
UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2001

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

For the transition period from _____ to _____.

Commission file number: 0-31659

NOVATEL WIRELESS, INC.

(exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
or incorporation or organization)

86-0824673
(I.R.S. Employer
Identification No.)

9360 Towne Centre Drive, San Diego, California
(Address of principal executive offices)

92121
(zip code)

Registrant's telephone number, including area code: (858) 320-8800

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 .

The number of shares of the Registrant's common stock outstanding as of July 25, 2001 was 54,418,475.

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Forward Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 based on our current expectations, assumptions, estimates and projections about Novatel Wireless and our industry. For this purpose, statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words “believes,” “anticipates,” “plans,” “expects,” “estimates” and similar expressions are intended to identify forward-looking statements. These forward-looking statements involve risks and uncertainties and are not guarantees of future performance. Actual results may differ materially from those indicated in such forward-looking statements. Novatel Wireless undertakes no obligation to update publicly any forward-looking statements.

Trademarks

The Novatel Wireless logo, Minstrel, Minstrel III, Minstrel IIIc, Minstrel V, Minstrel S, Minstrel Plus, Minstrel 540, Merlin, Sage, Lancer, Lancer 3W, Contact, Expedite, MissionONE and Viking are trademarks of Novatel Wireless. Minstrel and Sage are registered with the U.S. Patent and Trademark Office. All other brands, products and company names mentioned herein are trademarks of their respective holders.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

NOVATEL WIRELESS, INC.

CONSOLIDATED BALANCE SHEETS

	June 30, 2001	December 31, 2000
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents, including \$14,750,000 (2001) and \$0 (2000) of restricted cash	\$ 32,672,000	\$ 66,826,000
Accounts receivable, net of allowance for doubtful accounts of \$222,000 (2001) and \$253,000 (2000)	6,581,000	8,093,000
Accounts receivable — related parties (Note 6)	1,574,000	7,446,000
Inventories	16,841,000	13,123,000
Prepaid expenses and other	1,830,000	3,388,000
	<hr/>	<hr/>
Total current assets	59,498,000	98,876,000
	<hr/>	<hr/>
Property and equipment, net	11,748,000	8,986,000
Intangible assets	3,757,000	2,260,000
Other assets	456,000	702,000
	<hr/>	<hr/>
	\$ 75,459,000	\$110,824,000
	<hr/>	<hr/>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 14,829,000	\$ 23,829,000
Accrued expenses	13,513,000	5,390,000
Line of credit payable	8,500,000	
Restructuring accrual	2,519,000	
Deferred revenues	505,000	1,996,000
Current portion of capital lease obligations	132,000	182,000
	<hr/>	<hr/>
Total current liabilities	39,998,000	31,397,000
	<hr/>	<hr/>
Capital lease obligations, net of current portion	131,000	205,000
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock, par value \$.001, 15,000,000 shares authorized, no shares issued or outstanding		
Common stock, par value \$.001, 350,000,000 shares authorized, 54,401,600	54,000	54,000

(2001) and 53,800,830 (2000) shares issued and outstanding

Additional paid-in capital	183,863,000	183,300,000
Deferred stock compensation	(11,596,000)	(18,234,000)
Accumulated deficit	(136,991,000)	(85,898,000)
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Total stockholders' equity	35,330,000	79,222,000
	<hr/>	<hr/>
	\$ 75,459,000	\$110,824,000
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See accompanying notes to consolidated financial statements.

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NOVATEL WIRELESS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
Revenue	\$ 11,173,000	\$ 8,715,000	\$ 28,833,000	\$ 15,207,000
Revenue — related parties	1,335,000	379,000	3,411,000	724,000
	<hr/>	<hr/>	<hr/>	<hr/>
Total revenue	12,508,000	9,094,000	32,244,000	15,931,000
	<hr/>	<hr/>	<hr/>	<hr/>
Cost of revenue	23,991,000	9,857,000	47,293,000	17,449,000
Cost of revenue — related parties	936,000	292,000	2,555,000	565,000
	<hr/>	<hr/>	<hr/>	<hr/>
Total cost of revenue	24,927,000	10,149,000	49,848,000	18,014,000
	<hr/>	<hr/>	<hr/>	<hr/>
Gross margin	(12,419,000)	(1,055,000)	(17,604,000)	(2,083,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Operating costs and expenses:				
Research and development	5,054,000	3,127,000	11,676,000	5,203,000
Sales and marketing	3,453,000	4,153,000	8,088,000	6,472,000
General and administrative	1,884,000	1,246,000	4,271,000	2,192,000
Restructuring charges			3,900,000	
Amortization of deferred stock compensation(*)	3,319,000	142,000	6,638,000	262,000
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Total operating costs and expenses	13,710,000	8,668,000	34,573,000	14,129,000
	<hr/>	<hr/>	<hr/>	<hr/>
Operating loss	(26,129,000)	(9,723,000)	(52,177,000)	(16,212,000)
Other income (expense):				
Interest income	417,000	75,000	1,224,000	290,000
Interest expense	(72,000)	(9,000)	(136,000)	(20,000)
Other, net	(2,000)	(11,000)	(4,000)	6,000
	<hr/>	<hr/>	<hr/>	<hr/>
Net loss	\$(25,786,000)	\$ (9,668,000)	\$(51,093,000)	\$(15,936,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Accretion of preferred dividends and amortization of offering costs		1,100,000		2,200,000
Net loss applicable to common stockholders	\$(25,786,000)	\$(10,768,000)	\$(51,093,000)	\$(18,136,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Per share data:				
Weighted average shares used in computation of basic and diluted net loss per common share	54,290,863	10,157,327	52,995,366	10,088,661
Basic and diluted net loss per common	\$ (0.48)	\$ (1.06)	\$ (0.96)	\$ (1.80)

share

(*) Amortization of deferred stock compensation:

Cost of revenue	125,000		250,000	
Research and development	331,000		662,000	
Sales and Marketing	322,000		644,000	
General and Administrative	2,541,000	142,000	5,082,000	262,000

See accompanying notes to consolidated financial statements.

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NOVATEL WIRELESS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Six Months Ended June 30,	
	2001	2000
Operating activities:		
Net loss	\$(51,093,000)	\$(15,936,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,258,000	493,000
Provision for bad debt	(31,000)	51,000
Non-cash charge for excess and obsolete inventory	19,000,000	
Non-cash portion of restructuring accrual	3,035,000	
Amortization of deferred stock compensation	6,638,000	262,000
Non-cash recognition of deferred revenues	(1,491,000)	(3,105,000)
Changes in assets and liabilities:		
Accounts receivable	1,543,000	(3,841,000)
Accounts receivable — related parties	5,872,000	
Inventories	(12,594,000)	(1,477,000)
Prepaid expenses and other	1,558,000	(1,075,000)
Other assets	246,000	(120,000)
Accounts payable	(9,000,000)	4,672,000
Accrued expenses	(2,001,000)	863,000
Net cash used in operating activities	(36,060,000)	(19,213,000)
Investing activities:		
Purchases of property and equipment	(5,536,000)	(2,637,000)
Purchase of intangible assets	(848,000)	
Capitalized software development costs	(649,000)	
Net change in short-term investments		(1,250,000)
Net cash used in investing activities	(7,033,000)	(3,887,000)
Financing activities:		
Proceeds from borrowings on line of credit	8,500,000	
Issuance of convertible preferred stock		30,254,000
Proceeds from exercise of stock options and warrants	563,000	172,000
Payments under capital lease obligation	(124,000)	(46,000)
Net cash provided by financing activities	8,939,000	30,380,000
Net increase (decrease) in cash and cash equivalents	(34,154,000)	7,280,000
Cash and cash equivalents, beginning of period	66,826,000	25,455,000
Cash and cash equivalents, end of period	\$ 32,672,000	\$ 32,735,000

Supplemental disclosures of non-cash investing and financing activities:		
Accretion of dividends on minority interest		\$ (142,000)
Accretion of dividends on convertible and redeemable preferred stock		(1,767,000)
Amortization of offering costs for convertible and redeemable preferred stock		(291,000)
Deferred compensation for stock options issued		464,000
Fixed assets retired against restructuring accrual	\$ 516,000	
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	44,000	3,000

See accompanying notes to consolidated financial statements.

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NOVATEL WIRELESS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation

The information contained herein has been prepared by Novatel Wireless, Inc. (the "Company") in accordance with the rules of the Securities and Exchange Commission. The information at June 30, 2001 and for the three month and six month periods ended June 30, 2001 and 2000 is unaudited. The consolidated financial statements reflect all adjustments, consisting of only normal recurring accruals which are, in the opinion of management, necessary for a fair statement of the results of the interim periods presented. These consolidated financial statements and notes thereto should be read in conjunction with the audited financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2000. The results of operations for the interim periods are not necessarily indicative of results to be expected for any other interim period or for the year as a whole.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances are eliminated in consolidation. Certain reclassifications have been made to amounts included in the prior period's financial statements to conform to the presentation for the periods ended June 30, 2001.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements and related notes. Changes in those estimates may affect amounts reported in future periods.

2. Operational Overview and Restructuring Charges

Our financial condition, results of operations and cash flows were adversely affected during the first six months of 2001 by decreases in demand for wireless products and decreases in demand for wireless access services for the transmission of data, including the bankruptcy of Metricom which accounted for 16.8% of our revenue for the first six months of 2001. If demand for wireless products and services decreases from current levels, our financial condition, results of operations and cash flows may be further adversely affected for the remainder of 2001 and in future years. Assuming that our revenue for each of the third and fourth quarters of 2001 equals or exceeds our revenue for the second quarter of 2001, excluding sales to Metricom, we believe that our available cash reserves together with our operating cash flows will be sufficient to fund operations and satisfy our working capital requirements and anticipated capital expenditures for the remainder of the year. Management currently is evaluating debt and equity financing alternatives to meet our future capital requirements. However, additional financing may not be available when needed, on favorable terms, or at all.

As a result of the economic slowdown in the Company's industry sector, in the first quarter of 2001, the Company announced and began implementing an operational restructuring plan to reduce its operating costs and streamline its organizational structure. As a result of this plan, the Company recorded a restructuring charge of \$3.9 million during the first quarter of 2001. The restructuring plan provided for the reduction of employee staff, consultants and temporary labor, resulting in severance payments and other employee related expenses of approximately \$2.2 million. The restructuring also provided for the closure of the Company's fulfillment and distribution facility. This function has been transitioned to one of the Company's contract manufacturers. As a result of the closure of this facility, the restructuring charge includes \$1.7 million of the impairment for assets that will no longer be used and facility lease termination and other closure costs. During the second quarter of 2001, the Company began reducing its employee staff, consultants and temporary labor, and expects to make additional head count reductions during the balance of 2001. As of June 30, 2001, the Company had closed its fulfillment and

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distribution facility located in Carlsbad, California and is in the process of disposing of fixed assets associated with the facility.

The following table displays the activity and balances of the restructuring reserve from March 31, 2001 to June 30, 2001:

Type of Cost	March 31, 2001	Payments	Asset Disposals	June 30, 2001
Employee separations	\$2,200,000	\$(633,000)		\$1,567,000
Facility closing	1,700,000	(232,000)	\$(516,000)	952,000
	<u>\$3,900,000</u>	<u>\$(865,000)</u>	<u>\$(516,000)</u>	<u>\$2,519,000</u>

In connection with the first quarter of 2001 restructuring activities, the Company also determined that certain components in inventory had been adversely impacted by the slowing economy. Accordingly, the Company recorded a charge of \$6 million for excess and obsolete raw material components and finished goods in the first quarter of 2001. In accordance with Emerging Issues Task Force 96-9, "Classification of Inventory Markdowns and Other Costs Associated with a Restructuring," all inventory adjustments are classified in "Cost of revenue" in the accompanying consolidated statements of operations. In the second quarter of 2001, economic conditions in the Company's industry sector worsened resulting in reduced demand for the Company's products. Consequently, the Company recorded an additional charge of \$13 million (see Note 3).

3. Inventories

Inventories consist of the following:

	June 30, 2001 (unaudited)	December 31, 2000
Finished goods	\$ 8,680,000	\$ 4,503,000
Raw materials and components	8,161,000	8,620,000
	<u>\$16,841,000</u>	<u>\$13,123,000</u>

During the second quarter of 2001, the Company recorded a charge to write-off \$13 million of raw material components and finished goods that are considered excess or obsolete as a result of decreased demand. Approximately \$5.3 million of this charge relates to products shipped to Metricom, which filed for bankruptcy subsequent to shipment and prior to making payment, inventory on hand for future shipments to Metricom, and inventory purchase commitments for future shipments to Metricom. In addition, approximately \$4.3 million of this charge relates to excess and obsolete inventory on hand and the remaining \$3.4 million of this charge relates to excess and obsolete inventory under purchase commitments.

4. Capitalized Software Development Costs

The Company accounts for software development costs in accordance with SFAS No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed," whereby costs for the development of new software products and substantial enhancements to existing software products are expensed as incurred until technological feasibility has been established, at which time any additional costs are capitalized. During 2001, the Company began using the detail program design method for certain products for determining when technological feasibility has been established. During the second quarter of 2001, the Company reached technological feasibility with regards to certain software development activities. Software development costs of approximately \$649,000 incurred subsequent to the establishment of technological feasibility have been capitalized in Intangible assets in the accompanying balance sheet at June 30, 2001. These costs are amortized on a product-by-product basis, using the greater of the ratio of current revenue for a product to the total of current and anticipated future revenue for that product, or the straight-line method over the remaining estimated economic life of the product, which is currently estimated to be a five-year period.

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5. Line of Credit, Letter of Credit and Restricted Cash

In June 2001, the Company entered into a \$10 million credit facility with a bank. This credit facility bears interest at prime minus 1.25% (5.5% at June 30, 2001), is secured by \$10 million cash, that the Company has deposited in a restricted certificate of deposit, and expires on July 1, 2002. The line of credit and certificate of deposit is cancelable at any time by the Company prior to the expiration date. As of June 30, 2001, \$8.5 million of borrowings were outstanding under this facility. At June 30, 2001, the Company was in violation of a financial covenant requiring a specific level of earnings as defined in the line of credit facility. The covenant violation was caused substantially by the inventory write-off discussed in Note 3. The Company has obtained a waiver from the bank related to such covenant violation.

In March 2001, the Company entered into a letter of credit with one of its vendors in the amount of \$4.75 million. This letter of credit expires on September 14, 2001 and is secured by \$4.75 million cash, which the Company has deposited in a restricted certificate of deposit.

6. Segment Information, Concentrations of Risk and Related Parties

Segment Information

The Company operates in the wireless data modem technology industry and all sales of the Company's products and services are made in this segment. Management makes decisions about allocating resources based on this one operating segment.

The Company has operations in the United States and Canada. The distribution of the Company's assets in the United States and Canada as of June 30, 2001, and December 31, 2000 are \$63.2 million and \$12.3 million, and \$100.2 and \$10.6 million, respectively.

Concentrations of Risk and Related Parties

@Road, Metricom and Hewlett Packard accounted for 18.8%, 14.4% and 9.8% of revenues, respectively, for the three months ended June 30, 2001. @Road and OmniSky accounted for 22.0% and 20.4% of revenues, respectively, for the three months ended June 30, 2000. Metricom, Hewlett Packard and @Road accounted for 16.8%, 14.5% and 12.0% of revenues, respectively, for the six months ended June 30, 2001. @Road and OmniSky accounted for 22.7% and 22.4% of revenues, respectively, for the six months ended June 30, 2000. Substantially all of the Company's revenues come from wireless Internet products. Any further decline in market acceptance of the Company's products or a further decline in the financial condition of our existing customers may impair the Company's ability to operate effectively.

The Company sells products to Airlink Communications, Inc., ("Airlink") a wireless software infrastructure business. Airlink's Chairman of the Board is also a member of the Company's Board of Directors and a shareholder. Sales to Airlink were \$1.2 million and \$379,000 for the three months ended June 30, 2001 and 2000, respectively (unaudited) and \$1.8 million and \$724,000 for the six months ended June 30, 2001 and 2000, respectively (unaudited). Receivables from Airlink amounted to \$1.6 million as of June 30, 2001 (unaudited). In May 2001, the Company and Airlink entered into an agreement for the payment of products sold to Airlink. Specifically, Airlink will pay \$1.6 million for product purchases under terms of a promissory note with the first payment of \$300,000, plus accrued interest due September 1, 2001, and the remaining principal balance due in equal installments, plus accrued interest, over eight monthly equal installments with the final payment due May 1, 2002. The note bears interest at prime plus 3% (9.75% at June 30, 2001) and is secured by all of Airlink's assets. Airlink's Chairman of the Board has also personally guaranteed this promissory note. We have sold similar products to other parties at unit prices similar to those under our arrangement with Airlink. As of June 30, 2001, accounts receivable from Airlink totaled \$1,574,000.

On June 30, 2000, Aether Capital, LLC, purchased \$20 million of the Company's Series D convertible preferred stock. Aether Capital, LLC is the investment arm of Aether Systems, Inc., which is the sole member of Aether Capital, LLC. David S. Oros, one of the Company's directors, who joined the Company's board in July 2000, serves

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as Chairman, Chief Executive Officer and President of Aether Systems, Inc. Mr. Oros is also a director of OmniSky Corporation ("OmniSky"), in which Aether Systems, Inc. is an investor. As a result of this capital transaction, OmniSky, a significant customer, became a related party and the Company commenced recording sales to OmniSky as "Revenue — Related Party" in the third quarter of 2000. Sales to OmniSky amounted to \$148,000 and \$1.9 million for the three months ended June 30, 2001 and 2000, respectively (unaudited) and \$1.6 million and \$3.6 million for the six months ended June 30, 2001 and 2000, respectively (unaudited). As of June 30, 2001, no amounts were due from OmniSky.

7. Commitments and Contingencies

Legal proceedings

On July 18, 2001, Sanmina Corporation and Sanmina Canada ULC (collectively "Sanmina") filed suit against the Company in California Superior Court, San Diego County. The complaint alleges breach of contract with respect to the Company's modification and cancellation of certain purchase orders and revision of certain forecasts, which the Company issued in connection with Sanmina's procurement of components and manufacture of goods. The suit seeks payments for cancellation charges of \$18.8 million and outstanding trade payables of \$7.4 million. Sanmina is also seeking a writ of attachment prior to resolution of the lawsuit, which, if granted by the court, would limit the Company's ability to sell, transfer or dispose of those assets attached, and limit the Company's ability to use its working capital up to the amount of the attachment. Management believes that the Company has meritorious defenses regarding various elements of the claim and intends to contest those matters vigorously, though the Company cannot predict the ultimate outcome of this litigation. If this action were determined unfavorably to the Company, it could have a material adverse affect on the Company's financial condition, results of operations and cash flows.

Purchase commitments

The Company has entered into a firm purchase commitment of approximately \$4.9 million with one of its contract manufacturers for inventory purchases with scheduled receipts and payments through December 2001.

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

Overview

The following information should be read in conjunction with the consolidated financial statements and the accompanying notes included in Item 1 of this quarterly report, as well as the audited financial statements and accompanying notes and Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2000 contained in our 2000 annual report on Form 10-K.

Our financial condition, results of operations and cash flows were adversely affected during the first six months of 2001 by decreases in demand for wireless products and decreases in demand for wireless access services for the transmission of data, including the bankruptcy of Metricom which accounted for 16.8% of our revenue for the first six months of 2001. If demand for wireless products and services decreases from current levels, our financial condition, results of operations and cash flows may be further adversely affected for the remainder of 2001 and in future years. See discussion under "Liquidity and Capital Resources."

Revenue.

Our results of operations depend upon factors outside of our control including, among other things:

- our ability to maintain and increase our sales volumes with existing customers;

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- our ability to attract new customers for our product offerings;
- the demand for wireless technology access services and wireless technology products, including Personal Data Administration devices; and
- the on-going financial condition of our existing customers and suppliers.

We cannot predict with any certainty whether we will be able to maintain or improve upon our historical sales volumes with our existing customers, or whether we will be able to attract new customers for our wireless technology products. Continued decreases in the demand for the services of our wireless service customers could lead to a decrease in the demand for our wireless products used by these customers, and adversely impact our revenue, results of operations and cash flows.

Operating Costs and Expenses.

We continue to monitor and focus on reducing our operating costs and expenses and, as a result of our restructuring efforts, we have reduced our operating costs and expenses. If our operating costs and expenses were to increase significantly, our financial condition, results of operations and cash flows could be adversely affected.

Results of Operations

Three Months Ended June 30, 2001 Compared to Three Months Ended June 30, 2000

Revenue. Revenue for the three months ended June 30, 2001 increased \$3.4 million, or 38%, to \$12.5 million compared to \$9.1 million for the same period in 2000. For the three months ended June 30, 2001, sales of our PC cards increased by \$2.6 million, OEM product sales increased by \$1.5 million and cradle product sales decreased by \$700,000 compared to the same period in 2000. The overall increase in product sales is due to the introduction of new products compared to the same period a year ago. New products contributed to the overall sales increases by \$4.4 million with the introduction of the Minstrel 540 Wireless Modem for the HP Jornada Pocket PC in October 2000, the Minstrel S for the Handspring™ Visor™ in October 2000 and the Merlin Wireless PC Card for Metricom's 128 kbps Ricochet network in November 2000. Sales of existing products decreased by \$1.1 million.

Cost of Revenue. Our cost of revenue for the three months ended June 30, 2001 increased \$14.8 million, or 146%, to \$24.9 million compared to \$10.1 million for the same period in 2000. The increase in cost of revenue was primarily the result of \$13 million of charges relating to excess and obsolete inventory recorded in the second quarter of 2001, sales of new products (approximately \$3.2 million), offset by a reduction in costs associated with the production and sales of existing products (approximately \$1.1 million) and a reduction in costs associated with our manufacturing operating capacity (approximately \$300,000).

Gross Margin. Our gross margin for the three months ended June 30 2001 decreased by \$11.4 million, or 92%, to negative \$12.4 million compared to negative \$1.1 million during the same period in 2000. Excluding the \$13 million excess and obsolete inventory charge, our gross margin increased by \$1.6 million, or 155% to \$600,000 compared to negative \$1.1 million.

Research and Development. Our research and development expenses for the three months ended June 30, 2001 increased \$1.9 million, or 62%, to \$5.1 million compared to \$3.1 million for the same period in 2000. The increase was due to an increase in personnel expenses of approximately \$700,000, an increase in depreciation and facility overhead expenses of approximately \$600,000, an increase in research supplies and expendable equipment of approximately \$400,000, an increase in travel costs of approximately \$100,000 and an increase in other expenses relating to projects in development of approximately \$100,000. During the second quarter of 2001, the Company reached technological feasibility with regards to certain software development activities and has capitalized approximately \$649,000 as compared to \$0 during the same period in 2000.

Sales and Marketing. Sales and marketing expenses for the three months ended June 30, 2001 decreased \$700,000, or 17%, to \$3.5 million compared to \$4.2 million for the same period in 2000. The decrease was the result

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of a reduction in advertising and marketing costs of approximately \$1.0 million, a reduction in facility overhead expenses of approximately \$200,000, offset by increased personnel expenses of \$400,000 and outside services and consulting costs of approximately \$100,000.

General and Administrative. General and administrative expenses for the three months ended June 30, 2001 increased \$600,000, or 51%, to \$1.9 million compared to \$1.3 million for the same period in 2000. This increase was primarily due to an increase in facility expenses of approximately \$300,000, an increase in insurance expense of approximately \$200,000, an increase in depreciation expense of approximately \$200,000 and a decrease in the foreign currency exchange transaction gain of approximately \$100,000. These increases were offset by a reduction in professional fees of approximately \$100,000 and a reduction in payroll costs of approximately \$100,000.

Restructuring Charges. As a result of the restructuring efforts implemented during the first quarter of 2001, the Company expects to realize approximately \$22 million in annual cost savings. During the three months ended June 30, 2001, the Company's cost reductions amounted to approximately \$2.9 million as

compared to the immediately preceding quarter.

Amortization of deferred stock compensation. Amortization of deferred stock compensation for the three months ended June 30, 2001 increased \$3.2 million to \$3.3 million compared to \$100,000 for the same period in 2000. This increase is due to the issuance of a significant number of stock options during the third quarter of 2000, resulting in gross deferred compensation of \$30.3 million.

Interest Income. Interest income for the three months ended June 30, 2001 increased \$300,000 to \$400,000 compared to \$100,000 for the same period in 2000. The increase was due to income from the investment of proceeds from our initial public offering in November 2000.

Net Loss. The net loss for the three months ended June 30, 2001 increased \$16.1 million, or 167%, to \$25.8 million compared to \$9.7 million for the same period in 2000.

Six Months Ended June 30, 2001 Compared to Six Months Ended June 30, 2000

Revenue. Revenue for the six months ended June 30, 2001 increased \$16.3 million, or 102%, to \$32.2 million compared to \$15.9 million for the same period in 2000. For the six months ended June 30, 2001, sales of our PC cards increased by \$11.8 million, cradle product sales increased by \$3.3 million and OEM product sales increased by \$1.2 million compared to the same period in 2000. The overall increase in product sales is due to the introduction of new products and increased demand for existing products compared to the same period a year ago. New products contributed to the overall sales increases by \$14.1 million with the introduction of the Minstrel 540 Wireless Modem for the HP Jornada Pocket PC in October 2000, the Minstrel S for the Handspring™ Visor™ in October 2000 and the Merlin Wireless PC Card for Metricom's 128 kbps Ricochet network in November 2000. Sales of existing products increased by \$2.2 million.

Cost of Revenue. Our cost of revenue for the six months ended June 30, 2001 increased \$31.8 million, or 177%, to \$49.8 million compared to \$18.0 million for the same period in 2000. The increase in cost of revenue was primarily the result of \$19 million of charges relating to excess and obsolete inventory recorded during 2001, sales of new products (approximately \$11.5 million), an increase in costs associated with the production and sales of existing products (approximately \$1.6 million), offset by a reduction in costs associated with our manufacturing operating capacity (approximately \$300,000).

Gross Margin. Our gross margin for the six months ended June 30 2001 decreased by \$15.5 million to negative \$17.6 million compared to negative \$2.1 million during the same period in 2000. Excluding the \$19 million excess and obsolete inventory charges, our gross margins increased by \$3.5 million, or 167%, to \$1.4 million compared to negative \$2.1 million during the same period in 2000.

Research and Development. Our research and development expenses for the six months ended June 30, 2001 increased \$6.5 million, or 124%, to \$11.7 million compared to \$5.2 million for the same period in 2000. The increase was due to an increase in personnel expenses of approximately \$2.8 million, an increase in depreciation and facility overhead expenses of approximately \$1.7 million, an increase in research supplies and expendable equipment of approximately \$1.3 million, an increase in travel costs of approximately \$300,000, an increase in

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outside consulting services of approximately \$300,000 and an increase in other expenses relating to projects in development of approximately \$100,000. During the second quarter of 2001, the Company reached technological feasibility with regards to certain software development activities and has capitalized approximately \$649,000 compared to \$0 during the same period in 2000.

Sales and Marketing. Sales and marketing expenses for the six months ended June 30, 2001 increased \$1.6 million, or 25%, to \$8.1 million compared to \$6.5 million for the same period in 2000. The increase was the result of an increase in personnel expenses of \$1.9 million, an increase in consulting and outside services of approximately \$200,000, an increase in travel costs of \$200,000 and an increase of \$200,000 to support new products and to expand distribution channels. This increase is offset by a decrease in advertising and marketing costs of approximately \$900,000.

General and Administrative. General and administrative expenses for the six months ended June 30, 2001 increased \$2.1 million, or 95%, to \$4.3 million compared to \$2.2 million for the same period in 2000. This increase was primarily due to an increase in facility expenses of approximately \$400,000, an increase in insurance expense of approximately \$300,000, an increase in depreciation expense of approximately \$300,000, an increase in professional fees of approximately \$300,000, an increase in consulting expense of approximately \$300,000, and a decrease in the foreign currency exchange transaction gain of approximately \$200,000. The remaining increase of \$300,000 relates to additional expenses associated with operating as a public company.

Restructuring Charges. Restructuring charges for the six months ended June 30, 2001 amounted to \$3.9 million as a result of the implementation of an operational restructuring plan. These costs are made up of personnel termination benefits approximating \$2.2 million and facility lease termination and other closure costs of approximately \$1.7 million.

Amortization of deferred stock compensation. Amortization of deferred stock compensation for the six months ended June 30, 2001 increased \$6.4 million to \$6.6 million compared to \$300,000 for the same period in 2000. This increase is due to the issuance of a significant number of stock options during the third quarter of 2000, resulting in gross deferred compensation of \$30.3 million.

Interest Income. Interest income for the six months ended June 30, 2001 increased \$900,000 to \$1.2 million compared to \$300,000 for the same period in 2000. The increase was due to income from the investment of proceeds from our initial public offering in November 2000.

Net Loss. The net loss for the six months ended June 30, 2001 increased \$35.2 million, or 221%, to \$51.1 million compared to \$15.9 million for the same period in 2000.

Liquidity and Capital Resources

As a result of cost reduction measures implemented during the first two quarters of 2001, and assuming that our revenue for each of the third and fourth quarters of 2001 equals or exceeds our revenue for the second quarter of 2001, excluding sales to Metricom, we believe that our available cash reserves together

with our operating cash flows will be sufficient to fund operations and to satisfy our working capital requirements and anticipated capital expenditures for the remainder of the year. If, however, we experience decreases in revenue or increases in our operating costs and expenses, or otherwise experience a decrease in anticipated cash flows, we may be required to further reduce our operating costs or seek alternative sources of additional debt or equity financing sooner than otherwise planned. Management currently is evaluating debt and equity financing alternatives to meet our future capital requirements. However, additional financing may not be available when needed, on favorable terms, or at all.

We have funded our operations primarily through sales of our equity securities and the issuance of debt instruments, and to a lesser extent, capital lease arrangements and borrowings under our line of credit. To date, gross proceeds from these transactions have totaled approximately \$149.3 million, including the gross proceeds from our initial public offering in November 2000 of \$64.2 million. At June 30, 2001 we had approximately \$32.7 million in cash and cash equivalents, of which \$14.8 million is restricted cash pursuant to our line of credit and letter of credit facilities as discussed in Note 5 to our consolidated financial statements.

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For the six months ended June 30, 2001, we used net cash in operating activities of \$36.1 million compared to \$19.2 million during the same period in 2000. Our operating activities during the six months ended June 30, 2001, included major uses of cash to fund our net loss of \$51.1 million, which includes \$19.0 million of non-cash inventory charges, a \$6.6 million non-cash charge for deferred compensation expenses related to stock options issued to employees during 2000, a \$3.9 million non-cash restructuring charge, a depreciation and amortization expense of approximately \$2.3 million and non-cash recognition of deferred revenues of approximately \$1.5 million. During the six months ended June 30, 2001, we used cash by increasing inventories by \$12.6 million, decreasing accounts payable by \$9.0 million, decreasing accrued expenses by \$2.0 million and decreasing the restructuring accrual by \$900,000, offset by cash generated from decreasing accounts receivable by \$7.4 million and decreasing prepaid expenses and other assets by \$1.8 million.

Our net cash used in investing activities for the six months ended June 30, 2001 was \$7.0 million, which included purchases of property and equipment of \$5.5 million, purchases of intangible assets of \$800,000 and software development costs of \$700,000. Our net cash used in investing activities for the six months ended June 30, 2000 was \$3.9 million and was primarily for purchases of property and equipment. These capital expenditures were primarily investments for equipment to test our products and to support our business.

Cash provided from financing activities for the six months ended June 30, 2001 was \$8.9 million, primarily from borrowings on our line of credit of \$8.5 million, exercise of stock options and warrants of approximately \$600,000, offset by payments of capital lease obligations of \$200,000. Cash provided by financing activities for the six months ended June 30, 2000, amounted to \$30.4 million primarily due to proceeds from the issuance of convertible preferred stock.

In June 2001, we entered into a credit facility with a bank, which allows the Company to borrow up to \$10 million. This credit facility bears interest at prime minus 1.25% (5.5% at June 30, 2001), is secured by \$10 million cash, that the Company has deposited in a restricted certificate of deposit, and expires on July 1, 2002. The line of credit is cancelable at any time by the Company prior to the expiration date. As of June 30, 2001, \$8.5 million of borrowings were outstanding under this facility. At June 30, 2001, the Company was in violation of a financial covenant requiring a specific level of earnings as defined in the line of credit facility. The covenant violation was caused substantially by the inventory write-off discussed in Note 3. The Company has obtained a waiver from the bank related to such covenant violation.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We do not currently use derivative financial instruments. We generally place our cash and short-term investments in high-credit quality instruments, primarily U.S. Government obligations and corporate obligations with contractual maturities of less than one year. These investments are not held for trading or other speculative purposes. Changes in interest rates affect the investment income we earn on our investments and therefore, impact our cash flows and results of operations. The Company's credit facility and related interest cost on borrowings is affected by the variations in the U.S. prime rate of interest. As of June 30, 2001, we had \$8.5 million outstanding under our line of credit. We do not expect any material loss from our cash and cash equivalents and therefore believe that our potential interest rate exposure is not material; however, these investments are subject to interest rate risk. We do not currently enter into foreign currency hedge transactions. Through June 30, 2001, we had a foreign currency gain of approximately \$160,000 recorded in general and administrative expenses as a result of foreign currency exchange transactions related to our Canadian subsidiary. Revenues generated outside the United States, as a percentage of total revenues were 9.0% for the six months ended June 30, 2001 and 5.4% for the same period in 2000. Fluctuations in foreign exchange rates could impact future operating results.

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PART II — OTHER INFORMATION

Item 1. Legal Proceedings

See Note 7 to our consolidated financial statements.

Item 2. Changes in Securities and Use of Proceeds

Our Registration Statement on Form S-1 (Registration No. 333-42570) related to our initial public offering was declared effective by the SEC on November 15, 2000. A total of 8,025,000 shares of our common stock were registered on our behalf. Net offering proceeds to us (after deducting underwriting

discounts and commissions and offering expenses) were approximately \$57.2 million. As of June 30, 2001, approximately \$33.0 million of these net offering proceeds had been used for operating activities and the remainder had been held as cash and cash equivalents.

Item 4. Submission of Matters to a Vote of Security Holders

On May 10, 2001, we held our annual meeting at which our stockholders voted upon the election of two nominees to our board of directors to serve for three-year terms and until their respective successors are duly elected and qualified, and the ratification of the appointment of Arthur Andersen LLP as our independent public accountants for the fiscal year ending December 31, 2001.

Our stockholders elected both nominees to three-year terms as members of our board of directors and ratified the appointment of Arthur Andersen LLP as our independent public accountants for the 2001 fiscal year. The number of votes cast for, against or withheld, and the number of abstentions with respect to each matter voted upon is set forth below.

		<u>For</u>	<u>Against/Withheld</u>	<u>Abstentions</u>
1	Election of Directors:			
	Robert Getz	42,405,271	70,205	
	Peng K. Lim	39,448,972	3,026,504	
2	Ratification of Independent Public Accountants	42,345,768	122,102	7,606

Item 6. Exhibits

<u>Exhibit No.</u>	
10.1	Business Loan Agreement
10.2	First Amendment to Business Loan Agreement

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 6, 2001

Novatel Wireless, Inc.

By: /s/ MELVIN L. FLOWERS

 Melvin L. Flowers
*Senior Vice President of Finance, Chief
 Financial Officer and Secretary*

BUSINESS LOAN AGREEMENT

This Agreement dated as of June 28, 2001, is between Bank of America, N.A. (the "Bank") and Novatel Wireless, Inc. (the "Borrower").

1. LINE OF CREDIT AMOUNT AND TERMS

1.1 Line of Credit Amount.

(a) During the availability period described below, the Bank will provide a line of credit to the Borrower. The amount of the line of credit (the "Commitment") is Ten Million Dollars (\$10,000,000.00).

(b) This is a revolving line of credit providing for cash advances and letters of credit. During the availability period, the Borrower may repay principal amounts and reborrow them.

(c) The Borrower agrees not to permit the outstanding principal balance of advances under the line of credit plus the outstanding amounts of any letters of credit, including amounts drawn on letters of credit and not yet reimbursed, to exceed the Commitment.

1.2 Availability Period. The line of credit is available between the date of this Agreement and July 1, 2002, or such earlier date as the availability may terminate as provided in this Agreement (the "Expiration Date").

1.3 Interest Rate.

(a) Unless the Borrower elects an optional interest rate as described below, the interest rate is a rate per year equal to the Bank's Prime Rate minus one and one quarter (1.25) percentage points.

(b) The Prime Rate is the rate of interest publicly announced from time to time by the Bank as its Prime Rate. The Prime Rate is set by the Bank based on various factors, including the Bank's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans. The Bank may price loans to its customers at, above, or below the Prime Rate. Any change in the Prime Rate shall take effect at the opening of business on the day specified in the public announcement of a change in the Bank's Prime Rate.

1.4 Repayment Terms.

(a) The Borrower will pay interest on August 1, 2001, and then monthly thereafter until payment in full of any principal outstanding under this line of credit.

(b) The Borrower will repay in full all principal and any unpaid interest or other charges outstanding under this line of credit no later than the Expiration Date. Any

interest period for an optional interest rate (as described below) shall expire no later than the Expiration Date.

1.5 Optional Interest Rates. Instead of the interest rate based on the Bank's Prime Rate, the Borrower may elect the optional interest rates listed below during interest periods agreed to by the Bank and the Borrower. The optional interest rates shall be subject to the terms and conditions described later in this Agreement. Any principal amount bearing interest at an optional rate under this Agreement is referred to as a "Portion." The following optional interest rates are available:

(a) the IBOR Rate plus one and three quarters (1.75) percentage points.

1.6 Letters of Credit.

(a) This line of credit may be used for financing:

(i) commercial letters of credit with a maximum maturity of 180 days but not to extend beyond the Expiration Date. Each commercial letter of credit will require drafts payable at sight.

(ii) standby letters of credit with a maximum maturity of 360 days but not to extend beyond the Expiration Date. Standby letters of credit shall not include any provision for automatic renewal or extension of the maturity date.

(b) The Borrower agrees:

(i) any sum drawn under a letter of credit may, at the option of the Bank, be added to the principal amount outstanding under this Agreement. The amount will bear interest and be due as described elsewhere in this Agreement.

(ii) if there is a default under this Agreement, or if any letter of credit remains outstanding beyond the Expiration Date, to immediately prepay and make the Bank whole for any outstanding letters of credit.

(iii) the issuance of any letter of credit and any amendment to a letter of credit is subject to the Bank's written approval and must be in form and content satisfactory to the Bank and in favor of a beneficiary acceptable to the Bank.

(iv) to sign the Bank's form Application and Agreement for Commercial Letter of Credit or Application and Agreement for Standby Letter of Credit, as applicable.

(v) to pay any issuance and/or other fees that the Bank notifies the Borrower will be charged for issuing and processing letters of credit for the Borrower.

(vi) to allow the Bank to automatically charge its checking account for applicable fees, discounts, and other charges.

(vii) to pay the Bank a non-refundable fee equal to 1.75% per annum of the outstanding undrawn amount of each standby letter of credit, payable quarterly in advance, calculated on the basis of the face amount outstanding on the day the fee is calculated. If there is a default under this Agreement, at the Bank's option, the amount of the fee shall be increased to 4.75% per annum, effective starting on the day the Bank provides notice of the increase to the Borrower.

2. OPTIONAL INTEREST RATES

2.1 Optional Rates. Each optional interest rate is a rate per year. Interest will be paid on the last day of each interest period, and, if the interest period is longer than one month, then on the last day of each month during the interest period. At the end of any interest period, the interest rate will revert to the rate based on the Prime Rate, unless the Borrower has designated another optional interest rate for the Portion. No Portion will be converted to a different interest rate during the applicable interest period. Upon the occurrence of an event of default under this Agreement, the Bank may terminate the availability of optional interest rates for interest periods commencing after the default occurs.

2.2 IBOR Rate. The election of IBOR Rates shall be subject to the following terms and requirements:

(a) The interest period during which the IBOR Rate will be in effect will be no shorter than 30 days and no longer than 90 days. The last day of the interest period will be determined by the Bank using the practices of the offshore dollar inter-bank market.

(b) Each IBOR Rate Portion will be for an amount not less than One Million Dollars (\$1,000,000).

(c) The "IBOR Rate" means the interest rate determined by the following formula, rounded upward to the nearest 1/100 of one percent. (All amounts in the calculation will be determined by the Bank as of the first day of the interest period.)

$$\text{IBOR Rate} = \frac{\text{IBOR Base Rate}}{(1.00 - \text{Reserve Percentage})}$$

Where,

(i) "IBOR Base Rate" means the interest rate at which the Bank's Grand Cayman Banking Center, Grand Cayman, British West Indies, would offer U.S. dollar deposits for the applicable interest period to other major banks in the offshore dollar inter-bank market.

(ii) "Reserve Percentage" means the total of the maximum reserve percentages for determining the reserves to be maintained by member banks of the Federal Reserve System for Eurocurrency Liabilities, as defined in Federal Reserve Board Regulation D, rounded upward to the nearest 1/100 of one percent. The percentage will be expressed as a decimal, and will include, but not be limited to, marginal, emergency, supplemental, special, and other reserve percentages.

(d) Each prepayment of an IBOR Rate Portion, whether voluntary, by reason of acceleration or otherwise, will be accompanied by the amount of accrued interest on the amount prepaid, and a prepayment fee as described below. A "prepayment" is a payment of an amount on a date earlier than the scheduled payment date for such amount as required by this Agreement.

(e) The prepayment fee shall be equal to the amount (if any) by which:

(i) the additional interest which would have been payable during the interest period on the amount prepaid had it not been prepaid, exceeds

(ii) the interest which would have been recoverable by the Bank by placing the amount prepaid on deposit in the domestic certificate of deposit market, the eurodollar deposit market, or other appropriate money market selected by the Bank for a period starting on the date on which it was prepaid and ending on the last day of the interest period for such Portion (or the scheduled payment date for the amount prepaid, if earlier).

(f) The Bank will have no obligation to accept an election for an IBOR Rate Portion if any of the following described events has occurred and is continuing:

(i) Dollar deposits in the principal amount, and for periods equal to the interest period, of an IBOR Rate Portion are not available in the offshore dollar inter-bank market; or

(ii) the IBOR Rate does not accurately reflect the cost of an IBOR Rate Portion.

3. FEES AND EXPENSES

3.1 Fees.

(a) Loan fee. The Borrower agrees to pay a loan fee in the amount of Ten Thousand Dollars (\$10,000.00). This fee is due on or before the date of this Agreement.

(b) Unused commitment fee. The Borrower agrees to pay a fee on any difference between the Commitment and the amount of credit it actually uses, determined by the weighted average credit outstanding during the specified period. The fee will be calculated at 0.10% per year. The calculation of credit outstanding shall include the undrawn amount of letters of credit.

This fee is due on September 30, 2001, and quarterly thereafter until the expiration of the availability period.

(c) Waiver Fee. If the Bank, at its discretion, agrees to waive or amend any terms of this Agreement, the Borrower will, at the Bank's option, pay the Bank a fee for each waiver or amendment in an amount advised by the Bank at the time the Borrower requests the waiver or amendment. Nothing in this paragraph shall imply that the Bank is obligated to agree to any waiver or amendment requested by the Borrower. The Bank may impose additional requirements as a condition to any waiver or amendment.

(d) Late Fee. To the extent permitted by law, the Borrower agrees to pay a late fee in an amount not to exceed four percent (4%) of any payment that is more than fifteen (15) days late. The imposition and payment of a late fee shall not constitute a waiver of the Bank's rights with respect to the default.

3.2 Expenses. The Borrower agrees to immediately repay the Bank for expenses that include, but are not limited to, filing, recording and search fees and documentation fees.

3.3 Reimbursement Costs. The Borrower agrees to reimburse the Bank for any expenses it incurs in the preparation of this Agreement and any agreement or instrument required by this Agreement. Expenses include, but are not limited to, reasonable attorneys' fees, including any allocated costs of the Bank's in-house counsel.

4. COLLATERAL

4.1 Personal Property. The Borrower's obligations to the Bank under this Agreement will be secured by personal property the Borrower now owns or will own in the future as listed below. The collateral is further defined in security agreement(s) executed by the Borrower.

(a) Bank of America time deposits in an amount not less than Ten Million Dollars (\$10,000,000.00).

5. DISBURSEMENTS, PAYMENTS AND COSTS

5.1 Requests for Credit. Each request for an extension of credit will be made in writing in a manner acceptable to the Bank, or by another means acceptable to the Bank.

5.2 Disbursements and Payments.

(a) Each payment by the Borrower will be made at the Bank's banking center (or other location) selected by the Bank from time to time; and will be made in immediately available funds, or such other type of funds selected by the Bank.

(b) Each disbursement by the Bank and each payment by the Borrower will be evidenced by records kept by the Bank. In addition, the Bank may, at its discretion, require the Borrower to sign one or more promissory notes.

5.3 Telephone and Telefax Authorization.

(a) The Bank may honor telephone or telefax instructions for advances or repayments or for the designation of optional interest rates and telefax requests for the issuance of letters of credit given, or purported to be given, by any one of the individuals authorized to sign loan agreements on behalf of the Borrower, or any other individual designated by any one of such authorized signers.

(b) Advances will be deposited in and repayments will be withdrawn from the Borrower's account number 14504-09078, or such other of the Borrower's accounts with the Bank as designated in writing by the Borrower.

(c) The Borrower will indemnify and hold the Bank harmless from all liability, loss, and costs in connection with any act resulting from telephone or telefax instructions the Bank reasonably believes are made by any individual authorized by the Borrower to give such instructions. This paragraph will survive this Agreement's termination, and will benefit the Bank and its officers, employees, and agents.

5.4 Direct Debit (Pre-Billing).

(a) The Borrower agrees that the Bank will debit the Borrower's deposit account number 14504-09078, or such other of the Borrower's accounts with the Bank as designated in writing by the Borrower (the "Designated Account") on the date each payment of principal and interest and any fees from the Borrower becomes due (the "Due Date").

(b) Approximately 10 days prior to each Due Date, the Bank will mail to the Borrower a statement of the amounts that will be due on that Due Date (the "Billed Amount"). The calculation will be made on the assumption that no new extensions of credit or payments will be made between the date of the billing statement and the Due Date, and that there will be no changes in the applicable interest rate.

(c) The Bank will debit the Designated Account for the Billed Amount, regardless of the actual amount due on that date (the "Accrued Amount"). If the Billed Amount debited to the Designated Account differs from the Accrued Amount, the discrepancy will be treated as follows:

(i) If the Billed Amount is less than the Accrued Amount, the Billed Amount for the following Due Date will be increased by the amount of the discrepancy. The Borrower will not be in default by reason of any such discrepancy.

(ii) If the Billed Amount is more than the Accrued Amount, the Billed Amount for the following Due Date will be decreased by the amount of the discrepancy.

Regardless of any such discrepancy, interest will continue to accrue based on the actual amount of principal outstanding without compounding. The Bank will not pay the Borrower interest on any overpayment.

(d) The Borrower will maintain sufficient funds in the Designated Account to cover each debit. If there are insufficient funds in the Designated Account on the date the Bank enters any debit authorized by this Agreement, the Bank may reverse the debit.

5.5 Banking Days. Unless otherwise provided in this Agreement, a banking day is a day other than a Saturday, Sunday or other day on which commercial banks are authorized to close, or are in fact closed, in the state where the Bank's lending office is located, and, if such day relates to amounts bearing interest at an offshore rate (if any), means any such day on which dealings in dollar deposits are conducted among banks in the offshore dollar interbank market. All payments and disbursements which would be due on a day which is not a banking day will be due on the next banking day. All payments received on a day which is not a banking day will be applied to the credit on the next banking day.

5.6 Taxes.

(a) If any payments to the Bank under this Agreement are made from outside the United States, the Borrower will not deduct any foreign taxes from any payments it makes to the Bank. If any such taxes are imposed on any payments made by the Borrower (including payments under this paragraph), the Borrower will pay the taxes and will also pay to the Bank, at the time interest is paid, any additional amount which the Bank specifies as necessary to preserve the after-tax yield the Bank would have received if such taxes had not been imposed. The Borrower will confirm that it has paid the taxes by giving the Bank official tax receipts (or notarized copies) within thirty (30) days after the due date.

5.7 Additional Costs. The Borrower will pay the Bank, on demand, for the Bank's costs or losses arising from any statute or regulation, or any request or requirement of a regulatory agency which is applicable to all national banks or a class of all national banks. The costs and losses will be allocated to the loan in a manner determined by the Bank, using any reasonable method. The costs include the following:

(a) any reserve or deposit requirements; and

(b) any capital requirements relating to the Bank's assets and commitments for credit.

5.8 Interest Calculation. Except as otherwise stated in this Agreement, all interest and fees, if any, will be computed on the basis of a 360-day year and the actual number of days elapsed. This results in more interest or a higher fee than if a 365-day year is used. Installments of principal which are not paid when due under this Agreement shall continue to bear interest until paid.

5.9 Default Rate. Upon the occurrence of any default under this Agreement, principal amounts outstanding under this Agreement will at the option of the Bank bear interest at a rate which is 3 percentage point(s) higher than the rate of interest otherwise provided under this Agreement. This will not constitute a waiver of any default.

5.10 Interest Compounding. At the Bank's sole option in each instance, any interest, fees or costs which are not paid when due under this Agreement shall bear interest from the due date at the Bank's Prime Rate plus 3 percentage points. This may result in compounding of interest.

6. CONDITIONS

The Bank must receive the following items, in form and content acceptable to the Bank, before it is required to extend any credit to the Borrower under this Agreement:

6.1 Authorizations. Evidence that the execution, delivery and performance by the Borrower of this Agreement and any instrument or agreement required under this Agreement have been duly authorized.

6.2 Governing Documents. A copy of the Borrower's articles of incorporation.

6.3 Security Agreements. Signed original security agreements, assignments, which the Bank requires.

6.4 Perfection and Evidence of Priority. Financing statements and fixture filings (and any collateral in which the Bank requires a possessory security interest), together with evidence that the security interests and liens in favor of the Bank are valid, enforceable, and prior to all others' rights and interests, except those the Bank consents to in writing.

6.5 Insurance. Evidence of insurance coverage, as required in the "Covenants" section of this Agreement.

6.6 Good Standing. Certificates of good standing for the Borrower from its state of formation and from any other state in which the Borrower is required to qualify to conduct its business.

6.7 Payment of Fees. Payment of all accrued and unpaid expenses incurred by the Bank as required by the paragraph entitled "Reimbursement Costs."

6.8 Other Items. Any other items that the Bank reasonably requires.

7. REPRESENTATIONS AND WARRANTIES

When the Borrower signs this Agreement, and until the Bank is repaid in full, the Borrower makes the following representations and warranties. Each request for an extension of credit constitutes a renewal of these representations and warranties as of the date of the request:

7.1 Organization of Borrower. The Borrower is a corporation duly formed and existing under the laws of the state where organized.

7.2 Authorization. This Agreement, and any instrument or agreement required hereunder, are within the Borrower's powers, have been duly authorized, and do not conflict with any of its organizational papers.

7.3 Enforceable Agreement. This Agreement is a legal, valid and binding agreement of the Borrower, enforceable against the Borrower in accordance with its terms, and any instrument or agreement required hereunder, when executed and delivered, will be similarly legal, valid, binding and enforceable.

7.4 Good Standing. In each state in which the Borrower does business, it is properly licensed, in good standing, and, where required, in compliance with fictitious name statutes.

7.5 No Conflicts. This Agreement does not conflict with any law, agreement, or obligation by which the Borrower is bound.

7.6 Financial Information. All financial and other information that has been or will be supplied to the Bank is sufficiently complete to give the Bank accurate knowledge of the Borrower's (and any guarantor's) financial condition, including all material contingent liabilities. Since the date of the most recent financial statement provided to the Bank, there has been no material adverse change in the business condition (financial or otherwise), operations, properties or prospects of the Borrower (or any guarantor).

7.7 Lawsuits. There is no lawsuit, tax claim or other dispute pending or threatened against the Borrower which, if lost, would impair the Borrower's financial condition or ability to repay the loan, except as have been disclosed in writing to the Bank.

7.8 Collateral. All collateral required in this Agreement is owned by the grantor of the security interest free of any title defects or any liens or interests of others, except those which have been approved by the Bank in writing.

7.9 Permits, Franchises. The Borrower possesses all permits, memberships, franchises, contracts and licenses required and all trademark rights, trade name rights, patent rights and fictitious name rights necessary to enable it to conduct the business in which it is now engaged.

7.10 Other Obligations. The Borrower is not in default on any obligation for borrowed money, any purchase money obligation or any other material lease, commitment, contract, instrument or obligation.

7.11 Tax Matters. The Borrower has no knowledge of any pending assessments or adjustments of its income tax for any year and all taxes due have been paid[, except as have been disclosed in writing to the Bank.

7.12 No Tax Avoidance Plan. The Borrower's obtaining of credit from the Bank under this Agreement does not have as a principal purpose the avoidance of U.S. withholding taxes.

7.13 No Event of Default. There is no event which is, or with notice or lapse of time or both would be, a default under this Agreement.

7.14 Insurance. The Borrower has obtained, and maintained in effect, the insurance coverage required in the "Covenants" section of this Agreement.

7.15 ERISA Plans.

(a) Each Plan (other than a multiemployer plan) is in compliance in all material respects with the applicable provisions of ERISA, the Code and other federal or state law. Each Plan has received a favorable determination letter from the IRS and to the best knowledge of the Borrower, nothing has occurred which would cause the loss of such qualification. The Borrower has fulfilled its obligations, if any, under the minimum funding standards of ERISA and the Code with respect to each Plan, and has not incurred any liability with respect to any Plan under Title IV of ERISA.

(b) There are no claims, lawsuits or actions (including by any governmental authority), and there has been no prohibited transaction or violation of the fiduciary responsibility rules, with respect to any Plan which has resulted or could reasonably be expected to result in a material adverse effect.

(c) With respect to any Plan subject to Title IV of ERISA:

(i) No reportable event has occurred under Section 4043(c) of ERISA for which the PBGC requires 30-day notice.

(ii) No action by the Borrower or any ERISA Affiliate to terminate or withdraw from any Plan has been taken and no notice of intent to terminate a Plan has been filed under Section 4041 of ERISA.

(iii) No termination proceeding has been commenced with respect to a Plan under Section 4042 of ERISA, and no event has occurred or condition exists which might constitute grounds for the commencement of such a proceeding.

(d) The following terms have the meanings indicated for purposes of this Agreement:

(i) "Code" means the Internal Revenue Code of 1986, as amended from time to time.

(ii) "ERISA" means the Employee Retirement Income Security Act of 1974, as amended from time to time.

(iii) "ERISA Affiliate" means any trade or business (whether or not incorporated) under common control with the Borrower within the meaning of Section 414(b) or (c) of the Code.

(iv) "PBGC" means the Pension Benefit Guaranty Corporation.

(v) "Plan" means a pension, profit-sharing, or stock bonus plan intended to qualify under Section 401(a) of the Code, maintained or contributed to by the Borrower or any ERISA Affiliate, including any multiemployer plan within the meaning of Section 4001(a)(3) of ERISA.

7.19 Location of Borrower. The Borrower's place of business (or, if the Borrower has more than one place of business, its chief executive office) is located at the address listed under the Borrower's signature on this Agreement.

8. COVENANTS

The Borrower agrees, so long as credit is available under this Agreement and until the Bank is repaid in full:

8.1 Use of Proceeds. To use the proceeds of the credit only for general corporate purposes.

8.2 Financial Information. To provide the following financial information and statements in form and content acceptable to the Bank, and such additional information as requested by the Bank from time to time:

(a) Within 90 days of the Borrower's fiscal year end, the Borrower's annual financial statements. These financial statements must be audited (with an unqualified opinion) by a Certified Public Accountant acceptable to the Bank. The statements shall be prepared on a consolidated basis.

(b) Within 45 days of the period's end (including the last period in each fiscal year), the Borrower's quarterly financial statements, certified and dated by an authorized financial officer of the Borrower. These financial statements may be Borrower prepared. The statements shall be prepared on a consolidated basis.

(c) Promptly, upon sending or receipt, copies of any management letters and correspondence relating to management letters, sent or received by the Borrower to or from the Borrower's auditor, or, if no management letter is prepared, a letter from such auditor stating that no deficiencies were noted that would otherwise be addressed in a management letter.

(d) Copies of the Borrower's Form 10-K Annual Report, Form 10-Q Quarterly Report and Form 8-K Current Report within 30 days after the date of filing with the Securities and Exchange Commission.

(e) Within the period(s) provided in (a) and (b) above, a compliance certificate of the Borrower, substantially in the form of Exhibit A hereto, signed by an authorized financial officer of the Borrower setting forth (i) the information and computations (in sufficient detail) to establish that the Borrower is in compliance with all financial covenants at the end of the period covered by the financial statements then being furnished and (ii) whether there existed as of the date of such financial statements and whether there exists as of the date of the certificate, any default under this Agreement and, if any such default exists, specifying the nature thereof and the action the Borrower is taking and proposes to take with respect thereto.

8.3 Financial Covenants.

(a) Deficit Earnings. Not incur on a consolidated basis deficit earnings before interest (both interest income and interest expense), taxes, and non-cash deferred compensation in excess of the amounts shown below in any quarterly accounting period indicted below:

Quarter Ending -----	Maximum Amount -----
June 30, 2001	\$11,500,000
September 30, 2001	4,500,000
December 31, 2001	2,300,000
March 31, 2002	1,200,000

(b) Positive Earnings. Commencing with the quarter ending June 30, 2002, maintain on a consolidated basis positive earnings before interest (both interest income and interest expense), taxes, and non-cash deferred compensation of at least Fifty Thousand Dollars (\$50,000.00).

8.4 Change of Control. Not to cause, permit or suffer to exist any Change of Control of the Borrower. For the purposes hereof, "Change of Control" means (i) each and every issue, sale, series of sales or other disposition or purchase or series of purchases of shares of voting stock of the Borrower which results in a Person or a group of Persons acting in concert obtaining majority voting control or the right to elect the majority of the Board of Directors of the Borrower, or (ii) the consolidation or merger by the Borrower with another corporation, other than a wholly-owned subsidiary of the Borrower, in a transaction in which any of the then outstanding voting stock of the Borrower is exchanged. For purposes hereof "Person" means an individual, partnership, corporation, trust or unincorporated organization.

8.5 Notices to Bank. To promptly notify the Bank in writing of:

(a) any lawsuit over Two Hundred Fifty Thousand Dollars (\$250,000) against the Borrower.

(b) any substantial dispute between the Borrower and any government authority.

(c) any event of default under this Agreement, or any event which, with notice or lapse of time or both, would constitute an event of default.

(d) any material adverse change in the Borrower's business condition (financial or otherwise), operations, properties or prospects, or ability to repay the credit.

(e) any change in the Borrower's name, legal structure, place of business, or chief executive office if the Borrower has more than one place of business.

8.6 Books and Records. To maintain adequate books and records.

8.7 Compliance with Laws. To comply with the laws (including any fictitious name statute), regulations, and orders of any government body with authority over the Borrower's business.

8.8 Preservation of Rights. To maintain and preserve all rights, privileges, and franchises the Borrower now has.

8.9 Maintenance of Properties. To make any repairs, renewals, or replacements to keep the Borrower's properties in good working condition.

8.10 Perfection of Liens. To help the Bank perfect and protect its security interests and liens, and reimburse it for related costs it incurs to protect its security interests and liens.

8.11 Cooperation. To take any action reasonably requested by the Bank to carry out the intent of this Agreement.

8.12 General Business Insurance.

(a) To maintain insurance satisfactory to the Bank as to amount, nature and carrier covering property damage (including loss of use and occupancy) to any of the Borrower's properties, public liability insurance including coverage for contractual liability, product liability, workers' compensation, business interruption and any other insurance which is usual for the Borrower's business.

(b) Evidence of Insurance. Upon the request of the Bank, to deliver to the Bank a copy of each insurance policy, or, if permitted by the Bank, a certificate of insurance listing all insurance in force.

8.13 Additional Negative Covenants. Not to, without the Bank's written consent:

(a) engage in any business activities substantially different from the Borrower's present business.

(b) liquidate or dissolve the Borrower's business.

(c) voluntarily suspend its business for more than 7 days in any 30 day period.

8.14 Bank as Principal Depository. To maintain the Bank as its principal depository bank, including for the maintenance of business, cash management, operating and administrative deposit accounts.

8.15 ERISA Plans. With respect to a Plan subject to Title IV of ERISA, to give prompt written notice to the Bank of:

(a) The occurrence of any reportable event under Section 4043(c) of ERISA for which the PBGC requires 30-day notice.

(b) Any action by the Borrower or any ERISA Affiliate to terminate or withdraw from a Plan or the filing of any notice of intent to terminate under Section 4041 of ERISA.

(c) The commencement of any proceeding with respect to a Plan under Section 4042 of ERISA.

9. HAZARDOUS SUBSTANCES

9.1 Indemnity Regarding Hazardous Substances. The Borrower will indemnify and hold harmless the Bank from any loss or liability the Bank incurs in connection with or as a result of this Agreement, which directly or indirectly arises out of the use, generation, manufacture, production, storage, release, threatened release, discharge, disposal or presence of a hazardous substance. This indemnity will apply whether the hazardous substance is on, under or about the Borrower's property or operations or property leased to the Borrower. The indemnity includes but is not limited to attorneys' fees (including the reasonable estimate of the allocated cost of in-house counsel and staff). The indemnity extends to the Bank, its parent, subsidiaries and all of their directors, officers, employees, agents, successors, attorneys and assigns.

9.2 Definition of Hazardous Substances. "Hazardous substances" means any substance, material or waste that is or becomes designated or regulated as "toxic," "hazardous," "pollutant," or "contaminant" or a similar designation or regulation under any federal, state or local law (whether under common law, statute, regulation or otherwise) or judicial or administrative interpretation of such, including without limitation petroleum or natural gas. This indemnity will survive repayment of the Borrower's obligations to the Bank.

10. DEFAULT

If any of the following events occurs, the Bank may do one or more of the following: declare the Borrower in default, stop making any additional credit available to the Borrower, and require the Borrower to repay its entire debt immediately and without prior notice. If an event of default occurs under the paragraph entitled "Bankruptcy," below, with respect to the Borrower, then the entire debt outstanding under this Agreement will automatically be due immediately.

10.1 Failure to Pay. The Borrower fails to make a payment under this Agreement when due.

10.2 Lien Priority. The Bank fails to have an enforceable first lien (except for any prior liens to which the Bank has consented in writing) on or security interest in any property given as security for this Agreement (or any guaranty).

10.3 False Information. The Borrower or any guarantor or any party pledging collateral to the Bank (each an "Obligor") has given the Bank false or misleading information or representations.

10.4 Bankruptcy. The Borrower (or any Obligor) files a bankruptcy petition, a bankruptcy petition is filed against the Borrower (or any Obligor) or the Borrower (or any Obligor) makes a general assignment for the benefit of creditors

10.5 Receivers. A receiver or similar official is appointed for a substantial portion of the Borrower's (or any Obligor's) business, or the business is terminated.

10.6 Government Action. Any government authority takes action that the Bank believes materially adversely affects the Borrower's (or any Obligor's) financial condition or ability to repay.

10.7 Material Adverse Change. A material adverse change occurs, or is reasonably likely to occur, in the Borrower's (or any Obligor's) business condition (financial or otherwise), operations, properties or prospects, or ability to repay the credit.

10.8 Cross-default. Any default occurs under any agreement in connection with any credit the Borrower (or any Obligor) has obtained from anyone else or which the Borrower (or any Obligor) has guaranteed in the amount of Five Hundred Thousand Dollars (\$500,000) or more in the aggregate if the default is not cured within thirty (30) days if the default consists of failing to make a payment when due or gives the other lender the right to accelerate the obligation.

10.9 Default under Related Documents. Any default occurs under any guaranty, subordination agreement, security agreement, deed of trust, mortgage, or other document required by or delivered in connection with this Agreement or any such document is no longer in effect, or any guarantor purports to revoke or disavow the guaranty.

10.10 Other Bank Agreements. The Borrower (or any Obligor) fails to meet the conditions of, or fails to perform any obligation under any other agreement the Borrower (or any Obligor) has with the Bank or any affiliate of the Bank.

10.11 ERISA Plans. Any one or more of the following events occurs with respect to a Plan of the Borrower subject to Title IV of ERISA, provided such event or events could reasonably be expected, in the judgment of the Bank, to subject the Borrower to any tax, penalty or liability (or any combination of the foregoing) which, in the aggregate, could have a material adverse effect on the financial condition of the Borrower:

(a) A reportable event shall occur under Section 4043(c) of ERISA with respect to a Plan.

(b) Any Plan termination (or commencement of proceedings to terminate a Plan) or the full or partial withdrawal from a Plan by the Borrower or any ERISA Affiliate.

10.12 Other Breach Under Agreement. The Borrower fails to meet the conditions of, or fails to perform any obligation under, any term of this Agreement not specifically referred to in this Article. This includes any failure or anticipated failure by the Borrower to comply with any financial covenants set forth in this Agreement, whether such failure is evidenced by financial statements delivered to the Bank or is otherwise known to the Borrower or the Bank

11. ENFORCING THIS AGREEMENT; MISCELLANEOUS

11.1 GAAP. Except as otherwise stated in this Agreement, all financial information provided to the Bank and all financial covenants will be made under generally accepted accounting principles, consistently applied.

11.2 California Law. This Agreement is governed by California law.

11.3 Successors and Assigns. This Agreement is binding on the Borrower's and the Bank's successors and assignees. The Borrower agrees that it may not assign this Agreement without the Bank's prior consent. The Bank may sell participations in or assign this loan, and may exchange financial information about the Borrower with actual or potential participants or assignees; provided that such actual or potential participants or assignees shall agree to treat all financial information exchanged as confidential. If a participation is sold or the loan is assigned, the purchaser will have the right of set-off against the Borrower.

11.4 Arbitration and Waiver of Jury Trial.

(a) This paragraph concerns the resolution of any controversies or claims between the Borrower and the Bank, whether arising in contract, tort or by statute, including but not limited to controversies or claims that arise out of or relate to: (i) this Agreement (including any renewals, extensions or modifications); or (ii) any document related to this Agreement (collectively a "Claim").

(b) At the request of the Borrower or the Bank, any Claim shall be resolved by binding arbitration in accordance with the Federal Arbitration Act (Title 9, U. S. Code) (the "Act"). The Act will apply even though this Agreement provides that it is governed by the law of a specified state.

(c) Arbitration proceedings will be determined in accordance with the Act, the applicable rules and procedures for the arbitration of disputes of JAMS or any successor thereof ("JAMS"), and the terms of this paragraph. In the event of any inconsistency, the terms of this paragraph shall control.

(d) The arbitration shall be administered by JAMS and conducted in any U. S. state where real or tangible personal property collateral for this credit is located or if there is no such collateral, in California. All Claims shall be determined by one arbitrator; however, if Claims exceed Five Million Dollars (\$5,000,000), upon the request of any party, the Claims shall be decided by three arbitrators. All arbitration hearings shall commence within ninety (90) days of the demand for arbitration and close within ninety (90) days of commencement and the award of the arbitrator(s) shall be issued within thirty (30) days of the close of the hearing. However, the arbitrator(s), upon a showing of good cause, may extend the commencement of the hearing for up to an additional sixty (60) days. The arbitrator(s) shall provide a concise written statement of reasons for the award. The arbitration award may be submitted to any court having jurisdiction to be confirmed and enforced.

(e) The arbitrator(s) will have the authority to decide whether any Claim is barred by the statute of limitations and, if so, to dismiss the arbitration on that basis. For purposes of the application of the statute of limitations, the service on JAMS under applicable JAMS rules of a notice of Claim is the equivalent of the filing of a lawsuit. Any dispute concerning this arbitration provision or whether a Claim is arbitrable shall be determined by the arbitrator(s). The arbitrator(s) shall have the power to award legal fees pursuant to the terms of this Agreement.

(f) This paragraph does not limit the right of the Borrower or the Bank to: (i) exercise self-help remedies, such as but not limited to, setoff; (ii) initiate judicial or nonjudicial foreclosure against any real or personal property collateral; (iii) exercise any judicial or power of sale rights, or (iv) act in a court of law to obtain an interim remedy, such as but not limited to, injunctive relief, writ of possession or appointment of a receiver, or additional or supplementary remedies.

(g) The procedure described above will not apply if the Claim, at the time of the proposed submission to arbitration, arises from or relates to an obligation to the Bank secured by real property. In this case, both the Borrower and the Bank must consent to submission of the Claim to arbitration. If both parties do not consent to arbitration, the Claim will be resolved as follows: The Borrower and the Bank will designate a referee (or a panel of referees) selected under the auspices of JAMS in the same manner as arbitrators are selected in JAMS administered proceedings. The designated referee(s) will be appointed by a court as provided in California Code of Civil Procedure Section 638 and the following related sections. The referee (or the presiding referee of the panel) will be an active attorney or a retired judge. The award that results from the decision of the referee(s) will be entered as a judgment in the court that appointed the referee, in accordance with the provisions of California Code of Civil Procedure Sections 644 and 645.

(h) The filing of a court action is not intended to constitute a waiver of the right of the Borrower or the Bank, including the suing party, thereafter to require submittal of the Claim to arbitration.

(i) By agreeing to binding arbitration, the parties irrevocably and voluntarily waive any right they may have to a trial by jury in respect of any Claim. Furthermore, without intending in any way to limit this agreement to arbitrate, to the extent any Claim is not arbitrated, the parties irrevocably and voluntarily waive any right they may have to a trial by jury in respect of such Claim. This provision is a material inducement for the parties entering into this Agreement.

11.5 Severability; Waivers. If any part of this Agreement is not enforceable, the rest of the Agreement may be enforced. The Bank retains all rights, even if it makes a loan after default. If the Bank waives a default, it may enforce a later default. Any consent or waiver under this Agreement must be in writing.

11.6 Administration Costs. The Borrower shall pay the Bank for all reasonable costs incurred by the Bank in connection with administering this Agreement.

11.7 Attorneys' Fees. The Borrower shall reimburse the Bank for any reasonable costs and attorneys' fees incurred by the Bank in connection with the enforcement or preservation of any rights or remedies under this Agreement and any other documents executed in connection with this Agreement, and in connection with any amendment, waiver, "workout" or restructuring under this Agreement. In the event of a lawsuit or arbitration proceeding, the prevailing party is entitled to recover costs and reasonable attorneys' fees incurred in connection with the lawsuit or arbitration proceeding, as determined by the court or arbitrator. In the event that any case is commenced by or against the Borrower under the Bankruptcy Code (Title 11, United States Code) or any similar or successor statute, the Bank is entitled to recover costs and reasonable attorneys' fees incurred by the Bank related to the preservation, protection, or enforcement of any rights of the Bank in such a case. As used in this paragraph, "attorneys' fees" includes the allocated costs of the Bank's in-house counsel.

11.8 One Agreement. This Agreement and any related security or other agreements required by this Agreement, collectively:

(a) represent the sum of the understandings and agreements between the Bank and the Borrower concerning this credit;

(b) replace any prior oral or written agreements between the Bank and the Borrower concerning this credit; and

(c) are intended by the Bank and the Borrower as the final, complete and exclusive statement of the terms agreed to by them.

event of any conflict between this Agreement and any other agreements required by this Agreement, this Agreement will prevail.

11.9 Waiver of Confidentiality. The Borrower authorizes the Bank to discuss the Borrower's financial affairs and business operations with any accountants, auditors, business consultants, or other professional advisors employed by the Borrower, and authorizes such parties to disclose to the Bank such financial and business information or reports (including management letters) concerning the Borrower as the Bank may request.

11.10 Indemnification. The Borrower will indemnify and hold the Bank harmless from any loss, liability, damages, judgments, and costs of any kind relating to or arising directly or indirectly out of (a) this Agreement or any document required hereunder, (b) any credit extended or committed by the Bank to the Borrower hereunder, and (c) any litigation or proceeding related to or arising out of this Agreement, any such document, or any such credit. This indemnity includes but is not limited to attorneys' fees (including the allocated cost of in-house counsel). This indemnity extends to the Bank, its parent, subsidiaries and all of their directors, officers, employees, agents, successors, attorneys, and assigns. This indemnity will

survive repayment of the Borrower's obligations to the Bank. All sums due to the Bank hereunder shall be obligations of the Borrower, due and payable immediately without demand.

11.11 Notices. Unless otherwise provided in this Agreement or in another agreement between the Bank and the Borrower, all notices required under this Agreement shall be personally delivered or sent by first class mail, postage prepaid, or by overnight courier, to the addresses on the signature page of this Agreement, or sent by facsimile to the fax numbers listed on the signature page, or to such other addresses as the Bank and the Borrower may specify from time to time in writing. Notices and other communications sent by (a) first class mail shall be deemed delivered on the earlier of actual receipt or on the fourth business day after deposit in the U.S. mail, postage prepaid, (b) overnight courier shall be deemed delivered on the next business day, and (c) telecopy shall be deemed delivered when transmitted.

11.12 Headings. Article and paragraph headings are for reference only and shall not affect the interpretation or meaning of any provisions of this Agreement.

11.13 Counterparts. This Agreement may be executed in as many counterparts as necessary or convenient, and by the different parties on separate counterparts each of which, when so executed, shall be deemed an original but all such counterparts shall constitute but one and the same agreement.

This Agreement is executed as of the date stated at the top of the first page.

Bank of America, N.A.

Novatel Wireless, Inc.

By: /s/ Susan J. Pepping

Typed Name: Susan J. Pepping

Title: Senior Vice President

By: /s/ Dan L. Halvorson

Typed Name: Dan L. Halvorson

Title: Treasurer

By: /s/ Melvin L. Flowers

Typed Name: Melvin L. Flowers

Title: Senior Vice President and CFO

Address where notices to
the Bank are to be sent:
450 B Street, Suite 100
San Diego, CA 92101
Facsimile: (619) 515-7524

Address where notices to
the Borrower are to be sent:
9360 Towne Center Drive, Suite 110
San Diego, CA 92121
Facsimile: 858/812-3414

FIRST AMENDMENT TO BUSINESS LOAN AGREEMENT

This First Amendment to Business Loan Agreement (the "Amendment") is made as of July 10, 2001, between Bank of America, N. A. ("Bank"), and Novatel Wireless, Inc. ("Borrower").

RECITALS

A. Borrower and Bank entered into that certain Business Loan Agreement dated as of June 28, 2001 (the "Agreement").

B. Borrower and Bank desire to amend certain terms and provisions of the Agreement.

AGREEMENT

1. Definitions. Capitalized terms used but not defined in this Amendment shall have the meaning given to them in the Agreement.

2. Amendments. The Agreement is hereby amended as follows:

2.1 Paragraph 1.6(a) of the Agreement is amended to add clause (iii) to read as follows:

"(iii) The amounts of letters of credit outstanding at any one time (including amounts drawn on letters of credit and not yet reimbursed) may not exceed Five Million Dollars (\$5,000,000.00)."

3. Representations and Warranties. Borrower hereby represents and warrants to Bank that: (i) no default specified in the Agreement and no event which with notice or lapse of time or both would become such a default has occurred and is continuing and (ii) the representations and warranties of Borrower pursuant to the Agreement are true on and as of the date hereof as if made on and as of said date.

4. Effect of Amendment. Except as provided in this Amendment, the Agreement shall remain in full force and effect and shall be performed by the parties hereto according to its terms and provisions.

IN WITNESS WHEREOF, this Amendment has been executed by the parties hereto as of the date first above written.

BANK OF AMERICA, N.A.

By: /s/ Susan J. Pepping

Name: SUSAN J. PEPPING

Title: Senior Vice President

NOVATEL WIRELESS, INC.

By: /s/ Dan L. Halvorson

Name: Dan L. Halvorson

Title: Treasurer

By: /s/ Melvin L. Flowers

Name: Melvin L. Flowers

Title: Senior Vice President and CFO
