SIMPLETECH INC
Form S-1/A
October 15, 2003
Table of Contents

As filed with the Securities and Exchange Commission on October 15, 2003

Registration No. 333-109372

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

AMENDMENT NO. 1 TO

FORM S-1

REGISTRATION STATEMENT

Under

THE SECURITIES ACT OF 1933

SIMPLETECH, INC.

(Exact Name of Registrant as Specified in Its Charter)

California	**3572**	**33-0399154**
(State or Other Jurisdiction of Incorporation or Organization)	**(Primary Standard Industrial Classification Code Number)**	**(I.R.S. Employer Identification No.)**

3001 Daimler Street

Santa Ana, California 92705-5812

(949) 476-1180

(Address, Including Zip Code, and Telephone Number, Including Area Code, of Registrant s Principal Executive Offices)

Manouch Moshayedi

Chief Executive Officer

SIMPLETECH, INC.

3001 Daimler Street

Santa Ana, California 92705-5812

(949) 476-1180

(Name, Address, Including Zip Code and Telephone Number, Including Area Code, of Agent for Service)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box. ¨

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this prospectus is not complete and may be changed. Neither SimpleTech nor the Selling Shareholders may sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and we are not soliciting offers to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion, dated October 15, 2003

PROSPECTUS

14,000,000 Shares

Common Stock

This is an offering of shares of common stock of SimpleTech, Inc. Of the 14,000,000 shares being offered, SimpleTech is selling 10,000,000 shares and the selling shareholders are selling 4,000,000 shares. We will not receive any of the proceeds from the sale of shares by the selling shareholders.

Our common stock is traded on the Nasdaq National Market under the symbol STEC. On October 14, 2003, the last reported sale price of our common stock on the Nasdaq National Market was $10.05 per share.

Investing in our common stock involves risks. Risk Factors begin on page 7.

	Per Share	Total
Public Offering Price	$	$
Underwriting Discounts and Commissions	$	$
Proceeds to SimpleTech (before expenses)	$	$
Proceeds to Selling Shareholders (before expenses)	$	$

We and the selling shareholders have granted the underwriters a 30-day option to purchase up to 2,100,000 additional shares of our common stock to cover over-allotments.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Lehman Brothers, on behalf of the underwriters, expects to deliver the shares on or about , 2003.

LEHMAN BROTHERS

NEEDHAM & COMPANY, INC.

THOMAS WEISEL PARTNERS LLC

THE SEIDLER COMPANIES

, 2003

Table of Contents

Table of Contents

TABLE OF CONTENTS

You should rely only on the information contained in this prospectus. Neither we nor the underwriters have authorized anyone, including the selling shareholders, to provide you with information different from that contained in this prospectus. We and the selling shareholders are offering to sell, and seeking offers to buy, shares of common stock only in jurisdictions where such offers and sales are permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or any sale of the common stock.

Table of Contents

PROSPECTUS SUMMARY

The following summary highlights information we present more fully elsewhere in this prospectus. Because this is only a summary, it does not contain all of the information that may be important to you. You should read the entire prospectus carefully before deciding to invest in shares of our common stock. This prospectus contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of factors described under the heading Risk Factors and in our consolidated financial statements and related notes appearing elsewhere in this prospectus.

SimpleTech, Inc.

SimpleTech designs, manufactures and markets custom and open-standard memory solutions based on Flash memory and dynamic random access memory, or DRAM, technologies. We offer a comprehensive line of over 2,500 products and specialize in developing high-density memory modules, memory cards and storage drives. One way that we distinguish ourselves in the marketplace is by offering both Flash and DRAM-based solutions used by consumers and original equipment manufacturers, or OEMs. We believe this allows us to service a diverse customer base with multiple memory formats enabling our customers to purchase all of their memory requirements from one supplier. For the first half of 2003, our top five customers by revenues were CDW Computer Centers, Cisco Systems, Ingram Micro, Insight Direct and Sam s Club.

The growth in demand for consumer electronic devices such as digital cameras, MP3 digital audio players, personal digital assistants, or PDAs, digital camcorders and smart phones, as well as the increased memory requirements of these devices, has helped fuel the increased use of non-volatile data storage Flash memory, or NAND Flash. NAND Flash is the preferred technology for these applications because it is lightweight, durable, rugged, compact and retains data without power. Our Flash cards store digital content such as pictures, digital music, video clips and files in a small form factor with large storage capacity and low power consumption. We offer our Flash cards in all major media formats, including CompactFlash, Secure Digital, Memory Stick, SmartMedia and MultiMedia cards. In addition to the demand in consumer markets, our Flash business is also expanding as a result of the growing number of OEM applications in which Flash drives are replacing rotating disk drives due to improved performance, reliability and size. These OEM applications include military subsystems, in-flight information systems, casino gaming systems, embedded controls for industrial automation and medical equipment. According to Gartner Dataquest, in a report dated September 2003, NAND Flash industry revenues are expected to grow from $2.4 billion in 2002 to $7.3 billion in 2007. Our Flash revenues increased from $24.9 million for the year ended December 31, 1999 to $54.7 million for the year ended December 31, 2002, and were $35.4 million for the six-month period ended June 30, 2003.

Our DRAM products target primarily high-performance computing applications, including switches, routers, high-end servers, workstations, desktops and notebooks. As the applications that we serve expand and as the complexity of these applications increases, the need for the customization of our products in these applications also increases. We have developed proprietary technologies to address the increased need for customized solutions. For example, our patented IC Tower® stacking technology allows multiple memory chips to be stacked together to increase the capacity of a memory module without expanding its footprint. This technique increases memory board density significantly over conventional techniques and is particularly well-suited for applications where high memory capacity, cost and space are critical. We have recently experienced growing demand for our IC Tower stacking products driven by our increased penetration of the server market. We believe that this technology allows our customers to design memory-intensive systems on a differentiated and more price competitive basis. We also believe the growth of the DRAM market will be driven primarily by the next PC upgrade cycle, the demand for increased memory content per PC and a resumption of IT spending. According to Gartner Dataquest, in a report dated September 2003, the DRAM industry is expected to grow from $15.5 billion in 2002 to $25.3 billion in 2007.

1

Table of Contents

We offer memory solutions through our Consumer and OEM Divisions. Our Consumer Division sells open-standard memory storage products such as Flash cards, DRAM modules, USB mini drives and hard disk drives which are used primarily as upgrades in consumer electronic devices and computing systems. We believe our comprehensive line of products allows our customers to efficiently manage their inventory purchases and therefore reduce their costs by consolidating their purchases of memory and storage products into a single vendor. Our OEM Division sells primarily customized memory solutions for newly-manufactured systems, with most sales based on a cooperative design effort between our design engineers and our OEM customers. We believe the ability of these equipment manufacturers to shorten product development cycles and accelerate time-to-market is critical to their success. In response to this trend, we believe equipment manufacturers are increasingly outsourcing the design, development and manufacturing of memory products to third-party memory providers, such as SimpleTech. We believe our design, manufacturing, testing and logistics expertise, along with our proprietary technologies, enables us to respond quickly to our customers rapidly changing product and service requirements as well as meet their time-to-market schedules.

In addition, our Xiran Division develops advanced board-level solutions that optimize server performance for content delivery applications, including streaming media and video-on-demand, and networked storage applications, including IP storage. In September 2003, our Xiran Division received its first purchase orders from four companies which we expect will generate nominal revenues in the fourth quarter of 2003.

Our goal is to be a worldwide leader in the designing, manufacturing and marketing of custom and open-standard memory solutions. The following are key elements of our strategy:

- Increase our penetration of the consumer electronics and OEM markets by expanding our sales and marketing efforts;
- Expand and broaden our product line by leveraging our technology and design expertise;
- Maintain strong supplier relationships with our primary component vendors;
- Identify new applications and customers for our IC Tower stacking technology;
- Leverage our manufacturing efficiencies;
- Further penetrate international markets; and
- Pursue acquisitions of complementary businesses and technologies.

Recent Developments

The following are our expectations for the third quarter of 2003. However, we have not finalized our financial statements for this period. When actual results of operations are reported, it is possible that the results may vary from our expectations set forth below.

We expect our revenues to grow sequentially by 27% to 30% from $44.7 million for the second quarter of 2003 to between $57 million and $58 million for the third quarter of 2003. In addition, we expect earnings per share of $0.00 to $0.01 for the third quarter of 2003, compared to a net loss per share of $0.02 for the second quarter of 2003.

The following factors have impacted our expected results of operations for the third quarter of 2003:

- Approximately 70% quarterly growth in Flash revenue compared to the same quarter of 2002; fifth consecutive quarter of greater than 55% Flash revenue growth compared to the same period in the prior year;

- Current favorable pricing and demand environment in the Flash and DRAM markets; and

- Approximately 300% sequential increase in quarterly revenues from our IC Tower stacking products.

2

Table of Contents

This information should be read together with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes included elsewhere in this prospectus. See page 37 of this prospectus for selected quarterly results of operations for the eight quarters ended June 30, 2003.

Corporate Information

SimpleTech, Inc. was originally incorporated in California in March 1990 as Simple Technology, Inc. Our name was then changed to SimpleTech, Inc. in May 2001. Our principal executive offices are located at 3001 Daimler Street, Santa Ana, California 92705-5812. Our telephone number is (949) 476-1180. Our web site is located at www.simpletech.com. We also operate a web site for our Xiran Division located at www.xiran.com. The references to our web addresses do not constitute incorporation by reference of the information contained on those sites.

Table of Contents

THE OFFERING

Common stock offered by SimpleTech	10,000,000 shares
Common stock offered by the selling shareholders	4,000,000 shares
Common stock to be outstanding after this offering	49,244,235 shares
Use of proceeds	We plan to use the proceeds received by us in this offering for working capital and general corporate purposes, including expansion of sales and marketing activities, enhancement of our technology, improvement of our research and development, international expansion and possible acquisitions. See Use of Proceeds.
Nasdaq National Market symbol	STEC

The number of shares of common stock to be outstanding after this offering is based upon 38,994,235 shares of common stock outstanding as of August 31, 2003, 10,000,000 shares of common stock being sold by us and 250,000 shares to be issued upon the exercise of options by the selling shareholders immediately prior to this offering and excludes:

- 9,251,385 shares of common stock issuable upon exercise of stock options outstanding as of August 31, 2003 under our 2000 Stock Incentive Plan at a weighted average exercise price of $3.72 per share;
- 424,876 shares of common stock reserved for future issuance under our 2000 Stock Incentive Plan;
- 1,215,381 shares of common stock reserved for future issuance under our Employee Stock Purchase Plan; and
- Up to 1,200,000 shares of common stock to be sold by us if the underwriters exercise their over-allotment option in full.

You should read the discussion under Management Stock Plans/Employee Compensation Programs for additional information concerning our 2000 Stock Incentive Plan and our Employee Stock Purchase Plan.

ABOUT THIS PROSPECTUS

Unless otherwise indicated, the information in this prospectus assumes no exercise of the underwriters over-allotment option.

Prior to making a decision about investing in our common stock, you should consider carefully the specific risks contained in the section Risk Factors beginning on page 7, together with all of the other information contained in this prospectus and any prospectus supplement or appearing in the registration statement of which this prospectus is a part.

In this prospectus, SimpleTech, we, us and our refer to SimpleTech, Inc., a California corporation, and our subsidiaries.

Table of Contents

This prospectus includes statistical data regarding our company and the industries in which we compete. These data are based on our records taken or derived from information published or prepared by various sources, including Gartner Dataquest. Market data used throughout this prospectus are based upon industry sources and the good faith estimates of our management, based upon relevant information known to them. Although we believe those sources are reliable, the accuracy and completeness of this information is not guaranteed and has not been independently verified.

We own or have rights to product names, trade names and trademarks that we use in conjunction with the sale of our products, including Simple®, SimpleTech®, IC Tower®, SimpleDrive®, Bonzai, Xiran and CompactFlash. The CompactFlash Association makes the CompactFlash name and logo available royalty-free to member companies. References in this prospectus to CompactFlash are references only to our products unless otherwise indicated. This prospectus also contains other product names, trade names and trademarks that belong to other organizations.

Table of Contents

SUMMARY CONSOLIDATED FINANCIAL DATA

The following tables set forth summary consolidated financial data for SimpleTech. The historical results presented are not necessarily indicative of future results. The summary consolidated balance sheet data as of June 30, 2003 and consolidated statement of operations data for the six months ended June 30, 2003 and 2002 were derived from our unaudited financial statements and, in the opinion of management, reflect and include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of such results. The summary consolidated financial data set forth below should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes appearing elsewhere in this prospectus.

As adjusted amounts give effect to the issuance and sale of 10,000,000 shares of our common stock at an assumed public offering price of $10.05 per share, and the receipt of the net proceeds from this offering, after deducting the underwriting discounts and commissions and estimated offering expenses payable by us.

	Year Ended December 31,					Six Months Ended June 30,	
	1998	1999	2000	2001	2002	2002	2003
	(in thousands, except shares and per share data)						
Consolidated Statement of Operations Data:							
Net revenues	$ 122,288	$ 192,593	$ 308,316	$ 164,241	$ 176,531	$ 94,253	$ 85,663
Gross profit	24,358	39,850	68,352	36,550	32,949	17,610	14,655
Income (loss) from operations	(543)	14,113	29,356	2,482	(5,721) (3)	(2,466)	(4,722)
Net income (loss)	$ (2,163)	$ 12,503	$ 25,360	$ 2,340	$ (1,306)	$ (403)	$ (2,525)
Pro forma data (1):							
Pro forma net income (loss)	$ (1,327)	$ 7,431	$ 17,315				
Net income (loss) per share (pro forma in years 1998-2000) (2):							
Basic	$ (0.04)	$ 0.24	$ 0.53	$ 0.06	$ (0.03)	$ (0.01)	$ (0.06)
Diluted	$ (0.04)	$ 0.23	$ 0.50	$ 0.06	$ (0.03)	$ (0.01)	$ (0.06)
Shares used in computation of net income (loss) per share (2):							
Basic	30,601,027	30,601,027	32,393,218	38,126,687	38,515,825	38,413,980	38,874,014
Diluted	30,601,027	32,657,993	34,593,678	39,435,505	38,515,825	38,413,980	38,874,014

	As of June 30, 2003	
	Actual	As Adjusted
Consolidated Balance Sheet Data:		
Cash, cash equivalents and marketable securities	$ 44,016	$ 138,472
Working capital	57,917	152,373
Total assets	93,361	187,817
Total debt (including current maturities)		
Total shareholders equity	$ 71,625	$ 166,081

(1) From our formation in March 1990 to September 26, 2000, we elected for federal and state income tax purposes to be treated as an S corporation under Subchapter S of the Internal Revenue Code of 1986 and comparable state tax laws and filed our federal and state income tax returns on that basis. Accordingly, no provision has been made for federal or certain state income taxes. Pro forma net income (loss) has been computed using an effective tax rate of 38% to reflect the estimated income tax expense (benefit) as if we had been fully subject to federal and state income taxes as a C corporation for all periods presented. Subsequent to the termination of our S corporation status on September 26, 2000, we have paid federal and state corporate-level income taxes as a C corporation.

(2) Amounts reflect a 5.07 for 1 stock split of our common stock on September 8, 2000. All share and per share amounts have been adjusted to give retroactive effect to the stock split.

(3) Includes $1.4 million in-process research and development expenses related to our acquisition of the assets of Irvine Networks, LLC (currently our Xiran Division) in 2002.

Table of Contents

RISK FACTORS

Investing in our common stock involves a high degree of risk. Before purchasing our common stock, you should carefully consider the risks described below in addition to the other information in this prospectus. Our business, results of operations and financial condition may be materially and adversely affected due to any of the following risks. The risks described below are not the only ones we face. Additional risks we are not presently aware of or that we currently believe are immaterial may also impair our business operations. The trading price of our common stock could decline due to any of these risks, and you could lose all or part of your investment. In assessing these risks, you should also refer to the other information contained or incorporated by reference in this prospectus, including our financial statements and related notes.

Risks Related to Our Business and Industry

We expect our quarterly operating results to fluctuate in future periods, causing our stock price to fluctuate or decline.

Our quarterly operating results have fluctuated in the past, and we believe they will continue to do so in the future. Our future results of operations will depend on many factors including:

- Our suppliers production levels for the components used in our products;
- Our ability to procure required components or fluctuations in the cost of such components;
- Fluctuating market demand for, and changes in the average sales prices of our products;
- The effects of litigation;
- Changes in our product and revenue mix;
- Seasonal purchasing patterns for our products with lower sales generally occurring in the first and second quarters followed by higher sales in the fourth quarter of each year;
- Market acceptance of new and enhanced versions of our products;
- The timing of the introduction of new products or components and enhancements to existing products or components by us, our competitors or our suppliers;
- Order cancellations, product returns, inventory write-downs, price protections, and rebates;

- Manufacturing inefficiencies associated with the start-up of new products and volume production;
- Expenses associated with acquisitions;
- Our ability to adequately support future rapid growth;
- Our ability to absorb manufacturing overhead; and
- Increases in our sales and marketing expenses in connection with decisions to pursue new product initiatives.

Due to the above and other factors, quarterly revenues and results of operations are difficult to forecast, and period-to-period comparisons of our operating results may not be predictive of future performance. In one or more future quarters, our results of operations may fall below the expectations of securities analysts and investors. In that event, the trading price of our common stock would likely decline. In addition, the trading price of our common stock may fluctuate or decline regardless of our operating performance.

Our dependence on a small number of suppliers for integrated circuit, or IC, devices and inability to obtain a sufficient supply of these components on a timely basis could harm our ability to fulfill orders.

IC devices represent more than 90% of the component costs of our manufactured Flash cards and DRAM modules. We are dependent on a small number of suppliers that supply Flash and DRAM components. We have

Table of Contents

no long-term DRAM IC device supply contracts and only have a limited supply contract with Renesas, formerly Hitachi Semiconductor, for Flash IC devices. While some of our competitors have entered into long-term contracts with suppliers that guarantee them a certain allocation of Flash IC devices, our contract with Renesas provides no assurance that Renesas can or will agree to supply the quantities of Flash IC devices we may need to meet our production goals. Accordingly, we periodically review opportunities to develop alternative sources for our Flash and DRAM IC device needs. However, our options are very limited because of the small number of memory manufacturers. Our dependence on a small number of suppliers and the lack of any guaranteed sources of supply expose us to several risks, including the inability to obtain an adequate supply of components, price increases, late deliveries and poor component quality. Renesas, Matsushita and Samsung supply substantially all of the IC devices used in our Flash memory products. In addition, Micron Technology and Samsung currently supply a majority of the DRAM IC devices used in our DRAM and IC Tower stacking DRAM memory products. A disruption in or termination of our supply relationship with any of these significant suppliers due to natural disasters or other factors, or our inability to develop relationships with new suppliers, if required, would cause delays, disruptions or reductions in product shipments or require product redesigns which could damage relationships with our customers and negatively affect our revenues and could increase our costs or the prices of our products. In particular, if our supply relationships with Renesas or Samsung are disrupted or terminated, our ability to manufacture and sell our Flash products would be harmed and our Flash business would be adversely affected.

Moreover, from time to time, our industry experiences shortages in Flash and DRAM IC devices which have required some vendors to place their customers, ourselves included, on component allocation. This means that while we may have customer orders, we may not be able to obtain the materials that we need to fill those orders in a timely manner or at competitive prices. The market for Flash IC devices is currently undergoing a period of limited supply, and we cannot predict if this condition will continue or worsen and, if it does, for how long. During this period of limited supply we have had to refuse to accept some orders from our customers for some of our products. If we are unable to obtain sufficient Flash IC devices and other components to meet our customers requirements, they may reduce future orders or eliminate us as a supplier and our revenues may decline. Additionally, our reputation could be harmed, we may not be able to replace any lost business with new customers, and we may lose market share to our competitors.

Declines in our average sales prices may result in declines in our revenues and gross profit.

Our average sales prices may decline due to several factors. During the majority of 2001 and 2002, and the first four months of 2003, overcapacity in the DRAM memory component market resulted in significant declines in component prices, which negatively impacted our average sales prices, revenues and gross profit. Declines in semiconductor prices could also affect the valuation of our inventory, which could harm our financial results. During periods of overcapacity, our revenues and gross profit will decline if we do not increase unit sales of existing products or fail to introduce and sell new products in quantities sufficient to offset declines in sales prices. Our efforts to reduce costs and develop new products to offset the impact of further declines in average sales prices may not be successful. Declines in average sales prices would also enable OEMs to pre-install higher capacity base memory into new systems at existing price points, and thereby reduce the demand for our aftermarket memory products.

In addition, the continued transition to smaller design geometries and the use of 300 millimeter wafers by existing memory manufacturers could lead to a significant increase in the worldwide supply of DRAM and Flash components. Increases in the worldwide supply of DRAM and Flash components could also result from manufacturing capacity expansions. If not offset by increases in demand, these increases would likely lead to further declines in the average sales prices of our products and have a material adverse effect on our business and operating results. Furthermore, even if supply remains constant, if demand were to decrease, it would harm our average sales prices.

Table of Contents

We are subject to the cyclical nature of the semiconductor industry and any future downturn could continue to adversely affect our business.

The semiconductor industry, including the memory markets in which we compete, is highly cyclical and characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving standards, short product life cycles and wide fluctuations in product supply and demand. The industry has experienced significant downturns often connected with, or in anticipation of, maturing product cycles of both semiconductor companies and their customers products and declines in general economic conditions. These downturns have been characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average sales prices. Since 2001, a downturn in the semiconductor industry has negatively impacted our average sales prices, revenues and earnings. These negative conditions continued through the first quarter of 2003, but began to improve in the second and third quarters of 2003 as demand for Flash and DRAM products increased and component prices stabilized. However, there can be no assurance that Flash and DRAM demand or component prices will increase or remain stable or that a turnaround will occur or be sustained. Any future downturns could have a material adverse effect on our business and results of operations.

Sales to a limited number of customers represent a significant portion of our revenues, and the loss of any key customer would materially reduce our revenues.

Our dependence on a limited number of customers means that the loss of a major customer or any reduction in orders by a major customer would materially reduce our revenues. Historically, a relatively limited number of customers have accounted for a significant percentage of our revenues. Our ten largest customers accounted for an aggregate of 55.2% of our total revenues in the first half of 2003 and 55.5% of our total revenues in the full year 2002. Our ten largest Consumer Division customers accounted for an aggregate of 61.6% of our Consumer Division revenues, or 48.8% of our total revenues, in the first half of 2003 and 60.1% of our Consumer Division revenues, or 46.0% of our total revenues, in the full year 2002. Our largest Consumer Division customer in the first half of 2003 and in the full year 2002, CDW Computer Centers, accounted for 26.0% of our Consumer Division revenues, or 20.6% of our total revenues, for the first half of 2003 and 27.6% of our Consumer Division revenues, or 21.1% of our total revenues, in the full year 2002. No other Consumer Division customer accounted for more than 10.0% of our total revenues in the first half of 2003 or in the full year 2002.

Our ten largest OEM Division customers accounted for an aggregate of 67.4% of our OEM Division revenues, or 14.0% of our total revenues, in the first half of 2003 and 78.4% of our OEM Division revenues, or 18.4% of our total revenues, in the full year 2002. No single OEM Division customer accounted for more than 10.0% of our total revenues in the first half of 2003 or in the full year 2002.

Consolidation in some of our customers industries may result in increased customer concentration and the potential loss of customers as a result of acquisitions. In addition, the composition of our major customer base changes from quarter to quarter as the market demand for our customers products changes, and we expect this variability to continue in the future. We expect that sales of our products to a limited number of customers will continue to contribute materially to our revenues in the foreseeable future. The loss of, or a significant reduction in purchases by any of our major customers, could harm our business, financial condition and results of operations.

We may make acquisitions that are dilutive to existing shareholders, result in unanticipated accounting charges or otherwise adversely affect our results of operations.

We intend to grow our business through business combinations or other acquisitions of businesses, products or technologies that allow us to complement our existing product offerings, expand our market coverage, increase our engineering workforce or enhance our technological capabilities. If we make any future acquisitions, we could issue stock that would dilute our shareholders percentage ownership, incur substantial debt, reduce our

Table of Contents

cash reserves or assume contingent liabilities. In addition, we may fund all or a portion of the purchase price of a future acquisition with the proceeds from this offering.

Furthermore, acquisitions may require material infrequent charges and could result in adverse tax consequences, substantial depreciation, deferred compensation charges, in-process research and development charges, the amortization of amounts related to deferred compensation and identifiable purchased intangible assets or impairment of goodwill, any of which could negatively impact our results of operations.

Our limited experience in acquiring other businesses, product lines and technologies may make it difficult for us to overcome problems encountered in connection with any acquisitions we may undertake.

We continually evaluate and explore strategic opportunities as they arise, including business combinations, strategic partnerships, capital investments and the purchase, licensing or sale of assets. Our experience in acquiring other businesses, product lines and technologies is limited. The attention of our small management team may be diverted from our core business if we undertake any future acquisitions. Our recent and any potential future acquisitions also involve numerous risks, including, among others:

- Problems assimilating the purchased operations, technologies or products;
- Costs associated with the acquisition;
- Adverse effects on existing business relationships with suppliers and customers;
- Risks associated with entering markets in which we have no or limited prior experience;
- Potential loss of key employees of purchased organizations; and
- Potential litigation arising from the acquired company s operations before the acquisition.

We completed the acquisition of the assets of Irvine Networks, LLC, renamed our Xiran Division, in January 2002. There can be no assurance that the product development efforts completed thus far by our Xiran Division will result in future profitability of the Xiran Division. In addition, the success of the Xiran Division will depend in significant part upon the ability to develop, introduce and sell its products on a timely and cost-effective basis, and to respond to changing customer requirements.

Our inability to overcome problems encountered in connection with any acquisitions could divert the attention of management, utilize scarce corporate resources and otherwise harm our business. These challenges are magnified as the size of a potential future acquisition increases. In addition, we are unable to predict whether or when any prospective acquisition candidate will become available or the likelihood that any acquisition will be completed. Even if we do find suitable acquisition opportunities, we may not be able to consummate the acquisitions on commercially acceptable terms or realize the anticipated benefits of any acquisitions we do undertake.

Three of our beneficial shareholders have substantial influence over our operations and could control all matters requiring shareholder approval.

Manouch Moshayedi, Mike Moshayedi and Mark Moshayedi, each of whom is an executive officer and director of SimpleTech, are brothers and beneficially own approximately 78.6% of our outstanding common stock at August 31, 2003. Upon consummation of this offering, Manouch Moshayedi, Mike Moshayedi and Mark Moshayedi, together with their respective affiliates, will beneficially own approximately 54.6% of our outstanding common stock. If the underwriters over-allotment option is exercised in full, Manouch Moshayedi, Mike Moshayedi and Mark Moshayedi, together with their affiliates, will beneficially own 51.5% of our outstanding common stock. As a result, they have the ability to control all matters requiring approval by our shareholders, including the election and removal of directors, approval of significant corporate transactions and the decision of whether a change in control will occur. This control could affect the price that certain investors may be willing to pay in the future for shares of our common stock.

We are involved from time to time in claims and litigation over intellectual property rights, which may adversely affect our ability to manufacture and sell our products.

The semiconductor industry is characterized by vigorous protection and pursuit of intellectual property rights. We believe that it may be necessary, from time to time, to initiate litigation against one or more third parties to preserve our intellectual property rights. In addition, from time to time, we have received, and may continue to receive in the future, notices that claim we have infringed upon, misappropriated or misused other parties proprietary rights, and such claims could result in litigation. Such litigation, whether as plaintiff or defendant, would likely result in significant expense to us and divert the efforts of our technical and management personnel, whether or not such litigation is ultimately determined in our favor. In the event of an adverse result in such litigation, we could be required to pay substantial damages, cease the manufacture, use and sale of certain products, expend significant resources to develop non-infringing technology, discontinue the use of certain processes or obtain licenses to use the infringed technology. Such a license may not be available on commercially reasonable terms, if at all. Our failure to obtain a license on commercially reasonable terms, or at all, could cause us to incur substantial costs and suspend manufacturing products using the infringed technology. If we obtain a license, we would likely be required to pay license fees or make royalty payments for sales under the license. Such payments would increase our costs of revenues and reduce our gross margins and gross profit. If we are unable to obtain a license from a third party for technology, we could incur substantial liabilities or be required to expend substantial resources redesigning our products to eliminate the infringement. There can be no assurance that we would be successful in redesigning our products or that we could obtain licenses on commercially reasonable terms, if at all. Product development or license negotiating would likely result in significant expense to us and divert the efforts of our technical and management personnel.

We are currently a party to five lawsuits regarding intellectual property as further described under Business Legal Proceedings. Because litigation is inherently uncertain, we cannot predict the outcome of these lawsuits. These lawsuits have diverted, and are expected to continue to divert, the efforts and attention of our key management and technical personnel. In addition, we have incurred, and expect to continue to incur, substantial legal fees and expenses in connection with these lawsuits. As a result, our defense of these lawsuits, regardless of their eventual outcomes, has been, and will continue to be, costly and time consuming.

Our indemnification obligations for the infringement by our products of the intellectual property rights of others could require us to pay substantial damages.

We currently have in effect a number of agreements in which we have agreed to defend, indemnify and hold harmless our customers and suppliers from damages and costs which may arise from the infringement by our products of third-party patents, trademarks or other proprietary rights. We may periodically have to respond to claims and litigate these types of indemnification obligations. Any such indemnification claims could require us to pay substantial damages. Our insurance does not cover intellectual property infringement.

Our intellectual property may not be adequately protected, which could harm our competitive position.

Our intellectual property is critical to our success. We protect our intellectual property rights through patents, trademarks, copyrights and trade secret laws, confidentiality procedures and employee disclosure and invention assignment agreements. It is possible that our efforts to protect our intellectual property rights may not:

Prevent the challenge, invalidation or circumvention of our existing patents;

Result in patents that lead to commercially viable products or provide competitive advantages for our products;

Table of Contents

Prevent our competitors from independently developing similar products, duplicating our products or designing around the patents owned by us;

Prevent third-party patents from having an adverse effect on our ability to do business;

Provide adequate protection for our intellectual property rights;

Prevent disputes with third parties regarding ownership of our intellectual property rights;

Prevent disclosure of our trade secrets and know-how to third parties or into the public domain; and

Result in patents from any of our pending applications.

As part of our confidentiality procedures, we enter into non-disclosure and invention assignment agreements with all of our employees and attempt to control access to and distribution of our technology, documentation and other proprietary information. However, if such agreements are found to be unenforceable, we may be unable to adequately protect our intellectual property rights. In addition, despite these procedures, third parties could copy or otherwise obtain and make unauthorized use of our technologies or independently develop similar technologies.

In addition, if our IC Tower stacking patent is found to be invalid, our ability to exclude competitors from making, using or selling the same or similar products to our IC Tower stacking products would cease. We have on at least one occasion applied for and may in the future apply for patent protection in foreign countries. The laws of foreign countries, however, may not adequately protect our intellectual property rights. Many U.S. companies have encountered substantial infringement problems in foreign countries. Because we sell some of our products overseas, we have exposure to foreign intellectual property risks.

We may not be able to maintain or improve our competitive position because of the intense competition in the memory industry.

We conduct business in an industry characterized by intense competition, rapid technological change, evolving industry standards, declining average sales prices and rapid product obsolescence. Our primary competitors in the third-party memory module industry include: Crucial Memory, a division of Micron Technology, DPAC Technologies, Kingston Technology, Lexar Media, M-Systems, PNY Technologies, SanDisk, and SMART Modular, a division of Solectron. Our competitors include many large domestic and international companies that have substantially greater financial, technical, marketing, distribution and other resources, broader product lines, lower cost structures, greater brand recognition and longer-standing relationships with customers and suppliers. As a result, our competitors may be able to respond better to new or emerging technologies or standards and to changes in customer requirements. Further, some of our competitors are in a better financial and marketing position from which to influence industry acceptance of a particular industry standard or competing technology than we are. Our competitors may also be able to devote greater resources to the development, promotion and sale of products, and may be able to deliver competitive products at a lower price.

We expect to face competition from existing competitors and new and emerging companies that may enter our existing or future markets with similar or alternative products, which may be less costly or provide additional features. In addition, some of our significant suppliers, including Micron Semiconductor Electronics and Samsung Semiconductor, are also our competitors, many of whom have the ability to manufacture competitive products at lower costs as a result of their higher levels of integration. We also face competition from current and prospective customers that evaluate our capabilities against the merits of manufacturing products internally. Competition may arise due to the development of cooperative relationships among our current and potential competitors or third parties to increase the ability of their products to address the needs of our prospective customers. Accordingly, it is possible that new competitors or alliances among competitors may emerge and rapidly acquire significant market share.

Table of Contents

We expect our competitors will continue to improve the performance of their current products, reduce their prices and introduce new products that may offer greater performance and improved pricing, any of which could cause a decline in sales or loss of market acceptance of our products. In addition, our competitors may develop enhancements to, or future generations of, competitive products that may render our technology or products obsolete or uncompetitive.

We may be less competitive if we fail to develop new and enhanced products and introduce them in a timely manner.

The memory, high-performance computing, networking and communications, consumer electronics and OEM markets are subject to rapid technological change, product obsolescence, frequent new product introductions and enhancements, changes in end-user requirements and evolving industry standards. Our ability to compete in these markets will depend in significant part upon our ability to successfully develop, introduce and sell new and enhanced products on a timely and cost-effective basis, and to respond to changing customer requirements.

We have experienced, and may in the future experience, delays in the development and introduction of new products. These delays would provide a competitor a first-to-market opportunity and allow a competitor to achieve greater market share. Our product development is inherently risky because it is difficult to foresee developments in technology, anticipate the adoption of new standards, coordinate our technical personnel, and identify and eliminate design flaws. Defects or errors found in our products after commencement of commercial shipments could result in delays in market acceptance of these products. New products, even if first introduced by us, may not gain market acceptance. Accordingly, there can be no assurance that our future product development efforts, including the recent development by our Xiran Division of board-level solutions for servers designed to improve the efficiency and speed of data transport across a networking system, will result in future profitability or market acceptance. Lack of market acceptance for our new products will jeopardize our ability to recoup research and development expenditures, hurt our reputation and harm our business, financial condition and results of operations.

We may also seek to develop products with new standards for our industry. It will take time for these new standards and products to be adopted, for consumers to accept and transition to these new products and for significant sales to be generated from them, if this happens at all. Moreover, broad acceptance of new standards or products by consumers may reduce demand for our older products. If this decreased demand is not offset by increased demand for our new products, our results of operations could be harmed. We cannot assure you that any new products or standards we develop will be commercially successful.

The Flash-based storage market is constantly evolving, and we may not have rights to manufacture and sell certain types of products utilizing emerging new Flash formats, or we may be required to pay a royalty to sell products utilizing these formats.

The Flash-based storage market is constantly undergoing rapid technological change and evolving industry standards. Many consumer devices, such as digital cameras, PDAs and smartphones, may transition to emerging Flash memory formats, such the xD Picture Card format, which we do not currently manufacture and do not have rights to manufacture. This will likely result in a decline in demand, on a relative basis, for other products that we manufacture such as CompactFlash, Secure Digital, SmartMedia, Memory Stick and MultiMedia cards. If we decide to manufacture Flash products utilizing emerging formats, such as the xD Picture Card, we will be required to secure licensing arrangements to give us the right to manufacture such products which may not be available at reasonable rates or at all. If we are not able to supply all Flash card formats at competitive prices or if we were to have product shortages, our revenues could be adversely impacted and our customers would likely cancel orders or seek other suppliers to replace us.

Table of Contents

The execution of our growth strategy depends on our ability to retain key personnel, including our executive officers, and to attract qualified personnel.

Competition for employees in our industry is intense. We have had and may continue to have difficulty hiring the necessary engineering, sales and marketing and management personnel to support our growth. The successful implementation of our business model and growth strategy depends on the continued contributions of our senior management and other key research and development, sales and marketing and operations personnel, including Manouch Moshayedi, our Chief Executive Officer, Mike Moshayedi, our President, and Mark Moshayedi, our Chief Operating Officer, Chief Technical Officer and Secretary. The loss of any key employee, the failure of any key employee to perform in his or her current position, or the inability of our officers and key employees to expand, train and manage our employee base would prevent us from executing our growth strategy.

Our indemnification obligations to our customers and suppliers for product defects could require us to pay substantial damages.

A number of our product sales and product purchase agreements provide that we will defend, indemnify and hold harmless our customers and suppliers from damages and costs which may arise from product warranty claims or claims for injury or damage resulting from defects in our products. We maintain insurance to protect against certain claims associated with the use of our products, but our insurance coverage may not be adequate to cover all or any part of the claims asserted against us. A successful claim brought against us that is in excess of, or excluded from, our insurance coverage could substantially harm our business, financial condition and results of operations.

Order cancellations, product returns, inventory write-downs, price protection and rebates could adversely affect our results of operations.

To the extent we manufacture products in anticipation of future demand that does not materialize, or in the event a customer cancels outstanding orders, we could experience an unanticipated increase in our inventory. A lack of consumer demand for our products may also cause increased product returns. A majority of our sales through consumer channels include limited rights to return unsold inventory. In addition, while we may not be contractually obligated to accept returned products, we may determine that it is in our best interest to accept returns in order to maintain good relations with our customers. Product returns would increase our inventory and reduce our revenues. We have had to write-down inventory in the past for reasons such as obsolescence, excess quantities and declines in market value below our costs. These inventory write-downs were approximately $195,000, $304,000 and $759,000 in the first half of 2003, and in the full years 2002 and 2001, respectively. In addition, we offer some of our Consumer Division customers limited price protection rights for inventories of our products held by them. If we reduce the list price of our products, these customers may receive credits from us. We incurred price protection charges of approximately $680,000, $1.3 million and $1.8 million in the first half of 2003, and in the full years 2002 and 2001, respectively. We also offer rebate programs through some of our Consumer Division customers to end-users. We recorded rebate charges of $720,000, $1.1 million and $839,000 in the first half of 2003, and in the full years 2002 and 2001, respectively.

We are also subject to repurchase agreements with various financial institutions in connection with wholesale inventory financing. Under these agreements, we may be required to repurchase inventory upon customer default with a financing institution and then resell the inventory through normal distribution channels. As of June 30, 2003, we have not been required to repurchase inventory in connection with the customer default agreements noted above. However, it may be possible that we will be required to repurchase inventory, upon customer default, in the future. Sales under such agreements were approximately $510,000, $876,000 and $1.1 million in the first half of 2003, and in the full years 2002 and 2001, respectively.

We have no long-term volume commitments from our customers. Sales of our products are made through individual purchase orders and, in certain cases, are made under master agreements governing the terms and

Table of Contents

conditions of the relationships. Customers may change, cancel or delay orders with limited or no penalties. We have experienced cancellations of orders and fluctuations in order levels from period-to-period and we expect to continue to experience similar cancellations and fluctuations in the future, which could result in fluctuations in our revenues.

We face risks associated with doing business in foreign countries, including foreign currency fluctuations and trade barriers, that could lead to a decrease in demand for our products or an increase in the cost of the components used in our products.

The volatility of general economic conditions and fluctuations in currency exchange rates affect the prices of our products and the prices of the components used in our products. International sales of our products accounted for 21.4%, 14.8% and 16.0% of our revenues in the first half of 2003, and in the full years 2002 and 2001, respectively. Except for Europe, which accounted for 11.3% and 12.2%, respectively, of our revenues for the second quarter and first half of 2003, no other foreign geographic area or single foreign country accounted for more than 10.0% of our revenues in the first half of 2003, and full years 2002 or 2001. For the first half of 2003, and in the full years 2002 and 2001, more than 95.0% of our international sales were denominated in U.S. dollars. However, if there is a significant devaluation of the currency in a specific country, the prices of our products will increase relative to that country s currency and our products may be less competitive in that country. In addition, we cannot be sure that our international customers will continue to be willing to place orders denominated in U.S. dollars. If they do not, our revenues and results of operations will be subject to foreign exchange fluctuations, which could harm our business. We do not hedge against foreign currency exchange rate risks.

We purchase a majority of the IC devices used in our products from local distributors of foreign suppliers. Although our purchases of IC devices are currently denominated in U.S. dollars, devaluation of the U.S. dollar relative to the currency of a foreign supplier would likely result in an increase in our cost of IC devices.

Our international sales are subject to other risks, including regulatory risks, tariffs and other trade barriers, timing and availability of export licenses, political and economic instability, difficulties in accounts receivable collections, difficulties in managing distributors, lack of a local sales presence, difficulties in obtaining governmental approvals, compliance with a wide variety of complex foreign laws and treaties and potentially adverse tax consequences. In addition, the United States or foreign countries may implement quotas, duties, taxes or other charges or restrictions upon the importation or exportation of our products, leading to a reduction in sales and profitability in that country.

We have experienced quarterly and annual losses in the past and may continue to experience losses in the future.

Although we have been profitable for most of our history, we have experienced losses on a quarterly and annual basis in the past. For the first two quarters of 2003 and the full year 2002, we incurred net losses of $1.6 million, $864,000 and $1.3 million, respectively. We have expended, and will continue to be required to expend, substantial funds to pursue engineering, research and development projects, enhance sales and marketing efforts and otherwise operate our business. We cannot assure you that we will be profitable on a quarterly or annual basis in the future.

Disruption of our operations in our Santa Ana, California, manufacturing facility would substantially harm our business.

All of our manufacturing operations are located in our facility in Santa Ana, California. Due to this geographic concentration, a disruption of our manufacturing operations, resulting from sustained process abnormalities, human error, government intervention or natural disasters, including earthquakes, power failures, fires or floods, could cause us to cease or limit our manufacturing operations and consequently harm our business, financial condition and results of operations.

Table of Contents

Compliance with environmental laws and regulations could harm our operating results.

We are subject to a variety of environmental laws and regulations governing, among other things, air emissions, waste water discharge, waste storage, treatment and disposal, and remediation of releases of hazardous materials. Our failure to comply with present and future requirements could harm our ability to continue manufacturing our products. Such requirements could require us to acquire costly equipment or to incur other significant expenses to comply with environmental regulations. The imposition of additional or more stringent environmental requirements, the results of future testing at our facilities, or a determination that we are potentially responsible for remediation at other sites where problems are not presently known to us, could result in expenses in excess of amounts currently estimated to be required for such matters.

Failure to comply with governmental laws and regulations could harm our business.

Our business is subject to regulation by various federal and state governmental agencies. Such regulation includes the radio frequency emission regulatory activities of the Federal Communications Commission, the anti-trust regulatory activities of the Federal Trade Commission and Department of Justice, the consumer protection laws of the Federal Trade Commission, the import/export regulatory activities of the Department of Commerce, the product safety regulatory activities of the Consumer Products Safety Commission, the regulatory activities of the Occupational Safety and Health Administration, the environmental regulatory activities of the Environmental Protection Agency, the labor regulatory activities of the Equal Employment Opportunity Commission and tax and other regulations by a variety of regulatory authorities in each of the areas in which we conduct business. We are also subject to regulation in other countries where we conduct business. In certain jurisdictions, such regulatory requirements may be more stringent than in the United States. We are also subject to a variety of federal and state employment and labors laws and regulations, including the Americans with Disabilities Act, the Federal Fair Labors Standards Act, the WARN Act and other regulations related to working conditions, wage-hour pay, over-time pay, employee benefits, anti-discrimination, and termination of employment.

Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, mandatory product recalls, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties, or injunctions. In addition from time to time we have received, and expect to continue to receive, correspondence from former employees terminated by us who threaten to bring claims against us alleging that we have violated one or more labor and employment regulations. In certain of these instances the former employee has brought claims against us and we expect that we will encounter similar actions against us in the future. An adverse outcome in any such litigation could require us to pay contractual damages, compensatory damages, punitive damages, attorneys fees and costs.

These enforcement actions could harm our business, financial condition, results of operations and cash flows. If any governmental sanctions are imposed, or if we do not prevail in any possible civil or criminal litigation, our business, financial condition, results of operations and cash flows could be materially adversely affected. In addition, responding to any action will likely result in a significant diversion of management s attention and resources and an increase in professional fees.

Risks Related to this Offering

Our stock price might be volatile, and you might not be able to resell your shares at or above the price you have paid.

If you purchase shares of common stock, you might not be able to resell those shares at or above the price you have paid. The market price of our common stock might fluctuate significantly in response to many factors, some of which are beyond our control, including the following:

- actual or anticipated fluctuations in our annual and quarterly results of operations;
- changes in market valuations of other technology companies;

- changes in securities analysts expectations;
- variations in our operating results, which could cause us to fail to meet analysts or investors expectations;
- announcements by us or our competitors of significant technical innovations, contracts, acquisitions, strategic partnerships, joint ventures or capital commitments;
- conditions and trends in technology industries;
- general market, economic, industry and political conditions;
- changes in market values of comparable companies;
- additions or departures of key personnel;
- stock market price and volume fluctuations attributable to inconsistent trading volume levels; and
- future sales of equity or debt securities, including sales which dilute existing investors.

In addition, the stock market, and the stock of technology companies in particular, has experienced extreme volatility that often has been unrelated to the performance of these companies. Moreover, only a limited number of our shares are traded each day, which could increase the volatility of the price of our stock. These market fluctuations might cause our stock price to fall regardless of our performance. In the past, companies that have experienced volatility in the market price of their stock have been the objects of securities class action litigation. If we were involved in securities class action litigation, it could result in substantial costs and a diversion of management s attention and resources.

Management will have broad discretion for the use of proceeds from this offering, including the ability to apply the proceeds to uses that do not increase our operating results or market value.

The net proceeds of this offering to us will be approximately $94.5 million based on the assumed offering price of $10.05 per share, after deducting underwriters discounts and estimated offering expenses. Our management will retain broad discretion in the use of the net proceeds of this offering and could spend the net proceeds in ways that do not yield a favorable return or to which shareholders object. You will not have the opportunity, as part of your investment decision, to assess whether the net proceeds are being used appropriately. The net proceeds may be used for corporate purposes that do not increase our operating results or market value. We may use all or a portion of the proceeds to acquire complementary businesses or technologies. These acquisitions could prove to be unprofitable and harm our business. Until we need to use the proceeds of this offering, we plan to invest the net proceeds in interest-bearing investment-grade investments or bank deposits. See Use of Proceeds.

Anti-takeover provisions in our charter documents and stock option plan could prevent or delay a change in control and, as a result, negatively impact our shareholders.

We have taken a number of actions that could have the effect of discouraging a takeover attempt. For example, provisions of our amended and restated articles of incorporation and amended and restated bylaws could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our shareholders. These provisions also could limit the price that certain investors might be willing to pay in the future for shares of our common stock.

These provisions include:

- limitations on who may call special meetings of shareholders;
- advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted upon by shareholders at shareholder meetings;

Table of Contents

elimination of cumulative voting in the election of directors;

the right of a majority of directors in office to fill vacancies on the board of directors;

the ability of our board of directors to issue, without shareholder approval, blank check preferred stock to increase the number of outstanding shares and thwart a takeover attempt.

Provisions of our 2000 Stock Incentive Plan allow for the automatic vesting of all outstanding options granted under the 2000 Stock Incentive Plan upon a change in control under certain circumstances. Such provisions may have the effect of discouraging a third party from acquiring us, even if doing so would be beneficial to our shareholders. See Management Stock Plans/Employee Compensation Programs.

Purchasers in this offering will suffer immediate and substantial dilution of their investment.

The price for each share in this offering is substantially higher than the book value per share of our outstanding common stock immediately after the offering. Accordingly, if you purchase common stock in the offering, you will incur immediate dilution of approximately $6.67 in the book value of our common stock from the price you pay for our common stock, based on the offering price of $10.05 per share. For additional information on this calculation, see Dilution.

Future sales of our common stock in the public market could depress our stock price.

Our common stock began trading on the Nasdaq National Market on September 29, 2000. To date there have been a limited number of shares trading in the public market. This offering will result in additional shares being available on the open market. In addition, our current shareholders hold a substantial number of shares, which they will be able to sell in the public market in the near future. We have filed registration statements in September 2000, February 2001, April 2002 and May 2003 on Form S-8 under the Securities Act to register an aggregate of 11,615,825 shares of common stock issuable under our 2000 Stock Incentive Plan and 1,505,704 shares of common stock under our Employee Stock Purchase Plan. As of October 14, 2003, options to purchase 2,624,319 shares of common stock with a weighted-average exercise price of $3.45 per share were outstanding and currently exercisable. Moreover, in the event we are successful in acquiring additional businesses or technologies, we are likely to pay for these acquisitions, in whole or in part, with additional common stock. In connection with acquisitions we might issue or assume options to acquire our stock, and the exercise price of these options might be above or below the price of our stock. Sales of a substantial number of shares of our common stock after this offering could cause our stock price to fall. In addition, the sale of these shares could impair our ability to raise capital through the sale of additional stock. You should read Shares Eligible for Future Sale for a further discussion of shares that might be sold in the public market in the future.

Table of Contents

FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements that involve risks and uncertainties, including statements concerning conditions in the memory, high-performance computing, networking and communications, consumer electronics and OEM industries, and our business, financial condition and operating results, including in particular statements relating to our business and growth strategies, our product development efforts, and our operational and legal risks. We use words like believe, expect, anticipate, intend, future, plan and other similar expressio identify forward-looking statements. Investors should not place undue reliance on these forward-looking statements, which speak only as of the date of this prospectus. These forward-looking statements are based on our current expectations, and are subject to a number of risks and uncertainties, including those identified under Risk Factors and elsewhere in this prospectus. Our actual results could differ materially from those predicted in these forward-looking statements, and the events anticipated in the forward-looking statements may not actually occur. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We are under no duty to update any of the forward-looking statements after the date of this prospectus to conform these statements to actual results or to reflect the occurrence of unanticipated events, unless required by law.

Table of Contents

USE OF PROCEEDS

We expect to receive net proceeds of approximately $94.5 million from this offering after deducting the underwriting discount and estimated offering expenses. If the underwriters over-allotment option is exercised in full, our estimated net proceeds will be approximately $105.9 million. We will not receive any of the net proceeds from the sale of shares by the selling shareholders.

We intend to use the net proceeds for working capital and general corporate purposes, including expansion of sales and marketing activities, enhancement of our technology, improvement of our research and development, international expansion and possible acquisitions.

We have not yet determined the amount of net proceeds to be used specifically for each of the foregoing purposes. Accordingly, our management will have significant flexibility in applying the net proceeds of the offering. Pending their use as described above, we may invest the net proceeds of this offering in interest-bearing investment-grade instruments or bank deposits.

DIVIDEND POLICY

Since becoming a C corporation, in September 2000, we have not declared or paid any cash dividends on our common stock and do not expect to do so in the foreseeable future. We currently intend to retain all available funds for use in the operation and expansion of our business. Any future determination to pay dividends will be at the discretion of our board of directors and will depend principally upon our results of operations, financial conditions, capital requirements, contractual and legal restrictions and other factors the board deems relevant.

Table of Contents

MARKET PRICE FOR OUR COMMON STOCK

Our common stock has traded on the Nasdaq National Market under the symbol STEC since September 29, 2000. Prior to that time, there was no public market for our common stock. The following table sets forth the range of high and low intra-day sales prices reported on the Nasdaq National Market for our common stock for the periods indicated.

	Low	High
Year Ended December 31, 2001		
First Quarter	$ 2.50	$ 6.00
Second Quarter	$ 2.20	$ 3.49
Third Quarter	$ 1.03	$ 3.15
Fourth Quarter	$ 1.30	$ 3.60
Year Ended December 31, 2002		
First Quarter	$ 2.86	$ 8.99
Second Quarter	$ 3.20	$ 10.44
Third Quarter	$ 2.05	$ 4.28
Fourth Quarter	$ 1.80	$ 4.15
Year Ended December 31, 2003		
First Quarter	$ 1.97	$ 3.51
Second Quarter	$ 2.20	$ 4.36
Third Quarter	$ 3.50	$ 8.45
Fourth Quarter (through October 14, 2003)	$ 6.75	$ 10.05

On October 14, 2003, the last reported sale price for our common stock on the Nasdaq National Market was $10.05 per share. As of September 24, 2003, there were 52 shareholders of record of our common stock.

Table of Contents

CAPITALIZATION

The following table sets forth our capitalization as of June 30, 2003:

- on an actual basis; and

- on an as adjusted basis to reflect the sale of 10,000,000 shares of common stock offered by us in this offering (excluding the over-allotment shares) at an assumed public offering price of $10.05 per share, and the estimated net proceeds therefrom after deducting estimated underwriting discounts and commissions and estimated offering expenses.

You should read this table together with the sections of this prospectus entitled Selected Consolidated Financial Data and Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes included in this prospectus.

	As of June 30, 2003	
	Actual	As Adjusted
	(in thousands)	
Cash, cash equivalents and marketable securities	$ 44,016	$ 138,472
Total debt (including current maturities)		
Shareholders equity:		
Preferred stock, $0.001 par value, 20,000,000 shares authorized, no shares issued and outstanding		
Common stock, $0.001 par value, 100,000,000 shares authorized, 38,914,423 shares issued and outstanding, actual; and 49,244,235 shares issued and outstanding, as adjusted	39	49
Additional paid-in capital	67,051	161,497
Retained earnings	4,535	4,535
Total shareholders equity	71,625	166,081
Total capitalization	$ 71,625	166,081

The number of outstanding shares of our common stock as of June 30, 2003 excludes an aggregate of 424,876 shares of our common stock reserved for future issuance under our 2000 Stock Incentive Plan, 9,334,416 shares issuable upon exercise of stock options outstanding as of June 30, 2003, at a weighted average exercise price of $3.71 per share, and 1,261,136 shares reserved for future issuance under our Employee Stock Purchase Plan.

Table of Contents

DILUTION

Our net tangible book value as of June 30, 2003 was approximately $71.2 million, or $1.83 per share of common stock. Net tangible book value per share is calculated by subtracting our total liabilities from our total tangible assets, which equals total assets less intangible assets, and dividing this amount by the number of shares of common stock outstanding as of June 30, 2003. After giving effect to sale of 10,250,000 shares of common stock offered in this offering, which includes 250,000 shares to be issued upon the exercise of options by the selling shareholders concurrently with this offering, at an assumed offering price of $10.05 per share and the application of the estimated net proceeds from this offering, our net tangible book value as of June 30, 2003 would have been approximately $166.0 million, or $3.38 per share of common stock. Upon completion of this offering, there will be an immediate increase in the net tangible book value of approximately $1.55 per share to our existing shareholders and an immediate dilution in the net tangible book value of approximately $6.67 per share to new investors. The following table illustrates this per share dilution:

Assumed offering price per share		$ 10.05
Net tangible book value per share as of June 30, 2003	$ 1.83	
Increase value per share attributable to new investors	1.55	
Net tangible book value per share after the offering		3.38
Dilution per share to new investors		6.67

Dilution per share to new investors means the difference between the assumed public offering price per share of common stock and the net tangible book value per share as of June 30, 2003, after giving effect to the offering.

Table of Contents

SELECTED CONSOLIDATED FINANCIAL DATA

You should read the following selected consolidated financial data in conjunction with our consolidated financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations appearing elsewhere in this prospectus. The historical results presented are not necessarily indicative of future results. The consolidated statement of operations data for the years ended December 31, 2000 through 2002 and the consolidated balance sheet data at December 31, 2002 are derived from our consolidated financial statements that have been audited by PricewaterhouseCoopers LLP, independent accountants, and are included elsewhere in this prospectus. The consolidated statement of operations data for the years ended December 31, 1998 and 1999 are derived from our consolidated financial statements that have been audited and are not included in this prospectus. Statement of operations data for the six months ended June 30, 2002 and 2003, and the balance sheet data as of June 30, 2003, have been derived from our unaudited financial statements which are included elsewhere in this prospectus.

	Year Ended December 31,					Six Months Ended June 30,	
	1998	1999	2000	2001	2002	2002	2003
	(in thousands, except share and per share data)						
Consolidated Statement of Operations Data:							
Net revenues	$ 122,288	$ 192,593	$ 308,316	$ 164,241	$ 176,531	$ 94,253	$ 85,663
Cost of revenues	97,930	152,743	239,964	127,691	143,582	76,643	71,008
Gross profit	24,358	39,850	68,352	36,550	32,949	17,610	14,655
Operating expenses							
Sales and marketing	13,340	14,150	21,588	18,078	18,151	9,067	10,330
General and administrative	9,381	9,755	11,853	11,564	10,354	5,704	4,875
Research and development	2,180	1,832	3,745	4,426	8,805	3,945	4,172
Non-recurring expense			1,810		1,360(3)	1,360(3)	
Total operating expenses	24,901	25,737	38,996	34,068	38,670	20,076	19,377
Income (loss) from operations	(543)	14,113	29,356	2,482	(5,721)	(2,466)	(4,722)
Interest and other expense (income), net	1,597	2,128	1,158	(1,395)	(778)	(396)	(276)
Income (loss) before provision (benefit) for income taxes	(2,140)	11,985	28,198	3,877	(4,943)	(2,070)	(4,446)
Provision (benefit) for income taxes	23	(518)	2,838	1,537	(3,637)	(1,667)	(1,921)
Net income (loss)	$ (2,163)	$ 12,503	$ 25,360	$ 2,340	$ (1,306)	$ (403)	$ (2,525)
Pro forma data (1):							
Pro forma net income (loss)	$ (1,327)	$ 7,431	$ 17,315				

Net income (loss) per share (pro forma in years 1998-2000) (2):							
Basic	$ (0.04)	$ 0.24	$ 0.53	$ 0.06	$ (0.03)	$ (0.01)	$ (0.06)
Diluted	$ (0.04)	$ 0.23	$ 0.50	$ 0.06	$ (0.03)	$ (0.01)	$ (0.06)
Shares used in computation of net income (loss) per share (2):							
Basic	30,601,027	30,601,027	32,393,218	38,126,687	38,515,825	38,413,980	38,874,014
Diluted	30,601,027	32,657,993	34,593,678	39,435,505	38,515,825	38,413,980	38,874,014

Table of Contents

	As of December 31, 2002	As of June 30, 2003
	(in thousands)	
Consolidated Balance Sheet Data:		
Cash, cash equivalents and marketable securities	$ 43,972	$ 44,016
Working capital	60,433	57,917
Total assets	94,461	93,361
Total debt (including current maturities)		
Total shareholders equity	73,815	71,625

(1) From our formation in March 1990 to September 26, 2000, we elected for federal and state income tax purposes to be treated as an S corporation under Subchapter S of the Internal Revenue Code of 1986 and comparable state tax laws and filed our federal and state income tax returns on that basis. Accordingly, no provision has been made for federal or certain state income taxes. Pro forma net income (loss) has been computed using an effective tax rate of 38% to reflect the estimated income tax expense (benefit) as if we had been fully subject to federal and state income taxes as a C corporation for all periods presented. Subsequent to the termination of our S corporation status on September 26, 2000, we have paid federal and state corporate-level income taxes as a C corporation.

(2) Amounts reflect a 5.07 for 1 stock split of our common stock on September 8, 2000. All share and per share amounts have been adjusted to give retroactive effect to the stock split.

(3) Comprised of in-process research and development expenses related to our acquisition of the assets of Irvine Networks, LLC (currently our Xiran Division) in 2002.

Table of Contents

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this prospectus. The results described below are not necessarily indicative of the results to be expected in any future period. Certain statements in this discussion and analysis are forward-looking statements that involve risks and uncertainties, including statements concerning conditions in the memory, high-performance computing, networking and communications, consumer electronics and OEM industries, and our business, financial condition and operating results, including in particular statements relating to our business and growth strategies, our product development efforts, and our operational and legal risks. We use words like believe, expect, anticipate, intend, future, plan and other similar expressions to identify forward-looking statements. Investors should not place undue reliance on these forward-looking statements, which speak only as of the date of this prospectus. These forward-looking statements are based on our current expectations, and are subject to a number of risks and uncertainties, including those identified under Risk Factors and elsewhere in this prospectus. Our actual results could differ materially from those predicted in these forward-looking statements, and the events anticipated in the forward-looking statements may not actually occur. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We are under no duty to update any of the forward-looking statements after the date of this prospectus to conform these statements to actual results or to reflect the occurrence of unanticipated events, unless required by law.

Overview

SimpleTech, Inc. was originally incorporated in California in March 1990 as Simple Technology, Inc. Our name was then changed to SimpleTech, Inc. in May 2001. SimpleTech designs, manufactures and markets custom and open-standard memory solutions based on Flash and DRAM memory technologies. Headquartered in Santa Ana, California, SimpleTech offers a comprehensive line of over 2,500 products and specializes in developing high-density memory modules, memory cards and storage drives.

After we experienced revenue growth of 57.5% from 1998 to 1999 and 60.1% from 1999 to 2000, revenues declined 46.7% in 2001 and then increased 7.5% in 2002. Annual revenues in 2001 and 2002 were negatively impacted by deteriorating macroeconomic conditions, severe declines in the price of DRAM components and significantly reduced sales to customers in the communications and networking markets. These negative conditions continued in the first quarter of 2003 but began to improve through the second and third quarters of 2003 as demand for DRAM products increased and component prices stabilized. In addition, we believe that our better than expected results in the second quarter of 2003 and our anticipated results for the third quarter of 2003 may indicate a turnaround for our sector. However, there can be no assurance that Flash and DRAM demand or component prices will increase or remain stable or that a turnaround will occur or be sustained.

We have experienced an increase in demand for our Flash products as the result of the growth in consumer electronics and OEM applications, such as the replacement of rotating disk drives with Flash products. Our Flash revenues increased from $24.9 million for the year ended December 31, 1999 to $54.7 million for the year ended December 31, 2002, and were $35.4 million for the six-month period ended June 30, 2003.

We sell our products through our Consumer Division and OEM Division. Our Consumer Division sells our products through the following channels: value added reseller, or VAR, mail order, distributor and mass market retailer. Our OEM Division was created in late 1998 to enhance the marketing of our products to OEMs. We established our Xiran Division in 2002 as a result of our acquisition of the assets of Irvine Networks, LLC, including its intellectual property portfolio. Xiran develops advanced board-level solutions that optimize server

performance for content delivery applications, including streaming media and video on-demand, and networked storage applications, including IP storage. In September 2003, our Xiran Division received its first purchase orders from four companies which we expect will generate nominal revenues in the fourth quarter of 2003.

Gross profit as a percentage of revenues for our OEM Division is typically higher than our Consumer Division. We track revenues and gross margins for our Consumer, OEM and Xiran Divisions. We do not track separately, and do not intend to track separately, operating expenses for our Consumer and OEM Divisions. Conversely, we do track operating expenses for our Xiran Division.

Historically, a limited number of customers have accounted for a significant percentage of our revenues. Our ten largest customers accounted for an aggregate of 55.2% of our total revenues in the first half of 2003, 55.5% of our total revenues in the full year 2002 and 56.3% of our total revenues in the full year 2001. CDW Computer Centers accounted for 20.6% of our total revenues in the first half of 2003. In 2002, CDW Computer Centers accounted for 21.1% of our total revenues. In 2001, CDW Computer Centers and Unisys accounted for 19.7% and 11.0% of our total revenues, respectively. Other than CDW Computer Centers and Unisys, no other customer accounted for more than 10.0% of our total revenues in the first half of 2003, and the full years 2002 and 2001. The composition of our major customer base changes from quarter to quarter as the market demand for our products changes, and we expect this variability will continue in the future. We expect that sales of our products to a limited number of customers will continue to account for a majority of our revenues in the foreseeable future. The loss of, or a significant reduction in purchases by any of our major customers, would harm our business, financial condition and results of operations. See Risk Factors Sales to a limited number of customers represent a significant portion of our revenues, and the loss of any key customer would materially reduce our revenues. For further details on our major customers, see Business Customers.

International sales of our products constituted 21.4% of our total revenues in the first half of 2003, 14.8% of our total revenues in the full year 2002 and 16.0% of our total revenues in the full year 2001. Except for Europe, which accounted for 12.2% of our revenues in the first half of 2003, no other foreign geographical area or single foreign country accounted for more than 10.0% of our revenues in the first half of 2003, or the full years 2002 and 2001. Over 95.0% of our international sales were denominated in U.S. dollars between 2001 and the first half of 2003. In addition, our purchases of IC devices are currently denominated in U.S. dollars. However, we do face risks associated with doing business in foreign countries. See Risk Factors We face risks associated with doing business in foreign countries, including foreign currency fluctuations and trade barriers, that could lead to a decrease in demand for our products or an increase in the cost of the components used in our products.

In the past, we have been impacted by seasonal purchasing patterns resulting in lower sales in the first and second quarters of each year. Other factors, including component price fluctuations, may distort the effect of seasonality. Our ability to adjust our short-term operating expenses in response to fluctuations in revenues is limited. As a result, should revenues decrease to a level lower than expected in any given period, our results of operations would be harmed.

Revenues are recognized at the time of shipment. We face risks associated with declines in the market value of our products, product returns, inventory write-downs, price protection and rebates. See Risk Factors Order cancellations, product returns, inventory write-downs, price protection and rebates could adversely affect our results of operations.

From our formation in March 1990 through September 26, 2000, we elected for federal and state income tax purposes to be treated as an S corporation under Subchapter S of the Internal Revenue Code of 1986 and comparable state tax laws and filed our federal and state income tax returns during that period on that basis. Subsequent to our S corporation termination on September 26, 2000, we have paid federal and state corporate-level income taxes as a C corporation.

27

Table of Contents

The following table sets forth the summary statement of operations for our Consumer, OEM and Xiran Divisions for the three-year periods ended December 31, 2002:

	Year Ended December 31, 2002 (in thousands)				
	Consumer	OEM	Subtotal	Xiran	Consolidated
Net revenues	$ 134,995	$ 41,536	$ 176,531	$	$ 176,531
Cost of revenues	114,566	29,016	143,582		143,582
Gross profit	$ 20,429	$ 12,520	$ 32,949	$	$ 32,949
Gross margins	15.1%	30.1%	18.7%		18.7%
Operating expenses			$ 30,802	$ 7,868 (1)	$ 38,670
Income (loss) from operations			$ 2,147	$ (7,868)	$ (5,721)

	Year Ended December 31, 2001 (in thousands)				
	Consumer	OEM	Subtotal	Xiran	Consolidated
Net revenues	$ 116,204	$ 48,037	$ 164,241	$	$ 164,241
Cost of revenues	93,873	33,818	127,691		127,691
Gross profit	$ 22,331	$ 14,219	$ 36,550	$	$ 36,550
Gross margins	19.2%	29.6%	22.3%		22.3%
Operating expenses			$ 34,068	$	$ 34,068
Income from operations			$ 2,482	$	$ 2,482

	Year Ended December 31, 2000 (in thousands)				
	Consumer	OEM	Subtotal	Xiran	Consolidated
Net revenues	$ 164,138	$ 144,178	$ 308,316	$	$ 308,316
Cost of revenues	134,314	105,650	239,964		239,964
Gross profit	$ 29,824	$ 38,528	$ 68,352	$	$ 68,352
Gross margins	18.2%	26.7%	22.2%		22.2%
Operating expenses			$ 38,996	$	$ 38,996
Income from operations			$ 29,356	$	$ 29,356

(1) Includes $1.4 million in operating expenses related to in-process research and development expenses related to our acquisition of the assets of Irvine Networks, LLC (currently our Xiran Division) in 2002.

Recent Developments

The following are our expectations for the third quarter of 2003. However, we have not finalized our financial statements for this period. When actual results of operations are reported, it is possible that the results may vary from our expectations set forth below.

We expect our revenues to grow sequentially by 27% to 30% from $44.7 million for the second quarter of 2003 to between $57 million and $58 million for the third quarter of 2003. In addition, we expect earnings per share of $0.00 to $0.01 for the third quarter of 2003, compared to a net loss per share of $0.02 for the second quarter of 2003.

The following factors have impacted our expected results of operations for the third quarter of 2003:

- Approximately 70% quarterly growth in Flash revenue compared to the same quarter of 2002; fifth consecutive quarter of greater than 55% Flash revenue growth compared to the same period in the prior year;

- Current favorable pricing and demand environment in the Flash and DRAM markets; and

- Approximately 300% sequential increase in quarterly revenues from our IC Tower stacking products.

This information should be read together with our consolidated financial statements and the related notes included elsewhere in this prospectus. See page 37 of this prospectus for selected quarterly results of operations for the eight quarters ended June 30, 2003.

Table of Contents

Results of Operations

The following table sets forth, for the periods indicated, certain consolidated statement of operations data reflected as a percentage of revenues.

	Year Ended December 31,			Six Months Ended June 30,	
	2000	2001	2002	2002	2003
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	77.8	77.7	81.3	81.3	82.9
Gross profit	22.2	22.3	18.7	18.7	17.1
Operating expenses					
Sales and marketing	7.0	11.0	10.3	9.6	12.0
General and administrative	3.9	7.0	5.8	6.1	5.7
Research and development	1.2	2.7	5.0	4.2	4.9
Non-recurring expenses	0.6	0.0	0.8	1.4	0.0
Total operating expenses	12.7	20.7	21.9	21.3	22.6
Income (loss) from operations	9.5	1.6	(3.2)	(2.6)	(5.5)
Interest income (expense), net	(0.4)	0.8	0.4	0.4	0.3
(Loss) income before provision (benefit) for income taxes	9.1	2.4	(2.8)	(2.2)	(5.2)
Provision (benefit) for income taxes*	3.5	1.0	(2.1)	(1.8)	(2.2)
Net income (loss)*	5.6%	1.4%	(0.7)%	(0.4)%	(3.0)%

* From our formation in March 1990 to September 26, 2000, we elected for federal and state income tax purposes to be treated as an S corporation under Subchapter S of the Internal Revenue Code of 1986 and comparable state tax laws and filed our federal and state income tax returns on that basis. Accordingly, no provision has been made for federal or certain state income taxes. Pro forma net income (loss) has been computed using an effective tax rate of 38% to reflect the estimated income tax expense (benefit) as if we had been fully subject to federal and state income taxes as a C corporation for all periods presented. Subsequent to the termination of our S corporation status on September 26, 2000, we have paid federal and state corporate-level income taxes as a C corporation.

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002

Net Revenues

Our revenues were $44.7 million in the second quarter of 2003, compared to $43.3 million in the same period of 2002. Revenues increased 3.2% in the second quarter of 2003 due primarily to an 11% increase in units shipped, partially offset by a 6% decline in average sales price. The decrease in our average sales price resulted from lower DRAM and Flash component prices in the second quarter of 2003 compared to the second quarter of 2002. Unit shipments growth was comprised of unit volume increases of 57% for Flash products and 27% for IC Tower stacking products, partially offset by a decrease of 70% for non-DRAM, non-Flash products. Non-stacked DRAM memory product units shipped were relatively flat in the second quarters of 2003 compared with the same period in 2002. The mix of products sold varies from quarter to quarter and may vary in the future, affecting our overall average sales prices and revenues.

Our OEM Division revenues decreased 35.6% from $13.5 million in the second quarter of 2002 to $8.7 million in the second quarter of 2003. The decrease in OEM Division revenues was due primarily to a 27% decrease in OEM Division unit volume during this period and a 12% decrease in OEM Division average sales price in the second quarter of 2003. Our Consumer Division revenues increased 21.1% from $29.8 million

Table of Contents

in the second quarter of 2002 to $36.1 million in the second quarter of 2003. Consumer Division revenues increased in the second quarter of 2003 due primarily to a 27% increase in Consumer Division unit volume, partially offset by a 6% decline in Consumer Division average sales price. Consumer Division unit volume growth was due primarily to a significant increase in the sale of Flash memory products in the retail and mail order channels. The decrease in average sales price resulted primarily from lower DRAM and Flash component prices in the second quarter of 2003 compared to the second quarter of 2002.

Sales of our products are made under short-term cancelable purchase orders. We include in our backlog only those customer orders for which we have accepted purchase orders and to which we have assigned shipment dates within the upcoming six months. Since orders constituting our backlog are subject to change due to, among other things, customer cancellations and reschedulings, and our ability to procure necessary components, backlog is not necessarily an indication of future revenues. In addition, there can be no assurance that current backlog will necessarily lead to revenues in any future period. Our combined backlog was $5.5 million as of June 30, 2003, compared to $4.9 million as of June 30, 2002. Our OEM Division backlog was $2.7 million as of June 30, 2003, compared to $3.8 million as of June 30, 2002. Our Consumer Division backlog was $2.8 million as of June 30, 2003, compared to $1.1 million as of June 30, 2002. Consumer Division backlog is typically nominal since substantially all consumer orders are filled on a same-day or next-day basis. Our ability to predict future sales is limited because a majority of our quarterly product revenues come from orders that are received and fulfilled in the same quarter. We believe that our stronger than expected results in the second quarter of 2003, recent increases in DRAM and Flash demand along with the stabilization and increase of component prices towards the end of the second quarter of 2003 may indicate a turnaround for our sector. However, there can be no assurance that Flash and DRAM demand or component prices will increase or remain stable or that a turnaround will occur or be sustained.

Gross Profit

Our gross profit was $7.7 million in the second quarter of 2003, compared to $6.1 million in the same period of 2002. Gross profit as a percentage of revenues was 17.2% in the second quarter of 2003, compared to 14.2% in the same period of 2002. Gross profit for our OEM Division as a percentage of OEM Division revenues was 20.9% in the second quarter of 2003, compared to 28.9% in the second quarter of 2002. This decrease in gross profit as a percentage of revenues for our OEM Division resulted primarily from a 27% decrease in unit shipments resulting in a lower absorption of production labor and overhead costs. Gross profit for our Consumer Division as a percentage of Consumer Division revenues was 16.4% in the second quarter of 2003, compared to 7.5% in the second quarter of 2002. The gross profit for our Consumer Division as a percentage of Consumer Division revenues for the second quarter of 2002 was negatively affected by the impact of significant DRAM component price declines on our average sales price.

Operating Expenses

Sales and Marketing. Sales and marketing expenses are primarily comprised of personnel costs and travel expenses for our domestic and international sales and marketing employees, commissions paid to internal salespersons and independent manufacturers representatives, shipping costs and marketing programs. Sales and marketing expenses were $5.0 million in the second quarter of 2003, compared to $4.2 million in the same period of 2002. Sales and marketing expenses as a percentage of revenues were 11.2% in the second quarter of 2003, compared to 9.7% in the same period of 2002. Sales and marketing expenses increased due primarily to increased sales and marketing efforts for the Xiran Division and expanded Consumer Division marketing programs in the second quarter of 2003.

General and Administrative. General and administrative expenses are comprised primarily of personnel costs for our executive and administrative employees, professional fees and facilities overhead. General and administrative expenses were $2.4 million in the second quarter of 2003, compared to $2.7 million in the same period of 2002. General and administrative expenses as a percentage of revenues were 5.4% in the second quarter

30

Table of Contents

of 2003 and 6.2% in the second quarter of 2002. General and administrative expenses decreased due primarily to a $265,000 reduction in legal fees in the second quarter of 2003.

Research and Development. Research and development expenses are comprised primarily of personnel costs for our engineering and design staff and the cost of prototype supplies. Research and development expenses were $2.1 million in the second quarter of 2003, compared to $2.0 million in the same period 2002. Research and development expenses as a percentage of revenues were 4.7% in the second quarter of 2003, compared to 4.6% in the same period of 2002. Research and development expenses were relatively flat in the second quarter of 2003 compared to the same period in 2002.

Interest Income, Net

Interest income, net is comprised of interest earned on our cash, cash equivalents and marketable securities, less interest expense. Interest income, net was $125,000 in the second quarter of 2003, compared to $187,000 in the second quarter of 2002. Interest income was $125,000 in the second quarter of 2003, compared to $211,000 in the second quarter of 2002. This decrease in interest income resulted from lower interest rates and a reduced average cash balance in the second quarter of 2003, compared to the second quarter of 2002. Interest expense is comprised of interest related to equipment financing. There was no interest expense in the second quarter of 2003, compared to $24,000 in the second quarter of 2002.

Benefit for Income Taxes

Benefit for income taxes was $661,000 in the second quarter of 2003, compared to $1.9 million in the second quarter of 2002. As a percentage of income before benefit for income taxes, benefit for income taxes was 43.3% and 72.3% in the second quarter of 2003 and 2002, respectively. The percentage of income before benefit for income taxes for the second quarter of 2002 was abnormally high due to a non-recurring research and development income tax benefit of approximately $800,000. We expect that the quarterly research and development income tax credits to be approximately $75,000 to $100,000 for the foreseeable future.

Net Loss

Net loss was $864,000 and $716,000 in the second quarters of 2003 and 2002, respectively.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002

Net Revenues

Our revenues were $85.7 million in the first half of 2003, compared to $94.3 million in the same period of 2002. Revenues decreased 9.1% in the first half of 2003 due primarily to a 15% decline in average sales price, partially offset by a 5% increase in units shipped. The decrease in our average sales price resulted from lower DRAM and Flash component prices in the first half of 2003, compared to the first half of 2002. Unit shipments growth was comprised of unit volume increases of 51.0% for IC Tower stacking products and 44% for Flash products, partially offset by decreases of 74% for non-DRAM, non-Flash products and 5% for non-stacked DRAM memory products.

Our OEM Division revenues decreased 14.4% from $20.8 million in the first half of 2002 to $17.8 million in the first half of 2003. The decrease in OEM Division revenue was due primarily to a 5% decrease in OEM Division unit volume during this period and a 10% decrease in OEM Division average sales price in the first half of 2003. Our Consumer Division revenues decreased 7.6% from $73.4 million in the first half of 2002 to $67.8 million in the first half of 2003. Consumer Division revenues decreased in the first half of 2003 due to a 15% decline in Consumer Division average sales price, partially offset by a 9% increase in Consumer Division unit volume. Consumer Division unit volume growth was due primarily to a significant increase in the sale of

Table of Contents

Flash memory products in the retail and mail order channels. The decrease in average sales price resulted primarily from lower DRAM and Flash component prices in the first half of 2003, compared to the first half of 2002.

Gross Profit

Our gross profit was $14.7 million in the first half of 2003, compared to $17.6 million in the same period of 2002. Gross profit as a percentage of revenues was 17.2% in the first half of 2003, compared to 18.7% in the same period of 2002. Gross profit for our OEM Division as a percentage of OEM Division revenues was 24.7% in the first half of 2003, compared to 29.5% in the first half of 2002. This decrease in gross profit as a percentage of revenues for our OEM Division resulted primarily from a 5% decrease in unit shipments resulting in a higher absorption of production labor and overhead costs and a negative shift in product mix. Gross profit for our Consumer Division as a percentage of Consumer Division revenues was 15.1% in the first half of 2003, compared to 15.6% in the first half of 2002.

Operating Expenses

Sales and Marketing. Sales and marketing expenses were $10.3 million in the first half of 2003, compared to $9.1 million in the same period of 2002. Sales and marketing expenses as a percentage of revenues were 12.0% in the first half of 2003, compared to 9.7% in the same period of 2002. Sales and marketing expenses increased due primarily to increased sales and marketing efforts for the Xiran Division and expanded Consumer Division marketing programs in the first half of 2003.

General and Administrative. General and administrative expenses were $4.9 million in the first half of 2003, compared to $5.7 million in the same period of 2002. General and administrative expenses as a percentage of revenues were 5.7% in the first half of 2003 and 6.0% in the first half of 2002. General and administrative expenses decreased due primarily to a $450,000 reduction in legal fees in the first half of 2003.

Research and Development. Research and development expenses were $4.2 million in the first half of 2003, compared to $3.9 million in the same period of 2002. Research and development expenses as a percentage of revenues were 4.9% in the first half of 2003, compared to 4.1% in the same period of 2002. The increase in research and development expenses in the first half of 2003 resulted from a $505,000 increase in expenditures related to our Xiran Division, partially offset by a $212,000 decrease in expenditures related to our Consumer and OEM Divisions.

Non-recurring In-process Research and Development. We did not have non-recurring in-process research and development expenses in the first half of 2003. Non-recurring in-process research and development expenses were $1.4 million in the first half of 2002 and related to our acquisition of the assets of Irvine Networks, LLC (Xiran Division) in January 2002.

Interest Income, Net

Interest income, net was $276,000 in the first half of 2003 compared to $396,000 in the first half of 2002. Interest income was $276,000 in the first half of 2003 compared to $449,000 in the first half of 2002. This decrease in interest income resulted from lower interest rates and a reduced average cash balance in the first half of 2003 compared to the first half of 2002. Interest expense is comprised of interest related to equipment financing. There was no interest expense in the first half of 2003. Interest expense was $53,000 in the first half of 2002.

Benefit for Income Taxes

Benefit for income taxes was $1.9 million in the first half of 2003, compared to $1.7 million in the first half of 2002. As a percentage of loss before benefit for income taxes, benefit for income taxes was 43.2% and 80.5%

Table of Contents

in the first halves of 2003 and 2002, respectively. The percentage of loss before benefit for income taxes for the first half of 2002 was abnormally high due to a non-recurring research and development income tax benefit of approximately $800,000. We expect quarterly research and development income tax credits to be approximately $75,000 to $100,000 for the foreseeable future.

Net Loss

Net loss was $2.5 million and $403,000 in the first halves of 2003 and 2002, respectively.

Year Ended December 31, 2002 Compared to Year Ended December 31, 2001

Net Revenues

Our revenues increased 7.5% from $164.2 million in 2001 to $176.5 million in 2002. The increase in revenues from 2001 to 2002 was due primarily to a 24.1% increase in units shipped from 2.9 million units in 2001 to 3.6 million units in 2002, partially offset by a 12.3% decline in our average sales price from 2001 to 2002. The increase in unit volume resulted from unit volume increases of 93.2% for Flash products, 81.6% for IC Tower stacking products and 81.8% for non-DRAM, non-Flash products partially offset by a unit volume decrease of 12.1% for DRAM memory products. The increase in Flash product units shipped resulted primarily from an increase in sales of Flash products to consumers for applications such as digital camera, MP3 players and PDAs through mail order and mass market retailers. The decrease in DRAM memory units shipped resulted primarily from continued weakness in the PC market. The decrease in our average sales prices resulted primarily from a steady decline of Flash component prices during 2002, partially offset by a marginal increase in overall DRAM component prices in 2002.

Our OEM Division revenues decreased 13.5% from $48.0 million in 2001 to $41.5 million in 2002. Our OEM Division revenues were negatively impacted in 2002 due to reduced sales to customers in the networking and communications markets. Consumer Division revenues increased 16.2% from $116.2 million in 2001 to $135.0 million in 2002 due primarily to a 50.4% increase in Flash products.

Our combined backlog was $5.8 million as of December 31, 2002, compared to $4.5 million as of December 31, 2001. Our OEM Division backlog was $4.3 million as of December 31, 2002, compared to $3.8 million as of December 31, 2001. Our Consumer Division backlog increased from $721,000 as of December 31, 2001, to $1.5 million as of December 31, 2002, as a result of increased Consumer Division orders booked in the fourth quarter of 2002 compared to the fourth quarter of 2001.

Gross Profit

Our gross profit decreased 10.1% from $36.6 million in 2001 to $32.9 million in 2002. Gross profit as a percentage of revenues decreased from 22.3% in 2001 to 18.7% in 2002. Gross profit as a percentage of revenues decreased from 2001 to 2002 due primarily to sharp declines in DRAM pricing during the second quarter of 2002, which resulted in a 14.2% gross profit as a percentage of revenue in that quarter. We believe the sharp decline in DRAM pricing during the second quarter of 2002 resulted from failed consolidation discussions between Micron Technology and Hynix, two of the largest DRAM manufacturers in the industry. Gross profit as a percentage of revenues was relatively flat for our OEM Division at 30.1% in 2002 compared to 29.6% in 2001. Gross profit as a percentage of revenues for our Consumer Division decreased to 15.1% in 2002 from 19.2% in 2001 due primarily to the impact of DRAM price declines for the second quarter of 2002 on DRAM inventory held in stock.

Operating Expenses

Sales and Marketing. Sales and marketing expenses are comprised primarily of personnel costs and travel expenses for our domestic and international sales and marketing employees, commissions paid to internal

Table of Contents

salespersons and independent manufacturers representatives, shipping costs and marketing programs. Sales and marketing expenses remained flat at $18.2 million in 2002 compared to $18.1 million in 2001. Sales and marketing expenses as a percentage of revenues remained relatively flat at 10.3% in 2002 compared to 11.0% in 2001.

General and Administrative. General and administrative expenses are comprised primarily of personnel costs for our executive and administrative employees, professional fees and facilities overhead. General and administrative expenses decreased 10.3% from $11.6 million in 2001 to $10.4 million in 2002. The decline in general and administrative expenses was due primarily to reductions in legal expense of approximately $600,000, bad debt expense of approximately $400,000 and payroll expense of approximately $100,000 in 2002. General and administrative expenses as a percentage of revenues decreased from 7.1% in 2001 to 5.9% in 2002 due primarily to reduced legal, bad debt and payroll expenses and increased revenues.

Research and Development. Research and development expenses are comprised primarily of personnel costs for our engineering and design staff and the cost of prototype supplies. Research and development expenses increased 100.0% from $4.4 million in 2001 to $8.8 million in 2002. Research and development expenses as a percentage of revenues increased from 2.7% in 2001 to 5.0% in 2002. Research and development expenses increased from 2001 to 2002 due to a significant expansion of our research and development staff to serve our growing OEM Division customer base and to develop new product lines. In January 2002, we completed a $2.3 million acquisition of the assets, including intellectual property, of Irvine Networks, LLC, and hired their engineering staff. Operating costs for the Xiran Division were approximately $6.5 million in 2002, excluding a $1.4 million non-recurring in-process research and development charge related to the acquisition.

Non-Recurring Expenses. We did not have non-recurring expenses in 2001. Non-recurring expenses were $1.4 million in 2002 and were comprised of in-process research and development expenses related to the acquisition of Irvine Networks in January 2002.

Interest (Income) Expense, Net

Interest (income) expense, net is comprised primarily of interest income from our cash and cash equivalents and interest expense related to our line of credit and equipment financing. Interest (income) expense, net was ($778,000) in 2002, compared to ($1.4) million in 2001. Interest income was $855,000 in 2002 and $1.6 million in 2001. Interest income decreased from 2001 to 2002 due primarily to lower interest rates. Interest expense was $77,000 in 2002 and $200,000 in 2001. Interest expense decreased from 2001 to 2002 due to the maturation and pay down of a portion of our equipment loans and capital leases.

(Benefit) provision for income taxes

(Benefit) provision for income taxes was ($3.6) million in 2002 and $1.5 million in 2001. (Benefit) provision for income taxes as a percentage of (loss) income before (benefit) provision for income taxes was 39.6% in 2001 compared to 73.6% in 2002. The increase in the effective rate in 2002 resulted from the application of state net operating loss carryforwards, prior year research and development and state enterprise zone hiring credits of approximately $927,000 taken in 2002 and current year research and development and state enterprise zone hiring credits of approximately $934,000.

Net (Loss) Income

Net (loss) income was ($1.3) million in 2002 and $2.3 million in 2001.

Table of Contents

Year Ended December 31, 2001 Compared to Year Ended December 31, 2000

Net Revenues

Our revenues decreased 46.7% from $308.3 million in 2000 to $164.2 million in 2001. The decrease in revenues from 2000 to 2001 was due primarily to a 54.4% decrease in our average sales price from 2000 to 2001, offset partially by a 16.0% increase in units shipped from 2.5 million units in 2000 to 2.9 million units in 2001. The decrease in our average sales price resulted from significant declines in DRAM and Flash component prices from October 2000 through November 2001. The increase in unit volume resulted from unit volume increases of 37.7% for standard memory products and 29.7% for Flash products, partially offset by unit volume decreases of 68.4% for IC Tower stacking products and 41.2% for non-DRAM, non-Flash products. Increases in Flash and standard memory units shipped resulted primarily from market share gains achieved during 2001 in the mass market retailer channel. Decreases in IC Tower stacking units shipped resulted from excess OEM Division customer inventory levels throughout 2001.

Our OEM Division revenues decreased 66.7% from $144.2 million in 2000 to $48.0 million in 2001. Our Consumer Division revenues decreased 29.2% from $164.1 million in 2000 to $116.2 million in 2001. Both our OEM and Consumer Division revenues were negatively impacted in 2001 by deteriorating macro economic conditions and severe declines in the price of DRAM and Flash components, which resulted in significantly lower average sales prices. Our OEM Division revenues were further impacted by a build-up of inventory by our communications and networking customers during 2000.

Our combined backlog was $4.5 million as of December 31, 2001 compared to $22.4 million as of December 31, 2000. Our OEM Division backlog was $3.8 million as of December 31, 2001 compared to $21.4 million as of December 31, 2000. Our Consumer Division backlog was $721,000 as of December 31, 2001 compared to $1.0 million as of December 31, 2000. From 2000 to 2001, the decrease in OEM Division backlog resulted from a build-up of inventory by our OEM Division customers, which led to a significant reduction of orders.

Gross Profit

Our gross profit decreased 46.5% from $68.4 million in 2000 to $36.6 million in 2001. Gross profit as a percentage of revenues remained flat at 22.3% in 2001 compared to 22.2% in 2000. Gross profit as a percentage of revenues for our OEM Division increased to 29.6% in 2001 from 26.7% in 2000. Gross profit as a percentage of revenues for our Consumer Division increased to 19.2% in 2001 from 18.2% in 2000 due primarily to a positive shift in customer mix.

Operating Expenses

Sales and Marketing. Sales and marketing expenses decreased 16.2% from $21.6 million in 2000 to $18.1 million in 2001 due primarily to reduced commissions and channel marketing expenses related to lower revenues. Sales and marketing expenses as a percentage of revenues increased from 7.0% in 2000 to 11.0% in 2001 due primarily to reduced revenues.

General and Administrative. General and administrative expenses remained relatively flat at $11.6 million in 2001 compared to $11.9 million in 2000. General and administrative expenses as a percentage of revenues increased from 3.9% in 2000 to 7.0% in 2001 due primarily to reduced revenues.

Research and Development. Research and development expenses increased 18.9% from $3.7 million in 2000 to $4.4 million in 2001. Research and development expenses as a percentage of revenues increased from 1.2% in 2000 to 2.7% in 2001. Research and development expenses increased year-over-year from 2000 to 2001 due to a significant expansion of our research and development staff to serve our growing OEM Division customer base and to develop new product lines.

Table of Contents

Non-Recurring Expenses. We did not have non-recurring expenses in 2001. Non-recurring expenses were $1.8 million in 2000 and were comprised of expenses related to a litigation settlement with Interactive Flight Technologies, Inc. The settlement payment was made in January 2001.

Interest (Income) Expense, Net

Interest (income) expense, net is comprised primarily of interest income from our cash and cash equivalents and interest expense related to our line of credit and equipment financing. Interest income, net was $1.4 million in 2001 compared to interest expense, net of $1.2 million in 2000. Interest income was $1.6 million in 2001 and $406,000 in 2000. Interest income increased in 2001 compared to 2000 due to a higher average cash balance resulting primarily from initial public offering proceeds received in October 2000 and positive cash flow from operations in each quarter from the fourth quarter of 2000 through the fourth quarter of 2001. Interest expense was $200,000 in 2001 and $1.6 million in 2000. Interest expense decreased significantly from 2000 to 2001 due primarily to the reduction of our line of credit balance to zero in October 2000.

Provision for Income Taxes

Provision for income taxes was $1.5 million in 2001. Pro forma provision from income taxes was $10.9 million in 2000. Provision for income taxes as a percentage of income before provision for income taxes was 39.6% in 2001. Pro forma provision for income taxes as a percentage of income before provision for income taxes was 38.6% in 2000. From our formation in March 1990 to September 26, 2000, we elected for federal and state income tax purposes to be treated as an S corporation under Subchapter S of the Internal Revenue Code of 1986 and comparable state tax laws and filed our federal and state income tax returns on that basis. Accordingly, no provision has been made for federal or certain state income taxes. Pro forma net income (loss) has been computed using an effective tax rate of 38% to reflect the estimated income tax expense (benefit) as if we had been fully subject to federal and state income taxes as a C corporation.

Net Income

Net income was $2.3 million in 2001. Assuming the termination of our S corporation status, pro forma net income would have been $17.3 million in 2000.

Table of Contents

Selected Quarterly Results

The following table sets forth our unaudited quarterly consolidated statement of operations data for each of the eight quarters ended June 30, 2003. In the opinion of management, these data have been prepared on a basis substantially consistent with our audited consolidated financial statements appearing elsewhere in this prospectus, and reflect and include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the data. The quarterly data should be read together with our consolidated financial statements and related notes appearing elsewhere in this prospectus. The operating results for any one quarter are not necessarily indicative of the results to be expected for any future period.

	Three Months Ended							
	Sept. 30, 2001	Dec. 31, 2001	Mar. 31, 2002	June 30, 2002	Sept. 30, 2002	Dec. 31, 2002	Mar. 31, 2003	June 30, 2003
	(In thousands, except for per share data)							
Results of Operations								
Net revenues	$ 33,177	$ 35,581	$ 50,952	$ 43,301	$ 36,501	$ 45,777	$ 40,918	$ 44,745
Cost of revenues	27,526	25,763	39,476	37,167	29,911	37,028	33,987	37,021
Gross profit	5,651	9,818	11,476	6,134	6,590	8,749	6,931	7,724
Operating expenses								
Sales and marketing	4,057	4,116	4,837	4,230	4,065	5,019	5,372	4,958
General and administrative	2,354	2,857	3,031	2,673	2,316	2,334	2,514	2,361
Research and development	984	1,179	1,938	2,007	2,503	2,357	2,117	2,055
Non-recurring expenses			1,360					
Total operating expenses	7,395	8,152	11,166	8,910	8,884	9,710	10,003	9,374
Income (loss) from operations	(1,744)	1,666	310	(2,776)	(2,294)	(961)	(3,072)	(1,650)
Interest income, net	346	252	209	187	198	184	151	125
Income (loss) before (benefit) provision for income taxes	(1,398)	1,918	519	(2,589)	(2,096)	(777)	(2,921)	(1,525)
Provision (benefit) for income taxes	(555)	760	206	(1,873)	(1,040)	(930)	(1,260)	(661)
Net income (loss)	$ (843)	$ 1,158	$ 313	$ (716)	$ (1,056)	$ 153	$ (1,661)	$ (864)
Net income (loss) per share:								
Basic	$ (0.02)	$ 0.03	$ 0.01	$ (0.02)	$ (0.03)	$ 0.00	$ (0.04)	$ (0.02)
Diluted	$ (0.02)	$ 0.03	$ 0.01	$ (0.02)	$ (0.03)	$ 0.00	$ (0.04)	$ (0.02)

	Three Months Ended							
	Sept. 30, 2001	Dec. 31, 2001	Mar. 31, 2002	June 30, 2002	Sept. 30, 2002	Dec. 31, 2002	Mar. 31, 2003	June 30, 2003
	(As a percentage of revenues)							
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	83.0	72.4	77.5	85.8	81.9	80.9	83.1	82.7

Gross profit	17.0	27.6	22.5	14.2	18.1	19.1	16.9	17.3
Operating expenses								
Sales and marketing	12.2	11.6	9.5	9.8	11.1	11.0	13.1	11.1
General and administrative	7.1	8.0	5.9	6.2	6.3	5.1	6.1	5.3
Research and development	3.0	3.3	3.8	4.6	6.9	5.1	5.2	4.6
Non-recurring expense			2.7					
Total operating expenses	22.3	22.9	21.9	20.6	24.3	21.2	24.4	20.9
Income (loss) from operations	(5.3)	4.7	0.6	(6.4)	(6.3)	(2.1)	(7.5)	(3.7)
Interest income, net	1.0	0.7	0.4	0.4	0.5	0.4	0.4	0.3
Income (loss) before (benefit) provision for income taxes	(4.2)	5.4	1.0	(6.0)	(5.7)	(1.7)	(7.1)	(3.4)
Provision (benefit) for income taxes	(1.7)	2.1	0.4	(4.3)	(2.8)	(2.0)	(3.1)	(1.5)
Net income (loss)	(2.5)%	3.3%	0.6%	(1.7)%	(2.9)%	0.3%	(4.1)%	(1.9)%

From December 2001 to early May 2002, DRAM component prices increased significantly which had a positive impact on our revenue and gross margin percentage in the fourth quarter of 2001 and the first quarter of 2002. In May 2002, DRAM component prices declined materially over a two-week period and negatively impacted our revenue and gross margin percentage in the second quarter of 2002. Our sequential revenue growth

Table of Contents

during the second quarter of 2003 was driven by a 39% sequential increase Flash unit shipments during the quarter.

In January 2002, we completed a $2.3 million acquisition of the assets, including intellectual property, of Irvine Networks, LLC, and hired their engineering staff. Staffing and other expenditures related to Irvine Networks, which was renamed our Xiran Division, resulted in incremental research and development expenditures of approximately $800,000 beginning in the first quarter of 2002. In addition, a $1.4 million non-recurring charge was recognized in the first quarter of 2002 in conjunction with the acquisition. The non-recurring change was related to the write-off of in-process research and development costs associated with the acquisition.

In the foreseeable future, we expect our sales and marketing expenses to increase or decrease at a rate less than any corresponding increase or decrease in net revenues. In the foreseeable future, we also expect our general and administrative and research and development expenses to remain relatively flat regardless of any increase or decrease in net revenues.

Liquidity and Capital Resources

As of June 30, 2003, we had working capital of $57.9 million, including $34.0 million of cash and cash equivalents and $10.0 million of marketable securities. As of December 31, 2002, we had working capital of $60.4 million, including $34.0 million of cash and cash equivalents and $10.0 million in marketable securities, compared to working capital of $64.5 million, including $51.8 million of cash and cash equivalents, as of December 31, 2001 and $64.3 million working capital, including $33.7 million of cash and cash equivalents, as of December 31, 2000. Our cash and cash equivalents balance decreased over the 2002 period due primarily to an investment in marketable securities of $10.0 million and purchases of furniture, fixtures and equipment of $5.4 million. We had no outstanding principal balance under our $27.5 million line of credit with Comerica Bank at December 31, 2001 and 2000 and the line of credit expired in August 2002 and was not renewed. Current assets were 3.7 times current liabilities at June 30, 2003, compared to 3.9 times current liabilities at the end of 2002, 5.3 times current liabilities at the end of 2001 and 3.0 times current liabilities at the end of 2000. Assuming an offering price of $10.05, we expect to receive approximately $94.5 million in net proceeds ($105.9 million if the over-allotment option is exercised in full) from the sale of our common stock in this offering.

Net cash provided by operating activities was $609,000 for the first half of 2003 and resulted primarily from a $2.4 million decrease in accounts receivables, net of allowances, $2.1 million in non-cash depreciation and amortization, a $2.0 million increase in accounts payable and a $1.1 million decrease in income taxes receivable, partially offset by a net loss of $2.5 million, a $1.7 million increase in deferred income taxes, a $1.3 million decrease in inventory, a $1.1 million decrease in accrued and other liabilities and a $450,000 increase in other assets. Net cash used by operating activities was $217,000 in 2002 and resulted primarily from an increase in net accounts receivable of $6.4 million and an increase in net inventory of $4.3 million, partially offset by an increase in accounts payable of $6.1 million and non-cash depreciation of $3.6 million. Net inventory, net accounts receivable and accounts payable growth resulted from a 28.7% increase in revenues in the fourth quarter of 2002 compared to the fourth quarter of 2001. Net cash provided by operating activities was $24.2 million in 2001. Net cash provided by operating activities in 2001 resulted primarily from net income of $2.3 million, a decrease in net accounts receivable of $15.5 million and a decrease in net inventory of $21.2 million, partially offset by a decrease in accounts payable of $15.6 million. Inventory and accounts payable decreased due primarily to the implementation of consignment inventory programs with our three largest component suppliers during 2001 and a sharp decline in DRAM and Flash pricing during the year. Accounts receivable decreased due to the decline in overall revenues. Net cash provided by operating activities was $18.1 million in 2000 and resulted primarily from net income of $25.4 million, increases in accounts payable and accrued and other liabilities of $8.1 million, and depreciation and amortization of $3.4 million, partially offset by increases in net inventory of $12.8 million, net accounts receivable of $4.4 million and deferred income taxes of $1.6 million.

Table of Contents

Inventory increased to support increased OEM Division customer orders and lengthened time between our receipt of such orders and their required ship date. Accounts receivable increased due to increased overall revenues.

Net cash used in investing activities was $719,000 for the first half of 2003, $16.9 million in 2002, $5.4 million in 2001 and $2.4 million in 2000. Net cash used in investing activities for the first half of 2003 was attributable primarily to $823,000 in purchase of furniture, fixtures and equipment, partially offset by $104,000 in proceeds from the sale of furniture, fixtures and equipment. In 2002, net cash used in investing activities resulted primarily from an investment in marketable securities of $10.0 million, purchases of furniture, fixtures and equipment of $5.4 million and an acquisition of assets for $2.3 million. In 2001, net cash used in investing activities was attributable primarily to purchases of furniture, fixtures and equipment. In 2000, net cash used in investing activities was attributable primarily to purchases of furniture, fixtures and equipment. We expect to spend between $3.0 million to $5.0 million during the next 24 months, primarily for manufacturing, testing and engineering equipment.

Net cash provided by financing activities was $154,000 for the first half of 2003 and resulted from the receipt of $267,000 in proceeds from the issuance of common stock related to stock option exercises and purchases of stock by employees through the employee stock purchase plan, partially offset by payments of $113,000 related to equipment capital lease obligations. Net cash used in financing activities totaled $681,000 in 2002 and $674,000 in 2001. Net cash used in financing activities in 2002 resulted from the repayment of borrowings from banks and capital lease obligations of $1.5 million, partially offset by the issuance of common stock for proceeds of $772,000 related to our employee stock purchase plan and stock option exercises. Net cash used in financing activities in 2001 resulted primarily from the repayment of borrowings from banks and capital lease obligations of $1.6 million, partially offset by the issuance of common stock for proceeds of $1.1 million related to our employee stock purchase plan and stock option exercises. In 2001, we also repurchased a total of 72,500 shares of our common stock under our authorized stock repurchase program at an average price of approximately $1.25 per share, resulting in a total cash payment of approximately $92,000. Net cash provided by financing activities totaled $14.3 million in 2000 and resulted primarily from the receipt of $65.1 million in connection with our initial public offering in September 2000, partially offset by distributions of $35.0 million to S Corporation shareholders and line of credit repayments of $12.5 million.

In prior years, we entered into several capital leases and loans to finance manufacturing and testing equipment. Our obligations under capital leases were paid down to zero as of June 30, 2003 and had a balance of $113,000 at December 31, 2002, $554,000 at December 31, 2001 and $1.4 million at December 31, 2000, with interest rates ranging from 8.1% to 9.6% per annum. Our equipment financing loan balances were paid down to zero at December 31, 2002 and had a balance of $1.0 million on December 31, 2001 and $1.8 million on December 31, 2000, with interest rates ranging from 7.5% to 9.1% per annum.

Prior to our conversion from an S corporation to a C corporation in September 2000, we made cash distributions of a portion of our S Corporation earnings to our shareholders of record as of September 20, 2000, for reasons including payment of their overall personal income taxes. On September 26, 2000, we distributed to our shareholders of record as of September 20, 2000, in proportion to their ownership of our shares, notes in an aggregate principal amount of $25.1 million, equal to our undistributed earnings from the date of our formation through September 26, 2000. We used a portion of the net proceeds from our initial public offering to payoff the principal amount of these undistributed earnings notes on October 6, 2000 and November 3, 2000.

We believe that the net proceeds from this offering, our existing assets, cash, cash equivalents and investments on hand, together with cash that we expect to generate from our operations, will be sufficient to meet our capital needs for at least the next twelve months. However, it is possible that we may need or elect to raise additional funds to fund our activities beyond the next year or to consummate acquisitions of other businesses, products or technologies. We could raise such funds by selling more stock to the public or to selected investors, or by borrowing money. In addition, even though we may not need additional funds, we may still elect to sell

39

Table of Contents

additional equity securities or obtain credit facilities for other reasons. We cannot assure you that we will be able to obtain additional funds on commercially favorable terms, or at all. If we raise additional funds by issuing additional equity or convertible debt securities, the ownership percentages of existing shareholders would be reduced. In addition, the equity or debt securities that we issue may have rights, preferences or privileges senior to those of the holders of our common stock.

Although we believe we have sufficient capital to fund our activities for at least the next twelve months, our future capital requirements may vary materially from those now planned. The amount of capital that we will need in the future will depend on many factors, including:

- the market acceptance of our products;
- the levels of promotion and advertising that will be required to launch our new products and achieve and maintain a competitive position in the marketplace;
- price discounts on our products to our customers;
- our business, product, capital expenditure and research and development plans and product and technology roadmaps;
- the levels of inventory and accounts receivable that we maintain;
- capital improvements to new and existing facilities;
- technological advances;
- our competitors response to our products;
- our pursuit of strategic alternatives, including future market opportunities; and
- our relationships with suppliers and customers.

In addition, we may require additional capital to accommodate planned growth, hiring, infrastructure and facility needs or to consummate acquisitions of other businesses, products or technologies.

Inflation

Inflation was not a material factor in either revenue or operating expenses during the past three fiscal years ended December 31, 2002, 2001 and 2000.

Effect of Recent Accounting Pronouncements

In November 2002, the FASB issued Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Guarantees of Indebtedness of Others (Interpretation). This Interpretation elaborates on the existing disclosure requirements for most guarantees, including loan guarantees such as standby letters of credit and non-performance guarantees. It also requires that at the time a company issues a guarantee, the company must recognize an initial liability for the fair market value of the obligations it assumes under that guarantee and must disclose that information in its financial statements. Specifically, we are subject to repurchase agreements with various financial institutions in connection with wholesale inventory financing. The initial recognition and measurement provisions of the Interpretation apply on a prospective basis to guarantees issued or modified after December 31, 2002. We expect that the adoption of this statement will not have a significant impact on our consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities an interpretation of ARB No. 51. The objective of FIN 46 is to improve financial reporting by companies involved with variable interest entities. This new model for consolidation applies to an entity in which either (1) the powers or rights of the equity holders do not give them sufficient decision making powers or (2) the equity

Table of Contents

investment at risk is insufficient to finance that entity s activities without receiving additional subordinated financial support from other parties. FIN 46 requires a variable interest entity to be consolidated into the company that is subject to a majority of the risk of loss from the variable interest entity s activities or that is entitled to receive a majority of the entity s residual returns or both. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after January 31, 2003. For entities created on or prior to January 31, 2003, the consolidation requirements apply in the first fiscal year or interim period beginning after June 15, 2003. For variable interest entities created prior to January 31, 2003, we are currently evaluating the impact of the adoption of FIN 46 for these entities, and thus are not able to disclose the impact on our results of operations, financial position or cash flows.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses for each period. The following represents a summary of our critical accounting policies, defined as those policies that we believe are: (a) the most important to the portrayal of our financial condition and results of operations, and (b) that require management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effects of matters that are inherently uncertain.

Revenue Recognition

Reserves for inventory excess, obsolescence and lower of market values over costs. We generally purchase raw materials in quantities that we anticipate will be fully-used in the near term. Changes in operating strategy, customer demand and unpredictable fluctuations in market values of raw materials can limit our ability to effectively utilize all of the raw materials purchased and sold through resulting finished goods to customers for a profit. We regularly monitor potential inventory excess, obsolescence and lower market values compared to costs and, when necessary, reduce the carrying amount of our inventory to its market value.

Allowances for doubtful accounts and price protection. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Additionally, we maintain allowances for limited price protection rights for inventories of our products held by our customers as a result of recent sales transactions to them.

If we reduce the list price of our products, these customers may receive a credit from us. We estimate the impact of such pricing changes on a regular basis and adjust our allowances accordingly.

Product returns. We offer a majority of our customers that purchase products through our consumer channels limited rights to return unsold inventory. In addition, while we may not be contractually obligated to accept returned products, we may determine that it is in our best interest to accept returns in order to maintain good relationships with our customers. We provide for estimated future returns of inventory at the time of sale based on historical experience, and actual results have been within our expectations.

Sales and marketing incentives. Sales and marketing incentives were offset against revenues or charged to operations in accordance with Emerging Issues Task Force Issue No. 01-09, EITF 01-09. Sales and marketing incentives amounted to $3.8 million for the six months ended June 30, 2003 and $7.5 million for the year ended December 31, 2002, respectively, of which $1.8 million and $3.4 million, respectively, were offset against revenues, and $2.0 million and $4.1 million, respectively, were charged as an operating expense.

Consideration generally given by us to a customer is presumed to be a reduction of selling price, and therefore, a reduction of revenue. However, if we receive an identifiable benefit in return for the

Table of Contents

consideration given to our customer that is sufficiently separable from our sales to that customer, such that we could have paid an independent company to receive that benefit; and we can reasonably estimate the fair value of that benefit, then the consideration is characterized as an expense. We estimate the fair value of the benefits we receive by tracking the advertising done by our customers on our behalf and calculating the value of that advertising using a comparable rate for similar publications.

Income taxes. As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. The process incorporates an assessment of the current tax exposure together with temporary differences resulting from different treatment of transactions for tax and financial statement purposes. Such differences result in deferred tax assets and liabilities, which are included within the consolidated balance sheet. The recovery of deferred tax assets from future taxable income must be assessed and, to the extent that recovery is not likely, we establish a valuation allowance. Increases in valuation allowances result in the recording of additional tax expense. Further, if our ultimate tax liability differs from the periodic tax provision reflected in the consolidated statements of operations, additional tax expense may be recorded.

Litigation and other contingencies. Management regularly evaluates our exposure to threatened or pending litigation and other business contingencies. Because of the uncertainties related to the amount of loss from litigation and other business contingencies, the recording of losses relating to such exposures requires significant judgment about the potential range of outcomes. As additional information about current or future litigation or other contingencies becomes available, our management will assess whether such information warrants the recording of additional expense relating to our contingencies. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable. The results of these estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Valuation of long-lived assets. We assess the potential impairment of long-lived tangible and intangible assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Changes in our operating strategy can significantly reduce the estimated useful life of such assets.

Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Risk

At any time, fluctuations in interest rates could affect interest earnings on our cash and cash equivalents and interest expense on our existing variable rate debt. We believe that the effect, if any, of reasonably possible near term changes in interest rates on our financial position, results of operations and cash flows would not be material. Currently, we do not hedge these interest rate exposures. The primary objective of our investment activities is to preserve capital. We have not used derivative financial instruments in our investment portfolio.

Our cash and cash equivalent were $34.0 million at June 30, 2003 and December 31, 2002. Our variable rate equipment debt was paid down to zero at December 31, 2002, and our floating rate debt under the revolving credit facility expired in August 2002 and was not renewed. At June 30, 2003, our cash and cash equivalents include $24.2 million invested in money market and other interest bearing accounts and $9.8 million invested in securities. At December 31, 2002, our cash and cash equivalents included $25.4 million invested in money market and other interest bearing accounts and $8.6 million invested in securities. Our investment in securities represents investments in corporate bonds, auction rate securities and commercial paper with maturities of less than three months. At June 30, 2003, our investments in securities with maturities of less than three months had a weighted-average time to maturity of 19.5 days compared to 23.3 days at December 31, 2002.

At June 30, 2003 and December 31, 2002, our investment in marketable securities was $10.0 million. The marketable securities consist primarily of $100,000 certificates of deposit with an original maturity of one year at

Table of Contents

100 different financial institutions. At June 30, 2003, these marketable securities had a weighted-average time to maturity of approximately 262 days compared to 77 days at December 31, 2002. Marketable securities represent investments with an original maturity of greater than three months. These securities are classified as held to maturity because we have the intention and ability to hold the securities to maturity. Gross unrealized gains and losses on held-to-maturity marketable securities have historically not been material.

If interest rates were to decrease 1%, the result would be an annual decrease in our interest income related to our cash and cash equivalents of approximately $340,000. However, due to the uncertainty of the actions that would be taken and their possible effects, this analysis assumes no such action. Further, this analysis does not consider the effect of the change in the level of overall economic activity that could exist in such an environment.

Foreign Currency Exchange Rate Risk

More than 95.0% of our international sales are denominated in U.S. dollars. Consequently, if the value of the U.S. dollar increases relative to a particular foreign currency, our products could become relatively more expensive. In addition, we purchase a majority of our IC devices from local distributors of Japanese, Korean and Taiwanese suppliers. Fluctuations in the currencies of Japan, Korea or Taiwan could have an adverse impact on the cost of our raw materials. To date, we have not entered any derivative instruments to manage risks related to interest rate or foreign currency exchange rates.

Table of Contents

BUSINESS

Overview

SimpleTech designs, manufactures and markets custom and open-standard memory solutions based on Flash memory and dynamic random access memory, or DRAM, technologies. We offer a comprehensive line of over 2,500 products and specialize in developing high-density memory modules, memory cards and storage drives. One way that we distinguish ourselves in the marketplace is by offering both Flash and DRAM-based solutions used by consumers and original equipment manufacturers, or OEMs. We believe this allows us to service a diverse customer base with multiple memory formats thereby enabling our customers to purchase all of their memory requirements from one supplier. For the first half of 2003, our top five customers by revenues were CDW Computer Centers, Cisco Systems, Ingram Micro, Insight Direct and Sam s Club.

The growth in demand for consumer electronic devices such as digital cameras, MP3 digital audio players, personal digital assistants, or PDAs, digital camcorders and smart phones, as well as the increased memory requirements of these devices, has helped fuel the increased use of non-volatile data storage Flash memory, or NAND Flash. NAND Flash is the preferred technology for these applications because it is lightweight, durable, rugged, compact and retains data without power. Our Flash cards store digital content such as pictures, digital music, video clips and files in a small form factor with large storage capacity and low power consumption. We offer our Flash cards in all major media formats, including CompactFlash, Secure Digital, Memory Stick, SmartMedia and MultiMedia cards. In addition to the demand in consumer markets, our Flash business is also expanding as a result of the growing number of OEM applications in which Flash drives are replacing rotating disk drives due to improved performance, reliability and size. These OEM applications include military subsystems, in-flight information systems, casino gaming systems, embedded controls for industrial automation and medical equipment. According to Gartner Dataquest, in a report dated September 2003, NAND Flash industry revenues are expected to grow from $2.4 billion in 2002 to $7.3 billion in 2007. Our Flash revenues increased from $24.9 million for the year ended December 31, 1999 to $54.7 million for the year ended December 31, 2002, and were $35.4 million for the six-month period ended June 30, 2003.

Our DRAM products target primarily high-performance computing applications, including switches, routers, high-end servers, workstations, desktops and notebooks. As the applications that we serve expand and as the complexity of these applications increases, the need for the customization of our products in these applications also increases. We have developed proprietary technologies to address the increased need for customized solutions. For example, our patented IC Tower® stacking technology allows multiple memory chips to be stacked together to increase the capacity of a memory module without expanding its footprint. This technique increases memory board density significantly over conventional techniques and is particularly well-suited for applications where high memory capacity, cost and space are critical. We have recently experienced growing demand for our IC Tower stacking products driven by our increased penetration of the server market. We believe that this technology allows our customers to design memory-intensive systems on a differentiated and more price competitive basis. We also believe the growth of the DRAM market will be driven primarily by the next PC upgrade cycle, the demand for increased memory content per PC and a resumption of IT spending. According to Gartner Dataquest, in a report dated September 2003, the DRAM industry is expected to grow from $15.5 billion in 2002 to $25.3 billion in 2007.

We offer memory solutions through our Consumer and OEM Divisions. Our Consumer Division sells open-standard memory storage products such as Flash cards, DRAM modules, USB mini drives and hard disk drives which are used primarily as upgrades in consumer electronic devices and computing systems. We believe our comprehensive line of products allows our customers to efficiently manage their inventory purchases and therefore reduce their costs by consolidating their purchases of memory and storage products into a single vendor. Our OEM Division sells primarily customized memory solutions for newly-manufactured systems, with most sales based on a cooperative design effort between our design engineers and our OEM customers. We believe the ability of these equipment manufacturers to shorten product development cycles and accelerate time-

Table of Contents

to-market is critical to their success. In response to this trend, we believe equipment manufacturers are increasingly outsourcing the design, development and manufacturing of memory products to third-party memory providers, such as SimpleTech. We believe our design, manufacturing, testing and logistics expertise, along with our proprietary technologies, enable us to respond quickly to our customers rapidly changing product and service requirements as well as meet their time-to-market schedules.

Industry Background

The memory market can be divided into several types of IC devices that are designed to perform specific functions within computer and other electronic devices or systems. Two of the major types of memory products are Flash and DRAM. Flash is considered a non-volatile memory since it is able to retain data without a power source. Since DRAM requires a constant power supply to retain data, it is considered volatile memory. DRAM has historically dominated the memory industry in terms of market size and scale of production and continues to be one of the highest volume semiconductors manufactured today. In recent years, the memory market has expanded to include Flash due to the proliferation of consumer electronic devices designed to allow increasing user mobility. The growth in shipments of these consumer electronic devices and their unique and expanding storage requirements have led to the increased demand for Flash memory products.

The Flash memory industry is divided into two primary segments: data storage, or NAND, and code storage, or NOR. Data storage Flash products are commonly used for storing large volumes of data in small form factor and in environments characterized by high levels of shock, vibration or temperature fluctuation. In contrast, code storage Flash products are typically used in less memory-intensive applications. Substantially all of our Flash product revenues are derived from the sale of data storage Flash products. Data storage Flash products are primarily used to store digital content such as pictures, digital music, video clips and files in consumer electronic devices such as digital cameras, MP3 digital audio players, PDAs, digital camcorders and smart phones. The demand for these consumer electronic devices is growing rapidly. In addition, these consumer electronic devices are becoming smaller in size while requiring increasing amounts of memory which is driving the demand for high-density, small form factor Flash memory solutions. Flash memory is noiseless, considerably lighter, more rugged and consumes substantially less power than a rotating disk drive. These characteristics also make Flash drives a better storage alternative than rotating disk drives in extreme environments such as those often found in the military, aerospace and communication applications.

The DRAM industry growth is driven by unit growth in the markets for PCs, high-performance workstations, servers, switches, routers and the Internet infrastructure. In addition, DRAM growth is fueled by an increasing amount of memory content used in these systems. We also anticipate that the expected PC replacement cycle and resumption of IT spending will continue to drive the demand for DRAM memory.

The Flash and DRAM memory supply chain consists of numerous participants including semiconductor manufacturers, third-party module and card manufacturers and a variety of distributors and mass market retailers who sell to end-users. Major memory semiconductor manufacturers have focused primarily on large volume opportunities, producing open-standard modules and cards as base-level memory for the leading OEMs of desktops and notebooks, digital cameras, cell phones and other mass markets. In contrast to serving the base-level memory needs of these OEMs, third-party module and card manufacturers, such as SimpleTech, provide open-standard upgrades used by consumers. In addition, we believe the increasing complexity of computing systems as well as the demands placed on them has caused OEMs to rely increasingly on third-party design and manufacturing of custom memory products in which open-standard modules and cards are not adequate.

The SimpleTech Solution

SimpleTech designs, manufactures and markets a comprehensive line of memory and storage products used in consumer electronics, high-performance computing, defense and aerospace systems, networking and communications and other OEM applications. We believe our comprehensive line of products allows our customers to efficiently manage their supply chains by consolidating their memory and storage product purchases.

Product Features

High degree of customization. Products sold to our OEM Division customers are typically customized by our design and engineering teams to meet our customers specific design requirements.

High density. Our patented IC Tower stacking technology allows us to design and manufacture Flash cards and DRAM memory modules in which multiple memory chips are stacked together to increase the capacities of memory modules without increasing the product footprint. In some cases, our IC Tower stacking memory technology allows us to create a high capacity solution that is otherwise not currently available in the market using standard modules, in other cases it allows us to provide the same capacity as a standard module at a lower price point.

Compact size. We are able to manufacture high-density Flash and DRAM memory products with some of the smallest footprints on the market. As component chips increase in capacity, we are able to increase density in the same footprint.

High performance and reliability. Our memory products are built utilizing sophisticated error detection and correction processes to provide high data reliability and integrity. In addition, our memory products are designed to withstand high levels of shock and vibration as well as extreme temperature fluctuations typically associated with mobile computing and OEM applications.

Low power consumption. During read and write operations, Flash memory products typically use less power than rotating disk drives. At all other times during system operation, Flash memory products require no power. This low power consumption translates into longer battery life for many mobile computing and consumer electronic devices.

Consumer Division

Our Consumer Division sells open-standard memory storage products such as Flash cards, DRAM modules, USB mini drives and hard disk drives used as upgrades in or enhancements to consumer electronics and computing systems. Our Consumer Division customers sells our products through the following channels: VARs, mail order, distributors, and mass market retailers. We believe we are able to strengthen our relationships with these Consumer Division customers and develop the SimpleTech brand name through various marketing programs, such as volume purchase rebates, joint marketing, account manager incentives and lead generation. We also provide ongoing customer support, including on-line pricing and navigation tools, toll-free technical support and account manager training programs.

OEM Division

Our OEM Division sells primarily customized memory solutions for newly-manufactured systems, with most sales based on a cooperative design effort between our design engineers and our OEM customers. We offer our OEM Division customers a comprehensive technology solution from concept to design to the creation of prototypes through volume production and testing. We believe our quick-turn design capabilities and automated manufacturing and test processes allow our OEM Division customers to quickly and cost-effectively bring products to market. In addition, our capabilities allow our OEM Division customers to focus their resources on activities and technologies in which they add the greatest value, such as system design, sales, marketing and distribution. We believe our technical capabilities and manufacturing strengths allow our OEM Division customers to cost-effectively design and implement advanced memory chip technology in high-volume product applications.

Table of Contents

Xiran Division

In January 2002, we acquired the assets of Irvine Networks, LLC, including its intellectual property portfolio, and formed our Xiran Division. Xiran develops advanced board-level solutions that optimize server performance for content delivery applications, including streaming media and video-on-demand, and networked storage applications, including IP storage. The Xiran Division completed testing of its prototype units, successfully demonstrated product performance at several industry tradeshows and shipped evaluation units to potential customers during the third quarter of 2003. In September 2003, our Xiran Division received its first purchase orders from four companies which we expect will generate nominal revenues in the fourth quarter 2003. There can be no assurance that the efforts focused thus far will result in future profitability of the Xiran Division. In addition, the success of the Xiran Division will depend in significant part upon the ability to develop, introduce and sell its products on a timely and cost-effective basis, and to respond to changing customer requirements.

Products

We offer a comprehensive line of more than 2,500 memory and storage products using our proprietary design and manufacturing technologies. Substantially all of our Flash and DRAM memory products comply with industry standards and are based on a variety of industry architectures. Sales of memory products accounted for substantially all of our total revenues in the first half of 2003 and full years 2002 and 2001. The balance is composed of other product revenue such as hard disk drives.

Flash Products

Substantially all of our Flash product revenues are derived from the sale of data storage Flash products. Our Flash products are commonly used for storing large volumes of data in small form factors in environments characterized by high levels of shock, vibration or temperature fluctuation. Our Flash products are used primarily in consumer electronic devices, such as digital cameras, MP3 digital audio players and PDAs and are compatible with a majority of today s industry standards.

Data Storage Flash products. We offer a broad line of Flash products in various formats, capacities, sizes and operating voltages and temperatures and include:

CompactFlash. CompactFlash products provide full PC Card ATA functionality but are only one-fourth the size of a standard PC Card. CompactFlash s small size, durability, low power consumption and ability to operate at either 3.3 volts or 5.0 volts make it well-suited for a range of current and next-generation, small size consumer applications such as audio recorders, digital cameras, MP3 digital audio players and PDAs. CompactFlash products provide interoperability with systems based on the PC Card ATA standard by using a low-cost passive adapter.

Secure Digital and MultiMedia Flash Cards. Secure Digital and MultiMedia Flash Cards are used in storage, data backup and data logging applications and are about the size of a postage stamp. Their slim, compact design makes them an ideal removable storage solution for designs ranging from pocket-sized cellular phones, audio players and digital cameras, to PDAs and set-top boxes as well as other compact or multi-function digital products.