's products into broad categories is based on the characteristics of the individual products, the specification of the products and in some cases the specific uses that certain products have within applications. The categorization of products into categories is therefore subject to judgment in some cases and can vary over time. In instances where products move between product categories the Company reclassifies the amounts in the product categories for all prior periods. Such reclassifications typically do not materially change the sizing of, or the underlying trends of results within, each product category.

| | Three Months Ended August 4, 2007 | | | Three Months Ended July 29, 2006 | |
|------------------------------|--------------------------------------|-------------------------------------|--------------|-------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y % | Revenue | % of Total Product Revenue |
| Converters | \$ 281,530 | 41% | 5% | \$ 268,949 | 41% |
| Amplifiers | 144,103 | 21% | 4% | 138,634 | 21% |
| Power management & reference | 50,019 | 7% | (8%) | 54,661 | 8% |
| Other analog | 98,020 | 15% | 34% | 73,102 | 11% |
| Total analog products | \$ 573,672 | 84% | 7% | \$ 535,346 | 81% |
| General purpose DSP | 52,891 | 8% | (1%) | 53,187 | 8% |
| Wireless Chipsets | 45,030 | 7% | (33%) | 66,975 | 10% |
| Other DSP | 8,719 | 1% | 7% | 8,152 | 1% |
| Total DSP products | \$ 106,640 | 16% | (17%) | \$ 128,314 | 19% |
| Total Product Revenue | \$ 680,312 | 100% | 3% | \$ 663,660 | 100% |

| | Nine Months Ended August 4, 2007 | | | Nine Months Ended July 29, 2006 | |
|------------------------------|-------------------------------------|-------------------------------------|--------------|------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y % | Revenue | % of Total Product Revenue |
| Converters | \$ 819,850 | 41% | 8% | \$ 758,438 | 39% |
| Amplifiers | 419,018 | 21% | 7% | 390,982 | 20% |
| Power management & reference | 148,278 | 7% | (10%) | 163,957 | 9% |
| Other analog | 289,995 | 15% | 32% | 219,930 | 11% |
| Total analog products | \$ 1,677,141 | 84% | 9% | \$ 1,533,307 | 79% |
| General purpose DSP | 158,038 | 8% | 5% | 150,511 | 8% |
| Wireless Chipsets | 147,337 | 7% | (27%) | 201,895 | 11% |
| Other DSP | 23,542 | 1% | (45%) | 43,121 | 2% |
| Total DSP products | \$ 328,917 | 16% | (17%) | \$ 395,527 | 21% |

| | | | | | |
|---|---------------------|--------------|------------|---------------------|--------------|
| Total Product Revenue | \$ 2,006,058 | 100 % | 4 % | \$ 1,928,834 | 100 % |
| One-time payment associated with the licensing of IP* | 35,000 | | | | |
| Total Revenue | \$ 2,041,058 | | | \$ 1,928,834 | |

* During the first quarter of fiscal 2007, the Company recorded revenue of \$35 million received in exchange for licensing of certain intellectual property rights to a third party.

Table of Contents*Revenue Trends by Geographic Region*

Product revenue by geographic region, based upon point of sale, for the three- and nine-month periods ended August 4, 2007 and July 29, 2006 are as follows:

| Region | Three Months Ended | | Nine Months Ended | |
|------------------------------|--------------------|-------------------|---------------------|---------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| United States | \$ 155,839 | \$ 164,842 | \$ 487,425 | \$ 487,103 |
| Europe | 154,252 | 148,721 | 452,733 | 422,749 |
| Japan | 130,100 | 123,169 | 385,677 | 360,501 |
| China | 109,546 | 90,178 | 288,136 | 256,773 |
| Rest of Asia | 130,575 | 136,750 | 392,087 | 401,708 |
| Total Product Revenue | \$ 680,312 | \$ 663,660 | \$ 2,006,058 | \$ 1,928,834 |

Note 7 Goodwill and Intangible Assets*Goodwill*

The Company evaluates goodwill for impairment annually as well as whenever events or changes in circumstances suggest that the carrying value of goodwill may not be recoverable. Because the Company has one reporting segment under SFAS 142, the Company utilizes the entity-wide approach for assessing goodwill for impairment and compares its market value to its net book value to determine if an impairment exists. No impairment of goodwill resulted from the Company's most recent evaluation of goodwill for impairment, which occurred in the fourth quarter of fiscal 2006. No impairment of goodwill resulted in any of the fiscal periods presented. The Company's next annual impairment assessment will be made in the fourth quarter of fiscal 2007. The following table presents the changes in goodwill during the first nine months of fiscal 2007 and the fiscal year ended October 28, 2006:

| | For the nine months ended August 4, 2007 | For the fiscal year ended October 28, 2006 |
|--|--|--|
| Balance at beginning of period | \$ 256,209 | \$ 163,373 |
| Acquisition of TTPCom assets(1) | 4,273 | 812 |
| Acquisition of Integrant Technologies(2) | 13,282 | 80,641 |
| Acquisition of AudioAsics | | 7,250 |
| Foreign currency translation adjustment | 3,208 | 4,133 |
| Balance at end of period | \$ 276,972 | \$ 256,209 |

(1) The Company paid its final milestone related to this acquisition in the second quarter of fiscal 2007.

- (2) The Company completed the final purchase accounting for this transaction during the first quarter of fiscal 2007, which resulted in an additional \$5.6 million of goodwill. The Company also purchased additional outstanding minority shares related to this acquisition during the second and third quarters of fiscal 2007, which resulted in an additional \$7.7 million of goodwill.

Intangible Assets

The Company reviews identified intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value of assets may not be recoverable. Recoverability of these assets is measured by comparison of their carrying value to future undiscounted cash flows the assets are expected to generate over their remaining economic lives. If such assets are considered to be impaired, the impairment to be recognized in earnings equals the amount by which the carrying value of the assets exceeds their fair market value determined by either a quoted market price, if any, or a value determined by utilizing a discounted cash flow technique.

Table of Contents

Intangible assets, which will continue to be amortized, consisted of the following:

| | August 4, 2007 | | October 28, 2006 | |
|------------------------|-----------------------|--------------------------|-----------------------|--------------------------|
| | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount | Accumulated Amortization |
| Technology-based | \$ 54,409 | \$ 25,837 | \$ 53,177 | \$ 17,714 |
| Tradenname | 1,670 | 1,296 | 1,635 | 995 |
| Customer Relationships | 7,194 | 2,532 | 6,920 | 707 |
| Other | 6,585 | 6,300 | 6,617 | 6,125 |
| Total | \$ 69,858 | \$ 35,965 | \$ 68,349 | \$ 25,541 |

Intangible assets acquired prior to the third quarter of fiscal 2006 continue to be amortized on a straight-line basis over their estimated useful lives, which range from five to ten years. The \$43.1 million of intangible assets acquired during the third and fourth quarters of fiscal 2006 are being amortized over their estimated useful lives of five years using an accelerated method of amortization that is expected to reflect the estimated pattern of economic use. The remaining amortization expense will be recognized over a weighted-average period of approximately 1.7 years. Amortization expense related to intangibles was \$3.2 million and \$1.1 million for the three-month periods ended August 4, 2007 and July 29, 2006, respectively, and \$10.0 million and \$2.0 million for the nine-month periods ended August 4, 2007 and July 29, 2006, respectively.

The Company expects amortization expense for these intangible assets to be:

| Fiscal Year | Amortization Expense |
|-------------------|----------------------|
| Remainder of 2007 | \$ 3,117 |
| 2008 | \$ 12,477 |
| 2009 | \$ 9,426 |
| 2010 | \$ 5,924 |
| 2011 | \$ 2,761 |
| 2012 | \$ 188 |

Note 8 Pension Plans

The Company has various defined benefit pension and other retirement plans for certain non-U.S. employees that are consistent with local statutory requirements and practices. The Company's funding policy for its foreign defined benefit pension plans is consistent with the local requirements of each country. The plans' assets consist primarily of U.S. and non-U.S. equity securities, bonds, property and cash.

Net periodic pension cost of non-U.S. plans is presented in the following table:

| | Three Months Ended | |
|------------------------------------|--------------------|---------------|
| | August 4, 2007 | July 29, 2006 |
| Service cost | \$ 2,799 | \$ 2,712 |
| Interest cost | 2,251 | 1,850 |
| Expected return on plan assets | (2,428) | (1,819) |
| Amortization of prior service cost | 2 | 30 |
| Amortization of transitional asset | (10) | (7) |
| Recognized actuarial loss | 206 | 398 |
| Net periodic pension cost | \$ 2,820 | \$ 3,164 |

Table of Contents

| | Nine Months Ended | |
|------------------------------------|-------------------|---------------|
| | August | July 29, 2006 |
| | 4, 2007 | |
| Service cost | \$ 8,267 | \$ 7,836 |
| Interest cost | 6,704 | 5,344 |
| Expected return on plan assets | (7,239) | (5,256) |
| Amortization of prior service cost | 6 | 86 |
| Amortization of transitional asset | (27) | (20) |
| Recognized actuarial loss | 605 | 1,146 |
| Net periodic pension cost | \$ 8,316 | \$ 9,136 |

Pension contributions of \$2.0 million and \$6.3 million were made by the Company during the three and nine months ended August 4, 2007, respectively. The Company presently anticipates contributing an additional \$1.6 million to fund its defined benefit pension plans in fiscal year 2007 for a total of \$7.9 million.

Note 9 Product Warranties

The Company generally offers a 12-month warranty for its products. The Company's warranty policy provides for replacement of the defective product. Specific accruals are recorded for known product warranty issues. Product warranty expenses were not material during any of the three- and nine-month periods ended August 4, 2007 and July 29, 2006.

Note 10 Commitments and Contingencies*Tentative Settlement of the SEC's Previously Announced Stock Option Investigation*

In the Company's 2004 Form 10-K filing, the Company disclosed that the Securities and Exchange Commission (SEC) had initiated an inquiry into its stock option granting practices, focusing on options that were granted shortly before the issuance of favorable financial results. On November 15, 2005, the Company announced that it had reached a tentative settlement with the SEC.

At all times since receiving notice of this inquiry, the Company has cooperated with the SEC. In November 2005, the Company and its President and CEO, Mr. Jerald G. Fishman, made an offer of settlement to the Staff of the SEC. The settlement has been submitted to the Commission for approval. There can be no assurance a final settlement will be so approved.

The SEC's inquiry focused on two separate issues. The first issue concerned the Company's disclosure regarding grants of options to employees and directors prior to the release of favorable financial results. Specifically, the issue related to options granted to employees (including officers) of the Company on November 30, 1999 and to employees (including officers) and directors of the Company on November 10, 2000.

The second issue concerned the grant dates for options granted to employees (including officers) in 1998 and 1999, and the grant date for options granted to employees (including officers) and directors in 2001. Specifically, the settlement would conclude that the appropriate grant date for the September 4, 1998 options should have been September 8th (which is one trading day later than the date that was used to price the options); the appropriate grant date for the November 30, 1999 options should have been November 29th (which is one trading day earlier than the date that was used); and the appropriate grant date for the July 18, 2001 options should have been July 26th (which is five trading days after the original date).

In connection with the proposed settlement, the Company would consent to a cease-and-desist order under Section 10(b) of the Securities Exchange Act and Rule 10b-5 thereunder, would pay a civil money penalty of \$3 million, and would reprice options granted to Mr. Fishman in certain years. Options granted to all others would be excluded from the repricing. Mr. Fishman would consent to a cease-and-desist order under Sections 17(a)(2) and (3) of the Securities Act, would pay a civil money penalty of \$1 million, and would make a disgorgement payment with respect to options granted in certain years. With the exception of options granted in 1998, Mr. Fishman has not exercised or sold any of the options identified in this matter. The Company and Mr. Fishman would settle this matter without admitting or

denying the Commission's findings.

Table of Contents

The Company has determined that no restatement of its historical financial results would be necessary due to the proposed settlement.

Other Legal Proceedings

In May 2006, the Company received a document subpoena from the U.S. Attorney for the Southern District of New York requesting records from 2000 to the present relating to the Company's granting of stock options. The Company believes that the options at issue in this matter are the same option grants which have been the subject of investigation by the SEC. The Company is cooperating with the office of the U.S. Attorney in connection with this subpoena. The Company cannot predict the outcome of this matter, but believes the disposition of the matter will not have a material adverse effect on the Company or its financial position.

On May 25, 2006, the Company filed a lawsuit in United States District Court for the District of Delaware against Linear Technology Corp. (LTC), alleging infringement of three Company patents by LTC's making, selling and using various products. In addition, the Company also sought a declaratory judgment that its products do not infringe eight patents allegedly owned by LTC (the LTC patents) and that the LTC patents are invalid. On July 28, 2006, LTC filed an answer and counterclaims, denying that its products infringe the asserted Company patents and asking the court to declare such patents invalid. LTC also claimed that the Company, by making, selling and using various power management products, is infringing seven of the eight LTC patents. LTC seeks damages in an unspecified amount and injunctive relief. On August 21, 2006, the Company filed its answer to LTC's counterclaims, denying all liability to LTC. The case is currently in the discovery phase and trial is scheduled to begin in June 2008. The Company intends to vigorously pursue its claims against LTC, and to vigorously defend against LTC's counterclaims. The Company is unable at this time to predict the outcome of this litigation; however, the Company believes that the final disposition of this matter will not have a material adverse effect on the Company or its financial position.

On October 13, 2006, a purported class action complaint was filed in the United States District Court for the District of Massachusetts on behalf of participants in the Company's Investment Partnership Plan from October 5, 2000 to the present. The complaint named as defendants the Company, certain officers and directors, and the Company's Investment Partnership Plan Administration Committee. The complaint alleges purported violations of federal law in connection with the Company's option granting practices during the years 1998, 1999, 2000, and 2001, including breaches of fiduciary duties owed to participants and beneficiaries of the Company's Investment Partnership Plan under the Employee Retirement Income Security Act. The complaint seeks unspecified monetary damages, as well as equitable and injunctive relief. The Company intends to vigorously defend against these allegations. On November 22, 2006, the Company and the individual defendants filed motions to dismiss the complaint. On January 8, 2007, the Plaintiff filed memoranda in opposition. On January 22, 2007, the Company and the individual defendants filed further memoranda in support of the motions to dismiss. Although the Company believes it has meritorious defenses to the asserted claims, it is unable at this time to predict the outcome of this proceeding.

From time to time as a normal incidence of the nature of the Company's business, various claims, charges and litigation are asserted or commenced against the Company arising from, or related to, contractual matters, patents, trademarks, personal injury, environmental matters, product liability, insurance coverage and personnel and employment disputes. As to such claims and litigation the Company can give no assurance that it will prevail.

While the Company does not believe that any of the matters described above will have a material adverse effect on the Company's financial position, an adverse outcome of any of these matters is possible and could have a material adverse effect on the Company's consolidated results of operations or cash flows in the quarter or annual period in which one or more of these matters are resolved.

Note 11 Common Stock Repurchase

Since August 2004, the Company has had a common stock repurchase program in place. On December 6, 2006 the Board of Directors authorized the repurchase by the Company of an additional \$1 billion of the Company's common stock, increasing the total amount of the Company's common stock the Company is authorized to repurchase from \$2 billion to \$3 billion. On June 6, 2007 the Board of Directors authorized the repurchase by the Company of an additional \$1 billion of the Company's common stock, increasing the total amount of the Company's common stock the Company is authorized to repurchase from \$3 billion to \$4 billion. Under the repurchase program, the Company may repurchase outstanding shares of its common stock from time to time in the open market and through privately

negotiated transactions. Unless terminated earlier by resolution of

20

Table of Contents

the Company's Board of Directors, the repurchase program will expire when the Company has repurchased all shares authorized under the program. The Company repurchased approximately 16.9 million shares for approximately \$631.7 million during the third quarter of fiscal 2007. As of August 4, 2007 the Company had repurchased a total of approximately 86.4 million shares of its common stock for approximately \$3.0 billion under this program. The repurchased shares are held as authorized but unissued shares of common stock.

Note 12 Related Party Transactions

One of the Company's directors, who has served on the Company's Board of Directors since 1988, became a director of Taiwan Semiconductor Manufacturing Company, or TSMC, in fiscal 2002 and continues to serve as a director of TSMC. Management believes the terms and prices for the purchases of products from TSMC are not affected by the presence of one of the Company's directors on the Board of Directors of TSMC. The Company purchased approximately \$72 million and \$76 million of products from TSMC during the three-month periods ended August 4, 2007 and July 29, 2006, respectively, and approximately \$224 million and \$217 million during the nine-month periods ended August 4, 2007 and July 29, 2006, respectively. Approximately \$34 million and \$17 million was payable to TSMC as of August 4, 2007 and October 28, 2006, respectively. Management anticipates that it will make significant purchases from TSMC in the remaining quarter of fiscal year 2007.

Note 13 New Accounting Standards*Accounting for Financial Assets and Financial Liabilities*

In February 2007, the FASB, issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company is currently evaluating the impact, if any, that SFAS 159 may have on the Company's financial condition, results of operations or liquidity.

Accounting for Prior Year Misstatements

In September 2006, the SEC issued Staff Accounting Bulletin (SAB) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108). This SAB provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 establishes an approach that requires quantification of financial statement errors based on the effects on each of the company's balance sheet and statement of operations and the related financial statement disclosures. SAB 108 permits existing public companies to record the cumulative effect of initially applying this approach in the first year ending after November 15, 2006 by recording the necessary correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings. Additionally, the use of the cumulative effect transition method requires detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose. The adoption of SAB 108 in the first quarter of fiscal 2007 did not have any impact on the Company's financial statements.

Accounting for Defined Benefit Pension and Other Postretirement Plans

In September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - An Amendment of FASB Statements No. 87, 88, 106, and 132R* (SFAS 158). SFAS 158 requires companies to recognize the funded status of pension and other postretirement benefit plans on sponsoring employers balance sheets and to recognize changes in the funded status in the year the changes occur. It also requires the measurement date of plan assets and obligations to occur at the end of the employers' fiscal year. SFAS 158 is effective for the Company at the end of fiscal 2007, except for the change in measurement date, which is effective for the Company in fiscal 2008. The effect on the Company's financial statements is dependent upon the discount rate at the Company's fiscal 2007 measurement date (September 30, 2007) and actual returns on the Company's pension plan assets during the year. The Company is currently evaluating the impact, if any, that SFAS 158 may have on the Company's financial conditions, results of operations or liquidity.

Table of Contents

Accounting for Uncertainty in Income Taxes

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact, if any, that FIN 48 may have on the Company's financial condition or results of operations.

Note 14 Income Taxes

The Company's income tax payable at August 4, 2007 was approximately \$129.3 million, which included approximately \$121.4 million for current U.S. federal, state and foreign tax filings. The remaining \$7.9 million of income tax payable is for various other income taxes.

During fiscal year 2006, the United States Internal Revenue Service (IRS) invited the Company to participate in the Compliance Assurance Process (CAP) which is a voluntary pilot program the IRS is conducting for a limited number of large business taxpayers. The objective of CAP is to reduce taxpayer burden associated with IRS audits while assuring the IRS of the accuracy of tax returns prior to filing. The Company has agreed to participate in CAP for fiscal 2006 and fiscal 2007. Under the program, the IRS will contemporaneously work with the Company to achieve federal tax compliance and resolve issues prior to the filing of a tax return. CAP is designed to eliminate or substantially reduce the need for post-filing examinations of future tax returns. The routine audit of fiscal years 2004 and 2005 is currently underway.

Note 15 Maxim Litigation Settlement

The Company executed a legal settlement with Maxim Integrated Products, Inc. (Maxim) during the second quarter of fiscal 2007, which resulted in the Company receiving \$19 million. The Company recorded \$8.5 million as a credit to legal expense in selling, marketing, general and administrative expense based on management's conclusion that this amount represents the fair value of external legal costs incurred by the Company in this matter. The remaining \$10.5 million has been recorded in other income because the amount was not related to the reimbursement of external legal costs and management deems it to be an isolated event. This amount is earned in full because the Company has no future obligation to Maxim with respect to this payment.

Note 16 Subsequent Event

On August 20, 2007, the Company's Board of Directors declared a cash dividend of \$0.18 per outstanding share of common stock. The dividend will be paid on September 19, 2007 to all shareholders of record at the close of business on August 31, 2007.

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

This information should be read in conjunction with the unaudited condensed consolidated financial statements and related notes included in Item 1 of this Quarterly Report on Form 10-Q and the audited consolidated financial statements and related notes and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended October 28, 2006.

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements regarding future events and our future results that are subject to the safe harbors created under the Securities Act of 1933 (the Securities Act) and the Securities Exchange Act of 1934 (the Exchange Act). These statements are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as expects, anticipates, targets, goals, projects, intends, plans, believes, seeks, estimates, continues, may, variations of such words and similar are intended to identify such forward-looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characterizations of future events or circumstances are forward-looking statements. Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict, including those identified in Part II, Item 1A. Risk Factors and elsewhere in our Quarterly Report on Form 10-Q. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update any forward-looking statements for any reason.

Results of Operations

(all tabular amounts in thousands except per share amounts and percentages)

Overview

| | Three Months Ended | | Nine Months Ended | |
|------------------------------------|--------------------|---------------|-------------------|---------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Total Revenue | \$680,312 | \$663,660 | \$2,041,058 | \$1,928,834 |
| Gross Margin % | 57.1% | 58.8% | 58.2% | 58.7% |
| Net Income | \$120,435 | \$144,685 | \$ 399,018 | \$ 411,063 |
| Net Income as a % of Total Revenue | 17.7% | 21.8% | 19.5% | 21.3% |
| Diluted EPS | \$ 0.37 | \$ 0.39 | \$ 1.18 | \$ 1.09 |

Fiscal 2007 is a 53-week year and fiscal 2006 was a 52-week year. The additional week in fiscal 2007 was included in the first quarter ended February 3, 2007. Therefore, the first nine months of fiscal 2007 included an additional week of operations as compared to the first nine months of fiscal 2006.

Revenue

Revenue in the third quarter of fiscal 2007 increased by \$16.7 million, or 3%, from the amount recorded in the third quarter of fiscal 2006. This increase by end market and by product category is outlined below under *Revenue Trends by End Market* and *Revenue Trends by Product*. Revenue increased by \$112.2 million, or 6%, in the nine months ended August 4, 2007 from the comparable period in fiscal 2006. This was primarily the result of an additional week of operations in the first quarter of fiscal 2007 as compared to fiscal 2006 and \$35 million in revenue we recorded in the first quarter of fiscal 2007 in exchange for the licensing of certain intellectual property rights.

Table of Contents*Revenue Trends by End Market*

The categorization of revenue by end market is determined using a variety of data points including the technical characteristics of the product, the sold to customer information, the ship to customer information and the end customer product or application into which our product will be incorporated. As data systems for capturing and tracking this data evolve and improve, the categorization of products by end market can vary over time. When this occurs, we reclassify revenue by end market for prior periods. Such reclassifications typically do not materially change the sizing of, or the underlying trends of results within, each end market.

| | Three Months Ended August 4, 2007 | | | Three Months Ended July 29, 2006 | |
|------------------------------|--------------------------------------|-------------------------------------|-----------|-------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y% | Revenue | % of Total Product Revenue |
| Industrial | \$ 293,557 | 43% | 3% | \$ 285,334 | 43% |
| Communications | 191,082 | 28% | (4%) | 198,414 | 30% |
| Consumer | 136,577 | 20% | 24% | 110,270 | 17% |
| Computer | 59,096 | 9% | (15%) | 69,642 | 10% |
| Total Product Revenue | \$ 680,312 | 100% | 3% | \$ 663,660 | 100% |

| | Nine Months Ended August 4, 2007 | | | Nine Months Ended July 29, 2006 | |
|------------------------------|-------------------------------------|-------------------------------------|-----------|------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y% | Revenue | % of Total Product Revenue |
| Industrial | \$ 880,827 | 44% | 8% | \$ 818,728 | 43% |
| Communications | 550,960 | 27% | (5%) | 578,512 | 30% |
| Consumer | 398,597 | 20% | 27% | 314,412 | 16% |
| Computer | 175,674 | 9% | (19%) | 217,182 | 11% |
| Total Product Revenue | \$ 2,006,058 | 100% | 4% | \$ 1,928,834 | 100% |

One-time payment associated with the licensing of IP*

35,000

Total Revenue **\$ 2,041,058** **\$ 1,928,834**

* During the first quarter of fiscal 2007, we recorded revenue of \$35 million received in

exchange for
licensing of
certain
intellectual
property rights
to a third party.

Industrial The year-to-year increases in both the three- and nine-month periods were primarily the result of revenue growth in products sold into the automotive area of the industrial end market. The year-to-year increase in the nine-month period was also attributable to an increase in sales to the instrumentation portion of this end market.

Communications The year-to-year decreases in both the three- and nine-month periods were a result of a decline in handset chipsets sales as compared to the same periods of fiscal 2006. These decreases were partially offset by an increase in revenue from the wireless basestation end market. The year-to-year decrease in the nine-month period was also attributable to the loss of revenue from our DSP-based DSL ASIC and network processor product line that we sold in the second quarter of fiscal 2006.

Consumer The year-to-year increases in both the three- and nine-month periods were primarily the result of increased sales of our products into digital home applications, including advanced television systems and video game applications, during fiscal 2007.

Table of Contents

Computer The year-to-year decreases in both the three- and nine-month periods were partially the result of refocusing our power management portfolio toward portable devices and partially attributable to an overall weak personal computer market in fiscal 2007.

Intellectual Property Revenue During the first quarter of fiscal 2007 we recorded revenue of \$35 million received in exchange for licensing of certain intellectual property rights to a third party.

Revenue Trends by Product

The following table summarizes revenue by product categories. The categorization of our products into broad categories is based on the characteristics of the individual products, the specification of the products and in some cases the specific uses that certain products have within applications. The categorization of products into categories is therefore subject to judgment in some cases and can vary over time. In instances where products move between product categories we reclassify the amounts in the product categories for all prior periods. Such reclassifications typically do not materially change the sizing of, or the underlying trends of results within, each product category.

| | Three Months Ended August 4, 2007 | | | Three Months Ended July 29, 2006 | |
|------------------------------|--------------------------------------|-------------------------------------|--------------|-------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y % | Revenue | % of Total Product Revenue |
| Converters | \$ 281,530 | 41% | 5% | \$ 268,949 | 41% |
| Amplifiers | 144,103 | 21% | 4% | 138,634 | 21% |
| Power management & reference | 50,019 | 7% | (8%) | 54,661 | 8% |
| Other analog | 98,020 | 15% | 34% | 73,102 | 11% |
| Total analog products | \$ 573,672 | 84% | 7% | \$ 535,346 | 81% |
| General purpose DSP | 52,891 | 8% | (1%) | 53,187 | 8% |
| Wireless Chipsets | 45,030 | 7% | (33%) | 66,975 | 10% |
| Other DSP | 8,719 | 1% | 7% | 8,152 | 1% |
| Total DSP products | \$ 106,640 | 16% | (17%) | \$ 128,314 | 19% |
| Total Product Revenue | \$ 680,312 | 100% | 3% | \$ 663,660 | 100% |

| | Nine Months Ended August 4, 2007 | | | Nine Months Ended July 29, 2006 | |
|------------------------------|-------------------------------------|-------------------------------------|-----------|------------------------------------|-------------------------------------|
| | Revenue | % of Total Product Revenue | Y/Y % | Revenue | % of Total Product Revenue |
| Converters | \$ 819,850 | 41% | 8% | \$ 758,438 | 39% |
| Amplifiers | 419,018 | 21% | 7% | 390,982 | 20% |
| Power management & reference | 148,278 | 7% | (10%) | 163,957 | 9% |
| Other analog | 289,995 | 15% | 32% | 219,930 | 11% |
| Total analog products | \$ 1,677,141 | 84% | 9% | \$ 1,533,307 | 79% |
| General purpose DSP | 158,038 | 8% | 5% | 150,511 | 8% |

Edgar Filing: ANALOG DEVICES INC - Form 10-Q

| | | | | | |
|--|---------------------|-------------|--------------|---------------------|-------------|
| Wireless Chipsets | 147,337 | 7% | (27%) | 201,895 | 11% |
| Other DSP | 23,542 | 1% | (45%) | 43,121 | 2% |
| Total DSP products | \$ 328,917 | 16% | (17%) | \$ 395,527 | 21% |
| Total Product Revenue | \$ 2,006,058 | 100% | 4% | \$ 1,928,834 | 100% |
| One-time payment associated with the licensing of IP* | 35,000 | | | | |
| Total Revenue | \$ 2,041,058 | | | \$ 1,928,834 | |

* During the first quarter of fiscal 2007, we recorded revenue of \$35 million received in exchange for licensing of certain intellectual property rights to a third party.

Table of Contents

The significant changes in our revenue trends by product type in the three- and nine-month periods of fiscal 2007 as compared to the same periods of fiscal 2006 were the year-to-year increase in our other analog product category, primarily as a result of increased sales of products used in video game applications and a decline in products used in wireless chipsets, which is a function of the significant volatility in demand for products in the wireless chipset category. The power management and reference product category was lower in the three- and nine-month periods of fiscal 2007 as compared to fiscal 2006 partially as a result of refocusing our power management portfolio towards portable devices and partially attributable to an overall weak personal computer market in fiscal 2007. The year-to-year decline in sales for the nine-month period of fiscal 2007 as compared to the same period of fiscal 2006 in the other DSP product category was primarily attributable to the loss of revenue from our DSP-based DSL ASIC and network processor product line that we sold in the second quarter of fiscal 2006.

Revenue Trends by Geographic Region

Product revenue by geographic region, based upon point of sale, for the three- and nine-month periods ended August 4, 2007 and July 29, 2006 are as follows:

| Region | Three Months Ended | | Nine Months Ended | |
|------------------------------|--------------------|-------------------|---------------------|---------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| United States | \$ 155,839 | \$ 164,842 | \$ 487,425 | \$ 487,103 |
| Europe | 154,252 | 148,721 | 452,733 | 422,749 |
| Japan | 130,100 | 123,169 | 385,677 | 360,501 |
| China | 109,546 | 90,178 | 288,136 | 256,773 |
| Rest of Asia | 130,575 | 136,750 | 392,087 | 401,708 |
| Total Product Revenue | \$ 680,312 | \$ 663,660 | \$ 2,006,058 | \$ 1,928,834 |

Gross Margin

| | Three Months Ended | | Nine Months Ended | |
|----------------|--------------------|---------------|-------------------|---------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Gross Margin | \$ 388,585 | \$ 390,110 | \$ 1,187,243 | \$ 1,131,568 |
| Gross Margin % | 57.1% | 58.8% | 58.2% | 58.7% |

Gross margin percentage decreased 170 basis points in the third quarter of fiscal 2007 compared to the third quarter of fiscal 2006. This decrease in gross margin percentage was primarily the result of higher sales in the third quarter of fiscal 2007 of products used in consumer electronics, which currently earn relatively lower gross margins than our average products. Gross margin percentage was lower by 50 basis points in the nine months ended August 4, 2007 as compared to the same period of fiscal 2006, as the higher sales of our lower margin consumer products during the first nine months of fiscal 2007 was partially offset by the \$35 million in revenue recorded in the first quarter of fiscal 2007 in exchange for licensing of certain intellectual property rights to a third party with no associated cost of sales.

Stock-Based Compensation Expense

During the first quarter of fiscal 2006, on October 30, 2005, we adopted the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment*, or SFAS 123R, using the modified prospective application method. Compensation cost is calculated on the date of grant using the fair value of the options as calculated using the Black-Scholes valuation model. The Black-Scholes valuation model requires us to make several assumptions. One of the key assumptions is expected volatility. For options granted prior to fiscal 2005, we used historical volatility to estimate the grant-date fair value of stock options. We changed our method of estimating expected volatility for all stock options granted after fiscal 2004 from exclusively relying on historical volatility to exclusively relying on implied volatility. This change was the result of a thorough review we undertook that included consultations with several third-party advisors. We currently believe that the exclusive use of implied

volatility results in a more accurate estimate of the grant-date fair value of employee stock options because it more appropriately reflects the market's expectations of future volatility. Historical volatility during the period commensurate with the expected term of our stock options over the past

Table of Contents

several years included a period of time during which our stock price experienced unprecedented increases and subsequent declines. We believe that this past stock price volatility is unlikely to be indicative of future stock price behavior.

In the third quarter of fiscal 2007, we recognized \$17.2 million of stock-based compensation expense, or 2.5% of product revenue, as a result of the adoption of SFAS 123R. The adoption of SFAS 123R reduced diluted EPS for the third quarter of fiscal 2007 by \$0.04. For the nine months ended August 4, 2007, we recognized \$54.5 million of stock-based compensation expense, or 2.7% of product revenue, as a result of the adoption of SFAS 123R. The adoption of SFAS 123R reduced diluted EPS for the nine-month period ended August 4, 2007 by \$0.12. We expect that stock-based compensation related to our adoption of SFAS 123R will reduce diluted EPS by approximately \$0.04 in the fourth quarter of fiscal 2007.

As of August 4, 2007, the total compensation cost related to unvested awards not yet recognized in the statement of income was approximately \$163.9 million (before tax consideration), which we expect to recognize over a weighted-average period of 1.8 years.

See Note 2 to our Consolidated Financial Statements contained in Item 1 of this Quarterly Report on Form 10-Q for further information regarding our adoption of SFAS 123R.

Research and Development

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|----------------------|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| R&D Expenses | \$148,562 | \$136,061 | \$439,142 | \$399,197 |
| R&D Expenses as a % of Product Revenue | 21.8% | 20.5% | 21.9% | 20.7% |

Research and development, or R&D, expenses increased \$12.5 million, or 9%, in the third quarter of fiscal 2007 as compared to the third quarter of fiscal 2006. This increase was primarily the result of higher employee salary and benefit expense primarily as a result of an increase in our employee population and was partially offset by lower employee bonus expense.

R&D expenses increased \$39.9 million, or 10%, in the first nine months of fiscal 2007 as compared to the first nine months of fiscal 2006. This increase was primarily the result of the extra week of operations in the first quarter of fiscal 2007. In addition, salary and benefit expense was higher in the first nine months of fiscal 2007 compared to the same period of fiscal 2006 primarily as a result of an increase in our employee population. These increases were partially offset by lower employee bonus expense during the first nine months of fiscal 2007 as compared to the same period of fiscal 2006.

R&D expenses as a percentage of product revenue will fluctuate from quarter to quarter depending on the amount of product revenue and the success of new product development efforts, which we view as critical to our future growth. At any point in time we have hundreds of R&D projects underway, and we believe that none of these projects is material on an individual basis. We expect to continue the development of innovative technologies and processes for new products, and we believe that a continued commitment to R&D is essential in order to maintain product leadership with our existing products and to provide innovative new product offerings. Therefore, we are planning to continue to make significant R&D investments in the future.

Selling, Marketing, General and Administrative

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|--------------------------|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| SMG&A Expenses | \$102,379 | \$99,663 | \$300,105 | \$293,376 |
| SMG&A Expenses as a % of Product Revenue | 15.0% | 15.0% | 14.9% | 15.2% |

Selling, marketing, general and administrative, or SMG&A, expenses increased \$2.7 million, or 3%, in the third quarter of fiscal 2007 as compared to the third quarter of fiscal 2006. This increase was primarily the result of higher

employee salary and benefit expense partially offset by lower employee bonus expense. SMG&A expenses increased \$6.7 million, or 2%, in the first nine months of fiscal 2007 as compared to the comparable period of fiscal 2006. This increase was primarily the result of the extra week of operations in the first quarter of fiscal 2007 and

Table of Contents

higher employee salary and benefit expense, partially offset by lower employee bonus expense and the \$8.5 million related to the reimbursement of legal expenses we received as a result of the settlement of litigation in the second quarter of fiscal 2007.

Purchased In-process Research and Development

In the third quarter of fiscal 2006, we incurred a charge of \$5.5 million for the write-off of in-process research and development in connection with the acquisition of certain intellectual property assets of TTPCom Limited.

*Special Charges**Closure of Wafer Fabrication Facility*

During the fourth quarter of fiscal 2005, we recorded a special charge of \$20.3 million as a result of a decision to close our California wafer fabrication operations and transfer virtually all of the production of products manufactured there to our facility in Wilmington, Massachusetts. The charge was for severance and fringe benefit costs that were recorded pursuant to SFAS 88, *Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits*, or SFAS 88, under our ongoing benefit plan for 339 manufacturing employees and 28 general and administrative employees. The severance benefit was calculated based on length of past service, and employees had to continue to be employed until they were involuntarily terminated in order to receive the severance benefit. We completed the remaining cleanup and closure activities during the second quarter of fiscal 2007. We terminated the employment of all of the employees included in this action.

In addition to the charge recorded in the fourth quarter of fiscal 2005, we recorded additional expense during fiscal 2006, which consisted of \$18.3 million of non-cash cost of sales expenses for additional depreciation due to shortened useful lives of certain manufacturing equipment and \$2.0 million for stay-on bonuses. We reversed approximately \$2.0 million of our severance accrual during fiscal 2006 because some employees voluntarily left the company, other employees found alternative employment within the company, and there was an over accrual related to fringe benefits because severance payments, normally paid as income continuance, were paid as lump sum payments, which reduced the benefit costs associated with these payments.

We ceased production at the wafer fabrication facility on November 9, 2006. During the first quarter of fiscal 2007, we recorded additional expense, in accordance with SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities*, which consisted of \$3.2 million for clean-up and closure costs that were charged to expense as incurred and \$0.4 million for lease obligation costs for a warehouse facility we ceased using during the first quarter of fiscal 2007. During the second quarter of fiscal 2007, we recorded a special charge, in accordance with SFAS 146, which included \$5.0 million of expense for future lease obligation costs for the wafer fabrication facility that we ceased using during the second quarter of fiscal 2007. Also included in this special charge was \$1.7 million for clean-up and closure costs that were charged to expense as incurred. The clean-up activity was completed during the second quarter of fiscal 2007, and we do not expect to incur any additional expenses related to this action.

The closure of this facility has resulted in annual cost savings of approximately \$50 million per year beginning in fiscal 2007. These annual savings include: approximately \$49 million in cost of sales, of which approximately \$7 million relates to non-cash depreciation savings, and approximately \$1 million in SMG&A expenses. At current demand levels, if this facility were still in operation, the capacity of the facility would be largely underutilized resulting in significant adverse variances associated with the under utilization of our wafer fabrication facilities.

Reorganization of Product Development and Support Programs

During the fourth quarter of fiscal 2005, we recorded a special charge of \$11.2 million as a result of our decision to reorganize our product development and support programs with the goal of providing greater focus on our analog and digital signal processing product programs. The charge was for severance and fringe benefit costs that were recorded pursuant to SFAS 88 under our ongoing benefit plan or statutory requirements at foreign locations for 60 manufacturing employees and 154 engineering and selling, marketing, general and administrative employees.

During fiscal 2006, we recorded an additional special charge of \$3.8 million related to this reorganization action. Approximately \$1.5 million of this charge was for lease obligation costs for a facility we ceased using during the first quarter of fiscal 2006 and the write-off of property, plant and equipment and other items. The remaining \$2.3 million relates to the

Table of Contents

severance and fringe benefit costs that were recorded in the fourth quarter of fiscal 2006 pursuant to SFAS 88 under our ongoing benefit plan or statutory requirements at foreign locations for 46 engineering and selling, marketing, general and administrative employees.

During the first quarter of fiscal 2007, we recorded an additional special charge of \$1.6 million related to this reorganization action. Approximately \$0.6 million of this charge was for contract termination costs. The remaining \$1.0 million relates to severance and fringe benefit costs that were recorded in the first quarter pursuant to SFAS 88 under our ongoing benefit plan for six engineering employees.

During the second quarter of fiscal 2007, we recorded an additional special charge of \$3.4 million related to this reorganization action. Approximately \$3.2 million relates to the severance and fringe benefit costs that were recorded in the second quarter pursuant to SFAS 88 under our ongoing benefit plan or minimum statutory requirements at foreign locations for 20 engineering and selling, marketing, general and administrative employees. The remaining \$0.2 million of this charge was for lease obligation costs for a facility we ceased using during the second quarter of fiscal 2007.

As of August 4, 2007, eight of the 286 employees included in this reorganization action were still employed by us. These employees must continue to be employed until they are involuntarily terminated in order to receive the severance benefit.

We do not expect to incur any further material charges related to this reorganization action. These organizational changes are expected to result in savings of approximately \$30 million per year once fully completed in the fourth quarter of fiscal 2007. These savings are expected to be realized as follows: approximately \$17 million in R&D expenses, approximately \$10 million in SMG&A expenses and approximately \$3 million in cost of sales. A portion of these savings associated with these charges are reflected in our current results.

Operating Income

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|----------------------|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Operating Income | \$137,644 | \$148,886 | \$432,684 | \$432,482 |
| Operating Income as a % of Total Revenue | 20.2% | 22.4% | 21.2% | 22.4% |

The \$11.2 million decrease in operating income in the third quarter of fiscal 2007 as compared to the third quarter of fiscal 2006 was the result of a 1.7% decrease in the gross margin percentage and increases in other operating expenses of approximately \$9.7 million, which were partially offset by a \$16.7 million increase in revenue. The increases in other operating expenses are more fully described above under the headings *Research and Development* and *Selling, Marketing, General and Administrative and Purchased In-process Research and Development*.

Operating income was relatively flat in the first nine months of fiscal 2007 as compared to the same period of fiscal 2006. A \$112.2 million increase in revenue was offset by a 0.5% reduction in gross margin percentage and a \$55.5 million increase in operating expenses as more fully described above under the headings *Research and Development* and *Selling, Marketing, General and Administrative, Special Charges and Purchased In-process Research and Development*.

Nonoperating (Income) Expense

| | Three Months Ended | | Nine Months Ended | |
|-------------------------------|---------------------------|--------------------------|---------------------------|--------------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Interest expense | \$ | \$ 4 | \$ | \$ 35 |
| Interest income | (17,721) | (26,716) | (63,429) | (75,868) |
| Other (income) / expense, net | 1,272 | 435 | (16,414) | (10,261) |
| Total nonoperating income | \$ (16,449) | \$ (26,277) | \$ (79,843) | \$ (86,094) |

Nonoperating income decreased by \$9.8 million in the third quarter of fiscal 2007 as compared to the same period in the prior fiscal year as a result of lower invested cash balances, which was partially offset by higher interest rates in the third quarter of fiscal 2007 as compared to the third quarter of fiscal 2006.

Table of Contents

The \$6.3 million decrease in nonoperating income in the first nine months of fiscal 2007 as compared to the same period in the prior fiscal year was a result of lower invested cash balances that were partially offset by the higher interest rates in the first nine months of fiscal 2007 as compared to the same period of fiscal 2006. This decrease in interest income was partially offset by a \$7.9 million gain from the sale of an investment in the first quarter of fiscal 2007 and a \$10.5 million settlement we received in the second quarter of fiscal 2007. We recognized a \$13.0 million gain on the sale of a product line in the second quarter of fiscal 2006.

Provision for Income Taxes

| | Three Months Ended | | Nine Months Ended | |
|----------------------------|---------------------------|--------------------------|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Provision for Income Taxes | \$33,658 | \$30,478 | \$113,728 | \$107,513 |
| Effective Income Tax Rate | 21.8% | 17.4% | 22.2% | 20.7% |

Our effective tax rate reflects the applicable tax rates in effect in the various tax jurisdictions around the world where our income is earned.

Our effective tax rate for the third quarter of fiscal 2007 was higher by 440 basis points as compared to the same period in the prior fiscal year. The fiscal 2006 tax rate was lower primarily as a result of a one-time tax benefit of \$8.5 million associated with an IRS settlement which we recorded in the third quarter of fiscal 2006.

Our effective tax rate for the first nine months of fiscal 2007 was higher by 150 basis points as compared to the first nine months of fiscal 2006. The increase was primarily due to the higher tax rate on the following fiscal 2007 transactions: the one-time receipt of \$35 million associated with the licensing of intellectual property to a third party, the gain on the sale of an investment of \$7.9 million and the \$19 million received from the settlement of litigation. These items were partially offset by a one time tax benefit of \$8.5 million associated with the settlement of the IRS examination during the third quarter of fiscal 2006, a tax benefit from the reinstatement of the U.S. federal research and development tax credit in fiscal 2007 and a \$9.9 million cumulative adjustment recorded in fiscal 2007 related to the application of this credit to a portion of our fiscal 2006 results.

Net Income

| | Three Months Ended | | Nine Months Ended | |
|------------------------------------|---------------------------|----------------------|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 | August 4, 2007 | July 29, 2006 |
| Net Income | \$120,435 | \$144,685 | \$399,018 | \$411,063 |
| Net Income as a % of Total Revenue | 17.7% | 21.8% | 19.5% | 21.3% |
| Diluted EPS | \$ 0.37 | \$ 0.39 | \$ 1.18 | \$ 1.09 |

Net income in the third quarter of fiscal 2007 was lower than in the third quarter of fiscal 2006 by approximately \$24.3 million primarily as a result of the \$11.2 million decrease in operating income, the \$9.8 million decrease in nonoperating income and a higher provision for income taxes in fiscal 2007.

In the nine-month period ended August 4, 2007, net income was lower than in the same period of the prior year by approximately \$12.0 million primarily as a result of the \$6.3 million decrease in nonoperating income and a higher provision for income taxes in fiscal 2007.

Table of Contents*Related Party Transactions*

One of our directors, who has served on our Board of Directors since 1988, became a director of Taiwan Semiconductor Manufacturing Company, or TSMC, in fiscal 2002 and continues to serve as a director of TSMC. Management believes the terms and prices for the purchases of products from TSMC are not affected by the presence of one of our directors on the Board of Directors of TSMC. We purchased approximately \$72 million and \$76 million of products from TSMC during the three-month periods ended August 4, 2007 and July 29, 2006, respectively, and approximately \$224 million and \$217 million during the nine-month periods ended August 4, 2007 and July 29, 2006, respectively. Approximately \$34 million and \$17 million was payable to TSMC as of August 4, 2007 and October 28, 2006, respectively. Management anticipates that we will make significant purchases from TSMC in the remainder of fiscal year 2007.

Outlook

We are planning for revenues for the fourth quarter of fiscal 2007 to be in the range of \$680 million to \$710 million. We are also planning for our gross margin percentage for the fourth quarter of fiscal 2007 to be approximately flat to the third quarter of fiscal 2007. Operating expenses are planned to be flat or slightly higher in the fourth quarter of fiscal 2007 as a result of our plan to continue increasing R&D spending on new analog products while reducing spending in other product areas. Diluted EPS for the fourth quarter of fiscal 2007 is planned to be in the range of \$0.36 to \$0.40. This estimate of diluted EPS includes approximately \$0.05 per share related to stock-based compensation expense and previously announced acquisition-related expenses.

Liquidity and Capital Resources

| | Nine Months Ended | |
|---|---------------------------|----------------------|
| | August 4, 2007 | July 29, 2006 |
| Net Cash Provided by Operations | \$637,515 | \$454,367 |
| Net Cash Provided by Operations as a % of Total Revenue | 31.2% | 23.6% |

At August 4, 2007, cash, cash equivalents and short-term investments totaled \$1,283.6 million, a decrease of \$844.7 million from the fourth quarter of fiscal 2006. The primary sources of funds for the first nine months of fiscal 2007 were net cash generated from operating activities of \$637.5 million and proceeds of \$96.2 million from our various employee stock plans. The principal uses of funds for the first nine months of fiscal 2007 were the repurchase of approximately 37.3 million shares of our common stock for an aggregate of \$1,329.5 million, dividend payments of \$172.8 million and capital expenditures of \$108.6 million.

| | August 4, 2007 | October 28, 2006 |
|---------------------------------|---------------------------|-----------------------------|
| Accounts Receivable | \$ 350,868 | \$ 329,393 |
| Days Sales Outstanding | 47 | 47 |
| Inventory | \$ 371,773 | \$ 378,651 |
| Days Cost of Sales in Inventory | 116 | 128 |

Accounts receivable at August 4, 2007 increased \$21.5 million, or 7%, from the end of the fourth quarter of fiscal 2006. The increase in receivables was primarily related to the higher shipment rate in the last month of the third quarter of fiscal 2007 as compared to the fourth quarter of fiscal 2006.

Inventory at August 4, 2007 decreased by \$6.9 million, or 2%, from the end of fiscal 2006. The decrease in inventory was primarily caused by our continuing effort to balance production, demand and inventory levels.

Net additions to property, plant and equipment were \$108.6 million in the first nine months of fiscal 2007 and were funded with a combination of cash on hand and cash generated from operations. Capital expenditures are expected to be approximately \$152 million in fiscal 2007.

Table of Contents

On August 20, 2007, our Board of Directors declared a cash dividend of \$0.18 per outstanding share of our common stock. The dividend is payable on September 19, 2007 to shareholders of record on August 31, 2007 and is expected to be approximately \$56 million in the aggregate. The payment of future dividends will be based on several factors including our financial performance, outlook and liquidity. Quarterly dividends are expected to continue at \$0.18 per share, although they remain subject to declaration or change by our Board of Directors.

At August 4, 2007, our principal source of liquidity was \$1,283.6 million of cash and cash equivalents and short-term investments. We believe that our existing sources of liquidity and cash expected to be generated from future operations, together with anticipated available long-term financing, will be sufficient to fund operations, capital expenditures, research and development efforts, dividend payments (if any) and purchases of stock (if any) under our stock repurchase program for at least the next twelve months and thereafter for the foreseeable future.

New Accounting Pronouncements*Accounting for Financial Assets and Financial Liabilities*

In February 2007, the Financial Accounting Standards Board (FASB), issued Statement of Financial Accounting Standard (SFAS) 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. We are currently evaluating the impact, if any, that SFAS 159 may have on our financial condition, results of operations or liquidity.

Accounting for Prior Year Misstatements

In September 2006, the United States Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108). This SAB provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 establishes an approach that requires quantification of financial statement errors based on the effects on each of the company's balance sheet and statement of operations and the related financial statement disclosures. SAB 108 permits existing public companies to record the cumulative effect of initially applying this approach in the first year ending after November 15, 2006 by recording the necessary correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings. Additionally, the use of the cumulative effect transition method requires detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose. The adoption of SAB 108 in the first quarter of fiscal 2007 did not have any impact on our financial statements.

Accounting for Defined Benefit Pension and Other Postretirement Plans

In September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - An Amendment of FASB Statements No. 87, 88, 106, and 132R* (SFAS 158). SFAS 158 requires companies to recognize the funded status of pension and other postretirement benefit plans on sponsoring employers' balance sheets and to recognize changes in the funded status in the year the changes occur. It also requires the measurement date of plan assets and obligations to occur at the end of the employers' fiscal year. SFAS 158 is effective for us at the end of fiscal 2007, except for the change in measurement date, which is effective for us in fiscal 2008. The effect on our financial statements is dependent upon the discount rate at our fiscal 2007 measurement date (September 30, 2007) and actual returns on our pension plan assets during the year. We are currently evaluating the impact, if any, that SFAS 158 may have on our financial condition, results of operations or liquidity.

Accounting for Uncertainty in Income Taxes

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition

Table of Contents

threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently evaluating the impact, if any, that FIN 48 may have on our financial condition or results of operations.

Critical Accounting Policies and Estimates

Management's discussion and analysis of the financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. We base our estimates and judgments on historical experience, knowledge of current conditions and beliefs of what could occur in the future given available information. We consider the following accounting policies to be both those most important to the portrayal of our financial condition and those that require the most subjective judgment. If actual results differ significantly from management's estimates and projections, there could be a material effect on our financial statements. We also have other policies that we consider key accounting policies, such as our policy for revenue recognition, including the deferral of revenue on sales to distributors until the products are sold to the end user; however, the application of these policies does not require us to make significant estimates or judgments that are difficult or subjective.

Inventory Valuation

Inventories are valued at the lower of cost (first-in, first-out method) or market. Because of the cyclical nature of the semiconductor industry, changes in inventory levels, obsolescence of technology, and product life cycles, we write down inventories to net realizable value. We employ a variety of methodologies to determine the amount of inventory reserves necessary. While a portion of the reserve is determined via reference to the age of inventory and lower of cost or market calculations, an element of the reserve is subject to significant judgments made by us about future demand for our inventory. If actual demand for our products is less than our estimates, additional reserves for existing inventories may need to be recorded in future periods.

Allowance for Doubtful Accounts

We maintain allowances for doubtful accounts, when appropriate, for estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our customers were to deteriorate, our actual losses may exceed our estimates, and additional allowances would be required.

Long-Lived Assets

We review property, plant, and equipment and identified intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value of assets may not be recoverable. Recoverability of these assets is measured by comparison of their carrying value to future undiscounted cash flows the assets are expected to generate over their remaining economic lives. If such assets are considered to be impaired, the impairment to be recognized in earnings equals the amount by which the carrying value of the assets exceeds their fair market value determined by either a quoted market price, if any, or a value determined by utilizing a discounted cash flow technique. Although we have recognized no material impairment adjustments related to our property, plant, and equipment and identified intangible assets during the past three fiscal years, except those made in conjunction with restructuring actions, deterioration in our business in the future could lead to such impairment adjustments in future periods. Evaluation of impairment of long-lived assets requires estimates of future operating results that are used in the preparation of the expected future undiscounted cash flows. Actual future operating results and the remaining economic lives of our long-lived assets could differ from the estimates used in assessing the recoverability of these assets. These differences could result in impairment charges, which could have a material adverse impact on our results of operations. In addition, in certain instances, assets may not be impaired but their estimated useful lives may have decreased. In these situations, we amortize the remaining net book values over the revised useful lives.

Table of Contents*Goodwill*

In accordance with SFAS 142, *Goodwill and Other Intangible Assets*, goodwill is subject to annual impairment tests, or earlier if indicators of potential impairment exist and suggest that the carrying value of goodwill may not be recoverable from estimated discounted future cash flows. Because we have one reporting segment under SFAS 142, we utilize the entity-wide approach to assess goodwill for impairment and compare our market value to our net book value to determine if an impairment exists. These impairment tests may result in impairment losses that could have a material adverse impact on our results of operations.

Accounting for Income Taxes

We account for income taxes in accordance with SFAS 109, *Accounting for Income Taxes*, which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. SFAS 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax asset will not be realized. We evaluate the realizability of our deferred tax assets quarterly. At August 4, 2007, we had gross deferred tax assets of \$209.2 million primarily resulting from temporary differences between the book and tax bases of assets and liabilities. We have conducted an assessment of the likelihood of realization of those deferred tax assets and concluded that a \$44 million valuation allowance is needed to reserve the amount of the deferred tax assets that may not be realized due to the expiration of certain state credit carryovers. In reaching our conclusion, we evaluated certain relevant criteria including the existence of deferred tax liabilities that can be used to absorb deferred tax assets, the taxable income in prior carryback years in the impacted state jurisdictions that can be used to absorb net operating losses and taxable income in future years. Our judgments regarding future profitability may change due to future market conditions, changes in U.S. or international tax laws and other factors. These changes, if any, may require material adjustments to these deferred tax assets, resulting in a reduction in net income or an increase in net loss in the period when such determinations are made.

In the ordinary course of global business, there are many transactions and calculations where the ultimate tax outcome is uncertain. Some of these uncertainties arise as a consequence of cost reimbursement and royalty arrangements among related entities. Although we believe our estimates are reasonable, no assurance can be given that the final tax outcome of these matters will not be different than that which is reflected in our historical income tax provisions and accruals. Such differences could have a material impact on our income tax provision and operating results in the period in which such determination is made.

Stock-Based Compensation

The adoption of SFAS 123R in the first quarter of fiscal 2006 requires that stock-based compensation expense associated with stock options and related awards be recognized in the statement of income, rather than being disclosed in a pro forma footnote to the consolidated financial statements. Determining the amount of stock-based compensation to be recorded requires us to develop estimates to be used in calculating the grant-date fair value of stock options. We calculate the grant-date fair values using the Black-Scholes valuation model. The use of valuation models requires us to make estimates of the following assumptions:

Expected volatility - We are responsible for estimating volatility and have considered a number of factors, including third-party estimates, when estimating volatility. For options granted prior to fiscal 2005, we used historical volatility to estimate the grant-date fair value of stock options. We changed our method of estimating expected volatility for all stock options granted after fiscal 2004 from exclusively relying on historical volatility to exclusively relying on implied volatility. This change was the result of a thorough review we undertook which included consultations with several third-party advisors. We currently believe that the exclusive use of implied volatility results in a more accurate estimate of the grant-date fair value of employee stock options because it more appropriately reflects the market's expectations of future volatility. Historical volatility during the period commensurate with the expected term of our stock options over the past several years included a period of time that our stock price experienced unprecedented increases and subsequent declines. We believe that this past stock price volatility is unlikely to be indicative of future stock price behavior. Options in our stock are actively traded on several exchanges. Implied volatility is calculated for the period that is commensurate with the option's expected term assumption. Because this term often exceeds the period for which there are exchange-traded options in our stock, statistical techniques are used to derive the implied

volatility for traded options with terms commensurate with the option's expected term of 5.1 years. This calculation of implied volatility is derived from the closing prices of our stock and exchange-traded

Table of Contents

options from the most recent five trading days prior to the grant date of the employee stock option. In general, the higher the expected volatility used in the Black-Scholes valuation model, the higher the grant-date fair value of the option.

Expected term - We use historical employee exercise and option expiration data to estimate the expected term assumption for the Black-Scholes grant-date valuation. We believe that this historical data is currently the best estimate of the expected term of a new option, and that generally, all of our employees exhibit similar exercise behavior. In general, the longer the expected term used in the Black-Scholes valuation model, the higher the grant-date fair value of the option.

Risk-free interest rate - The yield on zero-coupon U.S. Treasury securities for a period that is commensurate with the expected term assumption is used as the risk-free interest rate.

Expected dividend yield - Expected dividend yield is calculated by annualizing the cash dividend declared by our Board of Directors for the current quarter and dividing that result by the closing stock price on the date of grant of the option. Until such time as our Board of Directors declares a cash dividend for an amount that is different from the current quarter's cash dividend, the current dividend will be used in deriving this assumption. Cash dividends are not paid on options, restricted stock or restricted stock units.

The amount of stock-based compensation expense recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term "forfeitures" is distinct from "cancellations" or "expirations" and represents only the unvested portion of the surrendered option. Based on an analysis of our historical forfeitures, we have applied an annual forfeiture rate of 4.3% to all unvested stock-based awards as of August 4, 2007. The rate of 4.3% represents the portion that is expected to be forfeited each year over the vesting period. This analysis is re-evaluated quarterly and the forfeiture rate is adjusted as necessary. Ultimately, the actual expense recognized over the vesting period will only be for those awards that vest.

Contingencies

From time to time, we receive notices that our products or manufacturing processes may be infringing the patent or intellectual property rights of others. We periodically assess each matter to determine if a contingent liability should be recorded in accordance with SFAS 5, *Accounting for Contingencies*. In making this determination, we may, depending on the nature of the matter, consult with internal and external legal counsel and technical experts. Based on the information we obtain, combined with our judgment regarding all the facts and circumstances of each matter, we determine whether it is probable that a contingent loss may be incurred and whether the amount of such loss can be reasonably estimated. If a loss is probable and reasonably estimable, we record a contingent loss in accordance with SFAS 5. In determining the amount of a contingent loss, we consider advice received from experts in the specific matter, current status of legal proceedings, settlement negotiations that may be ongoing, prior case history and other factors. If the judgments and estimates made by us are incorrect, we may need to record additional contingent losses that could materially adversely impact our results of operations. See Note 10 to our Consolidated Financial Statements contained in Item 1 of this Quarterly Report on Form 10-Q for additional information regarding our commitments and contingencies.

Table of Contents**ITEM 3. Quantitative and Qualitative Disclosures About Market Risk**

In our Annual Report on Form 10-K for the year ended October 28, 2006 we disclosed that our annual interest income would change by approximately \$16 million in fiscal 2006 and \$16 million in fiscal 2005 for each 100 basis point increase or decrease in interest rates. We also disclosed that the fair values of our investment portfolio would change by approximately \$6 million in fiscal 2006 and \$14 million in fiscal 2005 for each 100 basis point increase or decrease in interest rates. Based on our lower levels of cash and short term investment balances as of August 4, 2007, our interest income over the next twelve months would change by approximately \$8 million and the fair value of our investment portfolio would change by approximately \$0.3 million for each 100 basis point increase or decrease in interest rates. There have been no other material changes in the information provided under Item 7A. Qualitative and Quantitative Disclosures about Market Risk set forth in our Annual Report on Form 10-K for the year ended October 28, 2006.

ITEM 4. Controls and Procedures

(a) *Evaluation of Disclosure Controls and Procedures.* Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of Analog's disclosure controls and procedures as of August 4, 2007. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of August 4, 2007, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) *Changes in Internal Control over Financial Reporting.* No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the quarter ended August 4, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION**ITEM 1. Legal Proceedings***Tentative Settlement of the SEC's Previously Announced Stock Option Investigation*

In our 2004 Form 10-K filing, we disclosed that the Securities and Exchange Commission (SEC) had initiated an inquiry into our stock option granting practices, focusing on options that were granted shortly before the issuance of favorable financial results. On November 15, 2005, we announced that we had reached a tentative settlement with the SEC.

At all times since receiving notice of this inquiry, we have cooperated with the SEC. In November 2005, we and our President and CEO, Mr. Jerald G. Fishman, made an offer of settlement to the Staff of the SEC. The settlement has been submitted to the Commission for approval. There can be no assurance a final settlement will be so approved. The SEC's inquiry focused on two separate issues. The first issue concerned our disclosure regarding grants of options to employees and directors prior to the release of favorable financial results. Specifically, the issue related to options granted to our employees (including officers) on November 30, 1999 and to our employees (including officers) and directors on November 10, 2000.

The second issue concerned the grant dates for options granted to employees (including officers) in 1998 and 1999, and the grant date for options granted to employees (including officers) and directors in 2001. Specifically, the settlement would conclude that the appropriate grant date for the September 4, 1998 options should have been September 8th (which is one

Table of Contents

trading day later than the date that was used to price the options); the appropriate grant date for the November 30, 1999 options should have been November 29th (which is one trading day earlier than the date that was used); and the appropriate grant date for the July 18, 2001 options should have been July 26th (which is five trading days after the original date).

In connection with the proposed settlement, we would consent to a cease-and-desist order under Section 10(b) of the Securities Exchange Act and Rule 10b-5 thereunder, would pay a civil money penalty of \$3 million, and would reprice options granted to Mr. Fishman in certain years. Options granted to all others would be excluded from the repricing. Mr. Fishman would consent to a cease-and-desist order under Sections 17(a)(2) and (3) of the Securities Act, would pay a civil money penalty of \$1 million, and would make a disgorgement payment with respect to options granted in certain years. With the exception of options granted in 1998, Mr. Fishman has not exercised or sold any of the options identified in this matter. We and Mr. Fishman would settle this matter without admitting or denying the Commission's findings.

We have determined that no restatement of our historical financial results would be necessary due to the proposed settlement.

Other Legal Proceedings

In May 2006, we received a document subpoena from the U.S. Attorney for the Southern District of New York requesting records from 2000 to the present relating to our granting of stock options. We believe that the options at issue in this matter are the same option grants which have been the subject of investigation by the SEC. We are cooperating with the office of the U.S. Attorney in connection with this subpoena. We cannot predict the outcome of this matter, but believe the disposition of the matter will not have a material adverse effect on us or our financial position.

On May 25, 2006, we filed a lawsuit in United States District Court for the District of Delaware against Linear Technology Corp. (LTC), alleging infringement of three of our patents by LTC's making, selling and using various products. In addition, we also sought a declaratory judgment that our products do not infringe eight patents allegedly owned by LTC (the LTC patents) and that the LTC patents are invalid. On July 28, 2006, LTC filed an answer and counterclaims, denying that its products infringe the asserted patents and asking the court to declare such patents invalid. LTC also claimed that we, by making, selling and using various power management products, are infringing seven of the eight LTC patents. LTC seeks damages in an unspecified amount and injunctive relief. On August 21, 2006, we filed our answer to LTC's counterclaims, denying all liability to LTC. The case is currently in the discovery phase and trial is scheduled to begin in June 2008. We intend to vigorously pursue our claims against LTC, and to vigorously defend against LTC's counterclaims. We are unable at this time to predict the outcome of this litigation; however, we believe that the final disposition of this matter will not have a material adverse effect on us or our financial position.

On October 13, 2006, a purported class action complaint was filed in the United States District Court for the District of Massachusetts on behalf of participants in our Investment Partnership Plan from October 5, 2000 to the present. The complaint named as defendants us, certain officers and directors, and our Investment Partnership Plan Administration Committee. The complaint alleges purported violations of federal law in connection with our option granting practices during the years 1998, 1999, 2000, and 2001, including breaches of fiduciary duties owed to participants and beneficiaries of our Investment Partnership Plan under the Employee Retirement Income Security Act. The complaint seeks unspecified monetary damages, as well as equitable and injunctive relief. We intend to vigorously defend against these allegations. On November 22, 2006, we and the individual defendants filed motions to dismiss the complaint. On January 8, 2007, the Plaintiff filed memoranda in opposition. On January 22, 2007, we and the individual defendants filed further memoranda in support of the motions to dismiss. Although we believe we have meritorious defenses to the asserted claims, we are unable at this time to predict the outcome of this proceeding.

Table of Contents

ITEM 1A. Risk Factors

Set forth below and elsewhere in this report and in other documents we file with the SEC are descriptions of the risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report. The description below includes any material changes to and supersedes the description of the risk factors affecting our business previously disclosed in Part I, Item 1A. Risk Factors of our Annual Report on Form 10-K for the fiscal year ended October 28, 2006 and Part II, Item 1A. Risk Factors of our Quarterly Report on Form 10-Q for the quarter ended May 5, 2007.

Our future revenue, gross margins and operating results are difficult to predict and may materially fluctuate.

Our future revenue, gross margins and operating results are difficult to predict and may be materially affected by a number of factors, including:

changes in customer demand for our products and for end products that incorporate our products;

the timing of new product announcements or introductions by us, our customers or our competitors;

competitive pricing pressures;

fluctuations in manufacturing yields, adequate availability of wafers and other raw materials, and manufacturing, assembly and test capacity;

the risk that our backlog could decline significantly;

the timing, delay or cancellation of significant customer orders and our ability to manage inventory;

our ability to hire, retain and motivate adequate numbers of engineers and other qualified employees to meet the demands of our customers;

changes in geographic, product or customer mix;

potential significant litigation-related costs;

the difficulties inherent in forecasting future operating expense levels;

the costs related to compliance with increasing worldwide environmental regulations;

changes in our effective tax rate;

the effect of adverse changes in economic conditions in the United States and international markets; and

the effects of public health emergencies, natural disasters, terrorist activities, international conflicts and other events beyond our control.

In addition, the semiconductor market has historically been cyclical and subject to significant economic downturns. Our business is subject to rapid technological changes and there can be no assurance, depending on the mix of future business, that products stocked in inventory will not be rendered obsolete before we ship them. As a result of these and other factors, there can be no assurance that we will not experience material fluctuations in future revenue, gross margins and operating results on a quarterly or annual basis. In addition, if our revenue, gross margins and operating results do not meet the expectations of securities analysts or investors, the market price of our common stock may decline.

Table of Contents

Long-term contracts are not typical for us and reductions, cancellations or delays in orders for our products could adversely affect our operating results.

In certain markets where end-user demand may be particularly volatile and difficult to predict, some customers place orders that require us to manufacture product and have it available for shipment, even though the customer is unwilling to make a binding commitment to purchase all, or even any, of the product. At any given time, this situation could affect a portion of our backlog. As a result, we may incur inventory and manufacturing costs in advance of anticipated sales and are subject to the risk of cancellations of orders leading to a sharp reduction of sales and backlog. Further, those orders may be for products that meet the customer's unique requirements so that those canceled orders would, in addition, result in an inventory of unsaleable products, resulting in potential inventory write-offs. As a result of lengthy manufacturing cycles for certain of the products that are subject to these uncertainties, the amount of unsaleable product could be substantial. Reductions, cancellations or delays in orders for our products could adversely affect our operating results.

Our future success depends upon our ability to continue to improve our products, develop and market new products, and identify and enter new markets.

Our success significantly depends on our continued ability to improve our products and develop and market new products. Product development and enhancement is often a complex, time-consuming and costly process involving significant investment in research and development. There can be no assurance that we will be able to develop and introduce new and improved products in a timely or efficient manner or that new and improved products, if developed, will achieve market acceptance. Our products generally must conform to various evolving and sometimes competing industry standards, which may adversely affect our ability to compete in certain markets or require us to incur significant costs. In addition, our customers generally impose very high quality and reliability standards on our products, which often change and may be difficult or costly to satisfy. Any inability to satisfy such customer quality standards or comply with industry standards and technical requirements may adversely affect demand for our products and our results of operations. In addition, our growth is dependent on our continued ability to identify and penetrate new markets where we have limited experience and competition is intense. There can be no assurance that the markets we serve will grow in the future, that our existing and new products will meet the requirements of these markets, that our products will achieve customer acceptance in these markets, that competitors will not force prices to an unacceptably low level or take market share from us, or that we can achieve or maintain profits in these markets. Furthermore, a decline in demand in one or several of our end-user markets could have a material adverse effect on the demand for our products and our results of operations. Also, some of our customers in these markets are less established, which could subject us to increased credit risk.

We may not be able to compete successfully in markets within the semiconductor industry in the future.

Many other companies offer products that compete with our products. Some have greater financial, manufacturing, technical and marketing resources than we have. Some of our competitors may have better established supply or development relationships with our current and potential customers. Additionally, some formerly independent competitors have been purchased by larger companies. Our competitors also include emerging companies selling specialized products in markets we serve. Competition is based on design and quality of products, product performance, features and functionality, and price, with the relative importance of these factors varying among products, markets and customers. Existing or new competitors may develop products or technologies that more effectively address the demands of our customers and markets with enhanced features and functionality, lower power requirements, greater levels of integration or lower cost. Increased competition in certain markets has resulted in and may continue to result in declining average selling prices, reduced gross margins and loss of market share in such markets. There can be no assurance that we will be able to compete successfully in the future against existing or new competitors, or that our operating results will not be adversely affected by increased price competition.

We rely on third-party subcontractors and manufacturers for some industry-standard wafers and assembly/test services, and therefore cannot control their availability or conditions of supply.

We rely, and plan to continue to rely, on assembly and test subcontractors and on third-party wafer fabricators to supply most of our wafers that can be manufactured using industry-standard submicron processes. This reliance involves several risks, including reduced control over availability, capacity utilization, delivery schedules,

manufacturing yields, quality assurance and costs. Additionally, we utilize third-party wafer fabricators as sole-source suppliers, primarily Taiwan Semiconductor Manufacturing Company. These suppliers manufacture components in accordance with our proprietary designs and specifications. We have no written supply agreements with these sole-source suppliers and purchase our custom components through individual purchase orders. In addition, these suppliers often provide manufacturing services to our competitors and

Table of Contents

therefore periods of increased industry demand may result in capacity constraints. If these sole-source suppliers are unable or unwilling to manufacture and deliver sufficient quantities of components to us on the time schedule and of the quality that we require, we may be forced to seek to engage additional or replacement suppliers, which could result in additional expenses and delays in product development or shipment of product to our customers.

We may not be able to satisfy increasing demand for our products, and increased production may lead to overcapacity and lower prices.

The cyclical nature of the semiconductor industry has resulted in sustained and short-term periods when demand for our products has increased or decreased rapidly. During these periods of rapid increases in demand, our available capacity may not be sufficient to satisfy the available demand. In addition, we may not be able to expand our workforce and operations in a sufficiently timely manner, procure adequate resources, or locate suitable third-party suppliers, to respond effectively to changes in demand for our existing products or to the demand for new products requested by our customers, and our current or future business could be materially and adversely affected. Conversely, if we expand our operations and workforce too rapidly or procure excessive resources in anticipation of increased demand for our products, and such demand does not materialize at the pace at which we expect, our operating results may be adversely affected. These capacity expansions by us and other semiconductor manufacturers could also lead to overcapacity in our target markets which could lead to price erosion that would adversely impact our operating results. *Our revenue may not increase enough to offset the expense of additional capacity.*

We, and the semiconductor industry generally, expand production facilities and access to third-party foundries in response to periods of increased demand which can cause operating expenses to increase. Should customer demand fail to increase or should we enter a period of reduced customer demand, our financial position and results of operations could be adversely impacted as a result of increased operating expenses, reduced margins, underutilization of capacity or asset impairment charges.

Our semiconductor products are complex and may contain undetected defects which could result in significant costs, claims and damage to our reputation, and adversely affect the market acceptance of our products.

Semiconductor products are highly complex and may contain undetected defects when they are first introduced or as new versions are developed. We invest significant resources in the testing of our products; however, if any of our products contain defects, we may be required to incur additional development and remediation costs, including pursuant to indemnification provisions in our customer contracts. These problems may divert our technical and other resources from other product development efforts and could result in claims against us by our customers or others, including liability for costs associated with product recalls. If any of our products contains defects, or has reliability, quality or compatibility problems, our reputation may be damaged, which could make it more difficult for us to sell our products to existing and prospective customers and could adversely affect our operating results.

We may be unable to adequately protect our proprietary rights, which may limit our ability to compete effectively.

Our success depends, in part, on our ability to protect our intellectual property. We primarily rely on patent, mask work, copyright, trademark and trade secret laws, as well as nondisclosure agreements and other methods, to protect our proprietary technologies and processes. Despite our efforts to protect our proprietary technologies and processes, it is possible that competitors or other unauthorized third parties may obtain, copy, use or disclose our technologies and processes. Moreover, the laws of foreign countries in which we design, manufacture, market and sell our products may afford little or no effective protection of our proprietary technology.

There can be no assurance that the claims allowed in our issued patents will be sufficiently broad to protect our technology. In addition, any of our existing or future patents may be challenged, invalidated or circumvented. As such, any rights granted under these patents may not provide us with meaningful protection. We may not have foreign patents or pending applications corresponding to our U.S. patents and applications. Even if foreign patents are granted, effective enforcement in foreign countries may not be available. If our patents do not adequately protect our technology, our competitors may be able to offer products similar to ours. Our competitors may also be able to develop similar technology independently or design around our patents. Other companies or individuals have obtained patents covering a variety of semiconductor designs and processes, and we might be required to obtain licenses under some of these patents or be precluded from making and selling the infringing

Table of Contents

products, if such patents are found to be valid. There can be no assurance that we would be able to obtain licenses, if required, upon commercially reasonable terms, or at all.

We generally enter into confidentiality agreements with our employees, consultants and strategic partners. We also try to control access to and distribution of our technologies, documentation and other proprietary information. Despite these efforts, internal or external parties may attempt to copy, disclose, obtain or use our products, services or technology without our authorization. Also, former employees may seek employment with our business partners, customers or competitors, and there can be no assurance that the confidential nature of our proprietary information will be maintained in the course of such future employment.

We are involved in frequent litigation, including regarding intellectual property rights, which could be costly to bring or defend and could require us to redesign products or pay significant royalties.

The semiconductor industry is characterized by frequent claims and litigation involving patent and other intellectual property rights, including claims arising under our contractual obligations to indemnify our customers. We have received from time to time, and may receive in the future, claims from third parties asserting that our products or processes infringe their patents or other intellectual property rights. In the event a third party makes a valid intellectual property claim against us and a license is not available to us on commercially reasonable terms, or at all, we could be forced either to redesign or to stop production of products incorporating that intellectual property, and our operating results could be materially and adversely affected. Litigation may be necessary to enforce our patents or other of our intellectual property rights or to defend us against claims of infringement, and this litigation could be costly and divert the attention of our key personnel. We could be subject to warranty or product liability claims that could lead to significant costs and expenses as we defend such claims or pay damage awards. While we maintain product liability insurance, there can be no assurance that such insurance will be available or adequate to protect against all such claims. We may incur costs and expenses relating to a recall of one of our customers' products containing one of our products. See Note 10 in the Notes to our Consolidated Financial Statements contained in Item 1 of this Quarterly Report on Form 10-Q for information concerning certain pending litigation that involves us. An adverse outcome in these matters or other litigation could have a material adverse effect on our consolidated financial position or on our consolidated results of operations or cash flows in the period in which the litigation is resolved.

If we do not retain our key personnel, our ability to execute our business strategy will be limited.

Our success depends to a significant extent upon the continued service of our executive officers and key management and technical personnel, particularly our experienced engineers, and on our ability to continue to attract, retain and motivate qualified personnel. The competition for these employees is intense. The loss of the services of one or more of our key personnel could have a material adverse effect on our operating results. In addition, there could be a material adverse effect on us should the turnover rates for engineers and other key personnel increase significantly or if we are unable to continue to attract qualified personnel. We do not maintain any key person life insurance policy on any of our officers or employees.

To remain competitive, we may need to acquire other companies or purchase or license technology from third parties in order to introduce new products and services or enhance our existing products and services.

An element of our business strategy involves expansion through the acquisitions of businesses, assets, products or technologies that allow us to complement our existing product offerings, expand our market coverage, increase our engineering workforce or enhance our technological capabilities. We may not be able to find businesses that have the technology or resources we need and, if we find such businesses, may not be able to purchase or license the technology or resources on commercially favorable terms or at all. Acquisitions and technology licenses are difficult to identify and complete for a number of reasons, including the cost of potential transactions, competition among prospective buyers and licensees and the need for regulatory approvals. In order to finance a potential transaction, we may need to raise additional funds by selling our stock or borrowing money. We may not be able to find financing on favorable terms, and the sale of our stock may result in the dilution of our existing shareholders or the issuance of securities with rights that are superior to the rights of our common stockholders. Acquisitions also involve a number of risks, including:

Table of Contents

difficulty integrating acquired technologies, operations and personnel with our existing businesses;

diversion of management attention in connection with both negotiating the acquisitions and integrating the assets;

strain on managerial and operational resources as management tries to oversee larger operations;

the future funding requirements for acquired companies, which may be significant;

potential loss of key employees;

exposure to unforeseen liabilities of acquired companies; and

increased risk of costly and time-consuming litigation.

If we are unable to successfully address these risks, we may not realize some or all of the expected benefits of the acquisition, which may have an adverse effect on our business and results of operations.

We rely on manufacturing capacity located in geologically unstable areas, which could affect the availability of supplies and services.

We, and many companies in the semiconductor industry, rely on internal manufacturing capacity, wafer fabrication foundries and other sub-contractors in geologically unstable locations around the world. This reliance involves risks associated with the impact of earthquakes on us and the semiconductor industry, including temporary loss of capacity, availability and cost of key raw materials and equipment and availability of key services including transport of our products worldwide. Any prolonged inability to utilize one of our manufacturing facilities, or those of our subcontractors or third party wafer-fabrication foundries, as a result of fire, natural disaster, unavailability of electric power or otherwise, would have a material adverse effect on our results of operations and financial condition.

We are exposed to business, economic, political and other risks through our significant worldwide operations.

During the first nine months of fiscal 2007, approximately 76% of our revenue was derived from customers in international markets. Although we engage in hedging transactions to reduce our exposure to currency exchange rate fluctuations, there can be no assurance that our competitive position will not be adversely affected by changes in the exchange rate of the United States dollar against other currencies. Potential interest rate increases, particularly in the United States and China, as well as high energy costs could have an adverse impact on industrial and consumer spending patterns and could adversely impact demand for our products. We have manufacturing facilities outside the United States in Ireland and the Philippines. In addition to being exposed to the ongoing economic cycles in the semiconductor industry, we are also subject to the economic and political risks inherent in international operations and their impact on the United States economy in general, including the risks associated with ongoing uncertainties and political and economic instability in many countries around the world as well as the economic disruption from acts of terrorism, and the response to them by the United States and its allies. Other business risks associated with international operations include increased managerial complexities, air transportation disruptions, expropriation, currency controls, currency exchange rate movement, additional costs related to foreign taxes, tariffs and freight rate increases, exposure to different business practices and legal standards, particularly with respect to price protection and intellectual property, trade and travel restrictions, pandemics, import and export license requirements and restrictions, difficulties in staffing and managing worldwide operations, and accounts receivable collections.

Our future operating results are dependent on the performance of independent distributors and sales representatives.

A significant portion of our sales are through independent distributors that are not under our control. These independent distributors generally represent product lines offered by several companies and thus could reduce their sales efforts applied to our products or terminate their representation of us. We generally do not require letters of credit from our distributors and are not protected against accounts receivable default or bankruptcy by these distributors. Our inability to collect open accounts receivable could adversely affect our results of operations. Termination of a significant distributor, whether at our initiative or the distributor's initiative, could disrupt our current

business. If we are unable to find suitable replacements in the event of terminations by significant distributors or sales representatives, our operating results could be adversely affected.

Table of Contents

We are subject to increasingly strict environmental regulations, which could increase our expenses and affect our operating results.

Our industry is subject to environmental regulations that control and restrict the use, transportation, emission, discharge, storage and disposal of certain chemicals used in the manufacturing process. Public attention on environmental controls has increased, and changes in environmental regulations might require us to invest in costly remediation equipment or alter the way our products are made. In addition, we use hazardous and other regulated materials that subject us to risks of liability for damages caused by accidental releases, regardless of fault. Any failure to control such materials adequately or to comply with regulatory restrictions could increase our expenses and adversely affect our operating results.

Our manufacturing processes are highly complex and may be interrupted.

We have manufacturing processes that utilize a substantial amount of technology as the fabrication of integrated circuits is a highly complex and precise process. Minute impurities, contaminants in the manufacturing environment, difficulties in the fabrication process, defects in the masks used in the wafer manufacturing process, manufacturing equipment failures, wafer breakage or other factors can cause a substantial percentage of wafers to be rejected or numerous dice on each wafer to be nonfunctional. While we have significant expertise in semiconductor manufacturing, it is possible that some processes could become unstable. This instability could result in manufacturing delays and product shortages, which could have a material adverse effect on our financial position or results of operations.

Our stock price may be volatile.

The market price of our common stock has been volatile in the past and may be volatile in the future, as it may be significantly affected by the following factors:

actual or anticipated fluctuations in our revenue and operating results;

changes in financial estimates by securities analysts or our failure to perform in line with such estimates or our published guidance;

changes in market valuations of other semiconductor companies;

announcements by us or our competitors of significant new products, technical innovations, acquisitions or dispositions, litigation or capital commitments;

departures of key personnel;

actual or perceived noncompliance with corporate responsibility or ethics standards by us or any of our employees, officers or directors; and

negative media publicity targeting us or our competitors.

The stock market has historically experienced volatility, especially within the semiconductor industry, that often has been unrelated to the performance of particular companies. These market fluctuations may cause our stock price to fall regardless of our operating results.

Table of Contents**ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds
Issuer Purchases of Equity Securities**

| Period | Total Number of Shares Purchased | Average Price Paid Per Share (a) | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (b) | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|-------------------------------------|---|---|--|---|
| May 6, 2007 through June 2, 2007 | 2,168,677 | \$ 37.13 | 2,168,677 | \$ 534,113,498 |
| June 3, 2007 through June 30, 2007 | 9,767,800 | \$ 36.83 | 9,767,800 | \$ 1,174,329,864 |
| July 1, 2007 through August 4, 2007 | 4,954,889 | \$ 38.63 | 4,954,889 | \$ 982,920,556 |
| Total | 16,891,366 | \$ 37.40 | 16,891,366 | \$ 982,920,556 |

(a) The average price paid per share of stock repurchased under the stock repurchase program includes the commissions paid to the brokers.

(b) Repurchased pursuant to the stock repurchase program publicly announced on August 12, 2004. On December 6, 2006, our Board of Directors authorized the repurchase by us of an additional \$1

billion of our common stock, increasing the total amount of our common stock we are authorized to repurchase from \$2 billion to \$3 billion. On June 6, 2007, our Board of Directors authorized the repurchase by us of an additional \$1 billion of our common stock, increasing the total amount of our common stock we are authorized to repurchase from \$3 billion to \$4 billion. Under the repurchase program, we may repurchase outstanding shares of our common stock from time to time in the open market and through privately negotiated transactions. Unless terminated earlier by resolution of our Board of Directors, the repurchase program will expire when we have

repurchased all
shares
authorized for
repurchase
under the
repurchase
program.

ITEM 6. Exhibits

The exhibits listed in the Exhibit Index immediately preceding the exhibits are filed as part of this Quarterly Report on Form 10-Q and such Exhibit Index is incorporated herein by reference.

44

Table of Contents

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.

ANALOG DEVICES, INC.

Date: August 21, 2007

By: /s/ Jerald G. Fishman

Jerald G. Fishman
President and Chief Executive Officer (Principal
Executive Officer)

Date: August 21, 2007

By: /s/ Joseph E. McDonough

Joseph E. McDonough
Vice President-Finance and Chief Financial Officer
(Principal Financial and Accounting Officer)

45

Table of Contents

Exhibit Index

Exhibit

| No. | Description |
|------------|--|
| 10.1 | Form of Confirming Memorandum for Grants of Non-Qualified Stock Options to Directors for usage under the Registrant's 2006 Stock Incentive Plan. |
| 31.1 | Certification Pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer). |
| 31.2 | Certification Pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer). |
| 32.1 | Certification Pursuant to 18 U.S.C. Section 1350 (Chief Executive Officer). |
| 32.2 | Certification Pursuant to 18 U.S.C. Section 1350 (Chief Financial Officer). |