SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

|_| REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OR (G)
OF THE SECURITIES EXCHANGE ACT OF 1934
or
|X| ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE
SECURITIES EXCHANGE ACT OF 1934
for the fiscal year ended December 31, 1996
or
|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE
SECURITIES EXCHANGE ACT OF 1934
for the transition period from to
Commission File number: 1-13546

SGS-THOMSON Microelectronics N.V.
(Exact name of Registrant as specified in its charter)

N/A	The Netherlands
(Translation of Registrant's name into English)	(Jurisdiction of incorporation or organization)

Technoparc du Pays de Gex - B.P. 112
165, rue Edouard Branly
01630 Saint Genis Pouilly
France
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class:	Name of each exchange on which registered
Common Shares, nominal value NLG 13.75 per Common Share	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act:
None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:
None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report:

Common Shares, nominal value NLG 13.75 per Common Share	138,985,580

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

Yes |X| No |_|

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 |_| Item 18 |X|

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* Omitted because item is not applicable.

PART I

Item 1: Description of Business In 1996

The Company

SGS-THOMSON is a global independent semiconductor company that designs, develops, manufactures and markets a broad range of semiconductor integrated circuits and discrete devices used in a wide variety of microelectronic applications, including telecommunications systems, computer systems, consumer products, automotive products and industrial automation and control systems. According to preliminary industry data, SGS-THOMSON entered in 1996 the group of the top 10 worldwide suppliers of semiconductor devices. On the basis of preliminary 1996 industry rankings, SGS-THOMSON was the world's leading supplier of analog monolithic ICs, mixed signal ASICs ICs, smartcard ICs, special automotive ICs, EPROM and EEPROM memories and the world's second leading supplier of telecom ICs. According to industry data for 1995, SGS-THOMSON was the leading supplier of MPEG decoders ICs with approximately 44.3% share of the MPEG decoders market. The Company currently offers more than 3,000 main types of products to more than 1,500 customers including Alcatel, Bosch, Creative Technology, Ford, Hewlett-Packard, IBM, Motorola, Nokia, Nortel, Philips, Seagate Technology, Siemens, Sony, Thomson Multimedia and Western Digital.

The Company offers a diversified product portfolio and develops products for a wide range of market applications to reduce its dependence on any single product, industry or application market. The Company has focused on developing products that exploit its technological strengths, including differentiated ICs (which the Company defines as being its dedicated products, semicustom devices and microcontrollers). Differentiated ICs foster close relationships with customers, resulting in early knowledge of their evolving requirements and opportunities to access their markets for other products, and are less vulnerable to competitive pressures than standard commodity products. Differentiated ICs accounted for approximately 59% of the Company's net revenues in 1996 compared to approximately 51% in 1995. SGS-THOMSON also targets applications that require substantial analog and mixed-signal content and can exploit the Company's system level expertise. In 1996, analog ICs (including mixed-signal ICs), the majority of which are also differentiated ICs, accounted for approximately 46% of the Company's net revenues (unchanged from 1995), while discrete devices accounted for approximately 14% of the Company's net revenues (compared to approximately 17% in 1995). In recent years, analog ICs have experienced less volatility in sales growth rates and average selling prices than the overall semiconductor industry.

In 1996, the Company developed a number of important new products such as the first superintegrated chips for hard disk drives and set-top-boxes (OMEGA chip announced in 1997), new 8, 16 and 32 bits application-specific cores of its microcontrollers families, a new

family of mixed-signal semicustom chips, new integrated Audio/Video chips for MPEG-2 decompression functionality in multimedia and consumer applications, an antitaping chip that can be integrated in the Company video encoding devices, a new multimedia analog front-end for computer and a radiofrequency single chip for digital cellular phones.

In 1996, SGS-THOMSON reached an agreement with Samsung Electronics Co. Ltd. to cooperate in the development and sourcing of microcontrollers and digital signal processors designed specifically for high volume markets, such as set-top-boxes, multimedia PCs and mobile communication. The Company also signed an agreement with World Space for developing and producing chip sets for new generation personal satellite radios and an agreement with Chromatic Research Inc. to co-design, manufacture and market single-chip multimedia processors of the MPACT series (capable of 2D and 3D graphics, audio, video, fax/modem, telephony and videophone functionalities) for multimedia PC applications and entered into a strategic partnership with Microsoft to add hardware Digital Video Disk support to the Microsoft Active Movie platform.

In 1996, SGS-THOMSON's cumulative shipments of integrated circuits for smartcards surpassed the one billion mark. The Company's smartcard chip portfolio spans the full range of commercial applications, including GSM mobile phones, pay-TV, ID cards, banking, electronic purses, health cards, access control, toll payment and mass transport, and includes standard memory chips as well as the most advanced 8 bit cryptocontrollers. The Company is currently developing 32 bit cryptocontrollers as well as solutions for contactless applications. In 1996, SGS-THOMSON was the first company to obtain security certifications for banking and Pay-TV devices according to the ITSEC European Norms.

In November 1996, the Company announced that the research and development center jointly operated by the Company and the Centre National d'Etudes et des Telecommunications ("CNET"), the research laboratory of France Telecom, had completed the development of the 0.25 micron CMOS process, only one year after the qualification of the 0.35 micron process. The 0.25 micron process, currently used in the prototyping of a complex evaluation circuit of several million transistors, consists of six metal layers and involves more than 22 levels of masking. Other complex prototypes are being developed to further validate the process and accelerate the introduction of products based on this process, in particular a systolic processor for the estimation of movement in images.

In 1996, the Company established a small research laboratory in Berkeley, California, which will principally cooperate in the design of advanced macrocells and libraries for the Company's analog, digital and mixed signal technologies.

Since 1995, SGS-THOMSON adopted a plan to increase its manufacturing capacity through the addition of new 8-inch submicron fabrication plants that will be designed to meet the growing demand for VLSI devices. The Company also approved the building and equipping of a new 8-inch 0.5 micron front-end wafer fabrication plant (which will also be capable of 0.35 production) in Singapore, which was announced in 1996.

The Company's business is organized into five principal product groups:

The Dedicated Products Group produces application-specific semiconductor products using advanced bipolar, CMOS, BiCMOS, mixed-signal and power technologies. The Group's dedicated products are used in all major end-user applications, including such new applications as mobile communications networks, asynchronous transfer mode communications systems, global positioning systems, flat panel displays, hard disk drives and digital video systems. The breadth of the Group's customer and application base provides it with a source of stability in the cyclical semiconductor market, while its position as a strategic supplier of application-specific products provides it with opportunities to supply its customers' requirements for other products, including discrete devices, programmable products and memories.

The Discrete and Standard ICs Group produces discrete power devices, power transistors, standard linear and logic ICs and radio frequency ("RF") products. The Group's discrete and standard products are manufactured using mature technological processes that are less capital intensive than the Company's other principal products. The Group has a diverse customer base and broad product portfolio.

The Memory Products Group produces a broad range of memory products, including EPROMs, flash memories, EEPROMs, SRAMs, and chips for smartcards. According to preliminary industry data, the Company was the leading supplier of EPROMs in 1996, accounting for approximately 30% of worldwide EPROM sales, as well as the leading supplier of EEPROMs. The Company has developed a proprietary know-how for flash memory devices and has started mass production for this market. The Group does not produce DRAMs, a commodity memory product.

The Programmable Products Group produces microcomponents (including microcontrollers, microprocessors and digital signal processors), digital semicustom devices and mixed analog/digital semicustom devices.

The New Ventures Group identifies and develops new business opportunities to complement the Company's existing businesses and exploit its technological know-how, manufacturing capabilities and global marketing team. Initial activities have focused on manufacturing and marketing x86 microprocessors. New activities include design and manufacturing of "system on silicon" solutions based on the 486 CPU core and more recently media processors based on Very Long Instruction Word ("VLIW") processes.

As part of its activities outside the five principal products groups, the Company also produces subsystems for industrial and other applications.

SGS-THOMSON's products are manufactured and designed using a broad range of manufacturing processes and proprietary design methods. SGS-THOMSON uses all of the

prevalent function-oriented process technologies, including CMOS, bipolar and non-volatile memory technologies. In addition, by combining basic processes, the Company has developed advanced systems-oriented technologies that enable it to produce differentiated and application-specific products, including BiCMOS technologies (bipolar and CMOS) for mixed-signal applications, BCD technologies (bipolar, CMOS and DMOS) for intelligent power applications and embedded memory technologies. This broad technology portfolio, a cornerstone of the Company's strategy for many years, enables the Company to meet the increasing demand for "systems-on-a-chip" solutions. To complement this depth and diversity of process and design technology, the Company also possesses a broad intellectual property portfolio that it has used to enter into cross-licensing agreements with many major semiconductor manufacturers.

In 1996, SGS-THOMSON has expanded its diversified manufacturing infrastructure while improving the cost, quality and flexibility of its operations. SGS-THOMSON has applied 1996 investments in its manufacturing facilities to bring to full capacity the 8-inch front-end manufacturing facility in Crolles, France, to continue the ramp up of the new 8-inch front-end manufacturing facility in Phoenix, Arizona, to complete the building of and to begin equipping the third 8-inch front-end manufacturing facility in Catania, Italy, and to complete a new back-end facility and design center in Shenzhen, China, through its joint venture created in 1994 with a subsidiary of the Shenzhen Electronics Group. During 1996, the Company has also completed conversion from 4-inch to 5-inch of the two front-end wafer fabrication plants in Tours, France, from 5-inch to 6-inch of the front-end wafer fabrication facility in Rousset, France, and has installed a new 6-inch module in the Rancho Bernardo, California front-end wafer fabrication facility. In addition, the Company has started construction of a new 8-inch front-end wafer fabrication facility in Rousset, France, has initiated the 6-inch to 8-inch conversion of one of its Agrate, Italy front-end wafer fabrication plants, and has started planning the construction of a new 8-inch front-end wafer fabrication facility in Singapore, announced during 1996. Finally, the Company has also identified one more 8-inch front-end wafer fabrication plant to be built in Italy. The Company has many back-end manufacturing activities in large and modern facilities in lower-cost areas in the Mediterranean and Asia Pacific regions and has focused on continually improving the productivity of all of its manufacturing facilities. SGS-THOMSON has also centralized the management of its manufacturing operations and implemented computer-integrated manufacturing systems and statistical process control techniques. The Company fosters a corporate-wide Total Quality Management ("TQM") culture that defines a common set of objectives and performance measurements for employees in all geographic regions, at every stage of product design, development and production for all product lines.

SGS-THOMSON is international in scope, operating front-end and/or back-end manufacturing facilities in Europe, the United States, the Mediterranean and Asia Pacific regions, and conducting research and development primarily in France and Italy, and design, marketing and sales activities in each of the electronic industry's major economic regions: Europe, the United States, the Asia Pacific region and Japan. In 1996, approximately 44% of the Company's net revenues originated in Europe (compared to 46% in 1995), approximately 23% in the Americas (compared to 24% in 1995), approximately 27% in the Asia Pacific region

(compared to 26% in 1995) and approximately 6% in Japan (compared to 4% in 1995). In 1996 the Company's sales in the Asia Pacific region surpassed the $1 billion level for the first time. In 1996, approximately one-third of the 6-inch equivalent wafers manufactured by the Company were manufactured outside of Europe and more than one-half of the Company's employees were located outside of Europe.

SGS-THOMSON believes that strategic alliances are critical to success in the semiconductor industry, and has entered into strategic alliances with customers, other semiconductor manufacturers and major suppliers of design software. The Company has entered into several strategic customer alliances, including alliances with Alcatel, Seagate Technology, Thomson Multimedia and Western Digital, among others. Customer alliances provide the Company with valuable systems and application know-how and access to markets for key products, while allowing the Company's customers to share some of the risks of product development with the Company and gain access to the Company's process technologies and manufacturing infrastructure. Alliances with other semiconductor manufacturers permit costly research and development and manufacturing resources to be shared to mutual advantage for joint technology development. The Company has also entered into technology development alliances with customers and other manufacturers, including Nortel in North America to develop advanced 0.5 micron BiCMOS mixed-signal technologies and Mitsubishi Electric Corporation ("Mitsubishi") in Japan to develop a family of 16 Mbit flash memories for mass storage applications. The Company has also entered into an agreement with Philips Semiconductors to jointly develop sub-micron CMOS logic processes in Crolles, France through 1997. The Company has also established joint development programs with leading suppliers such as Applied Materials, ASM Lithography, LAM and Air Liquide, and with CAD Tools producers including Cadence, Synopsis and Mentor. It is a participant in Sematech I 300I for the development of 300 millimeter wafer manufacturing processes. SGS-THOMSON is active in joint European research efforts such as the new MEDEA program (which succeeded to JESSI as of 1997), and also cooperates with major research institutions and universities.

History

The Company was formed in June 1987 as a result of the combination of the non-military business of Thomson Semiconducteurs, the microelectronics business of the French state-controlled defense electronics company Thomson-CSF, and SGS Microelettronica, the microelectronics business owned by STET-Societa Finanziaria Telefonica S.p.A. ("STET"), the Italian state-controlled telephone company. Since its formation, the Company has significantly broadened and upgraded its range of products and technologies and has strengthened its manufacturing and distribution capabilities in Europe, North America, and the Asia Pacific region, while at the same time restructuring its operations to improve efficiency.

At the time of the Company's formation, SGS Microelettronica was the 20th largest semiconductor company in the world by revenues and the non-military semiconductor business of Thomson Semiconducteurs was of comparable size. At its inception, the Company was among the world's leading suppliers of intelligent power devices and bipolar power

transistors and a leading supplier to the telecommunications industry. SGS Microelettronica's strengths in power products, industrial products and automotive products and its presence in the emerging Asia Pacific market complemented Thomson Semiconducteurs' strengths in mixed-signal processing, telecommunications devices and consumer electronics, its presence in the North American market and its strong intellectual property portfolio, which included patents acquired when Thomson Semiconducteurs purchased substantially all of the assets of Mostek Corporation in 1985. The combination of the two European-based semiconductor businesses provided opportunities to realize operating efficiencies, consolidate global operations and better withstand downturns in the cyclical semiconductor industry, and facilitated the financing of research and development and capital expenditures necessary to compete effectively with the world's leading semiconductor companies.

Following the Company's formation, management implemented a comprehensive plan to rationalize the Company's operations, pursuant to which a variety of measures were taken to reduce fixed costs, improve product quality and increase yields. Between 1987 and 1992, the Company closed or sold ten manufacturing plants, and certain back-end and front-end production processes were shifted to lower cost facilities in the Mediterranean and Asia Pacific regions. Although it maintained a broad product line, the Company rationalized its product offerings and process technologies and focused on increasing its production of differentiated products. Management also standardized the Company's management information systems and consolidated management, administrative and sales staffs for the combined group.

To increase its presence in the microprocessor market, in April 1989 SGS-THOMSON acquired Inmos Ltd. ("Inmos"), a British semiconductor company that was founded in 1978 and purchased by Thorn EMI plc ("Thorn EMI") in 1984. In connection with its sale of Inmos to the Company, Thorn EMI and an affiliate acquired a 10% interest in SGS-THOMSON which has since been sold. In October 1989, the Company purchased the former microwave semiconductor business of Microwave Semiconductor Corporation, and in March 1993, SGS-THOMSON acquired the low current thyristors and triacs business of Tag Semiconductors Limited, a subsidiary of Raytheon Company.

Since its formation in 1987, the Company has maintained its commitment to research and development despite significant cost reductions during the Company's restructuring, particularly in 1990 and 1991 when the Company experienced losses. Management initially combined the research and development staffs of the predecessor companies and focused its expanded research and development resources on strategic products, applications and technologies. Beginning in 1993, the Company significantly increased its capital investments as part of a long-term program to upgrade and increase its manufacturing capabilities at existing plants and to build new facilities.

To provide the Company with a stronger capital structure, the Company's shareholders contributed capital totalling $800 million between 1988 and 1993. The Company used these funds in part to finance restructuring costs and to reduce net debt (total debt, including bank overdrafts, less cash and cash equivalents and marketable securities) from a high

of approximately $905 million at December 31, 1991 to 66.7 million at December 31, 1996. In December, 1994, the Company completed a registered public offering of Common Shares (the "Initial Public Offering") with net proceeds to the Company of approximately $198.7 million. In the Initial Public Offering, the Company sold 9,606,240 shares and the selling shareholders sold 11,393,760 shares at the initial price to public of $22.25 a share. In October 1995, the Company completed a secondary public offering of Common Shares in the U.S. and in France (the "Offering") with net proceeds to the Company of approximately $371.6 million. In the Offering, the Company sold 8,960,000 shares and the selling shareholders sold 11,740,000 shares at a price to public of $43.5 a share. See Item 4: "Control of Registrant". In February 1996, the Company also completed an offering of Common Shares to certain of its employees worldwide (the "1996 Employee Offering"). Common Shares offered in the 1996 Employee Offering were offered at a 5% discount to the market price as of January 5, 1996. In addition, eligible employees who purchased shares in the 1996 Employee Offering ("Participating Employees") and who held those shares at least until the first anniversary of the day on which such shares were issued to such Participating Employees, were entitled to purchase, for each lot of ten shares purchased in the 1996 Employee Offering, one additional share (a "Bonus Share") at a discounted price. The purchase price of each Bonus Share was the $ or FF equivalent of NLG 13.75, which is the nominal value per share. An aggregate of 253,397 new Common Shares were issued pursuant to the 1996 Employee Offering. In 1997, the Company intends to implement a share purchase plan which is intended to enable employees in most SGS-THOMSON locations worldwide to purchase, subject to various conditions, up to one million Common Shares to be newly issued.

Industry Background

Semiconductors are the basic building blocks used to create an increasing variety of electronic products and systems. Since the invention of the transistor in 1948, continuous improvements in semiconductor process and design technologies have led to smaller, more complex and more reliable devices at a lower cost per function. As performance has increased and size and cost have decreased, semiconductors have expanded beyond their original primary applications, computer systems, to applications such as telecommunications systems, automotive products, consumer goods and industrial automation and control systems. In addition, system users and designers have demanded systems with more functionality, higher levels of performance, greater reliability and shorter design cycle times, all in smaller packages at lower costs. These demands have resulted in increased semiconductor content as a percentage of system cost. Calculated on the basis of TAM (as defined below) as a percentage of worldwide revenues from production of electronic equipment according to published industry data (which for purposes of this annual report are data published by Dataquest, Inc. ("Dataquest")), semiconductor pervasiveness has increased from 9.0% in 1991 to 19.0% in 1995 and decreased to an estimated 15% in 1996. The demand for electronic systems has also expanded geographically with the emergence of new markets, particularly in the Asia Pacific region.

Semiconductor sales have increased significantly over the long term but have experienced significant cyclical variations in growth rates. According to trade association data

(which for all purposes of this annual report are World Semiconductor Trade Statistics ("WSTS")), worldwide sales of all semiconductor products (the total available market or "TAM") increased from $17.8 billion in 1983 to an estimate of $132 billion in 1996 (growing at a compound annual rate of approximately 17%, according to trade association data), while the market for products produced by the Company (the serviceable available market, or "SAM" -- which, prior to 1995 consisted of the TAM without DRAMs, microprocessors and opto-electronic products and commencing in 1995 and for all prior periods compared therewith includes microprocessors as a result of the Company's production of x86 products) increased from approximately $15.0 billion in 1983 to an estimate of $102.7 billion in 1996 (growing at a compound annual rate of approximately 16%). In 1996, the TAM decreased by 8.6% with sales in the Asia Pacific Region, the Americas, Europe and Japan decreasing by 6.7%, 9.2%, 2%, and 13.8%, respectively. In 1996, approximately 32.3% of all semiconductors were shipped to the Americas, 25.9% to Japan, 20.9% to Europe, and 20.9% to the Asia Pacific region.

Historically, cyclical changes in production capacity in the semiconductor industry and demand for electronic systems have resulted in pronounced cyclical changes in the level of semiconductor sales and fluctuations in prices and margins for semiconductor products from time to time. However, certain significant changes in the industry could contribute to continued growth over the long term notwithstanding cyclical variations from period to period. Such changes include the development of new semiconductor applications, increased semiconductor content as a percentage of total system cost, emerging strategic partnerships, growth in the electronic systems industry in the Asia Pacific region.

Business Outlook

From market data related to 1996, it is evident that the industry has started a correction from the extraordinary growth of recent years. The Company, however, entered 1997 in a healthy financial condition, and with a strong market position despite the strong corrections experienced by the industry in 1996. Market conditions remained difficult in the first quarter of 1997, with continuing overall price pressures that negatively impacted the Company's sales. As the quarter came to a close, however, the Company saw signs that the market was improving as prices of several standard products began to stabilize, and in some cases recover from recent low levels. In addition, the Company's order rates accelerated in March. Although overall order visibility remained modest, it improved over the fourth quarter of 1996. Certain industry analysts expect a growth rate for 1997 compared to a market decline in 1996. It is evident, however, that decreased visibility on customer demand has made it somewhat more difficult to predict market conditions.

On June 5, 1997, the Company announced that, based on available information for the first two months of its second quarter, it expects its net revenue for the second quarter ending June 28, 1997 to be above the first quarter level, but below analysts' expectations, and its gross margin to be similar to that of the first quarter due to a short-term shift in product mix.

The Company also stated that its net earnings for the second quarter are likely to be within a range approximating first quarter 1997 levels.

In the first two months of the quarter, a larger than anticipated percentage of net sales was derived from commodity products such as Standard ICs and Memories. Worldwide demand for these products has strengthened in the last several months, but pricing remains low and the gross margin associated with them is significantly below that of SGS-THOMSON's differentiated products.

Looking ahead, the Company reaffirmed that it expects 1997 to be a year of progressive improvement for the Company and that second half results should benefit from better overall market conditions and a greater contribution from sales of differentiated products.

In 1997, the Company intends to continue to emphasize its expertise in differentiated products while continuing to offer commodity products that contribute volume, profit and cash flow. The Company is confident, however, that the heavy emphasis on differentiated products in its portfolio, its strong customer base and strategic alliances, together with its well diversified sales base, both in terms of applications and geography, should allow SGS-THOMSON to again outpace the rate of growth in its served market. The Company also remains confident about its long-term growth prospects as well as those of the market it serves and consequently intends to move ahead with capital expenditure and research and development plans, committing a percentage of revenue on the same order of magnitude as during 1996.

The above statements contained in this "Business Outlook" are forward looking statements that involve a number of risks and uncertainties. In addition to the factors discussed above, among the other factors that could cause actual results to differ materially are the following: the cyclicality of the semiconductor and electronic systems industries; capital requirements and the availability of funding; competition; new product development and technological change; manufacturing risks; order cancellations or reduced bookings by key customers or distributors; intellectual property developments, international events, currency fluctuations; problems in obtaining adequate raw materials on a timely basis; and the loss of key personnel. Unfavorable changes in the above or other factors discussed under "Risk Factors" listed from time to time in the Company's SEC reports, including in the Company's Prospectus dated October 18, 1995 (pages 9 through 16), could materially affect the Company.

Semiconductor Classifications

The process technologies, levels of integration, design specificity, functional technologies and applications for different semiconductor products vary significantly. As differences in these characteristics have increased, the semiconductor market has become highly diversified as well as subject to constant and rapid change. Semiconductor product markets may be classified according to each of these characteristics.

Semiconductors can be manufactured using different process technologies, each of which is particularly suited to different applications. Since the mid-1970s, the two dominant processes have been bipolar (the original technology used to produce integrated circuits) and CMOS (complementary metal-oxide-silicon). Bipolar devices typically operate at higher speeds than CMOS devices, but CMOS devices consume less power and permit more transistors to be integrated on a single IC. While bipolar semiconductors were once used extensively in large computer systems, CMOS has become the most prevalent technology, particularly for devices used in personal computer systems. In connection with the development of new semiconductor applications and the demands of system designers for more integrated semiconductors, advanced technologies have been developed during the last decade that are particularly suited to more systems-oriented semiconductor applications. For mixed-signal applications, BiCMOS technologies have been developed to combine the high speed and high voltage characteristics of bipolar technologies with the low power consumption and high integration of CMOS technologies. For intelligent power applications, BCD technologies have been developed that combine bipolar, CMOS and DMOS technologies. Such systems-oriented technologies require more process steps and mask levels, and are more complex than the basic function-oriented technologies. The use of systems-oriented technologies requires knowledge of system design and performance characteristics (in particular, analog and mixed-signal systems and power systems) as well as expertise and experience with several semiconductor process technologies.

Semiconductors are often classified as either discrete devices (such as individual diodes or transistors) or integrated circuits (in which thousands of functions are combined on a single "chip" of silicon to form a more complex circuit). Compared to the market for ICs, there is typically less differentiation among discrete products supplied by different semiconductor manufacturers. Also, discrete markets have generally grown at slower, but more stable, rates than IC markets.

Semiconductors may also be classified as either standard components or application-specific ICs ("ASICs"). Standard components are used by a large group of systems designers for a broad range of applications, while ASICs are designed to perform specific functions in specific applications. Generally, there are three types of ASICs: full-custom devices, semicustom devices and application-specific standard products ("ASSPs"). Full custom devices are typically designed to meet the particular requirements of one specific customer. Semicustom devices are more standardized ICs that can be customized with efficient CAD tools within a short design cycle time to perform specific functions. ASSPs are standardized ASICs that are designed to perform specific functions in a specific application, but are not proprietary to a single customer.

The two basic functional technologies for semiconductor products are analog and digital. Analog (or linear) devices monitor, condition, amplify or transform analog signals, which are signals that vary continuously over a wide range of values. Analog circuits are critical as an interface between electronic systems and a variety of real world phenomena such as sound, light, temperature, pressure, weight or speed. Electronics systems continuously translate analog signals into digital data, and vice versa.

The analog semiconductor market consists of a large and growing group of specific markets that serve numerous and widely differing applications, including applications for automotive systems, instrumentation, computer peripheral equipment, industrial controls, communications devices, video products and medical systems. Because of the varied applications for analog circuits, manufacturers typically offer a greater variety of devices to a more diverse group of customers. Compared to the market for commodity digital devices such as standard memory and logic devices, the analog market is characterized by longer product life cycles, products that are less vulnerable to technological obsolescence, and lower capital requirements due to the use of mature manufacturing technologies. Such characteristics have resulted in growth rates that have been less volatile than growth rates for the overall semiconductor industry.

Digital devices perform binary arithmetic functions on data represented by a series of on/off states. Historically, the digital IC market has been primarily focused on the fast growing markets for computing and information technology systems. Increasing demands for high-throughput computing and networking and the proliferation of more powerful personal computers and workstations in recent years have led to dramatic increases in digital device density and integration. As a result, significant advances in electronic system integration have occurred in the design and manufacture of digital devices.

There are two major types of digital ICs: memory products and logic devices. Memory products, which are used in electronic systems to store data and program instructions, are generally classified as either volatile memories (which lose their data content when power supplies are switched off) or nonvolatile memories (which retain their data content without the need for constant power supply). Volatile memories are used to store data in virtually all computer systems, from large and mid-range computers to personal computers and workstations. The primary volatile memory devices are DRAMs, which accounted for 69.8% of semiconductor memory sales in 1996. Nonvolatile memories are typically used to store program instructions that control the operation of microprocessors and electronic systems. The primary nonvolatile memory devices are EPROMs, flash memories and EEPROMs. Memory products are typically standard, general purpose ICs that can be manufactured in high volumes using basic CMOS processes, and they are generally differentiated by cost and physical and performance characteristics, including data capacity, die size, power consumption and access speed.

Logic devices process digital data to control the operation of electronic systems. The largest segment of the logic market, standard logic devices, include microprocessors, microcontrollers and digital signal processors. Microprocessors are the central processing units of computer systems. Microcontrollers are complete computer systems contained on single integrated circuits that are programmed to control the operation of electromechanical systems by processing input data from electronic sensors and generating electronic control signals. Digital signal processors ("DSPs") are parallel processors used for high complexity, high speed real-time computations in a wide variety of applications, including digital cellular telephone systems and data compression systems. Standard devices are intended to be utilized by a large group of systems designers for a broad range of applications. Consequently, standard devices

usually contain more functions than are actually required and, therefore, may not be cost-effective for certain specific applications. In addition to standard logic devices, a broad range of full-custom, semicustom and ASSP logic devices has been developed for a wide variety of applications. These devices are typically designed to meet particular customer requirements. Compared to memory markets, logic device markets are much more differentiated and dependent upon intellectual property and advanced product design skills.

Analog/digital (or "mixed-signal") ICs combine analog and digital devices on a single chip to process both analog signals and digital data. Historically, analog and digital devices have been developed separately as they are fundamentally different and it has been technically difficult to combine analog and digital devices on a single IC. System manufacturers have generally addressed mixed-signal requirements using printed circuit boards containing many separate analog and digital circuits acquired from multiple suppliers. However, system designers are increasingly demanding system level integration in which complete electronic systems containing both analog and digital functions are integrated on a single IC.

Mixed-signal ICs are typically characterized as analog ICs due to their similar market characteristics, including longer product life cycles, diverse applications and customers and more stable growth through economic cycles as compared to digital devices. However, certain parts of the mixed-signal market are becoming higher volume markets as the increasing use of mixed-signal devices has enhanced the options of system designers and contributed to the development of new applications, including multimedia, video conferencing, automotive, mass storage and personal communications.

The Semiconductor Market

The following tables set forth information with respect to worldwide semiconductor sales by type of semiconductor and geographic region:

	Worldwide Semiconductor Sales(1)					Compound Annual Growth Rates(2)				
	1983	1988	1993	1995	1996	83-88	88-93	83-93	93-95	93-96
	(in millions)									
Integrated Circuits .	$ 13,335	$ 35,893	$ 66,018	$126,056	$114,941	21.9%	13.0%	17.3%	38.2%	20.3%
Analog (linear and mixed-signal)	2,875	7,228	10,673	16,646	17,044	20.2	8.1	14.0	24.6	16.9
Digital										
Logic	6,712	17,750	34,079	55,953	61,879	21.5	13.9	17.6	28.2	22.0
Memory										
DRAM	1,741	6,390	13,140	40,833	25,132	29.7	15.5	22.4	76.3	24.0
Others	2,007	4,524	8,127	12,624	10,886	17.7	12.4	15.0	24.6	10.2
Total Memory ...	3,748	10,914	21,267	53,457	36,018	23.8	14.3	19.0	58.5	19.2
Total digital	10,460	28,664	55,346	109,410	97,897	22.3	14.1	18.1	40.6	20.9
Discrete	3,696	6,999	8,637	14,004	12,878	13.6	4.3	8.9	27.3	14.2
Opto-electronics	736	2,113	2,654	4,344	4,147	23.5	4.7	13.7	27.9	16.0
TAM	$ 17,767	$ 45,005	$ 77,309	$144,404	$131,966	20.4%	11.4%	15.8%	36.7%	19.5
Europe	$ 3,320	$ 8,104	$ 14,599	$ 28,199	27,562	19.5%	12.5%	15.9%	39.0%	23.6%
Americas	7,761	13,418	24,744	46,998	46,679	11.6	13.1	12.3	37.8	19.9
Asia Pacific	1,150	5,374	14,168	29,540	27,550	36.1	21.4	28.5	44.4	24.8
Japan	5,536	18,109	23,798	39,667	34,175	26.7	5.6	15.7	16.1	12.8
TAM	$ 17,767	$ 45,005	$ 77,309	$144,404	$131,966	20.4%	11.4%	15.8%	36.7%	19.5

(1) Source: WSTS.
(2) Calculated using end points of the periods specified.

During the 1960s and 1970s, the development of semiconductor process technologies was critical to the success of participants in the industry. As process technologies matured, manufacturing sciences became important; in the 1980s, the emphasis shifted to increasing production volumes and yields and lowering production costs. The large capital expenditures and other resources required during this period to develop advanced manufacturing capabilities resulted in a stratification of the industry between broad range suppliers operating multiple front-end and back-end manufacturing facilities and specialty niche players operating small wafer fads or subcontracting wafer production.

With the continuing development of new semiconductor applications and increasing demands of system designers for more integrated systems-oriented products, semiconductor manufacturers must continually improve their core technology and manufacturing competencies. In addition, the increasing diversity and complexity of semiconductor products, the demands of technological change, and the costs associated with keeping pace with industry developments have contributed to the growth of cooperative product design and development and manufacturing alliances with customers as well as among semiconductor suppliers. Alliances with customers provide the manufacturer with valuable systems and application know-how and access to markets for key products, while allowing the manufacturer's customers to share some of the risks and benefits of product development. Customers also gain access to the manufacturer's process technologies and manufacturing infrastructure. Alliances with other semiconductor manufacturers permit costly research and development and manufacturing resources to be shared to mutual advantage for joint technology development.

To compete as a broad line semiconductor manufacturer, management believes that it is important to have: (i) a broad and diverse customer base; (ii) a diversified product portfolio (including analog, digital mixed-signal and power products) and experience in several application markets; (iii) a broad range of process technologies (including basic function-oriented and advanced systems-oriented technologies); (iv) an efficient, quality, global manufacturing infrastructure; (v) global marketing and technical support; and (vi) a worldwide network of strategic alliances with customers and other semiconductor manufacturers.

Strategy

Since the Company's formation in 1987, management's objectives have been to become one of the world's top ten semiconductor suppliers and to achieve operating results better than the average of the top ten semiconductor suppliers. According to preliminary industry data, in 1996 SGS-THOMSON became one of the top 10 worldwide suppliers of semiconductor devices. To achieve these objectives, the Company has focused on using its core technology and manufacturing competencies to produce innovative, quality and cost-effective products. The key elements of the Company's strategy are set forth below.

Maintain Broad Customer Base and Increase Customer Penetration. The Company works with its key customers to identify evolving needs and new applications and to develop innovative products and product features. The Company also seeks to use its access to key customers as a supplier of application-specific products to establish itself as a supplier across a broad range of products. The Company maintains a geographically diverse customer base across a broad range of market applications. Regional sales and marketing organizations operate in each of Europe, the United States, the Asia Pacific region and Japan. In addition, the Company's central strategic marketing team and key account management teams serve selected multinational customers.

Offer Diversified Product Portfolio in Evolving Application Markets. The Company offers a diversified product portfolio and develops products for a wide range of market

applications to reduce its dependence on any single product, industry or application market. As a broad range supplier, the Company provides its customers with a single source of supply for multiple product needs. In the telecommunications market, the Company is developing advanced BiCMOS and high frequency bipolar processes and focusing on products for the switching equipment and new, fast-growing telecommunications markets, including the digital cellular telephone and the asynchronous transfer mode communication systems market. In the computer market, the Company produces dedicated products, memories, microcontrollers, semicustom devices and microprocessors for use in all types of computer systems. The Company is focusing particularly on the development of a family of flash memory products and dedicated products for computer monitors, disk drives and printers. In addition, the Company has started to manufacture and market x86 microprocessors. In the consumer products market, the Company is developing dedicated products for television and home entertainment systems and devices for new multimedia applications, including digital video decoders. In the automotive market, management is using its BCD processes to develop dedicated products for a wide range of automotive applications, including engine management and safety, and is developing devices for new applications such as global positioning systems. In the industrial market, the Company is developing innovative power products, particularly for use in lighting systems and switch mode power supplies.

Develop Advanced Process and Design Technologies. The Company intends to continue to exploit its expertise and experience with a wide range of process and design technologies to develop more advanced technologies. The Company is committed to continuing to increase research and development expenditures in the future. Despite significant cost reductions following the Company's formation in 1987 and particularly during 1990 and 1991 when the Company experienced losses, management did not reduce research and development spending. The Company is using its memory products as the focal point of its process development efforts due to their standardized design features, manufacturability and potential high volumes. Technological advances in the areas of transistor performance and interconnection technologies are being developed through the Company's logic products and semicustom devices. In 1996, the Company developed a 0.25 micron, six-metal layers process that can be used to create either circuits which operate at high speed (clock frequency of 400 MHZ at 2.5V) or circuits with low power consumption (1.0V) and capable of densities of up to 30,000 gates per square millimeter. It is also working closely with many of its key customers on developing easy-to-use design equipment for specific applications. The Company is developing advanced and standardized design tools for its CMOS processes as well as libraries of macrofunctions and megafunctions for many of its products, and is focusing on improving its concurrent engineering practices to better coordinate design activities and reduce overall time-to-market.

Expand and Improve Manufacturing Capabilities. In 1996, SGS-THOMSON expanded its diversified manufacturing infrastructures while improving the cost, quality and flexibility of its operations. SGS-THOMSON has applied 1996 investments in its manufacturing facilities to bring to full capacity the 8-inch front-end manufacturing facility in Crolles, France, to continue the ramp-up of the new 8-inch front-end manufacturing facility in Phoenix, Arizona,

to complete the building of and to begin equipping the third 8-inch front-end manufacturing facility in Catania, Italy, and to continue to build and equip a new back-end facility and design center in Shenzhen, China, through its joint venture created in 1994 with a subsidiary of the Shenzhen Electronics group. During 1996, the Company has also completed conversion from 4-inch to 5-inch of the two front-end wafer fabrication modules in Tours, France, from 5-inch to 6-inch of the front-end wafer fabrication facility in Rousset, France, and has installed a new 6-inch module in the Rancho Bernardo, California front-end wafer fabrication facility. In addition, the Company has started construction of a new 8-inch front-end wafer fabrication facility in Rousset, France, has initiated the 6-inch to 8-inch conversion of one of its Agrate, Italy front-end wafer fabrication plants, and has started planning the construction of a new 8-inch front-end wafer fabrication facility in Singapore, announced during 1996. Finally, the Company plans one more 8-inch front-end wafer fabrication plant to be built in Italy. In 1996, approximately 93% of the ICs wafers manufactured by SGS-THOMSON were manufactured on 5-, 6- and 8-inch wafers. The Company fosters a corporate-wide Total Quality Management ("TQM") culture that defines a common set of objectives and performance measurements for employees in all geographic regions, at every stage of product design, development and production for all product lines. SGS-THOMSON has established front-end and back-end manufacturing facilities in each of Europe, the United States and the Mediterranean and Asia Pacific regions. The Company's geographically diverse facilities allow it to shift production to accommodate variable production requirements.

Emphasize Differentiated ICs. Within its diversified product portfolio, the Company has focused on developing products that exploit its technological strengths, including differentiated ICs (which the Company defines as being its dedicated products, semicustom devices and microcontrollers). Differentiated ICs foster close relationships with customers, resulting in early knowledge of their evolving requirements and opportunities to access their markets for other products, and are less vulnerable to competitive pressures than standard commodity products. Differentiated ICs accounted for approximately 59% of the Company's net revenues in 1996 compared to approximately 51% in 1995. The Company also targets applications that require substantial analog and mixed-signal content and can exploit the Company's system level expertise. Analog ICs (including mixed-signal ICs), the majority of which are also differentiated ICs, accounted for approximately 46% of the Company's 1996 net revenues (unchanged from 1995), while discrete devices accounted for approximately 14% of the Company's 1996 net revenues (compared to 17% in 1995). In recent years, analog ICs and discrete devices have experienced less volatility in sales growth rates and average selling prices than the overall semiconductor industry.

Expand Strategic Alliances. Consistent with its belief that strategic alliances are critical to success in the semiconductor industry, the Company has entered into such alliances with customers, other semiconductor manufacturers and a major supplier of design software. The Company has entered into several customer strategic alliances, including with Alcatel, Bosch, Seagate Technology, Thomson Multimedia, and Western Digital, among others. Alliances with customers provide the Company with valuable systems and application know-how and access to markets for key products, while allowing the Company's customers to share some

of the risks of product development with SGS-THOMSON and to gain access to the Company's process technologies and manufacturing infrastructure. Alliances with other semiconductor manufacturers are generally designed to permit costly research and development and manufacturing resources to be shared to mutual advantage for joint technology development. Technology development alliances have been formed with customers and other manufacturers, including Philips Semiconductors in Europe to develop sub-micron CMOS technologies and Northern Telecom in North America to develop advanced 0.5 micron BiCMOS mixed-signal technologies and Mitsubishi in Japan to develop a family of 16 Mbit flash memories for mass storage applications. The Company has also established joint development programs with leading suppliers such as Applied Materials, ASM Lithography, LAM and Air Liquide, and with CAD Tools producers including Cadence, Synopsis and Mentor. It is a participant in Sematech I 300I for the development of 300 millimeter wafer manufacturing processes. SGS-THOMSON is active in joint European research efforts such as the new MEDEA program (which succeeded to JESSI as of 1997), and also cooperates with major research institutions and universities.

Customers and Applications

SGS-THOMSON designs, develops, manufactures and markets over 3,000 main types of products that it sells to more than 1,500 customers. To many of its key customers the Company provides a wide range of products, including dedicated products, discrete devices, memory products and programmable products. The Company's position as a strategic supplier of application-specific products to certain customers fosters close relationships that provide it with opportunities to supply such customers' requirements for other products, including discrete devices, programmable products and memory products.

The following table sets forth certain of the Company's significant customers in 1996 and certain applications for its products:

Telecommunications				
Customers:	Alcatel	Gemplus	Nortel	Schlumberger
	AT&T	Goldstar	Orga	Siemens
	Daewoo	Italtel	Philips	
	Ericsson	Motorola	Sagem	
	Fujitsu	Nokia	Samsung	
Applications:	Answering machines		ISDN controllers	
	Central office switching systems		Modems	
	Chips for smartcards		PBX systems	
	Digital cellular telephones		Telephone sets (corded and cordless)	
Computer Systems				
Customers:	ACER	Creative Technologies	IBM	Tatung
	ATI Technologies	Cyrix	Matsushita	Western Digital
	Bull	DEC	Olivetti	Xerox
	Canon	Epson	Quantumi	
	Compaq	Hewlett-Packard	Seagate Technology	
Applications:	Chips for smartcards		Optical scanners	
	Disk drives		Photocopiers	
	Monitors		Printers	
	Network controllers			
Automotive				
Customers:	BMW	Daimler-Benz	Ford	Marelli
	Bosch	Delco	Hyundai	Valeo
	Chrysler	Fiat	Peugeot S.A.	Renault
Applications:	Alternator regulators		Ignition circuits	
	Airbags		Injection circuits	
	Antiskid braking systems		Instrument	
	Automotive entertainment systems		Electric Motor Controllers	
	Body and chassis electronics		Multiplex wiring kits	
	Central locking systems		Transmission control systems	
	Engine management systems			
Consumer Products				
Customers:	Canal Plus	Goldstar	Nokia	Sharp
	Canon	Grundig	Pace	Sony
	Creative Technology	Kenwood	Philips	Thomson Multimedia
	Daewoo	Matsushita	Pioneer	
	General Instrument	NEC	Samsung	
Applications:	Audio power amplifiers		Graphic equalizers	
	Audio processors		Pay television decoders	
	Cable television systems		Satellite receiver decoding circuits	
	Compact disc players		Set up boxes	
	Digital video encoders and decoders		TV sets and monitors	
			Video cassette recorders	
Industrial and Other Applications				
Customers:	Astec	Emerson	Philips	Siemens
	Asea Brown Boveri	Mannesman	Schlumberger	Schneider
Applications:	Battery chargers		Motor controllers	
	Industrial automation and control systems		Power supplies	
	Intelligent power switches		Smartcard readers	
	Lighting systems (lamp ballasts)		Switch mode power supplies	

Two customers each accounted for slightly above 5% of the Company's net revenues in 1996 and sales to the Company's top ten customers accounted for approximately 38% of the Company's net sales in 1996. The Company has several large customers, certain of whom have entered into strategic alliances with the Company. Many of the Company's key customers operate in cyclical businesses and have in the past, and may in the future, vary order levels significantly from period to period. In addition, approximately 21% of the Company's net revenues in 1996 were made through distributors. There can be no assurance that such customers or distributors, or any other customers, will continue to place orders with the Company in the future at the same levels as in prior periods. The loss of one or more of the Company's customers or distributors, or reduced bookings by its key customers or distributors, could adversely affect the Company's operating results. In addition, in a declining market the Company has in the past and may in the future be requested to reduce prices to limit the level of order cancellations. Despite price reductions, however, in an industry downturn order cancellations may be expected, particularly by distributors and for commodity products.

Products and Technology

SGS-THOMSON designs, develops, manufactures and markets a broad range of products used in a wide variety of microelectronic applications, including telecommunications systems, computer systems, consumer goods, automotive products and industrial automation and control systems. The Company's products include standard commodity components, full custom devices, semicustom devices and ASSPs for analog, digital and mixed-signal applications. Historically, the Company has not produced DRAMs or, until recently, x86 microprocessors. The SAM represented approximately 77.8% of the TAM in 1996, compared to 84% of the TAM in 1983. While the TAM increased at a compound annual growth rate of approximately 17% from $17.8 billion in 1983 to an estimate of $132 billion in 1996, the SAM increased at a compound annual growth rate of approximately 16% from $15.0 billion to an estimate of $102.7 billion during the same period.

The Company's products are organized into five principal product groups: Dedicated Products, Discrete and Standard ICs, Memory Products, Programmable Products and the New Ventures Group.

Dedicated Products Group

The Dedicated Products Group designs, develops and manufactures application-specific products using advanced bipolar, CMOS, mixed-signal and power technologies. The Group offers complete system solutions to customers in several application markets. As the largest of SGS-THOMSON's product groups, the Dedicated Products Group generated revenues of $1,757.7 million in 1996 (an increase of 29.3% over 1995 revenues), representing approximately 43% of SGS-THOMSON's 1996 revenues. Approximately 33.2% of the Group's revenues in 1996 were generated in Europe, while approximately 23.3%, 37.8%, and 5.7% were generated in the Americas, the Asia Pacific region, and Japan, respectively. Many of the dedicated products sold to the Asia Pacific region are sold to U.S.-based original equipment

manufacturers located in the region. All of the Group's products are ASSPs or full custom devices.

The Dedicated Products Group works closely with customers to develop application-specific products using SGS-THOMSON's technologies and manufacturing capabilities. The breadth of the Group's customer and application base provides it with a source of stability in the cyclical semiconductor market. In addition, the Company's position as a strategic supplier of application-specific products fosters close relationships that provide it with opportunities to supply such customers' requirements for other products, including discrete devices, programmable products and memory products.

The Group particularly emphasizes dedicated ICs for telecommunications, audio, automotive, power and computer applications.

The Group is organized into the following four product divisions: (i) telecommunications; (ii) computer and industrial; (iii) audio and automotive; and (iv) video. In addition, the Company created a business unit to design and manufacture products for the emerging digital video processing industry.

Telecommunications Products. According to preliminary published industry data, in 1996, SGS-THOMSON was the world's second largest supplier of dedicated telecommunications ICs. The Company's telecommunications products are used primarily in telephone sets, modems and subscriber line interface cards (SLICs) for digital central office switching equipment. The Group is targeting applications in mobile communications networks and telephone sets and asynchronous transfer mode ("ATM") communication systems.

Computer and Industrial Products. SGS-THOMSON's computer and industrial products include components for computer peripheral equipment, facsimile machines, photocopiers, industrial automation systems and lighting applications. Its key products are power ICs for motor controllers and read/write amplifiers, intelligent power ICs for spindle motor control and head positioning in computer disk drives and battery chargers for portable electronic systems, particularly mobile telephone sets.

Audio and Automotive Products. SGS-THOMSON's audio products include audio power amplifiers, audio processors and graphic equalizer ICs. The Company has sold more than 1.2 billion audio power amplifier ICs since 1972.

The Company's automotive products include alternator regulators, airbag controls, antiskid braking systems, ignition circuits, injection circuits, multiplex wiring kits and products for body and chassis electronics, engine management and instrumentation systems. The Company is currently targeting the emerging application of global positioning systems.

Video Products. SGS-THOMSON produces ICs for TV sets, monitors, videocassette recorders, satellite receivers, pay-tv decoders and digital video disks. The

Company is focusing on developing products for applications in the growing U.S. satellite and cable television markets. Leveraging its BCD Technology know how, the Group is now targeting the emerging market of flat panel displays.

Image Processing. SGS-THOMSON has created a business unit to design and manufacture products for the emerging digital video processing industry. Emerging digital video technologies offer a number of advantages over traditional analog video, including the ability to compress video data for transmission and storage, to transmit and reproduce video data without perceptible image degradation and to randomly access and edit video data.

Despite the advantages of digital video, its widespread adoption has been constrained by the lack of high-performance, cost-effective compression devices and by the absence of digital video compression standards. Video compression, which uses complicated mathematical algorithms operating at high speeds to encode the large amounts of data that result from digitizing video signals, is both highly complex and technically challenging. Digital video compression technology is expected to contribute to the development of a number of new or enhanced applications in the consumer electronics, computer and communications markets, including video CD players, interactive game consoles and video conferencing systems.

The Company's image processing business unit delivers large volumes of Motion Picture Experts Group ("MPEG") decoder ICs suitable for video CD products, personal computers, multimedia and digital TV applications. These products implement the MPEG 1 standard for CD ROM, video CD and personal computer applications and the MPEG 2 standard for digital TV applications (both cable and satellite digital TV). This unit is also developing products for emerging video phone applications. According to the latest published industry data, in 1995 SGS-THOMSON was the leading supplier of MPEG decoder ICs with an approximately 44.3% share of the MPEG decoders market.

Discrete and Standard ICs Group

The Discrete and Standard ICs Group designs, develops, and manufactures discrete power devices, power transistors, standard logic and linear ICs, and RF products (which were transferred to the Discrete and Standard ICs Group in May 1994). Including revenues from RF products, the Group generated revenues of $784.1 million in 1996 (a decrease of 6.4% over 1995 revenues), representing approximately 19% of SGS-THOMSON's net revenues. Approximately 53% of the Group's 1996 revenues were generated in Europe, while approximately 21.5%, 23.9%, and 1.6% were generated in the Americas, the Asia Pacific region, and Japan, respectively. According to preliminary published industry data, based on 1996 revenues, SGS-THOMSON is among the top four suppliers of power transistors (1996 total market of $4.9 billion) and thyristors (1996 total market of $738 million).

The Group's discrete and standard products are manufactured using mature technological processes. Although such products are less capital intensive than the Company's other principal products, the Company is continuously improving product performance and

developing new product features. The Group has a diverse customer base, and a large percentage of the Group's products are sold through distributors.

Discrete Power Devices. SGS-THOMSON manufactures and sells a variety of discrete power devices, including rectifiers, protection devices and thyristors (SCRs and triacs). The Company's devices are used in various applications, including in particular telecommunications systems (telephone sets, modems and line cards), household appliances and industrial systems (motor control and power control devices). More specifically, rectifiers are used in voltage converters and voltage regulators, protection devices are used to protect electronic equipment from power supply spikes or surges, and thyristors are used to vary current flows through a variety of electrical devices, including lamps and household appliances.

Power Transistors. SGS-THOMSON designs, manufactures and sells power transistors, which (like the Company's discrete power devices) operate at high current and voltage levels in a variety of switching and pulse mode systems. The Company has three power transistor divisions: bipolar transistors, power MOSFETs (metal-oxide-silicon field effect transistors) and new power transistors such as IGBTs.

The Company's bipolar power transistors are used in a variety of high-speed, high-voltage applications, including SMPS (switch mode power supply) systems, television/monitor deflection circuits and lighting systems. According to preliminary published industry data, on the basis of 1996 revenues, SGS-THOMSON is among the leading suppliers of bipolar transistors, including RF power transistors (1996 total market of $2.2 billion). The Company introduced power MOSFETs in 1991 to extend the use of power transistors to new high-frequency, high-voltage applications, including automotive components, crowbar protection devices, resonant converters and power factor correction devices. According to industry data, the Company has been ranked number five worldwide in the fast growing segment of the power MOSFETs.

The Company also offers a family of VIPower (vertical integration power) products, as well as omnifets and application-specific devices. VIPower products exhibit the operating characteristics of power transistors while incorporating full thermal, short circuit and overcurrent protection and allowing logic level input. VIPower products are used in consumer goods (lamp ballasts) and automotive products (ignition circuits, central locking systems and transmission circuits). Omnifets are power MOSFETs with fully-integrated protection devices that are used in a variety of sophisticated automotive and industrial applications. Application-specific devices are semicustom ICs that integrate diodes, rectifiers and thyristors on the same chip, thereby providing cost-effective and space-saving components with a short design time.

Standard Logic and Linear ICs. The Company produces a variety of bipolar and HCMOS logic devices, including clocks, registers, gates and latches. Such devices are used in a wide variety of applications, including increasingly in portable computers, computer networks and telecommunications systems.

The Company also offers standard linear ICs covering a variety of applications, including amplifiers, comparators, decoders, detectors, filters, modulators, multipliers and voltage regulators.

Radio Frequency Products. The Company supplies components for RF transmission systems used in television broadcasting equipment, radar systems, telecommunications systems and avionic equipment. At present, most of the Company's RF products are sold in the United States. The Company is targeting new applications for its RF products, including two-way wireless communications systems (in particular, cellular telephone systems) and commercial radio communication networks for business and government applications.

Memory Products Group

The Memory Products Group designs, develops and manufactures a broad range of semiconductor memory products. The Memory Products Group generated revenues of $736.8 million in 1996 (an increase of 12.8% over 1995 revenues), representing approximately 18% of SGS-THOMSON's 1996 revenues. Approximately 53.1% of the Group's 1996 revenues were generated in Europe, while approximately 19.5%, 14.4%, and 13.0% were generated in the Americas, the Asia Pacific region, and Japan, respectively. According to preliminary published industry data, on the basis of 1996 revenues, SGS-THOMSON was the leading producer of EPROMs (1996 total market of $1.1 billion) and the leading supplier of EEPROMs (1996 total market of $1.1 million).

There are two basic types of memory devices, random access memories ("RAMs") and non-volatile. RAMs are typically used in microprocessor systems to store data used in the operation of such systems, whereas Non-Volatile Memory is typically used to store program instructions that control the operation of microprocessors and electronic systems.

The most common types of RAMs are DRAMs (dynamic RAMs) and SRAMs (static RAMs). DRAMs are volatile memories that lose their data content when power supplies are switched off, whereas SRAMs are volatile memories that allow the storage of data in the memory array but without the need for clock or refresh logic circuitry. SRAMs are roughly four times as complex as DRAMs (four transistors per bit of memory compared to one transistor) and are significantly more expensive than DRAMs per unit of storage. DRAMs are used in a computer's main memory to temporarily store data retrieved from low cost external mass memory devices such as hard disk drives. SRAMs are principally used as caches and buffers between a computer's microprocessor and its DRAM-based main memory.

There are several types of non-volatile memories that offer varying degrees of functionality at varying costs. Among such non-volatile memories, read-only memories ("ROMs") are permanently programmed when they are manufactured while programmable ROMs (PROMs) can be programmed by system designers or end-users after they are manufactured. Erasable PROMs (EPROMs) may be erased and reprogrammed several times,

but to do so EPROMs must be physically removed from electronic systems, exposed to ultraviolet light, reprogrammed using an external power supply and then returned to the systems. Electrically erasable PROMs (EEPROMs) can be erased byte by byte and reprogrammed "in-system" without the need for removal. Using EEPROMs, a system designer or user can program or reprogram systems at any time.

"Flash" memories are relatively new products that represent an intermediate solution for system designers between EPROMs and EEPROMs based on their cost and functionality. Flash memories are typically less expensive than EEPROMs, but can also be erased and rewritten. The entire contents of a flash memory or large blocks of data (not individual bytes) can be erased with a "flash" of current. Because flash memories can be erased and reprogrammed electrically and in-system, they are more flexible than EPROMs and, therefore, may replace EPROMs in many of their current applications. Flash memories may also be used for solid state mass storage of data, a potentially high volume application, and in other applications, including, in particular mobile telephone systems. Flash memories are smaller and use less power than the hard disk drives now commonly used for mass data storage, and, therefore, are considered candidates to replace disk drives, particularly in portable computers.

According to preliminary published industry data, the TAM for memory devices in 1996 was approximately $36.0 billion, with DRAMs, SRAMs, ROMs, EPROMs, flash and EEPROMs accounting for approximately 69.8%, 13.2%, 3.7%, 3.1%, 7.2% and 3.0% of the total, respectively.

The Company's Memory Products Group is organized into the following divisions: (i) EPROMs; (ii) flash memories; (iii) EEPROMs and application-specific memories; (iv) SRAMs; and (v) smartcard products.

EPROMs. SGS-THOMSON produces a broad range of EPROMs, from 16 Kbit to 16 Mbit. According to preliminary industry data, SGS-THOMSON consolidated its world's leading market position for EPROMS in 1996, with revenues of $335.5 million (basically unchanged over 1995 despite a sharp market decline) or approximately 30.4% of worldwide EPROM sales. The Company currently produces EPROMs using 0.5 micron CMOS technologies.

The EPROM market is relatively mature and it has been declining in 1996 according to preliminary industry data. Nevertheless, in 1996, the Company succeeded in maintaining its sales level and in further consolidating its market leadership because of its best in class EPROM technology. This technology has, in fact, allowed the Group to build one of the broadest product portfolios currently offered in the market, and at the same time it has enabled continuous improvement of manufacturing yields and reduction of die size, thus leading the Company to an extremely advantageous cost position. Efficient manufacturing in the Singapore and Malaysia assembly plants together with SGS-THOMSON's large sales and

distribution channels around the world have allowed the full exploitation of the technological advantage.

Due to the volatility of EPROM supply, prices reached a top high at the beginning of 1996, and then progressively declined, because of industry oversupply, to an end of year low basically in line with the price at the beginning of 1995.

Flash Memories. The Company is using its EPROM and EEPROM know-how to develop advanced flash memory products, and currently produces flash memories up to 4 Mbit in size. The Company intends to develop a broad portfolio of flash memory devices to cover all EPROM-like market needs, including 0.5 micron dual voltage and single voltage devices up to 16 Mbit. The Company also intends to develop specific processes based on current technology to produce 64 Mbit 0.35 micron devices for the mass storage market. The Company is using its flash memories and fast SRAMs as the focal point of its process development efforts due to their standardized design features, manufacturability and potential high volumes.

In May 1993, the Company entered into a strategic alliance with Mitsubishi to jointly develop a family of compatible 16 Mbit dual voltage flash memories for mass storage applications using 0.5 micron CMOS wafer process technology and to standardize specific manufacturing processes. In addition, in December 1994, SGS-THOMSON signed an agreement with Advanced Micro Devices Inc. ("AMD"), the supplier of approximately 24% of flash memories sold in 1994, to cooperate in the definition of standards for future EPROM-like flash memory products based on AMD's single-voltage architecture. The cooperation is intended to help create an alternative industry standard to Intel's standard for flash memory products and thereby accelerate growth in the worldwide flash memory market. SGS-THOMSON and AMD currently plan to independently develop compatible products around the standard. The Company currently produces the 4 Mbit single voltage flash memory device which is designed to the same specifications as the equivalent device from AMD, with which it is pin-compatible, although built with a proprietary 0.6 um double-metal CMOS technology.

EEPROMs and Application-Specific Memories. The Company offers 1.2 micron serial EEPROMs up to 16 Kbit and parallel EEPROMs up to 64 Kbit. Serial EEPROMs are the most popular type of EEPROMs and are generally used in computer, automotive and consumer applications. Parallel EEPROMs account for a smaller portion of the EEPROM market, being used mainly in telecommunications equipment. SGS-THOMSON entered the parallel EEPROM market in late 1993. The Company intends to work closely with its key customers and strategic allies to identify and develop new application-specific memory devices using mixed technologies.

SRAMS. The Company focuses on producing fast SRAMs and specialty low power SRAMs, but not other more standardized types of SRAMs. The Company's fast SRAMS are used as cache memories in computer systems and as main memories in telecommunications systems. The Company produces fast SRAMs up to 1 Mbit with access speeds of 9 to 20 nanoseconds. The Company's low power SRAMs are used as main memories in portable

computers and telecommunications equipment. The Company produces low power SRAMs up to 1 Mbit with access speeds of 35 to 70 nanoseconds.

Smartcard Products. Smartcards are credit-card like devices containing integrated circuits that store data and provide an array of security capabilities. They are used in a wide and growing variety of applications, including public pay telephone systems (primarily in France and Germany), cellular telephone systems (primarily in Europe), bank cards (primarily in France) and pay television systems (primarily in the United Kingdom and France). Other potential applications include medical record applications, card-access security systems and toll-access applications. In 1996, SGS-THOMSON's cumulative shipments of integrated circuits for smartcards surpassed the one billion mark.

Smartcards incorporate a variety of products manufactured by the Company, including microcontrollers, EPROMs, EEPROMs and flash memory components. A key smartcard customer of the Company is Gemplus, a French company that was formed in 1988 as a spinoff from the Company. The Company retained a 32% interest in Gemplus until 1992. The Company is now developing 32 bits cryptocontrollers as well as solutions for contactless applications. In 1996, SGS-THOMSON was the first company to obtain security certification for banking and Pay-TV applications according to the ITSEC European Norms.

Programmable Products Group

The Programmable Products Group designs, develops and manufactures microcomponents (including microcontrollers, microprocessors and digital signal processors), digital semicustom devices, mixed analog and digital semicustom devices. The Group generated revenues of $720.5 million in 1996 (an increase of 34.6% over 1995), representing approximately 17% of SGS-THOMSON's 1996 revenues. Approximately 45.2% of the Group's 1996 revenues were generated in Europe, while approximately 27.7%, 24.5% and 2.6% were generated in the Americas, the Asia Pacific region and Japan, respectively.

Microcomponents. The Company's microcomponents division manufactures and sells microcontrollers, microprocessors and digital signal processors.

Microcontrollers are complete computer systems contained on single integrated circuits that are programmed to specific customer requirements. They contain microprocessor cores as well as logic circuitry and memory capacity. Microcontrollers control the operation of electronic and electromechanical systems by processing input data from electronic sensors and generating electronic control signals, and are used in a wide variety of consumer products (alarm systems, household appliance controls and video products), automotive systems (engine control and dashboard instrumentation), computer peripheral equipment (disk drives, facsimile machines, printers and optical scanners), industrial applications (motor drives and process controllers), and telecommunications systems (telephones, answering machines and digital cellular phones).

Based on its experience with a variety of second-sourced microcontrollers, the Company has developed its complete "ST" family of proprietary microcontroller products, ranging from the 8-bit ST6, ST7, ST9 microcontrollers to the 16-bit ST10 and 32-bit ST20 devices. The ST10 and ST20 families are designed to address the full spectrum of embedded processor applications, from computer peripherals such as hard disk drives and printers to high volume consumer appliances such as digital telephone handsets and digital satellite receivers. SGS-THOMSON's microcontrollers draw on the Company's large product and technology portfolios to combine logic devices, EPROMs, EEPROMs, flash memories and various macrofunctions around a range of second-sourced and proprietary cores. The Company has also developed a line of starter kits and code generators and compilers that permit system designers to quickly and easily implement the Company's microcontrollers into their electronic systems. The Company is targeting emerging applications for microcontrollers, including televisions, monitors, cable television, satellite receivers, cellular telephones and global positioning systems.

Microprocessors are the central processing units of computer systems. The Company second-sources a variety of microprocessors developed by other semiconductor manufacturers. The Company is currently developing a 64-bit RISC microprocessor.

Digital signal processors ("DSPs") are parallel processors used for high complexity, high speed real-time computations. DSPs are used in a wide variety of applications, including answering machines, modems, digital cellular telephone systems, audio processors and data compression systems. SGS-THOMSON and its predecessors have been producing DSPs for more than ten years. The Company is producing the D950-CORE, a fixed point DSP core based upon the Company's 0.5 micron/3.3V triple-level-metal HCMOS5 technology for a wide range of applications in the computer, telecommunications and consumer markets. The Company is prototyping a 0.35 micron/2.7V five-metal layers HCMOS6 technology version of the D950-CORE. Examples of applications include mobile phones, telephone answering machines, fax machines, modems, disk drives, video conferencing systems and speech, sound, music and other multimedia functions.

Digital Semicustom Devices. Semicustom devices are ICs containing standardized lines or arrays of transistors that can be configured or interconnected to perform specific functions after a short design cycle time. SGS-THOMSON manufactures a wide range of digital semicustom devices, including high-speed low-voltage 0.35 micron CMOS five-metal layer standard cells.

SGS-THOMSON's semicustom devices are supported by libraries of cells, macro functions and design tools. SGS-THOMSON supports popular CAD tools and platforms, and has strategic alliances with Cadence Design Systems, Inc. and Synopsys, Inc. to develop semicustom CAD tools. SGS-THOMSON is developing proprietary libraries for semicustom devices for telecommunications, computer and consumer applications.

Mixed-Signal Semicustom Devices. SGS-THOMSON and its predecessor companies have also manufactured mixed-signal BiCMOS semicustom gate arrays, standard cells

and embedded arrays since 1985. Mixed-signal devices combine standard cells of digital gates and analog devices on the same semicustom IC. Such devices can be used in a wide variety of analog/digital applications, including computer peripherals, telecommunications products and industrial systems. SGS-THOMSON manufactures a wide range of mixed-signal semicustom devices, including a 0.5 micron BiCMOS library of cells.

New Ventures Group

SGS-THOMSON established the New Ventures Group in May 1994 to bring together various major product initiatives that would otherwise have been coordinated within and across individual product groups. The Group identifies and develops new business opportunities to complement the Company's existing businesses and exploit its technological know-how, manufacturing capabilities and global marketing team. The Group's first activities have been the manufacture and sale of x86 microprocessors designed by Cyrix. The Group is also evaluating other business opportunities.

x86 microprocessors are the central processing units of IBM-compatible personal computer systems (which accounted for more than 84% of worldwide personal computer sales in 1995). SGS-THOMSON U.S. has manufactured Cyrix-designed x86 chips since 1992 as a foundry for Cyrix. In 1996, SGS-THOMSON U.S. produced x86 chips for the original equipment manufacturer market. The Company is also focusing on designing and manufacturing "system on silicon" solutions based on the 486 CPU core, and more recently media processors based on Very Long Instruction Word ("VLIW") processors.

In 1996, the Company enhanced its position in the emerging market for new consumer electronics products by forming a joint development arrangement with Microsoft for DVD products, and by licensing the MPACT media processor from Chromatic Research. The Company also announced the first product on the market to employ the Macrovision 7.0 Anti-Copy System for DVD and set-top box applications. Another important product introduction for DVD applications was the Dolby AC-3 decoder. In addition, the Company helped define industry standards with the development of the Video Interface Port, which was initiated together with several competitors and will create an architecture for using video in PCs.

The Company expects to be able to use microprocessor technology, its broad range of other products and technologies and its strengths in developing and marketing application-specific products to produce powerful x86 core-based embedded applications and derivative products.

Sales, Marketing and Distribution

In 1996, the Company derived approximately 79% of its revenues from sales directly to customers through its regional sales organizations (compared to approximately 77% in 1995) and 21% of its net revenues from sales through distributors (compared to approximately 23% in 1995). SGS-THOMSON operates regional sales organizations in Europe, North

America, the Asia Pacific region and Japan. In 1996, approximately 44% of the Company's revenues originated in Europe (compared to approximately 46% in 1995), while 23% originated in the Americas (compared to approximately 24% in 1995), 27% originated in the Asia Pacific region (compared to approximately 26% in 1995) and 6% originated in Japan (compared to approximately 4% in 1995). In 1996 the Company's sales in the Asia Pacific region surpassed for the first time the $1 billion level. In 1996, two customers each accounted for slightly more than 5% of the Company's net revenues.

The European region is divided into five main sales and services districts: Central Europe (Germany and Austria), Northern Europe (United Kingdom, Ireland and Scandinavia), Western Europe (France and the Benelux countries), Southern Europe (Italy, Spain, Portugal) and Export Group. The sales organization in each district is segmented by application market (i.e., telecommunications, computer, consumer, automotive and industrial), while marketing is segmented by product groups.

In North America, the sales and marketing team is organized into six business units that are located near major centers of activity for either a particular application or geographic region: automotive (Detroit, Michigan), industrial and consumer (Chicago, Illinois), computer and peripheral equipment (San Jose, California), communications (Dallas, Texas), distribution (Boston, Massachusetts), and Latin America (Phoenix, Arizona). Each business unit has a sales force that specializes in the relevant business sector. Each business unit also provides product-related marketing and application support. This structure allows SGS-THOMSON to monitor emerging applications, to provide local design support, and to develop new products in conjunction with the various product divisions as well as to develop new markets and applications with its current product portfolio. A central marketing operation in Boston provides market communications, data processing and customer quality services to the whole region, while a logistics center in Phoenix supports the distribution network in North America.

In the Asia Pacific region, sales and marketing is organized by country and is managed from the Company regional sales headquarters in Singapore. The Company has sales offices in Taiwan, Korea, China, Hong Kong, India, Malaysia, Thailand and Australia. The Singapore sales organization provides central marketing, customer service, technical support, shipping, laboratory and design services for the entire region. In addition, there are design centers in Taiwan, Korea, Hong Kong and India.

In Japan, the large majority of the Company's sales are made through distributors, as is typical for foreign suppliers to the Japanese market. Each distributor serves specific territories or customers and is responsible for maintaining the minimum inventories required by Japanese customers. The Company provides marketing and technical support services to distributors through sales offices in Tokyo and Osaka. In addition, the Company has established a design center and application laboratory in Tokyo. The design center designs custom ICs for Japanese clients, while the application laboratory allows Japanese customers to test SGS-THOMSON products in specific applications.

The Company's central marketing efforts are organized into a central strategic marketing organization and a key account management organization. The strategic marketing organization is organized by application market. In addition, in July 1992 the Company created a series of initiatives that it refers to as Golden Programs. These programs focus the Company's multi-divisional and multi-area organizations on 13 key application markets worldwide. Each Golden Program includes a team of personnel from corporate strategic marketing, the product groups and divisions and the regional sales offices. The Golden Program teams work closely with the Company's strategic allies in each application market. The current Golden Programs include television/terminals, memory disk drives, digital cellular telephones, color television, power supply, line card, multimedia graphics, automobile radio, monitors, satellite and cable television systems, lighting, engine management and asynchronous transfer mode data communications.

In 1996, the Company undertook the Gold Standard program, a long-term commitment to excellence in standard products. The program consists in manufacturing and offering standard products at the same price level as the market but with a superior level of quality, service and lead time. The related initiatives included worldwide advertising, promotional task forces in all regions, special distribution initiatives, worldwide training of salespeople and marketing personnel.

In addition to the central strategic marketing team, the Company has established key account management teams to serve key multinational customers. The key account management teams work with the Company's regional and divisional managers to provide a broad range of products to its major accounts and to develop complete systems solutions for customers. The teams build strategic relationships with the Company's major accounts that can lead to the development of new products, increased access to evolving technologies and enhanced knowledge of customer requirements.

Each of the four regional sales organizations operate dedicated distribution organizations. To support the distribution network, SGS-THOMSON operates logistic centers in Saint Genis, France, Phoenix, Arizona and Singapore, and has made considerable investments in warehouse computerization and logistics support.

The Company also uses distributors and representatives to distribute its products around the world. Typically, distributors handle a wide variety of products, including products that compete with SGS-THOMSON products, and fill orders for many customers. Most of the Company's sales to distributors are made under agreements allowing for price protection and/or the right of return on unsold merchandise. The Company recognizes revenues when it ships products to distributors. Sales representatives generally do not offer products that compete directly with the Company's products, but may carry complementary items manufactured by others. Representatives do not maintain a product inventory; instead their customers place large quantity orders directly with SGS-THOMSON and are referred to distributors for smaller orders.

Research and Development

Management believes that research and development is critical to the Company's success and is committed to increasing research and development expenditures in the future. Despite significant cost reductions following the Company's formation in 1987, and particularly in 1990 and 1991 when the Company experienced losses, management did not reduce research and development spending. The table below sets forth information with respect to the Company's research and development spending since 1992 (not including design center, process engineering, pre-production or industrialization costs):

	Year ended December 31,				
	1992	1993	1994	1995	1996
	(in millions, except percentages)				
Expenditures	$260.9	$270.9	$338.3	440.3	532.3
as a percentage of net revenues	16.6%	13.3%	12.8%	12.4%	12.9%

As a result of the history of the Company, approximately 89% of the Company's research and development expenses in 1996 were incurred in Europe, primarily in France and Italy. See "-- State Support for the Semiconductor Industry". As of December 31, 1996, approximately 2,980 employees were employed in research and development activities.

Central research and development units conduct research on the basic VLSI technologies, packaging technologies and design tools that are used by all product groups and the front-end manufacturing organization. SGS-THOMSON'S central research and development activities are conducted in Crolles, France; Agrate, Italy; Carrollton, Texas; Phoenix, Arizona; Berkeley, California; and Noida, India. The central research and development units participate in several strategic partnerships. The Company's manufacturing facility at Crolles, France houses a research and development center that is operated pursuant to a partnership agreement between the Company and CNET, the research laboratory of France Telecom, an indirect shareholder of the Company in 1993. This center is developing submicron process technologies. The Company has also entered into an agreement with Philips Semiconductors to jointly develop sub-micron CMOS logic processes in Crolles, France through 1997. A technical center in Noida, India, develops design software and CAD libraries and tools.

The Company has signed an agreement providing for a research and development cooperation with GRESSI, the research and development Groupement d'Interet Economique ("GIE") formed by the CNET, a research laboratory wholly owned by France Telecom, and the Laboratoire d'Electronique de Technologie d'Instrumentation ("LETI"), a research laboratory of CEA, the parent company of one of the indirect shareholders of the Company. The objectives of the cooperation is to develop know-how on innovative aspects of VLSI technology evolution which can be transferred to industrial applications, and to address the development of innovative

process steps and process modules to be used in future generations of VLSI products. The cooperation agreement is based upon a pluriannual plan through 1998, and the Company is expected to bear half of the program's total cost. See Item 13: "Management's Interest in Certain Transactions". The Company has developed a wide network of cooperation with several universities in the United Kingdom (Bristol and Newcastle), Italy (Bologna, Catania, Milan, Pavia and Turin), France (Grenoble, Marseille, Toulouse and Tours), in the United States (Carnegie Mellon, Stanford, Berkeley and UCLA) and Singapore for basic research projects on design and process development.

In addition to central research and development, each operating division also independently conducts research and development activities on specific processes and products.

State Support for the Semiconductor Industry

Due to the importance of the semiconductor industry, various government authorities in the world, including the European Commission and individual countries in Europe, have established programs for the funding of research and development, innovation, industrialization and training in the industry. In addition, many countries grant various forms of tax relief, direct grants and other incentives to semiconductor companies as well as other industries to encourage investment. The Company has structured its operations to benefit from such programs and incentives and expects to continue to do so in the future. Unlike certain of its competitors, however, the Company does not receive significant direct or indirect financing from defense development programs.

The main European programs in which the Company is involved include: (i) the joint European research program called JESSI, (ii) European Union research and development projects such as ESPRIT (European Strategic Programme for Information Technology) and RACE (Research and Development in Advanced Communications Technologies for Europe), (iii) national programs for research and development and industrialization in the electronics industries, and (iv) investment incentive programs for the economic development of certain regions. The pan-European programs are generally open to eligible companies operating and investing in Europe and cover an extended period. In Italy, both electronics and economic development programs are open to eligible companies regardless of their ownership or country of incorporation.

JESSI is a European cooperative project in microelectronics among several countries that covered the period 1988 through 1996 and involved more than 80 companies. ESPRIT started in 1983 and is being extended through 1998 within the fourth framework program of the European Commission on Information and Communication Technologies (ICT). In Italy, the "Programma Nazionale per la Microelettronica" has 18 participants, and various programs for intervention in the "Mezzogiorno" (southern Italy) are open to eligible companies, including non-European companies, operating in the region and regulated by specific laws. Italian programs often cover several years, but funding is typically subject to annual budget appropriation. In France, support for microelectronics is provided to over 30 companies

manufacturing or using semiconductors. The amount of support under French programs is decided annually and subject to budget appropriation.

The Company will also participate in the Micro-Electronics Development for European Application "MEDEA" cooperative research and development program which was launched in June 1996 by the Eureka Conference and is designed to bring together many of Europe's top researchers in a 12,000 man-year program that will cover the period 1997-2000.

In addition, management expects to have the opportunity to take part in the future in European "structural funds" that are intended to furnish important support through 1999 to dedicated regions in many European countries, and provide priorities in funding for productive investment, training and job creation. These funds are available to eligible companies, including non-European companies, operating in the dedicated regions.

As a result of the history of the Company, its research and development facilities and activities are mainly concentrated in France and Italy, and the substantial majority of the Company's state funding has been derived from programs in such countries. Umbrella agreements with the Republics of France and Italy, which set forth the parameters of state support under the national programs, ran from 1992 through 1996 and required, among other things, compliance with EC regulations and annual and project-by-project reviews and approvals. The agreements were based on the maintenance of an equilibrium in the levels of research and development and related expenditures between the two countries.

Public authority funding for research and development are reported in "Other Income and Expenses" in the Company's consolidated statements of income. See Note 19 to the Consolidated Financial Statements. Such funding has totalled $80.1 million, $89.6 million and $63.8 million in the years 1994, 1995 and 1996, respectively. Public funding for industrialization costs (which include certain costs incurred to bring prototype products to the production stage) is offset against expenses in computing cost of sales, and has the effect of increasing the Company's gross profit. Such funding of industrialization costs has totalled $19.3 million, $11.8 million and $4.6 million in 1994, 1995 and 1996, respectively. See Note 19 to the Consolidated Financial Statements. Government support for capital expenditures funding has totalled $40.4 million, $64.5 million and $93.3 million in the years 1994, 1995 and 1996, respectively. Such funding has been used to support the Company's capital investment; while receipt of these funds is not directly reflected in the Company's results of operations, the resulting lower amounts recorded in property, plant and equipment reduce the level of depreciation recognized by the Company.

Low interest financing has been made available (principally in Italy) under programs such as the Italian Republic's Fund for Applied Research, established in 1968 for the purpose of supporting Italian research projects meeting specified program criteria. At year-end 1994, 1995 and 1996, the Company had $133.2 million, $115.4 million and $176.3 million, respectively, of indebtedness outstanding under state-assisted financing programs at an average interest cost of 2.9%, 2.64% and 4.0%, respectively.

Funding for programs in France and Italy is subject to compliance with EU and national regulations as well as to annual appropriation; if such governments were unable to provide anticipated funding on a timely basis or if existing government-funded programs were curtailed or discontinued or if the programs were deemed not to comply with applicable regulations, such an occurrence could have a material adverse effect on the Company's business, operating results and financial condition. From time to time the Company has experienced delays in the receipt of funding under these programs. As the availability and timing of such funding are substantially outside the Company's control, there can be no assurance that the Company will continue to benefit from such government support, that funding will not be delayed from time to time, that sufficient alternative funding would be available if necessary or that any such alternative funding would be provided on terms as favorable to the Company as those previously provided.

Various programs that provide different forms of financial support and incentives (such as research and development grants, low interest loans, capital investment support and tax incentives) for companies in the semiconductor industry are offered in a number of countries. In connection with its long term expansion plans, management believes that opportunities for such financial support and incentives may be available to it in countries outside France and Italy.

Intellectual Property

Intellectual property rights which apply to various Company products include patents, copyrights, trade secrets, trademarks and maskwork rights. SGS-THOMSON owns more than 1,600 original invention patents or pending patent applications, most of which have been registered in several countries around the world. In 1996, the Company filed 493 original patent applications around the world. Management believes that its intellectual property represents valuable property and intends to protect the Company's investment in technology by enforcing all of its intellectual property rights.

The Company has entered into several patent cross-licenses with several major semiconductor companies, consisting primarily of most of the major Japanese semiconductor companies.

Pursuant to a 1977 license agreement (the "Intel License Agreement"), SGS-THOMSON U.S. is licensed to make, have made, use and sell (in addition to other rights) products that practice all Intel patents filed prior to 1999 for the life of such patents. The Intel License Agreement was originally entered into by Mostek Corporation ("Mostek") and Intel. Thomson Semiconducteurs, one of the constituent companies of the current Company, acquired Mostek assets in 1985 and SGS-THOMSON U.S. succeeded to the interest of Mostek under the Intel License Agreement upon the Company's formation in 1987. SGS-THOMSON U.S.'s succession rights under the Intel License Agreement were upheld in a court judgment rendered in July 1992 which is now final as well as in a court judgement dated December 30, 1994 which has been confirmed in appeal.

In January 1994, SGS-THOMSON U.S. and Cyrix entered into a non-exclusive production and license agreement (the "Cyrix License Agreement") pursuant to which SGS-THOMSON U.S. agreed to produce Cyrix-designed x86 chips to sell to Cyrix for resale as Cyrix-branded products. In addition, Cyrix granted SGS-THOMSON U.S. a license to sell (as SGS-THOMSON products) a proportion of the chips that it makes available to Cyrix and to use Cyrix architecture to produce application-specific ICs. The Cyrix License Agreement extends to future generations of x86 products. Cyrix and SGS-THOMSON U.S. signed an amendment to the Cyrix License Agreement in July 1995 that allows SGS-THOMSON U.S. to manufacture and sell to third parties additional quantities of Cyrix products at least through 1997. SGS-THOMSON U.S. may continue to manufacture and sell application-specific ICs using Cyrix architecture after termination of the agreement. In April 1994, Cyrix entered into x86 production and license agreements with IBM.

The Company's success depends in part on its ability to obtain patents, licenses and other intellectual property rights covering its products and manufacturing processes. To that end, the Company has acquired certain patents and patent licenses and intends to continue to seek patents on its inventions and manufacturing processes. The process of seeking patent protection can be long and expensive, and there can be no assurance that patents will issue from currently pending or future applications or that, if patents are issued, they will be of sufficient scope or strength to provide meaningful protection or any commercial advantage to the Company. In addition, effective copyright and trade secret protection may be unavailable or limited in certain countries. Litigation, which could demand financial and management resources, may be necessary to enforce patents or other intellectual property rights of the Company.

Also, there can be no assurance that litigation will not be commenced in the future against the Company regarding patents, mask works, copyrights, trademarks or trade secrets, or that any licenses or other rights to necessary intellectual property could be obtained on acceptable terms. The failure to obtain licenses or other intellectual property rights, as well as the expense or outcome of litigation, could adversely affect the Company's results of operations or financial condition. The Company has from time to time received, and it may in the future receive, communications alleging possible infringement of certain patents and other intellectual property rights of others and it is currently the defendant in a lawsuit charging the Company with patent infringement. Regardless of the validity or the successful assertion of such claims, the Company could incur significant costs with respect to the defense thereof which could have a material adverse effect on the Company's results of operations or financial condition. See Item 3: "Legal Proceedings".

Backlog

The Company's sales are made primarily pursuant to standard purchase orders that are generally booked from one to twelve months in advance of delivery. Quantities actually purchased by customers, as well as prices, are subject to variations between booking and delivery to reflect changes in customer needs or industry conditions.

The Company's backlog has decreased during 1996 following the tough semiconductor market conditions. On January 22, 1997, the Company announced that with lead times shrinking throughout the industry during 1996, the Company entered 1997 with less order visibility than it has historically enjoyed and on June 6, 1997, the Company announced that the third quarter order backlog as of May 31, 1997 was substantially above second quarter levels and reflected a significant increase in order visibility over the first and second quarters of 1997.

SGS-THOMSON also sells certain products to key customers pursuant to frame contracts. Frame contracts are annual fixed-price contracts with customers setting forth the terms of purchase and sale of specific products. These contracts allow the Company to schedule production capacity in advance and allow customers to manage their inventory levels consistent with just-in-time principles while shortening the cycle times required to produce ordered products. Orders under frame contracts are also subject to risks of price reduction and order cancellation.

Competition

Markets for the Company's products are highly competitive. While only a few companies compete with SGS-THOMSON in all of the Company's product lines, the Company faces significant competition in each of its product lines. SGS-THOMSON competes with major international semiconductor companies, some of which have substantially greater financial and other resources than the Company with which to pursue engineering, manufacturing, marketing and distribution of their products. Smaller niche semiconductor companies are also increasing their participation in the semiconductor market. Competitors include manufacturers of standard semiconductors, application-specific ICs and fully customized ICs, including both chip and board-level products, as well as customers who develop their own integrated circuit products.
Some of the Company's competitors are also its customers.

The Company's primary competitors include Advanced Micro Devices, Inc., Hitachi, Intel Corporation, Motorola, Inc., National Semiconductor Corporation, Nippon Electric Company, Ltd., Philips Semiconductors, Samsung, Siemens, Texas Instruments Incorporated and Toshiba. The market for the Company's new x86 microprocessors is currently dominated by Intel Corporation.

The Company competes in different product lines to various degrees on the basis of price, technical performance, product features, product system compatibility, customized design, availability, quality and sales and technical support. The Company's ability to compete successfully depends on elements both within and outside of its control, including successful and timely development of new products and manufacturing processes, product performance and quality, manufacturing yields and product availability, customer service, pricing, industry trends and general economic trends.

The market for the Company's products is characterized by rapidly changing technology. Therefore, the Company's success is highly dependent upon its ability to develop

complex new products on a cost-effective basis, to introduce them in the marketplace on a timely basis, and to have them selected for design into products of leading systems manufacturers. SGS-THOMSON has committed and intends to continue to commit substantial resources to the development of new products. Because new product development commitments must be made well in advance of sales, however, new product decisions must anticipate both future demand and the technology that will be available to supply such demand. Delays in developing new products with anticipated technological advances or in commencing volume shipments of new products may have an adverse effect on the Company's business. In addition, there can be no assurance that new products, if introduced, will gain market acceptance or will not be adversely affected by new technological changes or new product announcements by others. See "-- Research and Development".

In recent years the Company has introduced, among other new products, dedicated products for several applications, including, in particular, telecommunications, computer peripheral, and automotive applications, power MOSFETS for high-frequency and high-voltage applications, Omnifets (power MOSFETS with fully integrated protection devices). The Company has also introduced a digital signal processing core for 0.5 micron ASICs (DSP 950), the ST20 family of compatible 0.5 micron 32-bit microprocessor cores and a multimedia accelerator (Riva 128) as well as the STi 3540 DVD MPEG2 decoder. The Company also continually strives to improve the operating performance and design features of many of its products.

According to preliminary industry data, SGS-THOMSON consolidated its leading world market position for EPROMs in 1996 with revenues of $335.5 million, basically unchanged over 1995 despite a sharp market decline. According to preliminary industry data, the Company was the world's leading supplier of EEPROMs in 1996. Flash memory products may replace EPROMs in many applications in the second half of the 1990s. The Company currently supplies flash memory products up to 4 Mbit, and is currently developing families of 8 and 16 Mbit flash memories. The Company is also developing a new generation of digital video decompression chips, a 64-bit RISC microprocessor and 0.35 micron BiCMOS mixed-signal standard cells. There can be no assurance, however, that the Company's flash memories or other new products, including its x86 microprocessors, will be successfully developed or produced or that they will achieve market acceptance or contribute significantly to the Company's revenues. The market for the Company's new x86 microprocessors is dominated by Intel Corporation.

The Company's future success is also dependent in part upon its ability to develop and implement new design and process technologies. Semiconductor design and process technologies are subject to rapid technological change, and require large expenditures for capital investment and research and development. The Company is developing advanced and standardized design tools for its CMOS processes as well as libraries of macrofunctions and megafunctions for many of its products, and is focusing on improving its concurrent engineering practices to better coordinate design activities and reduce overall time-to-market. If the Company experiences substantial delays in developing new design or process technologies or

inefficiently implements production increases or transitions, the Company's results of operations could be adversely affected.

Employees

As of December 31, 1996, the Company employed approximately 25,893 people, of whom approximately 5,358 were employed in France, 5,514 were employed in Italy, 588 were employed in the rest of Europe, 2,555 were employed in the United States, 4,308 were employed in Malta and Morocco and 7,570 were employed in Singapore, Malaysia and Japan. As of December 31, 1996, approximately 2,980 employees were engaged in research and development, 1,296 in marketing and sales, 17,672 in manufacturing, 1,629 in administration and general services and 2,343 in divisional functions.

The Company's future success will depend, in part, on its ability to continue to attract, retain and motivate highly qualified technical, marketing, engineering and management personnel. Unions are present in France, Italy, Malta, Morocco and Singapore. The Company has not experienced any significant strikes or work stoppages in recent years, other than in connection with national strikes in Italy, and management believes that the Company's employee relations are good.

Environmental Matters

The Company's manufacturing operations use many chemicals and gases and the Company is subject to a variety of governmental regulations related to the use, storage, discharge and disposal of such chemicals and gases and other emissions and wastes. Consistent with the Company's TQM principles, the Company has established proactive environmental policies with respect to the handling of such chemicals and gases and emissions and waste disposals from its manufacturing operations. The Company has engaged outside consultants to audit its environmental activities and has created environmental management teams, information systems, education and training programs, and environmental assessment procedures for new processes and suppliers. By the end of 1996, ten of the Company's plants were certified for the Eco-Management and Audit Scheme ("EMAS") and five sites have also obtained ISO 14001 certification.

Although the Company has not suffered material environmental claims in the past and believes that its activities conform to presently applicable environmental regulations, in all material respects, environmental claims or the failure to comply with present or future regulations could result in the assessment of damages or imposition of fines against the Company, suspension of production or a cessation of operations.

Item 2: Description of Property

SGS-THOMSON currently operates 17 main manufacturing facilities around the world. The table below sets forth certain information with respect to SGS-THOMSON's current manufacturing facilities, products and technologies. Front-end manufacturing facilities are wafer fabrication plants and back-end facilities are assembly, packaging and final testing plants.

Location	Products	Technologies
Front-end Facilities:		
Crolles, France	Semicustom devices and dedicated products	8-inch 0.7/0.35 micron CMOS and 1.0/0.35 micron BiCMOS; R&D on submicron technologies in conjunction with CNET and Philips Semiconductors
Phoenix, Arizona	x86 microprocessors, EPROMs and other VLSI products	8-inch 0.5/0.35 micron CMOS
Agrate, Italy	EPROMSs, EEPROMs, semicustom devices, microcontrollers, flash memories and dedicated products	Fab 1 - 6-inch 0.8/0.6 micron CMOS Fab 2 - 6-inch 2.0/1.2 micron BiCMOS and BCD Fab 3 - 6-inch 0.65/0.35 micron CMOS pilot line being converted to 8-inch
Rousset, France	Microcontrollers, EEPROMs and smartcard products	6-inch 0.8 micron CMOS
Catania, Italy	Power transistors, smart devices and audio and automotive dedicated products	Fab 1 - 5-inch 3 micron bipolar power Fab 2 - 5-inch 3/4 micron power MOS/BCD (being converted to 6-inch) Fab 3 - 6-inch 4/6/1 micron pilot line
Rennes, France	Dedicated and power products	5-inch 2 micron BiCMOS, BCD and bipolar
Grenoble, France(1)	Dedicated products, semicustom devices, smartcard products	4-inch 2.0/1.2 micron BiCMOS
Castelletto, Italy	Smart power BCD	6-inch 4.0/1.2 micron bipolar and mixed BCD pilot line (converted from 5-inch in 1996)
Tours, France	Thyristors, diodes and application-specific discretes	Fab 1 - 5-inch discrete (converted from 4-inch in 1996) Fab 2 - 5-inch discrete (converted from 4-inch in 1996)
Ang Mo Kio, Singapore	Dedicated products, microcontrollers and commodity products	Fab 1 - 5-inch 2 micron CMOS Fab 2 - 5-inch 6 micron bipolar standard Fab 3 - 5-inch 3 micron bipolar complex
Carrollton, Texas	Memories, microprocessors and semicustom devices	Fab 1 - 4-inch 1.2 micron CMOS and BiCMOS (being converted to 6-inch) Fab 2 - 6-inch 0.6 micron CMOS
Rancho Bernardo, California(2)	CMOS/BiCMOS telecommunications ICs	4-inch 3 micron CMOS/BiCMOS (new 6-inch module in progress)
Back-end Facilities:		
Muar, Malaysia	Broad range	
Kirkop, Malta	Broad range	
Toa Payoh, Singapore	Broad range	
Ain Sebaa, Morocco	Discrete semiconductors	
Bouskoura, Morocco	Subsystems	
Shenzen, China	Discrete semiconductors	

(1) The closure of the Grenoble front-end facility is now scheduled to take place during 1997.
(2) This facility was acquired by the Company from Northern Telecom on January 1, 1994 in connection with entering into a strategic alliance with Northern Telecom.

In 1996, approximately 61% of the value of SGS-THOMSON manufactured devices were produced in Europe, 21% in the Asia Pacific region, and 18% in the United States. The major hubs for European manufacturing and product design and development are located in Agrate, Italy and Crolles, France. In the United States, the Company's main manufacturing facility are located in Carrollton, Texas and Phoenix, Arizona. In the Asia Pacific region, the Company operates a front-end wafer fab in Singapore and back-end facilities in Singapore and Muar, Malaysia.

In 1996, SGS-THOMSON has expanded its diversified manufacturing infrastructure while improving the cost, quality and flexibility of its operations. SGS-THOMSON has applied 1996 investments in its manufacturing facilities to bring to full capacity the 8-inch front-end manufacturing facility in Crolles, France, to continue the ramp up of the new 8-inch front-end manufacturing facility in Phoenix, Arizona, to complete the building of and to begin equipping the third 8-inch front-end manufacturing facility in Catania, Italy, and to complete a new back-end facility and design center in Shenzhen, China, through its joint venture created in 1996 with a subsidiary of the Shenzhen Electronics Group. During 1996, the Company has also completed conversion from 4-inch to 5-inch of the two front-end wafer fabrication plants in Tours, France, from 5-inch to 6-inch of the front-end wafer fabrication facility in Rousset, France, and has installed a new 6-inch module in the Rancho Bernardo, California front-end wafer fabrication facility. In addition, the Company has started construction of a new 8-inch front-end wafer fabrication facility in Rousset, France, has initiated the 6-inch to 8-inch conversion of one of its Agrate, Italy front-end wafer fabrication plants, and has started planning the construction of a new 8-inch front-end wafer fabrication facility in Singapore, announced during 1996. Finally, the Company has also identified one more 8-inch front-end wafer fabrication plant to be built in Italy. In 1996, approximately 93% of the ICs wafers manufactured by SGS-THOMSON were manufactured on 5-inch or larger wafers.

In 1994, the Company created a joint venture with a subsidiary of the Shenzhen Electronics Group ("SEG") that built and equipped a back-end manufacturing facility and design center in the Futian free-trade zone of Shenzhen in southern China. SGS-THOMSON owns a 60% interest in the joint venture, with a subsidiary of SEG owing the remaining 40%. Construction of the plant and equipment installation has been completed in 1996 as scheduled and production started at the end of 1996. The Company and SEG plan to invest initially approximately $77 million in the joint venture. SEG is a diversified export-oriented electronics company controlled by the Shenzhen Municipal Government that manufactures communications equipment, computers and electronic products and components and engages in import-export trading, financial investment management and real estate.

Although each fabrication plant is dedicated to specific processes, the Company's strategy is to have multiple plants for key process families. The Company subcontracts some back-end assembly and testing operations.

Manufacturing Risks

The Company's manufacturing processes are highly complex, require advanced and costly equipment and are continuously being modified in an effort to improve yields and product performance. Impurities or other difficulties in the manufacturing process can lower yields. Although the Company's increased manufacturing efficiency has been an important factor in its improved results of operations, as is common in the semiconductor industry, the Company has from time to time experienced production difficulties that have caused delivery delays and quality control problems. No assurance can be given that the Company will be able to increase manufacturing efficiency in the future to the same extent as in the past or that the Company will not experience production difficulties in the future.

The Company undertook in 1996 certain initiatives to expand its manufacturing resources in order to help relieve capacity constraints with regard to certain advanced products. In particular the manufacturing plan in Phoenix, Arizona, was qualified to produce a broader and more flexible range of products. SGS-THOMSON has applied 1994, 1995 and 1996 investments to build and equip two 8-inch front-end manufacturing facilities in Crolles, France and Phoenix, Arizona currently in operation, and has applied 1995 and 1996 investments to build and equip an additional 8-inch front-end manufacturing facility in Catania, Italy, now qualified, and to build a new back-end facility and design center in Shenzhen, China through its joint venture created in 1994 with a subsidiary of the Shenzhen Electronics Group. The Company also converted 4-inch and 5-inch wafer fabs to 5-inch and 6-inch production and is starting the conversion and expansion from 6-inch to 8-inch production of a front-end fabrication facility in Agrate, Italy. In addition, the Company has identified two other 8-inch front-end wafer fabrication facilities, one of which will be in Singapore, with the other one in Italy now under consideration. In 1995, the Company approved the building and equipping of a new 8-inch 0.5 micron front-end wafer fabrication plant (which will also be capable of 0.35 and 0.25 micron production) in Rousset, France which is now under construction. As is common in the semiconductor industry, the Company has from time to time experienced difficulty in ramping up production at new facilities or effecting transitions to new manufacturing processes and, consequently, has suffered delays in product deliveries or reduced yields. There can be no assurance that the Company will not experience manufacturing problems in achieving acceptable yields and/or product delivery delays in the future as a result of, among other things, capacity constraints, construction delays, ramping up production at new facilities, upgrading or expanding existing facilities or changing its process technologies, any of which could result in a loss of future revenues. The Company's operating results could also be adversely affected by the increase in fixed costs and operating expenses related to increases in production capacity if revenues do not increase commensurately.

SGS-THOMSON's principal executive office is located in Saint Genis, France, near Geneva, Switzerland. The Company also operates nine research and development centers and 26 design centers. The Company maintains regional sales headquarters in Saint Genis, France, Boston, Massachusetts, Singapore and Tokyo, Japan, and has 44 sales offices in 22

countries throughout Europe, North America and the Asia Pacific region. In general, the Company owns its manufacturing facilities and leases most of its sales offices.

Item 3: Legal Proceedings

As is the case with many companies in the semiconductor industry, the Company has from time to time received communications alleging possible infringement of certain intellectual property rights of others. Irrespective of the validity or the successful assertion of such claims, the Company could incur significant costs with respect to the defense thereof which could have a material adverse effect on the Company's results of operations or financial condition.

The Company is currently involved in certain legal proceedings; however, the Company does not believe that the ultimate resolution of pending legal proceedings will have a material adverse effect on its financial condition.

In May 1995, an investigation was ordered by the prosecutor of the court of Catania, Italy of the research and development consortium CORIMME. SGS-THOMSON Microelectronics s.r.l. holds a 662/3% voting interest in the consortium with the University of Catania holding the remaining 331/3% voting interest. A notice (Informazione di Garanzia) of the commencement of a criminal investigation was served on the President of CORIMME and to the Board of Directors and Statutory Auditors of CORIMME. Under Italian law, criminal liability cannot be attributed to a company and therefore notices relating to investigation of acts or events generally attributable to a company are sent to the legal representative of such company (i.e. the president or the statutory bodies). Investigations are still on going with regard to the dispute concerning value-added-tax ("VAT") between CORIMME and the Italian tax authority, and with regard to alleged misuse of public funds by SGS-THOMSON Microelectronics s.r.l. In order to become eligible for government research and development funding, the CORIMME consortium was required to submit detailed plans specifying the objectives of a program and the manner in which the funding would be used. The Company's management believes that the inquiry to date has focused on whether part of the funds and other resources designated for research were used for production or otherwise in violation of applicable requirements and on the proper use of, and allocation of expenses (such as rent and utilities) for, resources and the allocation of revenues between CORIMME and the Company. In another matter concerning a dispute on VAT deductions, CORIMME was granted a favorable ruling by the Commissione Tributaria di Primo Grado in Catania which has been confirmed by The Commissione Tributaria di Secundo Grado in Catania. The Company's management believes that CORIMME's contractual and other requirements have been honored in all material respects. The Company's management further believes that the management of CORIMME programs has been in all material respects in accordance with those plans and with applicable financial procedures provided by the Italian government. It is cooperating in full with the authorities in the conduct of the inquiry. Due to the preliminary nature of the inquiry it is impossible to determine the ultimate scope or outcome of the inquiry. Although the investigation

is at a preliminary stage, management believes based on information available to the Company to date and based on the advice of legal counsel that the outcome of the investigation will not have a material effect on the financial condition or results of operations of the Company.

Item 4: Control of Registrant

Principal Shareholders

In October, 1995, the Company completed a second public offering of the Common Shares. In the Offering, the Company sold 8,960,000 shares and the selling shareholders sold 11,740,000 shares at a price to public of $43.5 a share. The following table sets forth certain information with respect to the ownership of the Company's Common Shares, as of May 30, 1997.

	Common Shares Owned	
Shareholders	Number of Common Shares	%
SGS-THOMSON Microelectronics Holding II B.V.....	95,863,880	68.9

The officers and directors of the Company as a group own an insignificant number of Common Shares.

The chart below illustrates the current shareholding structure:

Description of Shareholding Structure:

SGS-THOMSON Microelectronics N.V. is owned 68.9% by SGS-THOMSON Microelectronics Holding II B.V. a wholly-owned subsidiary of SGS-THOMSON Microelectronics Holding N.V. SGS-THOMSON Microelectronics Holding N.V. is 50% owned by a consortium of French shareholders and 50% owned by a consortium of Italian shareholders. The French shareholder, FT2CI, is owned 49.9% and 50.1% by Thomson-CSF and FT1CI, respectively. Thomson-CSF is owned 58.0% by Thomson S.A. FT1CI is owned 51.0% and 49.0% by CEA-Industrie and France Telecom, respectively. The Italian shareholder, MEI, is owned 50.1% and 49.9% by I.R.I. and Comitato SIR, respectively.

SGS-THOMSON Microelectronics Holding II B.V. ("SGS-THOMSON Holding II") is a wholly owned subsidiary of SGS-THOMSON Microelectronics Holding N.V. ("SGS-THOMSON Holding"). SGS-THOMSON Holding is 50% owned by a consortium of French shareholders that are indirectly controlled by the French government and 50% owned by a consortium of Italian shareholders that are indirectly controlled by the Italian government. The consortium of French shareholders is comprised of Thomson-CSF, a subsidiary of the French state-controlled electronics company Thomson S.A., France Telecom, the French state-controlled telephone company, CEA-Industrie, a corporation controlled by the French atomic energy commission, and FT1CI and FT2CI, two French holding companies. The consortium of Italian shareholders is comprised of Istituto per la Ricostruzione Industriale S.p.A. ("I.R.I."), the holding company for Italian state-owned industrial and commercial interests, Comitato per l'Intervento nella SIR ed in settori ad Alta Technologia ("Comitato SIR") and MEI-Microelettronica Italiana s.r.l. ("MEI"), an Italian holding company. In December 1994, Finmeccanica, a subsidiary of I.R.I., transferred its interest in SGS-THOMSON Holding to MEI. Shares of Thomson-CSF are listed on the Bourse de Paris and Frankfurt Stock Exchange and American Depositary Receipts for its shares are quoted on Nasdaq. Certificats d'investissement of CEA-Industrie are listed on the Bourse de Paris.

SGS-THOMSON Holding II is a holding company whose only asset is the common stock of the Company. It has no Supervisory Board, and its Management Board is SGS-THOMSON Holding.

Shareholder Agreements

In connection with the formation of the Company, Thomson-CSF and STET, as shareholders of the Company, entered into a shareholders agreement on April 30, 1987. In connection with the formation of SGS-THOMSON Holding in 1989, which coincided with the acquisition by Thorn EMI of its interest in the Company, the shareholders agreement (as amended, the "Holding Shareholders Agreement") was amended to apply to the parties' ownership in SGS-THOMSON Holding. The rights and obligations of Thomson-CSF and STET under the Holding Shareholders Agreement were subsequently transferred to or assumed by, as the case may be, FT2CI for Thomson-CSF, and Finmeccanica and MEI for STET. In connection with the transfer by Finmeccanica of its interest in SGS-THOMSON Holding to MEI, the rights and obligations of Finmeccanica under the Holding Shareholders Agreement were subsequently transferred to or assumed by, as the case may be, MEI.

Pursuant to the terms of the Holding Shareholders Agreement and for the duration of such agreement, FT2CI (the "French Owner"), on the one hand, and MEI (the "Italian Owner"), on the other hand, have agreed to maintain equal interests in the share capital of SGS-THOMSON Holding and maintain, together, ownership of the majority of SGS-THOMSON Holding's issued voting shares. The admission of a third party to the share capital of SGS-THOMSON Holding, whether through the sale of SGS-THOMSON Holding's outstanding shares or through the issue by SGS-THOMSON Holding of new shares, or by any other means, must

be unanimously agreed upon. In the event of a new shareholder, the parties undertake to ensure that the balance between the French and Italian shareholdings shall be maintained.

The Holding Shareholders Agreement contemplates that the parties shall agree upon common proposals and jointly exercise their powers of decision and their full control of the strategies and actions of SGS-THOMSON Holding and the Company. Under the Holding Shareholders Agreement, the Supervisory Board of SGS-THOMSON Holding, which is composed of three representatives of the French Owner and three representatives of the Italian Owner, must give its prior approval before SGS-THOMSON Holding, the Company, or any subsidiary of the Company may: (i) modify its articles of incorporation; (ii) change its authorized share capital, issue, acquire or dispose of its own shares, change any shareholder rights or issue any instruments granting an interest in its capital or profits; (iii) be liquidated or dispose of all or a substantial and material part of its assets or any shares it holds in any of its subsidiaries; (iv) enter into any merger, acquisition or joint venture agreement (and, if substantial and material, any agreement relating to intellectual property) or form a new company; (v) approve such company's draft consolidated balance sheets and financial statements or any profit distribution by such company; or (vi) enter into any agreement with any of the direct or indirect French or Italian Owners outside the normal course of business. The Holding Shareholders Agreement also provides that long-term business plans and annual budgets of the Company and its subsidiaries, as well as any significant modifications thereto, shall be approved in advance by the Supervisory Board of SGS-THOMSON Holding. In addition, the Supervisory Board of SGS-THOMSON Holding shall also decide upon operations of exceptional importance contained in the annual budget even after financing thereof shall have been approved.

Such agreement also provides that similar and adequate levels of research, development and technological innovation shall be achieved by the Company and its subsidiaries in France and Italy and that there shall be no substantial discrepancy in the percentage of state financing compared to research, development and technological innovation expenditures by the Company and its subsidiaries in each such country. See "Item 1: Description of Business State Support for the Semiconductor Industry." Pursuant to the terms of the Holding Shareholders Agreement, SGS-THOMSON Holding is not permitted, as a matter of principle, to operate outside the field of semiconductor products. The parties to the Holding Shareholders Agreement also undertake to refrain directly or indirectly from competing with the Company in the area of semiconductor products, subject to certain exceptions, and to offer the Company opportunities to commercialize or invest in any semiconductor product developments by them. Any financing or capital provided by the parties to SGS-THOMSON Holding or the Company is intended to be provided pro rata based on the parties' respective shareholdings in SGS-THOMSON Holding. In the Holding Shareholders Agreement, the parties state that it is of the utmost importance that the French and Italian governments grant sufficient and continuous financial support for research and development, and undertake to take suitable actions with a view to obtaining such funding.

In the event of a disagreement that cannot be resolved between the parties as to the conduct of the business and actions contemplated by the Holding Shareholders Agreement,

each party has the right to offer its interest in SGS-THOMSON Holding to the other, which then has the right to acquire, or to have a third party acquire, such interest. If neither party agrees to acquire or have acquired the other party's interest, then together the parties are obligated to try to find a third party to acquire their collective interests, or such part thereof as is suitable to change the decision to terminate the agreement. The Holding Shareholders Agreement otherwise terminates in the event that one of the parties thereto ceases to hold shares in SGS-THOMSON Holding.

The Company has been informed that the shareholders of FT2CI as well as the shareholders of FT1CI (the majority shareholder of FT2CI) have also entered into separate shareholder agreements that require the consent of the Board of Directors of each such company to certain actions taken by SGS-THOMSON Holding, the Company and its subsidiaries. These agreements provide for the management of the interests of CEA-Industrie, France Telecom and Thomson-CSF in SGS-THOMSON Holding and the Company, with the object of defining among them the positions, strategies and decisions to be taken by the French Owner in SGS-THOMSON Holding affecting the management of SGS-THOMSON Holding, and the Company and its subsidiaries. The Company is not a party to either of these agreements.

In particular, the agreement between the shareholders of FT2CI (FT1CI and Thomson-CSF) provides that, subject to the fulfillment of their duties as Supervisory Board members in accordance with Dutch law, representatives of FT2CI on the Supervisory Board of SGS-THOMSON Holding and the Company can only take positions on specified matters at meetings of such Supervisory Boards if such positions are approved in advance by a majority (or in certain circumstances three-quarters) of the Board of Directors of FT2CI (which consists of nine members, six of whom are chosen by FT1CI and three of whom are chosen by Thomson-CSF). Such matters requiring majority approval include: (i) adoption and changes to long-term business plans of SGS-THOMSON Holding and the Company, (ii) approval of annual budgets prior to their adoption by the Supervisory Board of the Company, (iii) approval of the annual financial statements of SGS-THOMSON Holding and the Company, (iv) modification of the articles of association or capital increases of any of the Company's subsidiaries, (v) dissolution or sale of all or a substantial part of the assets of any of the Company's subsidiaries, (vi) any equity investment by SGS-THOMSON Holding, the Company or any of its subsidiaries in another company or group, (vii) any agreement between SGS-THOMSON Holding and/or the Company and any shareholder of FT1CI or FT2CI outside the ordinary course of business, (viii) any technology transfer agreement allowing the Company to create new families of technology or allowing competitors access to major technologies of the Company, and (ix) any major modification to the geographic distribution of industrial sites of the Company in Europe or the United States. Such matters requiring three-quarters' approval include: (i) any modification of the amount or breakdown of the capital of SGS-THOMSON Holding or the Company not constituting a strategic alliance or any issuance or repurchase by SGS-THOMSON Holding or the Company of their shares or any modification of the rights attached thereto, (ii) any issue by SGS-THOMSON Holding or the Company of shares giving rights to a minimum number of shares of capital stock, with the effect of or leading to a change in the ownership of share capital of SGS-THOMSON Holding or the Company, (iii) any distribution of profits of SGS-

THOMSON Holding and/or the Company, (iv) any liquidation or dissolution of SGS-THOMSON Holding or the Company, or any sale of all or a substantial part of the assets of either company, (v) any modification of the articles of association of SGS-THOMSON Holding or the Company, and (vi) any sale of assets or business likely to have a significant negative impact on the shareholders' equity of the Company. In addition, any modification of the Holding Shareholders Agreement requires the approval of three-quarters of the members of FT2CI's Board of Directors. The FT2CI shareholders agreement provides that the three representatives of the French Owner on the Supervisory Boards of SGS-THOMSON Holding and the Company shall be members of the FT2CI Board of Directors and will consist of two members chosen by FT1CI and one member chosen by Thomson-CSF. The FT2CI shareholders agreement also requires the consent of Thomson-CSF for the transfer of any shares in FT1CI. Under certain circumstances, FT1CI is required to acquire Thomson-CSF's interest in FT2CI, including if (i) CEA-Industrie and France Telecom no longer hold a majority of FT1CI's capital, (ii) FT1CI no longer holds a majority of FT2CI's capital, (iii) FT2CI and the Italian shareholders together no longer hold a majority of SGS-THOMSON Holding's capital, (iv) SGS-THOMSON Holding no longer holds a majority of the Company's share capital or (v) FT2CI obtains more than a 50% interest in SGS-THOMSON Holding. Under the FT2CI shareholders agreement, Thomson-CSF has agreed not to compete with the Company in the area of non-military semiconductor products until February 15, 1998. The FT2CI shareholders agreement terminates in 30 years or in the event one of the parties ceases to hold shares in FT2CI.

The agreement between the shareholders of FT1CI (CEA-Industrie and France Telecom) provides that the following acts of FT2CI with respect to SGS-THOMSON Holding or the Company must be approved by three-quarters of the Board of Directors of FT1CI (which consists of five directors, three of whom are chosen by CEA-Industrie and two of whom are chosen by France Telecom): (i) any modification of the articles of association of SGS-THOMSON Holding or the Company, (ii) any change in the capital of SGS-THOMSON Holding or the Company, or issuance, purchase or sale by SGS-THOMSON Holding or the Company of their shares or rights attached thereto, or the issuance of any securities giving rights to a share in the capital or profits of SGS-THOMSON Holding or the Company, (iii) the liquidation or dissolution of SGS-THOMSON Holding or the Company or the sale of all or an important and material part of the business or assets of SGS-THOMSON Holding or the Company representing at least $10,000,000 of the consolidated shareholders' equity of the Company, (iv) any merger, acquisition, partnership in interest or the execution of any material agreement relating to intellectual property rights, in each case in which SGS-THOMSON Holding or the Company participates or in which a proposal is made to participate, or the establishment by SGS-THOMSON Holding or the Company of new companies or groups, (v) approval of the balance sheets and consolidated accounts of SGS-THOMSON Holding, the Company and its subsidiaries as well as the policies of distributions of profits among the group, (vi) any agreement between SGS-THOMSON Holding and/or the Company and the shareholders of FT1CI which is out of the ordinary course of business, (vii) the approval of, or material modifications to, shareholders agreements with the Italian Owner with respect to SGS-THOMSON Holding or the Company and (viii) approval of strategic multi-year plans and annual consolidated budgets of SGS-THOMSON Holding and the Company. Transfers of shares in FT1CI to third parties are subject

to the approval of at least four members of the Board of Directors, and are subject to a right of first refusal of the other shareholders, as well as other provisions. In the event CEA-Industrie proposes to sell its interest in FT1CI, in whole or in part, France Telecom has the right to require the acquiror to purchase its interest as well. The FT1CI shareholders agreement terminates upon the termination of FT1CI.

As is the case with other companies controlled by the French Government, the French Government has appointed for each of FT1CI and FT2CI a Commissaire du Gouvernement and a Controleur d'Etat. Pursuant to decree No. 94-214, dated March 10, 1994, these Government representatives have the right (i) to attend any board meeting of FT1CI and FT2CI, and (ii) to veto any board resolution or any decision of the president of FT1CI and FT2CI within 10 days of such board meeting (or, if they have not attended the meeting, within 10 days of the receipt of the board minutes or the notification of such president's decision); such veto lapses if not confirmed within one month by the Ministry of the Economy or the Ministry of Industry. FT1CI and FT2CI are subject to certain points of the arrete of August 9, 1953 pursuant to which the Ministry of the Economy and any other relevant ministries (a) have the authority to approve decisions of FT1CI and FT2CI relating to budgets or forecasts of revenues, operating expenses and capital expenditures, and (b) may set accounting principles and rules of evaluation of fixed assets and amortization.

In connection with the Initial Public Offering, SGS-THOMSON Holding II and the Company entered into a registration rights agreement pursuant to which the Company agreed that, upon request from SGS-THOMSON Holding II, the Company will file a registration statement under the Securities Act of 1933, as amended, to register Common Shares held by SGS-THOMSON Holding II, subject to a maximum number of five requests in total as well as a maximum of one request in any twelve-month period. Subject to certain conditions, the Company will grant SGS-THOMSON Holding II the right to include its Common Shares in any registration statements covering offerings of Common Shares by the Company. SGS-THOMSON Holding II will pay a portion of the costs of any requested or incidental registered offering based upon its proportion of the total number of Common Shares being registered, except that SGS-THOMSON Holding II will pay any underwriting commissions relating to Common Shares that it sells in such offerings and any fees and expenses of its separate advisors, if any. Such registration rights agreement will terminate upon the earlier of December 15, 2004 and such time as SGS-THOMSON Holding II and its affiliates own less than 10% of the Company's outstanding Common Shares.

The Company has been informed by SGS-THOMSON Holding II that, although there may be additional offering by SGS-THOMSON Holding II of its shares in the Company, SGS-THOMSON Holding II does not currently have any plans to reduce its ownership interest to less than a controlling interest in the Company for the foreseeable future. The timing and size of any future primary and secondary offerings will depend upon a variety of factors, including in particular market conditions.

The French and Italian shareholders of SGS-THOMSON Holding have agreed that they will continue to manage their interest in the Company through SGS-THOMSON Holding at least until the end of 1996 or early 1997, and accordingly, for so long as they hold their interest in SGS-THOMSON Holding, they have undertaken (i) to jointly hold 100% of SGS-THOMSON Holding's capital and voting rights, (ii) to maintain equality between the interests of the French and Italian shareholders, (iii) to ensure that SGS-THOMSON Holding maintains more than 51% of the Company's share capital and voting rights, and (iv) to jointly exercise their decision-making powers and monitor strategies and actions as part of SGS-THOMSON Holding's management bodies.

Item 5: Nature of Trading Market

General

The Company's Common Shares are listed on the New York Stock Exchange, which is the principal trading market for the Common Shares, under the symbol "STM" and on the Bourse de Paris. Common Shares are also quoted on SEAQ International.

Trading Markets

The table below sets forth, for the period indicated, the reported high and low sales prices in U.S. dollars for the Common Shares on the New York Stock Exchange and the high and low sales prices in French francs for the Common Shares on the Bourse de Paris.

	New York Stock Exchange Price per Common Share		Bourse de Paris Price per Common Share	
Calendar Period	High	Low	High	Low
1995				
First quarter	$32 1/2	$22 1/2	FRF160.0	FRF119.0
Second quarter	$41 7/8	$29 3/4	FRF205.5	FRF142.0
Third quarter	$57 1/2	$40 3/8	FRF288.0	FRF197.0
Fourth quarter	$49	$40 3/8	FRF244.0	FRF201.0
1996				
First quarter	$41 1/3	$29 1/2	FRF211.9	FRF141.0
Second quarter	$47 1/2	$34 2/3	FRF246.5	FRF175.5
Third quarter	$49 4/5	$29 3/4	FRF258.0	FRF150.0
Fourth quarter	$70 5/8	$44 1/3	FRF397.0	FRF228.0

At December 31, 1996, there were 138,985,580 Common Shares issued and outstanding, of which 23,608,380 or 16.99% were registered in the Common Share registry maintained on the Company's behalf in New York.

Item 6: Exchange Controls and Other Limitations Affecting Security Holders

None.

Item 7: Taxation

The following is a summary of certain tax consequences of the acquisition, ownership and disposition of the Company's Common Shares based on tax laws of The Netherlands and the United States as in effect on the date of this annual report on Form 20-F, and is subject to changes in Netherlands or U.S. law, including changes that could have retroactive effect. The following summary does not take into account or discuss the tax laws of any country other than The Netherlands or the United States, nor does it take into account the individual circumstances of an investor. Prospective investors in the Company's Common Shares in all jurisdictions are advised to consult their own tax advisers as to Netherlands, U.S. or other tax consequences of the purchase, ownership and disposition of the Company's Common Shares.

Netherlands Taxation

The following summary of Netherlands tax considerations is based on present Netherlands tax laws as interpreted under officially published case law. The description is limited to the tax implications for an owner of Common Shares who is not, or is not deemed to be, a resident of The Netherlands for purposes of the relevant tax codes (a "non-resident Shareholder" or "Shareholder") and who owns less than 10% of the Company's Common Shares.

Dividend Withholding Tax

General. Dividends distributed by the Company are subject to a withholding tax imposed by The Netherlands at a rate of, generally, 25%. Dividends include dividends in cash or in kind, constructive dividends, repayment of paid-in capital not recognized for Netherlands tax purposes and liquidation proceeds in excess of, for Netherlands tax purposes, recognized paid-in capital. Stock dividends are also subject to withholding tax on the nominal value unless sourced out of the Company's paid-in share premium recognized for Netherlands tax purposes.

No withholding tax applies on the sale or disposition of Common Shares to persons other than the Company and affiliates of the Company.

A Shareholder can be eligible for a reduction or a refund of Netherlands dividend withholding tax under a tax convention which is in effect between the country of residence of the Shareholder and The Netherlands. The Netherlands has concluded such a convention with, among others, the United States, Canada, Switzerland, Japan and all EC Member States except

Portugal. Under all of those conventions, Netherlands dividend withholding tax is reduced to 15% or a lower rate.

U.S. Shareholders. Under the Tax Convention of December 18, 1992, concluded between the United States and The Netherlands (the "Convention"), the withholding tax on dividends paid by the Company to a resident of the United States (as defined in the Convention) who is entitled to the benefits of the Convention under Article 26 may be reduced to 15% pursuant to Article 10 of the Convention. Dividends paid by the Company to U.S. pension funds and U.S. exempt organizations may be eligible for an exemption from dividend withholding tax.

Relief/refund Procedure. If the 15% rate, or an exemption in case of a qualifying U.S. pension fund, is applicable pursuant to the Convention, the Company is allowed to pay out a dividend under deduction of 15%, or respectively without any deduction, if, at the payment date, the relevant shareholders have submitted the duly signed form IB 92 USA, which form includes a banker's affidavit. Holders of Shares through DTC will initially receive dividends subject to a withholding rate of 25%. An additional 10% of the dividend will be paid to holders upon receipt by the dividend disbursing agent of notification from the Participants in DTC that such holders are eligible for the reduced rate under the Convention. Only where the applicant has not been able to claim full or partial relief at source, will he be entitled to a refund of the excess tax withheld. In that case he should mention in the Form IB 92 USA the circumstances that prevented him from claiming relief at source.

Qualifying U.S. exempt organizations can only ask for a full refund of the tax withheld by using the Form IB 95 USA, which form also includes a banker's affidavit.

Income Tax and Corporate Income Tax

A non-resident individual or corporate Shareholder will not be subject to Netherlands income tax with respect to dividends distributed by the Company on the Common Shares or with respect to capital gains derived from the sale or disposition of Common Shares in the Company, provided that:

(a) the non-resident Shareholder does not own a business which is, in whole or in part, carried on through a permanent establishment or a permanent representative in The Netherlands to which or to whom the Common Shares are attributable;

(b) the non-resident Shareholder does not have a direct or indirect substantial or deemed substantial interest in the share capital of the Company as defined in The Netherlands tax code or, in the event the Shareholder does have such a substantial interest, such interest is a business asset; and

(c) the non-resident Shareholder is not entitled to a share in the profits of an enterprise effectively managed in The Netherlands other than by way of securities or through an employment contract, the Common Shares being attributable to that enterprise.

In general terms, a substantial interest in the share capital of the Company does not exist if the Shareholder alone or together with certain relatives does not own, and has not owned in the preceding five years, one-third or more of the nominal paid-in capital of any class of shares in the Company.

Net Wealth Tax

A non-resident individual Shareholder is not subject to Netherlands net wealth tax with respect to the Shares, provided that:

(a) the non-resident Shareholder does not own a business which is, in whole or in part, carried on through a permanent establishment or a permanent representative in The Netherlands to which or to whom the Common Shares are attributable; and

(b) the non-resident Shareholder is not entitled to a share in the profits of an enterprise effectively managed in The Netherlands other than by way of securities or through an employment contract, the Common Shares being attributable to that enterprise.

Corporations are not subject to Netherlands net wealth tax.

Gift and Inheritance Tax

A gift or inheritance of Common Shares from a non-resident Shareholder will not be subject to a Netherlands gift and inheritance tax, provided that:

(a) the non-resident Shareholder does not own a business which is, in whole or in part, carried on through a permanent establishment or a permanent representative in The Netherlands to which or to whom the Common Shares are attributable; and

(b) the non-resident Shareholder is not entitled to a share in the profits of an enterprise effectively managed in The Netherlands other than by way of securities or through an employment contract, the Common Shares being attributable to that enterprise.

United States Taxation

The following discussion addresses the U.S. federal income taxation of a beneficial owner of the Company's Common Shares that is an individual who is a citizen or resident of the United States, or a corporation, partnership or other entity created or organized under the laws of the United States or any other state or political subdivision thereof, or an estate or trust that is subject to U.S. federal income taxation without regard to the source of its

income (a "U.S. Investor"). The following summary does not address the U.S. tax treatment of certain types of U.S. Investors subject to special rules (e.g., dealers in securities, financial institutions, U.S. Investors whose functional currency is not the U.S. dollar, individual retirement and other tax deferred accounts, life insurance companies, tax-exempt organizations and investors owning 10% or more of the Common Shares) or of other U.S. federal taxes, such as U.S. federal estate tax, or of state or local tax laws. Prospective U.S. Investors are advised to consult their own tax advisers to ascertain the tax effect of ownership and disposition of the Common Shares with respect to their particular circumstances.

Taxation of Dividends

To the extent paid out of current or accumulated earnings and profits of the Company, as determined for United States federal income tax purposes, the gross amount of dividends (including the amount of Netherlands taxes withheld therefrom) paid with respect to the Common Shares (other than certain pro rata distributions of capital stock of the Company or rights to subscribe for shares of capital stock of the Company) will be included in the gross income of a U.S. Investor as ordinary foreign source income on the date of receipt. For foreign tax credit purposes, such dividends will generally constitute "passive income", or in the case of certain U.S. Investors, "financial services income". Such dividends will not be eligible for the dividends received deduction allowed to United States corporations. Any distribution that exceeds the Company's current and accumulated earnings and profits will be treated as a nontaxable return of capital to the extent of the U.S. Investor's tax basis in the Common Shares and thereafter as a capital gain. The amount of any cash distribution paid in any currency other than U.S. dollars ("foreign currency") will be equal to the U.S. dollar value of such foreign currency distribution on the date of receipt, regardless of whether a U.S. Investor converts the payment into U.S. dollars. Gain or loss, if any, recognized by a U.S. Investor on the sale or disposition of such foreign currency will be U.S. source ordinary income or loss.

Netherlands withholding tax imposed on dividends paid to a U.S. Investor by the Company at the Convention rate of 15% will be treated as a foreign income tax eligible, subject to certain limitations, for credit against such U.S. Investor's U.S. federal tax liability.

Taxation on Sale or Exchange

A U.S. Investor will generally recognize a gain or a loss for U.S. federal income tax purposes on the sale, exchange or other disposition of Common Shares equal to the difference, if any, between the amount realized on such sale, exchange or other disposition and the U.S. Investor's adjusted tax basis in the Common Shares. In general, a U.S. Investor's adjusted tax basis in Common Shares will be equal to the amount paid by the U.S. Investor for such Common Shares. Such gain or loss will be capital gain or loss if the Common Shares are held as a capital asset and will be long-term capital gain or loss if at the time of sale, exchange or other disposition the Common Shares have been held for more than one year. Gain, if any, will generally be U.S. source income.

Backup Withholding and Information Reporting

In general, information reporting will apply to certain dividends paid on the Common Shares and to the proceeds of sale of the Common Shares paid to U.S. Investors other than certain exempt recipients (such as corporations). A 31% backup withholding tax may apply to such payments if the U.S. Investor fails to provide an accurate taxpayer identification number or certification of exempt status or fails to report in full dividend and interest income.

Item 8: Selected Consolidated Financial Data

Reference is made to the information appearing under the caption "Selected Consolidated Financial Data" on page 29 of the Registrant's 1996 Annual Report to Shareholders, which information is hereby incorporated by reference.

Item 9: Management's Discussion and Analysis of Financial Condition and Results of Operations

Reference is made to the information appearing under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations" on pages 30 through 40 of the Registrant's 1996 Annual Report to Shareholders, which information is hereby incorporated by reference.

Item 10: Directors and Officers of Registrant

Supervisory Board

The management of the Company is entrusted to the Management Board under the supervision of the Supervisory Board. The Supervisory Board advises the Management Board and is responsible for supervising the policies pursued by the Management Board and the general course of affairs of the Company and its business. In fulfilling their duties, the members of the Supervisory Board must serve the interests of the Company and its business.

The Supervisory Board shall consist of such number of members as resolved by the general meeting of shareholders upon proposal of the Supervisory Board, with a minimum of six members. The members of the Supervisory Board are appointed upon proposal of the Supervisory Board by the general shareholders' meeting by a majority of the votes cast at a meeting where at least one-half of the outstanding share capital is present or represented. On June 24, 1996 the annual general meeting of shareholders approved a resolution of the Supervisory Board to increase the size of the Supervisory Board from six to seven members and appointed Robert M. White as a new member of the Supervisory Board. The Supervisory Board intends to propose a further increase in the size of the

Supervisory Board to up to eight members, two of which would not be affiliated with the Company or its direct or indirect shareholders. SGS-THOMSON Holding II has informed the Company that it intends to concur with this proposal.

Pursuant to various shareholders agreements, the members of the Supervisory Board of the Company are required to include three members designated by the French shareholders from the Board of Directors of FT2CI (of whom Thomson-CSF has the right to appoint one member and FTlCI, a corporation owned by CEA-Industrie and France Telecom, has the right to appoint two members), and three members designated by the Italian shareholders (of whom I.R.I. has the right to appoint two members and Comitato SIR has the right to appoint one member). See Item 4: "Control of Registrant -- Shareholder Agreements".

The members of the Supervisory Board shall appoint a chairman and vice chairman of the Supervisory Board from among the members of the Supervisory Board (with approval of at least three-quarters of the members of the Supervisory Board) and may appoint one or more members as a delegate supervisory director to communicate on a regular basis with the Management Board. Resolutions of the Supervisory Board require the approval of at least three-quarters of its members. The Supervisory Board must meet upon request by two or more of its members or by the Management Board. The Supervisory Board has adopted internal regulations to clarify the manner by which it carries out the supervisory duties imposed upon it by law, the Company's Articles of Association and resolutions of the shareholders and the Supervisory Board itself. By such resolution the Supervisory Board: (x) authorized (i) the establishment of a secretariat headed by an individual approved by it and appointed for a one-year renewable term (a) to assist the Chairman and Vice Chairman of the Supervisory Board in the operations of the board, (b) to implement and oversee the execution within the Company of decisions adopted by the Supervisory Board and (c) to cooperate in and contribute to the execution of the functions of the designated Secretary and Assistant Secretary of the Supervisory Board, (ii) (a) the possibility of the appointment by each member of the Supervisory Board of an assistant and (b) the appointment by such board of two controllers to exercise operational and financial control over the operations of the Company who, with assistants, will also review operation reports and the implementation of Supervisory Board decisions, and (iii) the establishment by the Supervisory Board of advisory committees; and (y) established the procedure for the preparation of Supervisory Board resolutions and the setting of such board's calendar.

Members of the Supervisory Board must retire no later than at the ordinary general meeting of shareholders held after a period of three years following their appointment, but may be reelected. A member of the Supervisory Board shall retire at the ordinary general meeting of shareholders held in the year in which he reaches the age prescribed by law for retirement of a supervisory director. Members of the Supervisory Board may be suspended or dismissed by the general meeting of shareholders. The Supervisory Board may make a proposal to the general meeting of shareholders for the suspension or dismissal of one or more of its members. The members of the Supervisory Board may receive compensation if authorized by the general meeting of shareholders.

The shareholders agreement between the consortium of French shareholders and the consortium of Italian shareholders, as shareholders of SGS-THOMSON Holding, also

includes certain provisions requiring the approval of the Supervisory Board of SGS-THOMSON Holding for certain actions by SGS-THOMSON Holding, the Company and its subsidiaries. In addition, pursuant to certain other shareholders agreements among the consortium of French shareholders and a decree issued by certain Ministries of The Republic of France, the approval by members of the Supervisory Board appointed by the French shareholders of certain actions to be taken by the Company or its subsidiaries requires the approval of the Board of Directors of certain companies in the consortium of French shareholders and is subject to a veto by certain Ministries of The Republic of France. See Item 1: "Description of Business -- Competition" and Item 4: "Control of Registrant --Shareholder Agreements". These requirements for the prior approval of various actions to be taken by the Company and its subsidiaries may give rise to a conflict of interest between the interests of the Company and the individual shareholders approving such actions, and may result in a delay in the ability of the Management Board to respond as quickly as may be necessary in the rapidly changing environment of the semiconductor industry. Such approval process is subject to the provisions of Dutch law requiring members of the Supervisory Board to act independently in the supervision of the management of the Company.

As of the date of this report, the members of the Supervisory Board were:

Name	Position	Year Appointed	Age
Bruno Steve	Chairman	1989	55
Jean-Pierre Noblanc	Vice Chairman	1994	58
Remy Dullieux	Member	1993	46
Riccardo Gallo	Member	1997	53
Alessandro Ovi	Member	1994	53
Henri Starck	Member	1987	68
Robert M. White	Member	1996	58

Bruno Steve has been a member of the Company's Supervisory Board since 1989. He served as Vice Chairman of the Supervisory Board from 1989 to July 1990. From July 1990 to March 1993, Mr. Steve served as Chairman of the Supervisory Board. He has been with I.R.I., Finmeccanica's parent company, Finmeccanica and other affiliates of I.R.I. in various senior positions for over 15 years. He has been the Chief Operating Officer of Finmeccanica since 1988 and Chief Executive Officer since May 1995. He was Senior Vice President of Planning, Finance and Control of I.R.I. from 1984 to 1988. Prior to 1984, Mr. Steve served in several key executive positions at STET, I.R.I.s holding company for the telecommunications sector.

Jean-Pierre Noblanc has been a member of the Supervisory Board since 1994 and its Chairman until June 1996. Mr. Noblanc is presently General Manager of the Components Sector of CEA Industrie. Prior to joining CEA Industrie, Mr. Noblanc served at CNET, the Research Center of France Telecom, as Director of the Applied Research Center of Bagneux and of the Microelectronics Center of Grenoble, successively. Mr. Noblanc holds a degree in engineering from the Ecole Superieure d'Electricite and a doctoral degree in the Physical Sciences from the University of Paris. Mr. Noblanc is an Associate Member of the Committee on Applications of the French Academy of Sciences and a director of Thomson S.A. Mr. Noblanc also serves on the board of Pixtech Inc. and Picogiga S.A.

Remy Dullieux has been a member of the Supervisory Board since 1993. He is a graduate of the Ecole Polytechnique. Since June 1996, Mr. Dullieux has served as a France Telecom Executive Manager for the Northern and Eastern areas of France. From 1991 to June 1996, Mr. Dullieux served as Group Executive Vice President for Strategic Procurement and Development of France Telecom. From 1985 to 1988, Mr. Dullieux served as Regional Manager of Creteil.

Alessandro Ovi has been a member of the Supervisory Board since 1994. He received a doctoral degree in Nuclear Engineering from the Politecnico of Milan and a master degree of science in Operations Research from Massachusetts Institute of Technology. He is currently the Chief Executive Officer of Tecnitel S.p.A., a subsidiary of STET, and President of MEI. Prior to joining Tecnitel S.p.A., Mr. Ovi was the Senior Vice President of International Affairs and Communications at I.R.I. He currently serves on the boards of Alitalia, STET, Italtel, a STET and Siemens Company, Sirti, Zambon and Carnegie Mellon University.

Riccardo Gallo was appointed to the Supervisory Board in 1997. He is Associate Professor of Industrial Economics at the Engineering Faculty of "La Sapienza" University in Rome. He is also a member of Comitato Sir. From 1982 to 1991 he served as General Director at the Italian Ministry of National Budget. At the beginning of the 1990s he served as Vice Chairman of I.R.I. In 1994, he was appointed by the Italian Minister of Industry as Extraordinary Commissioner of Fidia, a research-oriented pharmaceutical company.

Henri Starck has been a member of the Supervisory Board since 1987. Mr. Starck served as Chairman and Vice Chairman of the Supervisory Board from June 1987 to June 1990 and from June 1990 to January 1993, respectively, during which time he was General Manager of Thomson-CSF. Mr. Starck is currently an adviser to the President of Thomson-CSF and a director of Sextant Avionique. Mr. Starck is a graduate of the Ecole Polytechnique and the Ecole Nationale Superieure du Genie Maritime.

Robert M. White was appointed to the Supervisory Board in June 1996. Mr. White is currently a Professor and Department Head at Carnegie Mellon University and serves as a member of several academic and corporate boards, including those of Ontrack Computer Systems, Inc., Zilog, Inc., Foundation for the National Medals of Science and Technology, Industrial Advisory Board, Lawrence Livermore National Laboratory and NEA Academic. From 1990 to 1993, Mr. White served as Under Secretary of Commerce for Technology in the United States Government. Prior to 1990, Mr. White served in several key executive positions at Xerox Corporation, Control Data Corporation and MCC. He received a doctoral degree in Physics from Stanford University and graduated with a degree in Science from the Massachusetts Institute of Technology. Mr. White has published four books, three of which have been translated into foreign languages, and over one hundred articles in the field of Physics.

Management Board

The management of the Company is entrusted to the Management Board under the supervision of the Supervisory Board. Under the Articles of Association, the Management Board shall obtain prior approval (x) from the Supervisory Board for (i) all proposals to be submitted to a vote at the general meeting of shareholders, (ii) the formation of all companies, acquisition or sale of any participation, and conclusion of any cooperation and participation agreement, (iii) all pluriannual plans of the Company and the budget for the first coming year, covering investment policy, policy regarding research and development, as well as commercial policy and objectives, general financial policy, and policy regarding personnel, and (iv) all acts, decisions or operations covered by the foregoing and constituting a significant change with respect to decisions already taken by the Supervisory Board and (y) from the general meeting of shareholders for decisions relating to (i) the sale of all or of an important part of the Company's assets or concerns, and (ii) all mergers, acquisitions or joint ventures which the Company wishes to enter into. In addition, under the Articles of Association, the Supervisory Board may specify by resolution certain actions by the Management Board that require its prior approval. Following the adoption of such a resolution, the actions by the Management Board with respect to the Company and all direct or indirect subsidiaries of the Company requiring such prior approval include the following: (i) modification of its Articles of Association; (ii) change in its authorized share capital, issue, acquisition or disposal of its own shares, change in any shareholder rights or issue of any instruments granting an interest in its capital or profits; (iii) liquidation or disposal of all or a substantial and material part of its assets or any shares it holds in any of its subsidiaries; (iv) entering into any merger, acquisition or joint venture agreement (and, if substantial and material, any agreement relating to intellectual property) or formation of a new company; (v) approval of such company's draft consolidated balance sheets and financial statements or any profit distribution by such company; (vi) entering into any agreement with any of the direct or indirect French or Italian Owners outside the normal course of business; (vii) submission of documents reporting on (a) approved policy, expected progress and results and (b) strategic long-term business plans and consolidated annual budgets or any modifications to such; (viii) preparation of long-term business plans and annual budgets; (ix) adoption and implementation of such long-term business plans and annual budgets; (x) approval of all operations outside the normal course of business, including operations already provided for in the annual budget; and (xi) approval of the quarterly, semi-annual and annual consolidated financial statements prepared in accordance with internationally accepted accounting principles. Such resolution also requires that the Management Board obtain prior approval from the Supervisory Board for (i) the appointment of the members of the statutory management, administration and control bodies of SGS-THOMSON Microelectronics S.A. and SGS-THOMSON Microelectronics s.r.l.; and (ii) the nomination of the statutory management, administration and control bodies of the Company and each of the Company's other direct and indirect subsidiaries followed by confirmation to the Supervisory Board of such nominees' appointments. The general meeting of shareholders may also specify certain actions of the Management Board that require shareholder approval. The shareholders have resolved that the Management Board must obtain shareholder approval prior to: (i) the sale of all or of an important part of the Company's assets and concerns and (ii) all mergers, acquisitions or joint ventures which the Company wishes to enter into. See "Item 1: Description of Business -- Competition" and "Item 13: Interest of Management in Certain Transactions".

The Management Board shall consist of such number of members as resolved by the general meeting of shareholders upon the proposal of the Supervisory Board. The members of the Management Board are appointed for three year terms upon proposal by the Supervisory Board by the general shareholders' meeting by a majority of the votes cast at a meeting where at least one-half of the outstanding share capital is present or represented. The Supervisory Board appoints one of the members of the Management Board to be chairman of the Management Board (upon approval of at least three-quarters of the members of the Supervisory Board). Resolutions of the Management Board require the approval of a majority of its members. Mr. Pasquale Pistorio, the Company's President and Chief Executive Officer, is currently the sole member of the Management Board.

The general meeting of shareholders may suspend or dismiss one or more members of the Management Board at a meeting at which at least one-half of the outstanding share capital is present or represented. No quorum is required if a suspension or dismissal is proposed by the Supervisory Board. The Supervisory Board may suspend members of the Management Board, but a general meeting of shareholders must be convened within three months after such suspension to confirm or reject the suspension. The Supervisory Board shall appoint one or more persons who shall at any time in the event of absence or inability to act of all the members of the Management Board be temporarily responsible for the management of the Company. The Supervisory Board determines the compensation and other terms and conditions of employment of the members of the Management Board.

Executive Officers

As a legal matter, the executive officers of the Company support the Management Board in its management of the Company. In practice, the executive officers and the Management Board share management responsibilities. The Company is organized in a matrix structure with geographical regions interacting with product divisions, bringing all levels of management closer to the customer and facilitating communication among research and development, production, marketing and sales organizations.

The executive officers of the Company are (as of the date of this report):

Name	Position	Years with the Company(1)	Years in Semiconductor Industry	Age
Pasquale Pistorio	President and Chief Executive Officer	17	33	61
Laurent Bosson	Corporate Vice President, Front-end Manufacturing and Americas Region	14	14	54
Carlo Bozotti	Corporate Vice President, European and Headquarters Region	20	20	44
Salvatore Castorina	Corporate Vice President, Discrete and Standard ICs Group	15	31	61
Murray Duffin	Corporate Vice President, Total Quality Management	10	37	63
Alain Dutheil	Corporate Vice President, Strategic Planning and Human Resources	14	27	52
Ennio Filauro	Corporate Vice President, Memory Products Group	28	37	64
Philippe Geyres	Corporate Vice President, Programmable Products Group	13	21	44
Maurizio Ghirga	Corporate Vice President, Chief Financial Officer	14	14	59
Jean-Claude Marquet	Corporate Vice President Asia Pacific Region	11	30	55
Pier Angelo Martinotti	Corporate Vice President, New Ventures Group	16	29	56
Joel Monnier	Corporate Vice President, Central Research and Development	14	23	52
Piero Mosconi	Corporate Vice President, Treasurer	33	33	57
Aldo Romano	Corporate Vice President, Dedicated Products Group	31	31	56
Giordano Seragnoli	Corporate Vice President, Back-end Manufacturing and Subsystems	32	34	60
Keizo Shibata	Corporate Vice President, Japan Region	5	32	60

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(1) Including years with Thomson Semiconducteurs or SGS Microelettronica.

Pasquale Pistorio has more than 30 years of experience in the semiconductor industry. After graduating in Electrical Engineering from the Polytechnical University of Turin in 1963, he started his career selling Motorola products. Mr. Pistorio joined Motorola in 1967, becoming Director of World Marketing in 1977 and General Manager of the International Semiconductor Division in 1978. Mr. Pistorio joined SGS Microelettronica as President and Chief Executive Officer in 1980 and became President and Chief Executive Officer of the Company upon its formation in 1987.

Laurent Bosson has served as Corporate Vice President, Central Manufacturing and VLSI Fads since 1989 and in 1992 he was given additional responsibility as President and Chief Executive Officer of the Company's operations in the Americas. Mr. Bosson received a Masters degree in Chemistry from the University of Dijon in 1969. He joined Thomson-

CSF in 1964 and has held several positions in engineering and manufacturing. In 1982, Mr. Bosson was appointed General Manager of the Tours and Alencon facilities of Thomson Semiconducteurs. In 1985, he joined the French subsidiary of SGS Microelettronica as General Manager of the Rennes, France manufacturing facility.

Carlo Bozotti has served as Corporate Vice President, Europe and Headquarters Region since 1994. Mr. Bozotti joined SGS Microelettronica in 1977 after graduating in Electronic Engineering from the University of Pavia. Mr. Bozotti served as Product Manager for the Industrial, Computer Peripheral and Telecom divisions and as Product Manager for the Monolithic Microsystems' Telecom business unit from 1986 to 1987. He was appointed Director of Corporate Strategic Marketing and Key Accounts for the Headquarters Region in 1988 and became Vice President, Marketing and Sales, Americas Division in 1991.

Salvatore Castorina has served as Corporate Vice President, Discrete and Standard ICs Group since 1989. Mr. Castorina received his engineering degree in Electronics from the Polytechnical University of Turin and began his career as a teacher of electrical and electronic technologies prior to joining Thomson-CSF in Milan in 1965. In 1967, he joined Motorola Semiconductors and held various positions in sales and marketing. In 1981, Mr. Castorina joined the Company as Transistor General Manager in Catania and became the General Manager of the Company's Discrete Division in 1989.

Murray Duffin has served as Corporate Vice President, Total Quality Management since 1992. Mr. Duffin graduated from the University of Manitoba in Electrical Engineering and later studied Semiconductor Physics and Computer Logic at the University of California Los Angeles and received an MBA from Arizona State University. Mr. Duffin started his career in 1959 as an RF Applications Engineer and thereafter held numerous managerial positions within most of the departments at TRW and Motorola Semiconductors prior to joining the Company in 1986. From 1986 to 1992, Mr. Duffin was in charge of the quality and service organization.

Alain Dutheil has served as Corporate Vice President, Strategic Planning and Human Resources since 1994 and 1992, respectively. Mr. Dutheil is also President of the Company's French subsidiary, SGS-THOMSON S.A. After graduating in Electrical Engineering from the Ecole Superieure d'Ingenieurs de Marseilles (ESIM), Mr. Dutheil joined Texas Instruments in 1969 as a Production Engineer, becoming Director for Discrete Products in France and Human Resources Director for Texas Instruments, France in 1980 and Director of Operations for Texas Instruments, Portugal in 1982. He joined Thomson Semiconducteurs in 1983 as General Manager of a plant in Aix-en-Provence, France and then became General Manager of the Company's Discrete Products Division. From 1989 to 1994, Mr. Dutheil served as Director for Worldwide Back-end Manufacturing in addition to serving as Corporate Vice President for Human Resources from 1992 until the present.

Ennio Filauro has served as Corporate Vice President, General Manager Memory Products Group since 1990. After graduating with a degree in Electrical Engineering from the University of Palermo, Mr. Filauro began his career in 1958 as a member of the Engineering and Quality Control Group of Raytheon Italia. In 1968, Mr. Filauro joined SGS Microelettronica as head of Quality Control Services at the research and development center in Castelletto, and was subsequently responsible for the Central Production Direction of the

facilities in Rennes, Falkirk and Catania. From 1974 to 1979, Mr. Filauro served as General Manager of the facility in Catania, and thereafter served as Director of the Corporate Engineering Group in Agrate. He became General Manager of the VLSI Division of SGS Microelettronica in 1985.

Philippe Geyres has served as Corporate Vice President, General Manager Programmable Products Group since 1990. Mr. Geyres graduated from the Ecole Polytechnique in 1973 and began his career with IBM in France before joining Schlumberger Group in 1980 as Data Processing Director. He was subsequently appointed Deputy Director of the IC Division at Fairchild Semiconductors. Mr. Geyres joined Thomson Semiconducteurs in 1983 as Director of the Bipolar Integrated Circuits Division. He was appointed Strategic Programs Director in 1987, and later the same year, became Corporate Vice President, Strategic Planning of the Company.

Maurizio Ghirga became Corporate Vice President, Chief Financial Officer in 1987, after having served as chief financial controller of SGS Microelettronica since 1983. Mr. Ghirga has a degree in Business Administration from the University of Genoa. He spent more than ten years of his career in various financial capacities at ESSO Company (an Exxon subsidiary in Italy) and prior to joining the Company was Financial Controller of one of the largest refinery plants in Italy and of an ESSO chemical subsidiary.

Jean-Claude Marquet has served as Corporate Vice President, Asia Pacific Region since July 1995. After graduating in Electrical and Electronics Engineering from the Ecole Breguet Paris, Mr. Marquet began his career in the National French Research Organisation and later joined Alcatel. In 1969, he joined Philips Components. He remained at Philips until 1978, when he joined Ericsson, eventually becoming President of Ericsson's French operations. In 1985, Mr. Marquet joined Thomson Semiconducteurs as Vice President Sales and Marketing, France. Thereafter, Mr. Marquet served as Vice President Sales and Marketing for France and Benelux, and Vice President Asia Pacific and Director of Sales and Marketing for the region.

Pier Angelo Martinotti has served as Corporate Vice President, General Manager New Ventures Group since 1994. A graduate in Electronic Engineering from the Polytechnical University of Turin, Mr. Martinotti began his career at the Company in 1965 as an Application and Marketing Engineer. In 1968, he joined Motorola Semiconductors in the area of strategic marketing in Europe, and in 1975 became the Marketing (Sales) Director for Europe. From 1986 to 1990, Mr. Martinotti was Chief Executive Officer of Innovative Silicon Technology, a former subsidiary of the Company. Mr. Martinotti was appointed Director of Corporate Strategic Planning in 1990.

Joel Monnier has served as Corporate Vice President, Director of Central Research and Development since 1989. After graduating in Electrical Engineering from the Institut National Polytechnique of Grenoble, Ecole Nationale Superieure de Radio Electricite, Mr. Monnier obtained a doctoral degree in microelectronics at LETI/CENG. He began his career in the semiconductor industry in 1968 as a researcher with CENG, and subsequently joined the research and development laboratories of Texas Instruments in Villeneuve Loubet, France and Houston, Texas, eventually becoming Engineering Manager and Operation Manager at Texas Instruments. Mr. Monnier joined Thomson-CSF in 1983 as head of the

research and manufacturing unit of Thomson Semiconducteurs. In 1987, he was appointed Vice President and Corporate Director of Manufacturing.

Piero Mosconi has served as Corporate Vice President, Treasurer since 1987. After graduating in accounting from Monza in 1960, Mr. Mosconi joined the faculty at the University of Milan. Mr. Mosconi worked with an Italian bank before joining the Foreign Subsidiaries Department at SGS Microelettronica in 1964 and becoming Corporate Director of Finance in 1980.

Aldo Romano has served as Corporate Vice President, General Manager Dedicated Products Group since 1987. Mr. Romano is also Managing Director of the Company's Italian subsidiary, SGS-THOMSON Microelectronics s.r.l. A graduate in Electronic Engineering from the University of Padova in 1963, Mr. Romano joined SGS Microelettronica in 1965 as a designer of linear ICs, becoming head of the linear IC design laboratory in 1968 and head of Marketing and Applications in 1976. Mr. Romano became Director of the Bipolar IC Division (which has evolved into the Dedicated Products Group) in 1980.

Giordano Seragnoli has served as Corporate Vice President, General Manager Subsystems since 1987 and since 1994, Director for Worldwide Back-end Manufacturing. After graduating in Electrical Engineering from the University of Bologna, Mr. Seragnoli joined the Thomson Group as RF Application Designer in 1962 and joined SGS Microelettronica in 1965. Thereafter, Mr. Seragnoli served in various capacities within the Company, including Strategic Marketing Manager and Subsystems Division Manager, Subsystems Division Manager (Agrate), Technical Facilities Manager, Subsystems Division Manager and Back-End Manager.

Keizo Shibata has served as Corporate Vice President and President of the Company's Japanese subsidiary, SGS-THOMSON Microelectronics K.K., since 1992. Mr. Shibata obtained bachelors and masters degrees in Engineering from Osaka University and has 31 years of experience in the semiconductor industry. Prior to joining SGS-THOMSON, Mr. Shibata was employed with Toshiba Corporation since 1964 in various capacities. From 1987 to 1988, Mr. Shibata served as Chairman of both World Semiconductor Trade Statistics and the Trade Policy Committee of the Electric Industry Association of Japan.

As is common in the semiconductor industry, the Company's success depends to a significant extent upon, among other factors, the continued service of its key senior executives and research and development, engineering, marketing, sales, manufacturing, support and other personnel, and on its ability to continue to attract, retain and motivate qualified personnel. The competition for such employees is intense, and the loss of the services of any of these key personnel without adequate replacement or the inability to attract new qualified personnel could have a material adverse effect on the Company. The Company does not maintain insurance with respect to the loss of any of its key personnel.

Item 11: Compensation of Directors and Officers

The aggregate cash compensation offered for 1996 to the members of the Supervisory Board by the Company was approximately $462,000. The amount of cash compensation for 1996 to the executive officers of the Company and members of the Management Board as a group by the Company and its subsidiaries was approximately $7 million.

In 1989, the Company established a Corporate Executive Incentive Program (the "EIP") that entitles selected executives and members of the Management Board to a yearly bonus based upon the individual performance of such executives. The maximum bonus awarded under the EIP is based upon a percentage of the executive's or member's salary and is adjusted to reflect the overall performance of the Company. The participants in the EIP must satisfy certain personal objectives that are focused on customer service, profit, cash flow and market share.

The executive officers and members of the Management Board were also covered in 1996 under certain group life and medical insurance programs provided by the Company. The aggregate additional amount set aside by the Company in 1996 to provide pension, retirement or similar benefits for executive officers and members of the Management Board of the Company as a group was approximately $2.8 million.

Item 12: Option to Purchase Securities from Registrant or Subsidiaries

As of June 24, 1997, options to purchase up to an aggregate of 171,790 Common Shares were outstanding under the Company's first stock option plan (the "1989 Stock Option Plan"). Such options are fully vested and are exercisable at the original issue price, as adjusted to reflect the 40:1 stock split effected in connection with the Initial Public Offering, of NLG 25 per share ($14.51 based on the noon buying rate in New York City for cable transfers in Dutch guilders as certified for customs purposes by the Federal Reserve Bank of New York of US$1=NLG 1.7225 on May 22, 1996 (the "Noon Buying Rate")) or at the price of NLG 17.50 per share ($10.15 based on the Noon Buying Rate). Of such outstanding options, 49,000 are held by executive officers of the Company as a group and all outstanding options expire on December 18, 1999.

On October 20, 1995, the Shareholders of the Company approved resolutions authorizing the Supervisory Board for a period of five years to adopt and administer a new stock option plan which provides for the granting to managers and professionals of the Company of options to purchase up to a maximum of 5.5 million Common Shares (the "1995 Stock Option Plan"). The Company has granted 1,200,000 options pursuant to the 1995 Stock Option Plan to purchase up to 1,200,000 Common Shares at a price per Common Share of $36.25 and of which, as of May 1, 1997, 1,174,200 options were still exercisable. Such options are exercisable for a period of eight years following the date of grant.

On June 24, 1996 the general meeting of shareholders approved the granting of options to purchase up to 72,000 Common Shares to members and professionals of the Supervisory Board over a period of three consecutive years, beginning in 1996. Options

granted thereunder will be exercisable until the eighth anniversary date following the date of grant at the closing price of the Common Shares on the New York Stock Exchange on the date such options are exercised.

Item 13: Interest of Management in Certain Transactions

One of the Company's key customers is Thomson Multimedia. Thomson Multimedia and Thomson-CSF, one of the indirect shareholders of the Company (see "Item 4: Control of Registrant"), are both controlled by Thomson S.A. The Company sells a broad range of products to Thomson Multimedia, including dedicated products, microcontrollers and semicustom devices, for use in televisions, video cassette recorders and satellite receiver systems. The Company believes that all of the products that it sells to Thomson Multimedia are sold on commercial terms no less favorable to the Company than could be obtained with non-affiliated parties. The Company has also formed a joint venture with Thomson Multimedia to conduct joint research and development on advanced television products, including digital television products. The Company and Thomson Multimedia share the funding of the joint venture's designers, engineers and managers.

The Company has formed a joint venture research and development center with CNET in the form of a Groupement d'Interet Economique ("GIE"). CNET is a research laboratory that is wholly owned by France Telecom, one of the indirect shareholders of the Company. See "Item 4: Control of Registrant". The research center is housed at the Company's Crolles, France manufacturing facility. It is developing submicron process technologies. The joint venture between the Company and CNET was created before France Telecom became an indirect shareholder of the Company.

The Company participated in a joint research and development project with LETI with respect to high-density silicium integrated circuits. LETI is a research laboratory that is a department of CEA, the parent of one of the indirect shareholders of the Company. See "Item 4: Control of Registrant". In 1995, the Company has signed an agreement providing for a research and development cooperation with GRESSI, the research and development GIE formed by CNET and LETI. The objectives of the cooperation are to develop know-how on innovative aspects of VLSI technology evolution which can be transferred to industrial applications, and to address the development of innovative process steps and process modules to be used in future generations of VLSI products. The cooperation agreement is based upon a pluriannual plan through 1998, of which the Company is expected to bear half of the program's total cost.

The Company participates in certain programs sponsored by the French and Italian governments for the funding of research and development and industrialization through direct grants as well as low interest financing. See "Item 1: Description of Business -- State Support for the Semiconductor Industry". The shareholders of SGS-THOMSON Holding, the corporate parent of the Company's majority shareholder, are controlled, directly or indirectly, by the governments of the Republics of France and Italy. See "Item 4: Control of Registrant".

Sales to shareholders of the Company and their affiliates totalled $232.1 million in 1996. At December 31, 1996 there was no outstanding indebtedness guaranteed by indirect

shareholders, other than debt guaranteed by SGS-THOMSON Microelectronics Holding N.V. See Note 26 to the Consolidated Financial Statements.

From time to time, the Company may deposit with its direct or indirect shareholders, or their affiliates, available funds for investment on a short-term basis at market interest rates.

PART II

Item 14: Description of Securities to be Registered

Not applicable.

PART III

Item 15: Defaults upon Senior Securities

None.

Item 16: Changes in Securities and Changes in Security for Registered Securities

None.

PART IV

Item 17: Financial Statements

Not applicable.

Item 18: Financial Statements

Consolidated financial statements of SGS-THOMSON Microelectronics N.V. for each of the three years in the period ended December 31, 1996 are incorporated by reference from the Registrant's 1996 Annual Report to Shareholders, on pages 41 through 58.

Item 19: Financial Statements and Exhibits

(a) 1. Financial Statements

The financial statements listed in the accompanying Index to Financial Statements and Financial Statement Schedule are filed or incorporated by reference as part of this annual report.

2. Financial Statement Schedule

The financial statement schedule listed in the accompanying index is filed as part of this annual report.

(b) Exhibits

The exhibits listed in the accompanying index are filed or incorporated by reference as part of this annual report.

INDEX TO FINANCIAL STATEMENTS
AND FINANCIAL STATEMENT SCHEDULE
(Item 19(a))

AUDITOR'S REPORT

To the Supervisory Board and the Shareholders of SGS-THOMSON Microelectronics N.V.:

We have audited the accompanying consolidated balance sheets of SGS-THOMSON Microelectronics N.V. (a Dutch corporation) and subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of SGS-THOMSON Microelectronics N.V. and subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1995 in conformity with generally accepted accounting principles, as applied in the United States of America.

Arthur Andersen & Co.
Amsterdam, The Netherlands
January 26th, 1996

Schedule

SGS-THOMSON MICROELECTRONICS N.V.
VALUATION AND QUALIFYING ACCOUNTS
(Currency - Thousands of U.S. dollars)

	Balance at beginning of period	Translation adjustment	Charged to costs and expenses	Deductions	Balance at end of period
Valuation and qualifying accounts deducted from the related asset accounts					
1996					
Inventories	36,500	----	45,176	(36,500)	45,176
Accounts Receivable	17,881	(514)	1,114	(329)	18,152
1995					
Inventories	29,982	----	36,500	(29,982)	36,500
Accounts receivable	14,018	691	3,467	(295)	17,881
1994					
Inventories	28,121	----	29,982	(28,121)	29,982
Accounts receivable	12,181	893	3,198	(2,254)	14,018

To the Supervisory Board and the Shareholders of SGS-THOMSON Microelectronics N.V.:

We have audited the financial statements of SGS-THOMSON Microelectronics N.V. and subsidiaries as of December 31, 1995 and 1994 and for each of the three years in the period ended December 31, 1995 and have issued our report thereon dated January 26, 1996. We have also audited the schedule included in this Annual Report on Form 20-F as listed in item 19.

This schedule is the responsibility of the Company's management and is presented for purpose of complying with the Securities and Exchange Commission's rules and regulations and is not part of the basic financial statements.

In our opinion, the schedule referred to above fairly states, in all material respects, the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

Arthur Andersen & Co
Amsterdam, the Netherlands
June 26, 1996

Glossary

ASIC	application-specific integrated circuit
ASSP	application-specific standard product
BCD	bipolar, CMOS and DMOS process technology
BiCMOS	bipolar and CMOS process technology
CAD	computer aided design
CIM	computer integrated manufacturing
CMOS	complementary metal oxide silicon
DMOS	diffused metal oxide silicon
DRAMS	dynamic random access memory
DSP	digital signal processor
DVD	digital video disk
EEPROM	electrically erasable programmable read-only memory
EPROM	erasable programmable read-only memory
HCMOS	high-speed complementary metal-oxide-silicon
IC	integrated circuit
IGBT	insulated gate bipolar transistors
ISDN	integrated services digital network
Kbit	kilobit
Mbit	megabit
MOS	metal oxide silicon process technology
MOSFET	metal oxide silicon field effect transistor
MPEG	motion picture experts group
PROM	programmable read-only memory
RAM	random access memory
RF	radio frequency
RISC	reduced instruction set computing
ROM	read-only memory
SAM	serviceable available market
SLIC	subscriber line interface card
SMPS	switch mode power supply
SPC	statistical process control
SRAM	static random access memory
TAM	total available market
VLSI	very large scale integration

SIGNATURE

Pursuant to the Requirements of Section 12 of the Securities Exchange Act of 1934, the registrant certifies that it meets all of the requirements for filing on Form 20-F and has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

SGS-THOMSON Microelectronics N.V.

Date: June 27, 1997

By: /s/ Pasquale Pistorio

Name: Pasquale Pistorio
Title: President and Chief Executive Officer

INDEX TO EXHIBITS
(Item 19(b))

Exhibit Number	Description
13	SGS-THOMSON Microelectronics N.V. 1996 Annual Report to Shareholders
23	Consents of Independent Accountants

Exhibit 13

1996 Annual Report to Shareholders

SGS-THOMSON
MICROELECTRONICS
[GRAPHIC] 1996 ANNUAL REPORT

SGS-THOMSON Microelectronic N.V. is a global independent semiconductor company that produces a broad range of semiconductor integrated circuits (ICs) and discrete devices. Its products are used in high growth applications in the telecommunications, computer, consumer, automotive and industrial sectors. Based on the most recent available industry data, the Company is ranked among the top 10 worldwide semiconductor suppliers and is the world's leading supplier of analog ICs, EPROM/EEPROM non-volatile memories and MPEG decoder ICs. It serves customers in a variety of markets worldwide, including North America, Europe, Asia/Pacific and Japan. The common stock of SGS-THOMSON is listed on the New York Stock Exchange (symbol: STM) and the Bourse de Paris, and is quoted on SEAQ International.

CONTENTS

FINANCIAL HIGHLIGHTS

SGS-THOMSON Microelectronics N.V.

Twelve months ended December 31,

(In millions, except per share data)	1992	1993(1)	1994(1)	1995(1)	1996
CONSOLIDATED STATEMENT OF INCOME DATA:					
Net revenues	$ 1,568.1	$ 2,037.5	$ 2,644.9	$ 3,554.4	$ 4,122.4
Cost of sales(2)	(1,051.6)	(1,248.4)	(1,528.7)	(2,096.0)	(2,414.7)
Gross profit(2)	516.5	789.1	1,116.2	1,458.4	1707.7
Total operating expenses(3)	(464.7)	(573.6)	(683.2)	(807.4)	(908.3)
Operating income(4)	51.8	215.5	433.0	651.0	799.4
Net interest expenses/other(5)	(46.5)	(37.8)	(21.0)	(16.8)	(3.9)
Profit before tax	5.3	177.7	412.0	634.2	795.5
Income tax expense	(2.3)	(17.6)	(49.5)	(108.3)	(171.6)
Income before minority interests	3.0	160.1	362.5	525.9	623.9
Minority interests(6)	0	0	0	0.6	1.6
Net income(7)	$ 3.0	$ 160.1	$ 362.5	$ 526.5	$ 625.5
Earnings per share(8)	$ 0.06	$ 1.92	$ 3.04	$ 4.03	$ 4.50
Weighted average shares outstanding	53.6	83.5	119.4	130.6	138.7
CONSOLIDATED BALANCE SHEET DATA (END OF PERIOD):					
Cash, cash equivalents and marketable securities	$ 99.5	$ 327.4	$ 461.5	$ 758.4	$ 556.4
Working capital	467.7	390.0	291.1	417.4	611.8
Total assets	1,842.3	2,240.9	3,224.7	4,486.0	5,005.5
Short-term debt (including current portion of long-term debt)	360.6	231.1	322.5	492.8	428.2
Long-term debt (excluding current portion)(1)	547.6	374.8	277.2	200.7	194.9
Shareholders' equity(1)	412.9	1,004.0	1,680.0	2,661.7	3,260.0

(1) In October 1995, the Company completed a second public offering with net proceeds to the Company of approximately $371.6 million. In December 1994, the Company completed an Initial Public Offering with net proceeds to the Company of approximately $198.7 million. In 1993, the Company received a $500 million capital contribution that was effected in two steps, $250 million in May and $250 million in September. The Company also received a $100 million capital contribution in each of 1988, 1989 and 1991.

(2) Cost of sales is net of certain third-party funding for industrialization costs (which include certain costs incurred to bring prototype products to the production stage) included therein. See Note 19 to the Consolidated Financial Statements. For a discussion of certain significant charges reflected in cost of sales in 1994, 1995 and 1996, see "Management's Discussion and Analysis of Financial Condition and Results of Operations--Results of Operations."

(3) Includes, among other things, third-party funding for research and development, the expenses for which are reflected in research and development expenses, as well as foreign currency gains and losses, fab start-up costs, patent license payments received and patent costs incurred. The Company's reported research and development expenses do not include design center, process engineering, pre-production or industrialization costs.

(4) The Company has changed the title of this line item from "operating profit." The make-up of this line item has not changed.

(5) Includes mainly net interest expenses, plus a gain on disposal of an investment in 1992 and 1996.

(6) In 1994, the Company created a joint venture with a subsidiary of the Shenzhen Electronics Group ("SEG"). the Company owns a 60% interest in the joint venture, with a subsidiary of SEG owning the remaining 40%.

(7) The Company has changed the title of this line item from "net earnings." The make-up of this line item has not changed.

(8) Net earnings per share amounts have been restated to reflect a 40:1 stock split effected in connection with the Initial Public Offering.

In the original documents the following tables were represented by bar graphs:

NET REVENUES
($US Millions)
1992 - 1,568
1993 - 2,038
1994 - 2,645
1995 - 3,554
1996 - 4,122

NET INCOME
($US Millions)
1992 - 3.0
1993 - 160.1
1994 - 362.5
1995 - 526.5
1996 - 625.5

SHAREHOLDERS' EQUITY
($US Millions)
1992 - 412.9
1993 - 1,004.0
1994 - 1,680.0
1995 - 2,661.7
1996 - 3,260.0

[PHOTO]
/ PASQUALE PISTORIO
PRESIDENT AND CHIEF EXECUTIVE OFFICER

MESSAGE FROM THE PRESIDENT

SGS-THOMSON distinguished itself in 1996 by achieving consistent performance within a volatile semiconductor marketplace. The Company surpassed the $4 billion mark in net revenues, and both sales and profits increased at rates that outpaced the industry average and the served markets. We also maintained our market leadership in a variety of high growth applications, while at the same time investing in the future via a well-focused research and development effort.

Our ability to continue the Company's profitable growth in spite of a difficult market cycle was a direct reflection of SGS-THOMSON's established strategies of maintaining a high proportion of differentiated products, forming close alliances with major customers, and creating a balanced business mix by application and geography. It is also a tribute to a talented and dedicated team of people worldwide.

/ 1996 FINANCIAL HIGHLIGHTS

Net revenues for 1996 were a record $4.12 billion, an increase of 16% from 1995's results. Gross profit for the year amounted to $1.70 billion, increasing 17% year over year. This represented a gross margin of 41.4% of net revenues for 1996, compared with 41.0% in 1995. Operating income for the year increased 23% to $799.4 million. Expressed as a percentage of net revenues, the operating profit margin rose to 19.4% for the past year, versus 18.3% in 1995.

Net income for 1996 advanced 19% to $625.5 million, compared to $526.5 million for 1995. Earnings per share rose nearly 12% to $4.50, based on 138.7 million weighted average shares outstanding. The corresponding 1995 figure was $4.03 per share, based upon 130.6 million weighted average shares outstanding.

Due to our emphasis on differentiated products, focus on high growth applications, and breadth of geographic markets, 1996 clearly was a successful year for SGS-THOMSON from the perspective of overall sales and profitability. I should note that our rate of growth slowed in the latter part of the year due to the industry downturn. Also, our gross margin decreased to 38% in the fourth

"OUR PROFITABLE GROWTH REFLECTED SGS-THOMSON'S ESTABLISHED STRATEGIES TO FOSTER DIFFERENTIATED PRODUCTS, CLOSE ALLIANCES WITH CUSTOMERS, AND A BALANCED BUSINESS MIX."

quarter, which was within the expected range for this phase of the industry cycle, but nonetheless was below the strong levels of the past several quarters. This was partly due to the under-utilization of our non-VLSI fabs and a temporary reduction in output from Phoenix while we qualified that facility for additional manufacturing activities. The Company also experienced pricing pressures, especially on the commodity portion of our portfolio. We expect utilization at the non-VLSI fabs and Phoenix to improve as we move into 1997. However, we continue to see pricing pressure in the commodity area, and are thus maintaining cautious expectations for margins at least through the first quarter of the new year.

One of the ways in which we have responded to the challenging market conditions is by intensifying our control of operating costs. Total operating expenses were reduced as a percent of net revenues to 22.0% in 1996 from 22.7% in 1995, even though we continued to increase research and development expenses to support our technological leadership. Expenses also declined in absolute terms in the fourth quarter as compared with the year-ago period.

With confidence in the long-term prospects for our industry, we continued to invest in the growth of the Company. Last year, capital expenditures totalled $1.12 billion, compared with $1.00 billion in 1995. Research and development expenses increased by 21% to $532.3 million in 1996, and represented 12.9% of net revenues.

SGS-THOMSON finished the year with a sound balance sheet. At the end of 1996, cash, cash equivalents and marketable securities totaled $556.4 million. Total debt was $623.1 million, including $194.9 million of long-term debt, while net debt stood at $66.7 million. With shareholders' equity of $3.26 billion, our ratio of net debt-to-equity was a conservative 0.02.

/ OPERATING PERFORMANCE

The developments of 1996 clearly show that SGS-THOMSON has been the beneficiary of strategies to spur the growth of differentiated products and to create solid alliances with key customers. Differentiated products, which we define as dedicated/ASSPs, semicustom integrated circuits and microcontrollers, accounted for 58.6% of net revenues in 1996, compared to 51.5% in 1995. For the fourth quarter, differentiated products were a record 61.3% of net revenues, in spite of capacity constraints in our leading-edge, submicron technologies. The growth in differentiated products more than offset decreases in sales of commodity linear and discrete products. Further, we derived approximately 31% of our net revenues from significant customers with whom we have strategic alliances. Revenues generated by such alliances rose 36.5% over 1995. The stability produced by our strategic alliances also helped balance the industry-wide pressure on commodity business.

Our net revenues for 1996 were well-balanced from the perspective of applications. Consumer applications sales were up 26.4%, and accounted for 22.1% of net revenues. Sales of products used in the automotive market rose 20.4%, and represented 9.6% of the total. Business with the computer sector increased 13.8%, to reach 26.7% of net revenues. Sales of products for telecommunications applications increased 14.0%, representing 22.1% of net revenues. In the industrial area, sales rose at a rate of 8.8%, and were 19.6% of net revenues for the year.

Revenues from all major geographic regions advanced over the previous year, and outperformed the growth rates of the respective markets. Our North American sales posted a 10.4% increase for 1996, while the overall market decreased an estimated 9.2%. In the Asia/Pacific our sales were up 22.8%, versus a 6.7% decline for the region. SGS-THOMSON's sales in Europe rose 12.1%, compared with a 2.3% market decrease. Our Japan business enjoyed 46.8% sales growth, versus a 13.8% decrease for the region as a whole. As a percentage of net revenues, Europe represented 44.3%, North America 22.7%, Asia/Pacific 27.5% and Japan 5.5% for the year. Including products sold to the Asian operations of U.S. customers, North America represented more than 30% of net revenues.

/ SEMICONDUCTOR MARKET PERSPECTIVE

As I noted earlier, SGS-THOMSON's financial and operational progress during 1996 was achieved against the backdrop of a volatile semiconductor market environment. I would like to take this opportunity to provide an overview of the industry conditions that prevailed during much of the past year, and those that are expected to have an effect on our results in 1997. Please note that this is a general assessment, and that the timing of market phases may vary from our model by a quarter or two.

We believe there are four phases to the present market cycle. Phase I began in approximately the third or fourth quarter of 1995, and was marked by some overcapacity in certain commodity products, particularly DRAMs. While we do not manufacture such products, and thus were not seriously affected by the first phase, other producers suffered from price pressures.

Phase II began in the 1996 second and third quarters, characterized by an inventory liquidation period with prices falling more rapidly in response to very substantial over-supply. Again, the majority of the pricing pressure took place in commodity categories. Competitors in the most affected segments of the industry were obliged to adjust by liquidating inventory, cutting production and reducing employment.

"REVENUES WERE WELL-BALANCED FROM
THE PERSPECTIVE OF APPLICATIONS,
AND ALSO OUTPERFORMED THE GROWTH RATES
OF OUR REGIONAL MARKETS."

The 1996 fourth quarter represented the onset of Phase III of this market cycle. Production began to reach some equilibrium with demand, although total available capacity remains under-utilized, which has facilitated a reduction in excess inventories. Price pressures continue, but are showing signs of stabilizing with the exception of spot prices on certain commodity devices. We believe this phase will continue at least through the first quarter of 1997, and likely into the second quarter.

This will bring us to Phase IV, which should see the restoration of a greater balance between capacity and orders. Generally, demand should then start to outpace production, and conditions will be right for prices and margins to recover. With the start of this new phase of the cycle, we expect that the semiconductor market will return to its usual pattern of growth during the latter part of 1997.

SGS-THOMSON's approach to the changing conditions in our market has been to balance the need for restraint with prudent investments in new products and new facilities that will serve as our engines for continued growth. I would like to highlight some of the initiatives that we have undertaken recently with an eye toward the opportunities that we believe will arise in the near future.

/ NEW PRODUCT DEVELOPMENTS

Late in 1996, we announced the successful processing of the first wafers in the next generation of technology, using a 0.25 micron CMOS process (0.20 micron effective gate length). This exciting development will facilitate our program to manufacture "superintegrated" ICs for high speed applications, such as PCs; for low power applications, such as digital mobile phones; and for advanced consumer digital entertainment systems.

Also during the year, we further enhanced our position in the emerging market for new consumer electronics products by forming a joint development arrangement with Microsoft for DVD products, and by licensing the MPACT media processor from Chromatic Research. We also announced the first product on the market to employ the Macrovision 7.0 Anti-Copy System for DVD and set-top box applications. Another important product introduction for DVD applications was the Dolby AC-3 decoder. Also, we helped define industry standards with the development of the Video Interface Port, which was initiated together with several competitors and will create an architecture for using video in PCs.

We made an important addition to our portfolio of cores, introducing a fully compatible 486 core that customers can integrate into their own designs. Also, the Company entered into a promising new alliance, licensing to Samsung our ST20 32-bit micro core and D-950 DSP core technologies. Other innovations included a new generation of power MOSFET transistors with improved switching characteristics and better overall performance, and expanded offerings in Application Specific Discrete (ASD)(TM) products.

At the beginning of 1997, we announced an agreement for a joint technology, development and manufacturing program with Ramtron International, a specialized designer of advanced non-volatile memories. We anticipate that if this venture is successful, our two companies would develop--and SGS-THOMSON would manufacture--ferroelectric random access memory (FRAM) devices. The new FRAM products would combine the high speed of DRAMs, the non-volatility of ROMs, and the flexibility of EEPROMs to create features that are currently not available in any single semiconductor memory device. The resulting products would be targeted for use in communication products, palm-top computers, smart cards and other portable applications.

/ MANUFACTURING EXPANSION

Over the past year, we undertook a number of initiatives to expand our manufacturing resources in order to help relieve capacity constraints with regard to certain advanced products. Our Phoenix fab was qualified to produce a broader and more flexible range of products. We substantially increased our capacity to manufacture non-volatile memories, particularly the commonly used 2Mbit and 4Mbit Flash devices, by allocating more capacity in Agrate to this product line. The qualification of our new 8-inch fab in Catania is also nearly complete, with volume production of Flash memories expected in the second half of 1997. In addition, we took steps to strengthen our manufacturing presence in the Asia/Pacific region with the announcement of plans for a new state-of-the-art 8-inch submicron wafer diffusion plant in Singapore.

We were particularly pleased that our facility in Rancho Bernardo, California, became the first plant in the U.S. to receive international ISO 14001 certification as an environmentally-friendly manufacturing site. Rancho Bernardo also achieved compliance with respect to the even more stringent European Union environmental regulations known as the Eco-Management and Audit Scheme (EMAS). We now have a total of 12 sites approved according to the voluntary EMAS regulations, of which seven are also ISO 14001 certified. At SGS-THOMSON, we place a high priority on environmental policies, and work to maximize the use of recyclable or reusable materials while reducing consumption of resources and the amount of waste generated. We are confident that we are on target to achieve our goal of having all sites worldwide approved for EMAS before the end of 1997.

/ OUTLOOK

The decreased visibility on customer demand has made it somewhat difficult to predict market conditions, although we have set forth our view of the general direction of the market cycle. In any event, SGS-THOMSON enjoys both a strong financial position and a strong market position as we enter 1997. We will continue to emphasize our expertise in differentiated products in the coming year, while continuing to offer commodity products that contribute volume, profit and cash flow. As noted earlier, we are enthusiastic about the long-term growth prospects for the Company and the markets that we serve. We intend to move ahead with capital expenditure and R&D plans, committing a percentage of revenue on the same order of magnitude as during 1996.

With our ongoing focus on innovative differentiated products, diversification by applications and regions, and increasing productivity, we look forward to another year in which SGS-THOMSON will outperform the markets it serves.

PASQUALE PISTORIO
PRESIDENT AND CHIEF EXECUTIVE OFFICER

SGS-THOMSON AT A GLANCE

STRATEGIC STRENGTHS

/ BROAD LINE SUPPLIER OF DIFFERENTIATED PRODUCTS FOR HIGH GROWTH APPLICATIONS SUCH AS AUTOMOTIVE, COMPUTER, TELECOMMUNICATIONS, CONSUMER AND INDUSTRIAL MARKETS.

/ FOCUSED PORTFOLIO STRATEGY TO ACHIEVE WORLD LEADERSHIP IN DEDICATED, POWER AND NON-VOLATILE MEMORY PRODUCTS; "TOP 5" SHARE IN SEMICUSTOM, MICROCONTROLLERS AND SPECIAL SRAM PRODUCTS; AND PROFITABLE PARTICIPATION IN OTHER PRODUCTS, WHICH DO NOT INCLUDE DRAMS.

/ WIDE RANGE OF ADVANCED, INTER-MIXABLE TECHNOLOGIES FACILITATES SYSTEM-ON-A-CHIP APPROACH AND SUPPORTS DIFFERENTIATED PRODUCT STRATEGY.

/ GLOBAL, DIVERSIFIED CUSTOMER BASE NOTABLE FOR STRATEGIC ALLIANCES.

/ WORLDWIDE, HIGHLY EFFICIENT MANUFACTURING CAPACITY TO GIVE CUSTOMERS READY ACCESS TO PRODUCTS.

In the original document the following tables were represented by pie charts:

1996 Revenues by Region
- ----------
Europe - 44%
Asia/Pacific - 28%
Americas - 23%
Japan - 5%

1996 Revenues by Product Family
- ----------
Differentiated Products - 59%
Logic and Memories - 22%
Discretes - 14%
Standard/Commodities - 5%

1996 Revenues by Application
- ----------
Computers - 27%
Telecommunications - 22%
Consumer - 22%
Industrial - 19%
Automotive - 10%

SGS-THOMSON AT A GLANCE

/ 1996 REVENUES: US$4.12 BILLION / DIFFERENTIATED PRODUCTS/REVENUES: 58.6%

/ 17 MAIN MANUFACTURING SITES / 9 ADVANCED R&D SITES / 26,000 EMPLOYEES

/ 31 DESIGN AND APPLICATION CENTERS / 60 SALES OFFICES IN 24 COUNTRIES

/ OVER 12,000 PATENTS ISSUED AND PENDING, COVERING OVER 4,000 INVENTIONS

DPG - DEDICATED PRODUCTS GROUP /

Produces application-specific and custom products offering complete system solutions for all major end-user applications, including mobile communications terminals, automotive systems, digital and analog consumer systems and computer peripherals such as disk drives, monitors and printers.

Products are based on advanced bipolar, CMOS, BiCMOS, mixed-signal and power technologies.

[GRAPHIC]

MPG - MEMORY PRODUCTS GROUP /

Responsible for a broad range of memory products.

Products include non-volatile memories, EPROMs (of which MPG has been the leading supplier since 1993), Flash memories, EEPROMs, application specific memories and non-volatile RAMs; and smartcard products including chips and software support products. Does not produce DRAMs.

[GRAPHIC]

/ PPG - PROGRAMMABLE PRODUCTS GROUP

Products include microcomponents (such as a wide range of microcontrollers, microprocessors, digital signal processors); digital semicustom devices; PC graphic devices; multimedia acceleration ICs and digital video devices.

[GRAPHIC]

/ DSG - DISCRETE AND STANDARD ICS GROUP

Offers a broad product portfolio for a diverse customer base.

Products include discrete power devices such as power transistors (power bipolar, power MOS, 1GBT, VIPower), rectifiers, protection devices, thyristors and application-specific discrete (ASD) products; standard linear and logic ICs; radio frequency (RF) products.

[GRAPHIC]

NVG - NEW VENTURES GROUP /

Identifies and develops new business opportunities to complement the Company's existing activities and fully exploit its advanced technological expertise, manufacturing capabilities and global marketing team.

Initial activities have focused on manufacturing and marketing x86 microprocessors. New activities include design and manufacturing of "system on silicon" solutions based on the 486 CPU core, and more recently media processors based on Very Long Instruction Word (VLIW) processors.

[GRAPHIC]

SPG - SUBSYSTEMS PRODUCTS GROUP /

Produces electronic subsystems to provide complete solutions for OEM customer applications, particularly in accessories for cellular telephones.

Products include converters and complete power supplies; motor control modules; hands-free systems; battery chargers.

[GRAPHIC]

[GRAPHIC]

Automobile manufacturers have moved to increase the safety, comfort and engine performance of their products, with the result that the typical automobile has become a repository for a wide range of semiconductor products. Such innovations as anti-lock braking (ABS) systems and keyless door locks, as well as everyday requirements such as alternator regulators and directional signals, depend on SGS-THOMSON's technologies. The demand for microchip products in the automotive sector is so pervasive that industry sources estimate a compound annual growth rate of 16% in semiconductor content per vehicle between 1996 and the year 2000. SGS-THOMSON's sales of products for the automotive market increased 20.4% in 1996, and represented 9.6% of net revenues.

With its technological leadership, particularly in BCD/BiCMOS, the Company is able to accommodate a vast array of auto-related applications, including airbags, climate control, instrumentation, transmissions and on-board entertainment systems. Mixed analog/digital ICs produced by the Company have achieved strong market shares in such areas as engine management, battery charging, ABS and car information centers. SGS-THOMSON is considered to be a valued "technology partner" by car manufacturers such as BMW, Chrysler, Daimler-Benz, Ford and Peugeot, as well as systems and components companies like Bosch, Delco, Fiat/Marelli, Nippondenso and Valeo.

The next generation of vehicles will require even more sophisticated semiconductor products that will build upon SGS-THOMSON's expertise in superintegration. The Company is developing superintegrated digital cores for powertrain applications on behalf of a "Big Three" U.S. auto maker. Based on a multi-chip module consisting of an ASIC +2Mbit Flash and a 16-bit microprocessor, these cores add other technologies such as EEPROMs, discretes and multifunction drivers to perform engine management and transmission management tasks. Additional SGS-THOMSON products should be in demand as car manufacturers incorporate more advanced navigational, communications and entertainment systems.

AUTOMOTIVE APPLICATIONS

THE NEXT GENERATION OF VEHICLES WILL REQUIRE SOPHISTICATED SEMICONDUCTOR PRODUCTS, BUILDING ON THE COMPANY'S SUPERINTEGRATION EXPERTISE.

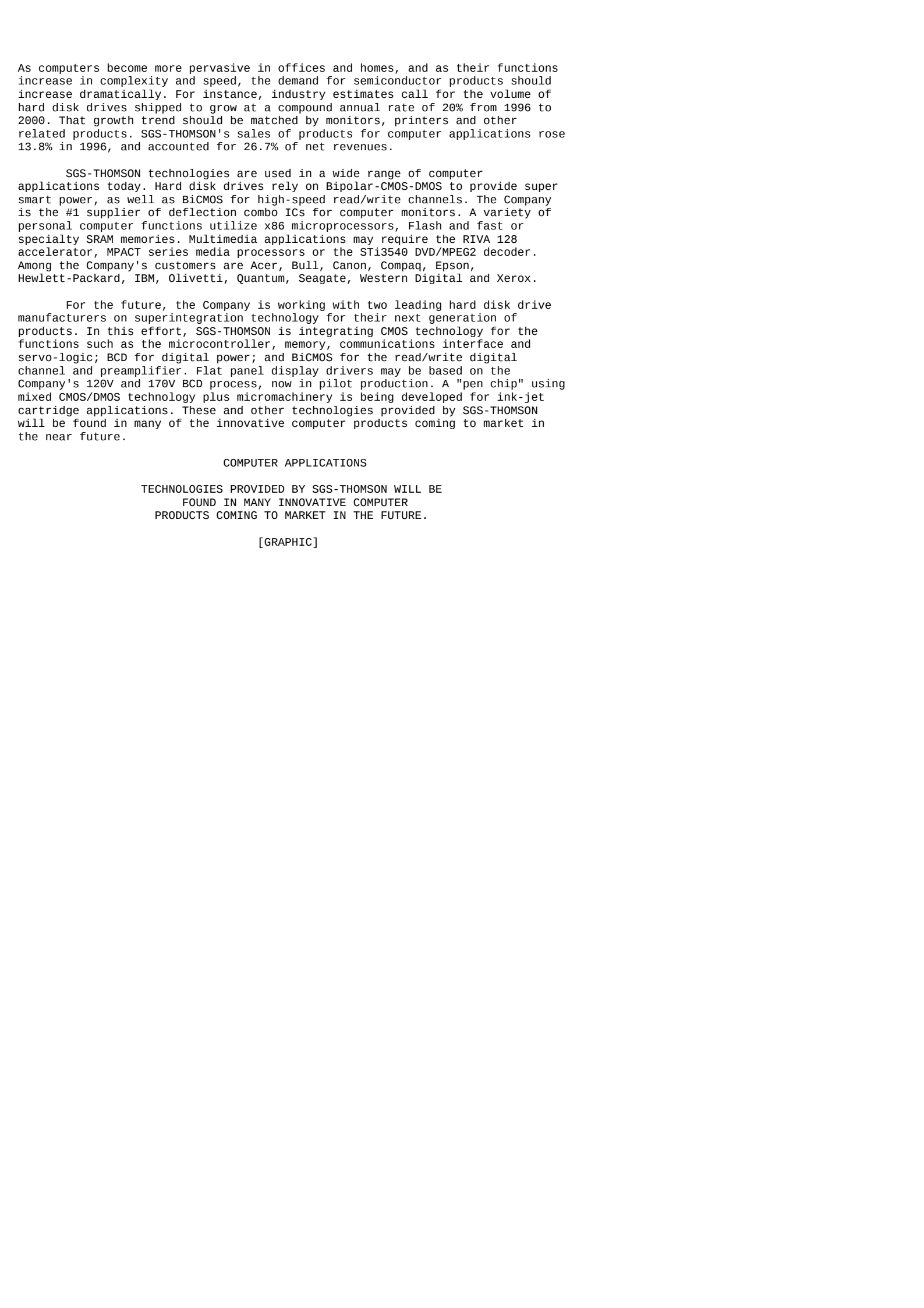
As computers become more pervasive in offices and homes, and as their functions increase in complexity and speed, the demand for semiconductor products should increase dramatically. For instance, industry estimates call for the volume of hard disk drives shipped to grow at a compound annual rate of 20% from 1996 to 2000. That growth trend should be matched by monitors, printers and other related products. SGS-THOMSON's sales of products for computer applications rose 13.8% in 1996, and accounted for 26.7% of net revenues.

SGS-THOMSON technologies are used in a wide range of computer applications today. Hard disk drives rely on Bipolar-CMOS-DMOS to provide super smart power, as well as BiCMOS for high-speed read/write channels. The Company is the #1 supplier of deflection combo ICs for computer monitors. A variety of personal computer functions utilize x86 microprocessors, Flash and fast or specialty SRAM memories. Multimedia applications may require the RIVA 128 accelerator, MPACT series media processors or the STi3540 DVD/MPEG2 decoder. Among the Company's customers are Acer, Bull, Canon, Compaq, Epson, Hewlett-Packard, IBM, Olivetti, Quantum, Seagate, Western Digital and Xerox.

For the future, the Company is working with two leading hard disk drive manufacturers on superintegration technology for their next generation of products. In this effort, SGS-THOMSON is integrating CMOS technology for the functions such as the microcontroller, memory, communications interface and servo-logic; BCD for digital power; and BiCMOS for the read/write digital channel and preamplifier. Flat panel display drivers may be based on the Company's 120V and 170V BCD process, now in pilot production. A "pen chip" using mixed CMOS/DMOS technology plus micromachinery is being developed for ink-jet cartridge applications. These and other technologies provided by SGS-THOMSON will be found in many of the innovative computer products coming to market in the near future.

COMPUTER APPLICATIONS

TECHNOLOGIES PROVIDED BY SGS-THOMSON WILL BE FOUND IN MANY INNOVATIVE COMPUTER PRODUCTS COMING TO MARKET IN THE FUTURE.



[GRAPHIC]

The market for semiconductor products in telecommunications is expected to continue to expand rapidly, with an estimated 20% compound annual growth rate projected for 1996-2000, according to industry sources. An even more pronounced growth rate of 39% over the same period is estimated for the mobile communication segment. As one of the largest suppliers of integrated circuits to the worldwide cellular and Personal Communication Services (PCS) markets, this expected growth should benefit SGS-THOMSON in the years ahead.

In 1996, the Company's sales to the telecommunications market increased 14%, and contributed 22.1% of net revenues. SGS-THOMSON products are found in many diverse telecom applications. In the wireless segment, the Company produces ASICS and memories in high volumes for various cellular systems (GSM, DCS, US-TDMA), as well as for pagers. Telephone sets, answering machines, faxes and advanced terminals depend on the Company's products. Networks and central office installations utilize line card chipsets (analog and ISDN) as well as protocol controllers (HDLC, X25, Frame Relay) from the Company. SGS-THOMSON is present as well in the emerging Asynchronous Transfer Mode (ATM) market. Significant customers include leading producers of mobile and fixed terminals, digital switches, modems and audioprocessing equipment, such as Alcatel, Motorola, Nokia, Northern Telecom, PC-Tel, Racal and Siemens.

As with the Company's other industry applications, the telecom segment is migrating to superintegration solutions. For instance, the next generation of digital cellular phone can use a SGS-THOMSON "system-on-a-chip" approach using no more than four chips (radio, digital signal processing and protocol, memories, energy management).

TELECOMMUNICATIONS APPLICATIONS

THE MARKET FOR SEMICONDUCTOR PRODUCTS IS EXPECTED TO CONTINUE EXPANDING RAPIDLY, WHICH SHOULD BENEFIT SGS-THOMSON IN THE YEARS AHEAD.

Semiconductors made by SGS-THOMSON are found in consumer products worldwide, and the Company enjoys relationships with leading customers in every region, including: General Instrument, Goldstar, Kenwood, Matsushita, Philips, Pioneer, Samsung, Sanyo, Sharp, Sony and Thomson Multimedia. In the past year, sales to the consumer segment increased 26.4%, and provided 22.1% of the Company's net revenues.

Many of the recent innovations in consumer products should greatly increase the need for SGS-THOMSON's technologies. Overall, industry analysts expect the market for semiconductors in digital consumer products (excluding video games) will grow at a compound annual rate of 28% from 1996 through the end of this decade. Two consumer applications with particularly promising growth characteristics are digital set-top boxes and digital video disk (DVD) players.

A look at the Company's product offerings for set-top boxes and DVD players provides a clear indication of SGS-THOMSON's important role in these growing areas. Its ST20 microcontroller core, which is needed for links to satellite services and conventional cable services, is used or has been designed-in by major set-top box manufacturers.

The MPEG2 audio/video decoder, in which the Company is the worldwide market leader, is also a key element for set-top boxes, as is its PAL/NTSC encoder and front end chip set. Through superintegration, many of these features are available on a single chip of the "Omega" family, the STi55xx, for both set-top box and DVD applications.

CONSUMER APPLICATIONS

THE COMPANY PRODUCT OFFERINGS FOR SET-TOP BOXES AND DVD PLAYERS CLEARLY INDICATE SGS-THOMSON'S KEY ROLE IN THESE GROWING AREAS.

[GRAPHIC]

[GRAPHIC]

Sales of SGS-THOMSON products for industrial applications increased 8.8% during the past year, and represented 19.6% of net revenues. While specialized applications such as robotics, control systems, automation systems and power supply equipment make extensive use of the Company's semiconductor products, even everyday items like lighting products, home appliances and battery chargers may incorporate SGS-THOMSON technology. Among the Company's major industrial customers are Siemens, Philips, Schneider, Emerson and Schlumberger.

The production of semiconductors for smart cards continues to be one of the Company's most significant growth opportunities. The powerful microchips embedded in smart cards allow the devices to store financial and medical information, activate telecommunications and video-on-demand equipment, and perform many other functions. SGS-THOMSON has been the leader in smart card chips since the inception of this technology, primarily as a result of its strong lead in non-volatile memory technology and sophisticated security functions. In fact, the Company was the first semiconductor company to receive security certifications for such applications as banking and pay-TV.

Industry analysts estimate that 3.5 billion smart card units will be produced in the year 2000, and that the value of the semiconductor content in the segment will reach approximately $3 billion. This growth trend is being driven by three factors. The number of applications is increasing, moving from the original telephone payment uses to include health care information, Internet payment and electronic purses. At the same time, the semiconductor content of the cards is growing, from EEPROMs to 8-bit microcontrollers to 32-bit microcontrollers. Finally, the regional acceptance of smart card technology has spread from the initial base in Europe to the Asia/Pacific and North America.

INDUSTRIAL APPLICATIONS

SPECIALIZED APPLICATIONS SUCH AS ROBOTICS, AND EVERYDAY ITEMS LIKE LIGHTING PRODUCTS, RELY ON SGS-THOMSON TECHNOLOGY.

With 12 main front-end and five back-end manufacturing sites in Europe, Asia and North America, SGS-THOMSON has delivered on its commitment to locate its facilities in close proximity to customers. The goal, wherever possible, is to have an integrated presence in each major macroeconomic system. In 1996, the Company continued to expand the capacity of its worldwide manufacturing machine, making capital expenditures totalling $1.12 billion. Highlights of the year included the allocation of additional capacity in Agrate, Italy, for Flash device production; the start-up of activity at a new 8-inch fab in Catania, Italy; and the announcement of plans for an advanced 8-inch submicron wafer diffusion plant in Singapore.

In addition to the global reach of its manufacturing resources, the Company is recognized by customers for its dedication to high efficiency manufacturing; its fast production ramp-up on new technologies; and its philosophy of double sourcing, so that there are always at least two fabs qualified for each major process. SGS-THOMSON also has placed a strong emphasis on meeting the needs of customers for larger diameter silicon wafers and smaller die sizes. By the year 2000, the Company expects to have seven 8-inch fabs in operation, and front-end modules capable of manufacturing chips with dimensions of 0.5 microns or less.

An important element of SGS-THOMSON's manufacturing operations is its dedication to quality. An Executive Total Quality Council, created in 1991, fosters quality at all levels, both in manufacturing and in all other aspects of the Company. The "TQM" program is built on five key principles: management commitment to drive, support and monitor the effort; employee empowerment through training, teamwork and recognition; fact-based decision making supported by statistical tools; continuous improvement through systematic measurement and increasingly higher standards; and a customer focus to embed the customer's quality standards in all phases of production.

MANUFACTURING OPERATIONS

THE COMPANY IS RECOGNIZED FOR THE GLOBAL REACH,
HIGH EFFICIENCY AND FAST PRODUCTION RAMP-UP
OF ITS MANUFACTURING RESOURCES.

[PHOTO]
AGRATE, ITALY

[PHOTO]
CASTELLETTO, ITALY

[PHOTO]
CATANIA, ITALY

[PHOTO]
RANCHO BERNARDO,
CA, USA

[PHOTO]
PHOENIX, AZ, USA

[PHOTO]
CARROLLTON, TX, USA

[PHOTO]
CROLLES, FRANCE

[PHOTO]
GRENOBLE, FRANCE

[PHOTO]
RENNES, FRANCE

[PHOTO]
TOURS, FRANCE

[PHOTO]
ROUSSET, FRANCE

[PHOTO]
AIN SEBAA, MOROCCO

[PHOTO]
BOUSKOURA, MOROCCO

[PHOTO]
KIRKOP, MALTA

MANUFACTURING

[PHOTO]
TOA PAYOH, SINGAPORE

[PHOTO]
SHENZHEN, CHINA

[PHOTO]
ANG MO KIO,
SINGAPORE

[PHOTO]
MUAR, MALAYSIA

[GRAPHIC]

MANUFACTURING FACILITIES

FRONT-END: / CROLLES, FRANCE / AGRATE, ITALY / ROUSSET, FRANCE / CATANIA, ITALY
/ RENNES, FRANCE / GRENOBLE, FRANCE / CASTELLETTO, ITALY
/ TOURS, FRANCE / ANG MO KIO, SINGAPORE / CARROLLTON, TX, USA
/ PHOENIX, AZ, USA / RANCHO BERNARDO, CA, USA

BACK-END: / MUAR, MALAYSIA / KIRKOP, MALTA / TOA PAYOH, SINGAPORE
/ AIN SEBAA, MOROCCO / BOUSKOURA, MOROCCO / SHENZHEN, CHINA

OPERATIONS
[GRAPHIC]

TECHNOLOGY
ROAD-MAP

PROTOTYPING/START	96/97	98/99	2000+
High performance logic	0.35/0.25u 5-6 ML	0.18u 6-7 ML	0.12u 8+ ML
BiCMOS digital/analog	0.5/0.35u 3-5 ML	0.25u 5-6 ML	0.18u 6-7 ML
BCD (Bipolar/CMOS/DMOS)	0.6/0.5u 3 ML	0.35u 3-5 ML	--
Programmable Logic*	0.6/0.5u 3 ML 8/16M	0.35/0.25u 5-6 ML 32/64M	0.18u 6-7 ML 256M
Flash Memories	0.4u 3V	0.35/0.25u 2.5/1.8V	0.18u 0.9V

*N.V. Memory capability

The SGS-THOMSON research and development effort is characterized by its proficiency in a wide range of advanced technologies; a concurrent engineering approach that can hasten time to market; the effective use of pilot lines for prototyping and faster ramp-up; and constructive cooperation with customers, suppliers, other semiconductor makers and laboratories. The strength of the Company's R&D effort has been a major contributor to its leadership in a host of technologies, including: CMOS logic, Flash memories, analog, BiCMOS and BCD for smart power applications.

In 1996, R&D expenditures totaled $532.3 million, representing 12.9% of net revenues, and were carried out by approximately 2500 employees at nine advanced research and development centers. Important technology milestones during the year included the first wafers using the 0.25 micron CMOS process, a variety of products and development programs for DVD applications, and a new generation of power MOSFET transistors.

Another distinguishing feature of the Company's technology is its expertise in superintegration -- the ability to create an entire "system-on-a-chip" to replace functions originally performed by an electronic system. In a typical superintegration example, a single chip might contain several diverse logic blocks, including a powerful microcontroller core, as well as embedded memories, such as SRAM, DRAM, Flash or ROM. It also would incorporate an interface to the surrounding electronic system, involving analog or power devices, and embedded micro-coded software for easier programming. SGS-THOMSON has become a leader in superintegration because, unlike many competitors who offer only logic or memory technologies, its technology platform is versatile. This permits the concurrent development of logic, volatile or non-volatile memory, linear and other essential components of the system-on-a-chip, including power devices. Additionally, its pilot line production and strong manufacturing capacity provide the "head start" that can result in rapid time to market. The Company is developing superintegration solutions for many of its customer applications, and the system-on-a-chip concept is expected to be a major driver of future growth.

RESEARCH and DEVELOPMENT

Strategic alliances with key customers, suppliers, research institutions and other parties in the semiconductor marketplace play a vital role in SGS-THOMSON's continued technological and market leadership. Such alliances allow the Company to blend its expertise in semiconductor production with the intimate knowledge of systems and product features contributed by its strategic partners. The alliances may result in joint product development, the definition of a common system architecture, and joint R&D or technology exchanges.

Alliances have been formed with customers in every main industry served by SGS-THOMSON. Seagate Technology and Western Digital are among the Company's partners in the computer peripheral sector. Automotive alliances include Fiat/Marelli. In telecommunications, strategic allies include Alcatel and Northern Telecom, while Thomson Multimedia is a long-term partner in the consumer market. In addition, there are a number of other strategic alliances with customers that for confidentiality reasons cannot be mentioned here.

The Company also has established joint development programs with leading suppliers such as Applied Materials, ASM Lithography, LAM and Air Liquide, and with makers of CAD tools including Cadence, Synopsis and Mentor. It is a participant in Sematech-I300I for the development of 300 millimeter wafer manufacturing processes. SGS-THOMSON is active in joint European research efforts, such as the new MEDEA program (successor to JESSI), and also cooperates with major research insti- tutes and universities. In 1996, SGS-THOMSON derived nearly $1.3 billion in revenues from products that resulted from strategic alliances -- a figure that has grown at a compound annual rate of 48% since 1992. Clearly, the Company's strategic alliances are a source of exceptional financial stability and growth opportunity.

STRATEGIC ALLIANCES

THE COMPANY'S STRATEGIC ALLIANCES ARE A SOURCE OF EXCEPTIONAL FINANCIAL STABILITY AND GROWTH OPPORTUNITY.

FINANCIAL CONTENTS

SELECTED CONSOLIDATED FINANCIAL DATA SGS-THOMSON Microelectronics N.V.

The table below sets forth selected consolidated financial data for the Company for each of the years in the five-year period ended December 31, 1996. Such data have been derived from the consolidated financial statements of the Company. Consolidated financial statements for the three-year period ended December 31, 1996, are included elsewhere in this annual report.

The following information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and the related notes thereto included elsewhere in this annual report.

	Twelve months ended December 31,				
(In millions except per share data)	1992	1993)(1)	1994)(1)	1995)(1)	1996
Consolidated Statement of Income Data:					
Net sales	$ 1,550.6	$ 2,007.7	$ 2,602.2	$ 3,520.7	$ 4,078.3
Other revenues	17.5	29.8	42.7	33.7	44.1
Net revenues	1,568.1	2,037.5	2,644.9	3,554.4	4,122.4
Cost of sales(2)	(1,051.6)	(1,248.4)	(1,528.7)	(2,096.0)	(2,414.7)
Gross profit(2)	516.5	789.1	1,116.2	1,458.4	1,707.7
Operating expenses:					
Selling, general and administrative	(270.0)	(302.5)	(339.9)	(413.2)	(421.1)
Research and development(3)	(260.9)	(270.9)	(338.3)	(440.3)	(532.3)
Restructuring costs	(38.9)	(49.9)	(37.0)	(13.0)	0.0
Other income and expenses(3)	105.1	49.7	32.0	59.1	45.1
Total operating expenses	(464.7)	(573.6)	(683.2)	(807.4)	(908.3)
Operating income(4)	51.8	215.5	433.0	651.0	799.4
Net interest expenses	(65.2)	(37.8)	(21.0)	(16.8)	(11.2)
Gain on disposal of investment	18.7	0.0	0.0	0.0	7.3
Income before income taxes and minority interests	5.3	177.7	412.0	634.2	795.5
Income tax expense	(2.3)	(17.6)	(49.5)	(108.3)	(171.6)
Income before minority interests	3.0	160.1	362.5	525.9	623.9
Minority interests(5)	0.0	0.0	0.0	0.6	1.6
Net income(6)	$ 3.0	$ 160.1	$ 362.5	$ 526.5	$ 625.5
Earnings per share(7)	$ 0.06	$ 1.92	$ 3.04	$ 4.03	$ 4.50
Number of weighted average shares used in calculating earnings per share	53.6	83.5	119.4	130.6	138.7
Consolidated Balance Sheet Data (end of period):					
Cash, cash equivalents and marketable securities	$ 99.5	$ 327.4	$ 461.5	$ 758.4	$ 556.4
Working capital	467.7	390.0	291.1	417.4	611.8
Total assets	1,842.3	2,240.9	3,224.7	4,486.0	5,005.5
Short-term debt (including current portion of long-term debt)	360.6	231.1	322.5	492.8	428.2
Long-term debt (excluding current portion)(1)	547.6	374.8	277.2	200.7	194.9
Shareholders' equity(1)	412.9	1,004.0	1,680.0	2,661.7	3,260.0
Consolidated Operating Data:					
Capital expenditures(8)	$ 196.0	$ 445.9	$ 779.7	$ 1,001.9	$ 1,125.2
Net cash from operating activities	198.7	460.9	728.1	825.1	980.7
Depreciation and amortization(8)	209.8	229.4	288.0	392.4	535.9

(1) In October 1995, the Company completed a second public offering with net proceeds to the Company of approximately $371.6 million. In December 1994, the Company completed an Initial Public Offering with net proceeds to the Company of approximately $198.7 million. In 1993, the Company received a $500 million capital contribution that was effected in two steps, $250 million in May and $250 million in September. The Company also received a $100 million capital contribution in each of 1988, 1989 and 1991.

(2) Cost of sales is net of certain third-party funding for industrialization costs (which include certain costs incurred to bring prototype products to the production stage) included therein. See Note 19 to the Consolidated Financial Statements. For a discussion of certain significant charges reflected in cost of sales in 1994, 1995 and 1996, see "Management's Discussion and Analysis of Financial Condition and Results of Operations--Results of Operations."

(3) Other income and expenses include, among other things, third-party funding for research and development, the expenses for which are reflected in research and development expenses, as well as foreign currency gains and losses, fab start-up costs, patent license payments received and patent costs incurred. The Company's reported research and development expenses do not include design center, process engineering, pre-production or industrialization costs.

(4) The Company has changed the title of this line item from "operating profit." The make-up of this line item has not changed.

(5) In 1994, the Company created a joint venture with a subsidiary of the Shenzhen Electronics Group ("SEG"). The Company owns a 60% interest in the joint venture, with a subsidiary of SEG owning the remaining 40%.

(6) The Company has changed the title of this line item from "net earnings." The make-up of this line item has not changed.

(7) Earnings per share amounts have been restated to reflect a 40:1 stock split effected in connection with the Initial Public Offering.

(8) Capital expenditures are net of certain third-party funding, the effect of which is to decrease depreciation.

OVERVIEW

The Company was formed in 1987 as a result of the combination of the non-military business of Thomson Semiconducteurs, the microelectronics business of the French state-controlled defense electronics company Thomson-CSF, and SGS Microelettronica, the microelectronics business owned by STET, the Italian state-controlled telecommunications company. Since its formation, the Company has significantly broadened and upgraded its range of products and technologies and has strengthened its manufacturing and distribution capabilities in Europe, North America and the Asia Pacific region, while at the same time restructuring its operations to improve efficiency.

From 1992 to 1996, the Company's net revenues increased from $1,568.1 million to $4,122.4 million, with the Company experiencing strong revenue growth during each year in this period. Such revenue gains were achieved despite the Company's absence during that period from the market for DRAMs (a commodity memory product) and, until the second half of 1994, from the market for personal computer microprocessors (such as the x86 family of products). According to trade association data, the TAM (total available market) increased from $59.9 billion in 1992 to a preliminary estimate of $132.0 billion in 1996, while the SAM (which prior to 1995 consisted of the TAM without DRAMs, microprocessors and opto-electronic products and commencing in 1995 and for all prior periods compared therewith includes microprocessors as a result of the Company's production of x86 products) increased from $49.0 billion in 1992 to a preliminary estimate of $102.7 billion in 1996. The Company's share of the TAM increased from 2.6% to 3.1% during this period, while the Company's share of the SAM increased from 3.2% to 4.0%. Revenue growth within the Company from 1992 through 1996 was particularly significant for dedicated products, EPROMs and semicustom devices. The Company has also succeeded in becoming a more global semiconductor supplier--the proportion of the Company's revenues derived outside Europe increased from approximately 46% in 1992 to approximately 56% in 1996.

Differentiated ICs (which the Company defines as being its dedicated products, semicustom devices and microcontrollers) accounted for approximately 59% of the Company's net revenues in 1996, compared to just over 51% in 1995. Such products foster close relationships with customers, resulting in early knowledge of their evolving requirements and opportunities to access their markets for other products, and are less vulnerable to competitive pressures than standard commodity products. In 1996, analog ICs (including mixed signal ICs), the majority of which are also differentiated ICs, accounted for approximately 46% of the Company's net revenues (no change from 1995), while discrete devices accounted for approximately 14% of the Company's net revenues (compared to approximately 17% in 1995). Over the last three years, these families of products, in particular analog ICs, have experienced less volatility in sales growth rates and average selling prices than the overall semiconductor industry.

In addition to increasing revenues, management's efforts to rationalize operations and increase manufacturing and other efficiencies have generated significant improvements in profitability. The Company's gross profit margin increased from 32.9% in 1992 to 41.4% in 1996. Benefiting from a favorable industry environment in 1993, 1994 and 1995, such increases in gross profit margins have combined with significant reductions in selling, general and administrative expenses as a percentage of net revenues and reduced interest costs to significantly increase profitability. In 1996, the gross profit margin was 41.4% compared to 41.0% in 1995. The stable gross profit margin in 1996 compared to 1995 was realized within an unfavorable industry environment (which resulted in tough pricing pressures), due primarily to a more favorable product mix and improved manufacturing productivity.

Historically, cyclical changes in production capacity in the semiconductor industry and demand for electronic systems have resulted in pronounced cyclical changes in the level of semiconductor sales and fluctuations in prices and margins for semiconductor products from time to time. However, certain significant changes in the industry could contribute to continued growth over the long term notwithstanding cyclical variations from period to period. Such changes include the development of new semiconductor applications, increased semiconductor content as a percentage of total system cost, emerging strategic partnerships and growth in the electronic systems industry in the Asia Pacific region.

The Company is entering 1997 in a healthy financial condition. It is, however, evident that the industry has started a correction from the extraordinary growth of recent years. According to preliminary estimated trade association data, in 1996 TAM revenues decreased approximately 9% over 1995 while SAM revenues increased approximately 3%. The Company cannot anticipate how deep or how long this correction phase will be. The Company is confident, however, that its heavy emphasis on differentiated products in its portfolio, its strong customer base and strategic alliances, its well diversified sales base, both in terms of applications and geography, recent contracts with key customers and new design wins in such high growth areas as hard disk drives, set top boxes and

digital cellular phones should allow the Company to continue to outperform the industry average in 1997. Based on currently available information, the Company believes that the second, third and fourth quarters of 1997 will show progressive improvement compared to the first quarter of 1997.

Some of the above statements contained in this "Overview" are forward looking statements that involve a number of risks and uncertainties. In addition to the factors discussed above, among the other factors that could cause actual results to differ materially are the following: the cyclicality of the semiconductor and electronic systems industries; capital requirements and the availability of funding; competition; new product development and technological change; manufacturing risks; order cancellations or reduced bookings by key customers or distributors; intellectual property developments, international events, currency fluctuations; problems in obtaining adequate raw materials on a timely basis; and the loss of key personnel. Unfavorable changes in the above or other factors discussed under "Risk Factors" listed from time to time in the Company's SEC reports, including in the Prospectus dated October 18, 1995 (pages 9 through 16), could materially affect the Company.

The table below sets forth information on the Company's net revenues by product group and by geographic region.

	Twelve months ended December 31,				
(In millions)	1992	1993	1994	1995	1996
Net Revenues by Product Group:					
Dedicated Products(1)	$ 562.6	$ 724.1	$ 987.7	$ 1,359.7	$1,757.7
Discrete and Standard ICs(2)	432.3	514.6	636.3	838.0	784.1
Memory Products(1)	279.2	440.0	560.7	653.3	736.8
Programmable Products	259.9	320.4	381.4	535.3	720.5
Others(3)	34.1	38.4	78.8	168.1	123.3
Total	$1,568.1	$2,037.5	$2,644.9	$3,554.4	$4,122.4
Net Revenues by Geographic Region:(4)					
Europe	$ 839.7	$ 976.0	$1,219.1	$1,627.5	$1,824.4
Americas(5)	350.5	495.5	673.5	846.4	934.1
Asia Pacific	328.7	463.2	617.6	925.1	1,135.7
Japan	49.2	102.8	134.7	155.4	228.2
Total	$1,568.1	$2,037.5	$2,644.9	$3,554.4	$4,122.4

(1) 1996 revenues for the Dedicated Products Group include $5.6 million of revenues from certain foundry activities which were moved from the Memory Products Group in January 1996. Revenues for the Dedicated Products Group and the Memory Products Group have been restated for prior periods to reflect this change.

(2) Includes revenues from sales of RF products, which were moved to the Discrete and Standard ICs product group in May 1994. Revenues for the Discrete and Standard ICs group have been restated for prior years to include RF product revenues.

(3) Includes revenues from sales of subsystems and other products and from the New Ventures Group, which was created in May 1994 to act as a focal point for the Company's new business opportunities.

(4) Revenues are classified by location of customer invoiced. For example, products ordered by U.S.-based companies to be invoiced to Asia Pacific affiliates are classified as Asia Pacific revenues.

(5) Substantially all of the revenues derived from the Americas are derived from the United States.

The following table sets forth certain financial data from the Company's consolidated statements of income since 1992, expressed in each case as a percentage of net revenues:

	Twelve months ended December 31,				
	1992	1993	1994	1995	1996
Net sales	98.9%	98.5%	98.4%	99.1%	98.9%
Other revenues	1.1	1.5	1.6	0.9	1.1
Net revenues	100.0	100.0	100.0	100.0	100.0
Cost of sales	(67.1)	(61.3)	(57.8)	(59.0)	(58.6)
Gross profit	32.9	38.7	42.2	41.0	41.4
Operating expenses:					
Selling, general and administrative	(17.2)	(14.8)	(12.9)	(11.6)	(10.2)
Research and development	(16.6)	(13.3)	(12.8)	(12.4)	(12.9)
Restructuring costs	(2.5)	(2.4)	(1.4)	(0.4)	0.0
Other income and expenses	6.7	2.4	1.2	1.7	1.1
Total operating expenses	(29.6)	(28.2)	(25.8)	(22.7)	(22.0)
Operating income	3.3	10.6	16.4	18.3	19.4
Net interest expenses	(4.2)	(1.9)	(0.8)	(0.5)	(0.3)
Gain on disposal of investment	1.2	0.0	0.0	0.0	0.2
Income before income taxes and minority interests	0.3	8.7	15.6	17.8	19.3
Income tax expense	(0.1)	(0.9)	(1.9)	(3.0)	(4.2)
Income before minority interests	0.2	7.9	13.7	14.8	15.1
Minority interests	0.0	0.0	0.0	0.0	0.1
Net income	0.2%	7.9%	13.7%	14.8%	15.2%

1996 versus 1995

The growth that the worldwide semiconductor market experienced in 1994 and 1995 did not materialize in 1996; total industry sales declined in 1996 compared to 1995. See "Overview." In the fourth quarter of 1996, however, the market increased slightly over the previous quarter after three straight quarters of decline. The Company experienced strong increases in operating income and net income in 1996, driven by significant growth in net revenues and improvements in manufacturing productivity. These increases were achieved in spite of the fact that the Company's average product selling prices in 1996 declined compared to 1995.

/Net Revenues. Net sales increased 15.8%, from $3,520.7 million in 1995 to $4,078.3 million in 1996. The increase in net sales of $557.6 million was primarily a result of an improved product mix, including sales of new products, in each of the Company's principal product groups. The exchange rate impact on net sales in 1996 was not significant. See "Impact of Changes in Exchange Rates." Other revenues (consisting primarily of co-development contract fees, certain contract indemnity payments and patent royalty income) increased from $33.7 million in 1995 to $44.1 million in 1996, primarily due to an increase in licensing fees and co-development fees, partly offset by a decrease in patent and royalty income. As a result net revenues increased 16.0%, from $3,554.4 million in 1995 to $4,122.4 million in 1996.

The Dedicated Products Group's net revenues increased 29.3% primarily as a result of an improved mix in computer, video/image processing and telecommunications products. In addition, 1996 revenues for the Dedicated Products Group include $5.6 million of revenues from certain foundry activities which were moved from the Memory Products Group in January 1996. Revenues for the Dedicated Products Group and the Memory Products Group have been restated for prior periods in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" to reflect this change. Higher volumes in computer, audio, automotive and telecommunication products also contributed to the increase in net revenues. The Discrete and Standard ICs Group's net revenues declined 6.4% as volume increases in transistors and an improved mix in discrete devices were not sufficient to offset declining volumes in discrete devices, standard commodities and standard logic devices. Net revenues of the Memory Products Group increased 12.8% due to higher volumes in smartcard ICs (primarily used in European telephone and bank cards) and an improved mix in EPROMs. Increased volume and an improved product mix in flash memories and EEPROMs also contributed to the increase in net revenues. The Programmable Products Group's net revenues increased 34.6% principally due to higher volumes and an improved product mix in analog arrays and microcontroller products.

In 1996 compared to 1995, the Company's net revenues increased 46.8% in Japan, 22.8% in the Asia Pacific region, 12.1% in Europe and 10.4% in the Americas.

The Company's net revenues increased in 1996 compared to 1995 despite the difficult conditions that the semiconductor industry experienced in 1996.

/Gross profit. The Company's gross profit increased 17.1%, from $1,458.4 million in 1995 to $1,707.7 million in 1996, primarily as a result of an improved product mix, higher other revenues and improvements in manufacturing performances. As a percentage of net revenues gross profit was 41.0% in 1995 and 41.4% in 1996.

Cost of sales increased from $2,096.0 million in 1995 to $2,414.7 million in 1996, due primarily to higher depreciation resulting from increased capital spending in recent periods and to higher variable costs associated with increased volume. Increased cost of sales were also attributable to the new plant in Phoenix, Arizona whose costs were not included in cost of sales until the third quarter of 1995 and to upgrades of manufacturing facilities in 1996.

The exchange rate impact on gross profit in 1996 was not significant. See "Impact of Changes in Exchange Rates." Cost of sales in 1996 and 1995 was net of $4.6 million and $11.8 million, respectively, of funds received to offset industrialization costs (which include certain costs incurred to bring prototype products to the production stage) included in cost of sales.

/Selling, general and administrative expenses. Selling, general and administrative expenses increased slightly, from $413.2 million in 1995 to $421.1 million in 1996. This increase was due primarily to increases in general and administrative activities and to a strengthening in the Company's marketing efforts. The 1995 period included a $10 million provision related to specific charges to cover the possible financial impact related to legal proceedings in one of the Company's subsidiaries. As a percentage of net revenues, selling, general and administrative expenses decreased from 11.6% in 1995 to 10.2% in 1996, due primarily to higher net revenues.

/Research and development expenses. Research and development expenses continued to represent a substantial amount of the Company's net revenues, increasing 20.9%, from $440.3 million in 1995 to $532.3 million in 1996. Despite the growth in net revenues in 1996, research and development expenses as a percentage of net revenues increased from 12.4% in 1995 to 12.9% in 1996. The Company continued to invest heavily in both its research and development staff and research and development activities. The Company's reported research and development expenses do not include design center, process engineering, pre-production or industrialization costs.

/Restructuring costs. There were no restructuring costs in 1996. The $13.0 million in restructuring costs in 1995 included costs associated with certain personnel lay-offs.

/Other income and expenses. Other income and expenses decreased from income of $59.1 million in 1995 to income of $45.1 million in 1996. Other income and expenses include primarily funds received from government agencies in connection with the Company's research and development programs, the cost of new plant start-ups, as well as foreign currency gains and losses, patent license payments, the costs of certain activities relating to intellectual property and miscellaneous revenues and expenses. The decrease in other income and expenses resulted primarily from a decrease in funds received from government agencies in connection with the Company's research and development programs and higher start-up costs, partly offset by foreign currency gains.

/Operating income. The Company's operating income increased 22.8%, from $651.0 million in 1995 to $799.4 million in 1996, primarily as a result of increased net revenues and improved efficiency in manufacturing. The exchange rate impact on operating income was marginal.

/Net interest expenses. Net interest expenses decreased from $16.8 million in 1995 to $11.2 million in 1996, primarily as a result of a capital increase undertaken by the Company in October 1995, which allowed the Company to repay a substantial majority of its outstanding debt.

/Gain on disposal of investment. In 1996, the Company recorded a one-time gain of $7.3 million from the sale of a distribution subsidiary in France.

/Income tax expense. Provision for income tax was $171.6 million in 1996 compared to $108.3 million in 1995, primarily as a result of the substantial increase in income before tax. The accrued effective tax rate increased from approximately 17% in 1995 to approximately 22% in 1996, since certain favorable tax benefits on capital investments were no longer available in certain countries in 1996 compared to 1995. These favorable rates were due to tax benefits available in certain countries. As such benefits may not be available in future periods, the Company could register an increase in the effective tax rate in the coming years.

1995 versus 1994

The growth that the worldwide semiconductor market experienced in 1994 continued through 1995 with the markets in Europe, the Americas and the Asia Pacific region all showing strong growth. Market growth in Japan was lower than in the other regions, however, due to general economic conditions. The Company experienced strong increases in revenues, operating income and net income in 1995, caused by significant increases in volume and an improved product mix, including sales of new products. Average selling prices of comparable products were slightly lower in 1995 than in 1994, but due to improved product mix the average price per unit increased.

Net Revenues. Net sales increased 35.3%, from $2,602.2 million in 1994 to $3,520.7 million in 1995. The increase in net sales of $918.5 million was primarily as a result of significantly increased sales volumes in each of the Company's principal product groups except the Memory Products Group, which also experienced a slower growth rate in net sales due to declining EPROM prices. Net sales were also positively impacted by an improved product mix, including sales of new products, and the benefits derived from the weakening U.S. dollar. See "Impact of Changes in Exchange Rates." In 1995, approximately $8.3 million in billings for research and development activity, which were classified as other revenues in 1994, were classified as net sales. Other revenues decreased from $42.7 million in 1994 to $33.7 million in 1995 due primarily to such reclassification. Net revenues increased 34.4%, from $2,644.9 million in 1994 to $3,554.4 million in 1995.

The Dedicated Products Group's net revenues increased 37.7% primarily as a result of significant volume growth in computer products, video/image processing products and audio and automotive products. The Discrete and Standard ICs Group's net revenues increased 31.7%, due principally to sales increases in transistors such as Power MOS and power transistors and discrete devices. Sales of standard commodities such as standard linears and voltage regulators also increased compared to 1994. The Memory Products Group's revenues grew by 16.5% as increased volumes of flash memory products and increased sales of EPROMs and smartcard ICs used in European telephone and bank cards were offset by declining EPROM sales due to lower prices. Net revenues of the Programmable Products Group increased 40.4% principally from growth in sales of microcontroller products and higher sales of digital semicustom products (which benefited from the introduction of advanced submicron product lines). In the second half of 1994, the Company commenced shipments of its own x86 microprocessor product family.

/Gross Profit. The Company's gross profit increased 30.7%, from $1,116.2 million in 1994 to $1,458.4 million in 1995, primarily as a result of significant volume growth in all the Company's principal product groups except the Memory Products Group, which also experienced a slower growth rate in net sales due to declining EPROM prices. As a percentage of net revenues, gross profit decreased from 42.2% in 1994 to 41.0% in 1995, due primarily to costs associated with the conversion of certain manufacturing facilities from the production of 4-inch and 5-inch wafers to production of 5-inch and 6-inch wafers and to a lesser extent due to higher depreciation resulting from increased capital spending.

Cost of sales increased from $1,528.7 million in 1994 to $2,096.0 million in 1995, due primarily to higher variable costs associated with significantly increased volume, the addition of the new fabrication plant in Crolles, France (which has started to reach a significant volume of production) and to certain manufacturing facilities, which were in the process of being upgraded in 1995. Increased cost of sales was also attributable to the new plant in Phoenix, Arizona whose costs were not included in cost of sales until the third quarter of 1995 and higher depreciation resulting from increased capital spending in recent periods.

The exchange rate impact on gross profit in 1995 compared to 1994 was marginally negative, as the negative impact of the depreciation of the U.S. dollar on cost of sales was marginally greater than the positive impact on net revenues. See "Impact of Changes in Exchange Rates." Cost of sales in 1995 and 1994 was net of $11.8 million and $19.3 million, respectively, of funds received from governmental agencies to offset industrialization costs included in cost of sales.

/Selling, general and administrative expenses. Selling, general and administrative expenses increased 21.6%, from $339.9 million in 1994 to $413.2 million in 1995. In 1994, selling, general and administrative expenses included a $15 million provision for potential patent infringements and in 1995 included a $10 million provision related to specific charges to cover the possible financial impact related to legal proceedings in one of the Company's subsidiaries. Excluding these provisions, the increase in selling, general and administrative expenses was primarily due to a strengthening in the Company's marketing efforts and to an increase in general and administrative functions. As a percentage of net revenues, selling, general and administrative expenses decreased from 12.9% in 1994 to 11.6% in 1995, due primarily to higher net revenues.

/Research and development expenses. Research and development expenses continued to represent a substantial amount of the Company's net revenues, increasing 30.2%, from $338.3 million in 1994 to $440.3 million in 1995. Due to the strong growth in net revenues attained in 1995, research and development expenses as a percentage of net revenues decreased slightly from 12.8% in 1994 to 12.4% in 1995. The Company continued to invest heavily in research and development.

/Restructuring costs. Restructuring costs decreased significantly from $37.0 million in 1994 to $13.0 million in 1995. The $13.0 million in restructuring costs in 1995 included costs associated with certain personnel lay-offs. In 1994, restructuring costs included primarily costs associated with the closure of certain older fab facilities and certain personnel lay-offs.

/Other income and expenses. Other income and expenses of the Company increased from income of $32.0 million to income of $59.1 million in 1995. In 1995, other income and expenses included increased contributions to research and development activities and start-up costs. In addition, in 1995 there were several nonrecurring items affecting other income and expenses, which taken together did not have a material impact. These include the reversal of the provision for the restructuring of the Rancho Bernardo plant in connection with the decision to retain and upgrade this facility. In 1994, other income and expenses included a charge for stock option compensation of $18.1 million.

/Operating income. The Company's operating income increased 50.3%, from $433.0 million in 1994 to $651.0 million in 1995, primarily as a result of the reduction of provisions for restructuring costs and an increase in net revenues.

/Net interest expenses. Net interest expenses decreased from $21.0 million in 1994 to $16.8 million in 1995, primarily as a result of the temporary reduction in debt due to application of the proceeds received by the Company in December 1994 from its initial public offering, and in October 1995 from an additional capital increase, which allowed the Company to repay a substantial majority of its outstanding debt.

/Income tax expense. Provision for income tax was $108.3 million in 1995 compared to $49.5 million in 1994, primarily as a result of the substantial increase in income before tax. The accrued effective tax rate increased from 12% in 1994 to 17% in 1995. The still favorable 1995 rate is mainly due to the application of benefits in certain countries associated with new capital expenditure programs.

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth certain financial information for the years 1994, 1995 and 1996. Such information is derived from unaudited consolidated financial statements, prepared on a basis consistent with the audited consolidated financial statements, that include, in the opinion of management, only normal recurring adjustments necessary for a fair presentation of the information set forth therein. Operating results for any quarter are not necessarily indicative of results for any future period. In addition, in view of the significant growth experienced by the Company in recent years as well as the changes in the composition of sales and production among different geographic regions, the Company believes that period-to-period comparisons of its operating results should not be relied upon as an indication of future performance.

(inmillions, except percentages and per share data)	Apr. 2, 1994	July 2, 1994	Oct. 1, 1994	Dec. 31, 1994	Apr. 1, 1995	July 1, 1995	Sept. 30, 1995	Dec.31 1995
Consolidated Statement of Income Data								
Net revenues	$ 599.3	$ 672.4	$ 657.2	$ 716.0	$ 778.6	$ 878.5	$ 922.6	$ 974.7
Cost of sales	(346.8)	(389.4)	(380.5)	(412.0)	(451.8)	(526.9)	(552.3)	(565.1)
Gross profit	252.5	283.0	276.7	304.0	326.8	351.6	370.3	409.6
Operating expenses:								
Selling, general and administrative	(91.3)	(82.1)	(81.5)	(85.0)	(90.7)	(99.8)	(103.6)	(119.0)
Research and development	(72.5)	(82.7)	(83.4)	(99.7)	(97.5)	(105.1)	(109.3)	(128.4)
Restructuring costs	(0.2)	(22.9)	(10.7)	(3.2)	(0.3)	(0.8)	(6.8)	(5.1)
Other income and expenses	13.8	15.3	3.3	(0.4)	3.4	11.8	15.7	28.3
Total operating expenses	(150.2)	(172.4)	(172.3)	(188.3)	(185.1)	(193.9)	(204.0)	(224.2)
Operating income	102.3	110.6	104.4	115.7	141.7	157.7	166.3	185.4
Net interest expenses	(4.8)	(5.6)	(5.6)	(5.0)	(2.9)	(5.1)	(6.7)	(2.1)
Gain on disposal of investment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income before income taxes and minority interests	97.5	105.0	98.8	110.7	138.8	152.6	159.6	183.3
Income tax expense	(18.0)	(18.5)	(11.5)	(1.5)	(31.9)	(30.1)	(30.7)	(15.7)
Income before minority interests	79.5	86.5	87.3	109.2	106.9	122.5	128.9	167.6
Minority interests	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.4
Net income	$ 79.5	$ 86.5	$ 87.3	$ 109.2	$ 106.9	$ 122.6	$ 129.0	$168.0
Earnings per share	$ 0.67	$ 0.73	$ 0.73	$ 0.90	$ 0.83	$ 0.95	$ 1.00	$ 1.24
Number of weighted average shares used in calculating earnings per share	119.0	119.0	119.0	120.6	128.6	128.8	129.1	135.9
As a percentage of net revenues								
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of sales	(57.9)	(57.9)	(57.9)	(57.5)	(58.0)	(60.0)	(59.9)	(58.0)
Gross profit	42.1	42.1	42.1	42.5	42.0	40.0	40.1	42.0
Operating expenses:								
Selling, general and administrative	(15.2)	(12.2)	(12.4)	(11.9)	(11.6)	(11.4)	(11.2)	(12.2)
Research and development	(12.1)	(12.3)	(12.7)	(13.9)	(12.5)	(12.0)	(11.8)	(13.2)
Restructuring costs	0.0	(3.4)	(1.6)	(0.4)	0.0	(0.1)	(0.7)	(0.5)
Other income and expenses	2.3	2.3	0.5	(0.1)	0.4	1.3	1.7	2.9
Total operating expenses	(25.1)	(25.6)	(26.2)	(26.3)	(23.8)	(22.1)	(22.1)	(23.0)
Operating income	17.1	16.4	15.9	16.2	18.2	18.0	18.0	19.0
Net interest expenses	(0.8)	(0.8)	(0.9)	(0.7)	(0.4)	(0.6)	(0.7)	(0.2)
Gain on disposal of investment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income before income taxes and minority interests	16.3	15.6	15.0	15.5	17.8	17.4	17.3	18.8
Income tax expense	(3.0)	(2.8)	(1.7)	(0.2)	(4.1)	(3.4)	(3.3)	(1.6)
Income before minority interests	13.3	12.9	13.3	15.3	13.7	13.9	14.0	17.2
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net income	13.3%	12.9%	13.3%	15.3%	13.7%	14.0%	14.0%	17.2%

	Quarter ended			
(inmillions, except percentages and per share data)	Mar. 30 1996	June 29, 1996	Sept. 28, 1996	Dec. 31, 1996

Consolidated Statement of Income Data				
Net revenues	$1,027.7	$1,047.4	$ 988.4	$1,058.9
Cost of sales	(586.4)	(582.1)	(589.2)	(657.0)
Gross profit	441.3	465.3	399.2	401.9
Operating expenses:				
Selling, general and administrative	(106.1)	(103.1)	(104.0)	(107.9)
Research and development	(121.4)	(136.0)	(134.5)	(140.4)
Restructuring costs	(1.8)	0.3	0.3	1.2
Other income and expenses	8.7	(2.2)	6.4	32.1
Total operating expenses	(220.6)	(241.0)	(231.8)	(215.0)
Operating income	220.7	224.3	167.4	186.9
Net interest expenses	(0.5)	(1.6)	(3.2)	(5.9)
Gain on disposal of investment	7.3	0.0	0.0	0.0
Income before income taxes and minority interests	227.5	222.7	164.2	181.0
Income tax expense	(52.7)	(46.9)	(32.1)	(39.8)
Income before minority interests	174.8	175.8	132.1	141.2
Minority interests	0.2	0.3	0.3	0.8
Net income	$ 175.0	$ 176.1	$ 132.4	$ 142.0
Earnings per share	$ 1.26	$ 1.27	$ 0.95	$ 1.02
Number of weighted average shares used in calculating earnings per share	138.4	138.7	138.8	138.9
As a percentage of net revenues				
Net revenues	100.0%	100.0%	100.0%	100.0%
Cost of sales	(57.1)	(55.6)	(59.6)	(62.0)
Gross profit	42.9	44.4	40.4	38.0
Operating expenses:				
Selling, general and administrative	(10.3)	(9.8)	(10.5)	(10.2)
Research and development	(11.8)	(13.0)	(13.6)	(13.3)
Restructuring costs	(0.2)	0.0	0.0	0.1
Other income and expenses	0.8	(0.2)	0.6	3.0
Total operating expenses	(21.5)	(23.0)	(23.5)	(20.3)
Operating income	21.5	21.4	16.9	17.7
Net interest expenses	0.0	(0.2)	(0.3)	(0.6)
Gain on disposal of investment	0.7	0.0	0.0	0.0
Income before income taxes and minority interests	22.1	21.3	16.6	17.1
Income tax expense	(5.1)	(4.5)	(3.2)	(3.8)
Income before minority interests	17.0	16.8	13.4	13.3
Minority interests	0.0	0.0	0.0	0.1
Net income	17.0%	16.8%	13.4%	13.4%

In 1996, approximately 44% of the Company's net revenues originated in Europe, compared to 54% in 1992. The Company's third quarter revenues in Europe have averaged less than average revenues during other quarters due to production slowdowns by its European customers in July and August. During strong industry conditions, the negative impact of third quarter seasonality in Europe has generally been offset by increased sales in other regions. In weak industry conditions, as was the case in 1996, the growth in other regions generally does not materialize, resulting in a decrease in net revenues in the third quarter. Quarterly results have also been and may be expected to continue to be substantially affected by the cyclicality of the semiconductor and electronic systems industries, the timing and success of new product introductions and the levels of provisions and other unusual charges incurred.

Gross profit as a percentage of net revenues in the second quarter of 1996 increased to 44.4% from 42.9% in the first quarter of 1996. This unusually high gross margin was caused by a very favorable product mix combined with higher utilization of the Company's manufacturing facilities. For the third quarter of 1996, gross profit as a percentage of net revenues declined to 40.4% (39.4%, net of revenue from licensing fees), primarily due to pricing pressures and a reduced loading of production lines as a result of the seasonal slowdown in Europe associated with the third quarter. Gross profit as a percentage of net revenues further declined for the fourth quarter of 1996 to 38.0%. This decline was attributable to a combination of factors, including under-utilization of non-VLSI fabs, the temporary de-saturation of the Phoenix fab due to a change in product mix and continued price pressure, mainly on the commodity portion of the Company's product portfolio.

The Company's quarterly and annual operating results are also affected by a wide variety of other factors that could materially and adversely affect revenues and profitability or lead to significant variability of operating results, including, among others, capital requirements and the availability of funding, competition, new product development and technological change and manufacturing. In addition, a number of other factors could lead to fluctuations in operating results, including order cancellations or reduced bookings by key customers or distributors, intellectual property developments, international events, currency fluctuations, problems in obtaining adequate raw materials on a timely basis, and the loss of key personnel. As only a portion of the Company's expenses varies with its revenues, there can be no assurance that the Company will be able to reduce costs promptly or adequately in relation to revenue declines to compensate for the effect of any such factors. As a result, unfavorable changes in the above or other factors have in the past and may in the future adversely affect the Company's operating results.

The Company believes that inflation has not had a material effect on the results of its operations during the periods presented.

IMPACT OF CHANGES IN EXCHANGE RATES

The Company's results of operations and financial condition can be significantly affected by changes in exchange rates between the U.S. dollar and other currencies, particularly the Italian lira, the French franc, the English pound, the German mark and the Singapore dollar.

Revenues for certain products (primarily dedicated products sold in Europe) that are quoted in currencies other than the U.S. dollar are directly affected by fluctuations in the value of the U.S. dollar. Revenues for all other products, which are quoted in U.S. dollars and translated into local currencies for payment, tend not to be affected significantly by fluctuations in exchange rates except to the extent that there is a lag between changes in currency rates and adjustments in the local currency equivalent price paid for such products.

Certain significant costs incurred by the Company, such as direct labor, selling, general and administrative expenses, and research and development expenses, are incurred in the currencies of jurisdictions where the Company's operations are located. Fluctuations in the value of these currencies, particularly the Italian lira and the French franc, compared to the U.S. dollar can affect the Company's costs and therefore its profitability.

In 1996, the U.S. dollar, on average, appreciated slightly against the principal European (except Italian) and Asian currencies which have a material impact on the Company. The exchange rate impact on results of operations in 1996 was not significant. In 1995, the strong depreciation which the U.S. dollar registered in the first six months of 1995 resulted in a negative impact on results of operations in 1995, because the positive impact on net revenues was more than offset by a negative impact on cost of sales resulting in a net negative impact on gross profit.

The Company's principal strategies to reduce the risks associated with exchange rate fluctuations have been (i) to purchase certain raw materials and equipment in transactions denominated in U.S. dollars (thereby reducing the exchange rate risk for costs relative to revenues, which are principally denominated or determined by reference to the U.S. dollar), and (ii) to manage certain other costs, such as financial costs, to maintain an appropriate balance between U.S. dollars and other currencies based upon the currency environment at the time. Although from time to time the Company purchases or sells currencies forward to hedge currency risk in obligations or receivables, the Company's policy is not to take speculative positions through forward currency contracts. The Company has not experienced significant gains or losses as a result of hedging activities. Its management strategies to reduce exchange rate risks have served to mitigate, but not eliminate, the positive or negative impact of exchange rate fluctuations.

Assets, shareholders' equity and liabilities of non-Dutch subsidiaries are for consolidation purposes translated into U.S. dollars at the year-end exchange rate. See Note 2.4 to the Consolidated Financial Statements. Income and expenses are translated at the average exchange rate for the period. Adjustments resulting from the translation are recorded directly in shareholders' equity, and are shown as "translation adjustment" in the consolidated statements of changes in shareholders' equity. The balance sheet impact of such translation adjustments has been, and may be expected to continue to be, material from period to period.

The Company's outstanding indebtedness is denominated principally in Italian lire, Maltese lira, U.S. dollars, Singapore dollars and French francs. See "Liquidity and Capital Resources" and Note 14 to the Consolidated Financial Statements.

LIQUIDITY AND CAPITAL RESOURCES

The Company's net cash generated from operations totalled $980.7 million in 1996 compared to $825.1 million in 1995 and $728.1 million in 1994.

Significant increased net cash from operations in 1994, 1995 and 1996 coupled with capital increases undertaken by the Company in December 1994 and October 1995, which resulted in net proceeds to the Company of $198.7 million and $371.6 million, respectively, enabled the Company to substantially reduce its indebtedness, finance capital expenditures and improve its balance sheet. The Company's net financial position (cash, cash equivalents and marketable debt securities net of total debt) moved from a positive net financial position of $64.9 million at December 31, 1995 to a negative net financial position of $66.7 million at December 31, 1996, primarily due to the need to finance increased capital expenditures in 1996. At December 31, 1996, cash and cash equivalents was $551.9, compared to $754.0 million at December 31, 1995 and $457.2 million at December 31, 1994. At December 31, 1996, the aggregate amount of the Company's long-term credit facilities was approximately $287 million, all of which was outstanding, and the aggregate amount of the Company's short-term facilities was approximately $975 million, under which approximately $316 million of indebtedness was outstanding. The Company has approximately $112 million of long-term indebtedness that will become due within one year, and expects to fund such debt repayments from available cash. The Company enters into interest rate swap agreements from time to time.

In 1996, the Company's capital expenditure payments totalled $1,125.2 million, compared to $1,001.9 million in 1995 and $779.7 million in 1994. Capital expenditures for 1996 were principally devoted to equip and upgrade both the new 8-inch and existing 6-inch front-end facilities at the Catania, Italy plant, to the expansion of the 8-inch front-end wafer fabrication plant in Crolles, France, to the extension and conversion of an existing 8-inch facility in Agrate, Italy, to the upgrading of the 8-inch front-end facility in Rousset, France and to the ramp-up of production at the Phoenix, Arizona 8-inch front-end manufacturing facility. Capital expenditures for 1995 were principally devoted to completion of the first phase of the Phoenix facility, completion of the

8-inch wafer equipment installation in the Crolles facility, conversion of existing facilities to 5-inch and 6-inch wafer fabrication and equipping of an 8-inch front-end manufacturing facility in the Catania plant. Capital expenditures for 1994 were principally devoted to completion of the Crolles facility, expansion of certain 5-inch facilities, conversion of certain facilities to 6-inch production, and expansion of certain back-end assembly and test facilities.

The Company currently expects that capital spending for the foreseeable future will continue to be at levels at least as high as in 1995 and 1996, and possibly higher. The Company will continue to monitor its level of capital spending, however, taking into consideration factors such as the trend of the semiconductor market for the foreseeable future. Based on currently expected market trends and conditions for 1997, the Company has again planned a significant amount for capital expenditures that will be used for a variety of projects, including (i) capacity expansion at the Crolles 8-inch front-end facility, (ii) the commencement of buildings and facilities at the Rousset 8-inch front-end facility, (iii) capacity expansion of the Catania 8-inch front-end facility, (iv) the commencement of buildings and facilities at the Agrate 8-inch facility and (v) capacity expansion and upgrading of the Carrollton, Texas facility.

In 1996, the Company's receivables from government agencies totalled $217.3 million compared to $184.7 million in 1995 and $178.0 million in 1994. The $32.6 million increase in 1996 was due primarily to certain important government contracts that were obtained in the fourth quarter of 1996. See Note 7 to the Consolidated Financial Statements. In 1996, the Company's advances from government agencies totalled $10.7 million compared to $11.2 million in 1995 and $6.8 million in 1994. See Note 15 to the Consolidated Financial Statements. Although the timing of receipt of funds under government contracts has been delayed from time to time in the past, the Company has so far received the amounts recorded in such receivables.

The Company expects to have significant capital requirements in the coming years and intends to continue to devote a substantial portion of its net revenues to research and development. The Company plans to fund its capital requirements from cash from operations, available funds, available support from third parties (including state support, principally from the French and Italian governments) and may make recourse to borrowings under available credit lines and, to the extent necessary or attractive based on market conditions prevailing at the time, the sale of debt or additional equity securities. There can be no assurance that additional financing will be available as necessary to fund the Company's working capital requirements, research and development, industrialization costs or expansion plans, or that any such financing, if available, will be on terms acceptable to the Company.

The Company believes that its available funds, available support from third parties and additional borrowings will be sufficient to meet its anticipated needs for liquidity through at least 1997.

CONSOLIDATED STATEMENTS OF INCOME SGS-THOMSON Microelectronics N.V.

(In thousands of U.S. dollars except per share amounts)	Year ended December 31, 1994	1995	1996
Net sales	2,602,205	3,520,670	4,078,246
Other revenues (note 16)	42,736	33,749	44,114
NET REVENUES	2,644,941	3,554,419	4,122,360
Cost of sales	(1,528,694)	(2,096,039)	(2,414,706)
GROSS PROFIT	1,116,247	1,458,380	1,707,654
Selling, general and administrative	(339,858)	(413,148)	(421,012)
Research and development	(338,361)	(440,334)	(532,294)
Restructuring costs (note 18)	(37,032)	(12,975)	0
Other income and expenses (note 19)	31,984	59,107	45,074
OPERATING INCOME	432,980	651,030	799,422
Net interest expenses (note 20)	(21,022)	(16,854)	(11,169)
Gain on disposal of investment	0	0	7,263
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS	411,958	634,176	795,516
Income tax expense (note 21)	(49,464)	(108,282)	(171,638)
INCOME BEFORE MINORITY INTERESTS	362,494	525,894	623,878
Minority interests	584	1,666	
NET INCOME	362,494	526,478	625,544
EARNINGS PER SHARE	3.04	4.03	4.50
Number of shares outstanding at the end of the year	128,603,880	138,208,680	138,985,580
Number of weighted average shares used in calculating earnings per share	119,392,417	130,647,079	138,695,540

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

CONSOLIDATED BALANCE SHEET SGS-THOMSON Microelectronics N.V.

(In thousands of U.S. dollars)	As at December 31, 1995	1996
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents (note 4)	754,046	551,896
Marketable securities (note 4)	4,354	4,508
Trade accounts and notes receivable (note 5)	595,419	645,923
Inventories (note 6)	450,649	521,402
Other receivables and assets (note 7)	360,262	418,051
TOTAL CURRENT ASSETS	2,164,730	2,141,780
Intangible assets, net (note 8)	13,386	17,350
Property, plant and equipment, net (note 9)	2,299,502	2,839,932
Investments and other non-current assets (note 10)	8,388	6,450
	2,321,276	2,863,732
TOTAL ASSETS	4,486,006	5,005,512
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Bank overdrafts and current portion of long-term debt (note 14)	492,788	428,245
Trade accounts and notes payable	507,889	444,166
Other payables and accrued liabilities (note 15)	342,738	318,556
Accrued and deferred income tax	138,256	210,805
TOTAL CURRENT LIABILITIES	1,481,671	1,401,772
Long-term debt (note 14)	200,660	194,910
Reserves for pension and termination indemnities (note 12)	94,956	100,685
Other non-current liabilities (note 13)	37,462	38,224
	333,078	333,819
TOTAL LIABILITIES	1,814,749	1,735,591
MINORITY INTERESTS	9,542	9,901
Capital stock	1,066,528	1,072,933
Capital surplus	922,065	930,330
Accumulated result	584,039	1,209,738
Translation adjustments	89,083	47,019
SHAREHOLDERS' EQUITY (note 11)	2,661,715	3,260,020
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	4,486,006	5,005,512

Other commitments and contingencies: Note 25
The accompanying notes are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS SGS-THOMSON Microelectronics N.V.

(In thousands of U.S. dollars)	Year ended December 31, 1994	1995	1996
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	362,494	526,478	625,544
Add (deduct) non-cash items:			
Depreciation and amortization	287,985	392,390	535,908
Gain on disposal of investment	0	0	(7,263)
Other non-cash items	60,121	(8,707)	7,298
Minority interest in net income of subsidiaries	0	(584)	(1,666)
Changes in assets and liabilities:			
Trade receivables	(71,290)	(126,603)	(71,774)
Inventories	(35,031)	(91,412)	(80,517)
Trade payables	78,144	17,005	(38,019)
Other assets and liabilities, net	45,705	116,562	11,156
NET CASH FROM OPERATING ACTIVITIES	728,128	825,129	980,667
CASH FLOWS FROM INVESTING ACTIVITIES:			
Payment for purchases of tangible assets	(779,696)	(1,001,936)	(1,125,205)
Proceeds from sales of tangible assets and investments	1,455	0	8,420
Other investing activities	(5,951)	2,868	(5,297)
Investment in marketable debt securities (net)	59,618	5	(196)
NET CASH USED IN INVESTING ACTIVITIES	(724,574)	(999,063)	(1,122,278)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issuance of long-term debt	13,702	11,741	84,623
Repayment of long term debt	(148,554)	(96,202)	(54,085)
Increase (decrease) in short-term facilities	101,224	165,298	(106,239)
Capital increase	202,836	391,321	16,671
NET CASH FROM (USED IN) FINANCING ACTIVITIES	169,208	472,158	(59,030)
Effect of changes in exchange rates	20,936	(1,412)	(1,509)
NET CASH INCREASE (DECREASE)	193,698	296,812	(202,150)
Cash and cash equivalents at beginning of the year	263,536	457,234	754,046
Cash and cash equivalents at end of the year	457,234	754,046	551,896

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

CONSOLIDATED STATEMENT OF

CHANGES IN SHAREHOLDERS' EQUITY SGS-THOMSON Microelectronics N.V.

(In thousands of U.S. dollars)	Capital stock	Capital surplus	Accumulated result	Translation adjustments	Shareholders' equity
BALANCE AS OF JANUARY 1, 1994	906,451	484,009	(304,778)	(81,671)	1,004,011
Capital increase	75,049	123,772			198,821
Stock option compensation		18,125			18,125
Net income			362,494		362,494
Translation adjustment				96,588	96,588
BALANCE AS OF DECEMBER 31, 1994	981,500	625,906	57,716	14,917	1,680,039
Capital increase	85,028	294,455			379,483
Deferred compensation		1,704	(155)		1,549
Net income			526,478		526,478
Translation adjustment				74,166	74,166
BALANCE AS OF DECEMBER 31, 1995	1,066,528	922,065	584,039	89,083	2,661,715
Capital increase	6,405	8,847			15,252
Deferred compensation		(582)	155		(427)
Net income			625,544		625,544
Translation adjustment				(42,064)	(42,064)
BALANCE AS OF DECEMBER 31, 1996	1,072,933	930,330	1,209,738	47,019	3,260,020

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

(Currency -- Thousands of U.S. dollars)

1. THE COMPANY

SGS-THOMSON Microelectronics N.V. (the "Company") was formed in 1987 by the combination of the semiconductor business of SGS Microelettronica (then owned by Societa Finanziara Telefonica (S.T.E.T.), an Italian corporation) and the non-military business of Thomson Semiconducteurs (then owned by Thomson-CSF, a French corporation) whereby each company contributed their respective semiconductor businesses in exchange for a 50% interest in the Company.

The Company is registered in the Netherlands with its statutory domicile in Amsterdam.

As of December 31, 1996, the Company was 69.04% (December 31, 1995: 69.36%) owned by SGS-THOMSON Microelectronics II B.V., and 30.96% by the public (December 31, 1995: 30.64%)

At December 31, 1996, SGS-THOMSON Microelectronics II B.V. was 100% owned by SGS-THOMSON Microelectronics Holding N.V. At December 31, 1996 and at December 31, 1995, SGS-THOMSON Microelectronics Holding N.V. was owned as follows:

o 50% by FT2CI, a French holding company, whose shareholders in turn are FT1CI (50.1%) and Thomson-CSF (49.9%); FT1CI, a French holding company, is owned by CEA-Industrie (51%) and France Telecom (49%).

o 50%, (48.14% in 1993) by M.E.I.--Microelettronica Italiana s.r.l. ("M.E.I."), an Italian holding company, whose Shareholders are Comitato per l'intervento nella SIR ed in settori ad alta tecnologia ("Comitato SIR") (49.9%) and Istituto per la Ricostruzione Industriale S.p.a. (I.R.I.) (50.1%).

2. SUMMARY OF ACCOUNTING POLICIES

2.1) PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (US GAAP). The Company maintains its accounting records in accordance with Dutch accounting principles, which have been restated to conform with US GAAP. No significant adjustments have arisen as a consequence of this restatement to conformity with US GAAP.

The Company's consolidated financial statements include the assets, liabilities and results of operations of its majority-owned subsidiaries. The ownership of the other interest holders is reflected as minority interests. All significant intercompany accounts and transactions have been eliminated in consolidation.

The initial combination of the SGS Microelettronica and Thomson Semiconducteurs civilian semiconductor businesses was accounted for as the creation of a joint venture. Accordingly, the assets and liabilities of the combined entities were recorded in the books of the joint venture at their carrying amounts at the date of combination.

2.2) USE OF ESTIMATES

The presentation of financial statements in accordance with US GAAP requires management to make estimates and assumptions that affect the reported results of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the related reported amounts of sales and expenses during the reporting period. Actual results could differ from those estimates. Management believes that the estimates are reasonable.

2.3) INCOME RECOGNITION

/SALES: Revenues on sales of semiconductor products are recognized upon shipment of the products. A portion of the Company's sales are made to distributors who participate in certain programs common to the semiconductor industry whereby the distributors are allowed to return merchandise under certain circumstances and may receive future price reductions. Provision is made at the time of sale for estimated product returns and price protection which may occur under programs the Company has with these customers.

/SUBSIDIES: Government subsidies are recognized as related costs are incurred, commencing when the subsidies' contract is signed with the relevant government department or agency. Government subsidies for research and development are included in "other income and expenses". Government subsidies

for industrialization costs are offset against related expenses in "cost of sales". Government subsidies for capital expenditures are deducted from the cost of the related fixed assets.

2.4) TRANSLATION OF FOREIGN SUBSIDIARIES' FINANCIAL STATEMENTS

The United States dollar is the reporting currency for the Company because the Company does not have any operations in the Netherlands and the dollar is the currency of reference in terms of market pricing in the worldwide semiconductor industry. Furthermore, there is no currency in which the majority of transactions are denominated, and revenues from external sales in U.S. dollars exceed revenues in any other currency.

The functional currency used by each significant subsidiary throughout the group is the local currency. Assets and liabilities of these subsidiaries are translated at current rates of exchange at the balance sheet date. Income and expense items are translated at the average exchange rate for the period. The effects of translating the financial position and results of operation of local functional currency are included in shareholders' equity.

2.5) FOREIGN CURRENCY TRANSACTIONS

Assets, liabilities, revenue, expenses, gains or losses arising from foreign currency transactions are recorded in the functional currency of the recording entity at the exchange rate in effect at the date of the transaction. At each balance sheet date, recorded balances denominated in a currency other than the recording entity's functional currency are translated at the exchange rate prevailing at that date. The related exchange gains and losses are recorded in the income statement.

2.6) INTANGIBLE ASSETS

Intangible assets include the cost of technologies and licenses purchased from third parties, amortized over a period ranging from five to eighteen years, and goodwill acquired in business combinations amortized over its estimated useful life, generally five to fifteen years.

2.7) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost, net of government subsidies. Major renewals and improvements are capitalized; minor replacements, maintenance and repairs are charged to current operations. Depreciation is computed using the straight-line method over the following estimated useful lives:

Buildings	33 years
Leasehold improvements	10 years
Machinery and equipment	6 years
Computer and R&D equipment	3-6 years
Other	2-5 years

Assets subject to leasing agreements and classified as capital leases are included in property, plant and equipment and depreciated over the shorter of the estimated useful life or the lease term.

2.8) INVESTMENTS

The equity accounting method is used when the Company has a 20% to 50% equity interest and the ability to exercise significant influence over the investee. Marketable debt and equity securities and other equity investments are classified as "available for sale" securities and stated at market value.

2.9) INVENTORIES

Inventories are stated at the lower of cost or market (net realizable value). Cost is computed on a currently adjusted standard basis (which approximates actual cost on a current average basis).

2.10) RESEARCH AND DEVELOPMENT

Research and development costs are charged to expense as incurred. Research and development costs include costs incurred by the Company as well as the Company's share of costs incurred by two French research and development interest groups. For some of its research and development programs, the Company receives grants from Governmental agencies; these grants are recognized in the income statement in "Other income and expenses".

2.11) PENSION AND TERMINATION INDEMNITIES

/PENSION: Upon retirement, the Company's employees receive such benefits as are provided by pension plan arrangements; these plans conform with local regulations and practices of the countries in which the Company operates.

/TERMINATION INDEMNITIES:

Italy Italian law provides for an indemnity to be paid to personnel upon termination of employment. The amount of indemnity is based upon the number of years of service. The undiscounted value of the vested obligation at the balance sheet date is recorded as a liability.

France In France, an indemnity is paid to personnel only upon retirement from the Company. The French entity recognizes the related cost and liability with the prior years' liability being amortized over the average remaining service period until retirement age.

2.12) RESTRUCTURING COSTS

Restructuring costs include incremental costs to be incurred as a result of the adoption by management of a formal plan to reorganize certain activities. Such costs may include severance payments, moving costs and fixed asset write-offs.

2.13) INCOME TAXES

The provision for current taxes represents the income taxes expected to be payable for the current year. Deferred tax assets and liabilities are recorded for all temporary differences arising between the tax and book basis of assets and liabilities and for the benefits of tax credits and loss carryforwards. Those deferred tax assets and liabilities are measured using the enacted tax rates at which they are expected to be realized or paid. A valuation allowance is provided where necessary to reduce deferred tax assets to the amount expected to be "more likely than not" realized in the future. Tax rate changes are reflected in income in the period such changes are enacted.

2.14) FINANCIAL INSTRUMENTS

/INTEREST RATE SWAP AGREEMENTS: The Company enters into interest swap agreements with the purpose of reducing its interest rate exposure by changing the floating rates of certain loans into fixed rates. The differential to be paid or received is recognized in interest expense over the life of the agreements.

/FOREIGN EXCHANGE FORWARD CONTRACTS: The Company enters into forward exchange contracts as a hedge against accounts payable and receivable in foreign currencies and against firm sale commitments (ranging from one to six months from the balance sheet date). Premiums or discounts on those contracts are recognized in the income statement over the life of the contract. Generally gains and losses associated with currency rate changes are recognized currently.

2.15) STOCK OPTIONS

In October 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123 (FAS 123), "Accounting for Stock-Based Compensation", which establishes a fair value-based method of accounting for compensation costs related to stock option plans and other forms of stock based compensation plans as an alternative to the intrinsic value-based method of accounting as defined under Accounting Principles Board Opinion no. 25 (APB 25). The Company has decided not to elect the new method of accounting, and will provide pro forma disclosure as if the fair value-based method prescribed by FAS 123 had been applied in measuring compensation expense (note 11).

2.16) ADVERTISING COSTS

Advertising costs are charged to operations when incurred. Advertising expenses for 1994, 1995 and 1996 were $6,644, $10,133 and $12,686, respectively.

2.17) EARNINGS PER SHARE

Earnings per share is calculated based upon the weighted average number of common shares and dilutive common stock equivalents using the treasury stock method. Dilutive common stock equivalents consist of stock options.

2.18) RECLASSIFICATIONS

Certain prior year amounts have been reclassified to conform with the current year presentation.

3. CONSOLIDATED ENTITIES

The consolidated financial statements include the accounts of SGS-THOMSON Microelectronics N.V. and the following entities as of December 31, 1996:

Legal Seat		Name	Common Stock (Thousands)	Percentage Ownership (Direct or Indirect)
United Kingdom	London	SGS-THOMSON Microelectronics LTD	9,900 GBP	100
	London	Thomson Components LTD	1,150 GBP	100
	Bristol	SGS-THOMSON E.E.I.G.	0 GBP	100
Sweden	Stockholm	SGS-THOMSON Microelectronics A.B.	16,000 SEK	100
Germany	Munich	SGS-THOMSON Microelectronics GmbH	12,901 DEM	100
Switzerland	Geneva	SGS-THOMSON Microelectronics S.A.	500 CHF	100
Malta	Malta	SGS-THOMSON Microelectronics LTD	21,590 MTP	100
Spain	Madrid	SGS-THOMSON Microelectronics S.A.	55,000 ESP	100
France	Paris	SGS-THOMSON Microelectronics S.A.	2,289,764 FRF	100
	Paris	SGS-THOMSON Microelectronics S.N.C.	0 FRF	100
Italy	Milano	SGS-THOMSON Microelectronics S.R.L.	502,000,000 ITL	100
	Catania	CORIMME	14,000,000 ITL	100
Singapore	Singapore	SGS-THOMSON Microelectronics PTE LTD	179,997 SGD	100
	Singapore	SGS-THOMSON Microelectronics ASIA PACIFIC PTE LTD	13,982 SGD	100
Malaysia	Muar	SGS-THOMSON Microelectronics SDN BHD	196,805 MYR	100
	Muar	SGS-THOMSON (Malaysia) SDN BHD	0.002 MYR	100
Japan	Tokyo	SGS-THOMSON Microelectronics KK	68,000 JPY	100
Hong Kong	Hong Kong	SGS-THOMSON Microelectronics LTD	780 HKD	100
Australia	Sydney	SGS-THOMSON Microelectronics PTY LTD	185 AUD	100
United States	Dallas	SGS-THOMSON Microelectronics Inc.	22,000 USD	100
	Rancho Ber.	SGS-THOMSON Microelectronics (RB), Inc.	1 USD	100
	Dallas	SGS-THOMSON Microelectronics Leasing Co Inc.	1 USD	100
Brazil	Sao Paulo	SGS-THOMSON Microelectronics Ltda	14,314 BRL	100
Morocco	Casablanca	SGS-THOMSON Microelectronics S.A.	66,000 MAD	100
	Casablanca	Electronic Holding S.A.	3,110 MAD	100
China	Shenzhen	Shenzhen STS Microelectronics Co LTD	252,748 CNY	60
India	New Delhi	SGS-THOMSON Microelectronics PTE LTD	62,000 INR	100

4. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consists of the following:

	December 31,	
	1995	1996
Cash	801	1,579
Bank accounts	748,591	548,777
Marketable securities (with maturity under 3 months)	4,654	1,540
TOTAL	754,046	551,896
Marketable securities (with maturity over 3 months)	4,354	4,508

Marketable securities consist mainly of certificates of deposit. There was no significant difference between the book value of traded marketable securities and their fair market value as of December 31, 1995 and 1996.

5. TRADE ACCOUNTS AND NOTES RECEIVABLE

Trade accounts and notes receivable consist of the following:

	December 31,	
	1995	1996
Trade accounts and notes receivable	613,300	664,075
Less valuation allowance	(17,881)	(18,152)
TOTAL	595,419	645,923

During 1994, 1995 and 1996 no customer represented individually over ten percent of consolidated net revenues.

6. INVENTORIES

Inventories consist of the following:

	December 31,	
	1995	1996
Raw materials	126,756	121,485
Work-in-process	202,817	278,289
Finished products	121,076	121,628
TOTAL	450,649	521,402

7. OTHER RECEIVABLES AND ASSETS

	December 31,	
	1995	1996
Receivables from government agencies*	184,670	217,334
Taxes and other government receivables	53,996	48,148
Down payment to suppliers	7,577	1,617
Loans to employees	5,201	3,821
Prepaid expenses	21,685	14,700
Sundry debtors	18,419	23,342
Deferred tax	43,331	65,291
Other	25,383	43,798
TOTAL	360,262	418,051

* Related to research and development contracts, industrialization contracts and capital expenditures.

8. INTANGIBLE ASSETS

Intangible assets consist of the following:

	December 31,	
	1995	1996
Technologies and licenses, gross	61,806	56,648
Pension transition obligation	2,142	2,423
Other	315	0
Less accumulated amortization	(50,877)	(41,721)
TOTAL	13,386	17,350

9. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following:

DECEMBER 31, 1995	Gross	Depreciation	Net
Land and buildings	344,439	(63,957)	280,482
Machinery and equipment	3,414,102	(1,689,923)	1,724,179
Other tangible fixed assets	197,375	(127,113)	70,262
Prepayments and construction in progress	224,579	--	224,579
TOTAL	4,180,495	(1,880,993)	2,299,502

DECEMBER 31, 1996	Gross	Depreciation	Net
Land and buildings	456,973	(88,926)	368,047
Machinery and equipment	4,147,941	(2,057,281)	2,090,660
Other tangible fixed assets	221,555	(144,943)	76,612
Prepayments and construction in progress	304,613	--	304,613
TOTAL	5,131,082	(2,291,150)	2,839,932

10. INVESTMENTS AND OTHER NON-CURRENT ASSETS

Investments and other non-current assets consist of the following:

	December 31,	
	1995	1996
Investments carried at fair value	578	1,176
Long-term deposits and receivables	7,810	5,274
TOTAL	8,388	6,450

Long-term deposits and receivables consist primarily of indemnities receivable from third parties on the sale of businesses, which bear interest or are discounted to reflect their present value.

11. SHAREHOLDERS' EQUITY

PUBLIC OFFERINGS OF SHARES

In December 1994, the Company increased its capital stock through the issuance of 9,606,240 new shares of capital stock, which resulted in an increase in capital stock and capital surplus of $75,049 and $123,772, respectively. In connection with a secondary offering of capital stock in October 1995, the Company issued 8,960,000 new shares of capital stock, which resulted in an increase in capital stock and capital surplus of $79,356 and $292,075, respectively.

OUTSTANDING SHARES

The authorized share capital of the Company is NLG 2,750,000,000, consisting of 200,000,000 shares, each with a nominal value of NLG 13.75. As of December 31, 1994, 1995 and 1996, the number of shares of capital stock outstanding at a par value of NLG 13.75 were 128,603,880 shares, 138,208,680 shares and 138,985,580 shares, respectively.

STOCK OPTION PLANS

In 1989, the Shareholders voted to adopt the 1989 Stock Option Plan ("the 1989 Plan") and approved the issuance of 1,634,400 options to 136 employees to purchase capital stock at a price of NLG 25 per share. Under the 1989 Plan, the options vest over four years and are exercisable for ten years. In 1994, the minimum exercise price of the options was reduced to NLG 17.50. As a result, the Company recorded a compensation charge of $18,125 in the fourth quarter of 1994.

In 1995, the Shareholders voted to adopt the 1995 Stock Option Plan ("the 1995 Plan") whereby options for up to 5,500,000 shares may be granted in installments over a five year period. Under the 1995 Plan, the options may be granted to purchase shares of capital stock at a price not lower than the market price of the shares on the date of grant, and generally vest over four years and are exercisable over a period of eight years. In March 1996, the Company granted 1,200,000 options to 497 employees at an exercise price of $36.25 per share.

In 1996, the Shareholders voted to adopt the Supervisory Board Option Plan whereby members of the Supervisory Board may receive, during the three-year period 1996-1998, 3,000 options for 1996 and 1,500 options for 1997 and 1998, to purchase shares of capital stock at the closing market price of the shares on the date of grant. Under the Plan, the options vest over one year and are exercisable for a period expiring eight years from the date of grant. In October 1996, options to purchase 25,500 shares were granted at an exercise price of $54.00 per share.

A summary of stock option transactions for the plans follows:

		Price Per Share	
OPTIONS OUTSTANDING	Number of Shares	Range	Average
December 31, 1993	1,474,400	17.5-25 NLG	20.0 NLG
Options canceled	(18,000)	17.5-25 NLG	19.2 NLG
December 31, 1994	1,456,400	17.5-25 NLG	20.0 NLG
Options exercised	(646,200)	17.5-25 NLG	19.6 NLG
December 31, 1995	810,200	17.5-25 NLG	20.0 NLG
Options granted			
1995 Plan	1,200,000	$36.25	$36.25
Supervisory Board Plan	25,500	$54.00	$54.00
Options canceled	(16,500)	$36.25	$36.25
Options exercised	(531,790)	17.5-25 NLG	20.1 NLG
December 31, 1996	1,487,410	17.5-25 NLG	20.1 NLG
		$36.25-$54.00	$36.73

EMPLOYEE OFFERING PLAN

Pursuant to a resolution of the Supervisory Board of the Company in November 1995, the Company offered to certain of its employees worldwide the right to acquire up to 1,000 shares of capital stock per employee, at a price of $33.725 per share, representing a discount of five percent from the market price. A total of 243,710 shares were sold to participating employees worldwide as a result of the offering. Participating employees who purchased shares in the offering and who hold such shares for at least one year will be entitled to purchase, for a price of 13.75 NLG, one share for each ten shares purchased in the offering.

FAIR VALUE OF STOCK-BASED COMPENSATION

The Company applies the principles of APB 25 in accounting for its stock option grants. Had compensation cost for the Company's stock-based compensation plans been determined based on the fair value at the grant dates for awards under the plans consistent with the method of SFAS 123 (Note 2.15), the Company's net earnings and net earnings per share would have been decreased to the pro forma amounts indicated below:

	Year ended December 31, 1995	1996
Net income		
As reported	526,478	625,544
Pro forma	526,478	620,084
Earnings per share		
As reported	4.03	4.50
Pro forma	4.03	4.47

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions: dividend yield of 0%, expected volatility of 55%, a risk-free interest rate of 5%, and expected life of five years.

RETAINED EARNINGS

At December 31, 1996, the amount of retained earnings available to pay dividends under Dutch law was approximately $2,187,000 (1995: $1,595,000). Retained earnings for purposes of this calculation are based upon generally accepted accounting principles in The Netherlands. The Company's subsidiaries are subject to the laws of the countries in which they are domiciled. These laws may restrict the ability of the subsidiaries to transfer funds to the Company. Such restrictions are not considered to be significant as of December 31, 1996.

12. RESERVES FOR PENSION AND TERMINATION INDEMNITIES

Reserves for pension and termination indemnities consist of the following:

	December 31, 1995	1996
Italy(a)	86,733	98,028
Other countries(b)	8,223	2,657
TOTAL	94,956	100,685

(A) ITALY

Changes in the undiscounted benefit consist of the following:

	December 31, 1995	1996
Accrual at the beginning of the period	75,237	86,733
Accrued benefits	14,533	18,469
Payments	(5,044)	(10,213)
Translation adjustment	2,007	3,039
Accrual at the end of the period	86,733	98,028

(B) OTHER COUNTRIES (FRANCE, UNITED STATES, JAPAN AND GERMANY)

The funded status of pension plans and termination indemnities is as follows:

	December 31,	
	1995	1996
Vested benefits	(36,635)	(47,816)
Non-vested benefits	(16,597)	(10,480)
Projected benefit obligation	(53,232)	(58,296)
Plan assets at fair value	45,455	54,562
Funded status	(7,777)	(3,734)
Unrecognized transition obligation	(4,377)	(4,404)
Unrecognized prior service cost	7,298	6,869
Unrecognized net gains or losses	825	514
Net accrued for pension plans	(4,031)	(755)

The accumulated benefit obligation amounted to $57,205 as of December 31, 1996 ($45,046 as of December 31, 1995).

The periodic net pension and termination indemnities cost includes the following:

			December 31,
	1994	1995	1996
Service cost of benefits earned	2,819	3,613	4,764
Interest cost on liability	2,482	3,016	3,960
Return on plan assets	986	(3,716)	(4,267)
Net amortization and deferral	(3,379)	418	(1,467)
TOTAL	2,908	3,331	2,990

ASSUMPTIONS	1994	1995	1996
Discount rate	7%	7-8.5%	6.5-8.5%
Salary increase rate	4.5-6%	4-6.5%	4-6.5%
Expected rate of return of funds	8.5%	8-10%	6.5-10%

13. OTHER NON-CURRENT LIABILITIES

		December 31,
	1995	1996
Provision for claims and litigation	16,000	11,550
Provision for patent risks	20,000	20,000
Other long-term payables	1,462	6,674
TOTAL	37,462	38,224

14. LONG-TERM DEBT

Long-term debt consists of the following:

		December 31,
	1995	1996
Secured (mainly mortgages on land, building and liens on equipment)	14,407	23,336
Unsecured	186,253	171,574
TOTAL	200,660	194,910

REPAYMENT SCHEDULE	December 31, 1996
1998	42,683
1999	51,885
2000	45,327
2001	17,106
Thereafter	37,909
TOTAL	194,910

		December 31,
INTEREST RATES	1995	1996
Non-interest bearing*	4,661	4,669
From 1 to 3 %	87,005	73,237
From 3 to 6 %	36,071	57,067
From 6 to 10 %	66,035	55,758
From 10 to 15 %	6,888	4,179
TOTAL	200,660	194,910

* Non-interest bearing and certain low interest bearing borrowings relate to borrowings under Italian and French governmental programs.

CURRENCIES	1995	December 31, 1996
U.S. dollar	141	6,950
Italian lira	120,333	143,258
French franc	15,830	9,698
Singapore dollar	26,622	0
Other	37,734	35,004
TOTAL	200,660	194,910

At December 31, 1996, the current portion of long-term debt included in current liabilities amounted to $112,372 (1995: $88,248). At December 31, 1996, the above long-term debt included $357 obligations under capital leases (1995:$746).

Financial debt includes mainly:

	1995	1996
SGS-THOMSON Microelectronics NV		
Libor 0.45% Bank Loan 1991-1996		
(US dollars 100,000,000)	33,333	--
SGS-THOMSON Microelectronics SA		
Libor 0.55% Bank Loan 1992-1997		
(French francs 100,000,000)	8,163	3,807
SGS-THOMSON Microelectronics PTE Ltd		
PR + 0.25% Bank Loan 1991-1997		
(Singapore dollars 50,000,000)	11,783	--
5.44% Bank Loan 1992-1997		
(Singapore dollars 40,000,000)	22,623	--
SGS-THOMSON Microelectronics s.r.l		
2.15% 1991-2001 Government Loan		
(Italian lira 155,694,000,000)	86,933	76,575

15. OTHER PAYABLES AND ACCRUED LIABILITIES

	December 31, 1995	1996
Taxes other than income taxes	29,739	24,754
Salaries and wages	69,062	95,553
Social charges	74,217	49,882
Advances received on fundings	11,188	10,724
Provision for restructuring costs and asset writedowns	23,957	5,981
Litigation and other risks	19,853	5,000
Commercial rebates	31,992	53,214
Royalties payable	38,427	19,612
Other	44,303	53,836
TOTAL	342,738	318,556

PROVISION FOR RESTRUCTURING COSTS

During 1993, the Company decided to upgrade the technology of its main production plants around the world. This upgrading began in 1994 and will continue through 1997. It has involved fixed asset write-offs and moving costs. The remaining provision as of December 31, 1995 and 1996 was $23,957 and $5,981 respectively.

16. OTHER REVENUES

Other revenues consist of the following:

			December 31,
	1994	1995	1996
Royalties and indemnities received	14,056	16,549	582
Development services invoiced to customers	23,126	9,800	975
Licensing revenues	0	0	16,693
Miscellaneous sales	5,554	7,346	18,675
Other	0	54	7,189
TOTAL	42,736	33,749	44,114

17. PERSONNEL

Labor costs consist of the following:

			December 31,
	1994	1995	1996
Salaries and wages	524,844	643,559	745,329
Social security contribution	162,235	194,650	210,611
Other	37,053	48,251	53,838
TOTAL	724,132	886,460	1,009,778

Labor costs are allocated to cost of sales, selling, general and administrative expenses and research and development costs. At December 31, 1996 the Company employed 25,893 persons (1995: 25,523).

18. RESTRUCTURING COSTS

Restructuring costs consist of the following:

		December 31,
	1994	1995
Cash items:		
Severance	13,009	3,602
Moving costs	2,957	9,373
Non-cash items:		
Asset write-offs	21,066	0
TOTAL	37,032	12,975

The cash outlays relating to the restructuring costs are for the most part made in the period the costs are recorded in the income statement or in the subsequent period.

The benefits of the asset write-offs effected in 1994 have not been significant because of the relative immateriality of the costs involved and the increased depreciation expense in future periods related to the upgrading of some manufacturing plants around the world (see Note 15).

19. OTHER INCOME AND EXPENSES

Other income and expenses consist of the following:

	December 31,		
	1994	1995	1996
Research and development funding*	80,139	89,643	63,792
Patents income (expense) net	(7,598)	(8,055)	(2,639)
Exchange gain (loss)	1,982	5,082	11,822
Start-up costs	(8,847)	(26,489)	(38,987)
Goodwill amortization	(1,437)	(1,437)	(315)
Stock option plan compensation charge	(18,125)	0	0
Other	(14,130)	363	11,401
TOTAL	31,984	59,107	45,074

* Does not include certain other funding received for industrialization costs (which include certain costs incurred to bring prototype products to the production stage). Such funding and costs are netted in cost of sales in the income statement ($19,276 for 1994, $11,825 for 1995 and $4,613 for 1996).

20. NET INTEREST EXPENSES

Net interest expenses consist of the following:

	December 31,		
	1994	1995	1996
Income	20,500	35,206	34,139
Expenses	(41,522)	(52,060)	(45,308)
TOTAL	(21,022)	(16,854)	(11,169)

Cash paid for interest was $51,156 for 1995 and $45,389 for 1996.

21. INCOME TAX

SGS-THOMSON Microelectronics N.V. and its subsidiaries are individually liable for income tax. Tax losses can only offset profits generated by the taxable entity incurring a loss.

	December 31,		
	1994	1995	1996
Domestic	0	0	(37,270)
U.S.	(6,304)	(9,558)	(221)
Foreign	(24,280)	(105,089)	(75,632)
Current	(30,584)	(114,647)	(113,123)
Deferred	(18,880)	6,365	(58,515)
INCOME TAX EXPENSE	(49,464)	(108,282)	(171,638)

The principal items accounting for the differences in income taxes computed at The Netherlands statutory rate (35%) and the effective income tax rate comprise the following:

Income tax expense computed at statutory rate	144,185	221,962	279,013
Deductions for financial reporting for which no current tax benefit is available	(12,403)	(50,601)	(14,894)
Variation in valuation allowance	(70,645)	(25,528)	(23,935)
Other tax and credits	(9,962)	(32,252)	(7,855)
Effect of tax rate differences	(1,711)	(5,299)	(60,691)
INCOME TAX EXPENSE	49,464	108,282	171,638

Permanent differences reflect mainly the effects of the special pioneer regimes existing in certain Southeast Asian countries and the non-deductible goodwill amortization.

Pioneer status currently applies to one of the Company's two Singapore factories. Under this regime all the profits of this operation--calculated in accordance with applicable taxation rules and after deduction of capital allowances--are exempt from Singapore income tax for the specified pioneer period. This pioneer period expired on December 31, 1996. Beginning in 1997, the part of the Company's operations currently enjoying pioneer status will continue to benefit from certain tax privileges since a half rate taxation basis will be applied when compared to the second non-pioneer factory. In calculating deferred taxes, the Company records a liability (or asset) for a temporary difference that reverses after the tax holiday period ends, using the applicable taxation rate.

Deferred tax assets and liabilities consist of the following:

	1995	1996
Tax loss carryforwards and capital allowances	103,789	14,976
Other assets	53,099	122,942
Total assets, gross	156,888	137,918
Valuation allowance	(28,091)	(4,156)
DEFERRED TAX ASSETS, NET	128,797	133,762
Fixed assets depreciation	140,224	148,562
Other liabilities	7,362	59,220
DEFERRED TAX LIABILITIES	147,586	207,782

As a result of offsetting deferred tax assets against deferred tax liabilities in each tax jurisdiction, the Company recorded a net deferred tax asset of $43,331 in 1995 and $65,291 in 1996, and a net deferred tax liability of $62,120 in 1995 and $139,311 in 1996.

As of December 31, 1996, the Company and its subsidiaries had tax credits of $2,813 with no expiration date and net operating loss carryforwards and capital allowance carryforwards expiring in the following years:

	December 31, 1996
1997	12,917
1998	12,565
1999	2,038
2000 and thereafter	904
TOTAL	28,424

The Company paid $52,545 cash for income taxes in 1995 and $109,277 cash for income taxes in 1996.

22. CREDIT FACILITIES

As of December 31, 1996, the aggregate amount of the Company's long-term credit facilities was approximately $287,000 under which $287,000 of indebtedness was outstanding, and the aggregate amount of the Company's short-term facilities was approximately $975,000 under which $315,873 indebtedness was outstanding.

23. LEASE COMMITMENTS

The Company leases land, building, plant and equipment under non-cancellable lease agreements. As of December 31, 1996 the future minimum lease payments to which the Company was committed under operating leases were as follows:

Year	
1997	13,372
1998	6,840
1999	2,056
2000	1,422
2001	1,289
Thereafter	50
TOTAL	25,029

24. FINANCIAL INSTRUMENTS

Financial instruments and derivatives are used exclusively for purposes other than trading.

FORWARD EXCHANGE CONTRACTS The Company enters into forward contracts as a hedge against potentially adverse changes in foreign currency exchange rates. Such contracts mature mainly during the first quarter of 1997, and amount to $153,200 forward sale of U.S. dollars and $83,660 forward sale of other foreign currencies and to $38,000 forward purchase of U.S. dollars and $32,939 forward purchase of other foreign currencies.

FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISKS AND CONCENTRATION OF CREDIT RISK

The Company uses financial instruments with off-balance sheet risks primarily to manage its exposure to fluctuations in interest rates and foreign currency exchange rates. The Company controls the credit risks associated with these financial instruments through credit approvals, investment limits and centralized monitoring procedures but does not normally require collateral or other security from the parties to the financial instruments with off-balance sheet risk. In addition, the Company conducts its operations with customers located throughout the world. Management believes that receivables are well diversified, thereby reducing potential credit risk to the Company. As a consequence, the Company does not anticipate non-performance by counterparties which could have a significant impact on its financial position or results of operations. In the event of a failure to honor one of the forward contracts by one of the banks with which the Company has contracted, management believes any loss would be limited to the exchange rate differential from the time the contract was made until the time it was compensated.

INTEREST RATE AND FOREIGN CURRENCY AGREEMENTS:

	December 31,	
xxx	1995	1996
Long-term interest rate swaps	30,000	0
Forward exchange contracts :		
sales	250,717	236,860
purchases	(32,588)	(70,939)

	Remaining term
Forward exchange contracts	1 to 6 months

FAIR VALUE OF FINANCIAL INSTRUMENTS The estimates of fair value were obtained using prevailing financial market information from various valuation techniques as of December 31, 1996. The methodologies used to estimate fair values are as follows:

CASH AND CASH EQUIVALENTS, ACCOUNTS AND NOTES RECEIVABLE, BANK OVERDRAFTS, SHORT-TERM BORROWINGS, ACCOUNTS AND NOTES PAYABLES The carrying amounts reflected in the consolidated financial statements are reasonable estimates of fair value because of the relatively short period of time between the origination of the instruments and their expected realization.

LONG-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT The fair values of these financial instruments were determined by estimating future cash flows on a borrowing-by-borrowing basis and discounting these future cash flows using the Company's incremental borrowing rates for similar types of borrowing arrangements.

INTEREST RATE SWAPS AND FORWARD EXCHANGE CONTRACTS The fair value of these instruments is the estimated amount that the Company would receive or pay to settle the related agreements as of December 31, 1995 and 1996 based upon current interest rates and the creditworthiness of the counterparties.

	1995		December 31, 1996	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
BALANCE SHEET				
Investments	578	578	--	--
Marketable securities	9,008	9,008	6,048	6,048
Bank loans (including current portion)	288,908	260,515	286,859	270,218
OFF-BALANCE SHEET				
Long-term interest swap		48		--
Forward exchange contracts		(507)		2,900

25. OTHER COMMITMENTS AND CONTINGENCIES

LITIGATION The Company is involved in various litigations incidental to the normal conduct of its operations. However, these contingencies are not considered to be material in relation to the consolidated results.

OTHER CONTINGENT LIABILITIES The Company's position on certain tax regulation may differ from the tax authorities' eventual interpretation, which could result in a tax liability. However, the Company believes the risk of incurring a significant liability is remote and, therefore, believes that provisions carried as at December 31, 1996 are sufficient.

26. RELATED PARTY TRANSACTIONS

The main transactions with the shareholders of SGS-THOMSON Microelectronics Holding NV and their affiliates were as follows:

			December 31,
	1994	1995	1996
Sales	158,457	195,352	232,057
Research and development expenses	(12,317)	(17,815)	(13,262)
Other purchases and expenses	(13,757)	(42,237)	(48,155)

Indebtedness of the Company was supported by guarantees from the shareholders of SGS-THOMSON Microelectronics Holding NV as follows:

		December 31,
	1995	1996
Long-term debt	156,359	119,858
Short-term debt	79,117	22,246
TOTAL	235,476	142,104
Accounts receivable	47,154	31,580
Accounts payable	11,393	10,519

27. SEGMENT INFORMATION

The Company, operating in a single industry segment, designs, develops, manufactures and markets a wide variety of semiconductors. Net revenues, earnings from operations, capital expenditures and identifiable assets classified by the major geographic areas in which the Company operates are:

	Americas	Asia Pacific	Europe	Other Corporate and Elimination	Total
1994					
Income statement					
Net revenues	673,514	752,301	1,217,126	2,000	2,644,941
Intersegment sales	130,575	1,352,481	2,521,539	(4,004,595)	0
Total	804,089	2,104,782	3,738,665	(4,002,595)	2,644,941
Operating profit	33,578	141,723	288,430	(30,751)	432,980
Depreciation	(29,442)	(70,000)	(188,543)	--	(287,985)
Research and development expenses	(37,157)	(1,705)	(299,499)	--	(338,361)
Cash flow statement					
Capital expenditures	163,302	131,996	484,398	--	779,696
Balance sheet					
Identifiable assets	411,555	591,202	1,742,175	479,759	3,224,691
Other information					
Number of employees	2,057	7,010	12,950	--	22,017
Wages and salaries	(110,840)	(101,111)	(512,181)	--	(724,132)
1995					
Income statement					
Net revenues	846,406	1,080,428	1,627,585	--	3,554,419
Intersegment sales	179,767	3,411,776	3,372,542	(6,964,085)	0
Total	1,026,173	4,492,204	5,000,127	(6,964,085)	3,554,419
Operating profit	63,348	242,113	355,208	(9,639)	651,030
Depreciation	(51,263)	(90,450)	(250,677)	--	(392,390)
Research and development expenses	(48,607)	(4,875)	(386,852)	--	(440,334)
Cash flow statement					
Capital expenditures	187,517	204,694	609,725	--	1,001,936
Balance sheet					
Identifiable assets	574,730	845,536	2,336,956	728,784	4,486,006
Other information					
Number of employees	2,439	7,934	15,150	--	25,523
Wages and salaries	(139,640)	(120,832)	(625,988)	--	(886,460)
1996					
Income statement					
Net revenues	934,224	1,363,771	1,824,365	--	4,122,360
Intersegment sales	268,688	3,764,473	5,068,912	(9,102,073)	0
Total	1,202,912	5,128,244	6,893,277	(9,102,073)	4,122,360
Operating profit	3,038	211,998	596,685	(12,299)	799,422
Depreciation	(77,967)	(105,363)	(352,211)	(367)	(535,908)
Research and development expenses	(73,710)	(7,816)	(450,465)	(303)	(532,294)
Cash flow statement					
Capital expenditures	179,326	165,404	780,305	170	1,125,205
Balance sheet					
Identifiable assets	686,455	933,115	2,848,124	537,818	5,005,512
Other information					
Number of employees	2,555	7,570	15,753	15	25,893
Wages and salaries	(166,486)	(133,471)	(708,826)	(995)	(1,009,778)

In the above information, sales include local sales and exports made by operations within each area. Total sales by geographic area include sales to unaffiliated customers and intergeographic transfers. To control costs, a substantial portion of the Company's products are transported between the US, Asia and Europe in the process of being manufactured and sold. Sales to unaffiliated customers have little correlation with the location of manufacture. Customers have little correlation with the location of manufacture. As a global participant in the semiconductor industry, the Company's business is subject to risks beyond its control, such as instability of foreign economies and governments and changes in law and politics affecting trade and investment.

REPORT OF
INDEPENDENT ACCOUNTANTS SGS-THOMSON Microelectronics N.V.

TO THE SUPERVISORY BOARD AND SHAREHOLDERS OF SGS-THOMSON MICROELECTRONICS N.V.

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of income, of cash flows and of changes in shareholders' equity present fairly, in all material respects, the financial position of SGS-THOMSON Microelectronics N.V. and its subsidiaries at December 31, 1996, and the results of their operations and their cash flows for the year in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the opinion expressed above. The consolidated financial statements of SGS-THOMSON Microelectronics N.V.for the two years ended December 31, 1995 were audited by other independent accountants whose report dated January 26, 1996 expressed an unqualified opinion on those statements.

PRICE WATERHOUSE NEDERLAND BV
Amsterdam, The Netherlands
January 17, 1997

SUPERVISORY BOARD
AND EXECUTIVE OFFICERS

SUPERVISORY BOARD(1)

Bruno Steve, Chairman
Chief Executive Officer -- Finmeccanica

Jean-Pierre Noblanc, Vice Chairman
General Manager, Components Sector -- CEA Industrie

Remy Dullieux
"Directeur Executif," Northern and Eastern Regions -- France Telecom

Riccardo Gallo
Associate Professor of Industrial Economics, Engineering Faculty,
"La Sapienza" University -- Rome

Alessandro Ovi
Chief Executive Officer -- Technitel S.p.A.

Henri Starck
Advisor to the President -- Thomson-CSF

Robert White
Professor and Department Head -- Carnegie Mellon University

(1) Reflects the composition of the Supervisory Board following the Annual General Meeting held on May 5, 1997.

EXECUTIVE OFFICERS

Pasquale Pistorio
President and Chief Executive Officer

Laurent Bosson
Corporate Vice President, Front-end Manufacturing

Carlo Bozotti
Corporate Vice President, European and Headquarters Region

Salvatore Castorina
Corporate Vice President, Discrete and Standard ICs Group

Murray Duffin
Corporate Vice President, Total Quality Management

Alain Dutheil
Corporate Vice President,
Strategic Planning and Human Resources

Ennio Filauro
Corporate Vice President, Memory Products Group

Philippe Geyres
Corporate Vice President, Programmable Products Group

Maurizio Ghirga
Corporate Vice President, Chief Financial Officer

Jean Claude Marquet
Corporate Vice President, Asia/Pacific Region

Pier Angelo Martinotti
Corporate Vice President, New Ventures Group

Joel Monnier
Corporate Vice President,
Central Research and Development

Piero Mosconi
Corporate Vice President, Treasurer

Richard Pieranunzi
Corporate Vice President, Americas Region

Aldo Romano

Corporate Vice President, Dedicated Products Group

Giordano Seragnoli
Corporate Vice President,
Back-end Manufacturing and Subsystems Products Group

Keizo Shibata
Corporate Vice President, Japan Region

Photomontages: Jeff Brice
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CORPORATE INFORMATION

PRINCIPAL EXECUTIVE OFFICE

SGS-THOMSON Microelectronics
Technoparc du Pays de Gex -- B.P. 112
165, Rue Edouard Branly
01637 St. Genis Pouilly Cedex -- France
Telephone: 33-4-50-40-26-40
http://www.st.com

STOCK LISTING

The common stock of SGS-THOMSON Microelectronics N.V. is traded on the New York Stock Exchange under the symbol "STM". The common stock is also listed on the Bourse de Paris and quoted on SEAQ International.

TRANSFER AGENT AND REGISTRAR

For questions about transfer procedures or other stock account matters, please contact:

Bank of New York
(for Shares of New York Registry)
Telephone: 212-815-5800 or 1-800-524-4458
Netherlands Management Company B.V.
(for Shares of Dutch Registry)
Telephone: 31-20-622-9726

INVESTOR RELATIONS

For copies of financial reports and other investor information, please contact:
Francois Guibert, Group Vice President -- Business Planning and Development, at the Principal Executive Office noted above, or call 33-4-50-40-25-94. In the U.S., you may call 214-466-7699.

SENIOR MANAGEMENT TEAM

[PHOTO]

Products Group

Aldo Romano
Corporate Vice President, Dedicated Products Group

Philippe Geyres
Corporate Vice President, Programmable Products Group

Pier Angelo Martinotti
Corporate Vice President, New Ventures Group

Ennio Filauro
Corporate Vice President, Memory Products Group

Salvatore Castorina
Corporate Vice President, Discrete and Standard ICs Group

REGIONAL

Richard Pieranunzi
Corporate Vice President, Americas Region

Carlo Bozotti
Corporate Vice President, European and Headquarters Region

Keizo Shibata
Corporate Vice President, Japan Region

Jean-Claude Marquet
Corporate Vice President, Asia Pacific Region

[PHOTO]

STAFF FUNCTIONS

Piero Mosconi
Corporate Vice President, Treasurer

Alain Dutheil
Corporate Vice President, Strategic Planning and Human Resources

Maurizio Ghirga
Corporate Vice President, Chief Financial Officer

Murray Duffin
Corporate Vice President, Total Quality and Environmental Management

CENTRAL FUNCTIONS

Laurent Bosson
Corporate Vice President, Front-end Manufacturing

Joel Monnier
Corporate Vice President, Central Research and Development

Giordano Seragnoli
Corporate Vice President, Back-end Manufacturing and Subsystems Products Group

Exhibit 23

Consents of Independent Accountants

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Prospectus constituting part of the Registration Statements on Form S-8 (No. 33-80797, No. 33-90616, No. 333-06390 and No. 333-06962) of our report dated January 17, 1997 appearing on page 59 of the Annual Report to Shareholders of SGS-Thomson Microelectronics NV for the year ended December 31, 1996 listed under Item 19(a) of SGS-Thomson Microelectronics NV's Annual Report on Form 20-F. We also consent to the application of such report to the Financial Statement Schedule for the year ended December 31, 1996 listed under Item 19(a) of SGS-Thomson Microelectronics NV's Annual Report on Form 20-F when such schedule is read in conjunction with the financial statements referred to in our report. The audit referred to in such report also included this schedule.

PRICE WATERHOUSE NEDERLAND BV

Amsterdam, The Netherlands
June 25, 1997

"As independent public accountants, we hereby consent to the use of our reports (and to all references to our Firm) included in or made a part of this registration statement."

Amsterdam, The Netherlands
June 25, 1997 Arthur Andersen & Co.