Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Statement

The statements in this Management's Discussion and Analysis that are forward looking involve numerous risks and uncertainties and are based on current expectations. Actual results may differ materially. Certain of these risks and uncertainties are discussed under "Factors Affecting Future Operating Results". Forward looking statements can often be identified by the use of forward looking words, such as "may," "will," "could," "should," "expect," "believe," "anticipate," "estimate," "continue," "plan," "intend," "project," or other similar words.

Nature of Operations

Xilinx, Inc. (Xilinx or the Company) designs, develops and markets complete programmable logic solutions, including advanced integrated circuits (ICs), software design tools, predefined system functions delivered as cores of logic and field engineering support. Our programmable logic ICs include field programmable gate arrays (FPGAs) and complex programmable logic devices (CPLDs). These components are standard ICs programmed by our customers to perform desired logic operations. Our products are designed to provide high integration and quick time-to-market for electronic equipment manufacturers primarily in telecommunications, networking, computing, and consumer markets. We market our products throughout the world through a direct sales organization, direct sales to manufacturers by independent sales representative firms, sales through franchised domestic distributors and sales through foreign distributors. Our products provide effective solutions for a wide range of customer logic requirements.

Results of Operations

Net Revenue

In thousands	2000	Change	1999	Change	1998
Net revenue	$1,020,993	54.2%	$661,983	7.9%	$613,593

Xilinx's net revenue increased 54.2% in fiscal 2000 compared to fiscal 1999. The increase was primarily due to the significant growth in XC4000XL, XC4000XLA, XC9500, Spartan™, and Virtex™ product lines, which was partially offset by decreased revenues in our mature XC4000 family. The 7.9% increase in fiscal 1999 over 1998 was primarily due to the penetration in high-growth end markets attributable to the XC4000EX, XC4000XL and XC9500 product lines.

We classify our product offerings into four categories by semiconductor manufacturing process technology. These four product categories are adjusted on a regular basis to accommodate corresponding changes in our technology. Advanced products include our newest technologies manufactured on 0.25-micron and smaller processes, which include the XC4000XV, XC4000XLA, Spartan XL, Spartan-II, Virtex™, and Virtex-E product lines. Advanced products represented 26.7% and 3.1% of total revenues in fiscal 2000 and 1999. The significant increases in revenues of advanced products were due to the introduction and strong market acceptance of XC4000XLA, Spartan XL and Virtex products. Mainstream products are currently manufactured on 0.35 and 0.5-micron technologies and include the XC4000E, XC4000EX, XC4000XL, XC5200, XC9500, XC9500XL, Spartan™ and CoolRunner® product lines. Mainstream products represented 52.6% of total revenues in fiscal 2000 and 63.0% in fiscal 1999. Increases in revenues of 28.7% were attributable mainly to growth in the XC4000XL, Spartan, and XC9500 product lines, along with the acquisition of CoolRunner and introduction of XC9500XL. Base products consist of our mature product families that are currently manufactured on technologies of 0.6-micron and older; this includes the XC2000, XC3000, XC3100, XC4000 and XC7000 families. Base products represented 12.3% of total revenues in fiscal 2000, as compared to 22.2% in fiscal 1999. Our Support products make up the remainder of our product offerings and include serial proms, HardWire, and software. Support products represented 8.4% and 11.7% of total revenues in fiscal 2000 and 1999, respectively. Revenues of Base products decreased 14.5% as customers migrated to newer product offerings

while revenues of Support products increased slightly due to increased revenues from serial proms. No end customer accounted for more than 10% of revenues in fiscal 2000, 1999 or 1998. The revenue by technology for the years ended March 31, 2000, 1999 and 1998 was as follows:

in millions	2000	%	1999	%	1998	%
Base products	$ 125.5	12.3	$146.8	22.2	$263.5	42.9
Mainstream products	537.0	52.6	417.1	63.0	274.0	44.7
Advanced products	272.8	26.7	20.4	3.1	0.1	–
Support products	85.7	8.4	77.7	11.7	76.0	12.4
Total revenue	$1,021.0	100.0	$662.0	100.0	$613.6	100.0

In order to compete effectively, we pass on to customers manufacturing cost reductions by reducing prices to the extent that we can maintain acceptable returns. Price erosion has been common in the semiconductor industry, as advances in both architecture and manufacturing process technology have permitted continual reductions in unit cost. We have historically been able to offset much of the revenue declines of our mature technologies with increased revenues from newer technologies, although no assurance can be given that we can continue to do so in the future.

International revenues represented approximately 33%, 32%, and 38% of total revenues for fiscal years 2000, 1999 and 1998, respectively. International revenues are derived from customers in Europe, Japan and Asia Pacific/Rest of World which represented approximately 20%, 8%, and 5% of our worldwide revenues, respectively, in fiscal 2000 as compared to approximately 21%, 7% and 4% in fiscal 1999. In fiscal 1998, Europe, Japan and Asia Pacific/Rest of World represented approximately 22%, 10% and 5% of worldwide revenues, respectively. Europe, Japan and Asia Pacific/Rest of World experienced significant revenue growth in fiscal 2000 as compared to fiscal 1999 due to wider adoption of our new products in consumer and telecommunication applications and the economic recovery in Japan and the Asia Pacific region. Japan and Asia Pacific/Rest of World experienced revenue declines in fiscal 1999 as compared to 1998 primarily due to a weak economic environment in those regions during fiscal 1999. (See Note 11 of Notes to Consolidated Financial Statements for revenue by geography for the three years ended March 31, 2000, 1999 and 1998.)

During the fourth quarter of fiscal 1999, we changed our accounting method for recognizing revenue on all shipments to international distributors. The change was made retroactive to the beginning of fiscal 1999. While we previously deferred revenue on shipments to domestic distributors until the products were sold to the end user, we recognized revenue upon shipment to international distributors, net of appropriate reserves for returns and allowances. Following the accounting change, revenue recognition on shipments to distributors worldwide is deferred until the products are sold to the end customer. We believe that deferral of revenue on shipments to distributors until the product is shipped by the distributor to an end customer is a more meaningful measurement of results of operations as it better conforms to the substance of the transaction considering the changing business environment in the international marketplace, is consistent with industry practice, and accordingly, it will focus us better on end customer sales; therefore it is a preferable method of accounting. The cumulative effect of the change in accounting method for prior years was a charge of $26.6 million, net of $12.0 million in taxes, or $0.09 net income per diluted share.

Gross Margin

In thousands	2000	Change	1999	Change	1998
Gross margin	$636,955	55.1%	$410,717	7.3%	$382,903
Percentage of revenue	62.4%		62.0%		62.4%

During fiscal 2000, our gross margin percentage increased slightly from the prior year as efficiencies from increased production volumes resulted in decreased costs as a percentage of revenue. In fiscal 1999, our gross margin percentage declined from fiscal 1998 as a result of a non-recurring royalty payment made pursuant to a license settlement with Lemelson Foundation Partnership which was partially offset by lower wafer prices from wafer suppliers, manufacturing process technology improvements, and improved yields that offset selling price reductions. (See Note 12 of Notes to Consolidated Financial Statements.) We recognize that ongoing price reductions for our integrated circuits are a significant element in expanding the demand for our products. Management believes that a gross margin objective of approximately 62% of revenues is consistent with expanding demand while realizing acceptable returns, although there can be no assurance that future gross margins can remain in this range.

Research and Development

In thousands	2000	Change	1999	Change	1998
Research and development	$123,584	36.0%	$90,893	13.0%	$80,456
Percentage of revenue	12.1%		13.7%		13.1%

We increased our expenditures in research and development as we have done each year during our sixteen-year history. The increase in research and development expenditures from fiscal 1999 to 2000 was due to designing and developing new product architectures of complex, high density devices including wafer purchases, development of advanced process technologies using 0.22-micron and 0.18-micron technologies, software development, increased labor-related costs, and testing of new products, along with increased costs associated with the acquisition of the CoolRunner® CPLD business. (See Note 13 of Notes to Consolidated Financial Statements.) The increase in research and development expenses from fiscal 1998 to 1999 was due to increased labor-related expenses along with increased costs associated with the assets purchased from MI Acquisition LLP. (See Note 13 of Notes to Consolidated Financial Statements.) We remain committed to a significant level of research and development effort in order to maintain our technology leadership in the programmable logic marketplace. Through March 31, 2000, we have received over 400 issued U.S. patents and we maintain an active program of filing for additional patents in the areas of IC architecture, circuit design, and software.

Sales, General and Administrative

In thousands	2000	Change	1999	Change	1998
Sales, general and administrative	$186,619	39.0%	$134,250	4.4%	$128,579
Percentage of revenue	18.3%		20.3%		21.0%

The 39.0% increase in sales, general and administrative expenses in fiscal 2000 was primarily attributable to increased personnel and facilities expenses, increased marketing expenses, increased outside sales commissions and sales incentives on higher revenues. Sales, general and administrative expenses increased 4.4% in fiscal 1999 over 1998 due to increased marketing expenses and increased sales commissions on higher revenues from U.S. distributors along with increased personnel costs. Although total sales, general and administrative expenses increased, they decreased as a percent of revenue because of strong revenue growth and improved operational efficiencies. We remain committed to controlling administrative expenses. However, the timing and extent of future legal costs associated with the ongoing enforcement of our intellectual property rights are not readily predictable and may significantly increase in the future.

Capital Gain from Merger of USIC with UMC

In January 2000, our equity position in United Silicon Inc. (USIC) was converted into shares of UMC which are publicly traded on the Taiwan Stock Exchange. We recognized a gain of $674.7 million ($398.1 million net of taxes) in our fiscal 2000 fourth quarter as a result of the merger of USIC with UMC. The gain represents the appreciation of our investment in USIC. As a result of this merger, we own approximately 222 million UMC shares, which represent approximately 2% of the combined UMC Group. We retain equivalent wafer capacity rights in UMC as we previously had in USIC, as long as we retain a percentage of our shares of UMC common stock. If our holdings fall below that percentage, our wafer capacity rights would be decreased prorated by the UMC shares we hold.

Due to restrictions imposed by UMC and the Taiwan Stock Exchange, the majority of our UMC shares may not be sold until July 2000. These regulatory restrictions will gradually expire between July 2000 and January 2004.

Interest and Other Income, net

In thousands	2000	Change	1999	Change	1998
Interest income and other income, net	$27,352	268.4%	$7,425	10.4%	$6,728
Percentage of revenue	2.7%		1.1%		1.1%

We earn interest income on our cash, cash equivalents and short-term and long-term investments. The amount of interest earned is a function of the balance of cash invested as well as prevailing interest rates. In fiscal 1999 and 1998, we incurred interest expense on the $250.0 million 5 1/4% convertible subordinated notes, which were fully converted in February 1999.

Average cash and investment balances increased 58% from the prior year while interest rates remained relatively flat from fiscal 1999 to fiscal 2000. The 268% increase in interest and other income in fiscal 2000 from fiscal 1999 was primarily due to the $11.2 million decrease in interest expense related to the redemption of the convertible notes in February 1999 and increased interest income on higher average cash and investment balances. In 1999, average cash and investment balances decreased slightly from the prior year while interest rates increased moderately, keeping interest income constant from fiscal 1998 to fiscal 1999. The 10.4% increase in interest and other income in fiscal 1999 was primarily due to the decrease in interest expense related to the redemption of the convertible notes offset partially by an increase in foreign currency exchange losses. The amount of net interest and other income in the future will continue to be impacted by the level of our average cash and investment balances, prevailing interest rates, the balance of any debt outstanding, and foreign currency exchange rates.

Provision for Income Taxes

In thousands	2000	Change	1999	Change	1998
Provision for taxes on income	$101,368[1]	84.5%	$54,925	(3.2%)	$56,728
Effective tax rate	29.0%[1]		29.0%		31.4%

[1] The total provision for taxes on income in fiscal 2000 was $378.0 million, including $276.6 million in capital gains tax on the UMC merger. The combined rate for the fiscal year 2000 was 36.9%.

The tax rates in fiscal 2000 and 1999 were lower than fiscal 1998 because of the R&D tax credit and increased profits from foreign operations where the tax rate is lower than the U.S. rate.

Joint Venture Equity Converted to UMC Shares

We recorded our proportional ownership of the net income (loss) of USIC, a wafer fabrication joint venture located in Taiwan, as joint venture equity income (loss) prior to the conversion of USIC shares to UMC shares. In fiscal 2000, net gains were generated as USIC began to realize volume wafer production and shipments. The fiscal 1999 net loss was a result of the continued ramp up in production of the wafer fabrication facility. Net income in fiscal 1998 was primarily attributable to foreign exchange gains as well as interest earned on the USIC investment portfolio.

As a result of the conversion of our equity position in USIC to shares of UMC in January 2000, as discussed above, we will no longer record joint venture equity income.

Inflation

To date, the effects of inflation upon our financial results have not been significant. We cannot assure, however, that inflation will not affect us materially in the future.

Financial Condition, Liquidity and Capital Resources

Our financial condition as of March 31, 2000 continued to be strong with total current assets exceeding total current liabilities by 4.3 times. At March 31, 1999, total current assets exceeded total current liabilities by 3.9 times. We have used a combination of equity and debt financing and cash flow from operations to support on-going business activities, secure acquisitions and investments in complementary technologies, obtain facilities and capital equipment, and finance inventory and accounts receivable. Additionally, our investment in UMC is available for future sale, subject to restrictions.

Cash, Cash Equivalents and Short-term Investments

Our cash, cash equivalents and short-term investments increased by $205.3 million in fiscal 2000 as we continued to generate positive cash flows from operations. Cash, cash equivalents and short-term investments represented 25.9% of total assets at March 31, 2000. During fiscal 2000, we generated cash flow of $341.1 million from operating activities and $89.1 million from financing activities, offset by $398.2 million of cash used for investing activities. Investing activities during fiscal 2000 included $231.7 million in net purchases of investments, $143.7 million expenditures for property, plant and equipment, and $22.8 million for the purchase of Philips' CPLD business. Financing activities during 2000 included $84.3 million in proceeds from sales of common stock under employee option and stock purchase plans and $10.0 million from sales of put warrants partially offset by $5.3 million of treasury stock acquisitions.

Receivables

Receivables increased 103% from $66.5 million at the end of fiscal 1999 to $135.0 million at the end of fiscal 2000. This increase was primarily attributable to an increased level of shipments.

Inventories

Inventories increased 152% from $52.0 million at March 1999 to $131.3 million at March 2000. Inventory levels increased during fiscal 2000 due to increased inventory requirements to support revenue growth and a planned build up of inventory for newer products. Additionally, inventory levels, measured as days of sales, declined at distributors compared to the prior fiscal year end due to the timing of shipments. We attempt to maintain sufficient levels of inventory in various product, package and speed configurations to meet anticipated customer demand. On the other hand, we also wish to minimize the handling costs associated with maintaining higher inventory levels and to fully realize the opportunities for cost reductions associated with architecture and manufacturing process advancements. We continually strive to balance these two objectives to provide excellent customer response at a competitive cost.

Property, Plant and Equipment

During 2000, we invested $143.7 million in property and equipment, as compared to $40.9 million in 1999. Primary investments in fiscal 2000 were for corporate building and land purchases, software development tools and semiconductor design tools, and test and manufacturing equipment at each of our manufacturing and test locations.

Current Liabilities

Current liabilities increased from $167.2 million at the end of fiscal 1999 to $244.7 million at the end of fiscal 2000. The increase was primarily attributable to the increase in accounts payable and deferred income on shipments to distributors. The increase in accounts payable was a result of business expansion and the increase in deferred income on shipments to distributors was due to increased inventory build up at distributors in response to the higher customer demand.

Long-term Debt and Lines of Credit

In fiscal 1999, we converted in full $250.0 million of 5 1/4% Convertible Subordinated Notes due 2002 for a total of 19.6 million shares of common stock at a price of $12.75 per share. We have credit facilities for up to $46.2 million of which $6.2 million is intended to meet occasional working capital requirements for our Ireland manufacturing facility. At March 31, 2000 and 1999, no borrowings were outstanding under the lines of credit. (See Note 5 of Notes to Consolidated Financial Statements.)

Stockholders' Equity

Stockholders' equity grew by 202% in fiscal 2000 to $1,776.7 million. The increase of $897.3 million was attributable to $652.5 million in net income, $196.5 million related to the issuance of common stock from employee stock plans and the tax benefit from stock options, $43.6 million from unrealized gains on available-for-sale securities and our cumulative translation adjustment, and $10.0 million related to the sale of put warrants partially offset by the $5.3 million used to acquire treasury stock.

Summary of Liquidity

We anticipate that existing sources of liquidity and cash flow from operations will be sufficient to satisfy our cash needs for the foreseeable future. However, the risk factors discussed below could affect our cash positions adversely. We will continue to evaluate opportunities for investments to obtain additional wafer capacity, procurement of additional capital equipment and facilities, development of new products, and potential acquisitions of businesses, products or technologies that would complement our businesses. We may use available cash or other sources of funding for such purposes.

Factors Affecting Future Operating Results

The semiconductor industry is characterized by rapid technological change, intense competition and cyclical market patterns. Cyclical market patterns are characterized by several factors, including:

- reduced product demand;
- limited visibility of demand for products beyond three months;
- accelerated erosion of average selling prices; and
- tight capacity availability.

Our results of operations are affected by several factors. These factors include general economic conditions, conditions specific to technology companies and to the semiconductor industry in particular, decreases in average selling prices over the life of particular products and the timing of new product introductions (by us, our competitors and others.) In addition, our results of operations are affected by the ability to manufacture sufficient quantities of a given product in a timely manner, the timely implementation of new manufacturing technologies, the ability to safeguard patents and intellectual

property from competitors, the impact of new technologies which result in rapid escalation of demand for some products in the face of equally steep declines in demand for others, and the inability to predict the success of our customers' products in their markets. Market demand for our products, particularly for those most recently introduced, can be difficult to predict, especially in light of customers' demands to shorten product lead times and minimize inventory levels. Unpredictable market demand could lead to revenue volatility if we were unable to provide sufficient quantities of specified products. In addition, any difficulty in achieving targeted wafer production yields could adversely affect our financial condition and results of operations. We attempt to identify changes in market conditions as soon as possible; however, the dynamics of the market make prediction of and timely reaction to such events difficult. Due to these and other factors, our past results, including those described in this report, are much less reliable predictors of the future than with companies in many older, more stable and less dynamic industries. Based on the factors noted herein, we may experience substantial period-to-period fluctuations in future operating results.

Our future success depends in a large part on the continued service of our key technical, sales, marketing and management personnel and on our ability to continue to attract and retain qualified employees. Particularly important are those highly skilled design, process, software and test engineers involved in the manufacture of existing products and the development of new products and processes. The competition for such personnel is intense, and the loss of key employees could have a material adverse effect on our financial condition and results of operations.

Sales and operations outside of the United States subject us to the risks associated with conducting business in foreign economic and regulatory environments. Our financial condition and results of operations could be adversely affected by unfavorable economic conditions in countries in which we do significant business and by changes in foreign currency exchange rates affecting those countries. For example, we have sales and operations in Asia Pacific and Japan. Past economic weakness in these markets adversely affected revenues, and such conditions may occur in the future. Customers may face reduced access to capital and exchange rate fluctuations may adversely affect their ability to purchase our products. In addition, our ability to sell at competitive prices may be diminished. Currency instability may increase credit risks as the weak currencies may impair our customers' ability to repay existing obligations. Any or all of these factors could adversely affect our financial condition and results of operations in the near future.

Our financial condition and results of operations are becoming increasingly dependent on the global economy. Any instability in worldwide economic environments could lead to a contraction of capital spending by our customers. Additional risks to us include government regulation of exports, imposition of tariffs and other potential trade barriers, reduced protection for intellectual property rights in some countries and generally longer receivable collection periods. Moreover, our financial condition and results of operations could be affected in the event of political conflicts in Taiwan where our main foundry partner, UMC, is located.

Our business is also subject to the risks associated with the imposition of legislation and regulations relating specifically to the import or export of semiconductor products. We cannot predict whether quotas, duties, taxes or other charges or restrictions will be imposed by the United States or other countries upon the import or export of our products in the future or what effect, if any, such actions would have on our financial condition and results of operations.

We do not directly manufacture our silicon wafers. Presently, all of our wafers are manufactured by our foundry partners in Taiwan by UMC and in Japan by Seiko. We depend on our foundry partners to deliver reliable silicon wafers, with acceptable yields, in a timely manner. If our foundry partners are unable to produce and deliver silicon wafers that meet our specifications, including acceptable yields, our results of operation could be adversely affected.

Our foundry partners in Taiwan and Japan and many of our operations in California are centered in areas that have been seismically active in the recent past. Should there be a major earthquake in our operating locations in the future, our operations, including our manufacturing activities, may be disrupted. This type of disruption could result in our inability to ship products in a timely manner, thereby materially adversely affecting our financial condition and results of operations.

The securities of many high technology companies have historically been subject to extreme price and volume fluctuations, which may adversely affect the market price of our common stock.

Dependence Upon Independent Manufacturers and Subcontractors

We do not manufacture the semiconductor wafers used for our products. During the past several years, most of our wafers have been manufactured by UMC and Seiko, with recent wafers also manufactured by USIC until its merger into UMC. We are dependent upon these suppliers and others to produce wafers with competitive performance and cost attributes which include transitioning to advanced manufacturing process technologies, producing wafers at acceptable yields and delivering them in a timely manner. While the timeliness, yield and quality of wafer deliveries have met our requirements to date, we cannot guarantee that our wafer suppliers will not experience future manufacturing problems, including delays in the realization of advanced manufacturing process technologies. Additionally, disruption of operations at these foundries for any reason, including natural disasters such as fires, floods, or earthquakes, as well as disruptions in access to adequate supplies of electricity, natural gas or water could cause delays in shipments of our products, and could have a material adverse effect on our results of operations. We are also dependent on subcontractors to provide semiconductor assembly services. Any prolonged inability to obtain wafers or assembly services with competitive performance and cost attributes, adequate yields or timely delivery, or any other circumstance that would require us to seek alternative sources of supply, could delay shipments and have a material adverse effect on our financial condition and results of operations.

Our growth will depend in large part upon our ability to obtain additional wafer fabrication capacity and assembly services from suppliers that are cost competitive. We consider various alternatives in order to secure additional wafer capacity. These alternatives include, without limitation, equity investments in, or loans, deposits, or other financial commitments to independent wafer manufacturers. We also consider the use of contracts which commit us to purchase specified quantities of wafers over extended periods. We are currently able to obtain wafers from existing suppliers in a timely manner. However, at times we have been unable, and may in the future be unable, to fully satisfy customer demand because of production constraints, including the ability of suppliers and subcontractors to provide materials and services to satisfy customer delivery dates, as well as our ability to process products for shipment. In addition, a significant increase in general industry demand or any interruption of supply could reduce our supply of wafers or increase our cost of such wafers. These events could have a material adverse effect on our financial condition and results of operations.

Dependence on New Products

Our success depends in large part on our ability to develop and introduce new products which address customer requirements and compete effectively on the basis of price, density, functionality and performance. The success of new product introductions is dependent upon several factors, including:

- timely completion of new product designs;
- ability to utilize advanced manufacturing process technologies;
- achieving acceptable yields;
- availability of supporting software design tools;
- utilization of predefined cores of logic;
- market acceptance; and
- successful deployment of systems by our customers.

We cannot assure that our product development efforts will be successful or that our new products will achieve market acceptance. Revenues relating to our mature products are expected to decline in the future. As a result, we will be increasingly dependent on revenues derived from newer products along with cost reductions on current products. We rely primarily on obtaining yield improvements and corresponding cost reductions in the manufacture of existing products and on introducing new products which incorporate advanced features and other price/performance factors that enable us to increase revenues while maintaining consistent margins. To the extent that such cost reductions and new product introductions do not occur in a timely manner, or to the extent that our products do not achieve market acceptance at prices with higher margins, our financial condition and results of operations could be materially adversely affected.

Competition

See “competition” discussed in Item 1.

Intellectual Property

We rely upon patent, trademark, trade secret and copyright law to protect our intellectual property. We cannot assure that such intellectual property rights can be successfully asserted in the future or will not be invalidated, circumvented or challenged. From time to time, third parties, including our competitors, have asserted patent, copyright and other intellectual property rights to technologies that are important to us. We cannot assure that third parties will not assert infringement claims against us in the future, that assertions by third parties will not result in costly litigation or that we would prevail in such litigation or be able to license any valid and infringed patents from third parties on commercially reasonable terms. Litigation, regardless of its outcome, could result in substantial costs and diversion of our resources. Any infringement claim or other litigation against us or by us could materially adversely affect our financial condition and results of operations. (See Part II – Other Information, Item 1 – Legal Proceedings for a discussion of litigation between Xilinx and Altera Corporation.)

Euro Currency

Beginning in 1999, 11 member countries of the European Union established fixed conversion rates between their existing sovereign currencies and adopted the Euro as their common legal currency. During the three-year transition, the Euro will be available for non-cash transactions and legacy currencies will remain legal tender. We are continuing to assess the Euro’s impact on our business. We are reviewing the ability of our accounting and information systems to handle the conversion, the ability of foreign banks to report on dual currencies, the legal and contractual implications of agreements, as well as reviewing our pricing strategies. We expect that any additional modifications to our operations and systems will be completed on a timely basis and do not believe the conversion will have a material adverse impact on our operations. However, we cannot assure that we will be able to successfully modify all systems and contracts to comply with Euro requirements.

Litigation

We are currently engaged in several legal matters. (See Legal Proceedings in Item 3 and Note 12 of Notes to Consolidated Financial Statements in Item 8.)