

THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

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THE WALL STREET TRANSCRIPT

CEO/COMPANY INTERVIEW

PAUL CHANG
Sunrise Telecom, Inc.

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Sunrise Telecom, Inc. (SRTI)



PAUL CHANG co-founded Sunrise Telecom, Inc., in October 1991 and has served as Chief Executive Officer, President and Chairman since that time. From 1984 to 1991, Mr. Chang was employed as Engineering Supervisor for the Wiltron division of Anritsu Corporation, a manufacturer of communications test equipment. Mr. Chang holds an MS in Electrical Engineering from the University of Kansas at Lawrence and a BS in Physics from Tunghai University in Taiwan.

SECTOR – COMMUNICATIONS EQUIPMENT (MAD243) TWST: Could we start out with a little history and a quick overview of Sunrise Telecom?

Mr. Chang: Sunrise Telecom was started in October 1991. The focus is on manufacturing verification tools for the telecom industry.

TWST: What do you mean by “verification tools”?

Mr. Chang: “Verification tools” is another name for test equipment. Basically, we make tools to help technicians in the telecom and cable companies to install, maintain and troubleshoot their telephone and cable networks. The technicians use our tools to make sure their network is verified properly before service is turned over to their customers. Also, when customers respond that there is a problem with their service, the service provider’s technician will use our tools to help them to identify

where the problem is, isolate the location of the problem in the last mile of the network, and fix the problem.

TWST: Typically, who is the customer here? Is it the telephone company?

Mr. Chang: Generally speaking, the telephone companies and cable companies worldwide, those are the major users of our products. Of course, there are equipment manufacturers who use our tools in their R&D labs or on their manufacturing floor to help them to verify the accuracy of their development or qualify or verify their manufacturing process with the help of our tools.

TWST: Why would these companies come to you for these tools rather

than developing the tools themselves?

Mr. Chang: In the telecom industry there is just a certain group of companies developing

Highlights

Sunrise Telecom is a leading manufacturer of verification tools for the telecommunications industry. CEO Paul Chang says the company makes the tools to help technicians install, maintain and troubleshoot telephone and cable networks. The areas that Sunrise Telecom specializes in include broadband access technologies, DSL, fiber optics and cable modems, and it focuses on customer drive applications and in making handheld products. Sunrise is a very cost-sensitive company, which is how it maintains its profitability. He says that the good thing about making verification tool equipment is that this business may slow down but it will never disappear. Because Sunrise has diversified into many areas, if a technology like DSL slows down, Sunrise still has fiber optics and cable modem revenue growth to keep it profitable.

test and measurement equipment. Our customers in the transmission service business are focused on delivering services and rely on companies like Sunrise to provide them tools to create efficiencies in the deployment of their broadband access services. Other customers that manufacture transmission equipment, like Cisco or Lucent Technologies, prefer to concentrate on developing their revenue producing product lines, which is making switchers or routers, rather than focus on developing test equipment.

TWST: How big is the market that you're addressing?

Mr. Chang: The verification tool market, we guesstimate, globally is about \$5 billion. The areas we specialize in — we specialize in the broadband access technologies, DSL, fiber-optics or cable modem area — is estimated at about \$1.5-\$1.8 billion range.

TWST: Is that market growing?

Mr. Chang: Broadband access is growing compared to other technology sectors.

TWST: Who are you competing with in this space?

Mr. Chang: There are two main competitors: one is Agilent, the biggest manufacturer in the world; the second one is called Acterna, which is a merger of the former TTC and WWG.

TWST: What do you do differently, or better than what they're doing today?

Mr. Chang: They make good products. But we specialize in the handheld products and focus on customer driven applications. We listen to our customers, so we develop and deliver the products and applications they need. So the user-friendliness and the willingness to listen to customers' demands are the key factors that help us expand our long-term customer relationships with our blue chip customer base.

TWST: So that's what sets you apart. Essentially, you're making the same kinds of products.

Mr. Chang: Some of the product features are similar. It's just the form factor and customer driven applications we provide in our package that makes a big difference. For example (I don't know how much you know about fiber optics), a few companies out there are making fiber-optic testers, but they are addressing only up to the bit level, so the customer can complete bit error rate testing (BERT), but many of our competitors do not focus on access technologies down through the edge of the fiber-optic network, whereas in our test sets, we are not only testing the bit error rate test that are carried on the fiber-optic network, but we're also verifying the services that are on the network. This is one example of an application Sunrise provides that differentiates us from the competition.

TWST: So that's a competitive advantage.

Mr. Chang: Yes, and in addition, we are small and price-sensitive competitors.

TWST: Are you the smallest of the three?

Mr. Chang: If you are asking about the compact size and light weight of our hand held test equipment, yes, we generally hold the smallest test equipment title in the worldwide market. Normally, when you're talking "small and powerful," you're talking about Sunrise Telecom equipment.

TWST: Is there a place for somebody your size in this market?

Mr. Chang: By my size, do you mean the equipment or the company size?

TWST: The company size?

Mr. Chang: Of course there are a lot of opportunities you can seek out there. I wouldn't say we dominate or monopolize the market. Somebody else can come in, of course.

Investors Brief



Ticker (exchange)	SRTI (NASDAQ)
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Corporate Headquarters

22 Great Oaks
San Jose, CA 95119

Phone: (408) 363-8000

Fax: (408) 363-8313

Web: sunrisetelecom.com

Corporate Officers

Paul Ker-Chin Chang
President & CEO

Paul A. Marshall
VP & COO

Peter L. Eidelman
CFO

Investor Relations Contact

Peter L. Eidelman

Corporate Business Description

Sunrise Telecom was founded in October of 1991 to make portable test equipment faster, simpler, more powerful, and more affordable. The company is leading the telecom portable test equipment industry forward through innovations like the use of a graphical interface for presenting information on circuit status and feature upgrades accomplished by means of a software memory card.

PRODUCT HISTORY

The company's first product, the SunSet T1, was introduced in June of 1992. The set is a first-rate T1 test set by traditional measures in addition to providing a number of unique, user-friendly features. The SunSet E1, introduced in October 1992, extended the same advantages into the CCITT market.

Versatility is the hallmark of the company's third product, the SunSet T3. Introduced in July of 1994, this product replaces two common 15-pound pieces of test equipment with a single 2.8-pound handheld set, and is unrivaled in its complement of DS3 and DS1 signal interfaces. In August 1994, the company debuted the SunSet E10; this groundbreaking unit offers a combination of datacom, 2.048 Mbps transmission, and telecom capabilities in a handheld instrument. Its features include a broad range of datacom interfaces and full duplex drop and insert.

In December 1995, the SunSet T10 was introduced. This unit packs the functionality of up to seven separate analyzers in a handheld package, including testing for 1.544 Mbps, ISDN PRI, SS#7, Datacom, DDS, VF, and Telephone Handset applications. The 2.048 Mbps equivalent, the SunSet E20, was introduced in 1999. This powerful unit verifies and troubleshoots line signaling and protocol problems. Its rich set of capabilities include GSM, SS#7, and ISDN PRI analysis.

Introduced in June 1998, the SunSet xDSL has been highly successful. The SunSet xDSL is the world's first field test set which can properly qualify copper lines, for a variety of DSL applications. Utilizing actual DSL line codes and providing a broad spectrum of physical impairment measurement capabilities, the SunSet xDSL supports verification and troubleshooting of DSL circuits. Its modular format allows versatility that enables the test set to evolve with the service provider's network. Currently, plug-in modules are

supported for ADSL, IDSL, SDSL, HDSL, Datacom, and VF TMS, with future offerings in development.

The most recent Sunrise Telecom products, the SunSet OCx, introduced in late 1999, and the SunSet SDH, introduced in 2000, start a new generation in optical field testing. These powerful system verification units analyze low-rate electrical through high-rate fiber optics SONET and SDH lines, respectively. SDH and SONET access is available at both electrical and optical interfaces, providing for in-depth analysis. In addition to transmission testing, the SunSet OCx and the SunSet SDH offer advanced protocol analysis features, including ATM testing. These new products are keeping Sunrise Telecom a step ahead.

Sunrise products have found broad acceptance in domestic and international markets alike with a customer base which includes local exchange carriers, cellular exchange operators, private network operators, and telecom equipment manufacturers. Telephone companies on five continents have standardized on the company's products.

Sunrise Telecom Reports Fourth Quarter and Year 2000 Financial Results

"The year 2000, our first year as a public company, was a year of extraordinary achievement for Sunrise Telecom, in virtually every area. We crossed the \$100 million mark in revenues, achieved solid revenue growth in all regions and product lines, and recorded record earnings per share," said Paul Chang, President and Chief Executive Officer of Sunrise Telecom Incorporated. "Our unique testing solutions and our successful penetration of new markets enabled us to continue to grow our business in 2000."

"We are pleased to report the fourth quarter of 2000 marks our 33rd consecutive quarter of profitability," added Peter Eidelman, Sunrise Telecom's Chief Financial Officer. "We diversified our product offerings to address the emerging broadband applications, while maintaining our historical trends of solid financial fundamentals."

Highlights in the Year 2000 include:

- Initial public offering completed in July 2000 with net proceeds to Sunrise Telecom from the offering totaling approximately \$51.6 million.
- Entrance into the Fiber Optics market with strong acceptance for the SunSet OCx and SunSet SDH fiber optics products. OC-48 rate announced in fourth quarter.
- Expansion in the Cable TV market with field trials for the CM-1000 cable modem tester among major cable modem service providers with shipments in the fourth quarter. Additionally, in January 2001, we completed the acquisition of Avantron Technologies, further expanding our Cable TV product offerings.
- Entrance into the Signaling / Protocol Analyzer market with the acquisition of Ghepardo products and introduction of added features and functionality to respond to the emerging Voice over IP requirements.

TWST: Are there any barriers to someone else coming in?

Mr. Chang: You know, making telecom hand held verification equipment, being the first with a three pound test set — we started in 1991 making the first handheld T1 test set — throughout the past almost 10 years we have accumulated a tremendous amount of technology in Sunrise Telecom's lab to produce something small and functionally strong, and if somebody wants to catch up, it probably would take some time. For example, Agilent and Acterna want to get into the handheld market, and they can announce they are making very small portable products, which weigh about double what ours weigh — that's what they have today — so we are still producing the smallest, the lightest in a powerful platform.

There is also a tremendous cost advantage. Let me put it this way, when you make a machine smaller, of course there is some cost you can save compared to making big products.

TWST: As we look out over the next two or three years, what changes do you see taking place in this market that you're going to have to adjust to?

Mr. Chang: You know, the market today, we're looking at a picture that's quite vague, and the entire telecom market seems to be a little bit uncertain. But in reality, communication and the Internet will not stop. People — customers, both in their homes and in any company — still demand broadband access and they want to have more bandwidth to allow them to use it. I would say that broadband access is going to be the key market grower down the road two or three years, so that's what we're focusing on, broadband access technologies.

TWST: So while we may have a little stumble in here because of the general economy, you think long term it will be fine.

Mr. Chang: Talking about forward-looking statements here, I don't believe the telecom market is stumbling, just resetting itself to digest the last couple years. Demand is still out there for high speed access. We can see that DSL in the USA is probably going to slow down a bit, but if you go to the international market, especially Asia and a few European countries, demand remains strong. In the US and globally, fiber optics and cable remains strong. The long term outlook is good for broadband access services and we provide the tools that allow the efficient and effective deployment of these services.

TWST: What's your strategy going to be over the next year or two to make sure you maintain or improve your market share?

Mr. Chang: Again, we're saying that the market we're in is about a \$4-\$5 billion market. Sunrise Telecom, as of the year 2000 we were about \$113 million, so we're still very small and there are still a lot of areas we can go. But our strategy is still going to be very focused on broadband access. We have leading edge products to enable the cable modem; in fiber optics we continue to introduce new applications for verifying the deployment of fiber optics and the services that are delivered over fiber; in DSL we still hold the leadership position, probably holding more than 60% of the field verification market domestically, and probably worldwide a very large percentage of the market as well, and we continue to deliver new applications for other wire line access technologies.

In addition, we're developing into other product areas. As I said before, we have been focusing on the portable, handheld area. Now we're diversifying our efforts into the larger systems. Those will be for the manufacturers and R&D labs to use, and that by itself is a huge market sector we are currently trying to get into.

TWST: Why weren't you in it before? You didn't have the capability or the time or both?

Mr. Chang: Getting into the R&D lab and the manufacturers is a different kind of business. In the handheld area you're generally talking about one technician, one test set, and you don't need to worry about other guys, as you do in a network environment. When you're in the R&D lab, generally people want to have larger machines which are a little more powerful, be able to hook it up to the network to do remote testing and resource sharing, those kinds of applications, applications that we didn't have in our hand held products. Those applications are not possible in a handheld because of the horsepower needed behind the CPU to run the whole process. But now we're getting into this market area. As you can see, we have protocol analyzers in the voice-over IP areas; we have spectrum analyzers in the cable industry as well. We are expanding our focus.

TWST: What are analysts expecting you to do over the next two or three years?

Mr. Chang: To tell you the truth, I don't really know what the specific analysts are expecting, but they all publish reports with their expectations.

Over the long term they all are looking for stable growth — I wouldn't say 50% or 100% growth a year, but for sure it's long-term stable growth analysts are interested in. We have a long-term history of maintaining the company to be profitable, with very nice gross margins, and profitable for close to nine years now. Cash flow has been positive and we have no significant interest bearing debt. Our balance sheet is quite strong.

TWST: Can you improve that profit margin?

Mr. Chang: That's something we're working on very hard. Actually to go into the R&D lab environment, to be more software-intensive will

improve the profit margin. That's something we're interested in.

TWST: So there are some opportunities there at this time.

Mr. Chang: There are a lot of opportunities. If this voice-over IP application is coming up, as we expect, that is going to be a very software-intensive task, and we can have a pretty good profit margin on those kinds of products.

TWST: Will the growth be internal, or would you be looking for acquisitions?

Mr. Chang: Acquisitions have been part of our diversification strategy. We just finished one acquisition about three months ago, Aventron Technologies in the cable sector.

If there is a technology that we do not have in our San Jose headquarters or within our divisions and it is something that we are interested in, we will evaluate the opportunity.

TWST: Is size an issue in terms of what you would look at?

Mr. Chang: We're basically looking for technologies. We're not looking to acquire revenue in an acquisition. So when we buy a company, normally the size of the acquisition is pretty small, say, within the \$20 million range. Then after we merge the company into the Sunrise Telecom family, we will help them to grow their market share with our sales channel and marketing group.

TWST: Do you have the management team in place that you need at this point?

Mr. Chang: Oh, yes, we have a very good team. Paul Marshall and I have been partners since 1991. We have a crew of teams helping us out. We have very good, experienced people in our R&D lab and marketing department. Our CFO, Peter Eidelman, came from a big six accounting firm and an international large company before joining Sunrise in 1997; now he's helping us out on the fi-

nancial side. We're doing very well. It's a very friendly teamwork environment here.

TWST: Do you have the balance sheet that you need?

Mr. Chang: Oh, yes.

TWST: How much cash did you have at the end of the last quarter that you reported?

Mr. Chang: I believe cash and short-term investments at the end of the first quarter of 2001 was approximately \$40-plus million.

TWST: You're solidly profitable. Are you supporting your capital-spending needs internally?

Mr. Chang: Operating capital spending, yes.

TWST: Is there any big capital spending planned at this point, or do you have what you need?

Mr. Chang: We just finished building our new facility about two miles away from our old facility. Other than that, we don't have any major spending plans. No, we don't see anything in the short term.

TWST: Do you make your own equipment, or are you outsourcing?

Mr. Chang: Half and half. Normally, we buy the inventories, we kit up the raw components and provide to a contract assembly house to do the sub-assembly and bring the sub-assembled parts back into Sunrise Telecom; we then do an assembly and final test before we ship to the customer. So it's a hybrid model. We believe that's the best way we can come toward our quality standard. The response time is quick, say, if during one manufacturing run process we see a low yield issue on the production floor, we can correct it real quick and then fix the process so that the next round we will not have a similar problem.

TWST: What's the risk here? What can go wrong — other than a general economic slowdown?

Mr. Chang: I guess that's the current risk. If the general economy is going to slow down quite a bit and people stop making phone calls, and using e-mail, then broad band access demand may slow down. We believe broadband demand is strong.

TWST: How about, if the phone companies — as it seems — are running out of money to invest in new infrastructure? Is that going to hurt you?

Mr. Chang: You have to put it this way. When the phone companies spend a lot of money building infrastructures — and the money spent on transmission equipment, like what they have already installed and continue to purchase from Cisco, Lucent and Northern Telecom's equipment — when they're building and installing the infrastructure they need the verification tools from us to help them to build it, and when the infrastructure is built they're still going to need our tools to bring those services to their customers so that they can generate revenue. So the spending on verification equipment will never stop. It is always needed. It's a tool kit. That's what's so good about the verification tool equipment market, that this type of business will never die, never go to zero — it may slow down a little bit, but it will never totally disappear.

Another thing is that we diversify the business into many areas — into the international market and into the broadband access area — so that if one USA economy is slowing down, internationally eventually it will pick up to cover up the holes we have over here; or if one technology, say, DSL, is slowing down in the US, we still have fiber optics and cable modem revenue growth.

TWST: How do you feel about the value the market is currently putting on your company?

Mr. Chang: Of course, I think it's low. Sunrise should probably be worth a lot more than the current market value. But then, looking at the competition that we have — Agilent, Acterna, Digital Lightwave — I guess everybody's in the same boat, anyway!

TWST: Are you just being affected by general industry conditions or is there some particular concern that investors have about you?

Mr. Chang: I think it's just a general thing about the market sector we're in, people thinking that we're in the telecom industry and that since the entire thing is slowing down the test equipment industry will be slowing down. There is some truth behind that, but somehow it doesn't really reflect the value of a company like Sunrise.

TWST: When you talk to investors, what key questions are you getting from them?

Mr. Chang: How can you maintain the growth? How can you maintain the profitability? They're typical questions like that, not really difficult questions. How do we maintain the growth when diversifying is our goal? We diversify into two sectors: one is the international market; also different product offerings. So we bring out more products to more customers as a way to maintain growth.

How can you stay profitable? Sunrise has always been a very cost-sensitive company. That's why we maintain such high gross margins and profit. We are very careful about capital expenditures. We're also very careful about doing acquisitions — we're not throwing money out there into somebody else's hand and getting nothing back. We're very careful about spending the money we have. So that's how we can maintain the profitability.

TWST: Thank you. (TM)

PAUL CHANG

President, CEO & Chairman

Sunrise Telecom, Inc.

22 Great Oaks Blvd.

San Jose, CA 95119

(408) 363-8000

(408) 363-8313 - FAX

www.sunrisetelecom.com

e-mail: info@sunrisetelecom.com

Each Executive who is the featured subject of a TWST Interview is offered the opportunity to include an Investors Brief or other highlight material to be provided and sponsored by and for the company. This Interview with Paul Chang, President, CEO & Chairman, Sunrise Telecom, Inc., is accompanied by an Investors Brief containing corporate information.