UTSTARCOM INC
Form 10-K
February 21, 2003

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended December 31, 2002.

OR

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

For the transition period from ________________ to________________ .

COMMISSION FILE NUMBER 000-29661

UTSTARCOM, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE	**52-1782500**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
1275 HARBOR BAY PARKWAY, ALAMEDA, CALIFORNIA	**94502**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (510) 864-8800
Securities registered pursuant to Section 12(b) of the Act: NONE
Securities registered pursuant to Section 12(g) of the Act: Common Stock, $0.00125 par value

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. / /

The aggregate market value of voting stock held by non-affiliates of the registrant as of January 31, 2003, was approximately $1,231,318,352 based upon the closing price of $19.27 reported for such date on The Nasdaq National Market. For purposes of this disclosure, shares of Common Stock held by persons who hold more than 5% of the outstanding shares of Common Stock and shares held by officers and directors of the registrant, have been excluded in that such persons may be deemed to be affiliates. This determination is not necessarily conclusive for other purposes.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes /x/   No / /

The aggregate market value of voting stock held by non-affiliates of the registrant as of the last business day of the registrant's most recently completed second fiscal quarter was approximately $1,378,658,004 based upon the closing price of $20.17 reported for such date on The Nasdaq National Market. For purposes of this disclosure, shares of Common Stock held by persons who hold more than 5% of the outstanding shares of Common Stock and shares held by officers and directors of the registrant, have been excluded in that such persons may be deemed to be affiliates. This determination is not necessarily conclusive for other purposes.

As of February 7, 2003 registrant had outstanding 107,017,039 shares of Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on May 9, 2003 are incorporated herein by reference in Part III.

UTSTARCOM, INC.

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PART I

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. These statements are based on information that is currently available to management. We intend such forward-looking statements to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, and we are including this statement for purposes of complying with those provisions. The forward-looking statements include, without limitation, those concerning the following: our expectations as to the nature of possible trends, the manner in which customers in Chinese provinces negotiate for the purchase of our products; our expectation regarding continued growth in our business and operations; our expectation that our PAS network access system will continue to be allowed in China's county-level cities and counties; our expectation that there will be no penalties or fines for our non-compliance with the licensing requirements in China for our PAS and iPAS systems and other products; our expectation concerning the anticipated cost and completion date of our new Hangzhou manufacturing facility, our expectation that there will be fluctuations in our overall gross profit, gross margin, product mix, quarter to quarter results, customer base and selling prices; our plans for expanding the direct sales organization and our selling and marketing campaigns and activities; our expectation that we may use part of the net proceeds of our initial and follow on public offerings to acquire or invest in complementary businesses, technologies or product offerings; our expectation that there will be increases in selling, marketing, research and development, general and administrative expenses; our expectation that we will continue to invest significantly in research and development; our expectation that we will fill the majority of our current backlog orders; our expectation regarding our future investments, particularly in Softbank China; and our expectation that existing cash and cash equivalents will be sufficient to finance our operations for at least the next 12 months. Additional forward-looking statements may be identified by the words, "anticipate," "expect," "believe," "intend," "will" and similar expressions, as they relate to us or our management. Investors are cautioned that these forward-looking statements are inherently uncertain. These statements are subject to risks and uncertainties that may cause actual results and events to differ materially. For a detailed discussion of these risks and uncertainties, see the "Factors Affecting Future Operating Results" section of this Form 10-K. We do not guarantee future results and undertake no obligation to update the forward-looking statements to reflect events or circumstances occurring after the date of this Form 10-K.

ADDITIONAL INFORMATION

UTStarcom is registered as a trademark in the United States. UTStarcom and PAS are registered as trademarks in China. We have applied to register the mSwitch and Netman trademarks in China.

In this Annual Report on Form 10-K, references to and statements regarding China refer to mainland China, references to "U.S. dollars" or "$" are to United States Dollars, and references to "Renminbi" are to Renminbi, the legal currency of China.

Unless specifically stated, information in this Annual Report on Form 10-K assumes an exchange rate of 8.3 Renminbi for one U.S. dollar, the exchange rate in effect as of December 31, 2002.

UTStarcom's public filings, including its annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, are available free of charge at its website, *www.utstar.com*. The information contained on our website is not being incorporated herein.

ITEM 1 BUSINESS

OVERVIEW

Incorporated in 1991 as a Delaware Corporation, UTStarcom designs, manufactures, and markets leading Broadband, Narrowband, wireless access, Softswitch and 3G products which offer a clean migration path to next-generation Internet Protocol (IP-based) networks. These products support service providers as they evolve their networks to meet the changing and growing demands of consumers. Providers are migrating voice services from the traditional copper-based network to wireless and packet-based networks. The copper-based network itself, once limited to carrying narrowband services, is evolving to support broadband services. Service providers are also migrating from circuit-based time division multiplex (TDM) services to packet-based services. Because UTStarcom engineers its solutions with migration needs in mind, service providers can implement them quickly and cost effectively.

We provide a range of next-generation wireless and wireline network service products that support widely adopted international standards and protocols, so service providers can easily integrate them into existing networks and deploy them in new networks.

UTStarcom solutions are based on four principle technology platforms mSwitch, PAS/iPAS (IP-based PAS), AN-2000, and 3G that carriers can use to build their networks in a modular fashion.

- mSwitch is a highly scalable, IP-based, multiservice switching architecture that seamlessly bridges the gap between existing circuit-switched and next-generation packet-switched networks.

- Our wireless network solution, Personal Access Services (PAS/iPAS), allows service providers to offer premium-quality voice, data, and value-added services over mobile and fixed wireless networks using our specially designed PAS handsets. PAS also provides an affordable pathway for service providers to migrate from wireline to community-based wireless in regions where there is little or no existing copper infrastructure. As of December 31, 2002, UTStarcom had cumulatively deployed or were in the process or deploying approximately 22 million lines of PAS/iPAS equipment servicing approximately 7.5 million subscribers in 21 provinces in China. Based on our knowledge of China's communications market, we believe that PAS is the most widely deployed wireless local access system in China. In the Taiwan market, approximately 500,000 subscribers were using our PAS systems as of December 31, 2002. In addition, we have deployed systems or begun trials for PAS in India, Vietnam and the Latin America region.

- For wireline networks, we provide a broadband-ready access platform called AN-2000. As of December 31, 2002, approximately 4 million AN-2000 lines had been deployed in China, including deployments of 80,000 broadband DSLAM lines in Zhejiang Province. We have launched significant deployments of our AN-2000 platform in Japan, Latin America and India.

- Our 3G network solution enables the transformation of voice-centric mobile communications to content-rich multimedia services. We support W-CDMA, CDMA 2000 and TD-SCDMA standards to deliver wireless multimedia over an IP core network.

UTStarcom is committed to offering products that make its customers more competitive and more successful. Service providers use our integrated suite of products to attract a wide range of customers by offering a wider selection of efficient and expandable voice, data and Internet access services. Because UTStarcom offers cost-effective deployment, we believe our products enable service providers to earn more money per customer by offering numerous additional services.

UTStarcom's range of wireless solutions enables service providers to sell highly affordable wireless communications services to the large population of users whose needs are not met by existing fixed line and cellular services. Our solutions also make it easy for service providers to offer value added services for a nominal amount or at no additional cost to themselves and for only a small incremental cost to

their customers. And because our solutions offer a migration path, the service providers can easily add new wireless services and additional revenue streams while maintaining the value of their previous technology investments.

Historically, substantially all of our sales have been to service providers in China. However, our range of solutions can be used wherever there is a need for cost-effective communications. We are currently expanding our sales efforts to include growing communications markets in Japan, Taiwan, Vietnam, India, Latin America, and elsewhere.

INDUSTRY BACKGROUND

Growth in China's Communications Market. China is the fastest-growing and largest communications markets in the world. Growth in China's communications equipment and services markets is being driven by the government of China's commitment to developing a communications infrastructure, strong demand for communications services and robust economic growth.

China's demand for communications services is highlighted by its relatively low tele-density rate, which is a measure of the number of lines per hundred people. According to data released by China's Ministry of Information Industry (MII) at the end of 2002, China had a fixed-line teledensity rate of only 16.8% and a population of approximately 1.3 billion. In contrast, according to a report by the International Telecommunication Union as updated in June 2002, fixed-line teledensity rates for the United Kingdom, France, Hong Kong and the United States were 58.8%, 57.4%, 57.7%, and 66.5%, respectively. While growth in China's communications market is currently driven predominantly by voice services, the increasing demand for data services also presents a growing opportunity both in China and in other international markets. According to data provided by the MII, Internet users in China reached 49.7 million by the end of 2002, an increase of 36% year over year. In order to support this growth in data traffic, service providers in China must continue to expand their networks. We believe this is best achieved by deploying IP-based equipment.

China's ability to invest heavily in its communications infrastructure is fueled by the country's strong economic activity. According to the China's State Statistics Bureau, China's gross domestic product, or GDP, grew 8.0% in 2002. The bureau also estimates that China's GDP will grow by approximately 7% through 2005.

Communications Needs of Developing Countries. Demand for voice and data communications services in developing countries continues to grow rapidly and is driven by both public sector infrastructure investment and private sector business growth. The governments of many developing countries have identified the development of a communications infrastructure as a key driver of modernization and economic growth. Governments are increasingly implementing and funding infrastructure development through privatization of state-owned telecommunications service providers. These service providers, in turn, are deploying advanced networks for voice and data services. In addition, increasingly affluent businesses and residential consumers in the highest growth regions of these countries are demanding state-of-the-art voice and data communications solutions to interact and compete on a global basis.

Communications Network Architecture in China. The development of China's communications infrastructure involves installing a nationwide network of high-bandwidth fiber-optic backbone networks and connecting each business and residential subscriber to this backbone. The wireline and wireless systems that link local subscribers to these backbone networks are referred to as the last mile or the local access network. The high growth rate, geographic dispersion and diverse communications needs of residences and businesses in China means that the direct wiring of subscribers to the backbone network using traditional copper connections is a lengthy, costly and inefficient process. Direct wiring of subscribers to traditional telephone switches often locks those subscribers into a limited set of communications services and limits expandability and migration to other services. In contrast, service

providers in China require communications equipment that allows them to provide services quickly, efficiently and cost-effectively. Given the relative absence of a legacy communications infrastructure in China, these service providers are less constrained and thus often seek to deploy the latest best-of-breed systems with the flexibility to handle voice and data services.

Needs of Service Providers. Voice and data service providers require network solutions that address all of their access needs and offer easy migration to next generation networks while minimizing operational expense. These service providers require products that enable them to quickly, and with minimal incremental investment, address the changing demands of their subscribers for expanded or more advanced services. Given the rapid growth in emerging communications markets in regions such as Southeast Asia, Latin American and India, network solutions must be scalable. The same architecture must provide an affordable entry-level solution to initially serve a few hundred subscribers, yet economically scale to serve several hundred thousand subscribers over time. In addition, service providers require the following:

- Return on Investment. As competition intensifies, service providers require the ability to offer advanced and flexible services to their customers. Service providers must ensure these new services drive subscriber growth and, ultimately, revenue and profitability. As a result, service providers are focused on return on investment, enabling them to deploy technology that provides increased services today while also providing a cost-effective migration path to future expansion and functionality.

- IP-Based Networks. An increasing amount of voice and data traffic travels across IP-based networks instead of traditional circuit-based networks. The principal advantages of highly flexible, IP-based networks over circuit-based networks are lower cost, higher speed and the support of multiple applications, including e-mail, short-messaging, Internet access, video and voice in a single network. Because of these advantages, investment in IP-based networks is increasing while investment in circuit-based networks is decreasing.

Integrated Voice and Data Solutions. Service providers are increasingly looking to expand their service offerings beyond traditional voice services to provide data and other value-added services. As advanced high speed data networks are deployed, service providers will require solutions that can be upgraded to adapt to new technologies while preserving the investment in their existing infrastructure. These networks will enable service providers to differentiate their service offerings, build customer loyalty and generate incremental revenue.

Rapid Deployment. Given the rapid growth in emerging communications markets such as China, service providers are focused on quickly deploying solutions to meet customer needs. Wireless access solutions allow for rapid deployment of relatively inexpensive networks that give service providers significant revenue potential and cost advantages over wireline networks. In addition, service providers require wireless networks that will allow for convergence of voice and data and migration to third generation networks, referred to as 3G networks.

Commitment to Local Markets. Service providers value equipment vendors that have made a strong commitment to their local markets. This commitment includes direct sales forces and local service organizations to respond to the needs of service providers and their subscribers.

Although markets such as China represent substantial opportunities for communications equipment vendors, few companies have delivered products that have the ability to smoothly migrate to next generation technologies, coupled with the local presence that service providers require.

THE UTSTARCOM SOLUTION

We design, manufacture, and market a full range of Broadband, Narrowband, Wireless, Softswitch and 3G solutions that enable easy migration to next-generation IP-based networks. Carriers use them to create IP-based networks, integrated voice and data solutions, and wireless access networks.

An important element of our strategy is our commitment to delivering lower cost-per-subscriber via lower operating costs, greater operating efficiencies, and higher and more diversified throughput levels. In addition, we provide our customers with a full range of solutions that they can tailor to their specific market needs and that enable them to offer a full range of services to their subscribers. We have been particularly successful in enabling our customers to offer high-bandwidth, multi-featured, affordable regional wireless services to portions of the large, unserved market of users that want mobile service but that do not require or cannot afford GSM cellular service. Finally, our solutions give carriers a full range of migration services, from voice to wireless, from copper to broadband, and from circuit switching to packet switching.

We offer our customers a number of key competitive advantages:

Migration to Next-Generation IP Networks. Our core IP products are designed with the flexibility to allow service providers to deliver voice and data services over today's circuit-based networks and to migrate to next-generation broadband wireline and wireless networks based on IP and other international open standards. As a result, service providers can preserve their investment in existing networks and generate incremental revenue from their investment in our products while migrating to next-generation networks over time. Our products enable service providers to effectively time their network equipment expenditures, expand voice and data capacity and rapidly introduce new services as demand warrants.

Cost-Effective Solutions. Our products are designed to provide operators with a high return on their investment. By reducing network complexity, integrating high performance capabilities and providing a flexible migration path to next generation networks, our products cost less to deploy and maintain than most alternative technologies.

Convergence of Voice and Data Services. We have designed our systems to offer a high degree of flexibility in terms of subscriber capacity and types of traffic delivered. Our equipment can be flexibly configured to offer a variety of services in response to subscriber demand. This flexibility is particularly important to those emerging communications markets that are currently undergoing rapid change and growth. As Internet usage achieves greater global penetration, we believe service providers around the world will desire systems that are designed to deliver high-speed data capability. Our access systems allow service providers to quickly and cost-effectively implement upgrades for new services, including high-speed data capability. Alternative solutions may require the purchase of an entirely new system to provide these services.

Wireless Access Networks. Our PAS and 3G wireless access solutions are ideally suited for the requirements of service providers in both robust and emerging communications markets. Service providers can deploy our products quickly to cost-effectively meet customer demand. Our systems allow service providers to rapidly add new subscribers and to scale network capacity in response to demand. Our IP-based wireless access solutions also provide a platform for service providers to migrate to 3G mobile networks.

Local Presence. We have established a strong local presence with China Telecom Corporation and China Netcom Corporation, the incumbent wireline service providers in China, which enables us to be responsive to them and the specific needs of their subscribers. We manufacture our products primarily at our facility in Hangzhou in Zhejiang province. By using local facilities in China, we have helped create new jobs within the provinces and have strengthened our relationships with the

Telecommunications Administrations in some of China's most modern and rapidly growing provinces. We also maintain 21 sales and customer support sites in China that allow us to deploy a customer support representative onsite anywhere in China within 24 hours. Our sales force develops direct relationships with decision makers at both the provincial and local levels through pre-sales design and consulting services. Additionally, through our relationships at the national, provincial and local levels in China, we receive a flow of information regarding market changes and insight into unique service provider needs and related opportunities. As part of this strategy to develop a local presence in markets that we serve, we also have sales, support and engineering personnel in Taiwan, India, Japan, Vietnam, as well as the Caribbean, Latin America, Europe and Africa regions.

STRATEGY

Our objective is to be a leading global provider of Broadband, Narrowband, Wireless, Softswitch, and 3G solutions. The principal elements of our strategy are as follows:

Capitalize on the Emerging IP-based Switching Market. We believe the increase in Internet usage, particularly voice over IP traffic, has resulted in a market need for a next-generation, IP-based switching platform. Accordingly, we are making a substantial investment in developing our mSwitch architecture, which is designed to integrate with our existing products and can be scaled in response to increased demand. We believe that mSwitch can deliver value to service providers, both as a stand-alone system and in combination with our PAS system and AN-2000 platform. In the future, we intend to incorporate additional functionality into the mSwitch platform that we believe will enable us to enter new markets in China and around the world.

Maintain and Grow Market Share. We believe we are well positioned to maintain and grow our worldwide business. According to a report by Synergy Research in the fourth quarter of 2002, we are the leading worldwide supplier of softswitch solutions, holding more than 51% of the global market. According to a report by Infonetics Research in the fourth quarter of 2002, we are the second leading supplier of DSLAM and IP-DSLAM solutions worldwide. Our solutions are easy to deploy, offer a clean migration strategy to future network requirements, and enable service providers to sell a wide range of high-value-added services. We expect to continue to build local and global market share, extending the benefits of our solutions to our global customer base through expansion of our international sales operations and direct sales forces outside of China.

Leverage Our Installed Base to Capitalize on Demand for Wireless and Wireline Broadband Services. We believe we are well positioned to leverage our existing global installed base of systems and service provider relationships to capitalize on an increasing demand for data and broadband services. To meet this demand, we intend to:

- leverage our installed base of AN-2000 platforms and our working relationships with providers to offer our wireless access systems;

- continue to enhance functionality and increase features of our mSwitch IP-based, multiservice softswitch platform, which is designed to enable geographically dispersed gateways and servers to interact over high-speed IP networks to serve millions of subscribers;

- enhance our PAS systems and handsets to enable the provisioning of high-speed data services over 128 Kilobits per second, or Kbps, wireless links;

continue to focus our development efforts on products that enable migration to 3G wireless technologies;

continue to innovate and develop new products so that we may offer new broadband upgrades to our installed base of AN-2000 platforms to enable the delivery of broadband services over copper connections through digital subscriber line, or xDSL, technologies;

broaden our PAS systems to enable value-added services, such as wireless content and applications which our customers offer in China under the brand name C-Mode, in Vietnam under the brand name CityPhone and in Taiwan under the brand name MiMi; and

work with original equipment manufacturers to offer service providers a complete solution for IP-based networks.

Expand Our Presence in China. We intend to further capitalize on favorable market conditions in China, including its large population, low teledensity and strong demand for communications services. Since our inception, we have focused our engineering, product development and sales and marketing efforts primarily on communications equipment for China. This focus has enabled us to be a leader in this market by quickly identifying the needs of service providers in China and rapidly developing market-specific products to address those needs. We intend to expand our presence in this market by:

increasing the number of sales and support staff and offices in China;

developing new products to address the demands of our existing and future customer base;

migrating our installed base from voice to data, from wireline to wireless, and from time division multiplex (TDM) switching to IP soft switching as market demand warrants; and

increasing our local research and development and manufacturing capabilities.

Penetrate Other Growing Communications Markets Worldwide. We have started offering our products in growing communications markets outside of mainland China, opening new international sales operations in North America, Europe, the Middle East and Africa, Central America and Latin America, and South and North Asia. We intend to penetrate these markets in several ways: through direct sales offices located in key market regions, licensing our technology to local manufacturers where import taxation favors this approach, the development of local sales agency and distributor relationships within specific market regions, and sales relationships with original equipment manufacturers. Our sales division has initiated expansion into Africa, Europe, India, Japan, Latin America, Taiwan, and other Pacific Rim markets. We have established regional offices to focus on non-China market development with sales and customer support operations in Bangkok, Hanoi, Ho Chi Minh, Manila, Miami, New Delhi, New Jersey, Shanghai, Taipei, Tel Aviv, and Tokyo. We also plan to establish local direct sales representative offices in key regions around the world. To date, we have deployed our products in a number of growing communications markets outside of mainland China, including India, Japan, Vietnam, and Taiwan.

PRODUCTS

We provide communications equipment for service providers that operate wireless and wireline networks. Our wireless and wireline access networks and IP-based switching systems include four principal technology platforms:

mSwitch our IP-based multiservice softswitch architecture;

PAS/iPAS our wireless access solution which includes infrastructure systems, handsets and value-added services;

AN-2000 our broadband access platform; and

3G offerings our third-generation mobile and multimedia solution.

Each comprises multiple hardware and software subsystems that can be offered in various combinations to suit individual customer needs. In addition, through original equipment manufacturer relationships, we provide customers in China with equipment for deployment in metropolitan area networks.

Our IP-Based Multiservice Softswitch (mSwitch)

mSwitch, our IP-based, multiservice softswitch architecture, is a cost-effective, flexible and scalable network solution designed to replace traditional central office switches. This architecture delivers multiple services, including broadband and narrowband remote access services, on an IP-based packet-switching infrastructure via wireless and wireline networks. Capacity of the mSwitch is highly scalable, allowing customers to increase their sources of revenue generation by supporting a wide range of new revenue-generating services.

A single mSwitch platform provides a variety of features and benefits:

It provides a cost effective way to upgrade an existing PSTN to a v5.2 interface.

It delivers a fully converged network that can be used to provide broadband access, Gigabit Ethernet, IP VPN, streaming video, 3G and other services.

The mSwitch architecture includes a new, revenue-generating Wireless PAS Access Gateway.

The architecture incorporates a 3G mobile core network capable of serving both immediate and future demands.

Voice over IP (VoIP) eliminates the need for the continued build-out of obsolete infrastructure.

The mSwitch's highly reliable transport carries bearer data along with signaling, control, and management information. The architecture includes operations support systems for associated billing, provisioning, and service management. The VoIP gateway functions of mSwitch seamlessly bridge service providers' existing circuit-switched platforms to next-generation, IP-based packet-switched architecture. In addition, service providers can use the mSwitch to implement a network migration strategy that protects their investments on every level. By combining our softswitch functionality with our wireless technology, mSwitch provides highly scalable, mobile switching centers that can operate with our PAS system.

mSwitch networks are distributed, which means that many geographically dispersed gateways and servers can interact over a high-speed, IP-based network to serve millions of subscribers. Gateways provide hardware resources to process voice and data and support widely used interface protocols. Servers provide functions like call routing, accounting, authorization, billing, provisioning, fault monitoring and recovery.

We have developed an advanced and comprehensive operations support system (OSS) for management of mSwitch equipment, billing for mSwitch services, and customer care for mSwitch subscribers. This OSS uses an online, Internet-based user interface that enables service provider personnel and individual subscribers to access provisioning and billing information through the Internet from an ordinary web browser.

We are also developing a set of capabilities to support 3G wireless technologies, including a mobile switching center, a radio network controller and a general packet radio service node. We were one of a select group of participants in China's technical trial of 3G mobile networks based on the 3GPP WCDMA standard. In 2002, we successfully completed the first phase of testing conducted by China's Ministry of Information Industry, or MII, and have begun field trials in two major cities. We also expect to launch two more field trials in 2003.

In addition, we are also developing mSwitch applications to provide wireline local exchange functionality, voice-over-IP gateways that will enable legacy public networks to connect to low-cost, IP-based, long-distance trunk lines, and modem and fax pools that will allow mSwitch to act as a remote access server for dial-up users who wish to access IP networks.

We are also developing IP routing capabilities that we will integrate in our mSwitch platform to further improve functionality and reduce cost to our customers. We intend to continue to enhance

mSwitch with additional applications in response to evolving market requirements and technology trends.

Our Wireless Access System (PAS)/(iPAS)

UTStarcom's Personal Access Services (PAS) wireless access system and IP-based (iPAS) wireless access system use micro cell radio technology and specialized handsets to offer business and consumer subscribers mobile and fixed access to telephone services.

PAS Wireless Access System

PAS takes advantage of unused switching capacity to let service providers offer a wide range of profitable services to a large subscriber base that other wireless technologies cannot reach. We specifically designed our PAS solution to meet the growing needs of a specific consumer-and//or subscriber population that desires limited and/or regional mobility (more than fixed line and less than a traditional cellular offering), a more cost-effective tariff plan, and access to value-added data services (VAS). When compared to macrocellular systems like GSM and CDMA, PAS offers lower deployment costs, easier radio planning, higher traffic capacity, better voice quality, faster data transmission speeds, lighter handsets with lower power requirements, and better support of advanced information services.

Because PAS is a limited-mobility system, it is ideal for deployment in urban and suburban areas; while traditional cellular systems that are based upon either GSM or CDMA standards cover larger regional areas. UTStarcom's wireless CityPhone feature allows service providers to offer subscribers same-number extension lines with citywide mobility. For additional coverage or capacity, service providers can easily deploy PAS in indoor spaces such as office buildings, airports, and shopping malls. PAS can provide wireless mobile phone service at densities of upwards of 15,000 subscribers per square kilometer. Our PAS solution integrates seamlessly into existing Public Switched Telephone Networks and offers unlimited scalability, enabling service providers to economically sell services to anywhere from 10,000 to a million subscribers.

The PAS wireless access network employs a mobile switching network based on our AN-2000 platform. The wireless access network formed by PAS components connects to the central office switch to provide local and long distance telephone service over a standard digital interface or an analog 2-wire interface. These open interfaces to the central office allow PAS to access any of the operator's installed switching capacity and to deliver existing switch based services, such as caller ID, call forwarding, and voice mail, to wireless subscribers.

iPAS Wireless Access System

IP-based PAS (iPAS)

With the UTStarcom iPAS wiress access network, operators can migrate their current wireline network to an IP-based wireless network that provides wireless voice and data services within a city or community. With this new system, service providers can offer new wireless services, such as citywide mobility, same-number wireless extension, email, mobile Internet access, short messaging and location-based services.

iPAS interconnects with the existing PSTN by way of the SS7 interface, making it an ideal solution for areas where the V5.2 interface is not yet available. With the IP trunking capability, iPAS can operate as an independent network over a unified IP-based infrastructure. iPAS also provides a standard V5.2 interface to support wireline services over a V5-based access network.

In 2002, we deployed more than 10 million lines of mSwitch-based iPAS systems in many cities in China and in several other locations outside of China. Chengdu now has the largest iPAS site in the world, with more than 500,000 users by the end of 2002.

PAS Handsets, Value Added Services and Network Management

We also design and manufacture handsets that are specifically configured to support PAS services. In 2002, we introduced 6 new handset models spanning a full spectrum of price ranges and functionalities, including our high-end 718U, a full-color handset that takes full advantage of our value-added services or VAS platform. Our strategy of designing in-house, manufacturing, licensing, and direct sourcing handset components gives us the flexibility to meet demand while offering the broadest line of PAS handsets to our global customer population. We expect to continue to invest in this area and to introduce additional handset models in 2003, including a dual-mode cellular/PAS handset.

In conjunction with our PAS system, we enable rich wireless content and applications similar to NTT DoCoMo's iMode service. To date, this service has been launched by our customers in Xian, Chengdu, and Hangzhou in China; Hanoi and Ho Chi Minh in Vietnam; and Taipei in Taiwan. This service, known in China as C-mode, as CityPhone in Vietnam, and as Mobile Information, Mobile Internet, or MiMi/WiWi in Taiwan, employs a high-function handset with expanded LCD display that subscribers can use to browse the worldwide web and to send and receive e-mail and short messages. We support standardized Chinese as well as English characters, and local content providers in China and Taiwan are accumulating hundreds of information services including news, stock quotes, sports results, job postings, dating services, chat rooms, and fortune telling. MiMi has a Global Positioning Service (GPS) feature that can accurately determine a user's location and can list local restaurants, shops, hotels, theaters, hospitals, or other location-sensitive information when queried.

Our Netman network management system, which is integrated with our network access products, provides for centralized management of our PAS products. Netman provides the ability to manage individual network components and to report on the status of the network as a whole. With Netman, a service provider can add and drop subscribers and continuously monitor all access network elements, providing for real-time reporting and alarms in addition to performance management, optimization and distribution of software updates. Netman uses scalable client/server architecture in a Windows NT environment. Server hardware may be scaled to handle several thousand nodes. Netman can also be installed on a portable personal computer and may be used as the local onsite maintenance terminal wherever remote nodes are installed.

By end of 2002, there were 7.5 million PAS subscribers on UTStarcom's systems throughout China, a net increase of 137% year over year. UTStarcom's installed and under construction PAS/iPAS system capacity in China reached 22.2 million lines, an increase of 236% over the capacity of 6.6 million lines at the end of 2001. Among the cities we added during 2002, several cities, such as Wenzhou, Chengdu and Taipei have reached over half a million active subscribers.

Our Broadband Access Platform (AN-2000)

UTStarcom understands that service providers want to bring the power of broadband into the homes and businesses they serve so they can offer a wide range of new services that generate new revenue streams. We give service providers a way to access these services and revenue streams with our economical, scalable, versatile, and powerful AN-2000 broadband solutions.

Because our broadband solutions conform to the most rigorous industry compatibility standards, they give our customers a number of advantages. Our solutions support modular network build out, enabling service providers to expand their networks easily. Customers can be confident that their UTStarcom solution is designed to work with their networks as they grow and evolve. Our solutions also work with existing equipment; service providers do not need to eliminate their legacy technologies to offer broadband services.

The AN-2000 family of integrated broadband access platforms delivers a mix of broadband and traditional voice and data services via copper or fiber, or a wireless network. The solutions also enable

network migration from narrowband to broadband. Services supported by the AN-2000 include the following:

- traditional analog voice;
- voice and data in digital format over integrated services digital network, or ISDN, lines;
- analog and digital leased lines;
- business data over integrated digital subscriber lines, or IDSL, and high-data-rate digital subscriber lines, or HDSL; and
- high-performance, always-on Internet access for residential and business subscribers using advanced asymmetric digital subscriber line, or ADSL, technology.

Our AN-2000 platform contains both central office terminals and remote terminals that are linked together by fiber, microwave radio, or copper to form a digital access network. The remote terminals are located close to the subscribers and offer last-mile wireline connections for voice and data services to the subscribers. Each remote terminal, which is scalable from 16 to 1,520 lines, can be connected into a ring to form a metropolitan access network of up to 23,000 subscriber lines. By connecting multiple metropolitan access networks, a metropolitan service network can potentially service hundreds of thousands of subscribers.

The AN-2000 platform offers a V5.2 exchange interface that benefits service providers by shifting network intelligence out into the access network, reducing reliance on costly proprietary distributed central office switch architectures. For service providers whose switches are not yet V5.2 compliant, we provide a migration capability whereby the AN-2000 terminates analog and ISDN ports in the central office, effectively creating a V5.2 interface to the remote AN-2000 platforms.

For broadband services based on ADSL, the AN-2000 platform has integral multiplexing capability for up to 384 users to share 155Mbps of Asynchronous Transfer Mode, or ATM, bandwidth to the Internet or, alternatively, 1.6Gbps in our IP-over-Ethernet version. The AN-2000 platforms can serve as a multi-service access node in which ADSL is delivered from a remote location combined with voice and leased line services or it can be configured as a pure central-office based Digital Subscriber Loop Access Multiplexer (DSLAM). Other DSL services, including HDSL and G.SHDSL, are also available. We also offer a Broadband Remote Access Server (B-RAS) to provide service management features, including authorization, accounting, virtual networking, and protocol translation. As with PAS, our integrated Netman network management system provides centralized management of the AN-2000 platforms. The ADSL service is compatible with most customer premise modems provided by third-party vendors. As of December 31, 2002, service providers have deployed approximately 4.0 million AN-2000 lines worldwide.

In 2001, we introduced our IP-DSLAM product, based on an extension of our AN-2000 technology. This product, which began shipping in the fourth quarter of 2001, provides extremely high density and high functionality at an attractive price. This product represents a new generation of DSLAM, which does not require ATM networking, and is therefore compatible with IP-based networks. Our IP-DSLAM lowers operator costs by eliminating the need for traditional high cost ATM-based networks.

Our 3G Solution

UTStarcom offers an end-to-end solution for 3G wireless networks that supports W-CDMA, CDMA 2000 and TD-SDCMA standards. Our solution consists of three primary elements:

1. mSwitch Mobile Core Network, which consists of a Softswitch server complex, an integrated Operations and Support System (OSS), and various types of media gateways.

2. Radio Access Network (RAN), which is a combination of Radio Node Controller (RNC) and a radio base station (Node-B).
3. A suite of portable multimedia devices, which supports a variety of new applications including mobile web browsing, video phone applications and mobile computing.

UTStarcom's 3G solution is based on forward-looking IP and softswitch architecture which we believe will significantly lower the investment and operational cost for operators. This simple and cost-efficient architecture provides the ability to migrate from 3GPP R99 to 3G PP R4/5 ALL IP in the future. Other unique advantages which UTStarcom's 3G solution offers include:

1. Co-existing with iPAS network, which provides operators the choice to share the iPAS core network with future 3G solutions and offer seamless upgrades of network and customer services.
2. Layered network for flexibility and efficiency, which consists of a service layer, control layer, connection layer and access layer.
3. Scalable network capacity, which supports 10,000 to 10,000,000 subscribers.

UTStarcom started the research and development of our 3G technology in 1997. UTStarcom has established a global team of hundreds of engineers across China and the US to engage in the different aspects of 3G solutions. One major development came in November 2001 when UTStarcom was selected by China's Ministry of Information Industry (MII) along with a select group of vendors to conduct technical trials in a comprehensive mobile communications trial system of MII (MTNet) using the 3GPP WCDMA standard. After several rounds of vigorous testing, UTStarcom successfully passed all the Phase I tests in March of 2002, whereby we not only provided a complete 3GPP R99 compliant system, including core networks, (MSC, GSN, HLR, etc.), network management, RNC, Node B, and user equipment emulators, but also demonstrated a total 3G solution with stable and consistent performance with IP transport technology.

As a result, in May 2002, UTStarcom moved onto the MII's Phase II test which focused on interoperability between different vendors and an operator trial. In addition, due to the successful outcome of the Phase I test, UTStarcom secured a 10 MHZ IMT-2000 frequency from the MII to be used for internal research and trials in a few select cities. To date, the two trial systems in Shenzhen and Shanghai are running smoothly, both utilizing commercial grade handsets, and have achieved high-quality voice, data and multimedia services.

UTStarcom also has strategic alliances with Matsushita, interWAVE and Datang Mobile in co-designing and jointly developing WCDMA, CDMA 2000 and TDS-CDMA 3G systems.

Our OEM Products for Metropolitan Area Networks (MANs)

We partner with original equipment manufacturers, or OEMs, which allows us to offer our customers a broader range of products. This OEM strategy allows us to provide benefits to our customers and also allows us to learn about specific technologies and market segments that may help us to shape our overall strategic planning. One such initiative is our program to penetrate China's Metropolitan Area Networks, or MANs, to provide Layer2/Layer3 switches.

Our ACD Products

Our in house design capabilities allow us to continue to develop leading carrier class broadband access solutions. ACD products and development are synergetic with the overall system development efforts at UTStarcom. In 2002, ACD successfully launched a new Single LAN Switch chip set.

MARKETS AND CUSTOMERS

China

With anticipated annual gross domestic product growth of 7-8% and a low teledensity of 16.9% for fixed line and 16.1% for mobile, we expect China to continue to be our single largest market in 2003. We expect 70-80% of our revenue will come from China in 2003, although no assurances can be provided in this regard. In addition to a China-based engineering force, we had 21 direct sales offices throughout China staffed by nearly 1,000 sales and service representatives as of December 31, 2002.

Our PAS systems are deployed in 21 provinces in China. At December 31, 2002 there were approximately 7.5 million subscribers.

We are also a strong competitor in DSLAM and IP-DSLAM product, with 80,000 lines deployed.

Furthermore, we are competitively positioned for our 3G offerings due to our incumbent position as the largest wireless provider to the fixed line operators with our mSwitch-based iPAS system that ensures easy migration to the next generation IP core network.

Geographically, we provide our communications equipment to local telecommunications companies in a wide variety of provinces of China. Market opportunities within China's 31 provinces vary greatly by region, with the more densely populated coastal provinces experiencing the strongest economic development. However, as China extends development to the western part of the country, we have expanded our focus from the more prosperous eastern coastal regions of China, including Guangdong, Zhejiang, Fujian, Shandong, and Jiansu, to almost all inland provinces in the western part of China. While each of the local telecommunications companies is part of the China Telecom or China Netcom systems and subject to their management control, equipment purchasing decisions for most of these provinces are generally made at the local level.

Vietnam

UTStarcom entered the Vietnam market in 2002, winning contracts worth more than $20.5 million from Vietnam Post and Telecommunications (VNPT). VNPT is deploying UTStarcom's IP-based PAS technology in two major cities Hanoi, with a population of 4 million, and Ho Chi Minh City, with a population of 6.5 million. In addition, UTStarcom is implementing its AN-2000 Network Solution in Ho Chi Minh City and installing another for trials in Hanoi.

The economy of Vietnam, which has a total population of nearly 80 million, is growing at 7% annually. Vietnam is the second-fastest-growing telecommunications market in the world after China, yet it has a teledensity of less than 5%.

India

UTStarcom has successfully implemented its mSwitch, PAS, and AN-2000 solutions in India. We have either implemented our products or conducted trials with Reliance, BSNL, MTNL, Tarta and Shanym, who are among India's eight basic service operators. We believe we have successfully positioned ourselves to rapidly expand the breadth and depth of our Indian operations.

In addition, we have built a major research and development facility in Gurgaon, on the outskirts of New Delhi, that focuses on developing the India market and global research and development initiatives. We have also established local manufacturing of our AN-2000 technology in association with Himachal Futuristic Communications Limited.

Japan

Yahoo! BB, the leading provider of broadband service in Japan, has deployed UTStarcom's AN-2000 IB IP-DSLAM equipment to support its 12 Mbps ADSL service. According to the Ministry of Public Management, Home Affairs, Posts and Telecommunications in Japan, Yahoo! BB reached more than one million subscribers by September 2002, less than 13 months after the service was introduced.

The following table is a list of our customers who purchased more than $1.0 million of our products in 2002.

Fujian Province

Fu Jiang Zhang Zhou Telecommunication Bureau
Fujian Hongyu Group Company
Fujian Longyan TB
Fujian Net-Com Material ltd.
Fujian Quanzhou TB
Fujian Sanming PTC

Gansu Province

Gan Su Lan Zhou Telecommunication Bureau
Gan Su Bai Yin Telecommunication Bureau
Gan Su Tian Shui Telecommunication Bureau

Guangdong Province

Guang Dong Jiang Men Telecommunication Bureau
Guang Dong Shao Guan Telecommunication Bureau
Guang Dong Zhao Qing Telecommunication Bureau
Guangdong Telecommunication Bureau Group Zhuhai Branch

Guangxi Province

Guangxi He Zhou Telecommunication Bureau
Guang Xi Gui Lin Telecommunication Bureau
Guang Xi Nan Ning Telecommunication Bureau
Guang Xi Wu Zhou Telecommunication Bureau
Guangxi Hechi Zone Telecom Indust. Company
Guangxi Qinzhou Com. Indus. Company
Guangxi Telecommunication Bureau Baise Branch
Guangxi Telecommunication Bureau Guigang Branch
Guangxi Telecommunication Bureau Liuzhou Branch

Hainan Province

Hainan Haikou Telecommunication Bureau
Hainan Telecommunication Bureau

Hebei Province

ShiJiazhuang Telecommunication Bureau
Hebei Baoding Customers
Hebei Handan PTC
Hebei Langfang Telecommunication Bureau

Heilongjiang Province

HeiLongjiang Haerbin Telecommunication Bureau

Henan Province

He Nan Luo Yang Telecommunication Bureau
Henan Telecom Material Ltd.
Henan Telecom. Jiaozuo Company
Henan Xinxiang Com. Material Maintenance Company
Henan Zhengzhou WeiKemu Company

Hubei Province

Huangshi Telecommunication Bureau
Hubei Telecom Huanggang Branch
Hubei Telecom Yichang Branch
Shiyan Telecommunication Bureau
Xiangfan Telecommunication Bureau

Jiangsu Province

Jiang Su Nan Tong Telecommunication Bureau
Jiang Su Yang Zhou Telecommunication Bureau
Jiangsu Jubang Zixun Indust. Ltd.
Jiangsu LianYungang Guomai Com.
Jiangsu Taizhou Telecommunication Bureau
Jiangsu Xuzhou Telecommunication Bureau Yongan Branch
Nantong Post Material Company

Jiangxi Province

Jiang Xi Gan Zhou Telecommunication Bureau
Jiangxi Telecom.Yichun Branch
Jiangxi Telecom. Pingxiang Branch
Jiang Xi Shang Rao Telecommunication Bureau
Jiang Xi Xin Yu Telecommunication Bureau
Jiang Xi Ying Tan Telecommunication Bureau
Jiangxi Nanchang Telecom Indust. Ltd.
Jiangxi Telecom. Jiujiang Branch
Jiang Xi Ji An Telecommunication Bureau

Jilin Province

Jilin Siping Com. Indust. Company

Liaoning Province

Liaoning Benxi Telecom Branch
Liaoning Post Material Group Panjin Company

Neimenggu Province

Dongsheng
Huhehaote Bibo Telecom Company
Neimenggu Huhehaote Telecommunication Bureau
NeiMenggu Wide Band

Ningxia Province

Ningxia Telecommunication Bureau

Shandong Province

Jinan Zhongheng Shopping Center Zhongxun Electronic
Shan Dong De Zhou Telecommunication Bureau
Shan Dong Ji Nan Telecommunication Bureau
Shan Dong Liao Cheng Telecommunication Bureau
Shan Dong Telecommunication Bureau
Shan Dong Zi Bo Telecommunication Bureau
Shandong Jining PTelecommunication Bureau Lutong Ltd.
Shandong Linyi Telecom. Lutong Ltd.
Shandong Telecom Jining Branch
Shandong Tonglian Inf. Indus. Group Material Company
Shandong Weihai Telecom Lutong Ltd.
Shandong Yantai Telecom Lutong Ltd.

Shanxi Province

Jinzhong Telecommunication Bureau
Shanxi Datong Telecommunication Bureau
Shanxi Jincheng Telecom Branch
Shanxi Lvliang
Shanxi Taiyuan Telecommunication Bureau
Shanxi Xinyuan Com. Trade Ltd.

Sichuan Province

Chengdu Fuchuan Com. Developing Ltd.
Chengdu Guowei Industrial Ltd.
Chengdu Homeclub Com. Material Ltd.
Chengdu Lantian Information Tech. Project Ltd.
Chengdu Taili PT Field Ltd.
China Post Material Southwest Company
Fu Jiang Pu Tian Telecommunication Bureau
Si Chuan Nei Jiang Telecommunication Bureau
Si Chuan Telecommunication Bureau
Si Chuan Yi Bin Telecommunication Bureau
Si Chuan Zi Gong Telecommunication Bureau
Si Chuan Zi Yuang Telecommunication Bureau
Sichuan Chengdu Telecommunication Bureau
Sichuan Hengtong Telecom Tech. Developing Company
Sichuan Litong S&T Ltd.
Sichuan Telecommunication Bureau PanZhihua Branch

Tibet Province

Tibet Changdu Telecom Branch

Shan Xi Province

Shan Xi Han Zhong Telecommunication Bureau
Shan Xi Telecommunication Bureau
Shan Xi Tong Chuan Telecommunication Bureau
Shan Xi Xi An Telecommunication Bureau
Shanxi Xi An Tonglian Telecom Ltd.
Xianyang Telecommunication Bureau

Xinjiang Province

Xi Jiang Yi Li Telecommunication Bureau
Xin Jiang Bo Le Telecommunication Bureau
Xin Jiang Ta Cheng Telecommunication Bureau
Xin Jiang Wu Lu Mu Qi Telecommunication Bureau
Xinjiang Aletai Telecommunication Bureau

Xinjiang Dushanzi Telecommunication Bureau
Xinjiang Telecom Hami Branch
Xinjiang Telecom Kelamayi Branch
Xinjiang Telecom Shihezi Branch

Yunnan Province

Banna Telecommunication Bureau
Diqing Telecommunication Bureau
Yunan Chuxiong Telecommunication Bureau
Yunan Dali Telecommunication Bureau
Yunan Telecom Company
Yunnan Kunming Telecommunication Bureau
Yunnan Lincang Telecom Company
Yunnan Telecom Lijiang Branch

Zhejiang Province

Huzhou Telecommunication Bureau
Jiang Su Xu Zhou Telecommunication Bureau
Zhejiang Hangzhou Telecommunication Bureau
Zhejiang Shaoxing Telecommunication Bureau
Zhejiang Telecom. Group Chunan Branch
Zhejiang Telecom. Group Jiande Branch
Zhejiang Telecom. Group Linan Branch
Zhejiang Telecom. Group Ningbo Branch
Zhejiang Telecom. Group Quzhou Branch
Zhejiang Telecom. Group Taizhou Branch
Zhejiang Telecom. Group Wenzhou Branch
Zhejiang Telecommunication Bureau
Zhejiang Xiaoshan Telecommunication Bureau
Zhejiang Yuhang Telecommunication Bureau

Outside Mainland China

BB Technologies Corporation
First International Telecom Corp.
Matsushita Communication Industrial Co. Ltd
Hitron Technologies Inc.
NEC USA, Inc.
Hughes Telecom (India) Ltd.
Himichal Futuristic Communications Ltd.
Corporate Access (HK) Ltd.

For the year ended December 31, 2002, sales to Zhejiang province and BB Technologies Corporation accounted for 18% and 13% our net sales, respectively. Approximately 77.8% of our net sales during 2002 were to entities affiliated with the government of China.

We also sell our network access equipment to service providers in high growth communications markets outside of China. These markets accounted for approximately 16.2% of our net sales in 2002. We have shipped equipment to service providers in Bangladesh, India, Japan, Mauritius, Russia, Taiwan, Thailand and Venezuela. We have also begun trial deployments in the United States and Vietnam.

As of December 31, 2002, our backlog totaled approximately $605.4 million, compared to approximately $360.7 million as of December 31, 2001. We include in our backlog, contracts and purchase orders for which we anticipate delivery to occur within 12 months and products delivered but for which final acceptance has not yet been received. Because contracts and purchase orders are generally subject to cancellation or delay by customers with limited or no penalty, our backlog is not necessarily indicative of future revenues or earnings.

SALES, MARKETING AND CUSTOMER SUPPORT

We pursue a direct sales and marketing strategy in China, targeting sales to individual Telecommunications Bureaus and to manufacturers or equipment distributors with closely associated customers. We maintain sales and customer support sites in Beijing, Chengdu, Fuzhou, Guangzhou, Hangzhou, Jinan, Kunming, Nanning, Nanjing, Inner Mongolia, Shanghai, Shenyang, Wuhan, Xian, and Zhengzhou. We also sell through relationships with regional government-owned telecommunications manufacturing companies, which act as agents in the sale of our products to Telecommunications Bureaus.

We believe our customer support services in China allow us to offer our customers high service quality. Our customer service operation in Hangzhou is co-located with our manufacturing joint venture and serves as both a technical resource and liaison to our product development organization. In China, customer service technicians are distributed in the regional sales and customer support sites to provide a local presence. We provide additional support on a 24-hour, 365-day basis from our customer support center in Hangzhou in the form of field dispatch personnel, who also provide training on installation, operation and maintenance of equipment. As of December 31, 2002, we employed 1,103 people in sales, marketing and customer support in China.

Our sales efforts in markets outside of China combine direct sales, original equipment manufacturers, distributors, resellers, agents and licensees. We maintain sales and customer support sites in Iselin, New Jersey to address North American markets; in Tokyo, Japan to address the Japan market; in Gurgaon, India to address the Indian market; in Miami, Florida and Mexico City, Mexico to address the Latin American markets; in Frankfurt, Germany to address the European and African markets; in Manila, Philippines to address the Philippine market; in Taipei, Taiwan to address the Taiwan market; in Hanoi, Vietnam to address the Vietnam market; and in Shanghai, China to address other Pacific Rim markets.

Our customer service operations in the U.S. and Hangzhou, China support our customers outside of mainland China with training, project supervision and problem resolution. We maintain and will continue to expand our staff of local personnel near customers who require support on a 24-hour, 365-day basis. In many cases our local in-country sales partners also provide customer support.

TECHNOLOGY

We believe the following key technologies have been instrumental in our ability to provide leading broadband wireline and wireless access networks and IP-based switching systems.

X-over-IP. X-over-IP refers to the transmission of various forms of traffic, including voice, video, fax, music and broadcast, over IP networks. An X-over-IP network requires the following equipment:

- media gateways at the edge of the network that convert legacy media like telephone lines, fax and data modems, or other non-IP data interfaces to IP and incorporate quality of service functionality designed to avoid delay and packet loss due to congestion;

- softswitching adds intelligence to a network platform, supporting a wide arry of functions which include address translation, service monitoring and assurance, billing, authorization, supplementary services like call forwarding, conferencing, and other signaling translations; and

- an IP network that provides high speed IP routing and transmission.

Our mSwitch platform provides the media gateway and the softswitching server and, when combined with industry-standard IP routers, creates a complete X-over-IP network.

The mSwitch gateway converts incoming TDM formats from POTS, ISDN, SS7 and leased lines into packetized voice over IP. The packetization process utilizes programmable digital signal processors that can code voice, fax and standard 56Kbps modem signals into IP. The gateway also terminates the associated TDM format signaling protocols and generates IP based signaling protocols like H.323, MGCP and SIP. The mSwitch gateway also provides IP routing functions that allow the IP packets to penetrate deeper into the core network with queuing, and route selection, consistent with the desired quality of service for each particular call.

The mSwitch softswitch provides switching intelligence to manage the calls in the network as they progress from gateway to gateway. The mSwitch operations support system provides the database management for service provisioning, authorization and flexible billing.

Service providers are increasingly offering X-over-IP services to reduce costs, reduce obsolescence, provide easier upgrades and generate incremental revenue through value-added voice and data services.

Softswitch Mobility Management. We are a founding member of the International Softswitch Consortium, an industry group formed to promote compatibility and interoperability of softswitch technologies. Based on our knowledge of the industry, we believe we are one of the first companies to develop a softswitch architecture to support mobile applications.

Softswitches control the signaling and call management functions in an X-over-IP network. Of the many possible types of softswitching services, mobile telephony and information delivery services are among the most demanding and complex. Mobile networks must track subscribers' locations dynamically whether or not they are on a call. They must provide real-time handovers between base stations, perform authorization of roaming visitors, provide real-time billing for pre-paid services and flexible routing to its roamers in foreign networks and support messaging, file transfer and assignment of data bandwidths. Based on our knowledge of the industry, we believe that our mSwitch platform is one of the first systems to provide mobile switching functionality.

mSwitch employs our proprietary, object oriented signaling protocol for mobility, known as SNSP, which we believe provides advantages over other similar protocols. mSwitch is commercially deployed

with mobility support for our PAS wireless infrastructure. The mSwitch gateway is also being developed to support the future WCDMA and TD-SCDMA radio network control protocols as well as the payload protocols for 3G. mSwitch will serve as an IP-based, mobile switching center and IP-based radio network controller. With this focus on mobility services, mSwitch is targeting one of the most complex and commercially important segments of softswitch applications.

PAS Value-Added Services. PAS offers a full suite of integrated value added services, which are easily customized, including short message services, location services, web browsing, e-mail, voice mail, and 64Kbps Internet access.

IP-switching and Transport. In support of the basic trends outlined above, we are also engaged in developing products to switch and transport IP traffic. We have introduced an IP-DSLAM which helps bring high speed IP services directly to consumer and residential users using ADSL, and are pursuing other xDSL technologies such as VDSL and G.SGDSL. In addition, we have developed products that provide Layer 2 and Layer 3 IP switching, and are working on products which will provide fiber interfaces in support of an overall FTTx standards initiative.

RESEARCH AND DEVELOPMENT

We believe that continued and timely development and introduction of new and enhanced products are essential if we are to maintain our competitive position. While we use competitive analyses and technology trends as factors in our product development plans, the primary input for new products and product enhancements comes from soliciting and analyzing information about service providers' needs. Our Ministry of Information Industry, Telecommunications Administration and Telecommunications Bureau relationships and Chinese full-service post-sale customer support provide our research and development organization with insight into trends and developments in the marketplace. The insight provided from these relationships allows us to develop market-driven products such as PAS, mSwitch and IP-DSLAM. We maintain a strong relationship between our research centers in the U.S. and China. We rotate engineers between the U.S. and China to further integrate our research and development operations. We have been able to cost-effectively hire highly skilled technical employees from a large pool of qualified candidates in China. We have also started a development center in Gurgaon, India to take advantage of the talent pool available there, and to support our operation in India.

In the past we have made, and expect to continue to make, significant investments in research and development. Our research and development expenditures totaled $86.2 million in 2002, $59.8 million in 2001 and $41.5 million in 2000.

MANUFACTURING, ASSEMBLY AND TESTING

We manufacture or engage in the final assembly and testing of our mSwitch, PAS systems and handsets and AN-2000 products at our manufacturing facility in the Chinese province of Zhejiang. The manufacturing operations consist of circuit board assembly, final system assembly, software installation and testing. We assemble circuit boards primarily using surface mount technology. Assembled boards are individually tested prior to final assembly and tested again at the system level prior to system shipment. We use internally developed functional and parametric tests for quality management and process control and have developed an internal system to track quality statistics at a serial number level.

Our manufacturing facility is ISO 9002 certified. ISO 9002 certification requires that the certified entity establish, maintain and follow an auditable quality process including documentation requirements, development, training, testing and continuous improvement which is periodically audited by an independent outside auditor.

We contract with third parties in China to undertake high volume assembly and manufacturing of our handsets and we conduct final assembly, testing and packaging at our own facilities. In addition, we generally use third parties for high volume assembly of circuit boards. HonXun Electrical Industry in Hangzhou, a subsidiary of Foxconn Group, manufactures our PAS handsets; Eastcom Communications manufactures our PAS handsets; and Shanghai Jingling Electronic manufactures line cards for our IP-ADSL product.

We have also contracted with Mitsubishi Electric Corporation to provide PAS wireless base station components for distribution under the UTStarcom label. Other suppliers include Wistron NeWeb Corporation and Sanyo Electric Co., Ltd., which provide handsets under the UTStarcom label. Our AN-2000 product line integrates some third party products for subscriber premises equipment and testing. In China, we undertake final assembly and test our wireless infrastructure products at our own facilities and have recently begun to manufacture some of these products ourselves.

STRUCTURE AND REGULATION OF THE TELECOMMUNICATIONS INDUSTRY IN CHINA

Structure of China's Telecommunications Industry. Historically, the China Telecom system was the sole provider of public telecommunications services in China. In 1993, the State Council, in an effort to promote competition, began issuing licenses to new telecommunications operators including China United Telecommunications Corporation, or Unicom, a provider of mobile communication services, and Jitong Communications Co., Ltd., a provider of data communications and Internet access services.

In February 1999, the State Council approved a restructuring plan for the China Telecom system, under which the telecommunications operations of the China Telecom system were separated along four business lines: fixed line, mobile, paging and satellite communications services. Following the announcement, we observed a reduction in orders from Telecommunications Companies, which we attributed to the uncertainties surrounding the restructuring and the ultimate impact the restructuring would have on the Telecommunications Companies.

The Ministry of Information Industry confirmed in December 2001 that the State Council had approved a plan to restructure China Telecom. The Ministry of Information Industry has been authorized to execute the plan. China Telecom was split into two regional entities. The assets of the present China Telecom in North China's Beijing and Tianjin municipalities, the Inner Mongolia Autonomous Region and Hebei and Shanxi provinces, Northeast China's Liaoning, Jilin and Heilongjiang provinces, Central China's Henan Province and East China's Shandong Province were merged with China Netcom Co. Ltd. and China Jitong Network Communications Co. Ltd. The new company was named China Netcom Group Corp., or New CNC. China Telecom's assets in the other 21 provinces, municipalities and autonomous regions retained the brand name and intangible assets of the old China Telecom. We refer to this entity as the New China Telecom. The New CNC inherited 30% of the old China Telecom's national backbone network, with the rest going to the New China Telecom. As this change is relatively recent and its implementation is ongoing, we cannot be certain what the final impact of this restructuring will be on our business operations. However, we may experience a decline in orders and related revenues during such restructuring as a result of uncertainty among our customers presently operating under China Telecom.

New CNC and New China Telecom will continue to operate through each of their own regional networks of approximately 2,400 local level telephone companies called Telecommunications Bureaus. Telecommunications Bureaus are responsible for purchasing, installing and operating the voice and data communications services in their local markets. Local telephone companies are funded by their own operational revenue from local telephone charges, a portion of shared long distance revenue through settlement, and headquarter allocation and cross subsidy, particularly in remote and poor regions. Among the funding sources, local revenue accounts for the majority of the revenue for local telephone companies.

In November of 2002, China Telecom and four of its subsidiaries became listed on the Hong Kong and New York stock exchanges.

Government Regulation of the Telecommunications Industry. The China telecommunications industry is regulated at the national, provincial and local levels. At the national level, the Ministry of Information Industry regulates the industry. The Ministry of Information

Industry was established in March 1998 to assume the regulatory, administrative and other governmental duties of the former Ministry of Posts and Telecommunications. The Ministry of Information Industry has broad discretion and authority to regulate all aspects of the telecommunications and information technology industry in China, including managing spectrum bandwidths, setting network equipment specifications and standards and drafting laws and regulations related to the electronics and telecommunications industries. Additionally, the Ministry of Information Industry can decide what types of equipment may be connected to the national telecommunications networks, the forms and types of services that may be offered to the public, the rates that are charged to subscribers for those services and the content of material available in China over the Internet. Based on our industry experience, we believe that the Ministry of Information Industry's general telecommunications equipment strategy is to ensure that China's infrastructure is based on advanced open architectures that are expandable, cost efficient and quickly deployed.

The Ministry of Information Industry also oversees the 31 Telecommunications Administrations that have regulatory responsibility over the telecommunications industry in their respective provinces. In China today, each Telecommunications Administration approves a subset of telecommunications products that meet Ministry of Information Industry standards from which Telecommunications Bureaus can then select the specific products they purchase, install and operate. Although historically the Ministry of Information Industry has shared regulation and operation of China's telecommunications industry with the China Telecom system, as part of the Chinese government's industry restructuring, the regulatory functions of the Ministry of Information Industry and the Telecommunications Administrations have been separated from the operational functions of the state-owned Telecommunications Bureaus under their control. The Ministry of Information Industry acts exclusively as the industry regulator and the local Telecommunications Bureaus act exclusively as operators. Given the multi-level regulatory environment, equipment providers in China must generally market intensively to all three levels of the communications industry.

Statutory Framework. China does not yet have a national telecommunications law. However, with China's recent entry into the World Trade Organization, or WTO, the Ministry of Information Industry, under the direction of the State Council, must present a draft Telecommunications Law of the People's Republic of China for ultimate submission to the National People's Congress for review and adoption. In order to comply with the WTO, subsets of draft telecommunications regulations were published in December 2001. One of the most significant of the draft regulations is the "Regulation of Foreign Investment over Telecom Enterprises." In December 2001, the State Council promulgated the Provisions on the Regulation of Foreign Invested Telecommunications Enterprises, which lifts the restrictions on foreign investment in the telecommunication industry, subject to certain equity ratio and geographic limitations. Also in December 2001, the Ministry of Information Industry issued the Measures on Regulation of Telecommunication Business Operation Permits, which details the procedures for obtaining permits for the operation of telecommunications businesses and makes it possible for those conducting telecommunications business to obtain the relevant permits. As we provide equipment rather than services, these two regulations should not have a direct effect on our business. Nevertheless, as the two regulations came into effect only recently, we are uncertain whether we will be indirectly affected by the impact of the two regulations on telecom service providers.

Currently, the governing regulation over telecommunications in China is the Telecommunications Regulations of the People's Republic of China issued by the State Counsel in September 2000. This set of regulations is known as the Telecom Regulations. The Telecom Regulations govern

telecommunications services and market regulations, pricing, interconnection and connection, as well as telecommunications construction and security issues. These regulations are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. As with the Telecommunications Law, we are uncertain what effect, if any, the Telecom Regulations will have on our business as presently conducted.

Licenses for Communication Equipment. Beginning January 1, 1999, China's government required that all telecommunications equipment connected to public or private telecommunications networks within China, which includes equipment that we sell in China, be approved by the Ministry of Information Industry, and the manufacturer of the equipment obtain a network access license for each of its products. Subsequently, the State Council issued the Telecom Regulations in September 2000. In May 2001, the Ministry of Information Industry issued the Administrative Measures of Network Access Licenses, known as the Access License Measures, to implement the Telecom Regulations and to replace the old access license regulation. Both the Telecom Regulations and the Access License Measures require the government to implement license systems for telecommunications terminal equipment, wireless communications equipment and equipment used in network interconnection that is connected to public telecommunications networks. The above equipment must meet government and industry standards, and a network access license for the equipment must be obtained. Without the license, the equipment is not allowed to be connected to public networks or sold in China. The Telecom Regulations require that manufacturers ensure that the quality of thetelecommunications equipment for which they have obtained a network access license is stable and reliable, and they may not lower the quality or performance of other installed licensed products. The State Council's product quality supervision department, in concert with the Ministry of Information Industry, performs spot checks to track and supervise the quality of telecommunications equipment for which a network access license has been obtained and publishes the results of such spot checks.

The regulations implementing these requirements are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. We have obtained the required network access licenses for our AN-2000 platform. We have applied for, but have not yet received, a network access license for our PAS system. Based upon conversations with the Ministry of Information Industry, we understand that our PAS system is considered to still be in the trial period and that sales of our PAS system may continue to be made by us during this trial period, but a license will ultimately be required. Network access licenses will also be required for most additional products that we are selling or may sell in China, including our mSwitch platform. If we fail to obtain the required licenses, we could be prohibited from making further sales of the unlicensed products, including our PAS system, in China, which would substantially harm our business, financial condition and results of operations. Our counsel in China has advised us that China's governmental authorities may interpret or apply the regulations with respect to which licenses are required and the ability to sell a product while a product is in the trial period in a manner that is inconsistent with information received by our counsel in China, either of which could have a material adverse effect on our business, financial condition and results of operations.

Software Registration. On October 27, 2000, the Ministry of Information Industry issued the Administrative Regulations on Software Products, known as the Software Regulations, to enhance software product management and stimulate the development of the software industry in China. Under the Software Regulations, the government imposes a registration and filing system on software and products incorporating software. Software cannot be produced and sold in China without registration and filing. The developers and producers of the software are responsible for the registration and filing of domestic software products. Registration under the Software Regulations is valid for five years and can be renewed upon expiration. The Ministry of Information Industry is responsible for the overall management of software. The local offices of the Ministry of Information Industry at the provincial level are responsible for the management and examination of and approval for the registration of the

domestic software within their own territories. The designated agencies authorized by these local offices are responsible for acceptance for registration of software. Before registration is approved by the government agencies, software products need to be tested by the authorized testing institutions.

We have accomplished the necessary registration with regards to the software incorporated in our AN-2000, PAS and mSwitch products. However, additional registration is required for software incorporated in additional products that we are selling or may sell in China. Based upon verbal advice received from the Ministry of Information Industry, we believe that we will be able to continue to sell our products incorporating our software during the period in which these regulations are being implemented and our application is pending. However, this implementation period may not last long enough for us to complete the registration of our software. Moreover, the Chinese government may interpret or apply the Software Regulations in such a way as to prohibit sales of products incorporating our unregistered software prior to registration. If the government prohibits sales pending registration, or if we fail in our efforts to register our software, we could be prohibited from making further sales of products incorporating the unregistered software in China, which could substantially harm our business and financial condition.

COMPETITION

We face intense competition in our target markets and expect competition to increase. Our principal competitors in our various product lines include:

mSwitch: Alcatel Alsthom CGE, S.A.; Cisco Systems, Inc.; Clarent Corporation; Ericsson LM Telephone Co.; Huawei Technology Co., Ltd.; Lucent Technologies, Inc.; Motorola, Inc.; Nokia Corporation; Nortel Networks Corporation; Nuera Communications, Inc.; Siemens AG; Sonus Networks, Inc.; and Zhongxing Telecommunications Equipment.

PAS systems and handsets: Lucent Technologies, Inc. and Zhongxing Telecommunications Equipment.

AN-2000: Advanced Fibre Communications, Inc.; Alcatel Alsthom CGE, S.A.; Datang Telecom Technology Co. Ltd.; Huawei Technology Co., Ltd.; Lucent Technologies, Inc.; and Zhongxing Telecommunications Equipment.

3G: potentially, we will compete with Ericsson LM Telephone Co.; Huawei Technology Co., Ltd.; Lucent Technologies, Inc.; Motorola, Inc.; Nokia Corporation; Nortel Networks Corporation; Siemens AG, Alcatel Alsthom CGE, S.A.; Zhongxing Telecommunications Equipment.

We are increasingly facing competition from domestic companies in China. We believe that our strongest competition comes from these companies, many of which operate under lower cost structures and more favorable governmental policies and have much larger sales forces than we do. Furthermore, other companies not presently offering competing products may also enter our target markets, particularly with the reduction of trade restrictions as a result of China's admission to the WTO. Many of our existing and potential competitors may have significantly greater financial, technical, product development, sales, marketing and other resources than we do. As a result, our competitors may be able to respond more quickly to new or emerging technologies and changes in service provider requirements. Our competitors may also be able to devote greater resources than we can to the development, promotion and sale of new products and offer significant discounts on handsets or other products. These competitors may also be able to offer significant financing arrangements to service providers, in some cases facilitated by government policies, which is a competitive advantage in selling systems to service providers with limited financial and foreign currency resources. Increased competition is likely to result in price reductions, reduced gross profit as a percentage of net sales and loss of market share, any one of which could materially harm our business, financial condition and results of operations.

Moreover, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties, including Telecommunications Administrations, Telecommunications Bureaus and other local organizations, to increase their ability to address the needs of prospective customers in our target markets. Accordingly, alliances among competitors or between competitors and third parties may emerge and rapidly acquire significant market share. To remain competitive, we believe that we must continue to partner with Telecommunications Administrations and other local organizations, maintain a high level of investment in research and development and in sales and marketing, and manufacture and deliver products to service providers on a timely basis and without significant defects. If we fail to meet any of these objectives, our business, financial condition and results of operations could be harmed.

The introduction of inexpensive wireless telephone service or other competitive services in China may also have an adverse impact on sales of our PAS systems in China. We may not be able to compete successfully against current or future competitors. In addition, competitive pressures in the future may materially adversely affect our business, financial condition and results of operations.

We believe that the principal competitive factors affecting the market for our network access products include:

- total initial cost of solution;
- for PAS, the availability, cost and functionality of our handsets;
- short delivery and installation intervals;
- design and installation support;
- ease of integration with the backbone network;
- flexibility in supporting multiple interfaces and services;
- operational cost and reliability; and
- manageability of the solution and scalability.

We may not be able to compete effectively against current and future competitors based on these or any other competitive factors in the future, and the failure to do so would have a material adverse affect on our business, financial condition and results of operations.

INTELLECTUAL PROPERTY

Our ability to compete is dependent in part on our proprietary technology. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as confidentiality agreements and licensing arrangements, to establish and protect our proprietary rights. To date, we have relied primarily on proprietary processes and know-how to protect our intellectual property. We presently hold three U.S. patents and one Taiwanese patent for existing products. The terms of one of the United States patents will expire in 2016, while the terms of the remaining United States patents will expire in 2019. The Taiwanese patent will expire in 2020. We have submitted 35 additional U.S. patent applications and 29 foreign patent applications. In addition, we have, from time to time, chosen to abandon previously filed applications. Patents may not issue and any patents issued may not cover the scope of the claims sought in the applications. Our U.S. patents do not afford any intellectual property protection in China or other international jurisdictions. Moreover, we have applied for but have not yet obtained patents in China and Taiwan. We may not be able to obtain patents in China on our products or the technology that we use to manufacture our products. KDDI, a Japanese service provider, has licensed key technology to us that serves as the base for the MiMi service in Taiwan. Our joint ventures in China rely upon our trademarks, technology and know-how to manufacture and sell our products. Under the terms of our joint venture agreements, any modifications or enhancements to or derivatives

of our intellectual property developed by the joint ventures will be owned by the joint ventures. Any infringement of our proprietary rights could result in significant litigation costs, and any failure to adequately protect our proprietary rights could result in our competitors offering similar products, potentially resulting in loss of a competitive advantage and decreased revenues. Despite our efforts to protect our proprietary rights, existing patent, copyright, trademark and trade secret laws afford only limited protection. In addition, the legal systems of some foreign countries, including China, do not protect our proprietary rights to the same extent as does the legal system of the United States.

Attempts may be made to copy or reverse engineer aspects of our products or to obtain and use information that we regard as proprietary. Accordingly, we may not be able to prevent misappropriation of our technology or deter others from developing similar technology. Furthermore, policing the unauthorized use of our products is difficult. Litigation may be necessary in the future to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. This litigation could result in substantial costs and diversion of resources and could significantly harm our business.

The communications industry is characterized by the existence of a large number of patents and frequent litigation based on allegations of patent infringement. From time to time, third parties may assert patent, copyright, trademark and other intellectual property rights to technologies and in various jurisdictions that are important to our business. Any claims asserting that our products infringe or may infringe proprietary rights of third parties, if determined adversely to us, could significantly harm our business. Any claims, with or without merit, could be time-consuming, result in costly litigation, divert the efforts of our technical and management personnel, cause product shipment delays or require us to enter into royalty or licensing agreements, any of which could significantly harm our business. Royalty or licensing agreements, if required, may not be available on terms acceptable to us, if at all. In the event a claim against us was successful and we could not obtain a license to the relevant technology on acceptable terms or license a substitute technology or redesign our products to avoid infringement, our business would be significantly harmed.

EMPLOYEES

As of December 31, 2002, we employed a total of 3,277 full-time employees. We also from time to time employ part-time employees and hire contractors. Of the total number of full-time employees at December 31, 2002, 1,352 were in research and development, 371 in manufacturing, 1,253 in marketing, sales and support, and 301 in administration. We had 2,750 employees located in China, 405 employees located in the United States, and 122 employees in other countries. Our employees are not represented by any collective bargaining agreement, and we have never experienced a work stoppage. We believe that our employee relations are good.

ITEM 2 PROPERTIES

UTStarcom leases the following facilities:

Location	**Functions**

		Square Footage	Date of Lease Expiration
HEADQUARTERS Alameda, CA	Administration, Sales/Customer Support and Research and Development	25,576	January, 2006
Alameda, CA	Research and Development/Sales	12,690	January, 2004
Fremont, CA	Research and Development	9,688	June, 2005
Iselin, NJ	Sales/Customer Support and Research and Development	48,991	July, 2004
Eatontown, NJ	Research and Development	13,375	October, 2005
Shenzhen, China	Research and Development	107,596	September, 2004
Shenzhen, China	Research and Development	3,660	April, 2004
Hefei, China	Research and Development	3,606	June, 2004
Hefei, China	Research and Development	3,767	July, 2005
Gurgaon, India	Research and Development	5,723	March, 2005
Gurgaon, India	Research and Development	5,479	December, 2005
Shanghai, China	Research and Development	15,421	December, 2007
Hangzhou, China	Administration, Sales/Customer Support, Engineering and Manufacturing	271,589	December, 2004
Hangzhou, China	Administration, Sales/Customer Support, Research and Development, and Manufacturing	269	March, 2004
Hangzhou, China	Administration, Sales/Customer Support, Research and Development, and Manufacturing	168,444	December, 2003
Huizhou, China	Manufacturing	37,728	December, 2002
Beijing, China	UTSC Headquarters Administration, Sales/Customer Support	16,695	July, 2003
Shanghai, China	Sales/Customer Support	8,214	April, 2003
Wuhan, China	Sales/Customer Support	1,658	April, 2003
Guangzhou, China	Sales/Customer Support	11,964	April, 2004
Chengdu, China	Sales/Customer Support	5,199	April, 2004
Jinan, China	Sales/Customer Support	3,229	March, 2003
Kunming, China	Sales/Customer Support	2,676	February, 2003
Xian, China	Sales/Customer Support	4,155	December, 2004
Shenyang, China	Sales/Customer Support	3,122	May, 2003
Fuzhou, China	Sales/Customer Support	4,445	June, 2003
Zhengzhou, China	Sales/Customer Support	2,422	October, 2003

Taipei, Taiwan	Sales/Customer Support	7,769	September, 2004
Hong Kong, China	Sales/Customer Support	800	December, 2002
NanNing, China	Sales/Customer Support	2,293	August, 2003
Nanjing, China	Sales/Customer Support	3,781	May, 2003
Nei Mon Gol, China	Sales/Customer Support	500	December, 2003
Taiyuan, China	Sales/Customer Support	732	February, 2003
Hebei, China	Sales/Customer Support	603	August, 2003
Tianjing, China	Sales/Customer Support	500	July, 2003
HaErBin, China	Sales/Customer Support	1,421	November, 2003
Hsin Chu, Taiwan	Sales/Customer Support (ACD)	2,639	February, 2003
Gurgaon, India	Sales/Customer Support	3,042	June, 2004
Miramar, Florida	Sales/Customer Support	4,796	April, 2006
Tokyo, Japan	Sales/Customer Support	3,217	February, 2004
Hanoi, Vietnam	Sales/Customer Support	2,336	June, 2004
Ho Chi Minh City, Vietnam	Sales/Customer Support	2,594	September, 2004
Bangkok, Thailand	Sales/Customer Support	1,259	August, 2005
Mexico City, Mexico	Sales/Customer Support	130	November, 2003

In 2001, we purchased the rights to use approximately 49 acres of land located in the Zhejiang Science and Technology Industry Garden of Hangzhou Hi-tech Industry Development Zone for a period of 50 years. As of December 31, 2002, we have completed the foundation and ground work and have commenced construction of the building. Construction of the new manufacturing facility is expected to be completed in late 2003. In addition, as we expand into markets outside of China, our facility needs may increase according to business needs.

ITEM 3 LEGAL PROCEEDINGS

On October 31, 2001, a complaint was filed in United States District Court for the Southern District of New York against our company, some of our directors and officers and various underwriters for our initial public offering. Substantially similar actions were filed concerning the initial public offerings for more than 300 different issuers, and the cases were coordinated as *In re Initial Public Offering Securities Litigation*, 21 MC 92. In April 2002 a consolidated amended complaint was filed in the matter against us, captioned *In re UTStarcom, Initial Public Offering Securities Litigation*, Civil Action No. 01-CV-9604. Plaintiffs allege violations of the Securities Act of 1933 and the Securities Exchange Act of 1934 through undisclosed improper underwriting practices concerning the allocation of IPO shares in exchange for excessive brokerage commissions, agreements to purchase shares at higher prices in the aftermarket, and misleading analyst reports. Plaintiffs seek unspecified damages on behalf of a purported class of purchasers of our common stock between March 2, 2000 and December 6, 2000. The claims against our directors and officers have been dismissed without prejudice pursuant to a stipulation. We believe that we have meritorious defenses to this lawsuit and will defend this lawsuit vigorously. Motions to dismiss have been filed on behalf of our company and the other defendants in the coordinated proceeding. Those motions are currently pending with the Court.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

EXECUTIVE OFFICERS OF UTSTARCOM

Our executive officers and directors, and their ages as of December 31, 2002, are as follows:

Name	Age	Position
Masayoshi Son	45	Chairman of the Board of Directors
Hong Liang Lu	48	President, Chief Executive Officer and Director
Ying Wu	43	Vice Chairman of the Board of Directors, Executive Vice President and Chief Executive Officer, China Operations
Michael Sophie	45	Vice President of Finance, Chief Financial Officer and Assistant Secretary
Bill Huang	40	Senior Vice President, Chief Technology Officer
Shao-Ning J. Chou	40	Senior Vice President and Chief Operating Officer, China Operations
Gerald Soloway	54	Senior Vice President, Engineering
Howard Kwock	53	Vice President, Engineering
David A. Robison	37	Vice President, International Sales
Betsy S. Atkins	47	Director
Larry D. Horner	68	Director
Thomas J. Toy	47	Director

MASAYOSHI SON has served as our Chairman of the Board of Directors since October 1995. For more than 16 years, Mr. Son served as President and Chief Executive Officer and as a director of SOFTBANK CORP., a leading global provider of Internet content, technology and services. Mr. Son also serves as a director of BB Technologies Corporation, Yahoo Japan Corporation and Aozora Bank, Ltd. Mr. Son also serves as Chairman of the Board of Directors and Chief Executive Officer of SOFTBANK Holdings Inc. and Chairman of the Board of Directors of SOFTBANK America Inc. From April 1998 to October 1999, Mr. Son served as a director of Ziff-Davis, Inc. Mr. Son holds a B.A. in Economics from the University of California at Berkeley.

HONG LIANG LU has served as our President and Chief Executive Officer and as a director since June 1991. Mr. Lu co-founded UTStarcom under its prior name, Unitech Telecom, Inc., in June 1991 which subsequently acquired StarCom Network Systems, Inc. in September 1995. From 1986 through December 1990, Mr. Lu served as President and Chief Executive Officer of Kyocera Unison, a majority-owned subsidiary of Kyocera International, Inc. From 1983 until its merger with Kyocera in 1986, he served as President and Chief

Executive Officer of Unison World, Inc., a software development company. From 1979 to 1983, he served as Vice President and Chief Operating Officer of Unison World, Inc. Mr. Lu holds a B.S. in Civil Engineering from the University of California at Berkeley.

YING WU has served as our Executive Vice President and Vice Chairman of the Board of Directors since October 1995. Mr. Wu has also served as the President and Chief Executive Officer of one of our subsidiaries, UTStarcom China, since October 1995. Mr. Wu was a co-founder of, and from February 1991 to September 1995 served as Senior Vice President of, StarCom Network Systems, Inc., a company that marketed and distributed third party telecommunications equipment. From 1988 to 1991, Mr. Wu served as a member of the technical staff of Bellcore Laboratories. From 1987 through 1988, Mr. Wu served as a consultant at AT&T Bell Labs. He holds a B.S. in Electrical Engineering from Beijing Industrial University and an M.S. in Electrical Engineering from the New Jersey Institute of Technology.

MICHAEL SOPHIE has been our Vice President of Finance and Chief Financial Officer since August 1999. Prior to joining our company, Mr. Sophie held executive positions at P-Com, Inc. from August 1993 to August 1999 as Vice President Finance, Chief Financial Officer and Group President. From 1989 through 1993, Mr. Sophie was Vice President of Finance at Loral Fairchild Corporation. He holds a B.S. degree from California State University, Chico and an M.B.A. from the University of Santa Clara.

BILL HUANG has been our Chief Technology Officer since September 1999. He was appointed Senior Vice President in September 2001. From December 1996 to September 1999, he was our Vice President of Strategic Product Planning. From June 1995 to December 1996, Mr. Huang served as our Vice President, China Operations. From 1994 to June 1995, Mr. Huang was our Director, Engineering. From 1992 to 1994, he was a Member of the Technical Staff and Project Leader at AT&T Systems. Mr. Huang serves on the board of Shenzhen Gin De (Group) Ltd., Goldfield Industries a real estate investment company in China. Mr. Huang holds a B.S. in Electrical Engineering from Huazhong University of Science & Technology, and an M.S. in Electrical Engineering and Computer Sciences from the University of Illinois.

SHAO-NING J. CHOU has been our Executive Vice President and Chief Operating Officer of China Operations since January 1999. He was appointed Senior Vice President in September 2001. From March 1997 to December 1998, he was Vice President of China Operations and from February 1996 to March 1997, he served as Vice President of Engineering. From March 1995 to June 1996, he was Director of Engineering for wireless systems and software with Lucent Technologies Microelectronics IC group. From April 1993 to March 1995, he was a Technical Manager for the Global Wireless product group with AT&T consumer products where he led multiple development teams for handset and wireless personal base station products. From February 1985 to April 1993, Mr. Chou was team leader and a member of the technical staff for advanced digital communication research in AT&T Bell Laboratories where he led and engaged in data communication equipment and multimedia product development. Mr. Chou holds a B.S. in Electrical Engineering from City College of New York, an M.S. in Engineering from Princeton University and an M.B.A. from the State University of New Jersey, Rutgers.

GERALD SOLOWAY has been our Vice President of Engineering since January 1999. He was appointed Senior Vice President of Engineering in September 2001. From April 1998 to January 1999, he served as our Director of Strategic Marketing. Prior to this, Dr. Soloway worked for Lucent Technologies, formerly Bell Labs, for 29 years. At Lucent, Dr. Soloway held executive positions in Consumer Products, Business Terminal Development, PBX Systems Engineering, Key System Development and Access Systems Development. He holds a Ph.D. from Polytechnic Institute of New York, an M.S. from New York University, and a B.S. from Cooper Union, all in Electrical Engineering. Dr. Soloway also holds seven patents in communications and computer graphics technology.

HOWARD KWOCK was appointed our Vice President of Engineering in September 2001. From March 2001 to September 2001, he served as our Senior Director of Engineering. From February 2000 to February 2001, Mr. Kwock worked as Director of Engineering at Zhone Technologies. From June 1995 to January 2001, Mr. Kwock served as Director of Engineering at Lucent Technologies, formerly Ascend Communications. Mr. Kwock holds a B.A. in Business Administration from California State University, Fullerton.

DAVID A. ROBISON has been our Vice President of International Sales since April 2002. From September 1999 to April 2002, Mr. Robison was Senior Vice President of International Sales and Business Development at Zhone Technologies. From September 1994 to September 1999, Mr. Robison held executive sales positions at Ascend Communications prior to and shortly after its merger with Lucent Technologies where he served as Senior Vice President Network Service Providers, Vice

President Network Service Providers, and Director Internet Service Providers. Mr. Robison studied both electrical engineering and business administration at Purdue University.

BETSY S. ATKINS has served as a director since March 2002. Ms. Atkins has served as Chief Executive Officer of the Operating Group of Accordiant Ventures since 1994. Ms. Atkins is also currently a director of Polycom Inc., and Lucent Technologies, Inc., where she sits on the audit and compensation committees. Ms. Atkins was a founder of Ascend Communications Corp. in 1989 and formerly served as a director. Ms. Aitkins served as a member of the Board of Directors for Olympic Steel from 1988 to 2000, Selectica, Inc. from 1996 to 1999, and Secure Computing, Inc. from 1997 to 1999. Ms. Atkins is a presidential appointee to the Pension Benefit Guarantee Trust Corporation. Ms. Atkins holds a B.A. from the University of Massachusetts.

LARRY D. HORNER has served as a director since January 2000. From 1994 until June 2001, Mr. Horner served as Chairman of Pacific USA Holdings Corp. and as Chairman of the Board and Chief Executive Officer of Asia Pacific Wire & Cable Corporation Limited. He is a director of Phillips Petroleum Company, Atlantis Plastics, Inc. and Newmark Homes Corp. Mr. Horner formerly served as Chairman and Chief Executive Officer of KPMG Peat Marwick from 1984 to 1990. Mr. Horner is a Certified Public Accountant, holds a B.S. from the University of Kansas and is a graduate of the Stanford Executive Program.

THOMAS J. TOY has served as a director since February 1995. Since March 1999, Mr. Toy has served as Managing Director of Pacrim Venture Partners, a professional venture capital firm specializing in investments in the information technology sector. Prior to that he was a partner at Technology Funding, a professional venture capital firm, from January 1987 to March 1999. While at Technology Funding, Mr. Toy was Managing Director of Corporate Finance and headed the firm's investment committee. Mr. Toy also serves as a director of White Electronic Designs Corporation and several private companies. Mr. Toy holds B.A. and M.M. degrees from Northwestern University.

PART II

ITEM 5 MARKET FOR UTSTARCOM, INC.'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Fiscal 2001	**High**	**Low**
First Quarter	$ 28.00	$ 13.56
Second Quarter	27.28	12.50
Third Quarter	25.61	12.98
Fourth Quarter	31.43	15.51
Fiscal 2002		
First Quarter	$ 33.95	$ 20.25
Second Quarter	27.03	18.58
Third Quarter	20.82	12.57
Fourth Quarter	21.10	15.66

Our common stock has been traded on The Nasdaq Stock Market under the symbol UTSI since our initial public offering on March 3, 2000. The preceding table sets forth the high and low closing sales prices per share of our common stock as reported on The Nasdaq National Market for the periods indicated. As of December 31, 2002 we had approximately 141 stockholders of record.

To date, we have not paid any cash dividends on our common stock. We currently anticipate that we will retain any available funds to finance the growth and operation of our business and we do not anticipate paying any cash dividends in the foreseeable future. Certain present or future agreements may limit or prevent the payment of dividends on our common stock.

Equity Compensation Plan Information

The following table sets forth information, as of December 31, 2002, about equity awards under the Company's equity compensation plans:

Plan category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans**

				(excluding securities reflected in column (a))
	(a)		**(b)**	**(c)**
Equity compensation plans approved by security holders (1)	14,903,746(2)	$	15.06	6,294,128(3)
Equity compensation plans not approved by security holders	51,169	$	2.85	115,943(4)
Total	14,954,915	$	15.02	6,410,071

(1) Includes the 1997 Stock Plan which provides for an annual increase in the number of shares available for issuance under the plan equal to the lesser of (i) 4% of the outstanding Shares on such date, (ii) 6,000,000 shares or (iii) a lesser amount determined by the Board, and the 2000 Employee Stock Purchase Plan, which provides for an annual increase in the number of shares available for issuance under the plan equal to the lesser of (i) 2% of the outstanding shares on such date, (ii) 2,000,000 shares or (iii) a lesser amount determined by the Board.

(2) Includes shares of common stock to be issued upon exercise of options granted under our 1995 Stock Plan, 1997 Stock Plan and 2001 Director Option Plan.

(3) Number of securities available for future issuance includes 3,533,857 shares of common stock available for issuance under our 2000 Employee Stock Purchase Plan, 1,955,271 under our 1997 Stock Plan and 805,000 under our 2001 Director Option Plan. See Note 15 of our "Notes to Consolidated Financial Statements" for a description of our equity compensation plans.

(4) Includes 76,067 shares of common stock available for issuance under our Advanced Communication Devices Corporation Incentive Program and 39,876 shares of common stock available for issuance under our Issanni Communications, Inc. Incentive Program.

RECENT SALES OF UNREGISTERED SECURITIES

On October 16, 2002, UTStarcom issued warrants to purchase an aggregate of 857,144 shares of common stock to thirty-nine residents of China who are employees and consultants of our wholly-owned subsidiary, UTStarcom Communication Co., Ltd. The warrants were exercisable for an aggregate of 857,144 shares of our common stock at an exercise price of $0.01 per share and were issued in partial consideration for their agreement to become employees or consultants of UTStarcom Communication Co., Ltd. On October 17, 2002, UTStarcom issued 857,144 shares of common stock pursuant to the exercise of all of such warrants a portion of which is subject to a right of repurchase by UTStarcom that lapses over time or upon the achievement of certain milestones.

The sales and issuances of securities in the transactions described above were deemed to be exempt from registration under the Securities Act of 1933, as amended, by virtue of Regulation S promulgated thereunder, as transactions not involving the issuance of securities to U.S. persons and not involving any public offering. Each purchaser represented that he or she is not a U.S. persons as defined in Regulation S and that his or her intention was to acquire the securities for investment only and not with a view to the distribution thereof.

ITEM 6 SELECTED CONSOLIDATED FINANCIAL DATA

You should read the selected consolidated financial data set forth below in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements and the Notes thereto included elsewhere in this report. Historical results are not necessarily indicative of results that may be expected for any future period.

	Years Ended December 31,				
	1998	1999	2000	2001	2002
	(in thousands, except per share data)				
Consolidated Statement of Operations Data:					
Net sales	$ 105,167	$ 187,516	$ 368,646	$ 626,840	$ 981,806
Gross profit	41,025	74,813	128,181	224,548	345,472
Operating income	3,013	16,719	33,780	76,728	145,962
Income from continuing operations	593	13,119	27,993	56,954	107,862
Net income (loss) available to common stockholders	(300)	(18,514)	27,013	56,954	107,862
Basic earnings (loss) per share:					
Income (loss) from continuing operations	$ 0.08	$ (1.94)	$ 0.35	$ 0.56	$ 0.98
Income (loss) from discontinued operations	(0.12)	(0.19)			
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"			(0.01)		
Net income (loss)	$ (0.04)	$ (2.13)	$ 0.34	$ 0.56	$ 0.98
Diluted earnings (loss) per share:					
Income (loss) from continuing operations	$ 0.01	$ (1.94)	$ 0.28	$ 0.52	0.94
Income (loss) from discontinued operations	(0.01)	(0.19)			
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"			(0.01)		
Net income (loss)	$	$ (2.13)	$ 0.27	$ 0.52	$ 0.94
Proforma amounts assuming application of SAB101, "Revenue Recognition in Financial Statements" is applied retroactively:					
Net income (loss) available to common stockholders	$ (300)	$ (19,494)	$ 27,993	$ 56,954	$ 107,862
Earnings (loss) per share:					
Basic	$ (0.04)	$ (2.25)	$ 0.35	$ 0.56	$ 0.98
Diluted	$	$ (2.25)	$ 0.27	$ 0.52	$ 0.94
Weighted average shares used in per share calculations:					
Basic	7,582	8,678	79,696	101,433	109,566
Diluted	77,050	8,678	101,867	108,612	114,407

	As of December 31,				
	1998	1999	2000	2001	2002
	(in thousands)				
Cash and cash equivalents	$ 17,626	$ 87,364	$ 149,112	$ 321,136	$ 231,944
Working capital	57,416	128,973	369,861	591,103	568,215
Total assets	142,121	271,788	591,837	1,005,880	1,305,552

	As of December 31,				
Total short-term debt	38,426	43,338	43,381	58,434	
Long-term debt			12,048	12,048	
Total stockholders' equity	72,336	165,720	412,319	681,887	766,395

ITEM 7 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. These statements are based on information that is currently available to management. We intend such forward-looking statements to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, and we are including this statement for purposes of complying with those provisions. The forward-looking statements include, without limitation, those concerning the following: our expectations as to the nature of possible trends, the manner in which customers in Chinese provinces negotiate for the purchase of our products; our expectation regarding continued growth in our business and operations; our expectation that our PAS and iPAS network access systems will continue to be allowed in China's county-level cities and counties; our expectation that there will be no penalties or fines for our non-compliance with the licensing requirements in China for our PAS system and other products; our expectation concerning the anticipated cost and completion date of our new Hangzhou manufacturing facility; our expectation that there will be fluctuations in our overall gross profit, gross margin, product mix, quarter to quarter results, customer base and selling prices; our plans for expanding the direct sales organization and our selling and marketing campaigns and activities; our expectation that we may use part of the net proceeds of our initial and follow on public offerings to acquire or invest in complementary businesses, technologies or product offerings; our expectation that there will be increases in selling, marketing, research and development, general and administrative expenses; our expectation that we will continue to invest significantly in research and development; our expectation that we will fill the majority of our current backlog orders; our expectation regarding our future investments; and our expectation that existing cash and cash equivalents will be sufficient to finance our operations for at least the next 12 months. Additional forward-looking statements may be identified by the words, "anticipate," "expect," "believe," "intend," "will" and similar expressions, as they relate to us or our management. Investors are cautioned that these forward-looking statements are inherently uncertain. These statements are subject to risks and uncertainties that may cause actual results and events to differ materially. For a detailed discussion of these risks and uncertainties, see the "Factors Affecting Future Operating Results" section of this Form 10-K. We do not guarantee future results and undertake no obligation to update the forward-looking statements to reflect events or circumstances occurring after the date of this Form 10-K.

OVERVIEW

Incorporated in 1991, UTStarcom designs, manufactures, and markets leading Broadband, Narrowband, wireless, Softswitch, and 3G products that support both fixed-line and mobility at the local loop while offering a clean migration path to next-generation IP-based networks. Our operations are conducted primarily by our foreign subsidiaries that manufacture, distribute and support our products, principally in China. Our systems and products allow service providers to offer cost-efficient and expandable voice, data and Internet access services. Because our systems are based on widely adopted international communications standards, service providers can easily integrate our systems into their existing networks and deploy our systems in new broadband, Internet Protocol and wireless network rollouts.

Since our incorporation, we have focused our resources on developing products for China's communications market. We shipped our first network access products in 1993. In 1995, we acquired StarCom Network Systems, Inc. and changed our name to UTStarcom, Inc. In 1996, we introduced our advanced, V5.1 and V5.2 compliant, multi-service network access platform, the AN-2000. Late in 1996, we introduced our PAS wireless access system. In December 1999, we completed the acquisition of the portion of our Wacos, Inc. subsidiary owned by the minority shareholders. Wacos, Inc. is a research and development subsidiary that develops IP-based switching systems. In November 2001, we completed the

acquisition of Advanced Communications Devices Corporation, or ACD, for $21.3 million. ACD is a system on chip semi-conductor company focusing on LAN and IP switching technology. On April 19, 2002, the Company completed the purchase of Issanni Communications, Inc. ("Issanni"). Our investment in Issanni was $2.0 million prior to the acquisition. The purchase consideration for all the outstanding shares of Issanni, other than those already held by us prior to the acquisition, was $2.1 million. In addition, $2.0 million will be payable in the form of an earnout to all Issanni shareholders of record at closing, subject to the completion of certain performance milestones during 2002, 2003 and 2004.

On December 18, 2001, we entered into an agreement to acquire the remaining 49% ownership interest in GUTS, one of our two primary manufacturing facilities in China, for a total consideration of $3.6 million in cash, in order to achieve 100% ownership in the joint venture. On January 21, 2002, we entered into an agreement to acquire the remaining 12% ownership interest in HUTS, our other manufacturing facility, for a total consideration of $14.5 million in cash. As a result of the GUTS and HUTS transactions, which closed in the second quarter of 2002, we now conduct our operations in China through wholly owned subsidiaries.

We have derived most of our revenues from sales of telecommunications equipment to service providers in China. However, we continue to expand our sales to service providers in other growing communications markets outside of China, including Japan, Taiwan, Vietnam, India and Latin America. Our customers often make a large initial purchase of our equipment followed by supplemental purchases of enhancements and upgrades. As a result, our largest revenue-producing customers typically vary from period to period. The evaluation period for our products by potential customers may span a year or more and our business generally depends on a relatively small number of large deployments. We sell our products in China through a direct sales force.

Approximately 83.8%, 90.3% and 98.8% of our net sales for the years ended December 31, 2002, 2001 and 2000, respectively, were in China. Accordingly, our business, financial condition and results of operations are likely to be influenced by the political, economic and legal environment in China, and by the general state of China's economy. Our results may be adversely affected by, among other things, changes in the political, economic, competitive and social conditions in China, including changes in governmental policies with respect to laws and regulations, changes in telecommunications industry and regulatory rules and policies, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation. We extend credit to our customers in China without requiring collateral. We monitor our exposure for credit losses and maintain allowances for doubtful accounts.

We have historically considered local telecommunications service providers serving municipalities and counties to be our primary customers in China. Recently, however, the provincial-level telecommunications service entity in the Zhejiang province of China has begun to consolidate telecommunications purchasing decisions for that province. As a result of this trend in the Zhejiang province, we have grouped all customers in Zhejiang province together and have treated these as one customer. Giving effect to this treatment, for the year ended December 31, 2002, sales to Zhejiang province and BB Technologies Corporation accounted for 18% and 13% of net sales, respectively. For the year ended December 31, 2001, Zhejiang province accounted for 24% of net sales. For the year ended December 31, 2000, sales to Hangzhou PTT accounted for 12% of net sales. At December 31, 2002, we have approximately thirty-three customers in Zhejiang province.

Whether this represents the beginning of a greater trend throughout China towards increased consolidation of negotiations and purchasing decisions into the control of provincial-level telecommunications service entities is unclear. To our knowledge, no telecommunications service entities in the other Chinese provinces in which we operate have centralized this process at this time. However, the nature of negotiations in China is still evolving. If a trend toward consolidation of purchasing decisions into the control of provincial-level telecommunications service entities in China does emerge, it could possibly take a variety of forms. For example, some provincial-level telecommunications service entities could simply coordinate purchase decisions to be made by local

telecommunications service providers, with local service providers retaining ultimate control over purchasing decisions. In other cases, however, provincial-level entities could wield greater control over the decision of whether or not to purchase our products. In any event, such a trend could streamline the negotiation process within Chinese provinces, but it could also place downward pressure on the prices we can charge for our products. We will continue to monitor business practices in China closely, and to the extent that any of these changes affect the manner in which our customers make their decisions about whether or not to purchase our products, we will re-evaluate what entities may best be described as our customers.

Under China's current regulatory structure, the communications products that we offer in China must meet government and industry standards, and a network access license for the equipment must be obtained. Without the license, the equipment is not allowed to be connected to public telecommunications networks or sold in China. Moreover, we must ensure that the quality of the telecommunications equipment for which we have obtained a network access license is stable and reliable, and may not lower the quality or performance of other installed licensed products. The State Council's product quality supervision department, in concert with the Ministry of Information Industry, performs spot checks to track and supervise the quality of licensed telecommunications equipment and publishes the results of such spot checks.

The regulations implementing these requirements are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. We have obtained the required network access licenses for our AN-2000 platform. We have applied for, but have not yet received, a network access license for our PAS systems and handsets. Based upon conversations with the Ministry of Information Industry, we understand that our PAS systems and handsets are considered to still be in the trial period and that sales of our PAS systems and handsets may continue to be made by us during this trial period, but a license will ultimately be required. Network access licenses will also be required for most additional products that we are selling or may sell in China, including our mSwitch platform. If we fail to obtain the required licenses, we could be prohibited from making further sales of the unlicensed products, including our PAS systems and handsets, in China, which would substantially harm our business, financial condition and results of operations. Our counsel in China has advised us that China's governmental authorities may interpret or apply the regulations with respect to which licenses are required and the ability to sell a product while a product is in the trial period in a manner that is inconsistent with the information received by our counsel in China, either of which could have a material adverse effect on our business, financial condition and results of operations.

Remittances from China which are of a capital nature, such as the repayment of bank loans denominated in foreign currencies, require approval from appropriate governmental authorities before Renminbi can be used to purchase foreign currency. Although the payment of cash dividends is permitted so long as our subsidiaries have sufficient reserves and adequate amounts of Renminbi to purchase foreign currency, regulations restrict the ability of our subsidiaries to transfer funds to us through intercompany loans and advances.

Business activity in China and many other countries in Asia declines considerably during the first quarter of each year in observance of the Lunar New Year. As a result, sales during the first quarter of our fiscal year have typically been lower than sales during the fourth quarter of the preceding year, and we expect this trend to continue.

Revenues from sales of telecommunications equipment are recognized when persuasive evidence of an agreement exists, delivery of the product has occurred as evidenced by customer acceptance, the fee is fixed or determinable and collectibility is reasonably assured. If the fee due from the customer is not fixed or determinable due to extended payment terms, revenue is recognized as payments become due from the customer, assuming all other criteria for revenue recognition are met. The majority of our

revenue is recognized upon receipt of final acceptance certificates. Where multiple elements exist in an arrangement, the arrangement fee is allocated to the different elements based upon verifiable objective evidence of the fair value of the elements. Revenue is then recognized as each element is earned, provided that the undelivered elements are not essential to the functionality of the delivered elements. Revenues from engineering services contracts and from sales of telecommunications equipment involving significant production, modification or customization of the product or where services being provided are deemed to be essential to the functionality of the product are recognized using the percentage of completion method if the project cost can be reasonably estimated. If the cost cannot be reasonably estimated, the completed contract method is applied. Any payments received prior to revenue recognition are recorded as deferred revenue.

In November 2002, the Emerging Issues Task Force reached a consensus on Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables" ("EITF No. 00-21"). This issue addresses how revenue arrangements with multiple deliverables should be divided into separate units of accounting and how the arrangement consideration should be allocated to the identified separate accounting units. EITF No. 00-21 is effective for fiscal periods beginning after June 15, 2003. We have not yet determined the impact of adopting EITF No. 00-21 on our consolidated results of operations or financial position.

Cost of sales consists primarily of material costs, third party commissions, costs associated with manufacturing, assembly and testing of products, costs associated with installation and customer training and overhead and warranty costs. Cost of sales also includes import taxes and tariffs on components and assemblies. Some components and materials used in our products are purchased from a single supplier or a limited group of suppliers and, in some cases, are subject to our obtaining Chinese import permits and approvals. We also rely on third party manufacturers in China to manufacture and assemble most of our handsets.

Our gross profit has been affected by product mix, average selling prices and material costs. Our gross profit, as a percentage of net sales, varies among our product families. The gross profit, as a percentage of net sales, on our handsets is lower compared to our other products. We believe that our handset sales in 2003 could represent up to approximately 35% to 45% of our net sales. We expect that our overall gross profit, as a percentage of net sales, will fluctuate from period to period as a result of shifts in product mix, anticipated decreases in average selling prices and our ability to reduce cost of sales.

Selling, general and administrative expenses include compensation and benefits, professional fees, sales commissions, provision for doubtful accounts receivable and travel and entertainment costs. A large percentage of our costs are fixed and are difficult to quickly reduce in periods of reduced sales. We intend to pursue aggressive selling and marketing campaigns and to expand our direct sales organization, and, as a result, our sales and marketing expenses will increase in future periods. We also expect that in support of our continued growth, general and administrative expenses will continue to increase for the foreseeable future.

Research and development expenses consist primarily of salaries and related costs of employees engaged in research, design and development activities, the cost of parts for prototypes, equipment depreciation and third party development expenses. A large percentage of our costs are fixed and are difficult to quickly reduce in periods of reduced sales. We believe that continued investment in research and development is critical to our long-term success. Accordingly, we expect that our research and development expenses will increase in future periods.

Amortization of intangible assets consists primarily of the amortization of intangible assets associated with acquisitions in China and outside of China, our acquisition of a minority interest in Wacos, Inc. and our acquisitions of Stable Gain International Ltd., Issanni and ACD.

Consolidated equity in net income (loss) of affiliated companies comprised our 51% share of the earnings from Guangdong UTStarcom, Ltd. ("GUTS"), our Guangdong manufacturing subsidiary, which we accounted for using the equity method prior to our acquisition of the remaining 49% ownership interest in GUTS in May 2002. We previously accounted for this under the equity method because we did not have voting control over significant matters.

Under current regulations in China, foreign investment enterprises that have been accredited as technologically advanced enterprises are entitled to additional tax incentives. These tax incentives vary in different locales and could include preferential national enterprise income tax treatment at 50% of the usual rates for different periods of time. All of our active subsidiaries in China were accredited as technologically advanced enterprises. The tax holidays applicable to our wholly-owned subsidiaries UTStarcom China and UTStarcom Telecom Co., Ltd. ("HUTS"), which together accounted for approximately 83.8% of our revenues in 2002, expired at the end of 2002 and 2001, respectively. Unless the tax holidays are extended for the entities, for 2003, the tax rates for these two subsidiaries will increase from 7.5% to 15%, and from 10% to 15%, respectively, which could negatively impact our financial condition and results of operations by increasing our tax rate. During the fourth quarter of 2002, we formed a new entity, Hangzhou UTStarcom Telecom Co., Ltd., to manufacture and sell handsets. This entity will benefit from a two year income tax exemption and a 50% income tax reduction in the following three years. The Chinese government is considering the imposition of a "unified" corporate income tax that would phase out, over time, the preferential tax treatment to which foreign-funded enterprises, such as UTStarcom, are currently entitled. We cannot be certain whether the government will implement such a unified tax structure, or, if implemented, whether it will adversely affect our financial results.

Minority interest in (earnings) loss of consolidated subsidiaries represented the share of earnings in HUTS, our Zhejiang manufacturing joint venture, attributable to our joint venture partner, prior to our acquisition of the remaining 12% ownership interest in HUTS in May 2002.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our financial condition and results of operations are based on certain critical accounting policies and estimates, which include judgments, estimates, and assumptions on the part of management. Estimates are based on historical experience, knowledge of economic and market factors and various other assumptions that management believes to be reasonable under the circumstances. Actual results may differ from those estimates. The following summary of critical accounting policies and estimates highlights those areas of significant judgment in the application of our accounting policies that affect our financial condition and results of operations.

Our business is concentrated in China. Therefore, a material adverse change in economic, political and social conditions in China could have an adverse effect on our accounting estimates and result in additional charges to income.

Revenue Recognition, Allowances for Doubtful Accounts and Product Warranty

We recognize revenue from sales of telecommunications equipment when persuasive evidence of an arrangement exists, delivery of the product has occurred, the fee is fixed or determinable and collectibility is reasonably assured. For transactions where we have yet to obtain customer acceptance, revenue is deferred until the terms of acceptance are satisfied. A sales reserve is established based on historical trends in sales returns. If actual future sales returns do not reflect the historical data, our revenue could be affected. Historically, the level of sales returns and our collection history have been within our expectations.

We also maintain allowances for doubtful accounts based on our assessment of the collectibility of our accounts receivable. We continually monitor collections from our customers and maintain

allowances for doubtful accounts based upon the age of outstanding invoices and any specific customer collection issues. Historically, doubtful accounts or credit losses have been within our expectations, and our doubtful account allowances have been adequate.

We provide a warranty on our equipment and handset sales for a period generally ranging from twelve to eighteen months. We provide for the expected cost of product warranties at the time that we recognize revenue, based on our assessment of past warranty experience. We continually monitor the level of our warranty expenses. If, however, there were a material adverse change in our product failure rates, an additional warranty provision would be required. Historically, our warranty experience has been within our expectations.

Inventories

Our inventories are stated at the lower of cost or net realizable value, net of write-downs for excess, slow moving and obsolete inventory. Inventory write-downs are based on our assumptions about future market conditions and customer demand. We continually monitor our inventory valuation. Historically, the level of inventory write-downs, our inventory turnover, and obsolescence experience have been within our expectations.

Research and Development and Software Development Costs

Our research and development costs are charged to expense as incurred. We capitalize costs incurred in the development of software that will ultimately be sold when technological feasibility has been attained and/or the development of the related product has been completed. Management judgment is required in assessing expected future revenues and changes in product technologies, and the ultimate recoverability of our capitalized software development costs.

Deferred Income Taxes

We recognize deferred income taxes as the difference between the tax bases of assets and liabilities and their financial statement amounts based on enacted tax rates. Management judgment is required in the assessment of the recoverability of our deferred tax assets based on our assessment of projected taxable income. Numerous factors could affect our results of operations in the future. If there were a significant decline in our future operating results, our assessment of the recoverability of our deferred tax assets would need to be revised, and any such adjustment to our deferred tax assets would be charged to income in that period.

Goodwill and Intangibles

We have recorded goodwill and intangible assets in connection with our business acquisitions. Management judgment is required in the assessment of the related useful lives, assumptions regarding our ability to successfully develop and ultimately commercialize acquired technology, and assumptions regarding the fair value and the recoverability of these assets. Historically, there have been no circumstances that resulted in revised assumptions or impairment charges. We completed the required transitional assessment of goodwill during the first quarter of fiscal 2002. Based on this assessment, there was no transition goodwill impairment charge. We completed our annual goodwill impairment review for 2002 in the fourth quarter of 2002, and no charge was required. We plan to carry out our annual goodwill impairment review for future years in the fourth quarter of each year.

Long-Term Investments

We have invested in a fund focused on investments in Internet companies in China and a fund focused on investments in companies in Asia undergoing restructuring or bankruptcy procedures. We have also invested directly in a number of private technology-based companies in the early stages of

development and in publicly listed technology companies traded on Nasdaq and NYSE. While quoted market prices are readily available to determine the fair value of our investments in these publicly traded companies, management judgment is required in evaluating the carrying value of our private company investments for possible impairment. For our private technology company investments, we assess impairment based on an evaluation of the achievement of business objectives and milestones, the financial condition and prospects of these companies and other relevant factors. We continually monitor these investments for impairment, and charge to income any impairment amounts in the period such a determination is made.

RELATED PARTY TRANSACTIONS

We recognized revenue of $123.0 million, $13.9 million, and $0.0 during the years ended December 31, 2002, 2001 and 2000, respectively, with respect to sales of telecommunications equipment to BB Technologies Corporation ("BBTC"), an affiliate of SOFTBANK CORP.

SOFTBANK America Inc., an entity affiliated with SOFTBANK CORP., is a significant stockholder of ours. BBTC offers asynchronous digital subscriber line ("ADSL") coverage throughout Japan, which is marketed under the name YAHOO. We provide ADSL technology to BBTC. The contract was competitively bid and the terms of this contract were on terms no more favorable than those with unrelated parties. Included in accounts receivable at December 31, 2002 is $0.8 million related to this agreement. There were no amounts included in deferred revenue in respect of this agreement at December 31, 2002. Included in accounts receivable in respect of this agreement at December 31, 2001 was $13.5 million. There were no amounts included in deferred revenue in respect of this agreement at December 31, 2001.

We have invested $10.0 million in Softbank China, an investment fund established by SOFTBANK CORP. focused on investments in Internet companies in China. This investment permits us to participate in the anticipated growth of Internet-related businesses in China. SOFTBANK CORP. and its related companies are significant stockholders of UTStarcom. Our investment constitutes 10% of the funding for Softbank China, with SOFTBANK CORP. contributing the remaining 90%. The fund has a separate management team, and none of our employees are employed by the fund. Many of the fund's investments are and will be in privately held companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky as the market for the technologies or products the companies have under development are typically in the early stages and may never materialize. We recorded losses on this investment of $2.8 million, $1.7 million and $0.0 million in 2002, 2001 and 2000, respectively. The balance remaining in this investment at December 31, 2002 was $5.5 million.

During the first quarter of fiscal 2002, we invested $2.0 million in Restructuring Fund No. 1, a venture capital investment limited partnership established by SOFTBANK INVESTMENT CORP., an affiliate of SOFTBANK CORP. SOFTBANK America Inc., an entity affiliated with SOFTBANK CORP., is a significant stockholder of UTStarcom. The fund focuses on leveraged buyout investments in companies in Asia undergoing restructuring or bankruptcy procedures. The total fund offering is expected to be between approximately $150.0 million and $226.0 million, with each investor contributing a minimum of $0.8 million. The fund has a separate management team, and none of the Company's employees are employed by the fund. The balance in this investment is $2.0 million at December 31, 2002.

On August 29, 2002, we completed the repurchase of six million shares of our common stock for $72.9 million from our largest shareholder, SOFTBANK Corp. As part of this transaction, SOFTBANK signed a voluntary "lock up""agreement stipulating that it will not sell any of our common stock within the next six months. This lock up agreement will end on March 1, 2003, which coincides with the start of our "blackout period," in which insiders are not permitted to buy or sell shares. The blackout period begins March 1, 2003 and ends commencing at the close of business on the second trading day

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following the public release of our first quarter fiscal 2003 results in April 2003. We may make additional repurchases of our common stock from SOFTBANK Corp. in order to continue to mitigate SOFTBANK Corp.'s ownership influence.

RESULTS OF OPERATIONS

The following table sets forth the percentage of net sales represented by certain items reflected in our consolidated statements of operations:

	Years Ended December 31,		
	2000	**2001**	**2002**
Percentage of Net Sales:			
Net sales	100.0%	100.0%	100.0%
Cost of sales	65.2	64.2	64.8
Gross profit	34.8	35.8	35.2
Operating expenses:			
Selling, general and administrative	13.1	12.1	11.2
Research and development	11.2	9.5	8.8
Amortization of intangible assets	1.3	1.2	0.2
In-process research and development		0.8	0.1

	Years Ended December 31,		
Total operating expenses	25.6	23.6	20.3
Operating income	9.2	12.2	14.9
Interest and other income (expenses)	2.9	0.7	(0.6)
Equity in net income (loss) of affiliated companies	(0.1)	(0.4)	(0.4)
Income before income taxes and minority interest	12.0	12.5	13.9
Income tax expense	(3.8)	(3.2)	(2.8)
Minority interest in (earnings) of consolidated subsidiaries	(0.6)	(0.2)	(0.1)
Income before cumulative effect of accounting change	7.6	9.1	11.0
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"	(0.3)		
Net income	7.3%	9.1%	11.0%

Comparison of years ended December 31, 2002 and December 31, 2001

NET SALES. Our net sales increased 56.6% to $981.8 million in 2002 from $626.8 million in 2001. Sales of telecommunications equipment, which includes our PAS, IP-based PAS products and wireline products, were $605.0 million in 2002, an increase of $166.1 million, or 38%, as compared to 2001. Sales of subscriber handsets were $376.8 million in 2002, an increase of $188.9 million, or 101%, as compared to 2001. Our handset sales increased as a result of higher than anticipated subscriber growth and the increased popularity of our PAS system. China sales remained strong, increasing by 45% in 2002 as compared to 2001. China sales accounted for 84% and 90% of our net sales for 2002 and 2001, respectively. International sales of telecommunications equipment increased to $159.2 million in 2002 as compared to $60.0 million in 2001, primarily driven by sales of equipment to BBTC in Japan to support its ADSL rollout. During the third quarter of 2002, the provincial-level telecommunications service entity in the Zhejiang province of China began to consolidate telecommunications purchasing decisions for that province. As a result of this trend in the Zhejiang province, we have grouped all customers in Zhejiang province together and have treated these as one customer. At December 31, 2002, we had approximately 33 such customers in Zhejiang province. In 2002, sales to Zhejiang province accounted

for 17.8% and sales to BBTC accounted for 12.5% of our net sales. In 2001, sales to Zhejiang province accounted for 23.7% of our net sales.

GROSS PROFIT. Gross profit increased 53.9% to $345.5 million in 2002 from $224.5 million in 2001. Gross profit, as a percentage of net sales, was 35.2% in 2002 compared to 35.8% in 2001. The decrease in gross profit, as a percentage of net sales, was primarily due to increased sales of lower margin handsets, which comprised 38.4% of net sales in 2002 compared to 30.0% in 2001. Increasing margins on our handset sales, which averaged 27.0% in 2002, as compared to 15.5% in 2001, partially offset this. We believe that our handset sales in 2003 could represent up to approximately 35% to 45% of our net sales. In addition, we believe that there will be continued competitive market pricing pressures on our other products in line with current trends in the industry. However, we believe that cost efficiencies arising from manufacturing efficiencies and the redesign of our PAS products will partially offset the impact of these factors on our gross profit as a percentage of net sales.

SELLING, GENERAL AND ADMINISTRATIVE. Selling, general and administrative expenses increased 45.5% to $110.3 million in 2002 from $75.8 million in 2001. The increase in selling, general and administrative expenses was primarily due to an increase of 450 sales and administrative personnel and related expenses, including sales commissions, associated with the growth in net sales and the expansion of our overall level of business activities. Selling, general and administrative expenses as a percentage of net sales decreased to 11.2% in 2002 from 12.1% in 2001. The decrease in selling, general and administrative expenses as a percentage of net sales was primarily due to economies of scale associated with the significant increase in net sales. We expect our selling, general and administrative expenses to increase in absolute dollar amounts in future periods as sales and marketing activities increase and we further invest in infrastructure and incur additional expenses related to the anticipated growth of our business and operations.

RESEARCH AND DEVELOPMENT. Research and development expenses increased 44.1% to $86.2 million in 2002 from $59.8 million in 2001. The increase in research and development expenses was primarily due to the hiring of an additional 303 technical personnel, and increased prototype expenses and licensing fees to support our research and development efforts. As a percentage of net sales, research and development expenses decreased to 8.8% in 2002 from 9.5% in 2001. This reduction was attributable to the decrease in non-cash compensation expense and an increase in sales in 2002. We expect our research and development expenses to increase in absolute dollar amounts in future periods as we expand our research and development organization to support new product development.

AMORTIZATION OF INTANGIBLE ASSETS. Amortization of intangible assets decreased to $2.4 million in 2002 from $7.5 million in 2001. The decrease in amortization of intangible assets was primarily due to the elimination of goodwill amortization upon the adoption of SFAS No. 142 on January 1, 2002 of $7.0 million, offset by an increase in amortization of intangibles of $2.0 million. Had SFAS No. 142 been in effect during the year ended December 31, 2001, amortization expense would have been $0.2 million.

IN-PROCESS RESEARCH AND DEVELOPMENT COSTS. In-process research and development costs of $0.7 million in 2002 resulted from our acquisition of Issanni on April 19, 2002. In-process research and development costs of $4.7 million in 2001 resulted from our acquisition of ACD in November 2001. These charges were based upon independent appraisals.

INTEREST INCOME (EXPENSE), NET. Interest income was $5.5 million in 2002 compared to interest income of $8.6 million in 2001. Interest expense was $1.3 million in 2002 compared to $3.9 million in 2001. The decrease in interest income was primarily due to a reduction in cash and cash equivalents and short-term investments of $58.3 million and a reduction in interest rates on deposits. The decrease of $2.7 million in interest expense was related to debt balances which were paid off in September 2002. At December 31, 2002, we did not have any debt.

OTHER INCOME (EXPENSE), NET. Net other expense was $9.9 million in 2002, compared to net other expense of $0.3 million in 2001. Net other expense in 2002 was primarily comprised of impairment write-downs of $4.4 million relating to our investment portfolio and foreign exchange losses of $5.4 million.

EQUITY IN NET INCOME (LOSS) OF AFFILIATED COMPANIES. Consolidated equity in net loss of affiliated companies was $4.1 million in 2002 and $3.0 million in 2001. This included equity losses of $2.9 million and $1.7 million in 2002 and 2001, respectively, related to our interest in investment funds. In May 2002, we acquired the remaining 49% ownership interest in GUTS, which is now a wholly-owned subsidiary. Its results of operations are included in our consolidated financial statements beginning June 1, 2002. Prior to May 2002, GUTS was accounted for using the equity method of accounting. On July 5, 2002, we entered into a joint venture agreement with Matsushita Communication Industrial Co., Ltd., and Matsushita Electric Industrial Co., Ltd., to jointly design, develop, manufacture and sell telecommunication products. We have a 49% ownership interest in this joint venture company. The investment in and results of operations of the joint venture company were accounted for using the equity method of accounting, commencing October 2002, and were not material for the year ended December 31, 2002.

INCOME TAX EXPENSE. Income tax expense was $27.3 million in 2002 and $19.8 million in 2001. The increase in income tax expense was due to our increased income. Our effective tax rate was 20% in 2002 compared to 25% in 2001. The reduction in our effective tax rate can be attributed to the increased portion of our net income derived from our operations in Chinese jurisdictions, which have granted us temporary tax holidays. The future rate may vary due to a variety of factors, including but not limited to, the relevant income contribution by domestic and foreign operations, changes in statutory tax rates, expiration of tax holidays, the amount of tax exempt interest income generated during the year, the ability to utilize foreign tax credits and non-deductible items relating to acquisitions, or other non-recurring charges.

MINORITY INTEREST IN EARNINGS OF CONSOLIDATED SUBSIDIARIES. Minority interest in earnings of consolidated subsidiaries was $1.2 million in 2002 and $1.3 million in 2001. The decrease is due to the acquisition of the remaining 12% ownership interest in HUTS in May 2002. HUTS is now a wholly-owned subsidiary of UTStarcom. The expected decrease was offset by an increase in HUTS net income for the four months ended April 30, 2002 as compared to the corresponding period in 2001.

Comparison of years ended December 31, 2001 and December 31, 2000

NET SALES. Our net sales increased 70.0% to $626.8 million in 2001 from $368.6 million in 2000. This increase was primarily due to an increase in sales volume of our PAS and IP-based PAS systems. Sales of telecommunications equipment for the year ended December 31, 2001 were $438.9 million, an increase of $176.9 million, or 67.5%, as compared to the corresponding period in 2000. Sales of subscriber handsets for the year ended December 31, 2001 were $187.9 million, an increase of $81.3 million, or 76.3%, as compared to the corresponding period in 2000. Sales of telecommunications equipment and subscriber handsets increased due to the continued growth in spending on telecommunications infrastructure in China, as China continues to modernize such infrastructure. During 2002, the provincial-level telecommunications service entity in the Zhejiang province of China began to consolidate telecommunications purchasing decisions for that province. As a result of this trend in the Zhejiang province, we have grouped all customers in Zhejiang province together and have treated these as one customer for comparison purposes. At December 31, 2001, we had approximately eight such customers in Zhejiang province. In 2001, Zhejiang province accounted for 23.7% of our net sales. In 2000, sales to Hangzhou PTT accounted for 12.1% of our net sales.

GROSS PROFIT. Gross profit increased 75.2% to $224.5 million in 2001 from $128.2 million in 2000. Gross profit, as a percentage of net sales, increased to 35.8% in 2001 from 34.8% in 2000. The increase in gross profit, as a percentage of net sales, was primarily due to increased margins on our handsets,

which comprised 30.0% of net sales in 2001 compared to 28.9% in 2000. Margins on our handset sales averaged 15.5% in 2001, as compared to 5.3% in 2000.

SELLING, GENERAL AND ADMINISTRATIVE. Selling, general and administrative expenses increased 57.7% to $75.8 million in 2001 from $48.1 million in 2000. The increase in selling, general and administrative expenses was primarily due to an increase of 388 in sales and administrative personnel and related expenses, including sales commissions, associated with the growth in net sales and the expansion of our overall level of business activities. This increase was partly offset by a decrease in non-cash stock compensation expense which decreased to $2.5 million in 2001 from $4.7 million in 2000. Selling, general and administrative expenses as a percentage of net sales decreased to 12.1% in 2001 from 13.1% in 2000. The decrease in selling, general and administrative expenses as a percentage of net sales was primarily due to economies of scale associated with the significant increases in net sales.

RESEARCH AND DEVELOPMENT. Research and development expenses increased 44.3% to $59.8 million in 2001 from $41.5 million in 2000. The increase in research and development expenses was primarily due to the hiring of an additional 396 technical personnel, increased prototype expenses and licensing fees to support our research and development efforts, partly offset by a decrease in non-cash stock compensation expense which decreased to $2.7 million in 2001 from $6.8 million in 2000. As a percentage of net sales, research and development expenses decreased to 9.5% in 2001 from 11.2% in 2000. This reduction was attributable to the decrease in non-cash compensation expense and an increase in sales in 2001.

AMORTIZATION OF INTANGIBLE ASSETS. Amortization of intangible assets increased to $7.5 million in 2001 from $4.9 million in 2000. The increase in amortization of intangible assets was primarily due to the amortization of additional goodwill associated with the acquisition of Stable Gain, a software development company, of $11.0 million in the first quarter of 2001.

IN-PROCESS RESEARCH AND DEVELOPMENT COSTS. In-process research and development costs resulted from our acquisition of ACD in November 2001. The aggregate purchase price of ACD was approximately $21.3 million which, based upon an independent appraisal of the assets acquired and liabilities assumed, was allocated to the specifically identifiable tangible and intangible assets acquired. In connection with the ACD acquisition, $4.7 million of in-process research and development costs were charged to operations in November 2001. There were no in-process research and development charges in 2000.

INTEREST INCOME (EXPENSE), NET. Interest income was $8.6 million in 2001 compared to interest income of $12.2 million in 2000. Interest expense was $3.9 million in 2001 compared to $3.3 million in 2000. Interest income decreased in 2001 due to lower interest rates, which were partially offset by higher average cash balances as a result of the completion of our follow-on public offering in July 2001. Interest expense increased due to higher borrowings in 2001 as compared to 2000.

OTHER INCOME (EXPENSE), NET. Net other expense was $0.3 million in 2001 and net other income was $1.9 million in 2000. The decrease in other income in 2001 was primarily due to impairment write-downs of $1.7 million relating to our investment portfolio.

EQUITY IN NET INCOME (LOSS) OF AFFILIATED COMPANIES. Consolidated equity in net loss of affiliated companies was $3.0 million in 2001 and $0.3 million in 2000. The change between the two periods was due to a $1.7 million loss related to our interest in investment funds and an increase in losses at our Guangdong manufacturing subsidiary, GUTS.

INCOME TAX EXPENSE. Income tax expense was $19.8 million in 2001 and $14.0 million in 2000. The increase in income tax expense was due to our increasing income. Our effective tax rate decreased from 32% in 2000 to 25% in 2001 primarily due to a favorable settlement with the Internal Revenue Service upon examination of our corporate income tax returns filed for the years 1997, 1998 and 1999.

MINORITY INTEREST IN EARNINGS OF CONSOLIDATED SUBSIDIARIES. Minority interest in earnings of consolidated subsidiaries was $1.3 million in 2001 and $2.3 million in 2000. The change between the two periods was primarily due to the decreased profitability at our Zhejiang manufacturing subsidiary, HUTS.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2002, we had lines of credit totaling $314.3 million available for future borrowings. We did not have any borrowings at December 31, 2002. We have not guaranteed any debt not included in the consolidated balance sheet. At December 31, 2002, we had working capital of $568.2 million, including $231.9 million in cash and cash equivalents and $107.3 million of short-term investments.

Net cash generated from operating activities in 2002 was $157.3 million as compared to $40.2 million in 2001, an increase of $117.1 million. This was primarily due to improved operating performance and accounts receivable collection efficiency. We will continue to focus our efforts on improving our operating performance through cost efficiencies arising from continued cost reduction and manufacturing efficiencies. Efficient accounts receivable collection resulted in an improvement in our Day Sales Outstanding (DSO), which was 66 days at December 31, 2002 as compared to 88 days at December 31, 2001. The DSO ratio shows the average time it takes us to turn our receivables into cash and the age in terms of days of our accounts receivable. This ratio is a measure of the effectiveness with which we convert our receivables to cash. DSO is calculated as follows: (net accounts receivable/sales) × number of days in period that is being analyzed. We are also continuing to focus our efforts on the efficient management of our inventory, which was $424.7 million at December 31, 2002. Our inventory turnover ratio for the fourth quarter of 2002 was 2.3 and was in line with the corresponding period in 2001. The inventory turnover ratio shows how often we turn our inventory in the course of the year. Inventory turnover is calculated as follows: (cost of goods sold /average inventory). Over half of our inventory is at customer locations against signed contracts. During 2002, some strategic uses of our cash included the retirement of $70.5 million in debt, a $72.9 million stock buy-back at $12.25 per share and capital expenditures of $38.6 million for our new manufacturing facility in Hangzhou. We believe this new facility will contribute to cost and manufacturing efficiencies and higher revenue and profits in the future.

Net cash provided by operations in 2002 of $157.3 million was primarily due to net income of $107.9 million, adjusted for non cash charges including depreciation and amortization expense of $22.4 million, amortization of stock compensation expense of $3.1 million, non-qualified stock option exercise tax benefits of $6.5 million, investment impairment write downs of $4.4 million, inventory write-downs of $12.4 million and allowance for doubtful accounts of $7.2 million. In addition, cash increased due to the growth in accounts payable of $170.5 million, other accrued liabilities of $27.7 million, deferred revenue of $87.8 million and income taxes payable of $2.5 million. This was offset by an increase in inventories, accounts receivable and other current and non-current assets of $207.3 million, $34.2 million and $60.5 million, respectively. Net cash provided by operations in 2001 of $40.2 million was primarily due to net income of $57.0 million adjusted for depreciation and amortization expense of $18.5 million, amortization of deferred stock compensation expense of $5.2 million, non-qualified stock option exercise tax benefits of $15.3 million, inventory write-downs of $11.1 million, allowance for doubtful accounts of $6.2 million and an increase in accounts payable, income taxes payable and other current liabilities and deferred revenue of $39.1 million, $3.4 million and $86.2 million, respectively. This was partially offset by an increase in inventories, accounts receivable and other current and non-current assets of $121.2 million, $39.2 million and $52.6 million, respectively.

Net cash used in investing activities in 2002 of $144.2 million was primarily due to purchases of property, plant and equipment of $75.3 million, of which $38.6 million related to our new

manufacturing facility in Hangzhou, business acquisitions of $17.7 million, including $14.1 million relating to the purchase of the remaining interest in HUTS, investment in affiliates of $28.9 million which primarily comprised investments in public and private technology companies, offset by net sales of short-term investments of $22.4 million. Net cash used in investing activities in 2001 of $43.7 million was primarily due to purchases of property, plant and equipment of $30.2 million, investments in affiliates of $9.8 million, and net purchases of short-term investments of $2.1 million.

Net cash used in financing activities in 2002 of $102.4 million was primarily due to the repurchase of our shares and related transaction costs of $72.9 million and net payments of $70.5 million on borrowings under our lines of credit. We paid off our short and long-term debt in September and, as of December 31, 2002, we had no debt. These uses of cash were partially offset by $40.9 million in proceeds from the sale of common stock in connection with the Softbank resale and the issuance of common stock through the exercise of stock options. Net cash provided by financing activities in 2001 of $175.5 million was primarily due to $160.6 million of proceeds from our follow-on public offering of common stock in August 2001 and exercise of stock options, and net proceeds from borrowings under our line of credit arrangements of $15.1 million.

In 2001, we purchased the rights to use 49 acres of land located in Zhejiang Science and Technology Industry Garden of Hangzhou Hi-tech Industry Development Zone. As of December 31, 2002, we have completed the foundation and ground work and have commenced construction of the building. We expect that construction of the new facility will be completed in 2003 at a projected cost of approximately $95.6 million. Capital expenditures for the facility were $38.6 million in 2002.

Our principal commitments at December 31, 2002 consist of obligations under operating leases and a commitment to invest up to an additional $4.0 million in one of our investments. We lease certain of our facilities under non-cancelable operating leases, which expire at various dates through 2007. We did not have any borrowings under our lines of credit at December 31, 2002.

We have not engaged in any transactions or arrangements with unconsolidated entities or other persons that are reasonably likely to materially affect our liquidity or the availability of, or requirements for, capital resources.

Our China sales are generally denominated in local currency. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China. Sales outside China are generally denominated in US dollars. As of December 31, 2002, we were not engaged in any hedging activities and did not hold any derivative financial instruments. We cannot guarantee that fluctuations in currency exchange rates in the future will not have a material adverse effect on revenues from international sales and, correspondingly, on our business, financial condition and results of operations. We have contracts negotiated in Japanese Yen and a multi-currency bank account in Japanese Yen for purchasing portions of our inventories and supplies. The balance of this Japanese Yen account at December 31, 2002 was approximately $7.1 million. As of December 31, 2002, we were not engaged in any hedging activities and did not hold any derivative financial instruments in respect of these Japanese Yen purchases.

We believe that our existing cash and cash equivalents, short-term investments and cash from operations will be sufficient to finance our operations through at least the next 12 months. As of December 31, 2002, we had cash, restricted cash and investments, of $349.0 million and lines of credit totaling $314.3 million available for future borrowings. $260.1 million of available lines of credit expire during 2003 and $54.2 million of available lines of credit expire between 2008 and 2010. However, in the event that our current cash balances, future cash flows from operations and current lines of credit are not sufficient to meet our obligations or strategic needs or in the event that market conditions are favorable, we would consider raising additional funds in the capital or equity markets. If additional financing is needed, there can be no assurance that such financing will be available to us on commercially reasonable terms, or at all.

CONTRACTUAL OBLIGATIONS AND OTHER COMMERCIAL COMMITMENTS

Our obligations under contractual obligations and commercial commitments are primarily with regards to leasing arrangements and standby letters of credit and are as follows:

	December 31, 2002			
	Payments Due by Period			
	Total	Less than 1 year	1-3 years	3-5 years
Contractual Obligations				
Operating leases	$ 10,536	$ 5,857	$ 4,504	$ 175
Other Commercial Commitments				
Standby letters of credit	$ 9,779	$ 9,779	$	$

INVESTMENT COMMITMENTS:

In June 2002, we invested $1.0 million in Global Asia Partners L.P. The fund size is anticipated to be $100 million and was formed to make private equity investments in private or pre-IPO technology and telecommunications companies in Asia. We have a commitment to invest up to a maximum of $5.0 million. The remaining amount is due at such times and in such amounts as shall be specified in one or more future capital calls to be issued by the general partner.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2002, the Financial Accounting Standards Board (the "FASB") issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which addresses the measurement, timing of recognition and reporting of costs associated with exit or disposal activities and restructuring activities. SFAS No. 146 requires that a liability for costs associated with exit or restructuring activities be recognized only when the liability is incurred as opposed to at the time that a company formally approves and commits to an exit plan as set forth in EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity." SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. We do not expect the adoption to have an impact on our consolidated financial statements.

In November 2002, the FASB issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued, including a reconciliation of changes in the entity's product warranty liabilities. The initial recognition and initial measurement provisions of FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. We believe that the adoption of this standard will not have a material impact on our consolidated financial statements.

In November 2002, the EITF reached a consensus on Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables." This issue addresses how revenue arrangements with multiple deliverables should be divided into separate units of accounting and how the arrangement consideration should be allocated to the identified separate accounting units. EITF No. 00-21 is effective for fiscal periods beginning after June 15, 2003. We have not yet determined the impact of adopting EITF No. 00-21 on our results of operations or financial position.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation Costs Transition and Disclosure". This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation", and provides alternative methods of transition for an entity that voluntarily changes to

the fair value-based method of accounting for stock-based compensation. It also requires additional disclosures about the effects on reported net income of an entity's accounting policy with respect to stock-based employee compensation. We account for stock-based compensation in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees" and have adopted the disclosure-only alternative of SFAS No. 123. We adopted the disclosure provisions of SFAS No. 148 in December 2002.

FACTORS AFFECTING FUTURE OPERATING RESULTS

RISKS RELATING TO OUR COMPANY

OUR FUTURE PRODUCT SALES ARE UNPREDICTABLE, OUR OPERATING RESULTS ARE LIKELY TO FLUCTUATE FROM QUARTER TO QUARTER, AND IF WE FAIL TO MEET THE EXPECTATIONS OF SECURITIES ANALYSTS OR INVESTORS, OUR STOCK PRICE COULD DECLINE SIGNIFICANTLY

Our quarterly and annual operating results have fluctuated in the past and are likely to fluctuate in the future due to a variety of factors, some of which are outside of our control. As a result, period-to-period comparisons of our operating results are not necessarily meaningful or indicative of future performance. Furthermore, it is likely that in some future quarters our operating results will fall below the expectations of securities analysts or investors. If this occurs, the trading price of our common stock could decline.

Factors that may affect our future operating results include:

- the timing, number and size of orders for our products, as well as the relative mix of orders for each of our products, particularly the volume of lower margin handsets;

- cancellation, deferment or delay in implementation of large contracts;

- the evolving and unpredictable nature of the economic, regulatory, competitive and political environments in China and other countries in which we market or plan to market our products;
- price reductions by our competitors;
- competitive market pressures resulting in decreased gross margins or increased inventory levels;
- changes in our customers' subscriber growth rate;
- currency fluctuations;
- market acceptance of our products and product enhancements;
- the lengthy and unpredictable sales cycles associated with sales of our products combined with the impact of this variability on our suppliers' ability to provide us with components on a timely basis;
- longer collection periods of accounts receivable in China and other countries; and
- the decline in business activity we typically experience during the Lunar New Year, which leads to decreased sales during our first fiscal quarter.

The limited performance history of some of our products, our limited forecasting experience and processes and the emerging nature of our target markets make forecasting our future sales and operating results difficult. Our expense levels are based, in part, on our expectations regarding future sales, and these expenses are largely fixed, particularly in the short term. In addition, to enable us to promptly fill orders, we maintain inventories of finished goods, components and raw materials. As a result, we commit to considerable costs in advance of anticipated sales. In the past, a substantial portion of our sales in each quarter resulted from orders received and shipped in that quarter, and we have operated with a limited backlog of unfilled orders. Accordingly, we may not be able to reduce our

costs in a timely manner to compensate for any unexpected shortfall between forecasted and actual sales. Any significant shortfall of sales may require us to maintain higher levels of inventories of finished goods, components and raw materials than we require, thereby increasing our risk of inventory obsolescence and corresponding inventory write-downs and write-offs.

COMPETITION IN OUR MARKETS MAY LEAD TO REDUCED PRICES, REVENUES AND MARKET SHARE

We are increasingly facing intense competition in our target markets, especially from domestic companies in China. We believe that our strongest competition in the future may come from these companies, many of which operate under lower cost structures and more favorable governmental policies and have much larger sales forces than we do. Furthermore, other companies not presently offering competing products may also enter our target markets, particularly with the reduction of trade restrictions as a result of China's admission to the World Trade Organization, or WTO. Many of our competitors have significantly greater financial, technical, product development, sales, marketing and other resources than we do. As a result, our competitors may be able to respond more quickly to new or emerging technologies and changes in service provider requirements. Our competitors may also be able to devote greater resources than we can to the development, promotion and sale of new products. These competitors may also be able to offer significant financing arrangements to service providers, in some cases facilitated by government policies, which is a competitive advantage in selling systems to service providers with limited financial and currency resources. Increased competition is likely to result in price reductions, reduced gross profit as a percentage of net sales and loss of market share, any one of which could materially harm our business, financial condition and results of operations.

Moreover, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties, including Telecommunications Administrations, Telecommunications Bureaus and other local organizations, to increase the ability of their products to address the needs of prospective customers in our target markets. Accordingly, alliances among competitors or between competitors and third parties may emerge and rapidly acquire significant market share. To remain competitive, we believe that we must continue to partner with Telecommunications Administrations and other local organizations, maintain a high level of investment in research and development and in sales and marketing, and manufacture and deliver products to service providers on a timely basis and without significant defects. If we fail to meet any of these objectives, our business, financial condition and results of operations could be harmed.

The introduction of inexpensive wireless telephone service or other competitive services in China may also have an adverse impact on sales of our PAS systems and handsets in China. We may not be able to compete successfully against current or future competitors, and competitive pressures in the future may materially adversely affect our business, financial condition and results of operations.

BECAUSE CONTRACTS AND PURCHASE ORDERS ARE GENERALLY SUBJECT TO CANCELLATION OR DELAY BY CUSTOMERS WITH LIMITED OR NO PENALTY, OUR BACKLOG IS NOT NECESSARILY INDICATIVE OF FUTURE REVENUES OR EARNINGS

As of December 31, 2002, our backlog totaled approximately $605.4 million, compared to approximately $360.7 million as of December 31, 2001. We include in our backlog contracts and purchase orders for which we anticipate delivery to occur within 12 months and products delivered but for which final acceptance has not yet been received. Because contracts and purchase orders are generally subject to cancellation or delay by customers with limited or no penalty, our backlog is not necessarily indicative of future revenues or earnings. In addition, we have a number of large contracts under which realization of our backlog is dependent on the successful implementation of our products by our customers and in some cases, the successful development of regional infrastructures.

OUR BUSINESS MAY SUFFER IF WE ARE UNABLE TO COLLECT PAYMENTS FROM OUR CUSTOMERS ON A TIMELY BASIS

Our customers often must make a significant commitment of capital to purchase our products. As a result, any downturn in a customer's business that affects the customer's ability to pay us could harm our financial condition. Moreover, accounts receivable collection cycles historically tend to be much longer in China than in other markets. The failure of any of our customers to make timely payments could require us to write-off accounts receivable or increase our accounts receivable reserves, either of which could adversely affect our financial condition.

OUR MARKET IS SUBJECT TO RAPID TECHNOLOGICAL CHANGE, AND TO COMPETE EFFECTIVELY, WE MUST CONTINUALLY INTRODUCE NEW PRODUCTS THAT ACHIEVE MARKET ACCEPTANCE

The emerging market for communications equipment in developing countries is characterized by rapid technological developments, frequent new product introductions and evolving industry and regulatory standards. Our success will depend in large part on our ability to enhance our network access and switching technologies and develop and introduce new products and product enhancements that anticipate changing service provider requirements and technological developments. We may need to make substantial capital expenditures and incur significant research and development costs to develop and introduce new products and enhancements. If we fail to timely develop and introduce new products or enhancements to existing products that effectively respond to technological change, our business, financial condition and results of operations could be materially adversely affected. From time to time, our competitors or we may announce new products or product enhancements, technologies or services that have the potential to replace or shorten the life cycles of our products and that may cause customers to defer purchasing our existing products, resulting in inventory obsolescence. Future technological advances in the communications industry may diminish or inhibit market acceptance of our existing or future products or render our products obsolete.

Even if we are able to develop and introduce new products, they may not gain market acceptance. Market acceptance of our products will depend on various factors including:

- our ability to obtain necessary approvals from regulatory organizations;
- the perceived advantages of the new products over competing products;
- our ability to attract customers who have existing relationships with our competitors;

product cost relative to performance; and

the level of customer service available to support new products.

Specifically, sales of PAS, our wireless access system, will depend in part upon consumer acceptance of the mobility limitations of this service relative to other wireless service systems, such as GSM or CDMA. If our existing or new products fail to achieve market acceptance for any reason, our business could be seriously harmed.

OUR BUSINESS WILL SUFFER IF WE ARE UNABLE TO DELIVER QUALITY PRODUCTS ON A TIMELY AND COST EFFECTIVE BASIS

Our operating results depend on our ability to manufacture products on a timely and cost effective basis. In the past, we have experienced reductions in yields as a result of various factors, including defects in components and human error in assembly. If we experience deterioration in manufacturing performance or a delay in production of any of our products, we could experience delays in shipments and cancellations of orders. Moreover, networking products frequently contain undetected software or hardware defects when first introduced or as new versions are released. In addition, our products are often embedded in or deployed in conjunction with service providers' products, which incorporate a

variety of components produced by third parties. As a result, when a problem occurs, it may be difficult to identify the source of the problem. These problems may cause us to incur significant warranty and repair costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relation problems or loss of customers, any one of which could harm our business.

We contract with third parties in China to undertake high volume manufacturing and assembly of our handsets. In addition, we sometimes use third parties for high volume assembly of circuit boards. We do not have any long-term contracts with these third party manufacturers, and in the event that these manufacturers are unable or unwilling to continue to manufacture our products, we may be unable to secure alternative manufacturers or could experience delays in qualifying new manufacturers.

WE DEPEND ON SOME SOLE SOURCE AND OTHER KEY SUPPLIERS FOR HANDSETS, BASE STATIONS, COMPONENTS AND MATERIALS USED IN OUR PRODUCTS, AND IF THESE SUPPLIERS FAIL TO PROVIDE US WITH ADEQUATE SUPPLIES OF HIGH QUALITY PRODUCTS AT COMPETITIVE PRICES, OUR COMPETITIVE POSITION, REPUTATION AND BUSINESS COULD BE HARMED

Some components and materials used in our products are purchased from a single supplier or a limited group of suppliers. If any supplier is unwilling or unable to provide us with high quality components and materials in the quantities required and at the costs specified by us, we may not be able to find alternative sources on favorable terms, in a timely manner, or at all. Our inability to obtain or to develop alternative sources if and as required could result in delays or reductions in manufacturing or product shipments. Moreover, these suppliers may delay product shipments or supply us with inferior quality products. If any of these events occur, our competitive position, reputation and business could suffer.

Our ability to source a sufficient quantity of high quality components used in our products may be limited by China's import restrictions and duties. We require a significant number of imported components to manufacture our products in China. Imported electronic components and other imported goods used in the operation of our business are subject to a variety of permit requirements, approval procedures, import duties and registration requirements. Non-payment of required import duties could subject us to penalties and fines and could adversely affect our ability to manufacture and sell our products in China. In addition, import duties increase the cost of our products and may make them less competitive.

In particular, components of our PAS system include the handset used by subscribers to make and receive mobile telephone calls and the base station unit. Our inability to obtain a sufficient number of high quality components and assemblies for handsets and base stations could severely harm our business. From time to time, there has been a worldwide shortage of handsets, and there currently exists a shortage of low-priced handsets, which we have found to be popular with many consumers in China. We have only used third parties to assemble and manufacture handsets in China for us for a limited period of time. These manufacturers may be unable to produce adequate quantities of high-quality handsets to meet the demand of our customers. In addition, we may be unable to obtain adequate quantities of base stations and may be unable to find alternative sources on favorable terms, in a timely manner, or at all. Our inability to obtain or to develop alternative sources if and as required could result in delays or reductions in manufacturing or product shipments.

IF WE ARE UNABLE TO EXPAND OUR DIRECT SALES OPERATION IN CHINA AND INDIRECT DISTRIBUTION CHANNELS ELSEWHERE OR SUCCESSFULLY MANAGE OUR EXPANDED SALES ORGANIZATION, OUR OPERATING RESULTS MAY SUFFER

Our distribution strategy focuses primarily on developing and expanding our direct sales organization in China and our indirect distribution channels outside of China. We may not be able to

successfully expand our direct sales organization in China and the cost of any expansion may exceed the revenue generated from these efforts. Even if we are successful in expanding our direct sales organization in China, we may not be able to compete successfully against the significantly larger and better-funded sales and marketing operations of current or potential competitors. In addition, if we fail to develop relationships with significant international resellers or manufacturers' representatives, or if these resellers or representatives are not successful in their sales or marketing efforts, we may be unsuccessful in our expansion efforts outside China.

WE EXPECT AVERAGE SELLING PRICES OF OUR PRODUCTS TO DECREASE WHICH MAY REDUCE OUR REVENUES AND OUR GROSS MARGIN AS A PERCENTAGE OF NET SALES, AND, AS A RESULT, WE MUST INTRODUCE NEW PRODUCTS AND REDUCE OUR COSTS IN ORDER TO MAINTAIN PROFITABILITY

The average selling prices for communications access and switching systems and subscriber terminal products, such as handsets, in China have been declining as a result of a number of factors, including:

- increased competition;
- aggressive price reductions by competitors; and
- rapid technological change.

We anticipate that average selling prices of our products will decrease in the future in response to product introductions by us or our competitors or other factors, including price pressures from customers. Therefore, we must continue to develop and introduce new products and enhancements to existing products that incorporate features that can be sold at higher average selling prices. Failure to do so could cause our revenues and gross profit, as a percentage of net sales, to decline.

Our cost reduction efforts may not allow us to keep pace with competitive pricing pressures or lead to improved gross profit, as a percentage of net sales. In order to be competitive, we must continually reduce the cost of manufacturing our products through design and engineering changes. We may not be successful in these efforts or delivering our products to market in a timely manner. Any redesign may not result in sufficient cost reductions to allow us to reduce the prices of our products to remain competitive or to improve or maintain our gross profit, as a percentage of net sales.

SHIFTS IN OUR PRODUCT MIX MAY RESULT IN DECLINES IN GROSS PROFIT, AS A PERCENTAGE OF NET SALES

Our gross profit, as a percentage of net sales, varies among our product groups. Our gross profit, as a percentage of net sales, is generally higher on our access network system products and is significantly lower on our handsets. We also anticipate that the gross profit, as a percentage of net sales, may be lower for our newly developed products due to start-up costs and may improve as unit volumes increase and efficiencies can be realized. Our overall gross profit, as a percentage of net sales, has fluctuated from period to period as a result of shifts in product mix, the introduction of new products, decreases in average selling prices for older products and our ability to reduce manufacturing costs.

SERVICE PROVIDERS SOMETIMES EVALUATE OUR PRODUCTS FOR LONG AND UNPREDICTABLE PERIODS WHICH CAUSES THE TIMING OF PURCHASES AND OUR RESULTS OF OPERATIONS TO BE UNPREDICTABLE

The period of time between our initial contact with a service provider and the receipt of an actual purchase order may span a year or more. During this time, service providers may subject our products to an extensive and lengthy evaluation process before making a purchase. The length of these qualification processes may vary substantially by product and service provider, making our results of operations unpredictable. We may incur substantial sales and marketing expenses and expend significant management effort during this process, which ultimately may not result in a sale. These qualification processes often make it difficult to obtain new customers, as service providers are reluctant to expend the resources necessary to qualify a new supplier if they have one or more existing qualified sources.

OUR MULTI-NATIONAL OPERATIONS SUBJECT US TO VARIOUS ECONOMIC, POLITICAL, REGULATORY AND LEGAL RISKS

We market and sell our products in China and other markets, including Taiwan, Japan, Vietnam, India and Latin America. The expansion of our existing multi-national operations and entry into additional international markets will require significant management attention and financial resources. Multi-national operations are subject to inherent risks, including:

- difficulties in designing products that are compatible with varying international communications standards;
- longer accounts receivable collection periods and greater difficulty in accounts receivable collection;
- unexpected changes in regulatory requirements or the regulatory environment;
- changes in governmental control or influence over our customers;
- changes to import and export regulations, including quotas, tariffs and other trade barriers;
- delays or difficulties in obtaining export and import licenses;
- potential foreign exchange controls and repatriation controls on foreign earnings;
- exchange rate fluctuations and currency conversion restrictions;
- the burdens of complying with a variety of foreign laws and regulations;
- difficulties and costs of staffing and managing multi-national operations, including but not limited to internal control and compliance;
- reduced protection for intellectual property rights in some countries;
- potentially adverse tax consequences; and
- political and economic instability.

Multi-national companies are required to establish intercompany pricing for transactions between their separate legal entities operating in different taxing jurisdictions. These intercompany transactions are subject to audit by taxing authorities in the jurisdictions in which multi-national companies operate. An additional tax liability may be incurred if it is determined that intercompany pricing was not done at arm's length. We believe we have adequately estimated and recorded our liability arising from intercompany pricing, but an additional tax liability may result from audits of our intercompany pricing policies.

In markets outside of China, we rely on a number of original equipment manufacturers, or OEMs, and third-party distributors and agents to market and sell our network access products. If these OEMs, distributors or agents fail to provide the support and effort necessary to service developing markets effectively, our ability to maintain or expand our operations outside of China will be negatively impacted. We may not successfully compete in these markets, our products may not be accepted and we may not successfully overcome the risks associated with international operations.

Moreover, in less developed markets we may face additional risks, such as inconsistent infrastructure support, unstable political and economic environments, and lack of a secure environment for our personnel, facilities and equipment. We have in the past experienced cases of vandalism and

armed theft of our equipment that had been or was being installed in the field. If disruptions for any of these reasons become too severe in any particular market, it may become necessary for us to terminate contracts and withdraw from that market and suffer the associated costs and lost revenue.

Due to the multi-national nature of our business and operations, we are subject to regulation in multiple governmental jurisdictions. Furthermore, as a result of the heavily regulated nature of the markets in which we operate, we are continually subject to the risk of governmental investigations regarding our compliance with the rules and regulations of such jurisdictions. Should we become subject to any such investigations, there may be significant and unanticipated expenses, and risks such as the distraction of our key employees and disruptions to our operations. Such expenses and risks may result even in the event that such investigations are decided in our favor and no instances of non-compliance are found.

WE ARE SUBJECT TO RISKS RELATING TO CURRENCY EXCHANGE RATE FLUCTUATIONS

We are exposed to foreign exchange rate risk because our sales to China are denominated in Renminbi and portions of our accounts payable are denominated in Japanese Yen. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China. Although the impact of currency fluctuations of Renminbi to date has been insignificant, fluctuations in currency exchange rates in the future may have a material adverse effect on our results of operations.

OUR FAILURE TO MEET INTERNATIONAL AND GOVERNMENTAL PRODUCT STANDARDS COULD BE DETRIMENTAL TO OUR BUSINESS

Many of our products are required to comply with numerous government regulations and standards, which vary by market. As standards for products continue to evolve, we will need to modify our products or develop and support new versions of our products to meet emerging industry standards, comply with government regulations and satisfy the requirements necessary to obtain approvals. Our inability to obtain regulatory approval and meet established standards could delay or prevent our entrance into or force our departure from particular markets.

OUR RECENT GROWTH HAS STRAINED OUR RESOURCES, AND IF WE ARE UNABLE TO MANAGE AND SUSTAIN OUR GROWTH, OUR OPERATING RESULTS WILL BE NEGATIVELY AFFECTED

We have recently experienced a period of rapid growth and anticipate that we must continue to expand our operations to address potential market opportunities. If we fail to implement or improve systems or controls or to manage any future growth and expansion effectively, our business could suffer.

Our expansion has placed and will continue to place a significant strain on our management, operational, financial and other resources. To manage our growth effectively, we will need to take various actions, including:

- enhancing management information systems and forecasting procedures;
- further developing our operating, administrative, financial and accounting systems and controls;
- maintaining close coordination among our engineering, accounting, finance, marketing, sales and operations organizations;

expanding, training and managing our employee base; and

expanding our finance, administrative and operations staff.

WE MAY NOT BE ABLE TO SUSTAIN PROFITABILITY

We may not be able to remain profitable in future periods. We anticipate continuing to incur significant sales and marketing, research and development and general and administrative expenses and, as a result, we will need to generate higher revenues to remain profitable. Numerous factors could negatively impact our results of operations, including a decrease in sales, price pressures and significant fixed costs. Our past results should not be relied on as an indication of our future performance.

OUR SUCCESS IS DEPENDENT ON CONTINUING TO HIRE AND RETAIN QUALIFIED PERSONNEL, AND IF WE ARE NOT SUCCESSFUL IN ATTRACTING AND RETAINING THESE PERSONNEL, OUR BUSINESS WOULD BE HARMED

The success of our business depends in significant part upon the continued contributions of key technical and senior management personnel, many of whom would be difficult to replace. In particular, our success depends in large part on the knowledge, expertise and services of Hong Liang Lu, our President and Chief Executive Officer, and Ying Wu, our Executive Vice President and Chief Executive Officer of China Operations. The loss of any key employee, the failure of any key employee to perform satisfactorily in his or her current position or our failure to attract and retain other key technical and senior management employees could have a significant negative impact on our operations.

To effectively manage our recent growth as well as any future growth, we will need to recruit, train, assimilate, motivate and retain qualified employees. Competition for qualified employees is intense, and the process of recruiting personnel with the combination of skills and attributes required to execute our business strategy can be difficult, time-consuming and expensive. We are actively searching for research and development engineers and sales and marketing personnel, who are in short supply. Additionally, we have a need for and have experienced difficulty in finding qualified accounting personnel knowledgeable in U.S. and China accounting standards who are resident in China. If we fail to attract, hire, assimilate or retain qualified personnel, our business would be harmed.

Competitors and others have in the past and may in the future attempt to recruit our employees. In addition, companies in the telecommunications industry whose employees accept positions with competitors frequently claim that the competitors have engaged in unfair hiring practices. We may be the subject of these types of claims in the future as we seek to hire qualified personnel. Some of these claims may result in material litigation and disruption to our operations. We could incur substantial costs in defending ourselves against these claims, regardless of their merit.

ANY ACQUISITIONS THAT WE UNDERTAKE COULD BE DIFFICULT TO INTEGRATE, DISRUPT OUR BUSINESS, DILUTE OUR STOCKHOLDERS AND HARM OUR OPERATING RESULTS

We may acquire complementary businesses, products and technologies. For example, in November 2001, we acquired Advanced Communication Devices Corporation, a system on chip semiconductor company. On April 19, 2002, the Company completed the purchase of Issanni Communications, Inc., a RAS (remote access server) and local access technology company, providing broadband over ADSL. On October 16, 2002, we acquired the assets and intellectual property of Shanghai Yi Yun Telecom Technology Co. Ltd., a provider of synchronous digital hierarchy ("SDH") transmission equipment. Any anticipated benefits of an acquisition may not be realized. We have in the past and will continue to evaluate acquisition prospects that would complement our existing product offerings, augment our market coverage, enhance our technological capabilities, or that may otherwise offer growth opportunities. Acquisitions of other companies may result in dilutive issuances of equity securities, the incurrence of debt and the amortization of expenses related to intangible assets. In addition, acquisitions involve numerous risks, including difficulties in the assimilation of operations, technologies, products and personnel of the acquired company, diversion of management's attention from other business concerns, risks of entering markets in which we have no direct or limited prior experience, and the potential loss of key employees of the acquired company.

WE MAY BE UNABLE TO ADEQUATELY PROTECT OUR INTELLECTUAL PROPERTY AND MAY BE SUBJECT TO CLAIMS THAT WE INFRINGE THE INTELLECTUAL PROPERTY OF OTHERS, EITHER OF WHICH COULD

SUBSTANTIALLY HARM OUR BUSINESS

We rely on a combination of patents, copyrights, trademarks, trade secret laws and contractual obligations to protect our technology. We have applied for patents in the United States, three of which have been issued. We have also filed patent applications in other countries. Additional patents may not be issued from our pending patent applications and our issued patents may not be upheld. In addition, we have, from time to time, chosen to abandon previously filed applications. Moreover, we have not yet obtained, and may not be able to obtain, patents in China on our products or the technology that we use to manufacture our products. Our subsidiaries and joint ventures in China rely upon our trademarks, technology and know-how to manufacture and sell our products. We cannot guarantee that these and other intellectual property protection measures will be sufficient to prevent misappropriation of our technology or that our competitors will not independently develop technologies that are substantially equivalent or superior to ours. In addition, the legal systems of many foreign countries, including China, do not protect intellectual property rights to the same extent as the legal system of the United States. Furthermore, in connection with acquisitions, we from time to time obtain intellectual property rights, including patents. These intellectual property rights could be found to infringe on third parties' rights. If such a situation were to occur, we would endeavor to obtain licenses to allow us to continue to use such intellectual property. However, no assurances can be provided that any intellectual property we acquire will not infringe on the rights of third parties, nor that we will be able to successfully negotiate licenses to use such intellectual property on terms that are acceptable to us. If we are unable to adequately protect our proprietary information and technology, our business, financial condition and results of operations could be materially adversely affected.

The increasing dependence of the communications industry on proprietary technology has resulted in frequent litigation based on allegations of the infringement of patents and other intellectual property. In the future we may be subject to litigation to defend against claimed infringements of the rights of others or to determine the scope and validity of the proprietary rights of others. Future litigation also may be necessary to enforce and protect our trade secrets and other intellectual property rights. Any intellectual property litigation could be costly and could cause diversion of management's attention from the operation of our business. Adverse determinations in any litigation could result in the loss of our proprietary rights, subject us to significant liabilities or require us to seek licenses from third parties which may not be available on commercially reasonable terms, if at all. We could also be subject to court orders preventing us from manufacturing or selling our products.

BUSINESS INTERRUPTIONS COULD ADVERSELY AFFECT OUR BUSINESS

Our operations are vulnerable to interruption by fire, earthquake, power loss, telecommunications failure and other events beyond our control. We do not have a detailed disaster recovery plan. Our headquarters facility in the State of California was subject to electrical blackouts as a consequence of a shortage of available electrical power. In the event these blackouts resume, they could disrupt the operations at our headquarters. In addition, we do not carry sufficient business interruption insurance to compensate us for losses that may occur and any losses or damages incurred by us could have a material adverse effect on our business.

WE ARE EXPOSED TO FLUCTUATIONS IN THE VALUES OF OUR PORTFOLIO INVESTMENTS

We maintain an investment portfolio of various holdings, types, and maturities. Part of this portfolio includes equity investments in publicly traded companies, the value of which are subject to market price volatility. Recent events have adversely affected the public equities market and general economic conditions may continue to worsen. Should the fair value of our publicly traded equity investments decline below their cost basis in a manner deemed to be other-than-temporary, it may become necessary for us to take an impairment charge.

We have also invested in several privately held companies as well as investment funds which invest primarily in privately held companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky, as the market for the technologies or products they have under development are typically in the early stages and may never materialize. We could lose our entire initial investment in these companies and investment funds.

IF WE SEEK TO SECURE ADDITIONAL FINANCING WE MAY NOT BE ABLE TO DO SO. IF WE ARE ABLE TO SECURE ADDITIONAL FINANCING OUR STOCKHOLDERS MAY EXPERIENCE DILUTION OF THEIR OWNERSHIP INTEREST OR WE MAY BE SUBJECT TO LIMITATIONS ON OUR OPERATIONS.

We currently anticipate that our available cash resources, which include existing cash and cash equivalents, short-term investments and cash from operations, will be sufficient to meet our anticipated needs for working capital and capital expenditure during the next 12 months. If we are unable to generate sufficient cash flows from operations to meet our anticipated needs for working capital and capital expenditures, we may need to raise additional funds to develop new or enhanced products, respond to competitive pressures, take advantage of acquisition opportunities or raise capital for strategic purposes. If we raise additional funds through the issuance of equity securities, our stockholders may experience dilution of their ownership interest, and the newly issued securities may have rights superior to those of common stock. If we raise additional funds by issuing debt, we may be subject to limitations on our operations.

WE HAVE BEEN NAMED AS A DEFENDANT IN SECURITIES LITIGATION

We, and various underwriters for our initial public offering are defendants in a putative shareholder class action. The complaint alleges undisclosed improper underwriting practices concerning the allocation of IPO shares, in violation of the federal securities laws. Similar complaints have been filed concerning the IPOs of more than 300 companies, and the litigation has been coordinated in federal court for the Southern District of New York as *In re Initial Public Offering Securities Litigation*, 21 MC 92. We believe we have meritorious defenses to the claims against us and intend to defend the litigation vigorously. However, as litigation is by its nature uncertain, an unfavorable resolution of the lawsuit could have a material adverse effect on our business, results of operations, or financial condition.

RISKS RELATING TO THE STRUCTURE AND REGULATION OF CHINA'S TELECOMMUNICATIONS INDUSTRY

CHINA'S TELECOMMUNICATIONS INDUSTRY IS SUBJECT TO EXTENSIVE GOVERNMENT REGULATION

China's telecommunications industry is heavily regulated by the Ministry of Information Industry. The Ministry of Information Industry has broad discretion and authority to regulate all aspects of the telecommunications and information technology industry in China, including managing spectrum bandwidths, setting network equipment specifications and standards and drafting laws and regulations related to the electronics and telecommunications industries. Additionally, the Ministry of Information Industry can unilaterally, or in concert with other relevant authorities, decide what types of equipment may be connected to the national telecommunications networks, the forms and types of services that may be offered to the public, the rates that are charged to subscribers for those services and the content of material available in China over the Internet. If the Ministry of Information Industry sets standards with which we are unable to comply or which render our products noncompetitive, our ability to sell products in China may be limited, resulting in substantial harm to our operations.

At the end of May 2000, we became aware of an internal notice, circulated within the Ministry of Information Industry, announcing a review of PHS-based telecommunications equipment for future

installation into China's telecommunications infrastructure. The Ministry of Information Industry requested service providers to temporarily halt new deployments of PHS-based telecommunications equipment, including our PAS systems and handsets, pending conclusion of a review by the Ministry of Information Industry. Subsequently, at the end of June 2000, the Ministry of Information Industry issued a notice stating that it had concluded its review of PHS-based equipment and that the continued deployment of PHS-based systems, such as our PAS systems and handsets, in China's county-level cities and towns and villages would be permitted. In addition, the notice stated that deployments within large and medium-sized cities would only be allowed in very limited areas of dense population, such as campuses, commercial buildings and special development zones. The notice confirmed, however, that new citywide deployments of our PAS system in large and medium cities would not be permitted. Failure of the Ministry of Information Industry to permit the sale or deployment of our PAS systems and handsets, or the sale or deployment of our other products, or the imposition of additional limitations on their sale in the future could have a material adverse effect on our business and financial condition. The Ministry of Information Industry may conduct further reviews or evaluations of PHS-based telecommunications equipment or may change its position regarding PHS-based systems in the future.

CHINA'S TELECOMMUNICATIONS REGULATORY FRAMEWORK IS IN THE PROCESS OF BEING DEVELOPED, WHICH HAS LED TO UNCERTAINTIES REGARDING HOW TO CONDUCT OUR BUSINESS IN CHINA

China does not yet have a national telecommunications law. However, to provide a uniform regulatory framework for the telecommunication industry, the Chinese government is currently preparing a draft of such a law (the "Telecommunication Law"). If and when the Telecommunication Law is adopted by the National People's Congress or its standing committee, it is expected to provide a new regulatory framework for telecommunications regulation in China. We do not yet know the final nature or scope of the regulation that would be created if the Telecommunications Law is passed. Accordingly, we cannot predict whether it will have a positive or negative effect on us or on some or all aspects of our business.

China's telecommunications regulatory framework is in the process of being developed. In September 2000, the State Council issued the Telecommunications Regulations of the People's Republic of China, known as the Telecom Regulations. The Telecom Regulations cover telecommunications services and market regulations, pricing, interconnection and connection, as well as telecommunications construction and security issues. In May 2001, the Ministry of Information Industry issued the Administrative Measures of Network Access Licenses to implement the Telecom Regulations. Regulations in this area often require subjective interpretation and, given the relative infancy of the Telecom Regulations and the implementing regulations, we do not know how the regulations will be interpreted or enforced. As a result, our attempts to comply with these regulations may be deemed insufficient by the appropriate regulatory agencies, which could subject us to penalties that adversely affect our business.

OUR BUSINESS MAY SUFFER AS A RESULT OF THE RECENT RESTRUCTURING OF CHINA TELECOM

In February 1999, the State Council approved a restructuring plan for the China Telecom system, under which the telecommunications operations of the China Telecom system were separated along four business lines: fixed line, mobile, paging and satellite communications services. Following the announcement, we observed a reduction in orders from Telecommunications Companies, which we attributed to the uncertainties surrounding the restructuring and the ultimate impact the restructuring would have on the Telecommunications Companies.

Effective in May 2002, China Telecom was split into two entities by region, northern and southern. The 10 northern provinces, municipalities and autonomous regions of China Telecom were merged with

China Netcom Co. Ltd. and China Jitong Network Communications Co. Ltd. to form a new company known as China Netcom ("China Netcom"). The remaining 21 provinces, municipalities and autonomous regions now constitute the southern entity, and have kept the name of China Telecom (the "New China Telecom"). China Netcom inherited 30% of the old China Telecom's national backbone network, with the rest going to the New China Telecom. As this change is very recent, we cannot be certain what impact the restructuring of China Telecom will have on our business operations. However, we may experience another decline in orders and related revenues similar to that which we experienced following the 1999 restructuring, resulting from uncertainty among our telecommunications company customers associated with the restructuring. Additionally, China Telecom completed its initial public offering in November 2002, and is now a publicly listed on the New York Stock Exchange. Moreover, following any restructuring, China Netcom, the New China Telecom or any other entity that may replace it as a result of any subsequent restructuring may restrict or prohibit the sales of our products, which could cause substantial harm to our business.

WE DO NOT HAVE SOME OF THE LICENSES WE ARE REQUIRED TO HAVE TO SELL OUR NETWORK ACCESS PRODUCTS IN CHINA

Under China's current regulatory structure, the communications products that we offer in China must meet government and industry standards, and a network access license for the equipment must be obtained. Without the license, the equipment is not allowed to be connected to public telecommunications networks or sold in China. Moreover, we must ensure that the quality of the telecommunications equipment for which we have obtained a network access license is stable and reliable, and may not lower the quality or performance of other installed licensed products. The State Council's product quality supervision department, in concert with the Ministry of Information Industry, performs spot checks to track and supervise the quality of licensed telecommunications equipment and publishes the results of such spot checks.

The regulations implementing these requirements are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. We have obtained the required network access licenses for our AN-2000 platform. We have applied for, but have not yet received, a network access license for our PAS systems and handsets. Based upon conversations with the Ministry of Information Industry, we understand that our PAS systems and handsets are considered to still be in the trial period and that sales of our PAS systems and handsets may continue to be made by us during this trial period, but a license will ultimately be required. Network access licenses will also be required for most additional products that we are selling or may sell in China, including our mSwitch platform. If we fail to obtain the required licenses, we could be prohibited from making further sales of the unlicensed products, including our PAS systems and handsets, in China, which would substantially harm our business, financial condition and results of operations. Our counsel in China has advised us that China's governmental authorities may interpret or apply the regulations with respect to which licenses are required and the ability to sell a product while a product is in the trial period in a manner that is inconsistent with the information received by our counsel in China, either of which could have a material adverse effect on our business and financial condition.

WE ARE REQUIRED TO REGISTER THE SOFTWARE INCORPORATED IN OUR PRODUCTS IN ACCORDANCE WITH RELEVANT CHINESE REGULATIONS

In October 2000, the Ministry of Information Industry issued regulations which prohibit the production and sale of software products, or products incorporating software, in China unless the software is registered with the government. We have accomplished the necessary registration with regards to the software incorporated in our AN-2000, PAS and mSwitch products. However, additional registration is required for software incorporated in additional products that we are selling or may sell in China. Based upon verbal advice received from the Ministry of Information Industry, we believe that we will be able to sell products incorporating our software while any of our applications for registration may be pending. However, the Chinese government may interpret or apply the regulations in such a way as to prohibit sales of products incorporating our unregistered software prior to registration. If the government prohibits sales pending registration, or if we fail in our efforts to register any software required to be registered, we could be prohibited from making further sales of products incorporating our unregistered software in China, which could substantially harm our business and financial condition.

MOST OF OUR CUSTOMERS IN CHINA HAVE HISTORICALLY BEEN PART OF THE CHINA TELECOM SYSTEM AND UNDER CHINA TELECOM'S ULTIMATE CONTROL; FOLLOWING THE RECENT RESTRUCTURING OF CHINA TELECOM, MOST OF OUR CUSTOMERS IN CHINA ARE NOW PART OF THE NEW CHINA TELECOM OR CHINA NETCOM, AND ARE SUBJECT TO THEIR ULTIMATE CONTROL

Our main customers in China are the local Telecommunications Companies (formerly known as Telecommunications Bureaus) which historically operated under China Telecom, China's state-owned fixed line operator, and were subject to its ultimate control. Following the recent restructuring of China Telecom, the Telecommunications Companies now operate under the ultimate control of either the New China Telecom or China Netcom. China Telecom completed its initial public offering in November 2002, and is listed on the New York Stock Exchange. Policy statements may be issued and decisions may be made by the New China Telecom and China Netcom, which govern the equipment purchasing decisions of most of our customers in China. For example, in late 1999, China Telecom prohibited all Telecommunications Companies from purchasing PHS systems, such as our PAS systems, for implementation in large cities, even before these sales were prohibited by the Ministry of Information Industry. As most of our sales are generated from our operations in China, any decisions by the New China Telecom or China Netcom restricting or prohibiting the sales or deployment of our products could cause significant harm to our business.

OUR CUSTOMER BASE IN CHINA COULD EFFECTIVELY BECOME INCREASINGLY CONCENTRATED IF MORE PURCHASING DECISIONS ARE COORDINATED OR MADE BY PROVINCIAL OR GREATER REGIONAL TELECOMMUNICATIONS SERVICE ENTITIES RATHER THAN BY LOCAL TELECOMMUNICATIONS SERVICE PROVIDERS

We have historically considered local telecommunications service providers serving municipalities and counties to be our primary customers in China. Recently, however, the provincial-level telecommunications service entity in the Zhejiang province of China has begun to consolidate telecommunications purchasing decisions for that province. As a result of this trend in the Zhejiang province, we have grouped all customers in Zhejiang province together and have treated these as one customer for 2002 and the comparative periods presented. In 2002 and 2001, Zhejiang province accounted for more than 10% of our net sales. At December 31, 2002, we have approximately thirty-three customers in Zhejiang province.

Whether this represents the beginning of a greater trend throughout China towards increased consolidation of negotiations and purchasing decisions into the control of provincial-level telecommunications service entities is unclear. If an increasing number of purchasing decisions and negotiations are controlled on a larger regional level in China by provincial-level telecommunications service entities, this would effectively result in a concentration of the Company's customer base. The Company's financial results may increasingly depend in significant part upon the success of a few major customers and the Company's ability to meet their future capital equipment needs. Although the composition of the group comprising the Company's largest customers may vary from period to period, the loss of a significant customer or any reduction in orders by any significant customer, including reductions due to market, economic or competitive conditions in the telecommunications industry, may have a material adverse effect on the Company's business, financial condition and results of operations.

In addition to the business risks associated with dependence on major customers, significant customer concentration may also result in significant concentrations of accounts receivable. Significant and concentrated receivables would expose the Company to additional risks, including the risk of default by one or more customers representing a significant portion of the Company's total receivables. If the Company is required to take additional accounts receivable reserves, its business, financial condition and results of operations would be materially adversely affected.

OUR ABILITY TO SELL OUR PAS WIRELESS SYSTEMS AND HANDSETS COULD BE SIGNIFICANTLY IMPAIRED IF THE NEW CHINA TELECOM OR CHINA NETCOM ARE GRANTED, OR IF THEY OTHERWISE ACQUIRE, MOBILE LICENSES

ALLOWING THE NEW CHINA TELECOM OR CHINA NETCOM TO DELIVER CELLULAR SERVICES

The New China Telecom and China Netcom hold and operate the fixed line telephone and data communications assets in China, and currently do not have the licenses necessary to offer cellular services. To offer wireless services to end users, the Telecommunications Companies must offer services that can be delivered over wireline networks, such as those delivered over our PAS wireless systems and handsets. China's media sources have widely reported that after the restructuring of China Telecom, the Ministry of Information Industry may grant mobile licenses to the New China Telecom or China Netcom, or to both. If the Ministry of Information Industry does grant a mobile license to the New China Telecom or China Netcom, or to both, or if such entities otherwise acquire mobile licenses, local Telecommunications Companies will be free to offer cellular services such as GSM or CDMA to their customers, and they may therefore elect not to deploy our PAS systems and handsets. If this were to occur, we could lose current and potential customers for our PAS systems and handsets, and our financial condition and results of operations could be materially adversely affected.

CHANGES IN TELECOMMUNICATIONS RATES OR PRICING POLICIES MAY RESULT IN DECREASED DEMAND FOR OUR PRODUCTS

In November 2000, the Ministry of Information Industry announced significant changes in rates for telecommunications services in China. While long distance, international, leased line and Internet connection fees were cut by up to 70%, the rates for local telephone services, which include certain types of wireless access services such as those offered over our PAS systems and handsets, were increased, from approximately $0.01 per minute to approximately $0.02 per minute. The increase in rates may result in a reduced demand by end users for wireless services delivered over our PAS system and a corresponding decline in demand for our products. In addition, mobile operators are offering price incentive plans that could impact demand for our products. Additionally, the Ministry of Information Industry may implement future rate changes for wireline or wireless services in China or change telecommunications pricing policies, including allowing carriers to set prices based on market conditions, any of which may lead to reduced demand for our systems and products and result in a material adverse effect on our business or results of operations.

RISKS RELATING TO CONDUCTING OPERATIONS IN CHINA

SALES IN CHINA HAVE ACCOUNTED FOR MOST OF OUR SALES, AND THEREFORE, OUR BUSINESS, FINANCIAL CONDITION AND RESULTS OF OPERATIONS ARE TO A SIGNIFICANT DEGREE SUBJECT TO ECONOMIC, POLITICAL AND SOCIAL EVENTS IN CHINA

Approximately $822.3 million, or 83.8%, of our net sales in fiscal 2002, $565.9 million, or 90.3%, of our net sales in fiscal 2001, and $364.0 million, or 98.8%, of our net sales in fiscal 2000 occurred in China. Additionally, a substantial portion of our fixed assets are located in China. Of our total fixed assets, approximately 87.8% as of December 31, 2002, 75.3% as of December 31, 2001 and 75.0% as of December 31, 2000 were in China. We expect to make further investments in China in the future. Therefore, our business, financial condition and results of operations are to a significant degree subject to economic, political and social events in China.

DEVALUATION IN THE VALUE OF THE RENMINBI AND FLUCTUATIONS IN EXCHANGE RATES COULD ADVERSELY AFFECT OUR FINANCIAL RESULTS

Exchange rate fluctuations could have a substantial negative impact on our financial condition and results of operations. We purchase substantially all of our materials in the United States and Japan and a significant portion of our cost of goods sold is incurred in U.S. dollars and Japanese yen. A significant portion of our operating expenses are incurred in U.S. dollars. At the same time, most of our sales are denominated in Renminbi. The value of the Renminbi is fixed by China's national government and is subject to changes in China's governmental policies and to international economic and political developments. China may choose to devalue the Renminbi against the U.S. dollar. Additionally, China's government has considered from time to time whether to partially or fully abandon the official exchange rate for Renminbi to the U.S. dollar. The abandonment of this official exchange rate policy may lead to sharp depreciation of the Renminbi against the U.S. dollar and other foreign currencies and to significantly more volatility in the Renminbi exchange rate in the future, both of which would adversely affect our financial results and make our future results more subject to fluctuation.

In the past, financial markets in many Asian countries have experienced severe volatility and, as a result, some Asian currencies have experienced significant devaluation from time to time. The devaluation of some Asian currencies may have the effect of rendering exports from China more expensive and less competitive and therefore place pressure on China's government to devalue the Renminbi. Any devaluation of the Renminbi could result in an increase in volatility of Asian currency and capital markets. Future volatility of Asian financial markets could have an adverse impact on our ability to expand our product sales into Asian markets outside of China. Moreover, due to the limitations on the convertibility of Renminbi, we are limited in our ability to engage in currency hedging activities in China and do not currently engage in currency hedging activities with respect to international sales outside of China.

CURRENCY RESTRICTIONS IN CHINA MAY LIMIT THE ABILITY OF OUR SUBSIDIARIES AND JOINT VENTURES IN CHINA TO OBTAIN AND REMIT FOREIGN CURRENCY NECESSARY FOR THE PURCHASE OF IMPORTED COMPONENTS AND MAY LIMIT OUR ABILITY TO OBTAIN AND REMIT FOREIGN CURRENCY IN EXCHANGE FOR RENMINBI EARNINGS

China's government imposes controls on the convertibility of Renminbi into foreign currencies and, in certain cases, the remittance of currency out of China. Under the current foreign exchange control system, sufficient foreign currency may not be available to satisfy our currency needs. Shortages in the availability of foreign currency may restrict the ability of our Chinese subsidiaries to obtain and remit sufficient foreign currency to pay dividends to us, or otherwise satisfy their foreign currency denominated obligations, such as payments to us for components which we export to them and for technology licensing fees. We may also experience difficulties in completing the administrative procedures necessary to obtain and remit needed foreign currency. Our business could be substantially harmed if we are unable to convert and remit our sales received in Renminbi into U.S. dollars. Under existing foreign exchange laws, Renminbi held by our China subsidiaries can be converted into foreign currencies and remitted out of China to pay current account items such as payments to suppliers for imports, labor services, payment of interest on foreign exchange loans and distributions of dividends so long as the subsidiaries have adequate amounts of Renminbi to purchase the foreign currency. Expenses of a capital nature such as the repayment of bank loans denominated in foreign currencies, however, require approval from appropriate governmental authorities before Renminbi can be used to purchase foreign currency and then remitted out of China. This system could be changed at any time by executive decision of the State Council to impose limits on current account convertibility of the Renminbi or other similar restrictions. Moreover, even though the Renminbi is intended to be freely convertible under the current account, the State Administration of Foreign Exchange, which is responsible for administering China's foreign currency market, has a significant degree of administrative

discretion in implementing the laws. From time to time, the State Administration of Foreign Exchange has used this discretion in ways which effectively limit the convertibility of current account payments and restrict remittances out of China. Furthermore, in many circumstances the State Administration of Foreign Exchange must approve foreign currency conversions and remittances. Under the current foreign exchange control system, sufficient foreign currency may not be available at a given exchange rate to satisfy our currency demands.

CHINA SUBJECTS FOREIGN INVESTORS IN THE TELECOMMUNICATIONS INDUSTRY TO OWNERSHIP AND GEOGRAPHIC LIMITATIONS

China's government and its agencies, including the Ministry of Information Industry and the State Council, regulate foreign investment in the telecommunications industry through the promulgation of various laws and regulations and the issuance of various administrative orders and decisions. Currently, foreign investors may engage in such activities only in accordance with certain ownership and geographic limitations. China may promulgate new laws or regulations, or issue administrative or judicial decisions or interpretations, which would further restrict or bar foreigners from engaging in telecommunications-related activities. The promulgation of laws or regulations or the issuance of administrative orders or judicial decisions or interpretations restricting or prohibiting telecommunications activities by foreigners could have a substantial impact on our ongoing operations.

GOVERNMENTAL POLICIES IN CHINA COULD IMPACT OUR BUSINESS

Since 1978, China's government has been and is expected to continue reforming its economic and political systems. These reforms have resulted in and are expected to continue to result in significant economic and social development in China. Many of the reforms are unprecedented or experimental and may be subject to change or readjustment due to a number of political, economic and social factors. We believe that the basic principles underlying the political and economic reforms will continue to be implemented and provide the framework for China's political and economic system. New reforms or the readjustment of previously implemented reforms could have a significant negative effect on our operations. Changes in China's political, economic and social conditions and governmental policies which could have a substantial impact on our business include:

- new laws and regulations or the interpretation of those laws and regulations;

the introduction of measures to control inflation or stimulate growth;

changes in the rate or method of taxation;

the imposition of additional restrictions on currency conversion and remittances abroad; and

any actions which limit our ability to develop, manufacture, import or sell our products in China, or to finance and operate our business in China.

ECONOMIC POLICIES IN CHINA COULD IMPACT OUR BUSINESS

The economy of China differs from the economies of most countries belonging to the Organization for Economic Cooperation and Development in various respects such as structure, government involvement, level of development, growth rate, capital reinvestment, allocation of resources, self-sufficiency, rate of inflation and balance of payments position. In the past, the economy of China has been primarily a planned economy subject to one- and five-year state plans adopted by central government authorities and largely implemented by provincial and local authorities, which set production and development targets.

Since 1978, increasing emphasis had been placed on decentralization and the utilization of market forces in the development of China's economy. Economic reform measures adopted by China's government may be inconsistent or ineffectual, and we may not in all cases be able to capitalize on any reforms. Further, these measures may be adjusted or modified in ways which could result in economic liberalization measures that are inconsistent from time to time or from industry to industry or across different regions of the country. China's economy has experienced significant growth in the past decade. This growth, however, has been accompanied by imbalances in China's economy and has resulted in significant fluctuations in general price levels, including periods of inflation. China's government has implemented policies from time to time to increase or restrain the rate of economic growth, control periods of inflation or otherwise regulate economic expansion. While we may be able to benefit from the effects of some of these policies, these policies and other measures taken by China's government to regulate the economy could also have a significant negative impact on economic conditions in China with a resulting negative impact on our business.

CHINA'S ENTRY INTO THE WORLD TRADE ORGANIZATION CREATES UNCERTAINTY AS TO THE FUTURE ECONOMIC AND BUSINESS ENVIRONMENTS IN CHINA

China's entry into the WTO was approved in September 2001. Entry into the WTO will require China to further reduce tariffs and eliminate non-tariff barriers, which include quotas, licenses and other restrictions by 2005 at the latest. While China's entry into the WTO and the related relaxation of trade restrictions may lead to increased foreign investment, it may also lead to increased competition in China's markets from international companies. China's entry into the WTO could have a negative impact on China's economy with a resulting negative impact on our business.

IF TAX BENEFITS AVAILABLE TO OUR SUBSIDIARIES LOCATED IN CHINA ARE REDUCED OR REPEALED, OUR BUSINESS COULD SUFFER

Our subsidiaries and joint ventures located in China enjoy tax benefits in China which are generally available to foreign investment enterprises, including full exemption from national enterprise income tax for two years starting from the first profit-making year and/or a 50% reduction in national income tax rate for the following three years. In addition, local enterprise income tax is often waived or reduced during this tax holiday/incentive period. Under current regulations in China, foreign investment enterprises that have been accredited as technologically advanced enterprises are entitled to additional tax incentives. These tax incentives vary in different locales and could include preferential national enterprise income tax treatment at 50% of the usual rates for different periods of time. All of our active subsidiaries in China were accredited as technologically advanced enterprises. The tax holidays applicable to our wholly-owned subsidiaries, UTStarcom China and HUTS, which together accounted for approximately 83.8% of our revenues in 2002, expired at the end of 2002 and 2001, respectively. Unless the tax holidays are extended for the entities, for 2003 the tax rates will increase from 7.5% to 15% and from 10% to 15%, respectively, which could negatively impact our financial condition and results of operations. During the fourth quarter of 2002, we formed a new entity, Hangzhou UTStarcom Telecom Co., Ltd., to manufacture and sell handsets. This entity will benefit from a two year income tax exemption, and a 50% income tax reduction in the following three years. The Chinese government is considering the imposition of "unified" corporate income tax that would phase out, over time, the preferential tax treatment to which foreign-funded enterprises, such as UTStarcom, are currently entitled. While it is not certain whether the government will implement such a unified tax structure or whether, if implemented, UTStarcom will be grandfathered into the new tax structure, if the new tax structure is implemented, it will adversely affect our financial condition.

CHINA'S LEGAL SYSTEM EMBODIES UNCERTAINTIES THAT COULD NEGATIVELY IMPACT OUR BUSINESS

China has a civil law system. Decided court cases do not have binding legal effect on future decisions. Since 1979, many new laws and regulations covering general economic matters have been promulgated in China. Despite this activity to develop the legal system, China's system of laws is not yet complete. Even where adequate law exists in China, enforcement of existing laws or contracts based on existing law may be uncertain and sporadic and it may be difficult to obtain swift and equitable enforcement, or to obtain enforcement of a judgment by a court of another jurisdiction. The relative inexperience of China's judiciary in many cases creates additional uncertainty as to the outcome of any litigation. Further, interpretation of statutes and regulations may be subject to government policies reflecting domestic political changes. Moreover, government policies and internal rules promulgated by governmental agencies may not be published in time, or at all. As a result, we may operate our business in violation of new rules and policies without having any knowledge of their existence.

China has adopted a broad range of related laws, administrative rules and regulations that govern the conduct and operations of foreign investment enterprises and restrict the ability of foreign companies to conduct business in China. These laws, rules and regulations provide some incentives to encourage the flow of investment into China, but also subject foreign companies, and foreign investment enterprises, including our subsidiaries in China, to a set of restrictions that may not always apply to domestic companies in China. As a result of its admission into the WTO, China is increasingly according foreign companies and foreign investment enterprises established in China the same rights and privileges as Chinese domestic companies. These special laws, administrative rules and regulations governing foreign companies and foreign investment enterprises may still place us and our subsidiaries at a disadvantage in relation to Chinese domestic companies and may adversely affect our competitive position. Moreover, as China's legal system develops, the promulgation of new laws, changes to existing laws and the pre-emption of local regulations by national laws may adversely affect foreign investors and companies. Many of our activities and products in China are subject to administrative review and approval by various national and local agencies of China's government. Because of the changes occurring in China's legal and regulatory structure, we may not be able to secure the requisite governmental approval for our activities and products. Failure to obtain the requisite government approval for any of our activities or products could substantially harm our business.

NEW MANUFACTURING FACILITY

We have purchased the rights to use 49 acres of land located in Zhejiang Science and Technology Industry Garden of Hangzhou Hi-tech Industry Development Zone. As of December 31, 2002, we have completed the foundation and ground work and have commenced construction of the building. Capital expenditures were $38.6 million in 2002. We expect that construction of the new facility will be completed in 2003 at a projected cost of approximately $95.6 million. If we are unable to complete the construction on a timely basis our business may be harmed.

RISKS RELATING TO OUR STOCK PERFORMANCE

OUR STOCK PRICE IS HIGHLY VOLATILE

The trading price of our common stock has fluctuated significantly since our initial public offering in March 2000. Our stock price could be subject to wide fluctuations in the future in response to many events or factors, including those discussed in the preceding risk factors relating to our operations, as well as:

- actual or anticipated fluctuations in operating results, actual or anticipated gross profit as a percentage of net sales, levels of inventory, our actual or anticipated rate of growth and our actual or anticipated earnings per share;

- changes in expectations as to future financial performance or changes in financial estimates or buy/sell recommendations of securities analysts;

- changes in governmental regulations or policies in China, such as the temporary suspension of sales of our PAS systems that occurred in May and June of 2000, which caused our stock price to drop;

- our, or a competitor's, announcement of new products, services or technological innovations;

- the operating and stock price performance of other comparable companies; and

- news and commentary emanating from the media, securities analysts, and government bodies in China relating to UTStarcom and to the industry in general.

General market conditions and domestic or international macroeconomic factors unrelated to our performance may also affect our stock price. For these reasons, investors should not rely on recent trends to predict future stock prices or financial results. In addition, following periods of volatility in a company's securities, securities class action litigation against a company is sometimes instituted. This type of litigation could result in substantial costs and the diversion of management time and resources.

SOFTBANK CORP. AND ITS RELATED ENTITIES, INCLUDING SOFTBANK AMERICA INC., HAS SIGNIFICANT INFLUENCE OVER OUR MANAGEMENT AND AFFAIRS, WHICH IT COULD EXERCISE AGAINST YOUR BEST INTERESTS

SOFTBANK CORP. and its related entities, including SOFTBANK America Inc., beneficially own 21.2% of our outstanding stock. As a result, SOFTBANK CORP. and its related entities, including SOFTBANK America Inc., have the ability to exercise significant influence over all matters submitted to our stockholders for approval and exert significant influence over our management and affairs. This concentration of ownership may delay or prevent a change of control or discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of our company, which could decrease the market price of our common stock. Matters that could require stockholder approval include:

- election and removal of directors;

- merger or consolidation of our company; and

- sale of all or substantially all of our assets.

The interests of SOFTBANK America Inc. may not always coincide with our interests. SOFTBANK America Inc., acting through its designees on the Board of Directors and through its ownership of voting securities, will have the ability to exercise significant influence over our actions irrespective of the desires of our other stockholders or directors. On August 29, 2002, we completed the repurchase of six million shares of our common stock for $72.9 million from SOFTBANK CORP., reducing their beneficial ownership to 21.2%. We may make additional stock repurchases in the future in order to continue to mitigate this ownership influence.

DELAWARE LAW AND OUR CHARTER DOCUMENTS CONTAIN PROVISIONS THAT COULD DISCOURAGE OR PREVENT A POTENTIAL TAKEOVER, EVEN IF THE TRANSACTION WOULD BENEFIT OUR STOCKHOLDERS

Other companies may seek to acquire or merge with us. An acquisition or merger of our company could result in benefits to our stockholders, including an increase in the value of our common stock. Some provisions of our Certificate of Incorporation and Bylaws, as well as provisions of Delaware law,

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may discourage, delay or prevent a merger or acquisition that a stockholder may consider favorable. These provisions include:

authorizing the Board of Directors to issue additional preferred stock;

prohibiting cumulative voting in the election of directors;

limiting the persons who may call special meetings of stockholders;

prohibiting stockholder action by written consent;

creating a classified Board of Directors pursuant to which our directors are elected for staggered three year terms; and

establishing advance notice requirements for nominations for election to the Board of Directors and for proposing matters that can be acted on by stockholders at stockholder meetings.

ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to the impact of interest rate changes, changes in foreign currency exchange rates and changes in the stock market.

Interest Rate Risk. Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio. The fair value of our investment portfolio would not be significantly affected by either a 10% increase or decrease in interest rates due mainly to the short-term nature of most of our investment portfolio. However, our interest income can be sensitive to changes in the general level of U.S. interest rates since the majority of our funds are invested in instruments with maturities less than one year. Our policy is to limit the risk of principal loss and ensure the safety of invested funds by generally attempting to limit market risk. Funds in excess of current operating requirements are mostly invested in government-backed notes, commercial paper, floating rate corporate bonds, fixed income corporate bonds and tax exempt instruments. In accordance with our investment policy, all short-term investments are invested in "investment grade" rated securities with minimum A or better ratings. Currently, most of our short-term investments have AA or better ratings.

The table below represents carrying amounts and related weighted-average interest rates of our investment portfolio at December 31, 2002:

(In thousands, except interest rates)	
Cash and cash equivalents	$ 231,944
Average interest rate	1.3%
Restricted cash	$ 9,779
Average interest rate	1.3%
Short-term investments	$ 107,305
Average interest rate	1.5%
Long-term investments	$ 1,092
Average interest rate	1.8%
Total investment securities	$ 350,120
Average interest rate	1.4%

Equity Investment Risk. Our investment portfolio includes equity investments in publicly traded companies, the values of which are subject to market price volatility. Recent events have adversely affected the public equities market and general economic conditions may continue to worsen. Should the fair value of our publicly traded equity investments decline below their cost basis in a manner deemed to be other-than-temporary, our earnings may be adversely affected. We have also invested in several privately held companies as well as investment funds which invest primarily in privately held

companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky, as the market for the technologies or products they have under development are typically in the early stages and may never materialize.

Foreign Exchange Rate Risk. We are exposed to foreign exchange rate risk because most of our sales in China are denominated in Renminbi and portions of our accounts payable are denominated in Japanese Yen. Due to the limitations on converting Renminbi, we are limited in our ability to engage in currency hedging activities in China. Although the impact of currency fluctuations of Renminbi to date has been insignificant, fluctuations in currency exchange rates in the future may have a material adverse effect on our results of operations. We have a multi-currency bank account in Japanese Yen for purchasing portions of our inventories and supplies. The balance of this Japanese Yen account at December 31, 2002 was approximately $7.1 million.

ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements and Financial Statement Schedules

All other schedules are omitted because they are not applicable or the required information is shown in the consolidated financial statements or notes thereto.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of UTStarcom, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of UTStarcom, Inc. and its subsidiaries (the Company) at December 31, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 3 to the Consolidated Financial Statements, in 2000 the Company changed its method of accounting for revenue recognition.

/s/ PRICEWATERHOUSECOOPERS LLP
San Francisco, California
January 23, 2003

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UTSTARCOM, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

	December 31, 2002	December 31, 2001
ASSETS		
Current assets:		
Cash and cash equivalents	$ 231,944	$ 321,136
Short-term investments	107,305	86,176
Accounts receivable, net of allowances for doubtful accounts of $26,250 and $19,053 at December 31, 2002 and 2001, respectively	222,050	194,716
Inventories	424,666	229,050
Other current assets	121,407	65,397
Total current assets	1,107,372	896,475
Property, plant and equipment, net	98,511	43,942
Long-term investments	35,360	17,818
Goodwill, net	44,806	34,813
Intangible assets, net	5,014	4,179
Other long-term assets	14,489	8,653
Total assets	$ 1,305,552	$ 1,005,880
LIABILITIES, MINORITY INTEREST AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 256,980	$ 83,649
Debt		58,434
Deferred revenue	164,247	76,424
Income taxes payable	13,003	10,536
Other current liabilities	104,927	76,329
Total current liabilities	539,157	305,372
Long-term debt		12,048
Total liabilities	539,157	317,420
Minority interest in consolidated subsidiaries		6,573
Commitments and Contingencies		

	December 31,	
Stockholders' equity:		
Preferred stock: $.00125 par value; authorized: 5,000,000 shares; issued and outstanding: none at December 31, 2002 and 2001		
Common stock: $.00125 par value; authorized: 250,000,000 shares; issued and outstanding: 106,787,908 at December 31, 2002 and 109,302,816 at December 31, 2001	135	138
Additional paid-in capital	658,546	638,697
Deferred stock compensation	(11,766)	(6,045)
Retained earnings	120,520	49,146
Notes receivable from stockholders	(282)	(381)
Accumulated other comprehensive income (loss)	(758)	332
Total stockholders' equity	766,395	681,887
Total liabilities, minority interest, and stockholders' equity	$ 1,305,552	$ 1,005,880

See accompanying notes to consolidated financial statements.

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UTSTARCOM, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Years Ended December 31,		
	2002	**2001**	**2000**
Net sales			
Unrelated parties	$ 858,768	$ 612,907	$ 368,646
Related parties	123,038	13,933	
Total net sales	981,806	626,840	368,646
Cost of sales (includes stock compensation expense of $20, $41, and $90)	636,334	402,292	240,465
Gross profit	345,472	224,548	128,181
Operating expenses:			
Selling, general and administrative expenses (includes stock compensation expense of $1,237, $2,499, and $4,676)	110,263	75,764	48,055
Research and development expenses (includes stock compensation expense of $1,843, $2,660, and $6,795)	86,182	59,809	41,452
Amortization of intangible assets	2,395	7,527	4,894
In-process research and development costs	670	4,720	
Total operating expenses	199,510	147,820	94,401

	Years Ended December 31,		
Operating income	145,962	76,728	33,780
Interest income	5,522	8,572	12,195
Interest expense	(1,251)	(3,909)	(3,311)
Other income (expense), net	(9,908)	(330)	1,945
Equity in net loss of affiliated companies	(4,053)	(2,962)	(288)
Income before income taxes, minority interest and cumulative effect of a change of accounting principle	136,272	78,099	44,321
Income tax expense	27,254	19,823	14,021
Income before minority interest and cumulative effect of a change in accounting principle	109,018	58,276	30,300
Minority interest in earnings of consolidated subsidiaries	(1,156)	(1,322)	(2,307)
Income before cumulative effect of a change of accounting principle	107,862	56,954	27,993
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"			(980)
Net income	$ 107,862	$ 56,954	$ 27,013
Basic earnings (loss) per share:			
Net income	$ 0.98	$ 0.56	$ 0.35
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"			(0.01)
Net income	$ 0.98	$ 0.56	$ 0.34
Diluted earnings (loss) per share:			
Net income	$ 0.94	$ 0.52	$ 0.28
Cumulative effect on prior years of the application of SAB 101, "Revenue Recognition in Financial Statements"			(0.01)
Net income	$ 0.94	$ 0.52	$ 0.27
Weighted average shares used in per-share calculation:			
Basic	109,566	101,433	79,696
Diluted	114,407	108,612	101,867

See accompanying notes to consolidated financial statements.

UTSTARCOM, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands, except share data)

Preferred Stock	Common Stock

	Preferred Stock		Common Stock								
	Issued	**Amount**	**Shares**	**Amount**	**Additional Paid-in-Capital**	**Deferred Stock Compensation**	**Retained Earnings (Accumulated Deficit)**	**Notes Receivable from Stockholders**	**Accumulated Other Comprehensive Income (Loss)**	**Total Stockholders' Equity**	**Comprehensive Income**
Balances, December 31, 1999	70,377,322	$ 88	8,929,837	$ 13	$ 218,692	$ (17,792)	$ (34,821)	$ (555)	$ 95	$ 165,720	
Common stock issued upon Initial Public Offering, net of expenses			11,500,000	14	189,391					189,405	
Conversion of preferred stock to common stock upon Initial Public Offering	(70,377,322)	(88)	70,377,322	88							
Exercise of common stock warrant			500,000	1	3,124					3,125	
Common stock issued upon exercise of options			3,651,687	4	4,551					4,555	
Common stock issued upon ESPP purchases			73,811		1,130					1,130	
Distribution to stockholders					1,889					1,889	
Deferred stock compensation related to grant of stock options					260	(260)					
Amortization of deferred stock compensation						11,561				11,561	
Tax Benefits for non-qualified stock option exercises					7,628					7,628	
Repayment of notes receivable from stockholders								241		241	
Net income							27,013			27,013	$ 27,013
Other comprehensive income:											
Unrealized holding gain (loss)									52	52	52
Total comprehensive income											$ 27,065
Balances, December 31, 2000			95,032,657	120	426,665	(6,491)	(7,808)	(314)	147	412,319	
Common stock issued upon exercise of options			5,363,601	8	18,756					18,764	
Common stock issued upon ESPP purchases			118,223		1,866					1,866	
Common stock issued related to acquisition of			439,810		10,700					10,700	

	Preferred Stock		Common Stock								
Stable Gain											
Common stock issued upon secondary offering, net of expenses				9	139,911					139,920	
Common stock issued for ACD acquisition, net of expenses			7,400,000 948,525	1	20,733					20,734	
ACD deferred compensation					5,000	(5,000)					
Amortization of deferred compensation related to ACD acquisition						1,250				1,250	
Amortization of deferred stock compensation related to grants of stock options to employees					23	3,928				3,951	
Cancellation of deferred compensation charges due to employee terminations					(268)	268					
Tax benefits for non-qualified stock option exercises					15,311					15,311	
Notes receivable from stockholders								(67)		(67)	
Net income							56,954			56,954	$ 56,954
Other comprehensive income (loss):											
Unrealized holding gain (loss)									211	211	211
Translation adjustment									(26)	(26)	(26)
Total comprehensive income											$ 57,139
Balances, December 31, 2001			109,302,816	138	638,697	(6,045)	49,146	(381)	332	681,887	
Common stock issued upon exercise of options			1,717,899	3	9,162					9,165	
Common stock issued upon Softbank offering, net of expenses			1,500,000	2	28,933					28,935	
Common stock issued upon ESPP purchases			182,437		2,828					2,828	
ACD acquisition-related			84,756								

	Preferred Stock		Common Stock								
stock issuances											
Buyback of Softbank shares, net of fees			)	(8)	(36,433)		(36,488)			(72,929)	
Cancellation of deferred compensation charges due to employee terminations			(6,000,000		(1,282)	1,282					
Amortization of deferred stock compensation					103	2,997				3,100	
Acquisition-related deferred compensation					10,000	(10,000)					
Tax benefits for non-qualified stock option exercises					6,538					6,538	
Notes receivable from stockholders								99		99	
Net income							107,862			107,862	$ 107,862
Other comprehensive income (loss):											
Unrealized holding gain (loss)									(952)	(952)	(952)
Translation adjustment									(138)	(138)	(138)
Total comprehensive income											$ 106,772
Balances, December 31, 2002		$	106,787,908	$ 135	$ 658,546	$ (11,766)	$ 120,520	$ (282)	$ (758)	$ 766,395	

See accompanying notes to the consolidated financial statements.

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UTSTARCOM, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Years ended December 31,		
	2002	**2001**	**2000**
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 107,862	$ 56,954	$ 27,013
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Cumulative effect of change in accounting principle			980

	Years ended December 31,		
Gain on change in ownership interest in subsidiary		(277)	
Depreciation and amortization	22,435	18,533	9,494
Non-qualified stock option exercise tax benefits	6,537	15,311	7,628
Write-off of in-process research and development costs	670	4,720	
Net loss on sale of assets	1,098	802	807
Impairment of long-term investments	4,442	1,690	
Stock compensation expense	3,100	5,200	11,561
Provision provided for doubtful accounts	7,197	6,218	6,045
Inventory write-downs	12,396	11,143	2,786
Equity in net (income) loss of affiliated companies	4,053	2,962	288
Minority interest in consolidated subsidiary	1,156	1,322	2,307
Changes in operating assets and liabilities:			
Accounts receivable	(34,207)	(39,196)	(87,177)
Inventories	(207,321)	(121,198)	(63,479)
Other current and non-current assets	(60,506)	(52,619)	(4,850)
Accounts payable	170,452	39,085	14,143
Income taxes payable	2,470	3,366	(1,721)
Other current liabilities	27,683	41,407	5,659
Deferred revenue	87,823	44,746	22,351
Net cash provided by (used in) operating activities	157,340	40,169	(46,165)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Additions to property, plant and equipment	(75,271)	(30,199)	(19,513)
Investment in affiliates	(28,933)	(9,779)	(8,226)
Purchase of minority interest		(705)	
Acquisition of businesses, net of cash acquired	(17,706)		
Proceeds from disposal of property, plant and equipment	175	214	164
Purchase of intangible assets		(1,078)	
Purchases of short-term investments	(140,583)	(89,625)	(124,096)
Sales of short-term investments	118,168	87,516	40,290
Net cash used in investing activities	(144,150)	(43,656)	(111,381)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Issuance of stock, net of expenses	40,928	160,550	198,213
Proceeds from borrowings	39,621	137,108	95,179
Payments for borrowings	(110,101)	(122,055)	(74,343)
Repurchase of common stock	(72,929)		
Proceeds (payments) from stockholder notes	99	(67)	245
Net cash (used in) provided by financing activities	(102,382)	175,536	219,294
Effects of exchange rates on cash		(25)	
Net (decrease) increase in cash and cash equivalents	(89,192)	172,024	61,748
Cash and cash equivalents at beginning of period	321,136	149,112	87,364
Cash and cash equivalents at end of period	$ 231,944	$ 321,136	$ 149,112

See accompanying notes to the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 DESCRIPTION OF BUSINESS

UTStarcom, Inc. ("the Company"), a Delaware corporation, designs, manufactures and markets wireline and wireless broadband access and switching equipment that enables migration to next generation IP-based networks. The Company's operations are conducted primarily by its foreign subsidiaries that manufacture, distribute and support the Company's products in international markets, principally China.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation:

The accompanying consolidated financial statements include the accounts of the Company and its wholly and majority (over 50 percent) owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in the preparation of the consolidated financial statements. Minority interest in consolidated subsidiaries and equity in affiliated companies are shown separately in the consolidated financial statements.

Reclassifications:

Certain reclassifications have been made in the prior years' financial statements to conform with the 2002 presentation. Such reclassifications had no impact on previously reported net income or stockholders' equity.

Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents:

Cash and cash equivalents consist of highly liquid monetary instruments with a maturity of three months or less at the date of purchase.

Short-term Investments:

Short-term investments consist of investments with original maturities of less than twelve months. In accordance with the Company's investment policy, all short-term investments are invested in "investment grade" rated securities with a minimum of A or better ratings. Currently, most of the Company's short-term investments have AA or better ratings. Marketable securities are classified as available-for-sale and are carried at fair value. Unrealized holding gains and losses on securities classified as available-for-sale are recorded as a separate component of stockholders' equity. Realized gains and losses are reported in earnings. The fair value of investments is based on quoted market

prices. The cost of securities is based on specific identification. At December 31, 2002 and 2001, short-term investments in available-for-sale securities consisted of (in thousands):

	December 31, 2002		
	Amortized Cost	Gross Unrealized Gains	Estimated Fair Value

	December 31, 2002		
Government and agency obligations	$ 11,006	$ 12	$ 11,018
Other debt securities	96,233	54	96,287
Total current available for-sale securities	$ 107,239	$ 66	$ 107,305

	December 31, 2001		
	Amortized Cost	Gross Unrealized Gains	Estimated Fair Value
Government and agency obligations	$ 32,695	$ 173	$ 32,868
Other debt securities	53,218	90	53,308
Total current available for-sale securities	$ 85,913	$ 263	$ 86,176

Inventories:

Inventories are stated at the lower of cost or market, net of an allowance for excess, slow-moving and obsolete inventory. Cost is computed using standard cost, which approximates actual cost on a first-in, first-out basis.

Revenue Recognition:

Revenues from sales of telecommunications equipment are recognized when persuasive evidence of an arrangement exists, delivery of the product has occurred as evidenced by customer acceptance, the fee is fixed or determinable and collectability is reasonably assured. If the fee due from the customer is not fixed or determinable due to extended payment terms, revenue is recognized as payments become due from the customer, assuming all other criteria for revenue recognition is met. Shipping and handling costs are recorded as revenues and costs of revenues. Where multiple elements exist in an arrangement, the arrangement fee is allocated to the different elements based upon verifiable objective evidence of the fair value of the elements. Revenue is then recognized as each element is earned, provided that the undelivered elements are not essential to the functionality of the delivered elements. Revenues from engineering service contracts and from sales of telecommunications equipment involving significant production, modification or customization of the product, or where services being provided are deemed to be essential to the functionality of the product, are recognized using the percentage of completion method if the project cost can be reasonably estimated. If the cost cannot be reasonably estimated, the completed contract method is applied. Any payments received prior to revenue recognition are recorded as deferred revenue.

Warranty Costs:

A warranty is provided under the terms of the Company's purchase contracts for a period generally ranging from twelve to twenty four months. The Company provides for these costs at the time of revenue recognition based on an assessment of past warranty experience.

Property, Plant and Equipment:

Property, plant and equipment are recorded at cost and are stated net of accumulated depreciation. Depreciation is provided for on a straight-line basis over the estimated useful lives of the related assets. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvements or the term of the lease. When assets are disposed of, the cost and related accumulated depreciation are removed from the accounts and the resulting gains or losses are included in results of operations. The Company generally depreciates its assets over the following periods:

	Years

Furniture, test or manufacturing equipment	5
Computers and software	2-3
Buildings	20
Automobiles	5
Leasehold improvements	lesser of 5 or remaining lease life

Goodwill and Intangible Assets:

Goodwill and intangible assets include the excess of costs of acquired companies over the fair value of tangible net assets and acquired in process research and development. Intangible assets are amortized on a straight-line basis generally over three to five years. With the adoption of SFAS No. 142 on January 1, 2002, goodwill is no longer amortized. See Note 10. Rather, goodwill is tested annually for impairment. There were no goodwill impairment charges in 2002, 2001 and 2000.

Impairment of Long-Lived Assets:

Long-lived assets and certain intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If undiscounted expected future cash flows are less than the carrying value of the assets, an impairment loss will be recognized based on the excess of the carrying amount over the fair value of the assets. Long-lived assets that are to be disposed of by sale are measured at the lower of book value or fair value less cost to sell.

Capitalized Software Development Costs:

Software development costs have been accounted for in accordance with SFAS No. 86, "Accounting for Costs of Computer Software to be Sold, Leased, or Otherwise Marketed." During 2002 and 2001, the Company capitalized costs of $3.4 million and $2.0 million, respectively, upon establishment of technological feasibility. Amortization of capitalized development costs begins when the products are available for general release to customers, and is provided on a straight-line basis over the remaining estimated economic life of the product, generally three years. Amortization of capitalized development costs was $1.1 million, $0.3 million and $0 in 2002, 2001 and 2000, respectively. Direct costs of software developed for internal use are expensed during the preliminary project stage and capitalized during the application development stage.

Research and Development Costs:

Research and development costs are expensed as incurred and consist primarily of salaries and related costs of employees engaged in research, design and development activities, the cost of parts for prototypes, equipment depreciation and third party development expenses.

Stock-Based Compensation:

The Company accounts for employee stock option grants in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and has adopted the disclosure-only alternative of SFAS No. 123, as amended by SFAS No. 148, "Accounting for Stock-Based Compensation" ("SFAS 123"). Under APB 25, compensation expense is based on the difference, if any, on the date of grant between the fair value of the common stock and the exercise price of the option.

The fair value of warrants, options or stock exchanged for services is expensed over the period benefited. The warrants and options are valued using the Black-Scholes option pricing model.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation (in thousands, except per share data):

	Year ended December 31,		
	2002	**2001**	**2000**
Net income, as reported	$ 107,862	$ 56,954	$ 27,013
Add: Stock-based employee compensation expense	2,209	3,706	8,238

	Year ended December 31,		
included in reported net income, net of related tax effects			
Deduct: Total stock based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(20,060)	(15,827)	(11,115)
Proforma net income	$ 90,010	$ 44,833	$ 24,136
Basic as reported	$ 0.98	$ 0.56	$ 0.34
Basic pro forma	$ 0.82	$ 0.44	$ 0.30
Diluted as reported	$ 0.94	$ 0.52	$ 0.27
Diluted pro forma	$ 0.81	$ 0.42	$ 0.24

The following assumptions were used to calculate the fair value of the options granted:

	Year ended December 31,		
	2002	2001	2000
Expected remaining term in years	3.00	3.00	3.00
Weighted average risk-free interest rate	3.43%	4.04%	5.86%
Expected dividend rate	0.00%	0.00%	0.00%
Volatility	67.50%	86.07%	100.00%

The weighted average fair value per share of options granted in 2002, 2001 and 2000 was $9.16, $11.30 and $9.03, respectively.

Comprehensive Income:

Comprehensive income includes all changes in equity (net assets) during a period from nonowner sources. Accumulated other comprehensive income or loss is shown in the consolidated statement of stockholders' equity.

Income Taxes:

Deferred income taxes are recognized for the differences between the tax bases of assets and liabilities and their financial statement amounts based on enacted tax rates. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

The Company does not provide for U.S. Federal taxes on undistributed earnings of its foreign subsidiaries or affiliates as they are considered to be reinvested for an indefinite period.

Segment Reporting:

The Company operates in a single segment, providing telecommunications equipment through an integrated suite of network access systems and subscriber terminal products.

Disclosures About Fair Value of Financial Instruments:

Financial instruments consist of cash and cash equivalents, short-term investments, accounts receivable and payable, and accrued liabilities. The carrying amounts of cash and cash equivalents, short-term investments, accounts receivable and payable and accrued liabilities approximate their fair values because of the short-term nature of those instruments.

Foreign Currency Translation:

Operations of the Company's subsidiaries are conducted primarily in China and the financial statements of those subsidiaries are translated from China's Renminbi, the functional currency, into U.S. Dollars in accordance with SFAS No. 52, "Foreign Currency Translation." Accordingly, all foreign currency assets and liabilities are translated at the period-end exchange rate and all revenues and expenses are translated at the average exchange rate for the period. The effects of translating the financial statements of foreign subsidiaries into U.S. Dollars are reported as a cumulative translation adjustment, a separate component of comprehensive income in stockholders' equity. Foreign currency transaction gains and losses are reported in earnings and were $5.4 million of losses in 2002. They were not material for 2001 and 2000.

Earnings Per Share:

Basic earnings per share ("EPS") is computed by dividing net income available to common stockholders by the weighted average number of shares of the Company's common stock outstanding during the period. Diluted earnings per share is determined in the same manner as basic earnings per share except that the number of shares is increased by potentially dilutive common shares outstanding during the period. Potentially dilutive common shares consist of employee stock options, warrants and restricted stock.

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The following is a summary of the calculation of basic and diluted EPS (in thousands, expect per share data):

	Year Ended December 31,		
	2002	**2001**	**2000**
Net income before cumulative effect of change in accounting principle:	$ 107,862	$ 56,954	$ 27,993
Shares used to compute basic EPS	109,566	101,433	79,696
Dilutive common equivalent shares:			
Stock options	4,510	7,151	10,157
Warrants	28	28	92
Other	303		11,922
Shares used to compute diluted EPS	114,407	108,612	101,867
Basic earnings per share	$ 0.98	$ 0.56	$ 0.35
Diluted earnings per share	$ 0.94	$ 0.52	$ 0.28

For the years ended December 31, 2002, 2001 and 2000, options to purchase approximately 2,801,200, 1,783,248 and 226,200 shares of common stock, respectively, with exercise prices greater than the fair market value of the Company's stock, were not included in the calculations because the effect would have been antidilutive.

Recent Accounting Pronouncements:

In July 2002, the Financial Accounting Standards Board (the "FASB") issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities", which addresses the measurement, timing of recognition and reporting of costs associated with exit or disposal activities and restructuring activities. SFAS No. 146 requires that a liability for costs associated with exit or restructuring activities be recognized only when the liability is incurred as opposed to at the time that a company formally approves and commits to an exit plan as set forth in EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity." SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not expect the adoption to have an impact on the consolidated financial statements.

In November 2002, the FASB issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosure about the guarantees that an entity has issued, including a reconciliation of changes in the entity's product warranty liabilities. The initial recognition and initial measurement provisions of FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. See Note 13. The Company believes that the adoption of this standard will not have a material impact on the consolidated financial statements.

In November 2002, the Emerging Issues Task Force reached a consensus on Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables." This issue addresses how revenue arrangements with multiple deliverables should be divided into separate units of accounting and how the arrangement consideration should be allocated to the identified separate accounting units. EITF No. 00-21 is

effective for fiscal periods beginning after June 15, 2003. The Company has not yet determined the impact of adopting EITF No. 00-21 on its consolidated financial statements.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation Costs Transition and Disclosure". This statement amends SFAS No. 123, "Accounting for Stock Based Compensation", and provides alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based compensation. It also requires additional disclosures about the effects on reported net income of an entity's accounting policy with respect to stock-based employee compensation. We account for stock-based compensation in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees" and have adopted the disclosure-only alternative of SFAS No. 123. The Company adopted the disclosure provisions of SFAS No. 148 in December 2002. See Note 15.

NOTE 3 ACCOUNTING CHANGES

Effective January 1, 2000, the Company adopted Staff Accounting Bulletin 101 ("SAB 101"), "Revenue Recognition in Financial Statements", issued by the Securities and Exchange Commission in December 1999. As a result of adopting SAB 101, the Company changed the way it recognizes revenue on certain contracts that had previously led to revenue being recognized as contract stages were completed and accepted. In light of the guidance issued in SAB 101, the Company changed its method of revenue recognition to the point of contractual final acceptance. In addition, certain contracts include service requirements for which revenue was previously recognized, and costs accrued, on contractual acceptance. In consideration of SAB 101, revenues associated with these service requirements are being deferred until the service obligations are completed. Due to these changes, the Company recorded a cumulative adjustment in the first quarter 2000 of $1.0 million (net of income taxes of $0) or $0.01 per share, basic and diluted.

NOTE 4 COMPLETION OF INITIAL PUBLIC OFFERING, FOLLOW-ON PUBLIC OFFERING AND RESALE PUBLIC OFFERING

On March 3, 2000, the Company completed its initial public offering ("IPO") and sold 11,500,000 shares of common stock at $18.00 per share for aggregate net proceeds of approximately $189.4 million. On August 3, 2001, the Company completed a follow-on public offering and sold an aggregate of 7,400,000 shares of common stock at $20.00 per share. Selling stockholders sold an additional 2,950,000 shares of common stock in the offering. The aggregate net proceeds to the Company were $139.9 million. On February 28, 2002, the Company sold 1,500,000 shares of common stock in connection with the resale public offering of 10,000,000 shares of our common stock by SOFTBANK America Inc., one of the Company's stockholders. The aggregate net proceeds to the Company were $28.9 million.

NOTE 5 SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

	Year ended December 31,		
(in thousands)	**2002**	**2001**	**2000**
Cash paid during the period for:			
Interest	$ 1,492	$ 3,798	$ 3,289
Income taxes	$ 18,442	$ 10,832	$ 8,038

Noncash investing and financing activities were as follows:

Year ended December 31,

(in thousands)	Year ended December 31,		
	2002	2001	2000
	$	$ 20,734	$
Issuance of shares upon the Stable Gain acquisition	$	$ 10,700	$
Issuance of shares and vested stock options upon the ACD acquisition			

NOTE 6 ACQUISITIONS AND DIVESTITURES OF COMPANIES

During 2002, the Company completed a number of purchase acquisitions which are summarized as follows (in thousands):

	Consideration	In-process R&D expense	Goodwill	Purchased Technology
Issanni Communications, Inc.	$ 4,120	$ 670	$ 202	$ 3,230
Guangdong UTStarcom, Ltd.	3,664		3,292	
UTStarcom (Hangzhou) Communication Co. Ltd.	14,546		6,398	
	$ 22,330	$ 670	$ 9,892	$ 3,230

On April 19, 2002, the Company completed the purchase of Issanni Communications, Inc. ("Issanni"). Issanni develops RAS (remote access server) and local access technology, which the Company incorporates into one of its products. The Company's investment in Issanni was $2.0 million prior to the acquisition. The purchase consideration for all the outstanding shares of Issanni, other than those already held by the Company prior to the acquisition, was $2.1 million, $0.5 million of which is held in escrow for any undisclosed liabilities or contingencies incurred by Issanni prior to closing. In addition, $2.0 million will be payable in the form of an earnout to all Issanni shareholders of record at closing, subject to the completion of certain performance milestones during 2002, 2003 and 2004. This earnout will be recorded as additional purchase price when earned. No amounts were earned in 2002. Furthermore, the Company adopted an incentive program providing for the issuance of 39,876 shares of common stock valued at $1.0 million to Issanni employees who will continue to perform services for the Company. These shares vest at the earlier of five years or upon the achievement of certain performance milestones. The Company records this amount as compensation expense ratably over the vesting period and will accelerate the amortization if the milestones are met. The amount of the purchase price allocated to in-process research and development of $0.7 million was charged to the Company's results of operations, as no alternative future uses existed at the acquisition date. Goodwill of $0.2 million was recorded in connection with the acquisition and is expected to be deductible for tax purposes. The results of operations of Issanni are included in the Company's consolidated results of operations beginning on April 19, 2002.

In September 1996, the Company purchased a 49% interest in Guangdong UTStarcom, Ltd. ("GUTS"), one of the Company's two primary manufacturing facilities. In February 1998, the Company acquired an additional 2% interest in GUTS, increasing its ownership interest to 51%. This investment was accounted for using the equity method prior to the Company's acquisition of the remaining 49% ownership interest in GUTS in May 2002, as the Company did not have voting control over significant matters. On December 18, 2001, the Company entered into an agreement to acquire the remaining 49% ownership interest in GUTS for a total consideration of $3.6 million in cash. The cash consideration was paid in the first quarter of 2002 and final government approvals were received in May 2002. Goodwill of $3.3 million was recorded in connection with the acquisition and is not expected

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to be deductible for tax purposes. GUTS is now a wholly-owned subsidiary of the Company and its results of operations are included in the Company's consolidated financial statements beginning June 1, 2002.

In July 1997, the Company, as part of its business operations in China, acquired an 88% interest in UTStarcom (Hangzhou) Communication Co., Ltd, which has since changed its name to UTStarcom Telecom Co., Ltd. ("HUTS"), one of the Company's primary manufacturing facilities. On January 21, 2002, the Company entered into an agreement to acquire the remaining 12% ownership interest in the joint venture company for a total consideration of $14.5 million in cash. Cash consideration of $7.3 million was paid in January 2002, and the remaining consideration was paid in the second quarter of fiscal 2002. Final government approvals were received in May 2002. Goodwill of $6.4 million, was recorded in connection with the acquisition and is not expected to be deductible for tax purposes.

Had the acquisitions of Issanni and the remaining interests in HUTS and GUTS, which were recorded in the second quarter of fiscal 2002, occurred on January 1, 2002, proforma net income for 2002 would have been $107.2 million, or $0.98 per share basic, and $0.94 per share fully diluted. Had the acquisitions occurred on January 1, 2001, proforma net income for 2001 would have been $52.9 million or $0.52 per share basic, and $0.49 per share fully diluted. Proforma revenues would have been $983.9 million for 2002 and $635.9 million for 2001. Proforma adjustments include the amortization of fixed asset step-ups and intangible assets as if the transactions had occurred on January 1, 2002.

On October 16, 2002, the Company acquired the assets and intellectual property of Shanghai Yi Yun Telecom Technology Co. Ltd., a provider of synchronous digital hierarchy ("SDH") equipment. Consideration was $0.2 million of cash and 342,854 shares of restricted stock valued at $6.0 million. The acquisition has not been recorded as of December 31, 2002 as the consideration is held in escrow for a year and the outcome of the contingencies that would allow the escrowed shares to ultimately be issued free and clear is not determinable beyond a reasonable doubt. In addition, the Company issued 514,290 shares of restricted stock valued at $9.0 million to the acquiree's employees. Such restricted stock vests over five years, with accelerated vesting upon the achievement of specified milestones. This stock has been treated as deferred compensation.

On July 24, 2000, the Company entered into an agreement with Stable Gain International Ltd. ("Stable Gain") to purchase intellectual property and certain related fixed assets, and to transfer development employees to the Company. Under the amended purchase agreement, the Company paid Stable Gain consideration of $10.7 million in the form of common stock of the Company and $0.3 million in cash. The transfer of the common stock was completed during the second quarter of 2001. The total purchase consideration of $11.0 million was allocated to property and equipment, intangible assets and goodwill under the purchase method of accounting. Goodwill totaling $7.4 million was recorded on acquisition and had an estimated life of three years.

In November 2001, the Company completed the purchase of Advanced Communication Devices Corporation ("ACD") for $21.3 million, comprised of approximately one million shares of the Company's common stock valued at $19.9 million, $0.9 million of vested common stock options valued using the Black-Scholes pricing model, and $0.5 million of acquisition-related expenses. ACD was a System on Chip ("SoC") semiconductor company focusing on LAN and IP switching technology whose then current markets included Taiwan, China and Korea. In addition, the Company adopted an incentive plan providing for the issuance of shares of common stock valued at $5 million to ACD employees who will continue to perform services for the Company. These shares vest at the earlier of

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five years or the achievement of certain performance milestones. The Company recorded the amount as deferred compensation. $0.8 million and $1.3 million of deferred compensation was charged to operations in 2002 and 2001, respectively. The number of shares issued for the acquisition was calculated using the average closing price of the common stock for the five trading days ended August 13, 2001 (the date the merger agreement was signed). The acquisition has been accounted for as a purchase and the results of operations have been included in the Company's consolidated financial statements since the acquisition. ACD results of operations prior to the acquisition were not material to the Company's results of operations on a pro forma basis. The acquisition cost has been allocated to the assets acquired based on their respective fair values. Intangible assets are comprised of intellectual property related to ACD Ethernet technology, which is being amortized on a straight-line basis over its estimated useful life of three years. In accordance with SFAS No. 141, the Company is not amortizing goodwill for this acquisition.

The Company recorded a $4.7 million charge for purchased in-process research and development at the date of acquisition of ACD. Technological feasibility was not established on the development of ACD's Ethernet Digital Subscriber Line (EDSL) chip design. The design was approximately 15% completed at the time of acquisition. The estimated completion date for the project was March 2003. In October 2002, the Board of Directors authorized the ACD Incentive Program Review Committee to review the remaining ACD Incentive Program milestones in light of certain changes in the strategic plans of ACD. Final approval of the revised milestones is pending.

The following table represents the allocation of the purchase price for ACD:

(in thousands)		
Fair value of tangible net assets acquired	$	58
Fair value of identified intangible assets		4,340
In process research and development		4,720
Excess of costs of acquiring ACD over fair value of identified net assets acquired (goodwill)		12,215
	$	21,333

(in thousands)

NOTE 7 INVENTORIES

As of December 31, 2002 and 2001, inventories consist of the following:

(In thousands)	December 31, 2002	December 31, 2001
Raw materials	$ 84,715	$ 54,700
Work-in-process	26,915	33,037
Finished goods	313,036	141,313
	$ 424,666	$ 229,050

NOTE 8 PROPERTY, PLANT AND EQUIPMENT

As of December 31, 2002 and 2001, property, plant and equipment consists of the following:

(In thousands)	December 31, 2002	December 31, 2001
Buildings	$ 38,901	$ 68
Land	6,702	7,319
Leasehold improvements	7,052	4,077
Automobiles	4,846	2,952
Software	16,512	11,752
Equipment and furniture	62,479	37,858
	136,492	64,026
Less accumulated depreciation	(37,981)	(20,084)
	$ 98,511	$ 43,942

Depreciation expense was $20.0 million, $11.0 million and $4.6 million for the years ended December 31, 2002, 2001 and 2000, respectively.

NOTE 9 LONG-TERM INVESTMENTS

The Company's investments are as follows:

(in thousands)	December 31, 2002	December 31, 2001
Investment in Softbank China	$ 5,526	$ 8,314
Investment in Cellon International	8,000	2,000
Investment in China Telecom	9,106	
Investment in Joint Venture with Matsushita	4,683	

	December 31,	
Investment in others	8,045	7,504
Total	$ 35,360	$ 17,818

The Company has invested $10.0 million in Softbank China, an investment fund established by SOFTBANK CORP. focused on investments in Internet companies in China. This investment permits the Company to participate in the anticipated growth of Internet-related businesses in China. SOFTBANK CORP. and its related companies are significant stockholders of the Company. The Company's investment constitutes 10% of the funding for Softbank China, with SOFTBANK CORP. contributing the remaining 90%. The fund has a separate management team, and none of the Company's employees are employed by the fund. Many of the fund's investments are and will be in privately held companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky as the market for the technologies or products the companies have under development are typically in the early stages and may never materialize. The Company accounts for this investment under the equity method and recorded losses of $2.8 million, $1.7 million and $0.0 million in 2002, 2001 and 2000, respectively, on this investment.

During the first quarter of fiscal 2002, the Company invested $2.0 million in Restructuring Fund No. 1, a venture capital investment limited partnership established by SOFTBANK INVESTMENT CORP., an affiliate of SOFTBANK CORP. SOFTBANK America Inc., an entity affiliated with

SOFTBANK CORP., is a significant stockholder of the Company. The fund focuses on leveraged buyout investments in companies in Asia undergoing restructuring or bankruptcy procedures. The total fund offering is expected to be between approximately $150.0 million and $226.0 million, with each investor contributing a minimum of $0.8 million. The fund has a separate management team, and none of the Company's employees are employed by the fund. The Company accounts for this investment under the equity method of accounting. The balance in this investment is $2.0 million at December 31, 2002.

The Company has also invested directly in a number of private technology-based companies in the early stages of development. These investments are accounted for on a cost basis. The Company continually evaluates the carrying value of these investments for possible impairment based on the achievement of business objectives and milestones, the financial condition and prospects of these companies and other relevant factors. During 2002 and 2001, impairment charges in respect of these private technology investments were $3.0 million and $1.7 million, respectively. These investment impairment charges are included in Other Income (Expense), Net in the consolidated statements of operations.

In June 2002, the Company invested $1.0 million in Global Asia Partners L.P., with a commitment to invest up to a maximum of $5.0 million. The remaining amount is due at such times and in such amounts as shall be specified in one or more future capital calls to be issued by the general partner. The fund size is anticipated to be $100 million and was formed to make private equity investments in private or pre-IPO technology and telecommunications companies. The fund's geographic focus is on technology investments in Asia, in particular India and China. The Company accounts for this investment under the equity method of accounting.

During 2002, the Company purchased approximately 5.8 million shares of common stock of InterWave Communications, Inc., a technology company listed on NASDAQ, for approximately $3.0 million. In addition, the Company received warrants to purchase 2.0 million shares of InterWave's common stock at $0.21 cents per share, which were valued at $0.3 million using the Black-Scholes option pricing model. The Company recorded a charge of $1.4 million in the fourth quarter of 2002 to reflect the other than temporary decline in the carrying value of these marketable securities.

In November 2002, the Company purchased approximately 0.5 million shares of common stock of China Telecom in its initial public offering for approximately $10.0 million. China Telecom is the leading provider of wireline telephone, data and Internet and leased line services in four of the most economically developed regions of China, and its affiliates are customers of the Company. China Telecom is listed on the New York Stock Exchange. The investment is considered available-for-sale, and the Company recorded the temporary decline of $0.9 million in the carrying value of these securities as of December 31, 2002 in comprehensive income in equity.

NOTE 10 GOODWILL AND INTANGIBLE ASSETS

As of December 31, 2002 and 2001, goodwill and other acquired intangible assets consisted of the following:

	December 31,	
(In thousands)	**2002**	**2001**
Goodwill	$ 57,629	$ 47,636
Less accumulated amortization	(12,823)	(12,823)
	$ 44,806	$ 34,813
Purchased technology	$ 7,570	$ 4,340
Less accumulated amortization	(2,556)	(161)
	$ 5,014	$ 4,179

Amortization expense was $2.4 million, $7.5 million and $4.9 million for the years ended December 31, 2002, 2001 and 2000, respectively. The estimated aggregate amortization expense for intangibles for each of the five years beginning 2003 through 2007 is $2.5 million, $2.4 million, $0.1 million, $0.0 million and $0.0 million, respectively.

Goodwill increased by $10.0 million in 2002. Goodwill totaling $6.3 million was recorded on the acquisition of the remaining 12% ownership interest in HUTS, goodwill of $3.3 million was recorded on the acquisition of the remaining 49% ownership in GUTS, and goodwill of $0.4 million was recorded on the acquisition of Issanni. Intangible assets increased by $3.2 million during 2002. This increase was due to purchased technology that was recorded on the acquisition of Issanni. The estimated useful life of this purchased technology is three years. See Note 6.

In July 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually. SFAS No. 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets."

SFAS No. 142 was adopted by the Company on January 1, 2002. SFAS No. 142 had the effect of eliminating amortization of goodwill commencing January 1, 2002; however, impairment reviews may result in future periodic write-downs. The Company completed the required transitional assessment of goodwill during the first quarter of fiscal 2002. Based on this assessment, there was no transition goodwill impairment charge. The Company performed its annual impairment review in the fourth quarter of 2002. No impairment in goodwill was noted.

The reconciliation of net income to adjusted net income as if there had been no goodwill amortization for the twelve months ended December 31, 2001 and 2000 is as follows (in thousands):

	Year Ended December 31,	
	2001	**2000**
Reported net income	$ 56,954	$ 27,013
Add back: goodwill amortization	7,365	4,894
Adjusted net income	$ 64,319	$ 31,907
Basic earnings per share:		
Reported net income	$ 0.56	$ 0.34

	Year Ended December 31,	
Goodwill amortization	0.07	0.06
Adjusted net income	$ 0.63	$ 0.40
Diluted earnings per share:		
Reported net income	$ 0.52	$ 0.27
Goodwill amortization	0.07	0.05
Adjusted net income	$ 0.59	$ 0.32
Average number of shares outstanding:		
Basic	101,433	79,696
Diluted	108,612	101,867

NOTE 11 DEBT

The following represents the outstanding borrowings at December 31, 2002 and 2001 (in thousands):

	December 31,	
Note	**2002**	**2001**
Bank of China	$	$ 34,338
China Merchants Bank		6,024
Commercial Bank of Hangzhou		12,048
CITIC Industrial Bank		6,024
China Everbright Bank		12,048
Total debt	$	$ 70,482
Long-term debt		12,048
Short-term debt	$	$ 58,434

All outstanding debt was repaid in September 2002, and there were no gains or losses on the early retirement of this debt. The Company has available borrowing facilities of $314.3 million as of December 31, 2002. $260.1 million of these facilities expire in 2003 and $54.2 million of these facilities expire between 2008 and 2010.

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NOTE 12 OTHER CURRENT LIABILITIES

Other current liabilities at December 31, 2002 and 2001 consist of the following:

	December 31,	
(In thousands)	**2002**	**2001**
Accrued contract costs	$ 45,756	$ 30,217

	December 31,	
Accrued payroll and compensation	24,633	18,055
Accrued other taxes	2,869	15,983
Warranty costs	13,297	6,271
Accrued construction costs	9,889	
Other	8,483	5,803
	$ 104,927	$ 76,329

NOTE 13 WARRANTY OBLIGATIONS AND OTHER GUARANTEES

Warranty obligations are as follows (in thousands):

Balance at January 1, 2001	$ 3,133
Accruals for warranties issued during the period	6,792
Settlements made during the period	(3,654)
Balance at December 31, 2001	6,271
Accruals for warranties issued during the period	15,156
Settlements made during the period	(8,130)
Balance at December 31, 2002	$ 13,297

Certain of the Company's sales contracts include provisions under which customers would be indemnified by the Company in the event of, among other things, a third-party claim against the customer for intellectual property rights infringement related to the Company's products. There are no limitations on the maximum potential future payments under these guarantees. The Company has accrued no amounts in relation to these provisions as no such claims have been made and the Company believes it has valid, enforceable rights to the intellectual property embedded in its products.

NOTE 14 PROVISION FOR INCOME TAXES

United States and foreign income (loss) before income taxes, minority interest and cumulative effect of a change in accounting principle were as follows (in thousands):

	Year ended December 31,		
	2002	2001	2000
United States	$ 13,245	$ (12,237)	$ (9,973)
Foreign	123,027	90,336	54,294
	$ 136,272	$ 78,099	$ 44,321

Undistributed foreign earnings at December 31, 2002 amounted to $290 million.

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The components of the provision (benefit) for income taxes are as follows (in thousands):

Year ended December 31,		
2002	2001	2000

	Year ended December 31,		
Current:			
Federal	$ 12,222	$ 7,246	$ 13,369
State/Other	1,515	621	782
Foreign	28,222	21,586	6,046
Deferred:			
Federal	(6,665)	(8,002)	(4,433)
State	(315)	(172)	2
Foreign	(7,725)	(1,456)	(1,745)
	$ 27,254	$ 19,823	$ 14,021

Deferred income taxes arise from temporary differences between the tax bases of assets and liabilities and their reported amounts in the consolidated financial statements. A summary of the components of net deferred tax assets is as follows (in thousands):

	U.S.	China	Hong Kong	Total
December 31, 2002:				
Current deferred tax assets:				
Allowances and reserves	$ 8,586	$ 8,184	$	$ 16,770
Gross profit in intercompany inventory	5,052			5,052
Total current deferred tax assets	$ 13,638	$ 8,184	$	$ 21,822
Non current deferred tax assets:				
Net operating loss carryforward	$ 1,988	$	$ 2,974	$ 4,962
Future period compensation deductions	1,575			1,575
Tax credit carryforwards	6,413			6,413
Fixed assets	356	461		817
Other	3,967			3,967
Total non current deferred tax assets	14,299	461	2,974	17,734
Valuation allowances	(4,964)			(4,964)
Net non-current deferred tax assets	$ 9,335	$ 461	$ 2,974	$ 12,770

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	U.S.	China	Hong Kong	Total
December 31, 2001:				
Current deferred tax assets:				
Allowances and reserves	$ 5,692	$ 3,894	$	$ 9,586
Gross profit in intercompany inventory	2,031			2,031
Total current deferred tax assets	$ 7,723	$ 3,894	$	$ 11,617

Non current deferred tax assets:

	U.S.	China	Hong Kong	Total
Net operating loss carryforward	$ 5,855	$	$	$ 5,855
Future period compensation deductions	1,581			1,581
Tax credit carryforwards	4,938			4,938
Fixed assets	(842)			(842)
Other	1,525			1,525
Total non current deferred tax assets	13,057			13,057
Valuation allowances	(4,787)			(4,787)
Net non-current deferred tax assets	$ 8,270	$	$	$ 8,270

As of December 31, 2002, the Company has research and development credit carryforwards of approximately $5.1 million for federal and state tax purposes expiring in varying amounts between 2017 and 2022. As of December 31, 2002, the Company has federal and state net operating loss carryforwards of $3.1 million and $7.8 million, respectively. The federal net operating loss carryforwards will expire in 2019. The state net operating loss carryforwards will expire in varying amounts between 2004 and 2006 and cannot be utilized in 2002 and 2003. Management believes that the Company's ability to use their deferred tax assets is limited based on the expectation that they will not be able to fully utilize the net operating losses from the purchase of Wacos in December 1999 and the research and development credits generated by Company's research and development center in New Jersey. The Company has created a valuation allowance against these deferred tax assets. The valuation allowance increased by $0.2 million and $0.6 million in 2002 and 2001, respectively. As of December 31, 2002, the Company had net operating loss carryforwards of approximately $18.0 million in Hong Kong, which do not expire and can be carried forward indefinitely.

UTSC and HUTS were granted tax holidays, which started to phase out in 1999. The net impact of these tax holidays was to increase net income by approximately $10.0 million, $6.7 million, and $4.5 million for the years ended December 31, 2002, 2001 and 2000, respectively.

The difference between the Company's effective income tax rate and the federal statutory rate is reconciled below:

	Year ended December 31,		
	2002	2001	2000
Federal statutory rate	34%	34%	34%
State taxes, net of federal income tax benefit			(1)
Permanent differences	5	5	7
Amortization of deferred compensation	1	2	8
Effect of difference in foreign taxes rates	(16)	(14)	(18)
Tax credits and other	(4)	(2)	2
Effective rate	20%	25%	32%

In 2001, audits of the Company's federal income tax returns for the years ended December 31, 1999, 1998 and 1997 were completed. No audits of the Company's income tax returns were underway as of December 31, 2002.

NOTE 15 COMMON STOCK AND STOCK INCENTIVE PLANS

Stock Option Plans

The 1995 Stock Plan. On July 31, 1995, the Board of Directors adopted, and in October 1995, the Company's stockholders approved, the Company's 1995 Stock Plan. Under the 1995 plan, officers, employees and consultants were eligible to acquire shares of common stock pursuant to options or stock purchase rights. At the time of adoption, 3,705,232 shares of common stock were reserved for issuance under the 1995 plan. In 1995 and 1996, the Company's Board and stockholders added an additional 5,400,000 shares to the 1995 plan, raising the total number of authorized shares reserved under the 1995 plan to 9,105,232. As of December 31, 2002, there were 6,711,744 shares authorized for issuance under the 1995 plan and options to purchase 523,885 shares of common stock were outstanding under the 1995 plan. On January 31, 1997, the Board of Directors elected not to grant any further options under the 1995 plan. Upon the adoption of the 1997 plan, all remaining unissued shares under the 1995 plan not already subject to options or other awards ceased to be reserved for issuance under the 1995 plan.

The 1997 Stock Plan. On January 31, 1997, the Board of Directors adopted, and the Company's stockholders approved, the Company's 1997 Stock Plan. Under the 1997 plan, officers, employees and consultants are eligible to receive options to purchase shares of common stock and stock purchase rights. In December 1999, the Board of Directors amended the 1997 plan, which the Company's stockholders approved in February 2000. As of December 31, 2002, the Company is authorized to issue up to 21,092,663 shares subject to options. During the term of the 1997 plan, the number of shares issuable under the plan will be increased annually on the first day of each fiscal year beginning in 2001 by an amount equal to the lesser of 6,000,000 shares or 4% of the outstanding shares of common stock on that date, or a lesser amount determined by the Board. The plan terminates in January 2007, but may be terminated earlier by the Board of Directors. As of December 31, 2002, there were options to purchase 13,984,861 shares of common stock outstanding under the 1997 plan. The Compensation Committee administers the 1997 plan.

Options granted under the 1997 plan may be incentive stock options, or ISOs, which are intended to qualify for favorable federal income tax treatment under the provisions of Section 422 of the Internal Revenue Code of 1986, as amended, or non-qualified stock options, or NSOs, which do not so qualify. The Compensation Committee selects the eligible persons to whom options will be granted and determines the grant date, amounts, exercise prices, vesting periods and other relevant terms of the options, including whether the options will be ISOs or NSOs. The exercise price of ISOs granted under the 1997 plan may not be less than 100% of the fair market value of common stock on the grant date, while the exercise price of NSOs can be determined by the Compensation Committee in its discretion. Options are generally not transferable during the life of the optionee.

Options vest and become exercisable as determined by the Compensation Committee, generally over four years. Options may generally be exercised at any time after they vest and before their expiration date as determined by the Compensation Committee. However, no option may be exercised more than ten years after the grant date. Options will generally terminate (i) 12 months after the death or permanent disability of an optionee and (ii) 90 days after termination of employment for any other reason. The aggregate fair market value of the shares of common stock represented by ISOs that become exercisable in any calendar year may not exceed $100,000. Options in excess of this limit are treated as NSOs.

In the event the Company is merged with or into another corporation, or all or substantially all of the Company's assets are sold, each outstanding option will be assumed or an equivalent option or right will be substituted by the successor corporation or its parent or subsidiary. If the successor corporation refuses to assume or substitute for the option or right, the options or rights will automatically vest and become exercisable in full for a period of at least fifteen days, after which time the option will terminate.

Under the 1997 plan, the Company may grant stock purchase rights to eligible participants. Any shares purchased pursuant to stock purchase rights will be subject to a restricted stock purchase agreement. Unless the Compensation Committee determines otherwise, this agreement will grant the Company a right to repurchase the stock upon the voluntary or involuntary termination of the employee for any reason, including death or disability. The purchase price for repurchased shares will be the original price paid and may be paid by cancellation of any indebtedness owed to the Company. The shares of stock subject to the right of repurchase lapse over time.

2001 Director Option Plan. On March 2, 2001, the Board of Directors adopted, and in May 2001, the Company's stockholders approved, the Company's 2001 Director Option Plan. Under the 2001 Director Option Plan, those directors who are not employees of the Company ("Outside Directors") are eligible to receive options to purchase shares of common stocks. Directors Horner, Atkins, Son and Toy are Outside Directors. All grants of options to Outside Directors are automatic and nondiscretionary. In July 2001, the Board of Directors amended the 2001 Director Option Plan. As of December 31, 2002, the Company is authorized to issue up to 1,200,000 shares subject to options. The Plan terminates in May 2011, but may be terminated earlier by the Board of Directors. As of December 31, 2002, there were options to purchase 395,000 shares of common stock outstanding under the 2001 Director Option Plan. The Compensation Committee administers the 2001 Director Plan.

Upon approval of the 2001 Director Plan, each Outside Director is automatically granted an option to purchase eighty thousand shares of common stock (the "First Option") on the date on which such person first becomes an Outside Director (the "Anniversary Date"). A director who is an employee of the Company and ceases employment with the Company to become an Outside Director

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shall receive an option to purchase twenty thousand shares of common stock (a "Subsequent Option") at the Company's first annual meeting of stockholders following such conversion to an Outside Director and at each subsequent annual stockholder meeting thereafter, provided he or she is serving as an Outside Director on each such date. As such time as each Outside Director's First Option is fully vested, each Outside Director shall be automatically granted a Subsequent Option on the Anniversary Date of each year provided he or she is then an Outside Director.

Under the terms of the 2001 Director Plan, the exercise price of each option granted is the market value of the common stock on the date of grant. Such options have terms of ten years, but terminate earlier if the individual ceases to serve as a director. The First Option grants vest as follows: 25% of shares subject to the First Option vest on each anniversary of its date of grant. The Subsequent Option grants vest as follows: 100% of the shares subject to the Subsequent Option vest on the first anniversary of its date of grant.

In August 2002, the Company granted each Outside Director options to purchase 25,000 shares of common stock. These options vest over twelve months.

ACD 1996 and 1997 Stock Plan. On August 27, 2001, the Board of Directors approved the assumption of the outstanding vested stock options issued under the ACD 1996 and 1997 Stock Plans upon the acquisition of ACD. A total of 868,701 fully vested shares issued under the ACD 1996 and 1997 Stock Plans were converted to 46,105 UTStarcom stock options at the date of merger on November 19, 2001.

A summary of activity under the Plans follows:

	Shares available for grant	Number of shares		Weighted average exercise price
Options Outstanding, December 31, 1999	172,243	14,405,714	$	3.25
Options Authorized in 2000	4,404,823		$	
Options Granted	(4,848,697)	4,848,697	$	15.74
Options Exercised		(3,651,687)	$	1.25
Options Forfeited or Expired	426,666	(428,000)	$	12.52
Options Outstanding, December 31, 2000	155,035	15,174,724	$	7.54
Options Authorized in 2001	5,062,760		$	
Options Granted	(3,326,957)	3,326,957	$	19.77
Options Exercised		(5,363,601)	$	3.48
Options Forfeited or Expired	559,663	(559,663)	$	13.79
Options Outstanding, December 31, 2001	2,450,501	12,578,417	$	12.22
Options Authorized in 2002	4,372,167		$	
Options Granted	(4,977,723)	4,977,723	$	19.46
Options Exercised		(1,717,899)	$	5.38
Options Forfeited or Expired	915,326	(915,326)	$	18.40
Options Outstanding, December 31, 2002	2,760,271	14,922,915	$	15.05

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The following table summarizes information with respect to stock options outstanding and exercisable as of December 31, 2002:

	Options Outstanding			Options Exercisable	
Range of exercise Price	Outstanding at December 31, 2002	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Exercisable at December 31, 2002	Weighted Average Exercise Price

	Options Outstanding				Options Exercisable		
	(in thousands)			(in years)	(in thousands)		
$ 0.06 - $ 0.06	105,476	$	0.06	4.9	105,476	$	0.06
$ 0.25 - $ 0.25	89,770	$	0.25	5.8	83,963	$	0.25
$ 0.85 - $ 0.85	523,885	$	0.85	2.8	523,885	$	0.85
$ 1.71 - $ 2.50	271,986	$	2.31	4.8	271,238	$	2.31
$ 3.39 - $ 4.71	1,533,359	$	4.27	6.4	1,249,068	$	4.29
$ 5.65 - $ 5.65	5,785	$	5.65	5.4	5,785	$	5.65
$ 9.38 - $13.61	2,909,251	$	11.44	7.3	1,665,180	$	11.22
$14.23 - $21.31	7,361,193	$	17.96	8.8	1,535,579	$	16.94
$21.85 - $32.65	2,112,210	$	24.15	8.5	609,784	$	24.42
$36.50 - $36.50	10,000	$	36.50	7.4	6,459	$	36.50
$ 0.06 - $36.50	14,922,915	$	15.05	7.9	6,056,417	$	10.95

2000 Employee Stock Purchase Plan. In February 2000, the Company's stockholders approved the 2000 Employee Stock Purchase Plan. The purchase plan is intended to qualify as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code.

The Company has reserved 2,000,000 shares of common stock for sale under the stock purchase plan. The number of shares reserved for sale under the plan will be increased annually on the first day of each fiscal year beginning in 2001 by an amount equal to the lesser of 4,000,000 shares or 2% of the outstanding shares of the Company's common stock on that date, or a lesser amount determined by the Board of Directors. The stock purchase plan will be administered by the Board or a committee appointed by the Board.

The stock purchase plan is implemented by offering periods, the duration of which may not exceed 24 months. Offering periods may contain interim purchase periods. Shares purchased under the stock purchase plan will be held in separate accounts for each participant. The first offering period began in March 2000 and ended on the last trading day before April 30, 2002. Subsequent consecutive overlapping offering periods begin on May 1 and November 1 annually. These offering periods end twenty-four months thereafter.

Employees will be eligible to participate in the stock purchase plan if they are employed by the Company for more than 20 hours per week and more than five months in a calendar year. The stock purchase plan permits eligible employees to purchase the Company's common stock through payroll deductions, which may not exceed 15% of the employee's total compensation. Stock may be purchased under the plan at a price equal to 85% of the fair market value of the Company's stock on either the date of purchase or the first day of the offering period, whichever is lower. However, the Board of Directors may in its discretion provide that the price at which shares of common stock are purchased under the plan shall be 85% of the fair market value of the Company's shares on the date of purchase. Participants may not purchase shares of common stock having a value greater than $25,000 during any calendar year.

Participants may increase or decrease their payroll deductions at any time during an offering period, subject to limits imposed by the Board of Directors. If a participant withdraws from the stock purchase plan, any contributions that have not been used to purchase shares shall be refunded. A participant who has withdrawn may not participate in the stock purchase plan again until the next offering period. In the event of retirement or cessation of employment for any reason, any contributions that have not yet been used to purchase shares will be refunded to the participant, or to the participant's designated beneficiary in the case of death, and a certificate will be issued for the full shares in the participant's account.

The Board of Directors may terminate or amend the stock purchase plan, subject to stockholder approval in some circumstances. Unless terminated earlier by the Board, the stock purchase plan will have a term of ten years.

Total shares purchased under the plan were 182,437 and 118,223 in 2002 and 2001, respectively. At December 31, 2002, there were 3,533,857 shares available for purchase under the plan.

NOTE 16 DEFERRED STOCK COMPENSATION

In connection with the grant of certain stock options and restricted common stock to employees, non-employees and members of the Board of Directors and in connection with certain acquisitions (see Note 6), the Company recorded net deferred stock compensation of $8.7 million, $4.7 million and $0.3 million for the years ended December 31, 2002, 2001 and 2000, respectively, representing the fair value of restricted stock and the difference between the fair value of common stock and the option exercise price of options at the date of grant. Deferred compensation is presented as a reduction of stockholders' equity, with amortization recorded over the vesting period of the related restricted stock and options. The Company recorded stock compensation expense of $3.1 million, $5.2 million and $11.6 million for the year ended December 31, 2002, 2001 and 2000, respectively. At December 31, 2002, approximately $11.8 million remained to be amortized over the corresponding vesting period of each respective option or restricted share, generally four to five years.

NOTE 17 401(K) PLAN

On January 1, 2000, the Company adopted the UTStarcom, Inc. 401(k) Savings Plan (the "401(k) Plan"), a cash-or-deferred arrangement, which covers the Company's eligible employees who have attained the age of 21. The 401(k) Plan is intended to qualify under Sections 401(a), 401(m) and 401(k) of the Internal Revenue Code of 1986, as amended (the "Code"), and the 401(k) Plan trust is intended to qualify under Section 501(a) of the Code. All contributions to the 401(k) Plan by eligible employees or by the Company, and the investment earnings thereon, are not taxable to such employees until withdrawn, and any contributions the Company may make are expected to be deductible by the Company. The Company's eligible employees may elect to reduce their current eligible compensation by one percent (1%) up to fifty percent (50%), subject to the maximum statutorily prescribed annual limit of $11,000 for participants under age 50 and $12,000 for participants age 50 and over, and to have such salary reductions contributed on their behalf to the 401(k) Plan. The 401(k) Plan permits, but does not require, the Company to make matching contributions on behalf of all eligible employees who make salary reduction contributions to the 401(k) Plan. Commencing with the plan year beginning January 1, 2001, the Company elected to begin making matching contributions on behalf of qualified employees who participate in the 401(k) Plan. The Company will contribute $0.50 for each dollar contributed by qualified employees to the 401(k) Plan, to a maximum of $3,000 for the 2002 and 2001 plan years. The Company's matching contributions are subject to a vesting schedule based upon longevity of employee service with the Company. Matching contributions were $0.7 million and $0.4 million for 2002 and 2001, respectively.

NOTE 18 COMMITMENTS AND CONTINGENCIES

Leases:

The Company leases certain facilities under non-cancelable operating leases which expire at various dates through 2007. The minimum future lease payments under the leases at December 31, 2002 are as follows:

	(in thousands)
Years ending December 31:	
2003	$ 5,863
2004	3,548
2005	988
2006	100
2007	75
Total minimum lease payments	$ 10,574

Rent expense for the years ended December 31, 2002, 2001 and 2000 was $6.5 million, $3.8 million, and $2.2 million, respectively.

Litigation:

On October 31, 2001, a complaint was filed in United States District Court for the Southern District of New York against the Company, some of its directors and officers and various underwriters for its initial public offering. Substantially similar actions were filed concerning the initial public offerings for more than 300 different issuers, and the cases were coordinated as *In re Initial Public Offering Securities Litigation*, 21 MC 92. In April 2002, a consolidated amended complaint was filed in

the matter against the Company, captioned *In re UTStarcom, Initial Public Offering Securities Litigation*, Civil Action No. 01-CV-9604. Plaintiffs allege violations of the Securities Act of 1933 and the Securities Exchange Act of 1934 through undisclosed improper underwriting practices concerning the allocation of IPO shares in exchange for excessive brokerage commissions, agreements to purchase shares at higher prices in the aftermarket, and misleading analyst reports. Plaintiffs seek unspecified damages on behalf of a purported class of purchasers of the Company's common stock between March 2, 2000 and December 6, 2000. The claims against our directors and officers have been dismissed without prejudice pursuant to a stipulation. The Company believes that it has meritorious defenses to this lawsuit and will defend this lawsuit vigorously. Motions to dismiss have been filed on behalf of the Company and the other defendants in the coordinated proceeding. Those motions are currently pending with the Court.

Investment Commitments:

In June 2002, the Company invested $1.0 million in Global Asia Partners L.P. The fund size is anticipated to be $100 million and was formed to make equity investments in private or pre-IPO technology and telecommunications companies in Asia. The Company has a commitment to invest up to a maximum of $5.0 million. The remaining amount is due at such times and in such amounts as shall be specified in one or more future capital calls to be issued by the general partner.

NOTE 19 OPERATING RISKS

Financial Risks:

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash, cash equivalents, short-term investments and accounts receivable. The Company places its temporary cash and short-term investments with several financial institutions. Approximately $115.1 million and $128.0 million of the Company's cash was on deposit in foreign accounts at December 31, 2002 and 2001, respectively. The Company invests excess cash in highly liquid investments with original maturities of twelve months or less, such as certificates of deposit, government sponsored entities notes, commercial paper, floating rate corporate bonds, fixed income corporate bonds, and money market funds, which the Company believes have limited exposure to risk.

Concentration of Credit Risk and Major Customers:

The Company's first and second largest customers accounted for 17.8% and 12.5% of the Company's sales in 2002 and 23.7% and 6.6% of the Company's sales in 2001, respectively, and 5.7% and 0.4% of accounts receivable at December 31, 2002 and 35.5% and 10.3% of accounts receivable at December 31, 2001, respectively. The Company's first and second largest customers accounted for 12.1% and 8.4% of the Company's net sales, respectively, in 2000. Approximately 84%, 90% and 90% of the Company's net sales during 2002, 2001 and 2000, respectively, were to entities affiliated with the government of China. Accounts receivable balances from these China government affiliated entities or state owned enterprises were $238.0 million and $192.8 million, respectively, as of December 31, 2002 and 2001. The Company extends credit to its customers generally without requiring collateral. The Company monitors its exposure for credit losses and maintains allowances for doubtful accounts.

Country Risks:

Approximately 84% of the Company's sales for the year ended December 31, 2002 were made in China. Accordingly, the Company's business, financial condition and results of operations may be

influenced by the political, economic and legal environment in China, and by the general state of China's economy. The Company's operations in China are subject to special considerations and significant risks not typically associated with companies in the United States. These include risks associated with, among others, the political, economic and legal environments and foreign currency exchange. The Company's results may be adversely affected by, among other things, changes in the political, economic and social conditions in China, and by changes in governmental policies with respect to laws and regulations, changes in China's telecommunications industry and regulatory rules and policies, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation.

Under China's current regulatory structure, the telecommunications products that the Company offers in China must meet government and industry standards, and a network access license for the equipment must be obtained. Without the license, the equipment is not allowed to be connected to public telecommunications networks or sold in China. Moreover, the Company must ensure that the quality of the telecommunications equipment for which it has obtained a network access license is stable and reliable, and may not lower the quality or performance of other installed licensed products. The State Council's product quality supervision department, in concert with the Ministry of Information Industry, performs spot checks to track and supervise the quality of licensed telecommunications equipment and publishes the results of such spot checks.

The regulations implementing these requirements are not very detailed, have not been applied by a court and may be interpreted and enforced by regulatory authorities in a number of different ways. The Company obtained the required network access licenses for its AN-2000 platform. The Company applied for, but has not yet received, a network access license for its PAS systems and handsets. Based upon conversations with the Ministry of Information Industry, the Company understands that its PAS systems and handsets are considered to still be in the trial period and that sales of the Company's PAS systems and handsets may continue to be made during this trial period, but a license will ultimately be required. Network access licenses will also be required for most additional products that the Company is selling or may sell in China, including the mSwitch platform. If the Company fails to obtain the required licenses, the Company could be prohibited from making further sales of the unlicensed products, including the PAS systems and handsets, in China, which would substantially harm its business, financial condition and results of operations. The Company's counsel in China has advised that China's governmental authorities may interpret or apply the regulations with respect to which licenses are required and the ability to sell a product while a product is in the trial period in a manner that is inconsistent with the information received by such counsel in China, either of which could have a material adverse effect on the Company's business and financial condition.

NOTE 20 SEGMENT REPORTING

The Company provides telecommunications equipment through an integrated suite of network access systems and subscriber terminal products. The Company primarily operates in two geographic areas, China and other regions. The chief operating decision makers evaluate performance, make operating decisions, and allocate resources based on consolidated financial data. Gross profit, operating income, income from operations, and income taxes are not allocated to specific individual departments within the organization. In accordance with SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information," the Company is considered a single reportable segment. The Company is required to disclose certain information about product revenues, information about geographic areas, information about major customers, and information about long-lived assets.

During the third quarter of 2002, the provincial-level telecommunications service entity in the Zhejiang province of China began to consolidate telecommunications purchasing decisions for that province. As a result of this trend in the Zhejiang province, the Company has grouped all customers in Zhejiang province together and has treated these as one customer. At December 31, 2002, the Company had approximately 33 such customers in Zhejiang province. For the year ended December 31, 2002, sales to Zhejiang province and BBTC accounted for 18% and 13% of net sales, respectively. For the year ended December 31, 2001, sales to Zhejiang province accounted for 24% of our net sales. For the year ended December 31, 2000, sales to Hangzhou PTT accounted for 12% of net sales. Revenue attributable to Japan was primarily due to sales to BB Technologies Corporation. Sales to BB Technologies Corporation were $123.0 million and $13.9 million and $0.0 million for the year ended December 31, 2002, 2001 and 2000, respectively.

Geographical area and product sales data are as follows (in thousands):

	Year ended December 31, 2002		
	Telecommunications Equipment	Subscriber Handsets	Total
Net sales:			
China	$ 445,789	$ 376,510	$ 822,299
Japan	130,104		130,104
Other	29,108	295	29,403

	Year ended December 31, 2002		
Total net sales	$ 605,001	$ 376,805	$ 981,806

	Year ended December 31, 2001		
	Telecommunications Equipment	Subscriber Handsets	Total
Net sales:			
China	$ 378,934	$ 186,946	$ 565,880
Japan	16,303		16,303
Other	43,701	956	44,657
Total net sales	$ 438,938	$ 187,902	$ 626,840

	Year ended December 31, 2000		
	Telecommunications Equipment	Subscriber Handsets	Total
Net sales:			
China	$ 257,474	$ 106,572	$ 364,046
Japan	1,084		1,084
Other	3,516		3,516
Total net sales	$ 262,074	$ 106,572	$ 368,646

Long-lived assets by geography are as follows (in thousands):

	December 31,	
	2002	2001
Foreign	$ 104,731	$ 41,289
U.S.	43,600	41,645
Total long-lived assets	$ 148,331	$ 82,934

NOTE 21 RELATED PARTY TRANSACTIONS

The Company recognized revenue of $123.0 million, $13.9 million, and $0.0 during the twelve months ended December 31, 2002, 2001 and 2000, respectively, with respect to sales of telecommunications equipment to BB Technologies Corporation ("BBTC"), an affiliate of SOFTBANK CORP. SOFTBANK America Inc., an entity affiliated with SOFTBANK CORP., is a significant stockholder of the Company. BBTC offers asynchronous digital subscriber line ("ADSL") coverage throughout Japan, which is marketed under the name YAHOO. The Company provides ADSL technology to BBTC. The contract was competitively bid and the terms of this contract were on terms no more favorable than those with unrelated parties. Included in accounts receivable at December 31, 2002 is $0.8 million related to this agreement. There were no amounts included in deferred revenue in respect of this agreement at December 31, 2002. Included in accounts receivable in respect of this agreement at December 31, 2001 was $13.5 million. There were no amounts included in deferred revenue in respect of this agreement at December 31, 2001.

The Company has invested in Softbank China and Restructuring Fund No. 1, which are investment vehicles established by SOFTBANK and its affiliates. See Note 9.

On August 29, 2002, the Company completed the repurchase of six million shares of the Company's common stock for $72.9 million from its largest shareholder, SOFTBANK Corp. As part of this transaction, SOFTBANK signed a voluntary "lock up" agreement stipulating that it will not sell any of the Company's common stock within the next six months. This lock up agreement will end on March 1, 2003, which coincides with the start of the Company's "blackout period" in which insiders are not permitted to sell shares. The blackout period begins March 1, 2003 and ends commencing at the close of business on the second trading day following the public release of our first quarter fiscal 2003 results in April 2003. The Company recorded the cost of the common stock repurchased and the related transaction costs of $36.4 million to additional paid-in capital and common stock based on the pro rata amount of shares repurchased, with the remaining $36.5 million recorded to retained earnings in accordance with Accounting Principles Board Opinion No. 6.

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QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

Quarterly financial data for the periods indicated are as follows:

	Quarters Ended							
(In thousands, except per share amounts)	**Dec. 31, 2002**	**Sept. 30, 2002**	**June 30, 2002**	**March 31, 2002**	**Dec. 31, 2001**	**Sept. 30, 2001**	**June 30, 2001**	**March 31, 2001**
Net sales	$ 301,095	$ 265,513	$ 231,508	$ 183,690	$ 197,128	$ 170,484	$ 140,047	$ 119,181
Gross profit	$ 101,101	$ 92,817	$ 85,912	$ 65,642	$ 68,952	$ 64,276	$ 49,907	$ 41,413
Net income	$ 33,852	$ 30,749	$ 25,735	$ 17,526	$ 16,535	$ 18,797	$ 12,260	$ 9,362
Net earnings per share:*								
Basic	$ 0.32	$ 0.28	$ 0.23	$ 0.16	$ 0.15	$ 0.18	$ 0.13	$ 0.10
Diluted	$ 0.30	$ 0.27	$ 0.22	$ 0.15	$ 0.14	$ 0.17	$ 0.12	$ 0.09

* Net earnings per share is computed independently for each of the quarters presented and, therefore, the sum of the quarterly net earnings per share may not equal the annual earnings per share.

ITEM 9 CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

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PART III

ITEM 10 DIRECTORS AND EXECUTIVE OFFICERS OF UTSTARCOM, INC.

The information required by this section is incorporated by reference from the information in the section entitled "Election of Directors" in the Proxy Statement. The required information concerning our executive officers is contained in the section entitled "Executive Officers" in Part I of this Form 10-K.

Item 405 of Regulation S-K calls for disclosure of any known late filing or failure by an insider to file a report required by Section 16 of the Exchange Act. This disclosure is contained in the section entitled "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement and is incorporated herein by reference.

ITEM 11 EXECUTIVE COMPENSATION

The information required by this section is incorporated by reference from the information in the sections entitled "Election of Directors Directors' Compensation," "Executive Compensation and Other Matters," "Report of the Compensation Committee," and "Stock Price Performance Graph" in the Proxy Statement.

ITEM 12 SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this section is incorporated by reference from the information in the section entitled "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement. The required information concerning our equity compensation plans is contained in the section entitled "Market for Registrant's Common Equity and Related Stockholder Matters" in Part II of this Form 10-K.

ITEM 13 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this section is incorporated by reference from the information in the section entitled "Certain Relationships and Related Transactions" in the Proxy Statement.

PART IV

ITEM 14 CONTROLS AND PROCEDURES

(a) *Evaluation of disclosure controls and procedures.* Our chief executive officer and our chief financial officer, after evaluating the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-14(c) and 15d-14(c) of the Securities Exchange Act of 1934) as of a date (the "Evaluation Date") within 90 days before the filing date of this quarterly report, believe that as of the Evaluation Date, the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company would be made known to them by others within the Company.

(b) *Changes in internal controls.* There were no significant changes in our internal controls or in other factors that could significantly affect our disclosure controls and procedures subsequent to the Evaluation Date.

ITEM 15 EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) (1) **Financial Statements** See Index to Consolidated Financial Statements and Financial Statement Schedules at page 69 of this Form 10-K.

(2) **Financial Statement Schedule** See Index to Consolidated Financial Statements and Financial Statement Schedules at page 69 of this Form 10-K.

(3) **Exhibits**

Exhibit Number	Description
3.1(1)	Thirteenth Amended and Restated Certificate of Incorporation of UTStarcom, Inc.

Exhibit Number	Description
3.2(1)	Amended and Restated Bylaws of UTStarcom, Inc.
4.1	See exhibits 3.1 and 3.2 for provisions of the Certificate of Incorporation and Bylaws defining the rights of holders of Common Stock.
4.2(1)	Specimen Common Stock Certificate.
4.3(1)	Third Amended and Restated Registration Rights Agreement dated December 14, 1999.
10.1(1)	Form of Indemnification Agreement.
10.2(1)	1992 Omnibus Equity Incentive Plan and form of related agreement.
10.3(1)	1995 Stock Plan and forms of related agreements.
10.4(1)	1997 Stock Plan, as amended, and forms of related agreements.
10.5(1)	2000 Employee Stock Purchase Plan and forms of related agreements.
10.6(1)	Common Stock Purchase Warrant dated February 5, 1998 between UTStarcom, Inc. and Lintech Limited.
10.7(1)	Common Stock Purchase Warrant dated September 20, 1999 between UTStarcom, Inc. and Talent Group International, Ltd.
10.8(1)	Employment and Non-Competition Agreement dated October 6, 1995 between UTStarcom, Inc. and Hong Lu.
10.9(1)	Employment and Non-Competition Agreement dated October 6, 1995 between UTStarcom, Inc. and Ying Wu.
10.10(1)*	Product Manufacture & License Agreement dated May 13, 1997 between UTStarcom, Inc. and Tollgrade Communications, Inc.
10.11(1)*	Sales Agreement dated February 12, 1999 between UTStarcom (China) Ltd. and BaoDing Telecommunication Bureau, Hebei Province.
10.12(1)*	Sales Contract dated August 23, 1999 between UTStarcom (China) Ltd. and Xian Telecommunication Bureau.
10.13(1)*	Technical License and Assistance Agreement dated November 2, 1999 between UTStarcom, Inc. and Mitsubishi Electric Corporation.
10.13(a)(1)*	Amendment No. 1 to Technical License and Assistance Agreement dated February 21, 2000 between UTStarcom, Inc. and Mitsubishi Electric Corporation.
10.14(1)*	Technical Assistance Agreement dated October 1, 1999 between Matsushita Communication Industrial Co. Ltd. and UTStarcom, Inc.
10.14(a)(1)	Addendum dated February 18, 2000 to the Technical Assistance Agreement dated October 1, 1999 between Matsushita Communication Industrial Co. Ltd. and UTStarcom, Inc.
10.15(1)*	Joint Product Development and Marketing Memorandum and Understanding dated September 2, 1999 between UTStarcom, Inc. and Matsushita Communication Industrial Co., Ltd.
10.16(1)*	Joint Patent Filing Agreement dated December 1, 1998 between UTStarcom, Inc. and Matsushita Communication Industrial Co., Ltd.

10.17(1)*	Loan Agreement dated June 15, 1998 between UTStarcom, Inc. and SOFTBANK Corp.
10.18(a)(1)*+	Loan Agreement dated March 9, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(b)(1)*	Loan Agreement dated June 7, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(c)(1)*	Loan Agreement dated June 29, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(d)(1)*	Loan Agreement dated July 7, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(e)(1)*	Loan Agreement dated July 14, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(f)(1)*	Loan Agreement dated July 21, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(g)(1)*	Loan Agreement dated August 5, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(h)(1)*	Loan Agreement dated August 17, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(i)(1)*	

	Loan Agreement dated September 2, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.18(j)(1)*	Loan Agreement dated September 17, 1999 between Bank of China and UTStarcom Hangzhou Telecommunications Co., Ltd.
10.19(1)*	Joint Venture Agreement dated July 31, 1997 between UTStarcom, Inc. and Zhejiang Telecommunication Equipment Factory.
10.20(1)*	Joint Venture Agreement dated December 8, 1995 between UTStarcom, Inc. and Chinese Guangdong Nanfeng Telecommunication Group Co. Ltd.
10.20(a)(1)*	Amendment Agreement to the Contract and Articles of Association of Guangdong UTStarcom Communications Co. Ltd. dated December 11, 1997.
10.21(1)*	Joint Venture Agreement dated September 12, 1997 between UTStarcom, Inc. and Zhejiang Nantian Post and Telecommunication Development Group Co. Ltd.
10.22(1)	Lease dated December 23, 1997 between UTStarcom, Inc. and Tech Center Partners.
10.23(1)	Lease Agreement dated April 1995, as amended, between UTStarcom, Inc. and Metro Park Associates.
10.24(1)	Lease Agreements dated December 31, 1997 and May 14, 1998 between Guangdong UTStarcom Telecom Co., Ltd. and Guangdong Southern Telecom Group Huizhou Company.
10.25(1)	Lease Contract dated December 15, 1996 between UTStarcom (Hangzhou) Telecommunications Co., Ltd. and Yile Village, Gudang Township.
10.26(1)*	Purchase Agreement for P.R. China Market dated April 1, 1999 between UTStarcom Inc., Matsushita Electric Industrial Co., Ltd. and Matsushita Communication Industrial Co., Ltd.
10.27(1)	Information Service Project Contract dated June 1, 1998 between UTStarcom (China) Ltd. and China Jitong Communication Co. Ltd.

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10.28(1)	Payment Agent Contract dated June 11, 1998 among UTStarcom, UTStarcom (China) Ltd, Softbank Corporation and Jitong Communication Co., Ltd.
10.29(1)	Agreement on Termination of Contract dated August 30, 1999 among UTStarcom, Inc., UTStarcom (China) Ltd., Softbank Corporation and Jitong Communication Co., Ltd.
10.30(1)	Exchange Agreement dated October 15, 1997 between UTStarcom, Inc. and certain investors.
10.31(1)	Exchange Agreement dated October 15, 1997 between UTStarcom, Inc. and certain investors.
10.32(1)	Employment and Non-Competition Agreement dated October 6, 1995 between UTStarcom, Inc. and Bill Huang.
10.33(1)	Lease contract on Housing and Vacant Land at Yunshan Post and Telecommunication Industrial Village dated January 3, 2000 between Guangdong UTStarcom Telecom Co., Ltd. and Guangdong Nanfang Communication Group, Huizhou Co.
10.34(1)	Loan Agreement dated October 8, 1996 between UTStarcom (China) Co., Inc. and Bill X. Huang.
10.35(1)	Promissory Note Secured by Deed of Trust dated February 13, 1999 issued to UTStarcom, Inc. by Bill X. Huang and Minnie Huang.
10.36(1)*	Supply Agreement dated February 18, 2000 between UTStarcom, Inc. and Matsushita Electric Industrial Co., Ltd.
10.37(2)*	Manufacturing License Agreement between Himachal Futuristic Communications Ltd. and UTStarcom, Inc. undated.
10.38(2)*	Sales Agreement between Japan Radio Company and UTStarcom, Inc. dated March 16, 2000.
10.39(2)*	Technical Collaboration Agreement between Sharp Corporation and UTStarcom, Inc., dated March 31, 2000.
10.40(2)*	Parts Supply Agreement between Sharp Corporation and UTStarcom, Inc. undated.
10.41(3)*	Joint Venture Agreement between SOFTBANK Corporation and UTStarcom, Inc. dated May 29, 2000.
10.42(3)*	Land Use Right Assignment Agreement between the Administration Committee of Hangzhou Hi-Tech Industry Development Zone of Zhejiang Province of the People's Republic of China and UTStarcom, Inc. dated May 18, 2000.
10.43(3)*	Supply Agreement between Matsushita Electric Industrial Co., Ltd., Matsushita Communications Industrial Co., Ltd., and UTStarcom, Inc. dated April 1, 2000.
10.44(4)*	OEM Agreement between UTStarcom, Inc. and Zaffire, Inc., dated August 10, 2000.
10.45(4)*	Development Agreement between UTStarcom, Inc. and Matsushita Communication Industrial Co., Ltd., dated September 26, 2000.

10.46(4)*	OEM Agreement between UTStarcom, Inc. and Interwave Communications International, Ltd., dated July 14, 2000.
10.47(4)*	OEM Agreement between UTStarcom, Inc. and Foundry Networks, Inc., dated August 24, 2000.
10.48(4)*	Loan Contract between UTSC Co., Ltd. and Bank of China Beijing Branch, dated August 29, 2000.

10.49(9)*	Sales Contract between UTStarcom (China), Ltd. and Zhejiang Telecom Company (Shaoxing Branch), dated November 18, 2000.
10.50(9)*	Sales Contract between UTStarcom (China), Ltd. and He Nan Telecom Company, dated October 28, 2000.
10.51(9)*	Sales Contract between UTStarcom (China), Ltd., Xian Equipment Import/Export Company, Ltd., and Shaanxi China Telecom Group, Ltd., dated September 29, 2000 (received by UTStarcom, Inc. on October 9, 2000).
10.52(9)*	Technical Assistance Agreement between UTStarcom, Inc. and Matsushita Communication Industrial Co. Ltd., dated December 1, 2000.
10.53(9)*	Definitive Agreement for Collaboration between UTStarcom, Inc. and Mitsubishi Electric Corporation, dated October 22, 2000.
10.54(9)*	Software License Agreement between UTStarcom, Inc. and DDI Corporation, Inc. dated October 4, 2000.
10.55(9)*	Strategic Alliance, Purchase and License Agreement between UTStarcom, Inc. and Telecommunication D'Haiti S.A.M., dated December 5, 2000.
10.56(5)*	Assignment Agreement between UTStarcom, Inc. and Stable Gain International Limited dated July 24, 2000.
10.57(5)*	Amendment No.1 to July 24, 2000 Assignment Agreement between UTStarcom, Inc. and Stable Gain International Limited, dated March 2, 2001.
10.58(5)*	Loan Agreement between China Merchant Bank and UTStarcom (China) Co., Ltd., dated March 14, 2001.
10.59(5)*	Technical Service Agreement between UTStarcom (China) Co., Ltd. and Hainan Xinhuangpu Investment Co., Ltd., dated August 18, 2000.
10.60(5)*	Assets Transfer Agreement between Hainan Xinhuangpu Investment Co., Ltd. and UTStarcom (China) Co., Ltd., dated August 18, 2000.
10.61(5)*	Equity Transferring Agreement between Zhe Jiang Nantian Telecommunication Development Group Share Company and UTStarcom, dated February 5, 2001.
10.62(5)*	Sales Contract between Zhejiang Telecom Co. and UTStarcom (China) Co., Ltd., dated March 23, 2001.
10.63(5)*	Manufacturing License Agreement between Himachal Futuristic Communications Ltd. and UTStarcom, Inc. dated March 6, 2001.
10.64(7)	2001 Director Option Plan.
10.65(7)*	Strategic Alliance, Purchase and License Agreement between UTStarcom, Inc. and Telecommunications D'Haiti S.A.M. dated as of April 12, 2001.
10.66(6)	2001 Director Option Plan, as amended on July 10, 2001.
10.67(8)*	Purchase Contract between UTStarcom Inc. and BB Technologies Corporation, dated October 9, 2001.
10.68(10)	Comprehensive Credit-Extension Agreement between UTStarcom (China) Ltd. and China Everbright Bank, Chaoyang Branch, Beijing, dated November 30, 2001.
10.69(10)	Equity Transfer Agreement between UTStarcom, Inc. and Guangdong Nanfang Communications Group Co. Ltd., dated December 18, 2001.
10.70(10)	Equity Transfer Agreement between UTStarcom, Inc. and Zhejiang Provincial Telecom. Instruments Factory and UTStarcom (Hangzhou) Communications Co., Ltd., dated January 21, 2002.

10.71(10)	Lease Agreement between UTStarcom, Inc. and Legend Tech., dated September 12, 2001.
10.72(11)	Comprehensive Credit-Extension Agreement between UTStarcom (China) Ltd. and Beijing City Commercial Bank, Yuhaiyuan Road Branch, dated February 20, 2002, and Maximum Amount Guaranty Contract between UTStarcom (Hangzhou) Telecommunication Co., Ltd. and Beijing City Commercial Bank, Yuhaiyuan Road Branch, dated February 20, 2002.
10.73(11)	Change of Control Severance Agreement between Gerald Soloway and UTStarcom, Inc. dated April 12, 2002.

10.74(11)	Change of Control Severance Agreement between Howard Kwock and UTStarcom, Inc. dated April 12, 2002.
10.75(11)	Change of Control Severance Agreement between Michael J. Sophie and UTStarcom, Inc. dated April 12, 2002.
10.76(12)	Comprehensive Credit-Extension Agreement between UTStarcom (China) Ltd. and Shenzhen Development Bank, Hangzhou, dated June 26, 2002.
10.77(12)	Merger Agreement by and between UTStarcom Telecom Co., Ltd. and Guangdong UTStarcom Teleco.
10.78(13)*	Professional Services Agreement between UTStarcom, Inc. and N. Lohr Bangle, Jr. dated as of September 10, 2002.
10.79(13)*	Teaming Agreement between UTStarcom, Inc. and Stellar Holdings, LLC dated as of September 10, 2002.
10.80(13)*	Joint Venture Contract between UTStarcom Telecom Co., Ltd., Matsushita Electric Industrial Co., Ltd. and Matsushita Communication Industrial Co., Ltd. dated as of July 5, 2002.
10.81(13)*	Amendment to OEM Agreement between UTStarcom, Inc. and InterWave Communications dated as of September 27, 2002.
10.82*	Joint Development Agreement between Datang Mobile Communications Equipment Co., Ltd and UTStarcom (China) Co., Ltd. dated November 22, 2002.
10.83*	Broadband Access Network General Terms and Conditions between Reliance Infocomm Limited and UTStarcom, Inc. dated as of October 1, 2002.
10.84*	Broadband Access Equipment Contract between Reliance Infocomm Limited and UTStarcom, Inc. dated as of October 1, 2002.
10.85*	Broadband Access Services Contract between Reliance Infocomm Limited and UTStarcom, Inc. dated as of October 1, 2002.
10.86*	Broadband Access Software Contract between Reliance Infocomm Limited and UTStarcom, Inc. dated as of October 1, 2002.
21.1	Subsidiaries of UTStarcom.
23.1	Consent of PricewaterhouseCoopers LLP.
23.2(10)	Consent of Willamette Management Associates.
24.1	Power of Attorney (included on signature page).

99.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*
Portions of the exhibit have been omitted pursuant to an order granted by the Securities and Exchange Commission for confidential treatment.

(1)
Incorporated by reference to the registrant's Registration Statement on Form S-1 (No. 333-93069), which became effective March 2, 2000.

(2)
Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000.

(3)
Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000.

(4)
Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000.

(5)
Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2001.

(6)

Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001.

(7) Incorporated by reference to the registrant's Registration Statement on Form S-3, which became effective July 18, 2001.

(8) Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2001.

(9) Incorporated by reference to the registrant's Annual Report on Form 10-K for the year ended December 31, 2000.

(10) Incorporated by reference to the registrant's Annual Report on Form 10-K for the year ended December 31, 2001.

(11) Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2002.

(12) Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2002.

(13) Incorporated by reference to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2002.

(b) Reports on Form 8-K:

1. UTStarcom filed a Report on Form 8-K with the Securities and Exchange Commission on August 29, 2002 in connection with its Repurchase of 6,000,000 shares of Common Stock from SOFTBANK Corp.

(c) Exhibits

See Item 15(a)(3) above.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934 as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 21st day of February, 2003.

UTSTARCOM, INC.

By: /s/ MICHAEL J. SOPHIE

Michael J. Sophie
Vice President of Finance, Chief Financial Officer
and Assistant Secretary

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENT, that each person whose signature appears below constitutes and appoints Hong Liang Lu and Michael J. Sophie, jointly and severally, his or her attorneys-in-fact, each with the power of substitution, for him in any and all capacities, to sign any amendments to this report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact, or his substitute or substitutes may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1934, this report has been signed below by the following persons in the capacities and on the dates indicated:

Signature	Title	Date
/s/ HONG LIANG LU Hong Lu	President and Chief Executive Officer (principal executive officer) and Director	February 21, 2003
/s/ MICHAEL J. SOPHIE Michael J. Sophie	Vice President of Finance, Chief Financial Officer and Assistant Secretary (principal financial and accounting officer)	February 21, 2003
/s/ BETSY S. ATKINS Betsy S. Atkins	Director	February 21, 2003
/s/ LARRY D. HORNER Larry D. Horner	Director	February 21, 2003
/s/ MASAYOSHI SON Masayoshi Son	Chairman of the Board of Directors	February 21, 2003
/s/ THOMAS J. TOY Thomas J. Toy	Director	February 21, 2003
/s/ YING WU Ying Wu	Executive Vice President, Chief Executive Officer, China Operations and Director	February 21, 2003

CERTIFICATIONS

I, Hong Liang Lu, certify that:

1. I have reviewed this annual report on Form 10-K of UTStarcom, Inc.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3.

Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4.
The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a)
designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

b)
evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

c)
presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5.
The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a)
all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b)
any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6.
The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 21, 2003

/s/ HONG LIANG LU

Hong Liang Lu
President and Chief Executive Officer

CERTIFICATIONS

I, Michael J. Sophie, certify that:

1.

I have reviewed this annual report on Form 10-K of UTStarcom, Inc.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

   c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 21, 2003

/s/ MICHAEL J. SOPHIE

Michael J. Sophie
Vice President of Finance, Chief Financial Officer and Assistant Secretary

INDEPENDENT ACCOUNTANTS REPORT ON FINANCIAL STATEMENT SCHEDULES

To the Board of Directors and Stockholders of UTStarcom, Inc.:

Our audits of the consolidated financial statements referred to in our report dated January 23, 2003 also included an audit of the financial statement schedules in this Annual Report on Form 10-K. In our opinion, these financial statement schedules present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

/s/ PricewaterhouseCoopers LLP
San Francisco, California
January 23, 2003

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SCHEDULE I

UTSTARCOM, INC. (UNCONSOLIDATED)

REGISTRANT BALANCE SHEETS

(in thousands, except share and per share data)

	December 31,	
	2002	**2001**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 117,003	$ 198,285
Short-term investments	80,662	86,176
Accounts receivable	234,917	116,265
Inventories	37,964	14,278
Other current assets	32,683	18,994
Total current assets	503,229	433,998
Property, plant and equipment, net	16,785	21,919
Investments in affiliated companies	346,645	223,200
Goodwill, net	43,542	33,549
Intangible assets, net	5,014	4,179
Deferred tax assets	9,335	8,270
Other long-term assets	1,545	383
Total assets	$ 926,095	$ 725,498
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 113,180	$ 11,354

	December 31,	
Income taxes payable	6,099	7,458
Deferred revenue	18,934	8,874
Other current liabilities	21,487	15,925
Total current liabilities	159,700	43,611
Stockholders' equity:		
Convertible preferred stock: $.00125 par value; authorized: 5,000,000 shares; issued and outstanding none at December 31, 2002 and 2001		
Common stock: $.00125 par value; authorized: 250,000,000 shares; issued and outstanding: 106,787,908 at December 31, 2002 and 109,302,816 at December 31, 2001	135	138
Additional paid-in capital	658,546	638,697
Deferred stock compensation	(11,766)	(6,045)
Retained earnings	120,520	49,146
Notes receivable from stockholders	(282)	(381)
Accumulated other comprehensive income (loss)	(758)	332
Total stockholders' equity	766,395	681,887
Total liabilities and stockholders' equity	$ 926,095	$ 725,498

The accompanying notes are an integral part of these financial statements.

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SCHEDULE I

UTSTARCOM, INC. (UNCONSOLIDATED)

CONDENSED INFORMATION AS TO THE RESULTS OF OPERATIONS OF THE REGISTRANT

(in thousands, except share and per share data)

	Years ended December 31,		
	2002	2001	2000
Net sales	$ 359,265	$ 351,373	$ 267,384
Cost of sales	309,544	294,995	228,624
Gross profit	49,721	56,378	38,760
Operating expenses:			
Selling, general and administrative expenses	38,793	25,199	14,814
Research and development expenses	9,146	56,937	40,957
Amortization of intangible assets	2,395	7,440	4,808

	Years ended December 31,		
In-process research and development costs	670	4,720	
Total operating expenses	51,004	94,296	60,579
Operating income	(1,283)	(37,918)	(21,819)
Interest income	4,454	7,832	12,426
Interest expense	(16)	(644)	(154)
Other income (expense), net	18,964	(1,737)	(139)
Equity in net income (loss) of affiliated companies	98,396	99,506	47,399
Income before income taxes and cumulative effect of a change of accounting principle	120,515	67,039	37,713
Income tax expense	12,653	10,085	9,720
Net income before cumulative effect of a change of accounting principle	107,862	56,954	27,993
Cumulative effect of a change in accounting principle, net of taxes			(980)
Net income	$ 107,862	$ 56,954	$ 27,013

The accompanying notes are an integral part of these financial statements.

SCHEDULE I

UTSTARCOM, INC. (UNCONSOLIDATED)

CONDENSED INFORMATION AS TO THE CASH FLOWS OF THE REGISTRANT

(In thousands)

	Years ended December 31,		
	2002	**2001**	**2000**
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 107,862	$ 56,954	$ 27,013
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Gain on change in ownership interest in subsidiary		(277)	
Depreciation and amortization	13,202	15,218	7,308
Non-qualified stock option exercise tax benefits	6,538	15,311	7,628
Write-off of in-process research and development costs	670	4,720	
Impairment of long-term investments	4,442	3,376	
Net loss on sale of assets	449	527	698
Cumulative effect of change in accounting principle			980
Stock compensation expense	3,100	5,201	11,560
Equity in net loss of affiliated companies	(95,608)	(97,816)	(47,399)
Changes in operating assets and liabilities:			

	Years ended December 31,		
Accounts receivable	(119,998)	(10,288)	(61,089)
Inventories	(22,995)	3,945	(6,744)
Other current and non-current assets	(12,908)	(19,060)	2,497
Accounts payable	98,947	(7,440)	14,363
Income taxes payable	(1,356)	3,459	(4,364)
Other current liabilities	4,649	2,956	(1,987)
Deferred revenue	10,060	(2,583)	10,957
Net cash provided by (used in) operating activities	(2,946)	(25,797)	(38,579)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Additions to property, plant and equipment	(5,511)	(19,853)	(6,044)
Investment in affiliates	(27,447)	(18,135)	(8,945)
Acquisition of businesses, net of cash acquired	(17,705)		
Purchases of intangible assets		(1,078)	
Purchases of short-term investments	(85,688)	(89,625)	(124,096)
Sales of short-term investments	89,916	87,516	40,290
Net cash used in investing activities	(46,435)	(41,175)	(98,795)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Issuance of stock, net of expenses	40,928	160,550	198,213
Repurchase of common stock	(72,929)		
Proceeds (payments) from borrowings, net		(5)	(8)
Proceeds (payments) from stockholder notes	99	(67)	245
Net cash (used in) provided by financing activities	(31,902)	160,478	198,450
Effects of exchange rates on cash	1	(26)	
Net increase (decrease) in cash and cash equivalents	(81,282)	93,480	61,076
Cash and cash equivalents at beginning of period	198,285	104,805	43,729
Cash and cash equivalents at end of period	$ 117,003	$ 198,285	$ 104,805

The accompanying notes are an integral part of these financial statements.

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SCHEDULE I

UTSTARCOM, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

UTStarcom, Inc., a Delaware corporation, is the parent company of all UTStarcom, Inc. subsidiaries. The accompanying condensed financial statements reflect the financial position, results of operations and cash flows of UTStarcom, Inc. on a separate basis. All subsidiaries of

UTStarcom, Inc. are reflected as investments accounted for using the equity method. Accordingly, intercompany transactions have not been eliminated. No cash dividends were paid to UTStarcom, Inc. by its subsidiaries during the three years ended December 31, 2002. For accounting policies and other information, see the Notes to Consolidated Financial Statements included elsewhere herein.

SCHEDULE II

UTSTARCOM, INC.

Valuation and Qualifying Accounts and Reserves

For the Years Ended December 31, 2002, 2001 and 2000.

Description	Balance at beginning of the period	Additions charged to costs and expenses	Deductions	Balance at end of the period
Year ended December 31, 2002				
Allowance for doubtful accounts	$ 19,053	$ 7,434	$ 237	$ 26,250
Accrued product warranty costs	$ 6,271	$ 15,156	$ 8,130	$ 13,297
Year ended December 31, 2001				
Allowance for doubtful accounts	$ 12,835	$ 6,218	$	$ 19,053
Accrued product warranty costs	$ 3,133	$ 6,792	$ 3,654	$ 6,271
Year ended December 31, 2000				
Allowance for doubtful accounts	$ 6,789	$ 6,448	$ 402	$ 12,835
Accrued product warranty costs	$ 1,236	$ 4,279	$ 2,382	$ 3,133

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