AGERE SYSTEMS INC
Form 424B4
June 14, 2002

Filed Pursuant to Rule 424(b)(2)
Registration No. 333-81632

PROSPECTUS

$410,000,000

[AGERE SYSTEMS LOGO]
6.5% CONVERTIBLE SUBORDINATED NOTES DUE 2009

Interest on the notes is payable on June 15 and December 15 of each year, beginning on December 15, 2002.

Holders may convert their notes into shares of our Class A common stock at an initial conversion price of $3.3075 per share (subject to adjustment in certain events) at any time following issuance of the notes, unless we have previously redeemed or repurchased the notes or unless the notes have matured.

The notes will mature on December 15, 2009. We may redeem the notes in whole or in part at any time on or after June 20, 2007. Redemption prices are set forth under "Description of Notes -- Optional Redemption."

Holders may require us to repurchase all or a portion of their notes upon a fundamental change involving us at a repurchase price equal to 100% of the principal amount of the notes to be repurchased plus any accrued and unpaid interest to, but not including, the repurchase date.

We have also granted the underwriters an option to purchase up to an additional $40.812 million principal amount of the notes to cover over-allotments.

The notes will be unsecured subordinated obligations and will be subordinated in right of payment to all our existing and future senior debt, including our bank debt.

Our Class A common stock is listed on the New York Stock Exchange under the symbol "AGR.A." The last reported sale price of our Class A common stock on June 13, 2002 was $2.45 per share. The notes will not be listed on any securities exchange.

INVESTING IN THE NOTES INVOLVES RISKS. SEE "RISK FACTORS" BEGINNING ON PAGE 8.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

	PER NOTE	TOTAL
Public offering price......................................	100.00%	$410,000,000
Underwriting discount......................................	2.95%	$ 12,095,000
Proceeds to Agere Systems Inc.	97.05%	$397,905,000

Interest on the notes will accrue from June 19, 2002.

The underwriters expect to deliver the notes in book-entry form through The Depository Trust Company to purchasers on or about June 19, 2002.

JPMORGAN SALOMON SMITH BARNEY

CREDIT SUISSE FIRST BOSTON DEUTSCHE BANK SECURITIES SG COWEN

ABN AMRO ROTHSCHILD LLC BNY CAPITAL MARKETS, INC.

June 13, 2002

YOU SHOULD RELY ONLY ON THE INFORMATION CONTAINED OR INCORPORATED BY REFERENCE IN THIS PROSPECTUS. WE HAVE NOT AUTHORIZED ANYONE TO PROVIDE YOU WITH DIFFERENT INFORMATION. WE ARE NOT MAKING AN OFFER OF THESE SECURITIES IN ANY JURISDICTION WHERE THE OFFER IS NOT PERMITTED. YOU SHOULD NOT ASSUME THAT THE INFORMATION CONTAINED IN THIS PROSPECTUS IS ACCURATE AS OF ANY DATE OTHER THAN THE DATE ON THE FRONT OF THIS PROSPECTUS.

TABLE OF CONTENTS

	PAGE
Industry Data	i
Forward-Looking Statements	ii
Summary	1
Risk Factors	8
Use of Proceeds	20
Capitalization	21
Common Stock Price Range and Dividends	22
Selected Financial Information	23
Management's Discussion and Analysis of Financial Condition and Results of Operations	25
Business	50
Management	67
Arrangements Between Lucent and Our Company	70
Principal Stockholders	82
Certain Indebtedness	83
Description of Notes	85
Description of Common Stock	103
Material Federal Income Tax Consequences	111
Underwriting	115
Legal Matters	117
Experts	117
Where You Can Find More Information	117
Index to Financial Statements	F-1

This prospectus contains trademarks, service marks and registered marks of Agere Systems Inc.

INDUSTRY DATA

In this document, we rely on and refer to information regarding the semiconductor market and its segments and competitors from (1) Gartner Dataquest Alert: Communications Semiconductor and Optical Component Market Share in 2000, issued on June 11, 2001, (2) Gartner, Wireless Communications Semiconductor Competitive Market Shares for 2000, issued on August 29, 2001, (3) Gartner, Wired Communications Semiconductor and Optical Component Market Share, 2000, issued on July 13, 2001, (4) analyst reports and (5) other publicly available sources. Gartner Dataquest is not aware of, and has not consented to, being named in this document. Although we believe that this information is reliable, we have not independently verified the accuracy and completeness of this information.

FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements that are based on current expectations, estimates, forecasts and projections about the industry in which we operate, management's beliefs and assumptions made by management. Such statements include, in particular, statements about our plans, strategies and prospects under the headings "Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Business." Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. We do not have any intention or obligation to update publicly any forward-looking statements after we distribute this prospectus, whether as a result of new information, future events or otherwise.

The assumptions underlying the information on our market segments and product areas have been derived from information currently available to us. If any one or more of these assumptions are incorrect, actual market results may differ from those we expect. While we do not know what impact any such differences may have on our businesses, our future results of operations and financial condition may be materially adversely affected. In addition, we generally cannot assure you that the forward-looking information regarding our market segments and product areas will be achieved, whether or not the assumptions are correct. Conditions in our industry change rapidly and such information must be continually evaluated in light of then current conditions. For a description of recent changes in conditions in our industry, please see "Risk Factors -- Risks Related to Our Business -- The demand for products in our industry has recently declined, and we cannot predict the duration or extent of this trend."

SUMMARY

The following is a summary of some of the information contained in this prospectus. In addition to this summary, we urge you to read the entire prospectus carefully, especially the risks of investing in our notes discussed under "Risk Factors" and our combined and consolidated financial statements and notes to our combined and consolidated financial statements included elsewhere in this prospectus.

We describe in this prospectus the businesses contributed to us by Lucent Technologies Inc. as part of our separation from Lucent as if they were our businesses for all historical periods prior to Lucent's contribution to us of the assets and liabilities related to those businesses, which began on February 1, 2001. Please see "Arrangements Between Lucent and Our Company" for a description of this separation. Our historical financial results as part of Lucent contained in this prospectus may not reflect our financial results in the future as a stand-alone company or what our financial results would have been had we been a stand-alone company during the periods presented. Our fiscal year ends on September 30.

AGERE SYSTEMS

OUR COMPANY

Agere Systems designs, develops and manufactures integrated circuits for use in a broad range of communications and computer systems and optoelectronic components for communications networks. We are the world leader in sales of communications components, which include both integrated circuits and optoelectronic components. Communications components are basic building blocks of electronic and photonic products and systems for terrestrial and submarine, or undersea, communications networks and for communications equipment.

As of March 31, 2002, we employed approximately 11,700 people worldwide. We have major research and development and manufacturing sites in the United States, Mexico, Singapore and Thailand. We had revenue of $1,088 million, a net loss of $594 million, net cash used in operating activities of $454 million and EBITDA, on an adjusted basis, of $(286) million for the six months ended March 31, 2002. We had revenue of $4,080 million, a net loss of $4,616 million, net cash provided by operating activities of $269 million and EBITDA, on an adjusted basis, of $(96) million in fiscal 2001. EBITDA equals operating income (loss) plus depreciation and amortization expense. Adjusted EBITDA equals EBITDA plus purchased in-process research and development, net restructuring and separation charges and impairment of goodwill and other acquired intangibles. EBITDA is not intended to represent cash flow or any other measure of performance or liquidity in accordance with generally accepted accounting principles. EBITDA is included here because we believe that you may find it to be a useful analytical tool. Other companies may calculate EBITDA differently, and we cannot assure you that our figures are comparable with similarly-titled figures for other companies.

Our business operations are organized into two market-focused groups, Client Systems and Infrastructure Systems, that target the consumer communications and network equipment markets, respectively. Each of these two groups is a reportable operating segment.

The Client Systems segment includes our wireless data, computer communications, storage and wireless terminal solutions products. This segment delivers integrated circuit solutions for a variety of end-user applications such as modems, Internet-enabled cellular terminals and hard-disk drives for computers as well as software, systems and wireless local area network solutions through the ORiNOCO(R) product family. Our Client Systems segment generated revenue of $599 million and $1,406 million for the six months ended March 31, 2002 and the year ended September 30, 2001, respectively.

The Infrastructure Systems segment delivers solutions to the high-speed communications systems market and facilitates the convergence of integrated circuit devices and optoelectronic components. We have consolidated research and development, as well as marketing, for both optoelectronic and integrated circuit devices aimed at communications systems. This allows us to design, develop and deliver complete, interoperable solutions to equipment manufacturers for advanced enterprise, access, metropolitan, long-haul and undersea applications. Our Infrastructure Systems segment generated revenue of $489 million and $2,674 million for the six months ended March 31, 2002 and the year ended September 30, 2001, respectively.

We sell integrated circuits for use in a broad range of communications networks and computer equipment. Integrated circuits, or chips, are made using semiconductor wafers imprinted with a network of electronic components. They are designed to perform various functions such as processing electronic signals, controlling electronic system functions and processing and storing data.

We also sell active optoelectronic components to manufacturers of communications equipment. Optoelectronic components transmit, process, change, amplify and receive light that carries data and voice traffic over optical networks. Optical networks transmit information as pulses of light, or optical signals, through optical fibers, which are hair-thin glass strands. An optical network utilizes a number of interdependent active optoelectronic and passive optical components. An active component is a device that has both optical and electronic properties. A passive component is a device that functions only in the optical domain. In addition to our broad portfolio of active optoelectronic components, we have started to sell some passive components.

OUR RELATIONSHIP WITH LUCENT

Agere was formed as part of Lucent Technologies' plan to spin-off to its stockholders its microelectronics business, including its integrated circuits and optoelectronics divisions. Our Class A common stock began trading on the New York Stock Exchange following our initial public offering in March 2001. The separation of our business from Lucent's other businesses was substantially completed, including the transfer of all assets and liabilities related to these divisions (other than pension and postretirement plan assets and liabilities) when we completed our initial public offering. On June 1, 2002, Lucent completed our spin-off, distributing to its stockholders all of the Class A common stock and Class B common stock it held on that date. See "Arrangements Between Lucent and Our Company" for further information about our spin-off and our relationship with Lucent.

2

THE OFFERING

ISSUER........................	Agere Systems Inc., a Delaware corporation.
SECURITIES OFFERED............	$410 million aggregate principal amount of 6.5% Convertible Subordinated Notes due 2009. We have also granted the underwriters an over-allotment option to purchase up to $40.812 million aggregate principal amount of the notes.
OFFERING PRICE................	100% of the principal amount of the notes plus accrued interest from June 19, 2002.
MATURITY......................	December 15, 2009, unless earlier redeemed, repurchased or converted. The principal amount of the notes will be paid in cash.
INTEREST......................	The notes will bear interest at an annual rate of 6.5%. Interest on the notes will be paid in

cash.

INTEREST PAYMENT DATES........	Interest will be payable semi-annually on June 15 and December 15 of each year, beginning on December 15, 2002.
CONVERSION RIGHTS.............	The notes are convertible at the option of the holder, at any time after the initial date of issuance and prior to redemption, repurchase or maturity, into our Class A common stock at an initial conversion price of $3.3075 per share, subject to adjustment in certain events. See "Description of Notes -- Conversion." The right to convert notes that have been called for redemption will terminate at the close of business on the business day immediately preceding the date of redemption.
REDEMPTION AT THE OPTION OF AGERE.........................	On or after June 20, 2007, at any time or from time to time, we may redeem the notes in cash at our option, in whole or in part, on not less than 30 nor more than 60 days' prior written notice to the holders by first-class mail, in cash at the redemption prices set forth herein, plus accrued and unpaid interest to, but not including, the date of the redemption. See "Description of Notes -- Optional Redemption."
REPURCHASE AT THE OPTION OF HOLDERS UPON THE OCCURRENCE OF A FUNDAMENTAL CHANGE..........	Upon a fundamental change, which includes a termination of trading and certain change of control events, each holder of the notes will have the right, subject to certain restrictions and conditions, to require us to repurchase in cash all or any part of such holder's notes at a repurchase price equal to 100% of the principal amount thereof, plus accrued and unpaid interest to, but not including, the date of repurchase. See "Description of Notes -- Fundamental Change Permits Holders to Require Us to Repurchase Notes" and "Risk Factors -- Risks Relating to the Offering -- Even if a fundamental change occurs triggering our obligation to repurchase the notes, we may not be able to repurchase the notes."

SUBORDINATION................	The notes will be our unsecured subordinated obligations. The notes will be subordinated in right of payment to all existing and future senior indebtedness, including our credit facility.
	Assuming we had completed this offering as of March 31, 2002 and applied the net proceeds as described in "Use of Proceeds" and the repayment of an additional $540 million of

	borrowings under the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources," the notes would have been subordinated to approximately $222 million of senior indebtedness. The notes will also be effectively subordinated to all indebtedness and other liabilities of our subsidiaries. The total balance sheet liabilities of our subsidiaries were approximately $515 million at March 31, 2002. The indenture under which the notes will be issued contains no limitation on the amount of indebtedness or other liabilities, including senior or secured indebtedness, that we or our subsidiaries may incur.
USE OF PROCEEDS...............	We intend to use approximately 50% of the net proceeds from this offering to repay a portion of the short-term debt outstanding under our credit facility and the balance for general corporate purposes.
TRADING.......................	We do not intend to apply for listing of the notes on any securities exchange or for inclusion of the notes in any automated quotation system. Our Class A common stock is listed on the New York Stock Exchange under the symbol "AGR.A."
SINKING FUND..................	None.
TRUSTEE.......................	The Bank of New York.

RISK FACTORS

See "Risk Factors," which begins on page 8, for a discussion of certain factors that you should consider in evaluating an investment in the notes.

Our principal executive offices are located at 555 Union Boulevard, Allentown, Pennsylvania 18109. Our telephone number is (610) 712-4323. Our World Wide Web site address is www.agere.com. Information contained in our website is not incorporated by reference in this prospectus and, therefore, is not part of this prospectus.

SUMMARY HISTORICAL FINANCIAL INFORMATION

The following table sets forth our summary historical financial information derived from our unaudited financial statements for the six month periods ended March 31, 2002 and 2001, and our audited financial statements for the fiscal years ended September 30, 2001, 2000 and 1999 included elsewhere in this prospectus. This summary financial information may not be indicative of our future performance as a stand-alone company. You should read the summary financial information in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations," our financial statements and the notes thereto included elsewhere in this prospectus.

	SIX MONTHS ENDED MARCH 31,		YEAR ENDED SEPTEMBER 30,		
	2002	2001	2001	2000	1999
	(DOLLARS IN MILLIONS)				
STATEMENT OF OPERATIONS INFORMATION:					
Revenue:					
Client Systems	$ 599	$ 769	$ 1,406	$1,649	$1,424
Infrastructure Systems	489	1,784	2,674	3,059	2,290
Total revenue	1,088	2,553	4,080	4,708	3,714
Costs	1,019	1,532	3,084	2,555	1,949
Gross profit	69	1,021	996	2,153	1,765
Operating expenses:					
Selling, general and administrative	199	336	597	535	573
Research and development	377	537	951	827	683
Purchased in-process research and development	--	--	--	446	17
Amortization of goodwill and other acquired intangibles	37	223	415	189	13
Restructuring and separation -- net	96	47	662	--	--
Impairment of goodwill and other acquired intangibles	176	--	2,762	--	--
Total operating expenses	885	1,143	5,387	1,997	1,286
Operating income (loss)	(816)	(122)	(4,391)	156	479
Cumulative effect of accounting change (net of provision (benefit) for income taxes)	--	(4)	(4)	--	32
Net income (loss)	(594)	(152)	(4,616)	(76)	351
OTHER FINANCIAL DATA:					
Net cash (used in) provided by operating activities	$ (454)	$ 369	$ 269	$ 762	$ 690
Ratio of earnings to fixed charges(1)	n/a	n/a	n/a	2.4	8.7
Deficiency(1)	$ 584	160	$ 4,553	n/a	n/a
SUPPLEMENTAL FINANCIAL DATA:					
EBITDA(2)	$ (558)	$ 320	$(3,520)	$ 822	$ 877
Adjusted EBITDA(3)	(286)	367	(96)	1,268	894

footnotes on next page

	MARCH 31, 2002		SEPTEMBER 30
	HISTORICAL	AS ADJUSTED(4)	HISTORIC
	(DOLLARS IN MILLIONS)		

BALANCE SHEET INFORMATION:			
Cash	$1,604	$1,293	$3,152
Working capital	93	494	156
Total assets	4,291	3,989	6,562
Short-term debt	1,111	400	2,516
Long-term debt	26	436	33
Total stockholders' equity	1,910	1,910	2,461

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(1) For purposes of determining the ratio of earnings to fixed charges, "earnings" are defined as income (loss) from continuing operations before income taxes less undistributed earnings of equity investments plus fixed charges less interest capitalized during the period. "Fixed charges" consist of interest expense on all indebtedness and that portion of operating lease rental expense that is representative of the interest factor. "Deficiency" is the amount by which fixed charges exceeded earnings.

(2) EBITDA equals operating income (loss) plus depreciation and amortization expense. EBITDA is not intended to represent cash flow or any other measure of performance or liquidity in accordance with generally accepted accounting principles. EBITDA is included here because we believe that you may find it to be a useful analytical tool. Other companies may calculate EBITDA differently, and we cannot assure you that our figures are comparable with similarly-titled figures for other companies.

(3) The calculation of adjusted EBITDA is shown below:

	SIX MONTHS ENDED MARCH 31,		YEAR ENDED SEPTEMBER 30,		
	2002	2001	2001	2000	1999
	(DOLLARS IN MILLIONS)				
EBITDA	$(558)	$320	$(3,520)	$ 822	$877
Purchased in-process research and development	--	--	--	446	17
Restructuring and separation -- net	96	47	662	--	--
Impairment of goodwill and other acquired intangibles	176	--	2,762	--	--
Adjusted EBITDA	$(286)	$367	$ (96)	$1,268	$894

(4) The "as adjusted" information is derived from data contained in our historical financial statements which has been adjusted to give pro forma effect to the issuance and sale of the notes and the application of the net proceeds therefrom as described under "Use of Proceeds" and the repayment of an additional $540 million of the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources," as if such transactions had occurred as of March 31, 2002.

RISK FACTORS

An investment in the notes is subject to a number of risks. You should carefully consider the following risk factors and all the other information contained in this prospectus before investing in our notes.

RISKS RELATED TO OUR SEPARATION FROM LUCENT

OUR HISTORICAL FINANCIAL INFORMATION PRIOR TO THE FEBRUARY 1, 2001 CONTRIBUTION TO US OF OUR BUSINESS FROM LUCENT MAY NOT BE REPRESENTATIVE OF OUR RESULTS AS A STAND-ALONE COMPANY AND, THEREFORE, MAY NOT BE RELIABLE AS AN INDICATOR OF OUR HISTORICAL OR FUTURE RESULTS.

Our historical consolidated and combined financial statements may not be indicative of our future performance as a stand-alone company. This is primarily a result of the three factors described below.

- First, our historical consolidated and combined financial statements reflect allocations, primarily with respect to general corporate expenses, research expense and interest expense, which may be less than the expenses we will incur in the future as a stand-alone company.

- Second, the information does not reflect significant changes that we expect to occur in the future as a result of our separation from Lucent, including changes in how we fund our operations, conduct research and handle tax and employee matters.

- Third, our historical consolidated and combined financial statements include substantial revenue from sales to Lucent. This revenue may not reflect the pricing, volume or percentage of our sales we would have derived from Lucent if we were a stand-alone company.

BECAUSE LUCENT'S BELL LABORATORIES' CENTRAL RESEARCH ORGANIZATION HISTORICALLY PERFORMED IMPORTANT RESEARCH FOR US, WE MUST CONTINUE TO DEVELOP OUR OWN CORE RESEARCH CAPABILITY. WE MAY NOT BE SUCCESSFUL, WHICH COULD MATERIALLY HARM OUR PROSPECTS AND ADVERSELY AFFECT OUR RESULTS OF OPERATIONS.

If our separate research efforts are not as successful as when we were part of Lucent, we may not be able to keep pace with the rapid technological change in our industry and our prospects may be harmed. Many of our products use technology and manufacturing processes derived from innovations developed by Lucent's Bell Laboratories central research organization. After the contribution to us of our business in February 2001, Lucent has no obligation to provide research and development for us except as agreed to in the development project agreement and joint design center operating agreement described under "Arrangements Between Lucent and Our Company." We cannot assure you that our independent research efforts will be as successful as the efforts of Bell Laboratories have been historically or that our efforts will not require us to increase our expenditures for the same services over the amounts in our historical combined and consolidated financial statements. A significant increase in our expenditures for the same services may adversely affect our results of operations. We may not be able to recruit engineers and other research and development employees as effectively as Bell Laboratories was able to because of its history, name recognition and size.

WE COULD INCUR SIGNIFICANT TAX LIABILITY IF LUCENT FAILS TO PAY THE TAX LIABILITIES ATTRIBUTABLE TO LUCENT UNDER OUR TAX SHARING AGREEMENT, WHICH COULD REQUIRE US TO PAY A SUBSTANTIAL AMOUNT OF MONEY.

We and Lucent have entered into a tax sharing agreement that allocates responsibility for tax liabilities between us and them. For a discussion of this agreement, please see "Arrangements Between Lucent and Our Company -- Agreements Providing for the Separation of Our Businesses from Lucent -- Tax Sharing Agreement." Under U.S. federal income tax laws, we and Lucent are jointly and severally liable for Lucent's federal income taxes attributable to periods prior to and including the most recent taxable year of Lucent, which ended on September 30, 2001. This means that if Lucent fails to pay the taxes attributable to it under the tax sharing agreement for those periods, we may be liable for any part of, including the whole amount of, these liabilities.

BECAUSE THE DIVISION OF ENFORCEMENT OF THE SECURITIES AND EXCHANGE COMMISSION IS INVESTIGATING MATTERS BROUGHT TO ITS ATTENTION BY LUCENT, OUR BUSINESS MAY BE AFFECTED IN A MANNER WE CANNOT FORESEE AT THIS TIME.

On November 21, 2000, and again on December 21, 2000, Lucent brought to the attention of the staff of the Securities and Exchange Commission matters relating to its recognition of revenue. Lucent also publicly disclosed these matters in press releases on those dates. Although Lucent has informed us that it has no reason to believe that this investigation by the Division of Enforcement of the Securities and Exchange Commission into these matters concerns our business and we are not aware of any reason why the investigation would affect us, it is possible that the results of the investigation may have an impact on us. Although the investigation could result in no action being taken by the Securities and Exchange Commission, if an action is taken and the investigation is found to concern our business, the action could result in monetary fines or changes in some of our financial and other practices and procedures that we are unable to foresee at this time.

WE ARE LIMITED IN THE AMOUNT OF STOCK THAT WE CAN ISSUE TO RAISE CAPITAL BECAUSE OF POTENTIAL ADVERSE TAX CONSEQUENCES.

Under Section 355(e) of the Internal Revenue Code, Lucent will recognize taxable gain on the distribution of our stock if there are one or more acquisitions of our stock representing 50% or more of our stock (by vote or value) and the stock acquisitions are part of a plan or series of related transactions that includes the distribution. Any shares of our stock acquired within two years before or after the distribution are presumed to be part of such a plan unless we can rebut that presumption. If an issuance of our stock causes the distribution to be taxable to Lucent under Section 355(e), we would be required to indemnify Lucent against that tax under the tax sharing agreement.

The shares of our Class A common stock issued in our initial public offering are considered to be part of a plan that includes the distribution, and the shares of our Class A common stock issued upon the conversion of the notes included in this offering may also be considered to be part of a plan that includes the distribution. We do not currently intend to enter into transactions whereby more than 47% of our outstanding shares may be treated as acquired as part of a plan that includes the distribution. After the completion of this offering, approximately 47% of our outstanding shares may be treated as acquired as part of such a plan. As a practical matter, this prevents us from effecting any significant issuance of our shares if such issuance might be treated as part of a plan that includes the distribution.

Treasury Regulations issued on April 24, 2002 provide safe harbors that may be used to rebut the presumption that shares issued less than two years after the spin-off are part of a plan that includes the spin-off. However, the application of the safe harbors is not clear in many respects, and they might not be available to us for future share issuances. As a result, Section 355(e) may effectively prevent us from issuing shares to raise capital for at least two years after the spin-off. See "Arrangements Between Lucent and Our Company -- Tax Limitations on Additional Issuances of Our Stock." However, the safe harbors in these new Treasury Regulations generally provide that issuances of our stock to our employees pursuant to ordinary course employee compensation arrangements (such as employee stock purchase plans) will not be treated as acquisitions of our stock pursuant to a plan that includes the spin-off.

RISKS RELATED TO OUR BUSINESS

THE DEMAND FOR PRODUCTS IN OUR INDUSTRY HAS RECENTLY DECLINED, AND WE CANNOT PREDICT THE DURATION OR EXTENT OF THIS TREND. SALES OF OUR INTEGRATED CIRCUITS AND OPTOELECTRONIC COMPONENTS ARE DEPENDENT ON THE GROWTH OF COMMUNICATIONS NETWORKS.

We derive, and expect to continue to derive, a significant amount of revenue from the sale of integrated circuits and optoelectronic components used in optical, wired and wireless communications networks. The current economic downturn has resulted in reduced purchasing in many of the markets we serve worldwide. In particular, the communications equipment industry is currently in a cycle characterized by diminished product demand, excess manufacturing capacity and the erosion of average selling prices. If

the long-term growth in demand for communications networks does not occur as we expect, the demand for many of our integrated circuits and optoelectronic components may decline or grow more slowly than we expect. As a result, we may not be able to grow our business and our revenue may decline from current levels.

IF WE DO NOT COMPLETE OUR ANNOUNCED RESTRUCTURING AND FACILITY CONSOLIDATION ACTIVITIES AS EXPECTED OR EVEN IF WE DO SO, WE MAY NOT ACHIEVE ALL OF THE EXPENSE REDUCTIONS WE ANTICIPATE.

Our business has been experiencing lower revenues due to decreased and canceled customer orders. Our revenue declined significantly in fiscal 2001 and the first quarter of fiscal 2002. During fiscal 2001 and the first quarter of fiscal 2002, we announced a series of restructuring initiatives to align Agere with market conditions. These initiatives are focused on improving gross profit, reducing expenses and streamlining operations. These restructuring initiatives include a worldwide workforce reduction, rationalization of manufacturing capacity and other restructuring initiatives. In addition, we are consolidating our operations at a number of facilities. If we do not complete these restructuring and consolidation activities as expected or even if we do so, we may not achieve all of the expense reductions we anticipate.

BECAUSE WE EXPECT TO CONTINUE TO DERIVE A MAJORITY OF OUR REVENUE FROM SEMICONDUCTOR DEVICES AND THE INTEGRATED CIRCUITS INDUSTRY IS HIGHLY CYCLICAL, OUR REVENUE MAY FLUCTUATE.

We expect to continue to derive a majority of our revenue from integrated circuits products. Because the integrated circuits market segment is highly cyclical, we may have declines in our revenue that are primarily related to industry conditions and not our products. This market segment has experienced significant downturns, often in connection with, or in anticipation of, excess manufacturing capacity worldwide, maturing product cycles and declines in general economic conditions, and we are currently experiencing such a downturn. Historically, revenue derived from integrated circuits has represented 70 to 85% of our consolidated revenues.

OUR QUARTERLY REVENUE AND OPERATING RESULTS MAY VARY SIGNIFICANTLY IN FUTURE

PERIODS DUE TO THE NATURE OF OUR BUSINESS.

Our quarterly revenue and income (loss) from operations may vary significantly from quarter to quarter because of the nature of our revenue and planned product introductions. For example, because of our lengthy sales and design processes, the effects of failing to be selected by a customer to provide a product may result in significantly lower revenue later, as compared to prior periods with more revenue from earlier design wins. In addition, sales of our products for specific customer projects often begin and end abruptly, so revenue may increase rapidly and later decrease just as quickly. The relative timing of the beginning and end of our sales and design processes can make our revenues less predictable.

IF WE FAIL TO KEEP PACE WITH TECHNOLOGICAL ADVANCES IN OUR INDUSTRY OR IF WE PURSUE TECHNOLOGIES THAT DO NOT BECOME COMMERCIALLY ACCEPTED, CUSTOMERS MAY NOT BUY OUR PRODUCTS AND OUR REVENUE MAY DECLINE.

The demand for our products can change quickly and in ways we may not anticipate because our industry is generally characterized by:

- rapid, and sometimes disruptive, technological developments;

- evolving industry standards;

- changes in customer requirements;

- limited ability to accurately forecast future customer orders;

- frequent new product introductions and enhancements; and

- short product life cycles with declining prices over the life cycle of the product.

10

If we fail to make sufficient investments in research and development programs in order to develop new and enhanced products and solutions, or if we focus on technologies that do not become widely adopted, new technologies could render our current and planned products obsolete, resulting in the need to change the focus of our research and development and product strategies and disrupting our business significantly.

BECAUSE MANY OF OUR CURRENT AND PLANNED PRODUCTS ARE HIGHLY COMPLEX, THEY MAY CONTAIN DEFECTS OR ERRORS THAT ARE DETECTED ONLY AFTER DEPLOYMENT IN COMMERCIAL COMMUNICATIONS NETWORKS, AND IF THIS OCCURS, IT COULD HARM OUR REPUTATION AND RESULT IN INCREASED EXPENSE.

Our products are highly complex and may contain undetected defects, errors or failures. These products can only be fully tested when deployed in commercial communications networks and other equipment. Consequently, our customers may discover errors after the products have been deployed. The occurrence of any defects, errors or failures could result in:

- cancelation of orders;

- product returns, repairs or replacements;

- diversion of our resources;

- legal actions by our customers or our customers' end-users;

- increased insurance costs; and

- other losses to us or to our customers or end users.

Any of these occurrences could also result in the loss of or delay in market acceptance of our products and loss of sales, which would harm our business and adversely affect our revenue and results of operations. We have from time to time experienced defects and expect to experience defects in the future. Because the trend in our industry is moving toward even more complex products in the future, this risk will intensify over time.

OUR PRODUCTS AND TECHNOLOGIES TYPICALLY HAVE LENGTHY DESIGN AND DEVELOPMENT CYCLES. A CUSTOMER MAY DECIDE TO CANCEL OR CHANGE ITS PRODUCT PLANS, WHICH COULD CAUSE US TO GENERATE NO REVENUE FROM A PRODUCT AND ADVERSELY AFFECT OUR RESULTS OF OPERATIONS.

We may never generate any revenue from our products after incurring significant design and development expenditures. A delay or cancelation of a customer's plans could significantly adversely affect our financial results. Unlike some of our competitors, we primarily focus on winning competitive selection processes to develop products for use in our customers' equipment. These selection processes can be lengthy. After winning and beginning a product design for a customer, that customer may not begin volume production of their equipment for a period of up to two years, if at all. Due to this lengthy design and development cycle, we may experience delays from the time we begin incurring expenses until the time we generate revenue from our products. We have no assurances that our customers will ultimately market and sell their equipment or that such efforts by our customers will be successful.

BECAUSE OUR SALES ARE CONCENTRATED ON LUCENT AND A FEW OTHER CUSTOMERS, OUR REVENUE MAY MATERIALLY DECLINE IF ONE OR MORE OF OUR KEY CUSTOMERS DO NOT CONTINUE TO PURCHASE OUR EXISTING AND NEW PRODUCTS IN SIGNIFICANT QUANTITIES.

Our customer base is highly concentrated. Our top ten end customers accounted for approximately 53% of our revenue in fiscal 2001. If any one of our key customers decides to purchase significantly less from us or to terminate its relationship with us, our revenue may materially decline. Because our strategy has generally been to develop long-term relationships with a few key customers in the product areas in which we focus and we have a long product design and development cycle for most of our products, we may be unable to replace these customers quickly or at all. We could lose our key customers or significant

sales to our key customers because of factors beyond our control, such as a significant disruption in our customers' businesses generally or in a specific product line.

In particular, we depend on Lucent as a key customer. We derived 14.9% of our revenue from sales to Lucent in fiscal 2001. We expect to continue to be dependent on Lucent for a significant percentage of our revenue.

IF WE FAIL TO ATTRACT, HIRE AND RETAIN QUALIFIED PERSONNEL, WE MAY NOT BE ABLE TO DEVELOP, MARKET OR SELL OUR PRODUCTS OR SUCCESSFULLY MANAGE OUR BUSINESS.

In some fields, there are only a limited number of people in the job market with the requisite skills, particularly people with optoelectronic technology expertise. We have in the past experienced difficulty in identifying and hiring qualified engineers in many areas of our business as well as in retaining our current employees. The loss of the services of any key personnel or our inability to hire new personnel with the requisite skills could restrict our ability to develop new products or enhance existing products in a timely manner, sell products to our customers or manage our business effectively.

BECAUSE WE ARE SUBJECT TO ORDER AND SHIPMENT UNCERTAINTIES, ANY SIGNIFICANT CANCELLATIONS OR DEFERRALS COULD CAUSE OUR REVENUE TO DECLINE OR FLUCTUATE.

We generally sell products pursuant to purchase orders that customers may cancel or defer on short notice without incurring a significant penalty. Cancelations or deferrals could cause us to hold excess inventory, which could adversely affect our results of operations and restrict our ability to fund our operations. If a customer cancels or defers product shipments, we may incur unanticipated reductions or delays in our revenue. If a customer refuses to accept shipped products or does not timely pay for these products, we could incur significant charges against our income, which could materially and adversely affect our operating results.

IF WE DO NOT ACHIEVE ADEQUATE MANUFACTURING UTILIZATION, YIELDS, VOLUMES OR SUFFICIENT PRODUCT RELIABILITY, OUR GROSS MARGINS WILL BE REDUCED.

Because the majority of our manufacturing costs are relatively fixed, efficient utilization of manufacturing facilities and manufacturing yields are critical to our results of operations. Some of our manufacturing facilities have been underutilized, which has reduced our gross margins. Lower than expected manufacturing yields could impair our gross margins and delay product shipments.

In the event of an increase in demand, failure to increase our manufacturing volumes to meet our customers' increasing needs and satisfy customer demand will have a significant effect on our gross margins. In some cases, existing manufacturing capacity may be insufficient to achieve the volume or cost targets of our customers.

The manufacture of our products involves highly complex and precise processes, requiring production in highly controlled and clean environments. Changes in our manufacturing processes or those of our suppliers or contractors, or their inadvertent use of defective or contaminated materials, could significantly reduce our manufacturing yields and product reliability.

WE HAVE RELATIVELY HIGH GROSS MARGIN ON THE REVENUE WE DERIVE FROM THE LICENSING OF OUR INTELLECTUAL PROPERTY, AND A DECLINE IN THIS REVENUE WOULD HAVE A GREATER IMPACT ON OUR NET INCOME THAN A DECLINE IN REVENUE FROM OUR INTEGRATED CIRCUITS AND OPTOELECTRONIC PRODUCTS.

The revenue we generate from the licensing of our intellectual property has a high gross margin compared to the revenue we generate from our integrated circuits and optoelectronic products. Although we have derived less than 6% of our total revenue in recent years from the licensing of intellectual property, a decline in this licensing revenue would have a greater impact on our profitability than a similar decline in revenues from our integrated circuits and optoelectronic products.

WE DEPEND ON JOINT VENTURES OR OTHER THIRD-PARTY STRATEGIC RELATIONSHIPS FOR THE MANUFACTURE OF SOME OF OUR PRODUCTS, ESPECIALLY INTEGRATED CIRCUITS. IF THESE MANUFACTURERS ARE UNABLE TO FILL OUR ORDERS ON A TIMELY AND RELIABLE BASIS, OUR REVENUE MAY DECLINE.

We currently manufacture our integrated circuits and optoelectronic components through a combination of internal capability, joint ventures and external sourcing with contract manufacturers. Over the past two quarters, approximately 30 to 40% of our revenue was derived principally from integrated circuits manufactured at joint ventures or through other external sourcing arrangements. To the extent we rely on joint ventures and third-party manufacturing relationships, especially with respect to integrated circuits, we face the following risks:

- their inability to develop manufacturing methods appropriate for our products;
- that the manufacturing costs will be higher than planned;
- that the reliability of our products will decline;
- their unwillingness to devote adequate capacity to produce our products;
- their inability to maintain continuing relationships with our suppliers; and
- the reduction of our control over delivery schedules and costs of our products.

If any of these risks is realized, we could experience an interruption in supply or an increase in costs, which could delay or decrease our revenue or adversely affect our results of operations.

IF OUR CUSTOMERS DO NOT QUALIFY OUR MANUFACTURING LINES OR THE MANUFACTURING LINES OF OUR THIRD-PARTY SUPPLIERS FOR VOLUME SHIPMENTS, OUR REVENUE MAY BE DELAYED OR REDUCED.

Customers will not purchase any of our products, other than limited numbers of evaluation units, prior to qualification of the manufacturing line for the product. We may not always be able to satisfy the qualifications. Delays in qualification can cause a customer to discontinue use of the product and result in a significant loss of revenue.

BECAUSE OUR INTEGRATED CIRCUIT AND OPTOELECTRONIC COMPONENT AVERAGE SELLING PRICES IN PARTICULAR PRODUCT AREAS ARE DECLINING AND SOME OF OUR OLDER PRODUCTS ARE MOVING TOWARD THE END OF THEIR PRODUCT LIFE CYCLES, OUR RESULTS OF OPERATIONS MAY BE ADVERSELY AFFECTED.

We have in the past, and will in the future, experience declines in the average selling prices for some of our integrated circuits and optoelectronic components. For our products, the declines are due to, among other things, downturns in the semiconductor and communications industries, increased competition, lower costs of producing products and greater unit volumes. In addition, because our industry is characterized by rapid technological change and short product life cycles, in any given year we may have a substantial amount of revenue from products that are nearing the end of their product lives. The average age of our products is approximately two years, and approximately one third of our revenues are from products older than two years. If we do not offset sales decreases in older products by increases in sales of other products, including new products, our revenue will decline. If we are not able to replace products in a timely manner, our results of operations may be adversely affected.

WE CONDUCT A SIGNIFICANT AMOUNT OF OUR SALES ACTIVITY AND MANUFACTURING EFFORTS OUTSIDE THE UNITED STATES, WHICH SUBJECTS US TO ADDITIONAL BUSINESS RISKS AND MAY ADVERSELY AFFECT OUR RESULTS OF OPERATIONS DUE TO INCREASED COSTS.

In fiscal 2001, we derived 55% of our revenue from sales of our products shipped to locations outside the United States. We also manufacture a significant portion of our products outside the United States and are dependent on international suppliers for many of our parts. We intend to continue to pursue growth opportunities in both sales and manufacturing internationally. International operations are subject to a

number of risks and potential costs, which could adversely affect our revenue and results of operations, including:

- our new brand will not be locally recognized, which will cause us to spend significant amounts of time and money to build a brand identity;

- unexpected changes in regulatory requirements;

- inadequate protection of intellectual property in some countries outside of the United States;

- currency exchange rate fluctuations; and

- political and economic instability.

WE ARE SUBJECT TO ENVIRONMENTAL, HEALTH AND SAFETY LAWS, WHICH COULD INCREASE OUR COSTS AND RESTRICT OUR OPERATIONS IN THE FUTURE.

We are subject to a variety of laws relating to the use, disposal, clean-up of, and human exposure to, hazardous chemicals. Any failure by us to comply with present and future environmental, health and safety requirements could subject us to future liabilities or the suspension of production. In addition, compliance with these or future laws could restrict our ability to expand our facilities or require us to acquire costly pollution control equipment, incur other significant expenses or modify our manufacturing processes. In the event of the discovery of additional contaminants or the imposition of additional cleanup obligations at these or other sites, we could be adversely affected.

THE COMMUNICATIONS COMPONENT INDUSTRY IS INTENSELY COMPETITIVE, AND OUR FAILURE TO COMPETE EFFECTIVELY COULD HURT OUR REVENUE.

The market segments for optoelectronic components and integrated circuits are intensely competitive and subject to rapid and disruptive technological change. We expect the intensity of competition to continue to increase in the future as existing competitors enhance and expand their product offerings and as new participants enter the market. Increased competition may result in price reductions, reduced gross margins and loss of market share. We cannot assure you that we will be able to compete successfully against existing or future competitors, which may hurt our revenue.

WE MAY BE SUBJECT TO INTELLECTUAL PROPERTY LITIGATION AND INFRINGEMENT CLAIMS, WHICH COULD CAUSE US TO INCUR SIGNIFICANT EXPENSES OR PREVENT US FROM SELLING OUR PRODUCTS. IF WE ARE UNABLE TO PROTECT OUR INTELLECTUAL PROPERTY RIGHTS, OUR BUSINESSES AND PROSPECTS MAY BE HARMED.

Like other companies in the semiconductor industry, we experience frequent litigation regarding patent and other intellectual property rights. From time to time, we receive notices from third parties of potential infringement and receive claims of potential infringement when we attempt to license our intellectual property to others. Defending these claims could be costly and time consuming and would divert the attention of management and key personnel from other business issues. The complexity of the technology involved and the uncertainty of intellectual property litigation increase these risks. Claims of intellectual property infringement also might require us to enter into costly royalty or license agreements. However, we may be unable to obtain royalty or license agreements on terms acceptable to us or at all. In addition, third parties may attempt to appropriate the confidential information and proprietary technologies and processes used in our business, which we may be unable to prevent and would harm our businesses and prospects.

IF WE CANNOT MAINTAIN OUR STRATEGIC RELATIONSHIPS OR IF OUR STRATEGIC RELATIONSHIPS FAIL TO MEET THEIR GOALS OF DEVELOPING TECHNOLOGIES OR PROCESSES, WE WILL LOSE OUR INVESTMENT AND MAY FAIL TO KEEP PACE WITH THE RAPID TECHNOLOGICAL DEVELOPMENTS IN OUR INDUSTRY.

In the past, we have entered into strategic relationships to develop technologies and manufacturing processes. If any of our strategic relationships do not accomplish our intended goals or do not develop the

technology or processes sought, we will not realize a return on our investment. Currently our only material strategic investment is Silicon Manufacturing Partners Pte Ltd., a joint venture entered into with Chartered Semiconductor. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources -- Contractual Obligations and Commitments."

WE MAY NOT HAVE FINANCING FOR FUTURE STRATEGIC INITIATIVES, WHICH MAY PREVENT US FROM ADDRESSING GAPS IN OUR PRODUCT OFFERINGS THAT MAY ARISE IN THE FUTURE, IMPROVING OUR TECHNOLOGY OR INCREASING OUR MANUFACTURING CAPACITY.

If we are unable to incur additional debt or issue equity for future strategic initiatives, we may fail to address gaps in our product offerings, improve our technology or increase our manufacturing capacity. We cannot assure you that such financing will be available to us on acceptable terms or at all. Our credit agreement restricts our ability to incur debt and requires us to use a portion of the proceeds from any debt or equity issuance to repay the credit facility, as described in "Certain Indebtedness." Also, in connection with our spin-off from Lucent, we are significantly restricted in our ability to issue stock in order to raise capital. See "Arrangements Between Lucent and Our Company -- Tax Limitations on Additional Issuance of Our Stock."

IF WE ARE UNABLE TO EXTEND OR REFINANCE OUR CREDIT FACILITY WHEN IT MATURES ON SEPTEMBER 30, 2002, WE MAY NOT HAVE SUFFICIENT CASH AVAILABLE TO REPAY THAT FACILITY OR TO FUND OUR OPERATIONS.

We cannot assure you that we will be able to extend or refinance our credit facility before it matures on September 30, 2002. While we currently have sufficient cash on hand to repay amounts outstanding under the credit facility when it matures, we cannot assure you that we will have sufficient cash to repay those amounts when due. In recent periods, we have incurred substantial losses and used cash on hand to fund our operations and other cash needs, and we expect these conditions to continue in the near future. If we are required to repay our credit facility, and we are unable to obtain alternate sources of financing, we may not be able to fund our operations, make capital expenditures or service our debt. Under these circumstances, we would consider actions such as eliminating employee bonuses, accelerating already planned expense reductions, imposing further limits on capital spending and retiming certain restructuring activities to enable us to meet our cash requirements. However, we cannot assure you that these actions will be feasible at the time or prove adequate. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources."

RISKS RELATED TO THE OFFERING

WE HAVE A SIGNIFICANT AMOUNT OF DEBT, WHICH SUBJECTS US TO VARIOUS RESTRICTIONS AND INTEREST COSTS.

We have a credit facility under which $960 million was outstanding at March 31, 2002. See "Certain Indebtedness" for a description of the credit facility. We will use approximately 50% of the net proceeds from the notes to repay a portion of this short-term debt. After giving pro forma effect to the issuance and sale of the notes and the application of the net proceeds therefrom as described under "Use of Proceeds" and the repayment of an additional $540 million of the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources," as of March 31, 2002, our total outstanding debt would have been $836 million.

The credit facility is secured by our principal domestic assets other than the proceeds of our initial public offering. The maturity date of the credit facility has been extended from February 22, 2002 to September 30, 2002. In addition, if we raise at least $500 million in equity or debt capital markets transactions before September 30, 2002, or $90 million after giving effect to this offering, the maturity date of the credit facility will be extended to September 30, 2004, with the credit facility required to be reduced to $750 million on September 30, 2002 and $500 million on September 30, 2003. The credit facility imposes, and future indebtedness may impose, various restrictions and covenants on us which could limit our ability to respond to market conditions, to provide for unanticipated capital investments or to take

advantage of business opportunities. Our interest expense may be materially different as a stand-alone company than the interest expense reflected in our historical combined statement of operations for periods prior to completion of our initial public offering. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources" for details about our historical interest expense and interest expense under our credit facility.

WE AND OUR SUBSIDIARIES MAY BE ABLE TO INCUR SUBSTANTIALLY MORE DEBT.

Subject to the restrictions in our credit facility, we may incur significant additional debt. Although the terms of our credit facility contain restrictions on the incurrence of additional debt, these restrictions are subject to a number of qualifications and exceptions, and debt incurred in compliance with these restrictions could be substantial. New debt may be senior debt. If new debt is added to our and our subsidiaries' current debt levels, the related risks that we and they now face could intensify.

RESTRICTIONS IN OUR CREDIT FACILITY MAY LIMIT OUR ACTIVITIES.

Our credit facility contain restrictions on our activities, including covenants limiting our ability to:

- incur indebtedness;

- incur or permit to exist liens or security interests on our assets;

- merge or consolidate with another entity or sell all or substantially all of our assets;

- make investments in non-affiliates and certain of our subsidiaries;

- declare or pay dividends on our capital stock;

- consummate certain transactions with our affiliates; and

- consummate certain sale and leaseback or collateralized mortgage obligation transactions.

We also are required to satisfy specified financial covenants under the terms of our credit facility. These restrictions may make it difficult for us to successfully execute our business strategy or to compete in the worldwide integrated circuits and optoelectronic components industries with companies not similarly restricted.

BECAUSE THE NOTES WILL BE OUR SUBORDINATED OBLIGATIONS, WE MAY NOT MAKE ANY PAYMENTS ON THE NOTES IF ANY OF OUR SENIOR INDEBTEDNESS IS NOT PAID WHEN DUE.

The notes will be our unsecured subordinated obligations, subordinate in right of payment to all of our existing and future senior indebtedness, including all indebtedness under our credit facility. We may not pay principal of, premium, if any, or interest on the notes when due if any senior indebtedness is not paid in cash when due. In addition, in the event of an acceleration of the notes because of an event of default, the holders of senior indebtedness will be entitled to payment in full in cash in respect of such senior indebtedness before the holders of the notes will be entitled to receive any payment in respect of the notes. Moreover, the indenture provides that, under certain circumstances, no payment with respect to the notes may be made if certain non-payment defaults occur with respect to certain designated senior indebtedness, including indebtedness under our credit facility.

IN THE EVENT OF OUR BANKRUPTCY OR LIQUIDATION, OUR ASSETS WILL NOT BE AVAILABLE TO MAKE ANY PAYMENTS TO THE HOLDERS OF THE NOTES UNTIL WE HAVE MADE ALL PAYMENTS TO HOLDERS OF SENIOR INDEBTEDNESS.

In the event of insolvency, liquidation, reorganization or a similar proceeding, our senior indebtedness must be paid in full before the principal of, and premium, if any, and interest on the notes may be paid. In the event of a bankruptcy, liquidation or reorganization, holders of the notes will participate ratably (based upon respective amounts owed to each holder or creditor) with all holders of subordinated indebtedness that is deemed to be of the same class as the notes in the remaining assets. If any of these events occur, we cannot assure you that there would be sufficient assets to pay amounts due on the notes. After giving

pro forma effect to the issuance and sale of the notes and the application of the net proceeds therefrom as described under "Use of Proceeds" and the repayment of an additional $540 million of the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources," as of March 31, 2002, we would have had approximately $222 million of senior indebtedness outstanding.

YOUR RIGHT TO RECEIVE PAYMENTS ON THE NOTES IS UNSECURED AND WILL BE EFFECTIVELY SUBORDINATED TO OUR AND OUR SUBSIDIARIES' EXISTING AND FUTURE SECURED INDEBTEDNESS.

The notes will be general unsecured subordinated obligations, effectively junior to any secured debt that we and our subsidiaries have and may have in the future to the extent of the value of the assets securing that debt. Our borrowings under our credit facility and accounts receivable securitization are secured. After giving pro forma effect to the issuance and sale of the notes and the application of the net proceeds therefrom as described under "Use of

Proceeds" and the repayment of an additional $540 million of the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources," as of March 31, 2002, we and our subsidiaries would have had $385 million of secured indebtedness outstanding.

In the event of liquidation, dissolution, reorganization, bankruptcy or any similar proceeding, whether voluntarily or involuntarily instituted, the holders of our secured debt will be entitled to be paid from our or our subsidiaries' assets, as applicable, before any payment may be made with respect to the notes. If any of the foregoing events occurs, we cannot assure you that we will have sufficient assets to pay amounts due on our secured debt and the notes. As a result, the holders of the notes may receive less, ratably, than the holders of secured debt in the event of our liquidation, dissolution, reorganization, bankruptcy or other similar occurrence.

SOME SIGNIFICANT RESTRUCTURING TRANSACTIONS MAY NOT CONSTITUTE A FUNDAMENTAL CHANGE, IN WHICH CASE WE WOULD NOT BE OBLIGATED TO OFFER TO REPURCHASE THE NOTES.

Upon the occurrence of a fundamental change, which includes certain specific kinds of change of control events, we will be required to offer to repurchase all outstanding notes. The fundamental change repurchase feature is a result of negotiations between us and the underwriters. The reason for giving holders of the notes this right to require us to repurchase the notes in the event of a change of control is that note holders will have purchased our notes based in part on their comfort with our management. However, the fundamental change provisions will not afford protection to holders of notes in the event of certain transactions. For example, certain transactions, such as leveraged recapitalizations, refinancings, restructurings or acquisitions initiated by us, would not constitute a change of control and therefore not constitute a fundamental change requiring us to repurchase the notes. Certain other transactions may not constitute a change of control because they do not involve a change in voting power or beneficial ownership of the magnitude required under the definition of change of control. In the event of any such transaction, note holders would not have the right to require us to repurchase the notes, even though each of these transactions could increase the amount of our indebtedness, or otherwise adversely affect our capital structure or credit ratings, thus adversely affecting the holders of notes.

In addition, the definition of change of control includes a phrase relating to the sale of all or substantially all of our assets, determined on a consolidated basis. Although there is a limited body of case law interpreting the phrase "substantially all," there is no precise established definition of the phrase under New York law (which governs the indenture and the notes). Accordingly, the ability of a holder of notes to require us to repurchase the notes as a result of a sale of less than all of our assets, determined on a consolidated basis, may be uncertain. See "Description of Notes -- Fundamental Change Permits Holders to Require Us to Repurchase Notes."

EVEN IF A FUNDAMENTAL CHANGE DOES OCCUR TRIGGERING OUR OBLIGATION TO REPURCHASE THE NOTES, WE MAY NOT BE ABLE TO REPURCHASE THE NOTES.

The source of funds for any repurchase required as a result of any fundamental change will be our available cash, cash generated from our operations or other sources, including borrowings, sales of assets or funds provided by a new controlling entity. We cannot assure you, however, that sufficient funds will be available at the time of the fundamental change to make the required repurchase of notes. Under our credit facility, a change in control (as defined in the credit agreement) constitutes an event of default allowing the lenders to require repayment of the facility. Even if the credit facility were to remain outstanding, restrictions in the credit facility will not allow such repurchases. Consequently, if we are unable to prepay our indebtedness under our credit facility or obtain the requisite consent under our credit facility, we will be unable to fulfill our repurchase obligations if holders of notes exercise their repurchase rights following a change of control that constitutes a fundamental change, resulting in an event of default under the indenture. Furthermore, such event of default under the indenture will result in a cross-default under our credit facility and may constitute an event of default under other, future senior debt. Under these circumstances, the subordination provisions in the indenture would restrict payments to you before these obligations are satisfied. Additionally, the fundamental change repurchase feature of the notes may in certain circumstances make it more difficult or discourage a sale or takeover of us and thus, the removal of incumbent management. See "Description of Notes -- Fundamental Change Permits Holders to Require Us to Repurchase Notes."

THERE IS NO ESTABLISHED TRADING MARKET FOR THE NOTES, AND ANY MARKET FOR THE NOTES MAY BE ILLIQUID.

We do not intend to apply for a listing of the notes on a securities exchange. There is currently no established market for the notes, and we cannot assure you of any of the following:

- the liquidity of any market that may develop for the notes;

- your ability to sell the notes; or

- the price at which you will be able to sell the notes.

Although the underwriters have advised us that they currently intend to make a market for the notes, the underwriters are not obligated to do so. Any underwriters that make a market in the notes may discontinue their market making at any time at their discretion without notice to the holders of the notes. In addition, market-making activity by the underwriters will be subject to the limits imposed by the Securities Act of 1933 and the Securities Exchange Act of 1934. As a result, we cannot assure you that any market in the notes will develop or, if one does develop, that it will be maintained. If a market for the notes does develop, prevailing interest rates, the markets for similar securities and other factors could cause the notes to trade at prices lower than their purchase price or reduce the liquidity of the notes.

BECAUSE OUR QUARTERLY REVENUE AND OPERATING RESULTS ARE LIKELY TO VARY SIGNIFICANTLY IN FUTURE PERIODS, OUR COMMON STOCK PRICE MAY DECLINE.

Our quarterly revenue and income from operations have varied and are likely to continue to fluctuate significantly from quarter to quarter because of the nature of our business and planned product introductions. If our quarterly revenue or operating results fall below the expectations of securities analysts or investors, the price of our common stock may fall substantially. For example, because of our lengthy sales and design processes described above, the effects of failing to be selected by a customer to provide a product may result in significantly lower revenue in subsequent periods, as compared to prior periods with more revenue from earlier design wins. We have experienced fluctuations in quarterly revenue for this reason in the past. In addition, sales of our products for specific customer projects often begin and end abruptly, so revenue may increase rapidly and later decrease just as quickly. The relative timing of the beginning and end of such sales can make our revenue less predictable.

BECAUSE OF DIFFERENCES IN VOTING POWER AND LIQUIDITY BETWEEN THE CLASS A COMMON STOCK AND THE CLASS B COMMON STOCK, THE MARKET PRICE OF THE CLASS A COMMON STOCK MAY BE LESS THAN THE MARKET PRICE OF THE CLASS B COMMON STOCK.

There are more shares of Class B common stock than Class A common stock outstanding. Consequently, the Class B common stock may be more liquid than the Class A common stock. In addition, because the Class B common stock has greater voting power per share for the election and removal of directors than the Class A common stock, some investors may prefer the Class B common stock as a means of investing in our company. Accordingly, the greater potential voting power and liquidity of the Class B common stock may cause the Class B common stock to trade at a higher market price than the Class A common stock.

IF YOU CONVERT ANY NOTES, THE VALUE OF THE CLASS A COMMON STOCK YOU RECEIVE MAY FLUCTUATE SIGNIFICANTLY.

Since our Class A common stock has been publicly traded, the market price has fluctuated significantly and may continue to do so in the future. Significant fluctuations in the market price of our Class A common stock may occur in response to various factors and events, including, among other things:

- the depth and liquidity of the trading market for our Class A common stock;

- variations in actual or anticipated operating results;

- market conditions in the semiconductor and optical components industries;

- announcements and performance by competitors;

- sales of large volumes of our common stock, including by Lucent stockholders who received shares in the spin-off and do not want to hold our common stock;

- regulatory actions; and

- general economic conditions.

USE OF PROCEEDS

We estimate that the net proceeds of this offering will be approximately $396 million after deducting the underwriting discount and our expenses in connection with the offering. We intend to use approximately 50% of the net proceeds to repay a portion of the short-term debt outstanding under our credit facility and the balance for general corporate purposes.

We have a credit facility under which $960 million was outstanding at March 31, 2002. The maturity date of the credit facility is September 30, 2002. If we raise at least $500 million in equity or debt capital markets transactions before September 30, 2002, or approximately $90 million after giving effect to this offering, the maturity date of the credit facility will be extended to September 30, 2004, with the credit facility required to be reduced to $750 million on September 30, 2002 and $500 million on September 30, 2003. The interest rates applicable to borrowings under the credit facility are based on a scale indexed to our credit rating. Based upon our current credit ratings of BB- from Standard & Poor's and Ba3 from Moody's, the interest rate under the facility is the applicable LIBOR rate plus 400 basis points. The only periodic debt service obligation under the credit facility, as amended, is to make quarterly interest payments.

CAPITALIZATION

The following table sets forth our consolidated capitalization as of March 31, 2002, on an actual basis and on an as adjusted basis to give effect to this offering and the use of approximately 50% of the net proceeds therefrom to repay a portion of the short-term debt outstanding under our credit facility and the repayment of an additional $540 million of the credit facility subsequent to March 31, 2002 as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources."

The table below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations," our financial statements and the notes thereto included elsewhere in this prospectus.

	MARCH 31, 2002	
	HISTORICAL	AS ADJUSTED
	(UNAUDITED) (DOLLARS IN MILLIONS)	
Cash and cash equivalents	$ 1,604	$ 1,293
Debt:		
Credit facility	$ 960	$ 222
Other secured debt	136	163
6.5% Convertible Subordinated Notes due 2009	--	410
Capitalized lease obligations	41	41
Total debt	1,137	836
Stockholders' equity:		
Class A common stock, par value $0.01 per share, 5,000,000,000 shares authorized and 727,431,519 shares issued and outstanding	7	7
Class B common stock, par value $0.01 per share, 5,000,000,000 shares authorized and 908,100,000 shares issued and outstanding	9	9
Additional paid in capital	7,032	7,032
Accumulated deficit	(5,136)	(5,136)
Accumulated other comprehensive loss	(2)	(2)
Total stockholders' equity	1,910	1,910
Total capitalization	$ 3,047	$ 2,746

COMMON STOCK PRICE RANGE AND DIVIDENDS

Our Class A common stock has been listed on the New York Stock Exchange under the symbol "AGR.A" since March 28, 2001. The following table sets forth, for the indicated periods, the quarterly high and low sale prices of our Class A common stock, as reported on the New York Stock Exchange.

	HIGH	LOW
FISCAL YEAR 2001		
Quarter ended March 31, 2001 (trading began March 28, 2001)	$6.23	$6.01
Quarter ended June 30, 2001	9.50	4.10
Quarter ended September 30, 2001	7.50	3.10
FISCAL YEAR 2002		
Quarter ended December 31, 2001	$6.30	$4.06
Quarter ended March 31, 2002	6.10	3.60
Quarter ended June 30, 2002 (through June 13, 2002)	4.49	2.06

On June 13, 2002, the last reported sales price of our Class A common stock, as reported on the New York Stock Exchange, was $2.45 per share.

Our Class B common stock has been listed on the New York Stock Exchange under the symbol "AGR.B" since June 3, 2002. The high and low sales price of our Class B common stock, as reported on the New York Stock Exchange, through June 13, 2002 is $3.32 and $2.08, respectively. On June 13, 2002, the last reported sales price of our Class B common stock, as reported on the New York Stock Exchange, was $2.47.

As of June 3, 2002 there were approximately 750,000 and 1,488,000 stockholders of record of our Class A and Class B common stock, respectively.

We have not declared or paid any dividends on our Class A or Class B common stock and do not anticipate doing so in the foreseeable future. Under our bank credit facility, we are not permitted to pay any dividends on our common stock other than dividends payable solely in additional shares of our common stock and dividends pursuant to our stockholders' rights plan.

22

SELECTED FINANCIAL INFORMATION
(DOLLARS IN MILLIONS)

The following table sets forth our selected financial information. The financial information for the six month periods ended March 31, 2002 and 2001 and as of March 31, 2002 has been derived from our unaudited financial statements included elsewhere in this prospectus. The financial information for the years ended September 30, 2001, 2000 and 1999 and as of September 30, 2001 and 2000 has been derived from our audited financial statements included elsewhere in this prospectus. The financial information for the year ended September 30, 1998 and as of September 30, 1999 has been derived from our audited financial statements not included in this prospectus. The financial information for the year ended September 30, 1997 and as of September 30, 1998 and 1997 has been derived from our unaudited financial statements not included in this prospectus. The historical selected financial information may not be indicative of our future performance as a stand-alone company and should be read in conjunction with the information contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and the related notes included elsewhere in this prospectus.

	SIX MONTHS ENDED MARCH 31,		YEAR ENDED SEPTEMBER 30,				
	2002	2001	2001(1)	2000(2)	1999	1998	
	(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS)						
STATEMENT OF OPERATIONS INFORMATION:							
Revenue	$ 1,088	$2,553	$ 4,080	$4,708	$3,714	$3,101	$
Gross profit	69	1,021	996	2,153	1,765	1,509	
Purchased in-process research and development	--	--	--	446	17	48	
Amortization of goodwill and other acquired intangibles	37	223	415	189	13	3	
Restructuring and separation -- net	96	47	662	--	--	--	
Impairment of goodwill and other acquired intangibles	176	--	2,762	--	--	--	
Other income (loss) -- net(3)	335	37	35	33	36	67	
Income (loss) before cumulative effect of accounting change	(594)	(148)	(4,612)	(76)	319	303	
Cumulative effect of accounting change (net of provision (benefit) for income taxes of $(2) for the six months ended March 31, 2001, $(2) in fiscal 2001, and $21 in fiscal 1999)(4)	--	(4)	(4)	--	32	--	
Net income (loss)	$ (594)	$ (152)	$(4,616)	$ (76)	$ 351	$ 303	$
BASIC AND DILUTED EARNINGS (LOSS) PER SHARE:(5)							
Income (loss) before cumulative effect of accounting change	$ (.36)	$ (.15)	$ (3.46)	$ (.07)	$ .31	$ .29	$
Cumulative effect of accounting change(4)	--	--	--	--	.03	--	
Net income (loss)	$ (.36)	$ (.15)	$ (3.46)	$ (.07)	$ .34	$ .29	$
Weighted average shares outstanding -- basic and diluted (in millions)	1,635	1,035	1,334	1,035	1,035	1,035	
STATEMENT OF CASH FLOWS INFORMATION:							
Net cash (used in) provided by operating activities	$ (454)	$ 369	$ 269	$ 762	$ 690	$ 524	
Net cash provided by (used in) investing activities	340	(486)	(723)	(829)	(753)	(541)	
Net cash (used in) provided by financing activities	(1,433)	186	3,607	67	63	17	
OTHER FINANCIAL DATA:							
Ratio of earnings to fixed charges(6)	n/a	n/a	n/a	2.4	8.7	12.5	
Deficiency(6)	$ 584	160	$ 4,553	n/a	n/a	n/a	
SUPPLEMENTAL FINANCIAL DATA:							
EBITDA(7)	$ (558)	$ 320	$(3,520)	$ 822	$ 877	n/a	
Adjusted EBITDA(8)	(286)	367	(96)	1,268	894	n/a	

	AT MARCH 31, 2002(9)	AT SEPTEMBER 30, 2001(1)	2000(2)	1999	1998
		(DOLLARS IN MILLIONS)			
BALANCE SHEET INFORMATION:					
Working capital	$ 93	$ 156	$ 428	$ 219	$ 409
Total assets	4,291	6,562	7,067	3,020	2,481
Short-term debt	1,111	2,516	14	14	--
Long-term debt	26	33	46	64	--
Stockholders' equity/invested equity	1,910	2,461	5,781	1,962	--

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(1) During fiscal 2001 we received approximately $3,400 million of net proceeds from our initial public offering and recorded a $2,762 million impairment of goodwill and other acquired intangibles related to our acquisitions of Ortel Corporation, Herrmann Technology, Inc., Agere, Inc. and Enable Semiconductor, Inc. We also assumed $2,500 million of debt from Lucent Technologies Inc., consisting of short-term borrowings under a credit facility provided by financial institutions. We did not receive any of the proceeds of this short-term debt.

(2) During fiscal 2000 net goodwill and other acquired intangibles increased by approximately $3,400 million due to the acquisitions of Ortel Corporation, Herrmann Technology, Inc., Agere, Inc. and substantially all the assets of VTC Inc., whose results of operations are included from their respective dates of acquisition.

(3) During the six months ended March 31, 2002, we recognized a gain of $243 million from the sale of our FPGA business.

(4) Effective October 1, 2000, we adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended.

Effective October 1, 1998, we changed our method for calculating the market-related value of plan assets used in determining the expected return-on-asset component of annual net pension and postretirement benefit costs.

(5) Basic and diluted earnings (loss) per common share are calculated by dividing income (loss) by the weighted average number of common shares outstanding during the period. The weighted average number of common shares outstanding on a historical basis includes the retroactive recognition to October 1, 1996 of the 1,035,000,000 shares owned by Lucent prior to our initial public offering.

(6) For purposes of determining the ratio of earnings to fixed charges, "earnings" are defined as income (loss) from continuing operations before income taxes less undistributed earnings of equity investments plus fixed charges less interest capitalized during the period. "Fixed charges" consist of interest expense on all indebtedness and that portion of operating lease rental expense that is representative of the interest factor. "Deficiency" is the amount by which fixed charges exceeded earnings.

(7) EBITDA equals operating income (loss) plus depreciation and amortization expense. EBITDA is not intended to represent cash flow or any other measure of performance or liquidity in accordance with generally accepted accounting principles. EBITDA is included here because we believe that you may find it

to be a useful analytical tool. Other companies may calculate EBITDA differently, and we cannot assure you that our figures are comparable with similarly-titled figures for other companies.

(8) The calculation of adjusted EBITDA is shown below:

	SIX MONTHS ENDED MARCH 31,		YEAR ENDED SEPTEMBER 30,		
	2002	2001	2001	2000	1999
	(DOLLARS IN MILLIONS)				
EBITDA	$(558)	$320	$(3,520)	$ 822	$877
Purchased in-process research and development	--	--	--	446	17
Restructuring and separation -- net	96	47	662	--	--
Impairment of goodwill and other acquired intangibles	176	--	2,762	--	--
Adjusted EBITDA	$(286)	$367	$ (96)	$1,268	$894

(9) For the six months ended March 31, 2002, we repaid $1,540 million of the $2,500 million of short-term debt outstanding under our credit facility to reduce the size of the facility to $960 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with our unaudited financial statements for the six month periods ended March 31, 2002 and 2001 and our audited financial statements for the years ended September 30, 2001, 2000 and 1999, and the notes thereto. This discussion contains forward-looking statements. See "Forward-Looking Statements" and "Risk Factors" for a discussion of the uncertainties, risks and assumptions associated with these statements.

OVERVIEW

We are the world's leading provider of components for communications applications, delivering integrated solutions that form the building blocks for advanced wired, wireless and optical communications networks. We also design and manufacture a wide range of semiconductor solutions for computer- and communications-related devices used by consumers, such as cellular phones, modems and hard disk drives for personal computers and workstations. In addition, we supply complete wireless computer networking solutions through the ORiNOCO(R) product family.

Our business operations are organized into two market-focused groups, Client Systems and Infrastructure Systems, that target the consumer communications and network equipment markets, respectively. Each of these two groups is a reportable operating segment. The segments each include revenue from the licensing of intellectual property related to that segment.

The Client Systems segment includes our wireless data, computer communications, storage and wireless terminal solutions products. This segment delivers integrated circuit solutions for a variety of end-user applications such as modems, Internet-enabled cellular terminals and hard-disk drives for computers as well as software, systems and wireless local area network solutions through the ORiNOCO product family.

The Infrastructure Systems segment delivers solutions to the high-speed communications systems market and facilitates the convergence of integrated circuit devices and optoelectronic components. We have consolidated research and development, as well as marketing, for both optoelectronic and integrated circuit devices aimed at communications systems. This allows us to design, develop and deliver complete, interoperable solutions to equipment manufacturers for advanced enterprise, access, metropolitan, long-haul and undersea applications.

SEPARATION FROM LUCENT

We were incorporated under the laws of the State of Delaware on August 1, 2000, as a wholly owned subsidiary of Lucent. We had no material assets or activities as a separate corporate entity until the contribution to us by Lucent of its integrated circuits and optoelectronic components businesses. Lucent had previously conducted these businesses through various divisions and subsidiaries. On February 1, 2001, Lucent began the separation of our company by transferring to us the assets and liabilities related to these businesses. The separation was substantially completed, including the transfer of all assets and liabilities other than pension and postretirement plan assets and liabilities, when we completed our initial public offering in April 2001. As of April 30, 2002, Lucent owned 100% of our outstanding Class B common stock and 37 million shares of our outstanding Class A common stock, which represented approximately 58% of the total outstanding common stock and approximately 84% of the combined voting power of both classes of our common stock with respect to the election and removal of directors. On June 1, 2002, Lucent distributed all of these shares to its shareholders, completing our spin-off.

In connection with our separation from Lucent, we entered into several agreements with Lucent regarding, among other things, interim services, intellectual property and product supply. The interim services agreement sets forth charges generally intended to allow the providing company to fully recover the allocated direct costs of providing the services, plus all out-of-pocket costs and expenses. For more

information, see note 19 to our annual financial statements and note 13 to our quarterly financial statements included elsewhere in this prospectus.

Lucent is our largest customer with purchases for the six months ended March 31, 2002 and 2001 representing 13.1% and 15.9%, respectively, and in fiscal 2001, 2000 and 1999 representing 14.9%, 21.3% and 25.7%, respectively, of our revenue. We expect Lucent will continue to represent a significant percentage of our revenue in the foreseeable future.

Our financial statements include amounts prior to February 1, 2001 that have been derived from the financial statements and accounting records of Lucent using the historical results of operations and historical basis of the assets and liabilities of our businesses. We believe the assumptions underlying our financial statements are reasonable. However, our financial statements for periods prior to February 1, 2001 may not necessarily reflect our results of operations, financial position and cash flows in the future or what our results of operations, financial position and cash flows would have been had we been a stand-alone company during the periods presented. Because a direct ownership relationship did not exist among all the various units comprising Agere, Lucent's net investment in us is shown in lieu of stockholders' equity in our financial statements for periods prior to February 1, 2001. For periods prior to February 1, 2001, our financial statements include allocations of Lucent's expenses, assets and liabilities, including allocations for general corporate expenses, basic research, interest expense, pension and postretirement costs, income taxes and cash and receivables, which are discussed in note 1 to our annual and quarterly financial statements included elsewhere in this prospectus.

ACQUISITIONS

During fiscal 1999 and 2000 we completed the acquisitions described below as part of our efforts to broaden our portfolio of product offerings. We did not have any significant acquisitions during the six months ended March 31, 2002 or fiscal 2001.

In June 2000, we acquired Herrmann, a developer and manufacturer of passive optical filters that can be used in conjunction with active optoelectronic components in products such as amplifiers. The purchase price was $432 million in Lucent common stock and options. In connection with this acquisition, certain former stockholders of Herrmann are entitled to receive up to a total of 677,019 additional shares of Lucent common stock based on retention and the achievement of specified milestones, which require the production of two products at improved manufacturing yields within the three-year period following the acquisition. As of September 30, 2001, 200,000 shares of Lucent common stock had been released based on the achievement of milestones, resulting in additional goodwill related to the acquisition. The achievement of additional milestones may also result in additional goodwill.

In April 2000, we acquired Ortel, a developer and manufacturer of semiconductor optoelectronic components used in fiber optic systems for cable television and data communications networks. The purchase price was $2,998 million in Lucent common stock and options.

In April 2000, we acquired Agere, Inc., a developer and supplier of network processor integrated circuits. Network processors control how data is sent over a network. The purchase price was $377 million in Lucent common stock and options.

In March 2000, we acquired substantially all the assets of VTC, a supplier of integrated circuits to computer hard disk drive manufacturers. The purchase price was $104 million in cash. In connection with this acquisition, stockholders of VTC are entitled to receive additional cash consideration of up to $50 million contingent on the delivery of product at specified manufacturing yields and the transfer and qualification of process technology to our manufacturing facilities. As of September 30, 2001, $30 million of the additional cash consideration had been paid, resulting in additional goodwill related to the acquisition. Any future contingent cash consideration paid will also be recorded as additional goodwill.

In March 1999, we acquired Enable, a developer of integrated circuits for local area network equipment. The purchase price was $51 million in cash.

In February 1999, we acquired Sybarus Technologies ULC, a developer of integrated circuits for communications networks. The purchase price was $41 million in cash.

We review our long-lived assets for impairment whenever events or changes in circumstances occur that indicate the carrying amount of the assets may not be fully recoverable. During fiscal 2001 and the second quarter of fiscal 2002, we performed impairment evaluations of the goodwill and other acquired intangibles from recent acquisitions. The assessments were performed in accordance with Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of," as a result of weakening economic conditions and decreased current and expected future demand for products in the markets in which we operate. We determined the fair value of the acquired entities using a discounted cash flow model based on growth rates and margins reflective of the current decrease in demand for our products, as well as anticipated future demand. Discount rates used were based upon our weighted average cost of capital adjusted for business risks. These assumptions were based on management's best estimate of future results. As a result of the assessments, we determined that an other-than-temporary impairment of goodwill and other acquired intangibles existed. In fiscal 2001, we recorded a charge to reduce goodwill and other acquired intangibles of $2,762 million during fiscal 2001, consisting of $2,220 million, $275 million, $240 million and $27 million related to Ortel, Herrmann, Agere, Inc. and Enable, respectively. During the second quarter of fiscal 2002, we performed additional impairment evaluations of goodwill and other acquired intangibles due to a continued weakening of economic conditions and decreased demand for our products. We recorded a charge to reduce goodwill and other acquired intangibles of $176 million during the second quarter of fiscal 2002, consisting of $113 million and $63 million related to Ortel and Hermann, respectively.

OPERATING TRENDS

During the second quarter of fiscal 2002, the Client segment experienced a 19% increase in revenues for the three months ended March 31, 2002 compared to the three months ended December 31, 2001. This increase was due to improved demand for PC-related components. However, the Infrastructure segment experienced a 14% decrease in revenues for the three months ended March 31, 2002 compared to the three months ended December 31, 2001. This decrease was due to lower demand from network equipment manufacturers, as service providers continue to reduce or defer spending. We would expect these general trends to continue into our third fiscal quarter. However, our ability to forecast future results is limited due to backlog levels that are lower than those experienced in the past and higher than normal order cancellations and reschedules.

Our costs consist primarily of manufacturing overhead, materials and labor. Similar to many semiconductor manufacturers, we have relatively high fixed costs associated with our wafer manufacturing. As a result, our ability to reduce costs quickly in times of decreased demand is limited, which has an adverse effect on margins. Because we anticipated higher revenues as we entered fiscal 2001, our cost structure reflected manufacturing capacity and resources greater than those actually required. In light of the lower revenues we have experienced in recent quarters, we have taken a number of steps to reduce our cost structure, including restructuring activities and reductions in capital spending, and we are considering additional actions to reduce our cost structure in the event that our revenues do not improve.

RESTRUCTURING ACTIVITIES

In fiscal 2001 and the first half of fiscal 2002, we announced a series of restructuring initiatives to reduce our cost structure in light of declining revenues. We recorded net restructuring charges of $91 million and $563 million for the six months ended March 31, 2002 and fiscal 2001, respectively, classified within restructuring and separation expenses -- net. These restructuring initiatives were focused on improving gross profit, reducing expenses and streamlining operations, and include a worldwide workforce reduction, rationalization of manufacturing capacity and other activities.

FISCAL YEAR ENDED SEPTEMBER 30, 2001

The restructuring initiatives announced in fiscal 2001 will result in a workforce reduction of approximately 6,000 employees across various business functions, operating units and geographic regions, and includes both management and occupational employees. We recorded a restructuring charge of $177 million in fiscal 2001 related to approximately 5,500 employees, of which approximately 4,300 employees had been taken off-roll as of September 30, 2001. Of this $177 million charge, $28 million represents termination benefits to certain U.S. employees that will be funded through pension assets. This amount was recognized in accordance with Statement of Financial Accounting Standards No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits." Severance costs and other exit costs noted above were determined in accordance with Emerging Issues Task Force No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity."

We recorded a restructuring charge of $386 million in fiscal 2001 relating to the rationalization of under-utilized manufacturing facilities and other restructuring-related activities. We have discontinued manufacturing operations at our chip fabrication plant in Madrid, Spain and have subsequently sold this facility. We are also rationalizing under-utilized manufacturing capacity at our facilities in Orlando, Florida, and in Allentown, Breinigsville and Reading, Pennsylvania. In addition, we are consolidating several satellite-manufacturing sites, as well as leased corporate offices. The restructuring charge for fiscal 2001 includes $37 million related to facility closings, primarily for lease terminations, non-cancelable leases and related costs. It also includes an asset impairment charge of $287 million. All affected assets were classified as held for disposal, in accordance with the guidance on impairment of assets in Statement 121, and depreciation was suspended. The $287 million non-cash impairment charge represents the write-down to fair value, less costs to sell, of property, plant and equipment that was disposed of or removed from operations. The remaining restructuring charge of $62 million relates primarily to contract terminations.

A summary of restructuring charges is outlined as follows:

	YEAR ENDED SEPTEMBER 30, 2001			AT SEPTEMBER 30, 2001
	TOTAL CHARGES	NON CASH CHARGES	CASH PAYMENTS	RESTRUCTURING RESERVE
	(DOLLARS IN MILLIONS)			
Workforce reduction	$177	$ (28)	$(57)	$ 92
Rationalization of manufacturing capacity and other charges	386	(293)	(14)	79
Total	$563	$(321)	$(71)	$171

SIX MONTHS ENDED MARCH 31, 2002

We recorded net restructuring charges of $91 million for the six months ended March 31, 2002, classified within restructuring and separation expenses -- net. These net restructuring charges are comprised of charges of $177 million, offset by reversals of $86 million. We recorded net restructuring charges of $12 million for the six months ended March 31, 2001, primarily related to contract terminations. The details of the initiatives announced during the first and second quarters of fiscal 2002 are outlined below.

On December 5, 2001, we announced a workforce reduction of 950 positions, which affects primarily management positions within our product groups, sales organizations and corporate support functions located in New Jersey and Pennsylvania.

On January 23, 2002, we announced plans to further improve our operating efficiency by consolidating our facilities. We are consolidating existing manufacturing, research and development, business management and administrative facilities in Pennsylvania and New Jersey. This consolidation is expected to be substantially completed 18 months from the announcement. Additionally, we are seeking a buyer for our wafer fabrication operation in Orlando, Florida. This site has approximately 1,100 employees.

We are moving the majority of our integrated circuits and optoelectrics operations from our sites in Reading and Breinigsville, Pennsylvania, into the Allentown, Pennsylvania campus. In addition, the majority of our assembly and test operations located in these three sites are moving to our assembly and test facilities in Bangkok, Thailand; Matamoras, Mexico; and Singapore. Subsequently, we will discontinue operations at the Reading and Breinigsville facilities and will seek buyers for those properties. We expect that our plans to combine operations from these facilities into Allentown will result in a net headcount reduction of approximately 300 positions.

The following table sets forth our restructuring reserves as of March 31, 2002 and reflects the activity related to the worldwide workforce reductions and the rationalization of manufacturing capacity and other charges affecting the reserves for the six months ended March 31, 2002:

	SEPTEMBER 30, 2001	SIX MONTHS ENDED MARCH 31, 2002			
	RESTRUCTURING RESERVE	RESTRUCTURING CHARGE	RESTRUCTURING REVERSAL	NON-CASH ITEMS	CASH PAYMENTS
Workforce reduction......	$ 92	$ 56	$(20)	$ (23)	$ (80)
Rationalization of manufacturing capacity and other charges......	79	121	(66)	(53)	(30)
Total...............	$171	$177	$(86)	$ (76)	$(110)

Worldwide Workforce Reduction

We recorded restructuring charges relating to workforce reductions of $56 million for the six months ended March 31, 2002. The charges include $23 million for the approximately 500 remaining employees associated with the workforce reduction of approximately 6,000 positions announced in fiscal 2001, $24 million relating to approximately 600 employees associated with the December 5, 2001 announcement and $9 million for approximately 100 employees associated with the January 23, 2002 announcement. Of the total workforce reduction charges, $23 million represents non-cash charges for termination benefits to certain U.S. employees that will be funded through pension assets.

During the six months ended March 31, 2002, we recorded a $20 million reversal of the restructuring reserve associated with workforce reductions, resulting from severance and benefit cost termination estimates that exceeded amounts paid during the second half of calendar year 2001. The original reserve included an estimate of termination pay and benefits for occupational employees that was based on the average rate of pay and years of service of the occupational employee pool at risk. Our collective bargaining agreements allow for a period when employees at risk can opt for positions filled by employees with less seniority. When that period ended, a series of personnel moves followed that ultimately resulted in lower severance and benefit payments than originally expected. This was due principally to the termination of occupational employees with fewer years of service and fewer weeks of severance entitlement. These personnel moves were substantially finished at the end of calendar 2001. Severance costs and other exit costs were determined in accordance with Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity."

We have completed the workforce reductions announced in fiscal 2001 with approximately 6,000 employees taken off-roll as of March 31, 2002. We have also made significant progress towards completing the workforce reduction of 950 employees announced on December 5, 2001 with approximately 500 employees taken off-roll by March 31, 2002 and expect to complete this workforce reduction by the end of fiscal 2002. With regard to the facilities consolidation plan announced on January 23, 2002, we expect that this action will result in a net reduction of approximately 300 positions by the end of fiscal year 2003, none of which were off-roll as of March 31, 2002.

Rationalization of Manufacturing Capacity and Other Charges

We recorded restructuring charges of $121 million for the six months ended March 31, 2002, relating to the rationalization of under-utilized manufacturing facilities and other activities. The charges included $69 million related to asset impairments, $40 million for facility closings, and $12 million of other related costs primarily for contract terminations.

The asset impairment charge of $69 million includes the impairment of assets under construction that had not been placed into service and were associated with the facilities consolidation initiative announced on January 23, 2002 to move the majority of our operations in Reading and Breinigsville, Pennsylvania to our Allentown, Pennsylvania campus and the impairment of property, plant and equipment relating to earlier restructuring initiatives for the rationalization of underutilized manufacturing facilities and other activities. All affected assets were classified as held for disposal, in accordance with the guidance on impairment of assets in Statement 121, and depreciation was suspended. These non-cash impairment charges represent the write-down to fair value, less costs to sell, of property, plant and equipment that were disposed of, held for sale, or removed from operations.

The facility closing charge of $40 million consists principally of a non-cash charge of $35 million for the realization of the cumulative translation adjustment resulting from our decision to substantially liquidate our investment in the legal entity associated with our Madrid, Spain manufacturing operations. This charge was recognized in accordance with Emerging Issues Task Force Issue No. 01-5, Issue Summary No. 1, "Application of SFAS No. 52, and Foreign Currency

Translation, to an Investment Being Evaluated for Impairment That Will Be Disposed Of." The $5 million balance of the charge related to the facility closing is primarily for lease terminations and non-cancelable leases and related costs.

We recorded restructuring charge reversals of $66 million for the six months ended March 31, 2002. The restructuring charge reversals include adjustments to estimates of $27 million for asset impairments, a $25 million reversal due to receiving more proceeds from the sale of the assets associated with our Madrid, Spain manufacturing operations than originally estimated, $6 million for contract terminations, a $6 million reversal of a restructuring reserve deemed no longer necessary, and $2 million for facility lease terminations. The asset impairment adjustments were due principally to realizing more proceeds than expected from asset dispositions and from assets that were placed back into service in the second quarter of fiscal 2002.

Restructuring Reserve Balances

We anticipate that substantially all of the $25 million restructuring reserve as of March 31, 2002, relating to the workforce reductions, will be paid by end of fiscal 2002. We anticipate that the restructuring reserve balance of $51 as of March 31, 2002, relating to the rationalization of manufacturing capacity and other charges, will be paid as follows: the majority of the contract terminations of $30 million will be paid by the end of fiscal 2002; the non-cancelable lease obligations of $11 million, due to consolidation of facilities, will be paid over the respective lease terms through fiscal 2005; and the majority of the other related costs of $10 million will be paid by December 31, 2002.

These cash outlays will be funded through cash and cash equivalents on hand. Excluding the facilities consolidation initiative announced on January 23, 2002, we currently estimate future annualized pre-tax savings to be approximately $600 million, of which approximately $120 million is associated with reduced depreciation and $480 million is cash savings resulting from lower employee costs and reduced costs associated with contract and facility lease obligations. The full impact of these savings is expected to be achieved during the third quarter of fiscal 2002. We expect that approximately 75% of these savings will affect gross margin and 25% will affect operating expenses. Our savings in the second quarter of fiscal 2002 were approximately $140 million, resulting from reduced depreciation and lower employee costs and reduced costs associated with contract and facility lease obligations. Of that amount, we estimate that approximately 75% affected gross margin and 25% affected operating expenses.

30

Facilities Consolidation

In addition to the charges we recorded as restructuring expenses related to our January 23, 2002 announcement concerning our facilities consolidation, we also recorded $17 million of charges within gross margin for the six months ended March 31, 2002, substantially all of which resulted from accelerated depreciation. This accelerated depreciation charge is due to the shortening of estimated useful lives of certain assets in connection with the planned facility closings.

We expect to incur total cash expenditures of approximately $250 million to $350 million associated with the moving of operations and the consolidating of existing manufacturing, research and development, business management and administrative facilities in Pennsylvania and New Jersey. There will also be additional non-cash impacts associated with accelerated depreciation and asset impairments as we continue to evaluate the property, plant and equipment located at Breinigsville and Reading, which had a combined net book value of approximately $455 million as of March 31, 2002. As part of this evaluation, we are determining which assets will be transferred to other locations, temporarily remain in service until the completion of the facilities consolidation, or be removed from service and disposed of by sale or abandonment. We expect the transfer of equipment and manufacturing capability to be substantially complete within eighteen months from the date of the announcement. Our wafer fabrication operation in Orlando, Florida, for which we are seeking a buyer, had property, plant and equipment with a net book value of approximately $445 million as of March 31, 2002.

Through the consolidation of operations in Pennsylvania and New Jersey, we are reducing our square footage in the two states by about two million square feet, or approximately 50 percent, significantly lowering costs. We expect to realize approximately $100 million annually in cash savings from these actions, commencing in the first quarter of fiscal 2003, driven primarily by a reduction in rent and building infrastructure costs.

SEPARATION EXPENSES

We incurred costs, fees and expenses relating to our separation from Lucent. These costs, fees and expenses were primarily related to legal separation matters, designing and constructing our computer infrastructure, information and data storage systems, marketing expenses relating to building a company brand identity and implementing treasury, real estate, pension and records retention management services. For fiscal 2001 we recorded $99 million of separation expenses. For the six months ended March 31, 2002 we incurred separation expenses of $5 million compared to $35 million for the six months ended March 31, 2001. As we incurred the majority of the necessary expenses related to our separation from Lucent in fiscal 2001, we would expect these expenses to be substantially lower in fiscal 2002.

INVENTORY PROVISION

We recorded inventory provisions, classified within cost of sales, of $66 million and $74 million for the six months ended March 31, 2002 and 2001, respectively, and $409 million in fiscal 2001 compared to inventory provisions of $29 million in fiscal 2000 and $11 million in fiscal 1999. The inventory provisions were calculated in accordance with our inventory valuation policy, which is based on a review of forecasted demand compared with existing inventory levels.

We experienced significant revenue growth over the five years ending September 30, 2000, and this pattern of growth continued through the first quarter of fiscal 2001. In the second quarter of fiscal 2001, we noted softness in customers' demand. However, we did not believe this to be other than temporary, given the recent history of growth. Our belief that the weakness in demand was temporary was supported by the observation that customers were delaying orders to later periods rather than canceling them, and third-party market projections indicating that there could be a rebound in demand in the following months. During the third quarter of fiscal 2001, the decline in the market accelerated. Our customers provided evidence of a longer lasting market decline, both through canceled orders and through direct communications with us. Given our forecast of continuing reductions in demand in the fourth quarter, the majority of the fiscal 2001 inventory charge was recorded in the third quar