

NETLOGIC MICROSYSTEMS INC
Form 10-Q
May 05, 2009

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2009

OR

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

For the Transition Period from _____ to _____

Commission File Number: 000-50838

NETLOGIC MICROSYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

77-0455244
(I.R.S. Employer
Identification No.)

1875 Charleston Rd.
Mountain View, CA 94043
(650) 961-6676
(Address and telephone number of principal executive offices)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes

No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class | Outstanding at April 30, 2009 |
|--|-------------------------------|
| Common Stock, \$0.01 par value per share | 21,956,196 shares |

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NETLOGIC MICROSYSTEMS, INC.

FORM 10-Q

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PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

NETLOGIC MICROSYSTEMS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS)
(UNAUDITED)

| | March 31, 2009 | December 31, 2008 |
|--|-------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 69,134 | \$ 83,474 |
| Short-term investments | 19,741 | 13,067 |
| Accounts receivables, net | 8,283 | 8,382 |
| Inventories | 10,900 | 13,707 |
| Deferred income taxes | 2,908 | 3,217 |
| Prepaid expenses and other current assets | 3,890 | 1,937 |
| Total current assets | 114,856 | 123,784 |
| Property and equipment, net | 4,826 | 5,513 |
| Goodwill | 68,712 | 68,712 |
| Intangible asset, net | 36,213 | 39,538 |
| Other assets | 5,197 | 8,224 |
| Total assets | \$ 229,804 | \$ 245,771 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities | | |
| Accounts payable | \$ 8,297 | \$ 7,618 |
| Accrued liabilities | 10,141 | 25,920 |
| Deferred margin | 625 | 1,638 |
| Software licenses and other obligations, current | 774 | 755 |
| Total current liabilities | 19,837 | 35,931 |
| Software licenses and other obligations, long-term | 41 | 464 |
| Other liabilities | 9,433 | 9,109 |
| Total liabilities | 29,311 | 45,504 |
| Stockholders' equity | | |
| Common stock | 219 | 219 |
| Additional paid-in capital | 280,161 | 276,042 |
| Accumulated other comprehensive income (loss) | 11 | (13) |
| Accumulated deficit | (79,898) | (75,981) |
| Total stockholders' equity | 200,493 | 200,267 |
| Total liabilities and stockholders' equity | \$ 229,804 | \$ 245,771 |

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

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NETLOGIC MICROSYSTEMS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (IN THOUSANDS, EXCEPT FOR PER SHARE AMOUNTS)
 (UNAUDITED)

| | Three Months Ended March 31, | |
|---|---------------------------------|-----------|
| | 2009 | 2008 |
| Revenue | \$ 30,366 | \$ 34,180 |
| Cost of revenue | 13,544 | 15,383 |
| Gross profit | 16,822 | 18,797 |
| Operating expenses: | | |
| Research and development | 12,198 | 12,206 |
| Selling, general and administrative | 6,814 | 6,464 |
| Total operating expenses | 19,012 | 18,670 |
| Income (loss) from operations | (2,190) | 127 |
| Interest and other income, net | 173 | 487 |
| Income (loss) before income taxes | (2,017) | 614 |
| Provision for (benefit from) income taxes | 1,900 | (513) |
| Net income (loss) | \$ (3,917) | \$ 1,127 |
| Net income (loss) per share-basic | \$ (0.18) | \$ 0.05 |
| Net income (loss) per share-diluted | \$ (0.18) | \$ 0.05 |
| Shares used in calculation-basic | 21,838 | 21,239 |
| Shares used in calculation-diluted | 21,838 | 22,064 |

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

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NETLOGIC MICROSYSTEMS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

| | Three Months Ended March 31, | |
|--|---------------------------------|-----------|
| | 2009 | 2008 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ (3,917) | \$ 1,127 |
| Adjustments to reconcile net income to net cash provided by operating activities | | |
| Depreciation and amortization | 4,285 | 4,260 |
| Accretion of discount relating to debt securities | (20) | - |
| Stock-based compensation | 4,300 | 3,701 |
| Provision for (recovery of) doubtful accounts | (14) | - |
| Provision for inventory reserves | 286 | 493 |
| Deferred income taxes, net | 3,335 | - |
| Changes in current assets and liabilities, net of effects of acquisitions: | | |
| Accounts receivable | 113 | (4,920) |
| Inventories | 2,498 | (2,390) |
| Prepaid expenses and other assets | (1,980) | (197) |
| Accounts payable | 679 | 5,228 |
| Accrued liabilities | (225) | (2,127) |
| Deferred margin | (1,013) | 175 |
| Other long-term liabilities | 324 | 222 |
| Net cash provided by operating activities | 8,651 | 5,572 |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | (273) | (365) |
| Purchase of short-term investments | (14,633) | - |
| Sales and maturities of short-term investments | 7,950 | - |
| Cash paid for acquisitions | (15,501) | - |
| Net cash used in investing activities | (22,457) | (365) |
| Cash flows from financing activities: | | |
| Payments of software license and other obligations | (404) | (455) |
| Proceeds from issuance of Common Stock | 218 | 1,046 |
| Payments for retirement of Common Stock | (348) | (652) |
| Net cash used by financing activities | (534) | (61) |
| Effects of exchange rate on cash and cash equivalents | - | (10) |
| Net increase (decrease) in cash and cash equivalents | (14,340) | 5,136 |
| Cash and cash equivalents at beginning of year | 83,474 | 50,689 |
| Cash and cash equivalents at end of year | \$ 69,134 | \$ 55,825 |

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

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NetLogic Microsystems, Inc.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of NetLogic Microsystems, Inc. (“we,” “our” and the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America and with the instructions for Form 10-Q and Regulation S-X statements. Accordingly, they do not include all of the information and notes required for complete financial statements. In the opinion of management, all adjustments, consisting of only normal recurring items, considered necessary for a fair statement of the results of operations for the periods are shown.

These unaudited financial statements should be read in conjunction with the audited financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2008. Operating results for the three months ended March 31, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009.

Critical Accounting Policies and Estimates

The preparation of our unaudited condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We based these estimates and assumptions on historical experience and evaluate them on an on-going basis to help ensure they remain reasonable under current conditions. Actual results could differ from those estimates. During the three months ended March 31, 2009, there were no significant changes to the critical accounting policies and estimates discussed in our 2008 annual report on Form 10-K with the exception of those discussed below.

Foreign Currency

Effective January 1, 2009, the functional currency for all of our foreign subsidiaries became the United States dollar. Assets and liabilities denominated in non-U.S. dollars are remeasured into U.S. dollars at end-of-period exchange rates for monetary assets and liabilities, and historical exchange rates for nonmonetary assets and liabilities. Revenue and expenses are remeasured at average exchange rates in effect during the period, except for those revenue and expenses related to the nonmonetary assets and liabilities, which are measured at historical exchange rates. The gains or losses from foreign currency remeasurement are included in interest and other income, net. Such gains or losses have not been material for the three months ended March 31, 2009. The impact of this change was not material to all prior periods presented.

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Recently Issued Accounting Pronouncements

In April 2009, the FASB issued three related Staff Positions: (i) FSP 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability have Significantly Decreased and Identifying Transactions That Are Not Orderly, or FSP 157-4, (ii) SFAS 115-2 and SFAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments, or FSP 115-2 and FSP 124-2, and (iii) SFAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments, or FSP 107 and APB 28-1, which will be effective for interim and annual periods ending after June 15, 2009. FSP 157-4 provides guidance on how to determine the fair value of assets and liabilities under SFAS 157 in the current economic environment and reemphasizes that the objective of a fair value measurement remains an exit price. If we were to conclude that there has been a significant decrease in the volume and level of activity of the asset or liability in relation to normal market activities, quoted market values may not be representative of fair value and we may conclude that a change in valuation technique or the use of multiple valuation techniques may be appropriate. FSP 115-2 and FSP 124-2 modify the requirements for recognizing other-than-temporarily impaired debt securities and revise the existing impairment model for such securities, by modifying the current intent and ability indicator in determining whether a debt security is other-than-temporarily impaired. FSP 107 and APB 28-1 enhance the disclosure of instruments under the scope of SFAS 157 for both interim and annual periods. We are currently evaluating these Staff Positions.

In April 2009, the FASB issued FSP No. 141R-1 Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies, or FSP 141R-1. FSP 141R-1 amends the provisions in Statement 141R for the initial recognition and measurement, subsequent measurement and accounting, and disclosures for assets and liabilities arising from contingencies in business combinations. The FSP eliminates the distinction between contractual and non-contractual contingencies, including the initial recognition and measurement criteria in Statement 141R and instead carries forward most of the provisions in SFAS 141 for acquired contingencies. FSP 141R-1 is effective for contingent assets and contingent liabilities acquired in business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. We will apply the provisions of SFAS141(R) if and when a future acquisition occurs.

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2. Basic and Diluted Net Income Per Share

We compute net income per share in accordance with SFAS 128, "Earnings per Share." Basic net income per share is computed by dividing net income attributable to common stockholders (numerator) by the weighted average number of common shares outstanding (denominator) during the period. Diluted net income per share gives effect to all dilutive potential common shares outstanding during the period including stock options and warrants using the treasury stock method.

The following is a reconciliation of the weighted average number of common shares used to calculate basic net income per share to the weighted average common and potential common shares used to calculate diluted net income per share for the three months ended March 31, 2009 and 2008 (in thousands, except per share data):

| | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2009 | 2008 |
| Numerator: | | |
| Net (loss) income: basic and diluted | \$ (3,917) | \$ 1,127 |
| Denominator: | | |
| Add: common shares outstanding | 21,871 | 21,272 |
| Less: unvested common shares subject to repurchase | (33) | (33) |
| Total shares: basic | 21,838 | 21,239 |
| Add: stock options and warrants outstanding, if dilutive | - | 792 |
| Add: shares subject to repurchase, if dilutive | - | 33 |
| Total shares: diluted | 21,838 | 22,064 |
| Basic earnings per share | \$ (0.18) | \$ 0.05 |
| Diluted earnings per share | \$ (0.18) | \$ 0.05 |

For the three months ended March 31, 2009 and 2008, employee stock options to purchase the following number of shares of common stock were excluded from the computation of diluted net income per share as their effect would be anti-dilutive (in thousands):

| | Three Months Ended March 31, | |
|---------------|---------------------------------|-------|
| | 2009 | 2008 |
| Stock options | 3,475 | 3,041 |

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3. Stock-Based Compensation

We have adopted stock plans that provide for grants to employees of equity-based awards, which include stock options and restricted stock. In addition, we have an Employee Stock Purchase Plan (“ESPP”) that allows employees to purchase our common stock at a discount through payroll deductions. The estimated fair value of our equity-based awards, less expected forfeitures, is amortized over the awards’ service period. We also grant stock options and restricted stock to new employees in accordance with Nasdaq Marketplace rule 4350(i)(1)(A)(iv) as an inducement material to the new employee’s entering into employment with the Company.

The following table summarizes stock-based compensation expense recorded for the periods presented (in thousands):

| | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2009 | 2008 |
| Cost of revenue | \$ 175 | \$ 280 |
| Research and development | 2,151 | 2,018 |
| Selling, general and administrative | 1,974 | 1,403 |
| Total stock-based compensation expense | \$ 4,300 | \$ 3,701 |

In addition, we capitalized approximately \$0.2 million and \$0.2 million of stock-based compensation in inventory as of March 31, 2009 and December 31, 2008, respectively, which represented indirect manufacturing costs related to our inventory.

Stock Options

The exercise price of each stock option generally equals the market price of our common stock on the date of grant. Most options vest over four years and expire no later than ten years from the grant date. During the three months ended March 31, 2009 and 2008, we granted stock options to purchase approximately 258,000 and 205,000 shares of common stock, respectively. The weighted average grant date fair value of options granted during the three months ended March 31, 2009 and 2008 was \$12.29 and \$14.83, respectively. As of March 31, 2009 there was approximately \$23.6 million of total unrecognized compensation cost related to unvested stock options granted and outstanding with a weighted average remaining vesting period of 2.3 years.

Restricted Stock

During the three months ended March 31, 2009 and 2008, we granted restricted stock units representing the future right to acquire approximately 123,000 and 163,000 shares of common stock, respectively. These awards vest over the requisite service period, which ranges from two to four years. The fair value of the restricted stock was determined using the fair value of our common stock on the date of the grant. The fair value of the restricted stock is being amortized on a straight-line basis over the service period, and is reduced for estimated forfeitures. As of March 31, 2009, there was approximately \$16.6 million of total unrecognized compensation cost related to unvested restricted stock granted which is expected to be recognized over a weighted average period of 2.7 years.

Employee Stock Purchase Plan

Our ESPP provides that eligible employees may purchase up to \$25,000 worth of our common stock annually over the course of two six-month offering periods. The purchase price to be paid by participants is 85% of the price per share of our common stock either at the beginning or the end of each six-month offering period, whichever is less.

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Valuation Assumptions

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. This model was developed for use in estimating the value of publicly traded options that have no vesting restrictions and are fully transferable. Our employee stock options have characteristics significantly different from those of publicly traded options as they have vesting requirements and are not fully transferable. The weighted average assumptions used in the model are outlined in the following table:

| | Three Months Ended March 31, | |
|--------------------------------------|---------------------------------|----------|
| | 2009 | 2008 |
| Stock Option Plans: | | |
| Risk-free interest rate | 1.87% | 3.09% |
| Expected life of options (in years) | 5.90 | 5.18 |
| Expected dividend yield | 0.00% | 0.00% |
| Volatility | 60% | 60% |
| Weighted average fair value | \$ 12.29 | \$ 14.83 |
| Employee Stock Purchase Plan: | | |
| Risk-free interest rate | 0.27% | 3.32% |
| Expected life of options (in years) | 0.49 | 0.50 |
| Expected dividend yield | 0.00% | 0.00% |
| Volatility | 55% | 60% |
| Weighted average fair value | \$ 6.67 | \$ 9.99 |

The computation of the expected volatility assumption used in the Black-Scholes calculations for new grants is based on a combination of historical and implied volatilities. When establishing the expected life assumption, we review on a semi-annual basis the historical employee exercise behavior with respect to option grants with similar vesting periods.

4. Income Taxes

At January 1, 2009 and March 31, 2009, we had \$15.2 million and \$15.5 million of unrecognized tax benefits. Approximately \$13.3 million of the balance as of March 31, 2009 would affect our effective tax rate if recognized. This was partially offset by 2009 unrecognized tax benefits recorded during the period.

We recognize interest and penalties related to uncertain tax positions in income tax expense. As of March 31, 2009, we had \$737,000 of accrued interest and zero penalties related to uncertain tax positions.

The tax years 1997-2008 remain open to examination by one or more of the major taxing jurisdictions in which we are subject to taxation on our taxable income. We do not anticipate that total unrecognized tax benefits will significantly change due to the settlement of audits and the expiration of statute of limitations prior to March 31, 2010.

In February 2009, the California 2009-2010 budget legislature was enacted into law, allowing companies to elect, for income tax purposes, to apply a single sales factor apportionment for years beginning after January 1, 2011. Based on our anticipated election, we determined a need to establish a valuation allowance on certain deferred tax assets, totaling \$3.0 million during the three months ended March 31, 2009.

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5. Business Combination

Aeluros, Inc.

In October 2007, we acquired all outstanding equity securities of Aeluros, Inc. (“Aeluros”) a privately-held, fabless provider of industry-leading 10-Gigabit Ethernet physical layer products (“PLPs”). The PLP family extended our product offerings to the physical layer, or Layer 1, of the Open Systems Interconnection (“OSI”) reference model, which is a layered abstract description for communications and computer network protocol design developed as part of the Open Systems Interconnection initiative. The physical layer provides the physical and electrical means for transmitting data between different nodes on a network. We paid \$57.1 million in cash. During the fourth quarter of fiscal 2008, we became obligated to pay an additional \$15.5 million in cash to the former Aeluros stockholders due to our attainment of post-acquisition revenue milestones, subject to certain adjustments as provided in the Aeluros acquisition agreement. The additional consideration was included in goodwill and accrued liabilities at December 31, 2008, and was paid to the former Aeluros stockholders in February 2009. The results of operations relating to Aeluros have been included in our results of operations since the acquisition date.

6. Goodwill and Intangible Assets

The following table summarizes the components of goodwill, other intangible assets and related accumulated amortization balances, which were recorded as a result of prior business combinations (in thousands):

| | March 31, 2009 | | | December 31, 2008 | | |
|-----------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
| | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Goodwill | \$ 68,712 | \$ - | \$ 68,712 | \$ 68,712 | \$ - | \$ 68,712 |
| Other intangible assets: | | | | | | |
| Developed technology | \$ 34,180 | \$ (13,665) | \$ 20,515 | \$ 34,180 | \$ (11,668) | \$ 22,512 |
| Composite intangible asset | 11,246 | (4,452) | 6,794 | 11,246 | (3,749) | 7,497 |
| Patents and core technology | 5,590 | (1,605) | 3,985 | 5,590 | (1,325) | 4,265 |
| Customer relationships | 6,900 | (1,981) | 4,919 | 6,900 | (1,636) | 5,264 |
| Backlog | 2,106 | (2,106) | - | 2,106 | (2,106) | - |
| Total | \$ 60,022 | \$ (23,809) | \$ 36,213 | \$ 60,022 | \$ (20,484) | \$ 39,538 |

As of March 31, 2009 and December 31, 2008, goodwill represented approximately 30% and 28%, respectively, of our total assets.

For the three months ended March 31, 2009 and 2008, amortization expense related to intangible assets was \$3.3 million and \$3.3 million, respectively. The amortization expense related to intangible assets is included in cost of sales because it related to products sold during such periods, except for the amortization of the customer relationships of \$0.3 million and \$0.3 million for the three months ended March 31, 2009 and 2008, respectively, which was included in selling, general and administrative expenses.

As of March 31, 2009, the estimated future amortization expense of intangible assets in the table above is as follows (in thousands):

| Fiscal Year Ending | Estimated Amortization |
|--------------------|------------------------|
|--------------------|------------------------|

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| | | |
|---------------------------|----|--------|
| 2009 (remaining 9 months) | \$ | 9,974 |
| 2010 | | 13,299 |
| 2011 | | 10,154 |
| 2012 | | 2,786 |
| Total | \$ | 36,213 |

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7. Cash, Cash Equivalents and Short-Term Investments

The following is a summary of available-for-sale investments as of March 31, 2009 and December 31, 2008 (in thousands):

| | March 31, 2009 | | | Estimated Fair Value |
|-----------------------------------|-------------------|-----------------------------|-----------------------------|----------------------------|
| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized Loss | |
| U.S. government agency securities | \$ 19,730 | \$ 11 | \$ - | \$ 19,741 |
| Money market funds | 46,498 | - | - | 46,498 |
| Total | \$ 66,228 | \$ 11 | \$ - | \$ 66,239 |

Reported as:

| | | | | |
|---------------------------|------------------|--------------|-------------|------------------|
| Cash and cash equivalents | \$ 46,498 | \$ - | \$ - | \$ 46,498 |
| Short-term investments | 19,730 | 11 | - | 19,741 |
| Total | \$ 66,228 | \$ 11 | \$ - | \$ 66,239 |

| | December 31, 2008 | | | Estimated Fair Value |
|-----------------------------------|-------------------|-----------------------------|-----------------------------|----------------------------|
| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized Loss | |
| U.S. government agency securities | \$ 16,413 | \$ 40 | \$ - | \$ 16,453 |
| Corporate commercial paper | 2,944 | 4 | - | 2,948 |
| Money market funds | 61,717 | - | - | 61,717 |
| Total | \$ 81,074 | \$ 44 | \$ - | \$ 81,118 |

Reported as:

| | | | | |
|---------------------------|------------------|--------------|-------------|------------------|
| Cash and cash equivalents | \$ 68,047 | \$ 4 | \$ - | \$ 68,051 |
| Short-term investments | 13,027 | 40 | - | 13,067 |
| Total | \$ 81,074 | \$ 44 | \$ - | \$ 81,118 |

The fair value of the Company's investments at March 31, 2009 and December 31, 2008, by contractual maturity, was as follows:

| | March 31, 2009 | December 31, 2008 |
|-----------------------|-------------------|----------------------|
| Due in 1 year or less | \$ 19,741 | \$ 19,401 |
| Total | \$ 19,741 | \$ 19,401 |

Net unrealized holding gains and losses on available-for-sale investments are included as a separate component of stockholders' equity at March 31, 2009 and December 31, 2008.

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8. Fair Value Measurements

SFAS No. 157 defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and considers assumptions that market participants would use when pricing the asset or liability, such as inherent risk, transfer restrictions, and risk of nonperformance.

Fair Value Hierarchy

SFAS No. 157 establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. SFAS No. 157 establishes three levels of inputs that may be used to measure fair value:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities.

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Assets and Liabilities Measured at Fair Value on a Recurring Basis

The Company measures its financial assets, specifically its cash equivalents and short-term investments, at fair value on a recurring basis. The Company does not have any financial liabilities that are measured at fair value on a recurring basis. The fair value of these financial assets was determined using the following inputs as of March 31, 2009 and December 31, 2008 (in thousands):

| | Total | Fair Value Measurements at March 31, 2009 Using | | |
|---------------------------------------|------------------|--|---|---|
| | | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Other Unobservable Inputs (Level 3) |
| Money market funds (1) | \$ 46,498 | \$ 46,498 | \$ - | \$ - |
| U.S. government agency securities (2) | 19,741 | - | 19,741 | - |
| Total | \$ 66,239 | \$ 46,498 | \$ 19,741 | \$ - |

(1) Included in cash and cash equivalents on the Company's condensed consolidated balance sheet.

(2) \$19.7 million of which is included in short-term investments on the Company's condensed consolidated balance sheet.

| | Total | Fair Value Measurements at December 31, 2008 Using | | |
|---------------------------------------|------------------|--|---|---|
| | | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Other Unobservable Inputs (Level 3) |
| Money market funds (3) | \$ 61,717 | \$ 61,717 | \$ - | \$ - |
| U.S. government agency securities (4) | 16,453 | - | 16,453 | - |
| Corporate commercial paper (5) | 2,948 | - | 2,948 | - |
| Total | \$ 81,118 | \$ 61,717 | \$ 19,401 | \$ - |

(3) Included in cash and cash equivalents on the Company's condensed consolidated balance sheet.

(4) \$6.3 million of which is included in cash and cash equivalents and \$10.1 million of which is included in short-term investments on the Company's condensed consolidated balance sheet.

(5) Included in short-term investments on the Company's condensed consolidated balance sheet.

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9. Balance Sheet Components

The components of our inventory at March 31, 2009 and December 31, 2008 were as follows (in thousands):

| | March 31, 2009 | December 31, 2008 |
|---------------------|-------------------|----------------------|
| Inventories: | | |
| Finished goods | \$ 6,060 | \$ 8,170 |
| Work-in-progress | 4,840 | 5,537 |
| | \$ 10,900 | \$ 13,707 |

The components of our accrued liabilities at March 31, 2009 and December 31, 2008 were as follows (in thousands):

| | March 31, 2009 | December 31, 2008 |
|--|-------------------|----------------------|
| Accrued Liabilities: | | |
| Accrued payroll and related expenses | \$ 4,753 | \$ 4,784 |
| Accrued accounts payable | 137 | 131 |
| Accrued inventory purchases | 559 | 729 |
| Accrued warranty | 1,415 | 1,445 |
| Accrual for Aeluros earn-out based on post-acquisition revenue milestone | - | 15,501 |
| Other accrued expenses | 3,277 | 3,330 |
| | \$ 10,141 | \$ 25,920 |

10. Product Warranties

We provide a limited product warranty from one to three years from the date of sale. We provide for the estimated future costs of repair or replacement upon shipment of the product. Our warranty accrual is estimated based on actual and historical claims compared to historical revenue and assumes that we have to replace products subject to a claim. The following table summarizes activity related to product warranty liability during the three months ended March 31, 2009 and 2008 (in thousands):

| | Three Months Ended March 31, | |
|------------------------------------|---------------------------------|----------|
| | 2009 | 2008 |
| Warranty accrual: | | |
| Beginning balance | \$ 1,445 | \$ 1,512 |
| Provision for warranty | 23 | 192 |
| Settlements made during the period | (53) | (338) |
| Ending balance | \$ 1,415 | \$ 1,366 |

During the first two quarters of 2006, we provided an additional warranty reserve of \$0.9 million to address a warranty issue related to specific devices sold to one of our international customers. The devices were tested by both us and the customer and passed quality assurance inspection at the time they were sold. The customer subsequently identified malfunctioning systems that included our devices. No specific warranty reserve was provided for additional units shipped subsequent to September 30, 2006 as the customer modified the software associated with its products to remedy the observed malfunction. As of March 31, 2009, we maintained \$0.7 million of warranty reserves for anticipated replacement costs of the parts sold to this customer.

We entered into a master purchase agreement with Cisco in November 2005 under which we provided Cisco and its contract manufacturers a warranty period of as much as five years (in the case of epidemic failure). The extended warranty period in the master purchase agreement with Cisco has not had a material impact on our results of operations or financial condition based on our warranty analysis, which included an evaluation of our historical warranty cost information and experience.

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11. Commitments and Contingencies

The Company leases its facilities under non-cancelable operating leases, which contain renewal options and escalation clauses, and expires through 2011. The Company also acquires certain assets under software licenses.

Future minimum lease commitments under non-cancelable software licenses and operating leases agreements, which include common area maintenance charges as of March 31, 2009, were as follows (in thousands):

| | Software licenses and other obligations | Operating Leases | Total |
|--|--|---------------------|----------|
| 2009 | \$ 365 | \$ 752 | \$ 1,117 |
| 2010 | 483 | 1,021 | 1,504 |
| 2011 | - | 517 | 517 |
| 2012 and thereafter | - | - | - |
| | 848 | \$ 2,290 | \$ 3,138 |
| Less: Interest component | (33) | | |
| Present value of minimum lease payment | 815 | | |
| Less: Current portion | (774) | | |
| Long-term portion of obligations | \$ 41 | | |

Purchase Commitments

At March 31, 2009, we had approximately \$4.6 million in firm, non-cancelable and unconditional purchase commitments with suppliers.

Contingencies

From time to time we are party to claims and litigation proceedings arising in the normal course of business. Currently, we do not believe that there are any claims or litigation proceeds involving matters will result in the payment of monetary damages, net of any applicable insurance proceeds, that, in the aggregate, would be material in relation to our business, financial position, results of operations or cash flows. There can be no assurance, however, that any such matters will be resolved without costly litigation, in a manner that is not adverse to our business, financial position, results of operations or cash flows, or without requiring royalty payments in the future that may adversely impact gross margins.

Indemnities, Commitments and Guarantees

In the normal course of business, we have made certain indemnities, commitments and guarantees under which we may be required to make payments in relation to certain transactions. These include agreements to indemnify our customers with respect to liabilities associated with the infringement of other parties' technology based upon our products, obligation to indemnify our lessors under facility lease agreements, and obligation to indemnify our directors and officers to the maximum extent permitted under the laws of the state of Delaware. The duration of such indemnification obligations, commitments and guarantees varies and, in certain cases, is indefinite. We have not recorded any liability for any such indemnification obligations, commitments and guarantees in the accompanying balance sheets. We do, however, accrue for losses for any known contingent liability, including those that may arise from indemnification provisions, when future payment is estimable and probable.

Under master purchase agreements signed with Cisco in November 2005, we have agreed to indemnify Cisco for costs incurred in rectifying epidemic failures, up to the greater of (on a per claim basis) 25% of all amounts paid to us by Cisco during the preceding 12 months (approximately \$12.4 million at March 31, 2009) or \$9.0 million, plus replacement costs. If we are required to make payments under the indemnity, our operating results may be adversely affected.

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12. Comprehensive Income

Comprehensive income is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. The components of comprehensive income are as follows (in thousands):

| | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2009 | 2008 |
| Net income (loss) | \$ (3,917) | \$ 1,127 |
| Currency translation adjustments | (53) | (10) |
| Unrealized gain/(loss) on short term investments | 29 | - |
| Comprehensive income (loss) | \$ (3,941) | \$ 1,117 |

13. Related Party Transactions

We lease our headquarters facility in Mountain View, California from an affiliate of Berg & Berg Enterprises, LLC, which holds shares of our common stock. During the three months ended March 31, 2009 and 2008, we made lease payments of approximately \$247,000 and \$242,000, respectively, under this lease arrangement.

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14. Operating Segments and Geographic Information

We operate as one operating and reportable segment and sell our products directly to customers in North America, Asia and Europe. Sales for the geographic regions reported below are based upon the customer headquarter locations. Following is a summary of the geographic information related to revenues for the three months ended March 31, 2009 and 2008 (in thousands):

| | Three Months Ended March 31, | |
|---------------|---------------------------------|------|
| | 2009 | 2008 |
| Revenue: | | |
| United States | 34% | 42% |
| Malaysia | 29% | 27% |
| China | 21% | 19% |
| Other | 16% | 12% |
| Total | 100% | 100% |

The following table summarizes customers comprising 10% or more of our gross account receivable for the periods indicated:

| | March 31, 2009 | December 31, 2008 |
|---------------------------------|-------------------|----------------------|
| Huawei Technologies Corporation | 29% | * |
| Wintec Industries Inc | 22% | 48% |
| Celestica Corporation | * | 15% |
| Sanmina Corporation | 19% | 12% |
| Jabil Circuit Incorporated | * | 11% |

* Less than 10% of gross account receivable

15. Subsequent Events

On April 30, 2009, we entered into a purchase agreement with Integrated Device Technology, Inc. ("IDT"), pursuant to which we agreed to acquire certain assets and intellectual property relating to IDT's network search engines, route and search accelerator products and inventory for those products. Under the purchase agreement, we will pay IDT \$90 million plus the cost of inventory on hand at the closing date. At closing, we may, at our option, choose to pay the entire purchase price in cash or pay \$60 million plus the cost of inventory in cash, and issue a secured promissory note for \$30 million payable in two installments of \$15 million each on the first and second anniversaries of the closing date.

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Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which include, without limitation, statements about the market for our technology, our strategy and competition. Such statements are based upon current expectations that involve risks and uncertainties. Any statements contained herein that are not statements of historical fact may be deemed forward-looking statements. For example, the words "believes", "anticipates", "plans", "expects", "intends" and similar expressions are intended to identify forward-looking statements. In addition, all the information under Item 3 below constitutes a forward-looking statement. Our actual results and the timing of certain events may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such a discrepancy include, but are not limited to, those discussed in "Business", "Risk Factors", "Management's Discussion and Analysis of Financial Condition and Results of Operation" and "Qualitative and Quantitative Disclosures About Market Risk" in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 4, 2009 and under "Management's discussion and Analysis of Financial Condition and Results of Operations" and "Risk Factors" below. All forward-looking statements in this document are based on information available to us as of the date of this report and we assume no obligation to update any such forward-looking statements. The following discussion should be read in conjunction with our condensed financial statements and the accompanying notes contained in this quarterly report, except as required by law. Unless expressly stated or the context otherwise requires, the terms "we", "our", "us" and "NetLogic Microsystems" refer to NetLogic Microsystems, Inc.

Overview

We are a semiconductor company that designs, develops and sells proprietary high-performance processors and high-speed integrated circuits that are used by original equipment manufacturers (OEMs) in routers, switches, wireless infrastructure equipment, network security appliances, datacenter servers, network access equipment and network storage devices to accelerate the delivery of voice, video, data and multimedia content for advanced enterprise, datacenter, communications and mobile wireless networks. Our knowledge-based processors, PLPs, and network search engine products are incorporated in systems used throughout multiple types of networks that comprise the global Internet infrastructure, including the enterprise, metro, access, edge and core networking markets, and are designed into systems offered by leading networking OEMs such as AlaxaA Networks Corporation, Alcatel-Lucent, ARRIS Group, Inc., Brocade Communication Systems, Inc., Cisco Systems, Inc., Huawei Technologies Co., Ltd., and Juniper Networks, Inc.

The products and technologies we have developed and acquired are targeted to enable our customers to develop systems that support the increasing speeds and complexity of the Internet infrastructure. We believe there is a growing need to include knowledge-based processors and high speed integrated circuits in a larger number of such systems as networks transition to all Internet Protocol (IP) packet processing at increasing speeds.

The equipment and systems that use our products are technically complex. As a result, the time from our initial customer engagement design activity to volume production can be lengthy and may require considerable support from our design engineering, research and development, sales, and marketing personnel in order to secure the engagement and commence product sales to the customer. Once the customer's equipment is in volume production, however, it generally has a life cycle of three to five years and requires less ongoing support.

In general, we recognize revenue from sales of our products upon shipment to our customers or our international stocking sales representatives. Usually, we sell the initial shipments of a product for a new design engagement directly

to the OEM customer. Once the design enters volume production, the OEM frequently outsources its manufacturing to contract manufacturers who purchase the products directly from us.

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As a fabless semiconductor company, our business is less capital intensive than others because we rely on third parties to manufacture, assemble, and test our products. In general, we do not anticipate making significant capital expenditures aside from business acquisitions that we might make from time to time. In the future, as we launch new products or expand our operations, however, we may require additional funds to procure product mask sets, order elevated quantities of wafers from our foundry partners, perform qualification testing and assemble and test those products.

Because we purchase all wafers from suppliers with fabrication facilities and outsource the assembly and testing to third party vendors, a significant portion of our costs of revenue consists of payments to third party vendors. We do not have long-term agreements with any of our suppliers and rely upon them to fulfill our orders.

On October 24, 2007, we completed the acquisition of Aeluros, Inc (the "Aeluros Acquisition"). The acquisition was accounted for as a business combination during the fourth quarter of fiscal 2007. We paid \$57.0 million in cash upon the closing of the transaction in exchange for all of the outstanding equity securities of Aeluros. We reserved 104,770 shares of common stock for future issuance upon the exercise of unvested employee stock options of Aeluros that we assumed and are subject to continued employment vesting requirements. In addition, under the terms of the definitive agreement, we paid \$15.5 million cash in February 2009 based on the attainment of revenue performance milestones for the acquired business over the one year period following the close of the transaction.

Some of our challenges in fiscal 2009 include improving operating efficiencies in the light of continued challenging macroeconomic conditions, diversifying our product offerings and inventory management. We experienced two consecutive quarter-over-quarter declines in revenue from \$38.3 million for our third fiscal quarter in 2008 to \$30.9 million for our fourth fiscal quarter in 2008 to \$30.4 million for our first fiscal quarter in 2009. We believe the decrease in demand was primarily due to macroeconomic conditions that decreased customer demand for our products. In response, we have focused on operating efficiencies and lowered our operating expenses from \$20.8 million for the third quarter of fiscal 2008 to \$20.1 million for the fourth fiscal quarter in 2008 to \$19.0 million for the first quarter in 2009. We expect to remain focused on maintaining our operating expenses at an appropriate level relative to our revenue during this period of macroeconomic weakness.

During the three months ended March 31, 2009 and 2008, our top five customers accounted for approximately 75% and 69%, respectively, of total product revenue, respectively. Favorable market trends, such as the increasing number of 10 Gigabit ports as enterprises and datacenters upgrade their legacy networks to better accommodate the proliferation of video and virtualization applications, growth in the cable infrastructure area of our business, and the growing mobile wireless infrastructure and IPTV markets, have enabled us to broaden our customer base and increase demand for our knowledge-based processors and network search engines. Additionally, we have further diversified our customer and product revenues by expanding our product portfolio to address Layer 7 content processing with our NETL7™ processor family, the Layer 1 physical layer with our 10 Gigabit Ethernet products, and entry level equipment with our NETLite™ processors.

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As an integral part of our efforts to diversify our product and customer base, as well as strengthen our competitive positioning, and broaden our technology portfolio and research and development capabilities, we have entered into strategic acquisitions of products and technology, including the acquisition of the TCAM2 products and Sahasra algorithmic technology from Cypress and the acquisition of Aeluros and its PLP products.

Cisco and its contract manufacturers have accounted for a large percentage of our historical revenue, although the percentage of our overall revenue attributable to Cisco and its contract manufacturers declined for 2008. At Cisco's request, in 2007, we transitioned into a just-in-time inventory arrangement covering substantially all of our product shipments to Cisco and its contract manufacturers. Pursuant to this arrangement we deliver products to Wintec Industries ("Wintec") based on orders they place with us, but we do not recognize product revenue unless and until Wintec reports that it has delivered the product to Cisco or its contract manufacturer to incorporate into its end products. Given this arrangement, unless Cisco or its contract manufacturers take possession of our products from Wintec in accordance with the schedules provided to us, our predicted future revenue stream could vary substantially from our forecasts, and our results of operations could be materially and adversely affected. Additionally, because we own the inventory physically located at Wintec until it is shipped to Cisco and its contract manufacturers, our ability to effectively manage inventory levels may be impaired, causing our total inventory levels to increase. This, in turn, could increase our expenses associated with excess and obsolete product and negatively impact our cash flows. During the three months ended March 31, 2009 and 2008, our revenues from Cisco and Cisco's contract manufactures were \$9.7 million and \$12.7 million, or approximately 32% and 37% of total revenue.

Critical Accounting Policies and Estimates

The preparation of our condensed unaudited financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base these estimates and assumptions on historical experience and evaluate them on an on-going basis to help ensure they remain reasonable under current conditions. Actual results could differ from those estimates. There were no changes to our critical accounting policies and estimates discussed in our 2008 Annual Report on Form 10-K.

Foreign Currency

Effective January 1, 2009, the functional currency for all of our foreign subsidiaries became the United States dollar. Assets and liabilities denominated in non-U.S. dollars are remeasured into U.S. dollars at end-of-period exchange rates for monetary assets and liabilities, and historical exchange rates for nonmonetary assets and liabilities. Revenue and expenses are remeasured at average exchange rates in effect during the period, except for those revenue and expenses related to the nonmonetary assets and liabilities, which are measured at historical exchange rates. The gains or losses from foreign currency remeasurement are included in interest and other income, net. Such gains or losses have not been material for the three months ended March 31, 2009. The impact of this change was not material to all prior periods presented.

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Results of Operations

Comparison of Three Months Ended March 31, 2009 with Three Months Ended March 31, 2008

Revenue, cost of revenue and gross profit

The table below sets forth data concerning the fluctuations in our revenue, cost of revenue and gross profit data for the three months ended March 31, 2009 and the three months ended March 31, 2008 (in thousands, except percentage data):

| | Three Months ended March 31, 2009 | Percentage of Revenue | Three Months ended March 31, 2008 | Percentage of Revenue | Year-to-Year Change | Percentage Change |
|-----------------|--|-----------------------------|--|-----------------------------|------------------------|----------------------|
| Revenue | \$ 30,366 | 100.0% | \$ 34,180 | 100.0% | \$ (3,814) | -11.2% |
| Cost of revenue | 13,544 | 44.6% | 15,383 | 45.0% | (1,839) | -12.0% |
| Gross profits | \$ 16,822 | 55.4% | \$ 18,797 | 55.0% | \$ (1,975) | -10.5% |

Revenue. Revenue for the three months ended March 31, 2009 decreased by \$3.8 million compared with the three months ended March 31, 2008. Revenue from sales to Wintec, Cisco and Cisco's contract manufacturers (collectively "Cisco") represented \$9.7 million of our total revenue for the three months ended March 31, 2009, compared with \$12.7 million during the three months ended March 31, 2008. The decrease in sales to Cisco was primarily due to a decrease of \$4.7 million in revenue from sales of our NL5000 and network search engine products, although this decline was largely offset by increased revenue of our new products to Cisco, including NL7000 and NL8000 products which increased \$1.8 million. Revenue from non-Cisco customers represented \$20.7 million of total revenue for the three months ended March 31, 2009 compared with \$21.5 million in the same quarter of the prior year. During the three months ended March 31, 2009 and 2008, Alcatel Lucent and Huawei accounted for 16% and 11%, and 13% and 6%, respectively, of our total revenue. Notwithstanding these increases, in the first quarter of 2009, we recorded an overall decrease in sales to other non-Cisco customers, reflecting an overall softening of customer demand in light of recently deteriorating macroeconomic conditions.

Cost of Revenue/Gross Profit/Gross Margin. Cost of revenue for the three months ended March 31, 2009 decreased by \$1.8 million compared with that of the three months ended March 31, 2008. Cost of revenue decreased primarily due to a decrease in product sales. Cost of revenue for the three months ended March 31, 2009 and 2008 included \$3.0 million and \$3.0 million, respectively, of amortization of intangible assets expense, and \$0.2 million and \$0.4 million of a provision for excess and obsolete inventory.

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Operating expenses

The table below sets forth operating expense data for the three months ended March 31, 2009 and the three months ended March 31, 2008 (in thousands, except percentage data):

| | Three Months ended March 31, 2009 | Percentage of Revenue | Three Months ended March 31, 2008 | Percentage of Revenue | Year-to-Year Change | Percentage Change |
|-------------------------------------|--|-----------------------------|--|-----------------------------|------------------------|----------------------|
| Operating expenses: | | | | | | |
| Research and development | \$ 12,198 | 40.2% | \$ 12,206 | 35.7% | \$ (8) | -0.1% |
| Selling, general and administrative | 6,814 | 22.4% | 6,464 | 18.9% | 350 | 5.4% |
| Total operating expenses | \$ 19,012 | 62.6% | \$ 18,670 | 54.6% | \$ 342 | 1.8% |

Research and Development Expenses. Research and development expenses increased for the three months ended March 31, 2009, compared with the same period in 2008 primarily due to increases in payroll and payroll related expenses of \$0.8 million, software licenses expenses of \$0.4 million, and stock-based compensation expenses of \$0.1 million, offset by decreases in product development and qualification expenses of \$0.7 million, travel expenses of \$0.3 million and consulting and outside vendor expenses of \$0.2 million. The increase in payroll and payroll related expenses was primarily due to increases in engineering headcount to support our new product development efforts. The increase in software license expenses was primarily due to amortization expense for our software licenses used for our internal research and development projects. The decrease in product development and qualification expense was primarily due to the production qualification and characterization of our processors. Product development and qualifications costs vary from period to period depending on the timing of development and tape-out of various products. The remainder of the increase in research and development expenses was caused by individually minor items.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by \$0.4 million during the three months ended March 31, 2009, compared with the same period in 2008, primarily due to increases in payroll and payroll related expenses of \$0.3 million, and stock-based compensation of \$0.6 million, offset by decreases in commission expenses of \$0.2 million, other professional service expenses of \$0.1 million and consulting and outside vendor expenses of \$0.1 million. The increase in payroll and payroll related expenses and stock-based compensation expenses resulted primarily from increased headcount to support our growing operations in the sales and marketing areas. The decrease in commission expense was primarily a result of our decrease in revenue. Selling, general and administrative expenses also included \$0.3 million of amortization expense for the customer relationship intangible asset in the three months ended March 31, 2009 and 2008. The remainder of the fluctuation in selling, general and administrative expenses was caused by individually minor items.

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Other items

The table below sets forth other data for the three months ended March 31, 2009 and the three months ended March 31, 2008 (in thousands, except percentage data):

| | Three Months ended March 31, 2009 | Percentage of Revenue | Three Months ended March 31, 2008 | Percentage of Revenue | Year-to-Year Change | Percentage Change |
|---|---|-----------------------------|---|-----------------------------|------------------------|----------------------|
| Other income, net: | | | | | | |
| Interest income | \$ 181 | 0.6% | \$ 483 | 1.4% | \$ (302) | -62.5% |
| Other income (expense), net | (8) | 0.0% | 4 | 0.0% | (12) | -300.0% |
| Total interest and other income, net | \$ 173 | 0.6% | \$ 487 | 1.4% | \$ (314) | -64.5% |

Interest and Other Income (Expenses), Net. Interest and other net income decreased by \$0.3 million for the three months ended March 31, 2009, compared with the three months ended March 31, 2008 primarily due to lower market yields for our investments. Our cash, cash equivalents and short-term investments balance increased from \$55.8 million at March 31, 2008 to \$88.9 million at March 31, 2009.

| | Three Months ended March 31, 2009 | Percentage of Revenue | Three Months ended March 31, 2008 | Percentage of Revenue | Year-to-Year Change | Percentage Change |
|--|--|-----------------------------|--|-----------------------------|------------------------|----------------------|
| Provision for (benefit from) income taxes | \$ 1,900 | 6.3% | \$ (513) | 1.4% | \$ 2,413 | -470.4% |

Provision for Income Taxes. During the three months ended March 31, 2009, we recorded an income tax provision of \$1.9 million. We established a valuation allowance of \$3.0 million for tax credits that are unlikely to be utilized in California in light of a legislative change enacted in February 2009 which affected the rules on state income apportionment for tax years beginning in 2011. Excluding the aforementioned, our effective tax rate for the three months ended March 31, 2009 was primarily driven by a rate differential for book income generated in foreign jurisdictions and book losses generated in the United States.

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Liquidity and Capital Resources: Changes in Financial Condition

At March 31, 2009, our principal sources of liquidity were our cash, cash equivalents, and short-term investments which totaled \$88.9 million. In February 2009, we paid \$15.5 million to the former Aeluros stockholders due to attainment of post-acquisition revenue milestones, subject to certain adjustments as provided in the Aeluros acquisition agreement

The Company's cash, cash equivalents and short-term investments are invested with financial institutions in deposits that, at times, may exceed federally insured limits. The Company had not experienced any losses on its deposits of cash and cash equivalents as of March 31, 2009. However, we believe that the capital and credit markets have been experiencing unprecedented levels of volatility and disruption and that recent U.S. sub-prime mortgage defaults have had a significant impact across various sectors of the financial markets, causing global credit and liquidity issues. We can provide no assurance that our cash, cash equivalents, and short-term investments will not be adversely affected by these matters in the future.

The table below sets forth the key components of cash flow for the three months ended March 31, 2009 and 2008 (in thousands):

| | Three Months Ended March 31, | |
|---|---------------------------------|----------|
| | 2009 | 2008 |
| Net cash provided by operating activities | \$ 8,651 | \$ 5,572 |
| Net cash used in investing activities | \$ (22,457) | \$ (365) |
| Net cash used in financing activities | \$ (534) | \$ (61) |

Cash Flows during the Three Months Ended March 31, 2009

Our net cash provided by operating activities was \$8.7 million for the three months ended March 31, 2009, which primarily consisted of \$3.9 million of net loss, \$12.2 million of non-cash operating expenses and \$0.4 million in changes in operating assets and liabilities. Non-cash operating expenses for the three months ended March 31, 2009, included stock-based compensation of \$4.3 million, depreciation and amortization of \$4.3 million, deferred income taxes, net of \$3.3 million, and provision for inventory reserve of \$0.3 million. Changes in operating assets and liabilities were primarily driven by a decrease in deferred margin of \$1.0 million, inventory of \$2.5 million, and accrued liabilities of \$0.2 million due a decrease in product sales, offset by an increase in prepaid and other current assets of \$2.0 million, accounts payable of \$0.7 million and other long-term liabilities of \$0.3 million.

Our net cash used in investing activities was \$22.5 million for the three months ended March 31, 2009, of which we used \$15.5 million for the payment of Aeluros post-acquisition revenue milestone, \$14.6 million for the purchase of short-term investments, and \$0.3 million to purchase property and equipment, offset by \$7.9 million of sales and maturities of short-term investments. We expect to make capital expenditures of approximately \$2.5 million primarily for design tools during the remainder of 2009, to support product development activities. We will use our cash and cash equivalents to fund these expenditures.

Our net cash used in financing activities was \$0.5 million for the three months ended March 31, 2009, primarily for prepayments of software licenses and other obligations of \$0.4 million and payments for retirement of common stock of \$0.3 million, offset from proceeds of stock option exercises of \$0.2 million.

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Cash Flows during the Three Months Ended March 31, 2008

Our net cash provided by operating activities was \$5.6 million for the three months ended March 31, 2008, which resulted primarily from net income of \$1.1 million adjusted for non-cash reconciling items of approximately \$8.5 million, related to depreciation and amortization expenses of \$4.3 million, stock-based compensation expenses of \$3.7 million, and a provision for inventory reserves of \$0.5 million. Net cash provided by operating activities was negatively impacted by net changes in assets and liabilities of \$4.0 million. Net changes in assets and liabilities primarily consisted of increases in accounts receivables of \$4.9 million and inventory of \$2.4 million on higher product sales, and an increase in accounts payable and accrued liabilities of \$3.1 million.

Our net cash used in investing activities was \$0.4 million for the three months ended March 31, 2008. We used \$0.4 million to purchase computer equipment and research and development design tools to support our on-going R&D projects. We expect to make capital expenditures of approximately \$3.1 million primarily for design tools during the remainder of 2008, to support product development activities. We will use our cash and cash equivalents to fund these expenditures.

Our net cash used in financing activities was \$0.1 million for the three months ended March 31, 2008, as, \$0.4 million of proceeds of stock option exercises were offset by \$0.5 million of prepayments of software licenses and other obligations.

Capital Resources

We believe that our existing cash, cash equivalents and short-term investment balance of \$88.9 million will be sufficient to meet our anticipated cash needs for at least the next 12 months. On April 30, 2009, we entered into a purchase agreement with Integrated Device Technology, Inc (“IDT”), pursuant to which we agreed to acquire certain assets and intellectual property relating IDT’s network search engines, route and search accelerator products and inventory for those products. Under the purchase agreement, we will pay IDT \$90 million plus the cost of inventory on hand at the closing date. At closing, we may, at our option, choose to pay the entire purchase price in cash or pay \$60 million plus the cost of inventory in cash, and issue a secured promissory note for \$30 million payable in two installments of \$15 million each on the first and second anniversaries of the closing date.

Our future cash needs will depend on many factors, including the amount of revenue we generate, the timing and extent of spending to support product development efforts, the expansion of sales and marketing activities, the timing of introductions of new products, the costs to ensure access to adequate manufacturing capacity, and the continuing market acceptance of our products, and any future business acquisitions that we might undertake. We may seek additional funding through public or private equity or debt financing. However, additional funds may not be available on terms acceptable to us or at all. We also might decide to raise additional capital at such times and upon such terms as management considers favorable and in the interests of the Company, including, but not limited to, from the sale of our debt and/or equity securities (before reductions for expenses, underwriting discounts and commissions) under our shelf registration statement.

Contractual Obligations

Our principal commitments as of March 31, 2009 consisted of operating lease obligation payments, wafer purchases, and payments on software licenses and other obligations, which are summarized below (in thousands):

| Total | Less than 1 year | 1 - 3 years | 4 -5 years | After 5 years |
|-------|---------------------|----------------|---------------|------------------|
|-------|---------------------|----------------|---------------|------------------|

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| | | | | | |
|------------------------------|----------|----------|----------|------|------|
| Operating lease obligations | \$ 2,290 | \$ 1,005 | \$ 1,285 | \$ - | \$ - |
| Software license obligations | 815 | 774 | 41 | - | - |
| Wafer purchases | 4,571 | 4,571 | - | - | - |
| Total | \$ 7,676 | \$ 6,350 | \$ 1,326 | \$ - | \$ - |

In addition to the enforceable and legally binding obligations quantified in the table above, we have other obligations for goods and services entered into in the normal course of business. These obligations, however, are either not enforceable or legally binding, or are subject to change based on our business decisions.

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Item 3: Quantitative and Qualitative Disclosures About Market Risk

The primary objective of our investment activities is to preserve principal while maximizing the income we receive from our investments without significantly increasing the risk of loss. Some of the investable securities permitted under our cash management policy may be subject to market risk for changes in interest rates. To mitigate this risk, we plan to maintain a portfolio of cash equivalent and short-term investments in a variety of securities which may include investment grade commercial paper, money market funds, government debt issued by the United States of America, state debt, certificates of deposit and investment grade corporate debt. Presently, we are exposed to minimal market risks associated with interest rate changes. We manage the sensitivity of our results of operations to these risks by maintaining investment grade short-term investments. Our cash management policy does not allow us to purchase or hold derivative or commodity instruments or other financial instruments for trading purposes. Additionally, our policy stipulates that we periodically monitor our investments for adverse material holdings related to the underlying financial solvency of the issuer. As of March 31, 2009, our investments consisted primarily of money market funds and U.S. government securities. Our results of operations and financial condition would not be significantly impacted by either a 10% increase or decrease in interest rates due mainly to the short-term nature of our investment portfolio.

Our sales outside the United States are transacted in U.S. dollars; accordingly our sales are not generally impacted by foreign currency rate changes. Our operating expenses are denominated primarily in U.S. Dollars, except for expenses incurred by our wholly owned subsidiaries, which are denominated in the local currency. To date, fluctuations in foreign currency exchange rates have not had a material impact on our results of operations.

Item 4: Controls and Procedures

The change in our internal controls over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting consisted of the implementation of a new enterprise resource planning system and related control processes.

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of March 31, 2009. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2009 to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934, as amended, is (i) recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

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PART II. OTHER INFORMATION

Item 1A: Risk Factors

We face many significant risks in our business, some of which are unknown to us and not presently foreseen. These risks could have a material adverse impact on our business, financial condition and results of operations in the future. We have disclosed a number of material risks under Item 1A of our annual report on Form 10-K for the year ended December 31, 2008, which we filed with the Securities and Exchange Commission on March 4, 2009. The following discussion is of material changes to risk factors disclosed in that report.

Because we rely on a small number of customers for a significant portion of our total revenue, the loss of, or a significant reduction in, orders for our products from these customers would negatively affect our total revenue and business.

To date, we have been dependent upon orders for sales of knowledge-based processors to a limited number of customers, and, in particular, Cisco, for most of our total revenue. During the three months ended March 31, 2009 and 2008, Cisco and its contract manufacturers accounted for 32% and 37% of our total revenue, respectively. We expect that our future financial performance will continue to depend in large part upon our relationship with Cisco and several other networking OEMs.

We cannot assure you that existing or potential customers will not develop their own solutions, purchase competitive products or acquire companies that use alternative methods in their systems. We do not have long-term purchase commitments from any of our OEM customers or their contract manufacturers. Although we entered into master purchase agreements with Cisco, one of Cisco's foreign affiliates and a Cisco purchasing agent, these agreements do not include any long-term purchase commitments. Cisco and our other customers do business with us currently only on the basis of short term purchase orders (subject, in the case of Cisco, to the terms of the master purchase agreements), which often are cancelable prior to shipment. The loss of orders for our knowledge-based processors for Cisco products or products of other major users of our knowledge-based processors would have a significant negative impact on our business.

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Item 6. Exhibits

An Exhibit Index has been attached as part of this quarterly report and is incorporated herein by reference.

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SIGNATURE

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

NETLOGIC MICROSYSTEMS, INC.

Dated: May 5, 2009

By: /s/ RONALD JANKOV
Ronald Jankov
President and Chief Executive
Officer
(Principal Executive Officer)

Dated: May 5, 2009

By: /s/ MICHAEL TATE
Michael Tate
Vice President and Chief
Financial Officer
(Principal Financial and
Accounting Officer)

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EXHIBIT INDEX

| | |
|------|----------------------------|
| 31.1 | Rule 13a-14 certification |
| 31.2 | Rule 13a-14 certification |
| 32.1 | Section 1350 certification |
| 32.2 | Section 1350 certification |