SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 1997

Commission File Number: 0-21393

SEACHANGE INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

Delaware	04-3197974
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

124 Acton Street, Maynard, MA 01754
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (978) 897-0100

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:

COMMON STOCK, $.01 PAR VALUE

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 preceeding 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [_].

As of March 23, 1998 the aggregate market value of the voting stock held by non-affiliates of the registrant, based upon the closing price for the registrant's Common Stock on the Nasdaq National Market on such date was $50,401,890. The number of shares of the registrant's Common Stock outstanding as of the close of business on March 23, 1998 was 13,595,019.

DOCUMENTS INCORPORATED BY REFERENCE:
Portions of the definitive Proxy Statement in connection with the Annual Meeting of Stockholders to be held on or about May 21, 1998 to be filed pusuant to Regulation 14A are incorporated by reference into Part III of this Form 10-K.

PART I

This Annual Report on Form 10-K includes certain statements of a forward-looking nature which reflect the Company's current views relating to future events or the future financial performance of the Company. These forward-looking statements are only predictions and are subject to risks and uncertainties, particularly the matters set forth in "Certain Risk Factors" below, which could cause actual events or results to differ materially from historical results or those indicated by such forward-looking statements.

ITEM 1. BUSINESS

SeaChange International, Inc. ("SeaChange"or the "Company") provides products to digitally manage, store and distribute digital video for television operators and telecommunications companies. The Company's products utilize its proprietary distributed application software and standard industry components to automate the management and distribution of video streams including advertisements, movies, news and other video programming requiring precise, accurate and continuous execution. The Company's digital video products are designed to provide higher image quality and to be more reliable, easier to use and less expensive than video tape-based systems. In addition, SeaChange's products enable its customers to increase revenues by offering more targeted services such as geography-specific spot advertising and video-on-demand movies.

SeaChange's products address a number of specific markets. The SeaChange SPOT System is the leading digital advertisement insertion system for the multichannel television market in terms of installations in the United States, based on currently available industry sources and the Company's internal data. The SeaChange SPOT System encodes analog video forms such as advertisements and

news, stores them in remote or local digital libraries, and inserts them automatically into television network streams. The SPOT System provides high run-rate accuracy and video image quality, permits geographic and demographic specificity of advertisements and reduces operating costs. The Company also sells two variants of this product-SPOT PRO which provides ad insertion capability to small to mid-size television stations, and the SeaChange SPOT Long Form System, a long-form video storage and delivery product for cable television operators and telecommunications companies. The Company also sells the SeaChange Movie System, which provides long-form video storage and delivery for the pay-per-view movie markets and the SeaChange GuestServe System for delivering video-on-demand and other services to hotels. The SeaChange Advertising Management Software operates in conjunction with the SeaChange SPOT System to automate and simplify complex sales, scheduling and billing processes for the multichannel television market. The Company also sells its Video Server 100, which is designed to store and distribute video streams of various lengths, and MediaCluster, SeaChange's proprietary software technology that enables multiple Video Server 100s to operate together as an integrated video server, to systems integrators and value added resellers ("VARs"). In addition, the Company is developing its Broadcast MediaCluster systems for the broadcast television industry for storage, archiving, on-air playback of advertising and other video programming. The Company is also developing its video-on-demand system to allow cable television and other telecommunication companies to offer interactive services to its subscribers.

The Company was incorporated in Delaware in July 1993.

INDUSTRY BACKGROUND

Television operators, the largest users of professional quality video, historically have relied on videotape technology for the storage and distribution of video streams. These systems, which use video tapes as the primary mechanism for the storage and distribution of video, have substantial limitations. Video tapes and their associated playback mechanisms are subject to mechanical failure and generational loss of video quality. Tape-based systems also require significant manual intervention, which makes them expensive and cumbersome to operate and also limits their flexibility for programming changes. Finally, video tapes are bulky and have limited storage capacity.

Over the past decade, the limitations of video tape-based systems have become increasingly apparent. Changes in government regulation and increased competition have forced television operators to seek new revenue sources and reduce costs. In addition, television operators are increasingly seeking to offer new and enhanced video services while simultaneously improving the efficiency of their operations. While video tape-based systems are sufficient for some traditional applications, they do not meet the performance and cost requirements of these new, targeted applications.

Cable Television Operators & Telecommunications Companies

According to industry sources, there are approximately 12,000 cable systems currently in the United States, serving over 70 million households. In 1997, 97% of all cable systems provided over 30 channels of programming to their subscribers. Because cable television programming is sent over broadband lines, operators can segment and target their programming to viewers in selected geographies. In addition, the continuing growth in cable television's multiple specialized programming networks, such as CNN, MTV and ESPN and other networks such as Black Entertainment Television, the Discovery Channel and Nickelodeon, allow advertisers to target viewers in selected demographic profiles.

Despite this advantage over television broadcasters, cable television operators historically have not realized advertising revenues in proportion to their share of television viewers. According to industry sources, in 1997, 46% of all television viewers were watching cable networks, yet cable television advertising revenue accounted for only 19.5% of the total television advertising revenue. In addition, advertising represents the major source of revenue for television broadcasters, while most cable television operators derive less than 5% of their gross revenue from advertising. The limitations of video tape-based technology are a major factor which has prevented cable television operators from historically exploiting their advantages over television broadcasters. These systems are difficult to manage in multichannel and multi-zone environments, resulting in relatively poor video insertion accuracy and high operating costs.

Video-on-demand represents a new opportunity for cable television operators. Increased channel capacity through the installation of fiber optic cables is providing many cable television operators with the capacity to offer video-on-demand programming capability to hotels and apartments using existing analog set-top technology. However, wide deployment to residential subscribers is not as practical or feasible with existing analog technology. The initial deployment of the digital set-top which is necessary to making wide scale video-on-demand practical, is expected in 1998.

The recent deregulation of the United States telecommunications industry has lowered the legal barriers to entry for telecommunications companies to enter the multichannel video delivery market. Telecommunications companies are attempting to capitalize on the new growth opportunities by acquiring existing cable television operators and by leveraging their existing telephony networks to establish new multichannel video delivery operations. However, telecommunications companies face the same limitations as cable television operators in cost-effectively offering targeted, value-added services with analog tape-based systems.

Increased demand for video and audio content over the Internet will require a substantial increase in storage capacity and bandwidth over time. The Company believes that cable television operators and telecommunications companies will play an integral role in providing these broadband Internet applications. The Company also believes that in order to offer high quality video applications over the Internet, cable television operators and telecommunications companies will need storage and distribution products capable of complex management and scheduling of video data streams.

Television Broadcasters

The more than 1,500 broadcast stations in the United States, including network affiliates and independent stations, face many of the same technological issues as cable television operators. Additionally, television broadcasters rely on advertising for nearly all of their revenue and require high advertisement run-rate reliability and image quality. To date, television broadcasters have utilized tape-based systems with robotic libraries, which are cumbersome and require high levels of maintenance and manual intervention to ensure that the needed performance requirements are met. Also, the video tapes in these systems need to be replaced frequently due to repeated use.

In addition, many broadcasters are contemplating the use of the cable infrastructure for the delivery of geography-specific advertising. These broadcasters will insert targeted advertising into their television signals and distribute them directly, often via microwave, to cable operators' distribution sites. If this application develops, television operators will require video storage and delivery systems that can effectively manage and deliver multiple television signals to targeted markets. In late 1998 several television stations in major markets are expected to begin broadcasting Digital Television (DTV) signals. The advent of DTV is expected to increase the demand for digital storage, retrieval, and distribution technology.

THE SEACHANGE SOLUTION

SeaChange develops, markets and supports digital video solutions designed to enhance its customers' ability to store, retrieve, manage and distribute short- and long-form video streams, including advertisements, movies, news updates and other video programming requiring precise, accurate and continuous execution. The Company's solutions are based on five core areas of functionality: (i) real-time conversion of analog video into digital video format; (ii) storage and retrieval of video content to and from digital libraries; (iii) scheduled distribution of video streams between digital libraries via local and wide area data networks; (iv) delivery of video streams over single and multiple channels; and (v) management of video sales, scheduling, billing and execution of related business transactions.

SeaChange uses these core capabilities to provide solutions to a number of commercial markets. The Company's products are designed to provide a consistent set of features and benefits, including:

Viewer Targeting. The Company's digital video products enable television operators to efficiently target viewers in specific demographic or geographic groups. The ability to target selected viewers enables television operators to increase revenues by offering more targeted services. The SeaChange SPOT System offers this

capability to television operators, while the SeaChange Movie System makes it possible for television operators to offer video-on-demand movies to individual hotel rooms or apartments.

Cost Reduction. The Company's products are designed to provide its customers operating cost reductions as compared to analog tape-based systems due to, among other things, the elimination of video tapes and their storage and lower operating personnel requirements. The Company is also able to price its products on a competitive basis by using standard operating systems and components. The Company believes that the combination of competitive pricing of its products and reductions in the operating costs of its customers results in attractive pay-back periods on customers' initial capital outlay for the Company's products.

Scalability. The Company's products are scalable to the needs of a particular cable television operator or television broadcaster whether operating in a single channel system concentrated in one specific zone or a

system with hundreds of channels serving multiple zones and markets. Moreover, the Company's proprietary storage technology enables the scalability of storage of digital video from a few minutes to hundreds of hours of video.

Reliability. The Company's products eliminate the need for traditional mechanical tape-based systems, thereby reducing the likelihood of breakdowns. Furthermore, through the use of redundant components and proprietary storage technology and application software, SeaChange's products are designed to be fault resilient, providing the high reliability required for television operations.

Scheduling Flexibility. The digitizing and storage of video streams allows advertisements, news updates and movies to be inserted on channels in local communities and allows cable television operators to insert or delete video content rapidly. This flexibility enables the provision of services such as video-on-demand movies and provides advertisers and television broadcasters the opportunity to insert new video content on short notice.

Video Image Quality. Because digital video streams do not degrade with playback, image content and quality remain at the original professional level even after multiple airings.

Ease of Use. The Company's products are simple to learn, require less maintenance, and are less personnel intensive than analog systems. Due to their innovative architecture, the Company's products offer a number of features that simplify their use, including remote monitoring and service and automated short- and long-form video distribution.

STRATEGY

SeaChange's objective is to be a leader in the emerging market for the storage, management and distribution of professional quality digital video. The key elements of the Company's strategy are to:

Develop Long-Term Customer Relationships. The Company is focusing its product development, marketing and direct sales efforts on developing long-term customer relationships with cable television operators, telecommunications companies and television broadcasters in the United States and internationally. The Company has formed its customer relationships by providing software-based digital video solutions to address customers' immediate problems, such as advertisement and other short-form video insertion. The Company intends to continue to leverage its customer relationships to offer new, compatible products to meet evolving market needs, such as video-on-demand programming. The Company believes that the fundamental shift from analog to digital video and the growing emphasis on interactive technologies will continue to present opportunities for the Company to develop, market and support its products to both its existing customer base and to customers in additional markets.

Offer Complete Solutions. SeaChange's customers operate complex networks that require the delivery and management of video programming across multiple channels and target zones. SeaChange believes television operators desire complete solutions that integrate all steps of digital video delivery from scheduling to post-air verification and billing. To address these needs, SeaChange provides integrated applications and support services which are more valuable to customers than individual functional products not specifically designed to work together. The Company believes that providing complete solutions has been a significant factor in its success and will be an increasingly important competitive advantage.

Establish and Maintain Technological Leadership Through Software. SeaChange believes its competitive position is dependent in large part on the features and performance of its application and network and storage software. As a result, the Company focuses a majority of its research and development efforts on introducing new software applications and improving its current software. The Company seeks to use standard hardware components wherever possible to maintain its focus on software development.

Provide Superior Customer Service and Support. The Company's products operate in environments where continuous operation is critical. As a result, the Company believes that providing a high level of service and support gives it a competitive advantage and is a differentiating factor in developing key customer relationships. The Company's in-depth industry and application knowledge allows it to better understand the service needs of its customers. As of December 31, 1997, more than 30% of the Company's employees were dedicated to customer service and support, including project design and implementation, installation and training. In addition, using remote diagnostic and communications features embedded in the Company's products, the service organization has the ability to monitor the performance of customer installations and, in most cases, rectify problems remotely. Customers have access to service personnel via 24-hour, seven-day a week telephone support.

PRODUCTS

SeaChange develops digital video products and related applications for the television industry. Its products are marketed to cable television operators, telecommunication companies, television broadcasters, systems integrators and VARs.

SeaChange SPOT System

The SeaChange SPOT System automates the complex process of advertisement insertion across multiple channels and geographic zones for cable television operators and telecommunications companies. Through its proprietary software, the SeaChange SPOT System allows cable television operators to insert local and regional advertisements and other short-form video streams into the time allocated for these video streams by cable television networks such as CNN, MTV, ESPN, Black Entertainment Television, the Discovery Channel and Nickelodeon.

The SeaChange SPOT System is an integrated solution composed of software applications, hardware platforms, data networks and easy to use graphical interfaces. The SeaChange SPOT System is designed to be installed at local cable transmission sites, known as headends, and advertising sales business offices. The SeaChange video insertion process consists of six steps:

Encoding: The process begins with the SeaChange Encoding Station, which is based on SeaChange's proprietary encoding software, where analog-based short- and long-form video is digitized and compressed in real-time using standard MPEG-2 hardware.

Storage: Digital video is then stored in a disk-based video library, capable of storing thousands of spots, where the SeaChange SPOT System organizes, manages and stores these video streams.

Scheduling: SeaChange's scheduling and management software coordinates with the traffic and billing application to determine the designated time slot, channel and geographic zone for each video stream.

Distribution: SeaChange's strategic digital video software then copies the video streams from the master video library and distributes them over the operator's data network to headends, where they are stored in video servers for future play.

Insertion: Following a network cue, the SeaChange video switch module automatically initiates the conversion of video streams to analog and inserts them into the network feed, where they are then seen by television viewers.

Verification: After the video streams run, SeaChange's proprietary software and hardware verifies the content, accuracy, timing and placement of such video streams to facilitate proper customer billing.

SeaChange has developed two additional product offerings, the SeaChange SPOT Long Form System ("the SeaChange SPOT LF System") and the SeaChange SPOT PRO System, that are based on the SeaChange SPOT System technology. The SeaChange SPOT LF System, which employs the same underlying technology and basic functionality of the SeaChange SPOT System, is designed to be a platform for the delivery of long-form video streams in a multichannel environment. The SeaChange SPOT LF System is designed to permit television operators to store, manage and distribute long-form video streams, such as movies, infomercials and other local origination programming. The SeaChange SPOT PRO System, also employs the same underlying technology and basic functionality of the SeaChange SPOT System and is designed to be a platform for the delivery of advertising and other video content in a small to mid-sized television broadcast environment.

The selling price for all SeaChange SPOT Systems ranges from under $100,000 to several million dollars with an average system selling price of approximately $250,000.

SeaChange Advertising Management Software

The SeaChange Advertising Management Software (formerly Traffic and Billing Software) is designed to permit television operators to manage advertising sales, scheduling, packaging and billing operations. This product provides advertising sales executives with: (i) management performance reports; (ii) inventory tracking; and (iii) order entry, billing and accounts receivable management. Advetising Management Software can be integrated with the SeaChange SPOT System and is also compatible with many other advertisement insertion systems currently in use.

Movie and Interactive Products

SeaChange GuestServe System. The SeaChange GuestServe System is a platform for the storage and delivery of long-form video streams, particularly movies and interactive services such as Hotel Checkout. SeaChange had worked together with IPC Interactive Pte. Ltd. (''IPC''), a provider of video-on-demand systems, to integrate IPC's Guestnet system and its related movie programming with the

SeaChange MediaCluster Technology. On December 10, 1997, the Company acquired IPC. The system is designed to permit viewers in hotels and apartments to choose particular movies on demand and also offers a variety of ancillary interactive services, such as hotel checkout and advertisements. SeaChange is marketing the SeaChange GuestServe System featuring movie programming to cable television operators who package these services with their television services and sell to hotels and apartments. The Company is currently developing other interactive services such as Internet Access and Computer Games.

The integrated system consists of user interfaces and application hardware and software, including set-top boxes and remote control devices, and SeaChange's MediaCluster technology and software architecture for the delivery and storage of movies. The video servers are installed at the cable headend and the video is delivered over a dedicated fiber optic line. The integrated system is designed to provide cable television operators with a new source of revenue and a competitive advantage over the encroaching services of direct broadcast satellite companies. The SeaChange GuestServe System has an average selling price of approximately $1,000,000.

The SeaChange Movie System. The SeaChange Movie System provides cable television operators, pay-per-view (PPV) movie service providers and Direct-to-Home (DTH) providers with capability to originate multiple PPV movie channels or any other scheduled video programming. The Movie System includes SeaChange MediaCluster technology for storage and delivery of the video programming as well as an MPEG-2 encoder for capturing movies from video tape, and scheduling software and hardware to enable creating programming schedules for the PPV channels. This system includes fault resiliency in both the video server technology and scheduling technology so as to insure the highest levels of up time. The SeaChange Movie System has an average selling price of approximately $500,000.

Interactive Television. SeaChange is developing technology and product for the Interactive Television (VOD) market. This product will work over two way cable television systems with digital set-top boxes and will be based on SeaChange's MediaCluster technology.

Broadcast Television Products

SeaChange plans to introduce products to the broadcast market in 1998.

SeaChange Broadcast MediaCluster. The SeaChange Broadcast MediaCluster System is designed to provide high quality, MPEG-2 4:2:2 based video storage and playback for use with automation systems in broadcast television stations. This product is intended to replace on-air tape decks used to store and play back advertising from video tape cart systems and, in some cases, to replace the cart systems themselves. The SeaChange Broadcast MediaCluster is designed for customers in larger broadcast television markets which use station automation systems or to smaller markets using control software included with the system.

The System is designed to simultaneously record, encode, store to a disk and play video content, using SeaChange designed MPEG-2 4:2:2 compression and decompression hardware. This product is designed to seamlessly integrate into television broadcasters' current tape-based operations and meet the high performance requirements of television broadcasters.

OEM Products

Video Server 100 (and variants). The Video Server 100, which is the Company's second generation video server, is designed to store and distribute video streams of various lengths. The Video Server 100 together with the MediaCluster provides the base technology for all of SeaChange's digital video products. The Video Server 100 is offered to systems integrators and VARs as a platform for the storage and delivery of primarily short-form video in a wide range of applications.

The Video Server 100 provides custom power and packaging and software for use in professional video applications. It has features such as RAID and a redundant power supply to enable the continuous uninterrupted airing of video. The Video Server 100 uses industry standard components, which differentiates it from various video servers based on proprietary processors and specialized hardware components and operating systems.

MediaCluster. MediaCluster is SeaChange's proprietary software technology that enables multiple Video Server 100s to operate together as an integrated video server. While the Video Server 100 is the base technology for short-form video applications, MediaCluster serves as the base technology for primarily long-form video applications.

Through its software architecture, MediaCluster can join multiple SeaChange Video Servers to support large-scale applications by storing large amounts of video data and delivering multiple video streams, with no single point of failure in the system. The Company currently has a patent application pending for its MediaCluster technology.

The Company established a subsidiary, SeaChange Systems, Inc., at its Greenville, New Hampshire location for the manufacture, development and OEM sale of the Video Server 100 and MediaCluster products. Certain employees of the Company and subsidiary have been granted stock options to acquire up to a 20% interest in the subsidiary and the Company owns the remaining interest in the subsidiary. The Company intends that the subsidiary will license the necessary technology from the Company and will manufacture these products on a contract basis for the Company. The subsidiary will have the right to sell these products to OEM customers that do not compete with the Company. The Company intends to provide administrative and management services and, at least initially, selling and marketing and customer support services, to the subsidiary on a negotiated fee basis. It is expected that the subsidiary will conduct research and development on video server-based products, including the Video Server 100 and MediaCluster products, and will license all developments to the Company on a royalty-free basis. It is intended that after December, 1999, the Company will have the right, but not the obligation, to acquire the interest from the employees at fair market value.

CUSTOMER SERVICE AND SUPPORT

The Company installs, maintains and supports its products in North America, Asia, South America and Europe. Annual maintenance contracts are generally required for the first year of a customer's use of the Company's products and customers are billed for the initial maintenance fee at the time of the placement of the purchase order. The maintenance contracts are renewable on an annual basis. The Company also offers basic and advanced formal on-site training for customer employees at the time of product installation. The Company currently provides installation, maintenance and support to international customers but, in the future, plans to provide such services through agents and distributors. Pursuant to the acquisition of IPC, the Company also provides movie content in conjunction with sales of the SeaChange GuestServe System. In addition, as a result of the acquisition the Company acquired contracts varying from three to five years, whereby, the Company will continue to operate IPC's tape based systems for hotels.

The Company offers technical support to customers, agents and distributors on a 24-hour, seven-day a week basis. Support engineers are committed to providing a response to technical support calls within two hours. The Company's products are designed with remote diagnostic capabilities which permit the support engineers to immediately begin to diagnose any problems without having to travel to the customer's location, thereby reducing both response time and cost. When necessary, however, support engineers are dispatched to the customer's facility.

CUSTOMERS

The Company currently sells its products primarily to cable television operators and telecommunications companies. In addition, the Company is developing several products for television broadcasters.

The Company's customer base is highly concentrated among a limited number of large customers, primarily due to the fact that the cable and telecommunications industries in the United States are dominated by a limited number of large companies. A significant portion of the Company's revenues in any given fiscal period have been derived from substantial orders placed by these large organizations. In 1995, 1996 and 1997, revenues from the Company's five largest customers represented approximately 91%, 76% and 68%, respectively, of the Company's total revenues. Customers accounting for more than 10% of total revenues consisted of Continental Cablevision (29%), Tele-Communications, Inc. (29%), Time Warner, Inc. (16%) and Cox Communications, Inc. (12%) in 1995; Tele-Communications, Inc. (29%), U.S. West Media Group (17%), Comcast Corporation (13%) and Time Warner, Inc. (12%) in 1996; and Tele-Communications, Inc. (24%), Time Warner, Inc. (18%) and Comcast Corporation (10%) in 1997. The Company expects that it will continue to be dependent upon a limited number of customers for a significant portion of its revenues in future periods. As a result of this customer concentration, the Company's business, financial condition and results of operations could be materially adversely affected by the failure of anticipated orders to materialize and by deferrals or cancellations of orders as a result of changes in customer requirements or new product announcements or introductions.

The Company believes that its backlog at any particular time is not meaningful as an indicator of its future level of sales for any particular period. Because of the nature of the Company's products and its use of standard components, substantially all of the backlog at the end of a quarter can be manufactured by the Company and is intended to be shipped by the end of the following quarter. However, because of the requirements of particular customers, the seasonality of the business and, in respect to certain sales, the acceptance criteria necessary for revenue recognition, such backlog may not be shipped or, if shipped, the related revenues may not be recognized in such quarter. Therefore, there is no direct correlation between the backlog at the end of any quarter and the Company's total sales for the following quarter or other periods.

SELLING AND MARKETING

The Company sells and markets its products in the United States primarily through a direct field sales organization and internationally primarily through independent agents and distributors, complemented by a coordinated marketing effort of the Company's marketing group. Direct sales activities in the United States are conducted from the Company's Massachusetts headquarters and six field offices. In October 1996, the Company entered into an exclusive sales and marketing representative agreement with a private Italian company which covers continental Europe. The Company also markets certain of its products, namely the Video Server 100 and MediaCluster, to systems integrators and VARs. As of December 31, 1997, the Company's selling and marketing organization consisted of 28 people.

In light of the complexity of the Company's digital video products, the Company primarily employs a consultative direct sales process. Working closely with customers to understand and define their needs enables the Company to obtain better information regarding market requirements, enhance its expertise in its customers' industries and more effectively and precisely convey to customers how the Company's solutions address the customer's specific needs. In addition to the direct sales process, customer references and visits by potential customers to sites where the Company's products are in place are often critical in the sales process.

The Company uses several marketing programs focused on the Company's targeted markets to support the sale and distribution of its products. The Company uses exhibitions at a limited number of prominent industry trade shows and conferences and presentations at technology seminars to promote awareness of the Company and its products. The Company also publishes technical articles in trade and technical journals and product promotional literature.

RESEARCH AND PRODUCT DEVELOPMENT

Management believes that the Company's success will depend to a substantial degree upon its ability to develop and introduce in a timely fashion new products and enhancements to its existing products that meet changing customer requirements in the Company's current and new markets. The Company has in the past made, and intends to continue to make, substantial investments in product and technological development. Through its direct sales process the Company monitors changing customer needs, changes in the marketplace and emerging industry standards, and is therefore better able to focus its research and development efforts to address such evolving industry requirements.

The Company's research and development expenditures totaled approximately $2.4 million, $5.4 million and $11.8 million for the years ended December 31, 1995, 1996 and 1997, respectively. See discussion below regarding the write-off of acquired in-process research and development in 1997. At December 31, 1997, 90 employees were engaged in research and product development. The Company believes that the experience of its product development personnel is an important factor in the Company's success. The Company performs its research and product development activities at its headquarters and in offices in Greenville, New Hampshire, Duluth, Georgia, Englewood, Colorado and Novato, California. The Company has historically expensed its direct research and development costs as incurred.

The Company has a variety of new products being developed and tested, including video-on-demand products for cable television operators and telecommunications companies, Broadcast MediaCluster systems for television broadcasters and interactive television. There can be no assurance that the Company will be able to successfully develop and market such products, or to identify, develop, manufacture, market or support other new products or enhancements to its existing products successfully or on a timely basis, that new Company products will gain market acceptance, or that the Company will be able to respond effectively to product announcements by competitors or technological changes.

ACQUIRED IN-PROCESS RESEARCH AND DEVELOPMENT

In connection with the acquisition of IPC, $5,290,000 of the purchase price, based on upon an independent appraisal, was allocated to in-process research and development, resulting in an immediate charge to the Company's operations as of the date of acquisition. The amount allocated to in-process research and development represented technology which had not reached technological feasability and did not have an alternative future use. The Company intends to continue developing this in-process technology over the next year as a means of increasing the marketability of the Company's movie systems.

MANUFACTURING

The Company's manufacturing operations are located at facilities in Maynard, Massachusetts, Greenville, New Hampshire and Novato, California. The manufacturing operations in Massachusetts consist primarily of component and

subassembly procurement, system integration and final assembly, testing and quality control of the complete systems. The Company's operations in New Hampshire consist primarily of component and subassembly procurement, video server integration and final assembly, testing and quality control of the video servers. The Company's operations in Novato, California consist primarily of component and subassembly procurement, system integration and final assembly, testing and quality control of the SeaChange GuestServe System. The Company relies on independent contractors to manufacture components and subassemblies to the Company's specifications. Each of the Company's products undergoes testing and quality inspection at the final assembly stage.

The Company attempts to use standard parts and components available from multiple vendors. Certain components used in the Company's products, however, are currently purchased from a single source, including a computer chassis manufactured by Trimm Technologic Inc., a disk controller manufactured by Mylex Corporation, an MPEG-2 decoder card manufactured by Vela Research, Inc., set-top boxes manufactured by IPC Corp. and an MPEG-2 encoder manufactured by Optivision, Inc. While the Company believes that there are alternative suppliers available for the foregoing components, the Company believes that the procurement of such components from alternative suppliers would take anywhere from 45-120 days. There can be no assurance that such alternative components would be functionally equivalent or would be available on a timely basis or on similar terms. The Company purchases several other components from a single supplier, although the Company believes that alternative suppliers for such components are readily available on a timely basis. The Company generally purchases sole source or other components pursuant to purchase orders placed from time to time in the ordinary course of business and has no written agreements or guaranteed supply arrangements with its sole source suppliers. The Company has experienced quality control problems and supply shortages for sole source components in the past and there can be no assurance that the Company will not experience significant quality control problems or supply shortages for these components in the future. The Company has begun to increase its inventory of these components. However, any interruption in the supply of such single source components could have a material adverse effect on the Company's business, financial condition and results of operations. Because of the Company's reliance on these vendors, the Company may also be subject to increases in component costs which could adversely affect the Company's business, financial condition and results of operations.

COMPETITION

The markets in which the Company competes are characterized by intense competition, with a large number of suppliers providing different types of products to different segments of the markets. The Company currently competes principally on the basis of: (i) the breadth of its products' features and benefits, including the ability to precisely target viewers in specific geographic or demographic groups, and the flexibility, scalability, professional quality, ease of use, reliability and cost effectiveness of its products; and (ii) the Company's reputation and the depth of its expertise, customer service and support. While the Company believes that it currently competes favorably overall with respect to these factors and that its ability to provide software-based solutions to manage, store and distribute digital video differentiates the Company from its competitors, there can be no assurance that the Company will be able to continue to compete successfully with respect to such factors.

In the digital advertisement insertion market, the Company generally competes with Channelmatic Inc., a subsidiary of Indenet, Inc., SkyConnect, Inc., Digital Video, and other smaller suppliers of systems. In the market for NVOD and GuestServe Movie Systems, the Company competes against various computer companies offering video server platforms such as EMC Inc., Digital Equipment Corporation and Silicon Graphics, Inc., and more traditional movie application providers like The Ascent Entertainment Group, Panasonic Company, On Command, Inc, and Lodgenet Entertainment. In addition, the SeaChange Advertising Management Software competes against certain products of Columbine Cable Systems, Inc., Cable Computerized Management Systems, Inc., a subsidiary of Indenet Inc., LAN International USA, Inc., Visiontel, Inc. and various suppliers of sales, scheduling and billing software products. In the television broadcast market, the Company expects to compete against Tektronix, Inc., BTS Inc., a division of Robert Bosch GmgH, Hewlett-Packard Company, Sony Corporation, Silicon Graphics, Inc., Sun Microsystems, Inc. and ASC Incorporated. The Company expects the competition in each of these markets to intensify.

Many of the Company's current and prospective competitors have significantly greater financial, technical, manufacturing, sales, marketing and other resources than the Company. As a result, these competitors may be able to devote greater resources to the development, promotion, sale and support of their products than the Company. Moreover, these companies may introduce additional products that are competitive with those of the Company or enter into strategic relationships to offer complete solutions, and there can be no assurance that the Company's products would compete effectively with such products.

Although the Company believes that it has certain technological and other advantages over its competitors, maintaining such advantages will require continued investment by the Company in research and development, selling and marketing and customer service and support. In addition, as the Company enters

new markets, distribution channels, technical requirements and levels and bases of competition may be different than those in the Company's current markets. There can be no assurance that the Company will be able to compete successfully against either current or potential competitors in the future.

PROPRIETARY RIGHTS

The Company's success and its ability to compete is dependent, in part, upon its proprietary rights. Although the Company has filed one U.S. and one foreign patent application for its MediaCluster technology, it does not hold any issued patents and currently relies on a combination of contractual rights, trademark laws, trade secrets and copyright laws to establish and protect its proprietary rights in its products. There can be no assurance that a patent will be issued with respect to the pending application or that, if issued, the validity of such patent would be upheld. Nor can there be any assurance that the steps taken by the Company to protect its intellectual property will be adequate to prevent misappropriation of its technology or that the Company's competitors will not independently develop technologies that are substantially equivalent or superior to the Company's technology. In addition, the laws of some foreign countries in which the Company's products are or may be distributed do not protect the Company's proprietary rights to the same extent as do the laws of the United States.

The Company is also subject to the risk of adverse claims and litigation alleging infringement of intellectual property rights of others. The Company attempts to ensure that its products do not infringe any existing proprietary rights of others. The Company received a letter in January 1996 stating that the Company's video insertion system may be utilizing technology patented by a third party. The Company did not respond to such letter and has received no further communication from the holder of these patents. The Company does not believe that its products infringe such patents. There can be no assurance that the holder of these patents or other third parties will not assert infringement claims against the Company in the future based on patents, copyrights, trademarks or trade secrets, or that any such claims will not be successful. The Company could incur substantial costs in defending itself and its customers against any such claims, regardless of the merits of such claims. Parties making such claims may be able to obtain injunctive or other equitable relief which could effectively block the Company's ability to sell its products in the United States and abroad, and could result in significant litigation costs and expenses or an award of

substantial damages. In the event of a successful claim of infringement, the Company and its customers may be required to obtain one or more licenses from third parties or to develop alternative technologies. There can be no assurance that the Company or its customers could obtain necessary licenses from third parties at a reasonable cost or at all, or would be able to develop alternative technologies. The defense of any lawsuit could result in time consuming and expensive litigation, damages, license fees, royalty payments and restrictions on the Company's ability to sell its products, any of which could have a material adverse effect on the Company's business, financial condition and results of operations.

A version of the SeaChange Advertising Management Software in limited distribution was based on software the Company licensed from Summit Software Systems, Inc. of Boulder, Colorado in May 1996. The Company has been granted a perpetual, nonexclusive license to such software in return for the payment of an up-front license fee and royalties for sales occurring prior to June 1998.

EMPLOYEES

As of December 31, 1997, the Company employed 264 persons, including 90 in research and development, 83 in customer service and support, 28 in selling and marketing, 33 in manufacturing and 30 in finance and administration. The Company believes that its relations with its employees are good.

CERTAIN RISK FACTORS

Limited Operating History and Operating Results. The Company was founded in July 1993 and commenced shipment of its initial products in the third quarter of 1994. Accordingly, the Company has only a limited operating history upon which an evaluation of the Company and its prospects can be based. The Company's prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in their early stage of development, particularly companies in new and rapidly evolving markets. To address these risks, the Company must, among other things, respond to competitive developments, continue to attract, retain and motivate qualified persons, and continue to upgrade its technologies and commercialize products and services incorporating such technologies. There can be no assurance that the Company will be successful in addressing such risks. Increases in operating expenses are expected to continue and may result in a decrease in operating income.

Fluctuations in Quarterly Operating Results. The Company's quarterly operating results have in the past varied and in the future will be affected by

factors such as: (i) the timing and recognition of revenue from significant orders, (ii) the seasonality of the placement of customer orders, (iii) the success of the Company's products, (iv) increased competition, (v) changes in the Company's pricing policies or those of its competitors, (vi) the financial stability of major customers, (vii) new product introductions or enhancements by competitors, (viii) delays in the introduction of products or product enhancements by the Company, (ix) customer order deferrals in anticipation of upgrades and new products, (x) the ability to access a sufficient supply of sole source and third party components, (xi) the quality and market acceptance of new products, (xii) the timing and nature of selling and marketing expenses (such as trade shows and other promotions), (xiii) personnel changes, (xiv) the risks associated with international sales as the Company expands its markets, (xv) the Company's ability to integrate the operations of acquired subsidiaries and (xvi) economic conditions affecting the Company's customers. Any significant cancellation or deferral of purchases of the Company's products could have a material adverse effect on the Company's business, financial condition and results of operations in any particular quarter, and to the extent significant sales occur earlier than expected, operating results for subsequent quarters may be adversely affected. The Company's expense levels are based, in part, on its expectations as to future revenues, and the Company may be unable to adjust spending in a timely manner to compensate for any revenue shortfall. If revenues are below expectations, operating results are likely to be adversely affected and net income may be disproportionately affected because a significant portion of the Company's expenses do not vary with revenues.

Because of these factors, the Company believes that period-to-period comparisons of its results of operations are not necessarily meaningful and should not be relied upon as indications of future performance. Due to all of the

foregoing factors, in some future quarter the Company's operating results may be below the expectations of public market analysts and investors.

Seasonality. The Company's business has been seasonal with more orders being placed and greater revenues being recognized in the first and second quarters than in the third and fourth quarters. The Company believes that the concentration of order placements in specific quarterly periods is due to customers' buying patterns and budgeting cycles in the cable television industry. The Company anticipates that these patterns will continue in the future. As a result, the Company's results of operations have in the past and likely will in the future vary seasonally in accordance with such purchasing activity. Due to the relatively fixed nature of certain of the Company's costs throughout each quarterly period, including personnel and facilities costs, the decline of revenues in any quarter typically results in lower profitability in that quarter.

Management of Growth. The Company has experienced growth in revenues and expansion of its operations which have placed significant demands on the Company's management, administrative and operational resources. The Company believes that further improvements in management and operational controls are needed, and would continue to be needed to manage any future growth. Continued growth will also require the Company to hire more technical, selling and marketing, support and administrative personnel, expand manufacturing and customer service capabilities, and update or expand management information systems. There can be no assurance that the Company will be able to attract and retain the necessary personnel to accomplish its growth strategies or that it will not experience constraints that will adversely affect its ability to satisfy customer demand in a timely fashion or to satisfactorily support its customers and operations. Also, the Company may in the future acquire complementary service or product lines, technologies or businesses, although the Company has no present understandings, commitments or agreements with respect to any significant acquisitions. If the Company's management is unable to manage growth effectively or integrate any acquisition into the Company's operations successfully, the Company's business, financial condition and results of operations could be materially and adversely affected.

Product Concentration. Through December 31, 1997, substantially all of the Company's revenues were derived from the sale of the SeaChange SPOT System, movie systems and related services. The Company's success depends in part on continued sales of the SeaChange SPOT System, movie systems and the introduction of new products. A decline in demand or average selling prices for the SeaChange SPOT System or movie product lines, whether as a result of new product introductions by others, price competition, technological change, inability to enhance the products in a timely fashion, or otherwise, would have a material adverse effect on the Company's business, financial condition and results of operations.

Highly Competitive Market. The market for digital video products is highly competitive. The Company currently competes against suppliers of both analog tape-based and digital systems in the advertisement insertion market and against both computer companies offering video server platforms and more traditional movie application providers in the movie system market. When the Company introduces products in the television broadcast market, the Company expects to compete in that market against various computer companies offering video server platforms and television equipment manufacturers. Due to the rapidly evolving

markets in which the Company competes, additional competitors with significant market presence and financial resources, including computer hardware and software companies and television equipment manufacturers, may enter those markets, thereby further intensifying competition. Increased competition could result in price reductions and loss of market share which would adversely affect the Company's business, financial condition and results of operations. Many of the Company's current and potential competitors have greater financial, selling and marketing, technical and other resources than the Company. Moreover, the Company's competitors may also foresee the course of market developments more accurately than the Company. Although the Company believes it has certain technological and other advantages over its competitors, realizing and maintaining such advantages will require a continued high level of investment by the Company in research and product development, marketing and customer service and support. There can be no assurance that the Company will have sufficient resources to continue to make such investments or that the Company will be able to make the technological advances necessary to compete successfully with its existing competitors or with new competitors.

Dependence on Emerging Digital Video Market. Cable television operators and television broadcasters have historically relied on traditional analog technology for video management, storage and distribution. Digital video technology is still a relatively new technology and requires a significant initial investment of capital. The Company's future growth will depend both on the rate at which television operators convert to digital video systems and the rate at which digital video technology expands to additional market segments. There can be no assurance that the use of digital video technology will expand among television operators or into additional markets. Any failure by the market to accept digital video technology will have a material adverse affect on the Company's business, financial condition and results of operations.

Risks Associated with Expansion into New Markets. To date the Company's products have been purchased primarily by cable television operators and telecommunications companies. The Company's success depends in part on the penetration of new markets. In particular, the Company plans to introduce several products for use by television broadcasters. These broadcast products will be directed toward a market that the Company has not previously addressed. There can be no assurance that the Company will be successful in marketing and selling these new products to customers in the broadcast television market. Any inability of the Company to penetrate this new market would have a material adverse effect on the Company's business, financial condition and results of operations.

Risk of New Product Introductions. The Company's future success requires that it develop and market additional products that achieve significant market acceptance and enhance its current products. The Company has recently introduced a new product which enables television operators to provide video-on-demand and scheduled playback services to hotels and apartments. The success of this product may depend in part on relationships with movie content providers. There can be no assurance that the Company will not experience difficulties that could delay or prevent the successful development, introduction and marketing of this and other new products and enhancements, or that its new products and enhancements will adequately meet the requirements of the marketplace and achieve market acceptance. Announcements of currently planned or other new product offerings may cause customers to defer purchasing existing Company products. Moreover, there can be no assurance that, despite testing by the Company, and by current and potential customers, errors or failures will not be found in the Company's products, or, if discovered, successfully corrected in a timely manner. Such errors or failures could cause delays in product introductions and shipments, or require design modifications that could adversely affect the Company's competitive position. The Company's inability to develop on a timely basis new products, enhancements to existing products or error corrections, or the failure of such new products or enhancements to achieve market acceptance could have a material adverse effect on the Company's business, financial condition and results of operations.

Rapid Technological Change. The markets for the Company's products are characterized by rapidly changing technology, evolving industry standards and frequent new product introductions and enhancements. Future technological advances in the television and video industries may result in the availability of new products or services that could compete with the solutions provided by the Company or reduce the cost of existing products or services, any of which could enable the Company's existing or potential customers to fulfill their video needs better and more cost efficiently than with the Company's products. The Company's future success will depend on its ability to enhance its existing digital video products, including the development of new applications for its technology and to develop and introduce new products to meet and adapt to changing customer requirements and emerging technologies. There can be no assurance that the Company will be successful in enhancing its digital video products or developing, manufacturing and marketing new products which satisfy customer needs or achieve market acceptance. In addition, there can be no assurance that services, products or technologies developed by others will not render the Company's products or technologies uncompetitive, unmarketable or obsolete, or that announcements of currently planned or other new product offerings by either the Company or its competitors will not cause customers to defer or fail to purchase existing Company solutions. The failure of the Company

to respond to rapidly changing technologies related to digital video could have a material adverse effect on the Company's business, financial condition and results of operations.

Significant Concentration of Customers. The Company's customer base is highly concentrated among a limited number of large customers, primarily due to the fact that the cable television and telecommunications industries in the United States are dominated by a limited number of large companies. A fairly limited number of customers account for a significant percentage of the Company's revenues in any year. In 1995, 1996 and 1997, revenues from the Company's five largest customers represented approximately 91%, 76% and 68%, respectively, of the Company's total revenues. In each of 1995 and 1996, four customers each accounted for more than 10% of the Company's revenues and in 1997 three customers accounted for more than 10% of the Company's revenues, two of which accounted for more than 10% of the Company's revenues in 1995, 1996 and 1997. The Company generally does not have written continuing purchase agreements with its customers and does not have any written agreements that require customers to purchase fixed minimum quantities of the Company's products. The Company's sales to specific customers tend to vary significantly from year to year depending upon such customers' budgets for capital expenditures and new product introductions. In addition, the Company derives a substantial portion of its revenues from products that have a selling price in excess of $150,000. The Company believes that revenue derived from current and future large customers will continue to represent a significant proportion of its total revenues. The loss of, or reduced demand for products or related services from, any of the Company's major customers could have a material adverse effect on the Company's business, financial condition and results of operations.

Dependence on Sole Source Suppliers and Third Party Manufacturers. Certain key components of the Company's products are currently purchased from a sole supplier, including a computer chassis manufactured by Trimm Technologic Inc., a disk controller manufactured by Mylex Corporation, an MPEG-2 decoder card manufactured by Vela Research, Inc. and an MPEG-2 encoder manufactured by Optivision, Inc. The Company does not have material written supply agreements with these or any of its suppliers. The Company has in the past experienced quality control problems, where products did not meet specifications or were damaged in shipping, and delays in the receipt of such components. These problems were generally of short duration and did not have a material adverse effect on the Company. However, the Company may in the future experience similar types of problems which could be more severe or more prolonged. The inability to obtain sufficient key components as required, or to develop alternative sources if and as required in the future, could result in delays or reductions in product shipments which, in turn, could have a material adverse effect on the Company's business, financial condition and results of operations. Moreover, the Company relies on a limited number of third parties who manufacture certain components used in the Company's products. While to date there has been suitable third party manufacturing capacity readily available at acceptable quality levels, there can be no assurance that such manufacturers will be able to meet the Company's future volume or quality requirements or that such services will continue to be available to the Company at favorable prices. Any financial, operational, production or quality assurance difficulties experienced by such third party manufacturers that result in a reduction or interruption in supply to the Company could have a material adverse effect on the Company's business, financial condition and results of operations.

Regulation of Telecommunications and Television Industries. The telecommunications and television industries are subject to extensive regulation in the United States and other countries. The Company's business is dependent upon the continued growth of such industries in the United States and internationally. Although recent legislation has lowered the legal barriers to entry for telecommunications companies into the United States multichannel television market, there can be no assurance that such telecommunications companies will successfully enter this or related markets. Moreover, the growth of the Company's business internationally is dependent in part on similar deregulation of the telecommunications industry abroad and there can be no assurance that such deregulation will occur. Television operators are also subject to extensive government regulation by the Federal Communications Commission (''FCC'') and other federal and state regulatory agencies. These regulations could have the effect of limiting capital expenditures by television operators and thus could have a material adverse effect on the Company's business, financial condition and results of operations. The enactment by federal, state or international governments of new laws or regulations, changes in the interpretation of existing regulations or a reversal of the trend toward deregulation in these industries could adversely affect the Company's customers, and thereby materially adversely affect the Company's business, financial condition and results of operations.

Lengthy Sales Cycle. Digital video products are relatively complex and their purchase generally involves a significant commitment of capital, with attendant delays frequently associated with large capital expenditures and implementation procedures within an organization. Moreover, the purchase of such products typically requires coordination and agreement among a potential customer's corporate headquarters and its regional and local operations. For these and

other reasons, the sales cycle associated with the purchase of the Company's digital video products is typically lengthy and subject to a number of significant risks, including customers' budgetary constraints and internal acceptance reviews, over which the Company has little or no control. Based upon all of the foregoing, the Company believes that the Company's quarterly revenues, expenses and operating results are likely to vary significantly in the future, that period-to-period comparisons of its results of operations are not necessarily meaningful and that, in any event, such comparisons should not be relied upon as indications of future performance.

Dependence on Key Personnel and Hiring of Additional Personnel. The Company's success depends to a significant degree upon the continued contributions of its key management, engineering, selling and marketing and manufacturing personnel, many of whom would be difficult to replace. The Company does not have employment contracts with its key personnel. The Company believes its future success will also depend in large part upon its ability to attract and retain highly skilled managerial, engineering, selling and marketing, finance and manufacturing personnel. Competition for such personnel is intense, and there can be no assurance that the Company will be successful in attracting and retaining such personnel. The loss of the services of any of the key personnel, the inability to attract or retain qualified personnel in the future or delays in hiring required personnel, particularly software engineers and sales personnel, could have a material adverse effect on the Company's business, financial condition and results of operations.

Dependence on Proprietary Rights. The Company's success and its ability to compete is dependent, in part, upon its proprietary rights. The Company relies primarily on a combination of patent, copyright, trademark and trade secret laws, as well as confidentiality procedures and contractual provisions to protect its proprietary rights. There can be no assurance that such measures will be adequate to protect the Company's proprietary rights. The Company attempts to ensure that its products and technology do not infringe the proprietary rights of third parties. The Company received a letter in January 1996 stating that the Company's video insertion system may be utilizing technology patented by a third party. The Company did not respond to such letter and has received no further communication from the holder of these patents. The Company does not believe that its products infringe the patents mentioned in such letter. However, there can be no assurance that the holder of these patents or other third parties will not assert infringement claims against the Company in the future or that any such claim will not be successful.

Risks Associated with International Sales. Prior to 1996, the Company derived no significant revenues from international operations. International sales accounted for approximately 5% and 12% of the Company's total revenues in the years ended December 31, 1996, and 1997, respectively. The Company expects that international sales will account for a significant portion of the Company's business in the future. However, there can be no assurance that the Company will be able to maintain or increase international sales of its products. International sales are subject to a variety of risks, including difficulties in establishing and managing international distribution channels, in servicing and supporting overseas products and in translating products into foreign languages. International operations are subject to difficulties in collecting accounts receivable, staffing and managing personnel and enforcing intellectual property rights. Other factors that can also adversely affect international operations include fluctuations in the value of foreign currencies and currency exchange rates, changes in import/export duties and quotas, introduction of tariff or non-tariff barriers and economic or political changes in international markets.

Concentration of Ownership. The Company's officers, directors and their affiliated entities, and other holders of 5% or more of the Company's outstanding capital stock, together beneficially owned approximately 64% of the outstanding shares of Common Stock of the Company as of March 23, 1998. As a result, such persons will have the ability to elect the Company's directors and to determine the outcome of corporate actions requiring stockholder approval, irrespective of how other stockholders of the Company may vote. This concentration of ownership may have the effect of delaying or preventing a change in control of the Company which may be favored by a majority of the remaining stockholders, or cause a change of control not favored by the Company's other stockholders.

ITEM 2. PROPERTIES

The Company's corporate headquarters, which is also its principal administrative, selling and marketing, customer service and support and product development facility, is located in Maynard, Massachusetts and consists of approximately 44,000 square feet under a lease which originally expired on March 31, 1998, however, the lease term has been extended to July 31, 1998 with a revised annual base rent of $342,000. The Company is currently negotiating a lease for premises for its principal facility and anticipates that space under terms acceptable to the Company will be available as needed. The Company leases a facility of approximately 9,000 square feet in Greenville, New Hampshire that is used for the development and final assembly of its video servers. The Company leases a facility of approximately 29,000 square feet in Novato, California that is principally used for product development and customer support. The Company also leases small research and development and sales and support offices in

Atlanta, Georgia, Englewood, Colorado, Burlingame, California and St. Louis, Missouri. The Company believes its existing and planned facilities are adequate for its current needs and that suitable additional or substitute space will be available as needed.

ITEM 3. LEGAL PROCEEDINGS

From time to time, the Company is involved in litigation relating to claims arising out of its operations in the normal course of business. The Company believes that it is not currently involved in any legal proceedings the resolution of which, individually or in the aggregate, would have a material adverse effect on the Company's business, financial condition or results of operation.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITIES HOLDERS

No matters were submitted during the fourth quarter of the fiscal year ended December 31, 1997 to a vote of security holders of the Company through the solicitation of proxies or otherwise.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's Common Stock is traded on the Nasdaq National Market under the symbol "SEAC." Public trading of the Common Stock commenced on November 5, 1996. Prior to such date, there was no public market for the Common Stock. The following table sets forth the high and low sale prices for the Common Stock for the periods indicated, as reported on the Nasdaq National Market.

YEAR ENDED DECEMBER 31, 1997	High	Low
First Quarter	$33.00	$12.13
Second Quarter	$28.25	$16.75
Third Quarter	$29.38	$13.75
Fourth Quarter	$14.75	$ 6.38
YEAR ENDED DECEMBER 31, 1996		
Fourth Quarter (from November 5, 1996)	$39.50	$17.38

On March 23, 1998, the last reported sale price of the Common Stock on the Nasdaq National Market was $7.50. As of March 23, 1998, there were approximately 162 stockholders of record of the Company's Common Stock, as shown in the records of the Company's transfer agent. The Company believes that most of its stock (other than shares held by its officers and directors) is held in street names through one or more nominees. The Company has not paid any cash dividends on its capital stock since its inception, and does not expect to pay cash dividends on its Common Stock in the foreseeable future. The Company currently intends to retain future earnings for use in the operation and expansion of the business.

ITEM 6. SELECTED FINANCIAL DATA

The consolidated statement of operations data for the period from July 9, 1993 (inception) through December 31, 1993 and each of the four years ended December 31, 1994, 1995, 1996 and 1997 and the consolidated balance sheet data at December 31, 1993, 1994, 1995, 1996 and 1997 are detailed below. The following selected consolidated financial data should be read in conjunction with the Company's consolidated financial statements and related notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in Item 7.

<TABLE>
<CAPTION>

	PERIOD FROM JULY 9, 1993 (INCEPTION) THROUGH DECEMBER 31,	YEAR ENDED DECEMBER 31,			
	1993	1994	1995	1996	1997
	(in thousands, except per share data)				
<S>	<C>	<C>	<C>	<C>	<C>
Consolidated Statement of Operations Data:					
Revenues					
Systems..	$ --	$5,037	$21,999	$45,745	$60,414
Services...	--	116	1,204	3,521	7,473

Other	213	537	--	--	--
	213	5,690	23,203	49,266	67,887
Costs of revenues					
Systems	--	3,406	14,917	27,133	34,740
Services	--	176	1,641	4,030	7,607
Other	112	304	--	--	--
	112	3,886	16,558	31,163	42,347
Gross profit	101	1,804	6,645	18,103	25,540
Operating expenses					
Research and development	43	885	2,367	5,393	11,758
Selling and marketing	16	443	1,609	4,254	6,049
General and administrative	59	273	858	2,064	3,744
Write-off of acquired in-process research and development	--	--	--	--	5,290
	118	1,601	4,834	11,711	26,841
Income (loss) from operations	(17)	203	1,811	6,392	(1,301)
Interest income, net	(1)	7	113	353	657
Income (loss) before income taxes	(18)	210	1,924	6,745	(644)
Provision for income taxes	--	55	713	2,483	1,776
Net income (loss)	$ (18)	$ 155	$ 1,211	$ 4,262	$(2,420)
Basic earnings (loss) per share (1)	$ (.05)	$ .09	$ .33	$ .82	$ (.24)
Diluted earnings (loss) per share (1)	$ (.05)	$ .02	$ .11	$ .36	$ (.24)

<CAPTION>

<S>	December 31,				
	1993	1994	1995	1996	1997
	<C>	<C>	<C> (IN THOUSANDS)	<C>	<C>
Consolidated Balance Sheet Data:					
Working capital	$ 90	$ 154	$ 3,493	$26,593	$24,490
Total assets	228	3,494	13,595	46,035	51,950
Long-term liabilities	125	--	--	--	--
Deferred revenue	72	152	767	2,192	3,851
Total liabilities	246	2,977	8,644	14,205	17,468
Redeemable convertible preferred stock	--	--	4,008	--	

--

Total stockholders' equity (deficit).........................	(18)	517	943	31,830	34,482

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(1) For an explanation of the determination of the number of shares used in computing earnings (loss) per share see Notes to Consolidated Financial Statements.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the Company's Consolidated Financial Statements and the related notes thereto included elsewhere in this Annual Report on Form 10-K. The following discussion contains certain trend analysis and other statements of a forward-looking nature relating to future events or the future financial performance of the Company. Readers are cautioned that such statements are only predictions and that actual results or events may differ materially. In evaluating such statements, readers should specifically consider the risk factors set forth in this Annual Report on Form 10-K, particularly the matters set forth under the caption "Certain Risk Factors," in Item 1 "Business", which could cause actual results to differ materially from those indicated by such forward-looking statements.

OVERVIEW

The Company shipped its first digital video insertion product, the SeaChange SPOT System, in the third quarter of 1994. Through December 31, 1997, substantially all of the Company's revenues were derived from the sale of digital video insertion systems, movie systems and related services primarily to cable television operators and telecommunications companies in the United States and internationally. In 1997, the Company derived revenues from the sales of movie systems, a new version of which was introduced in the quarter ended September 30, 1997. Revenues from the sale of systems is recognized upon shipment provided that there are no uncertainties regarding customer acceptance and collection of the related receivables is probable. If such uncertainties exist, such as performance criteria beyond the Company's standard terms and conditions, revenue is recognized upon customer acceptance. Installation and training revenue is deferred and recognized as these services are performed. Revenue from technical support and maintenance contracts is deferred and recognized ratably over the period of the related agreements, generally twelve months. Customers are billed for installation, training and maintenance at the time of the product sale.

The Company's business has been seasonal with more customer orders being placed and greater revenues being generated in the first and second quarters than in the third and fourth quarters. The Company believes that this pattern of order placements in specific quarterly periods is due to cable television customers' buying patterns and budgeting cycles. Many television operators want new video insertion systems to be operational in the second half of the year in order to be able to respond to higher seasonal advertising demand from their customers in this period. The Company expects that these patterns will continue and that, at least in the near future, the Company's revenues and results of operations will reflect these seasonal variations.

The Company's results are significantly influenced by a number of factors, including the Company's pricing, the costs of materials used in the Company's products and the expansion of the Company's operations. The Company prices its products and services based on its costs as well as the prices of competitive products and services in the marketplace. The costs of the Company's products primarily consist of the costs of components and subassemblies. The costs of such materials have generally declined over time. As a result of the expansion of the Company's operations, operating expenses of the Company have increased in the areas of research and development, selling and marketing, customer service and support and general and administration.

On December 10, 1997, the Company acquired all of the outstanding capital stock of IPC Interactive Pte. Ltd. ("IPC"). IPC, together with the Company's centralized video server platform, provides interactive television network systems to the hospitality and commercial property markets. Additionally, IPC deploys and operates its interactive network television systems at customer locations and charges fees for providing services and content, primarily movies. The transaction was accounted for under the purchase method and, accordingly, the results of operations of the Company include the operating results of IPC from the date of acquisition. IPC was renamed GuestServe Networks.

RESULTS OF OPERATIONS

The following table sets forth for the periods indicated the percentage of total revenues represented by certain items reflected in the Company's Consolidated Statement of Operations. Gross profit shown for systems and services revenues at the bottom of the table is stated as a percentage of related revenues.

<TABLE>

<CAPTION>

Year ended December 31,

	1995	1996	1997
<S>	<C>	<C>	<C>
REVENUES			
Systems	94.8 %	92.9 %	89.0 %
Services	5.2	7.1	11.0
	100.0	100.0	100.0
COST OF REVENUES			
Systems	64.3	55.1	51.3
Services	7.1	8.2	11.2
	71.4	63.3	62.5
Gross profit	28.6	36.7	37.5
Operating expenses			
Research and development	10.2	10.9	17.3
Selling and marketing	6.9	8.6	8.9
General and administrative	3.7	4.2	5.5
Write-off of acquired in-process research and development	--	--	7.8
	20.8	23.7	39.5
Income (loss) from operations	7.8	13.0	(2.0)
Interest income, net	.5	.7	1.0
Income (loss) before income taxes	8.3	13.7	(1.0)
Provision for income taxes	3.1	5.0	2.6
Net income (loss)	5.2 %	8.7 %	(3.6)%
Gross profit			
Systems	32.2%	40.7%	42.5%
Services	(36.4)%	(14.5)%	(1.8)%

</TABLE>

YEARS ENDED DECEMBER 31, 1995, 1996 AND 1997

REVENUES

Systems. The Company's systems revenues consist of sales of its digital video insertion and movie system products. Systems revenues increased 108% from $22.0 million in 1995 to $45.7 million in 1996, and increased 32% to $60.4 million in 1997. The increased systems revenues in 1996 reflect the Company's introduction, in January 1996, of the second generation of its digital video insertion system which significantly improved the scalability and performance of the Company's products, and the subsequent increase in the number of systems sold. The increased systems revenues in 1997 compared to 1996 resulted from the increase in the number of the Company's digital video insertion systems sold to television operators primarily in the United States and the sale of approximately $4.4 million of movie systems compared to $232,000 in 1996. The Company expects the sales of its digital ad insertion products to decrease in 1998 as compared to the $55.7 million in 1997, primarily due to an anticipated decrease in spending by U.S. cable operators on these products and the slowness in the development of international demand for such products. The Company anticipates that future growth in systems revenue will come from its movie system products, a new version of which was introduced in the quarter ended September 30, 1997, and its broadcast products, which are expected to be introduced in 1998.

For the years ended December 31, 1995, 1996 and 1997, certain customers accounted for more than 10% of the Company's total revenues. Individual customers accounted for 29%, 29%, 16% and 12% of total revenues in 1995, 29%, 17%,13% and 12% of total revenues in 1996 and 24%, 18% and 10% of total revenues in 1997. The Company believes that revenues from current and future large customers will continue to represent a significant proportion of total revenues.

International sales accounted for approximately 5% and 12% of total revenues in the years ended December 31, 1996 and 1997, respectively. The Company expects that international sales will continue to increase as a percentage of the Company's business in the future. Prior to 1996, the Company had no significant international sales. As of December 31, 1997, all sales of the Company's products were made in United States dollars. The Company does not expect to change this practice significantly in the foreseeable future. Therefore, the Company has not experienced, nor does it expect to experience in the near term, any material impact from fluctuations in foreign currency exchange rates on its results of operations or liquidity. If this practice changes in the future, the Company will reevaluate its foreign currency exchange rate risk.

Services. The Company's services revenues consist of fees for installation, training and product maintenance and technical support services. The Company's services revenues increased 193% from approximately $1.2 million in 1995 to $3.5 million in 1996, and increased 112% to $7.5 million in 1997. These increases in

services revenues primarily resulted from the increase in product sales and renewals of maintenance and support contracts related to the growing installed base of systems. Service and content revenues resulting from the acquisition of IPC were not significant in 1997.

GROSS PROFIT

Systems. Costs of systems revenues consist primarily of the cost of purchased components and subassemblies, labor and overhead relating to the final assembly, testing and quality control of complete systems and related expenses. Costs of systems revenues increased 82% from $14.9 million in 1995 to $27.1 million in 1996, and increased 28% to $34.7 million in 1997. The increases in costs of systems revenues primarily reflect the overall growth in systems sales including the increase in movie system sales in 1997, partially offset by the change in product mix upon the introduction of the second generation video insertion product in January 1996 and the decreasing costs of various components.

Systems gross profit as a percentage of systems revenues was 32.2%, 40.7% and 42.5% in 1995, 1996 and 1997, respectively. The increases in systems gross profit in 1996 and 1997 resulted from lower costs of certain purchased components and subassemblies for systems, the Company achieving certain manufacturing efficiencies as a result of increased volume of systems and from design improvements in the second generation video insertion product. The increases in 1996 and 1997 were partially offset by increases of approximately $694,000 and $1.7 million in the Company's inventory valuation allowance, respectively. The Company evaluates inventory levels and expected usage on a periodic basis and provides a valuation allowance for estimated inactive, obsolete and surplus inventory.

Services. Costs of services revenues consist primarily of labor, materials and overhead relating to the installation, training and product maintenance and technical support services provided by the Company. Costs of services revenues increased 146% from approximately $1.6 million in 1995 to $4.0 million in 1996, and increased 89% to $7.6 million in 1997, primarily as a result of the costs associated with the Company building a service organization to support the installed base of digital ad insertion systems and movie systems. Costs of services exceeded services revenues by 36.4%, 14.5% and 1.8% in 1995, 1996 and 1997, respectively. Improvements in the services negative gross profit in 1996 and 1997 reflected the increase in the installed base of systems under service contracts.

RESEARCH AND DEVELOPMENT. Research and development expenses consist primarily of compensation of development personnel, depreciation of equipment and an allocation of related facilities expenses. Research and development expenses increased 128% from approximately $2.4 million in 1995 to $5.4 million in 1996, and increased 118% to $11.8 million in 1997. The increases in the dollar amounts were primarily attributable to the hiring and contracting of additional development personnel. All internal software development costs to date have been expensed by the Company. The Company expects that research and development expenses will continue to increase in dollar amount as the Company continues its development of new and existing products.

SELLING AND MARKETING. Selling and marketing expenses consist primarily of compensation expenses, including sales commissions and travel expenses, depreciation of equipment and certain promotional expenses. Selling and marketing expenses increased 164% from approximately $1.6 million in 1995 to $4.3 million in 1996, and increased 42% to $6.0 million in 1997. The increases in the dollar amounts were attributable to the hiring of additional selling and marketing personnel, expanded promotional activities, increased international selling efforts and an increase in commissions relating to increased revenues. The Company expects that selling and marketing expenses will continue to increase in dollar amount as the Company hires additional personnel and expands selling and marketing activities in 1998.

GENERAL AND ADMINISTRATIVE. General and administrative expenses consist primarily of compensation of executive, finance, human resource and administrative personnel, legal and accounting services and an allocation of related facilities expenses. General and administrative expenses increased 140% from $858,000 in 1995 to approximately $2.1 million in 1996, and increased 81% to approximately $3.7 million in 1997. The increases in the dollar amounts were primarily attributable to increased staffing and related costs to support the Company's growth and expenses associated with being a public company. The Company believes that its general and administrative expenses will continue to increase as a result of an expansion of the Company's administrative staff to support its growing operations.

WRITE-OFF OF ACQUIRED IN-PROCESS RESEARCH AND DEVELOPMENT. In connection with the acquisition of IPC the Company acquired certain technology which can be used with the Company's video server technology to provide interactive television network systems to the hospitality and commercial property markets. As discussed in Note 3 to the consolidated financial statements, the Company recorded a charge to operations of $5,290,000 for the write-off of in-process research and development, the value of which was determined based upon an independent appraisal. In addition, the Company recorded intangible assets of $1,635,000 which included approximately $850,000 of software. Of the acquired technology, the capitalized amount reflects the allocation of the purchase price to the software technology deemed technologically feasible, including the operating

system and software for the distribution of movies over the network. Acquired technology included in the in-process write-off reflects the purchase price allocated to technology currently under development and not considered technologically feasible at the time of the acquisition and did not have an alternative future use, including software to provide certain new interactive features and functions over the network. The Company intends to continue developing this in-process technology over the next year as a means of increasing the marketability of its movie systems.

INTEREST INCOME. Interest income was approximately $113,000, $353,000 and $657,000 in 1995, 1996 and 1997, respectively. The increase in interest income primarily resulted from interest earned on a higher invested balance primarily due to the net proceeds of $24.1 million from the initial public offering of the Company's common stock in November 1996.

PROVISION FOR INCOME TAXES. The Company's effective tax rates were 37.1% and 36.8% in 1995 and 1996, respectively. The Company's effective tax rate for 1997 was significantly impacted by the write-off of the acquired in-process research and development which, due to the tax-free nature of the transaction to IPC stockholders, is not deductible for tax purposes by the Company. Accordingly, in 1997 the Company recorded a tax provision of approximately $1.8 million despite a book pre-tax operating loss. Through the first three quarters of 1997, the Company's effective tax rate was 38%.

The Company had net deferred tax assets of $575,000 and $1,091,000 at December 31, 1996 and 1997, respectively. The Company has made the determination that it is more likely than not that it will realize the benefits of the net deferred tax assets. As a result of the acquisition of IPC, the Company acquired deferred tax assets of $3.4 million, consisting primarily of net operating loss carryforwards. As discussed in Note 5 of the consolidated financial statements, the Company maintains a full valuation allowance on the acquired net deferred tax assets.

QUARTERLY RESULTS OF OPERATIONS

The following table presents certain unaudited quarterly information for the eight quarters ended December 31, 1997. Gross profit shown for systems and services revenues at the bottom of the table is stated as a percentage of related revenues. This information is derived from unaudited financial statements and has been prepared on the same basis as the Company's audited financial statements which appear elsewhere in this Annual Report on Form 10-K. In the opinion of the Company's management, this data reflects all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the information when read in conjunction with the Company's Consolidated Financial Statements and Notes thereto. The results for any quarter are not necessarily indicative of future quarterly results of operations, and the Company believes that period-to-period comparisons should not be relied upon as an indication of future performance.

QUARTERLY FINANCIAL DATA (UNAUDITED)
<TABLE>
<CAPTION>

	Quarter Ended							
	March 31, 1996	June 30, 1996	Sept. 30, 1996	Dec. 31, 1996	March 31, 1997	June 30, 1997	Sept. 30, 1997	Dec. 31, 1997
	(in thousands)							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
REVENUES								
Systems	$ 9,684	$13,222	$11,738	$11,101	$16,796	$20,184	$13,188	$10,246
Services	545	903	1,188	885	1,256	1,668	2,063	2,486
	10,229	14,125	12,926	11,986	18,052	21,852	15,251	12,732
COSTS OF REVENUES								
Systems	6,342	8,088	6,665	6,038	9,457	11,079	7,889	6,315
Services	729	1,087	1,055	1,159	1,386	1,622	1,953	2,646
	7,071	9,175	7,720	7,197	10,843	12,701	9,842	8,961
Gross profit	3,158	4,950	5,206	4,789	7,209	9,151	5,409	3,771
Operating expenses								
Research and development	992	994	1,256	2,151	2,416	2,750	3,159	3,433
Selling and marketing	755	1,155	1,125	1,219	1,268	1,842	1,431	1,508
General and administrative	294	568	648	554	930	866	792	1,156
Write-off of acquired and in-process research and development	--	--	--	--	--	--	--	5,290

	2,041	2,717	3,029	3,924	4,614	5,458	5,382	11,387
Income (loss) from operations	1,117	2,233	2,177	865	2,595	3,693	27	(7,616)
Interest income, net	48	52	37	216	200	187	136	134
Income (loss) before income taxes	1,165	2,285	2,214	1,081	2,795	3,880	163	(7,482)
Provision (benefit) for income taxes	446	882	788	367	1,062	1,475	61	(822)
Net income (loss)	$ 719	$ 1,403	$ 1,426	$ 714	$ 1,733	$ 2,405	$ 102	(6,660)
Basic earnings (loss) per share	$ .20	$ .32	$ .29	$ .09	$ .19	$ .24	$ .01	$ (.61)
Diluted earnings (loss) per share	$ .06	$ .12	$ .12	$ .06	$ .13	$ .18	$ .01	$ (.61)
Gross profit								
Systems	34.5%	38.8%	43.2%	45.6%	43.7%	45.1%	40.2%	38.4%
Services	(33.7)%	(20.5)%	11.2%	(31.0)%	(10.4)%	2.8%	5.3%	(6.4)%

</TABLE>

The Company has experienced significant variations in revenues, expenses and operating results from quarter to quarter and such variations are likely to continue. A significant portion of the Company's revenues have been generated from a limited number of customers and it is difficult to predict the timing of future orders and shipments to these and other customers. Customers can cancel or reschedule shipments, and development or production difficulties could delay shipments.

The Company has also experienced significant variations in its quarterly gross margins. In the third quarter of 1995, the Company decreased the selling price of its first generation SeaChange SPOT digital video insertion system in anticipation of the introduction of the second generation system in the first quarter of 1996. This price reduction had a negative impact on the Company's systems gross margins in the first and second quarters of 1996. In the third and fourth quarters of 1997, the decrease in the number of systems sold affected the Company's ability to achieve manufacturing efficiencies and, accordingly, the gross profit was negatively impacted. Quarterly services gross margins have historically fluctuated significantly because installation and training service revenue varies by quarter, while the related costs are relatively consistent by quarter.

Operating expenses also vary with the number, timing and significance of new product and product enhancement introductions by the Company and its competitors, increased competition, changes in pricing policies by the Company or its competitors, the gain or loss of significant customers, the hiring of new personnel and general economic conditions. All of the above factors are difficult for the Company to forecast, and these or other factors may materially adversely effect the Company's business, financial condition and results of operations for one quarter or a series of quarters. Only a small portion of the Company's expenses vary with revenues in the short-term and there would likely be a material adverse effect on the operating results of the Company if future revenues are lower than expectations.

Based upon all of the foregoing, the Company believes that quarterly revenues and operating results are likely to vary significantly in the future and that period-to-period comparisons of its results of operations are not necessarily meaningful and should not be relied upon as indications of future performance.

LIQUIDITY AND CAPITAL RESOURCES

From inception through November 1996, the Company funded its operations primarily through cash provided by operations and the private sale of equity securities. In November 1996, in connection with the initial public offering of the Company's common stock, the Company received net proceeds of $24.1 million.

Cash, cash equivalents and marketable securities decreased $11.1 million from $23.4 million at December 31, 1996 to $12.3 million at December 31, 1997. Working capital decreased from approximately $26.6 million at December 31, 1996 to approximately $24.5 million at December 31, 1997.

Net cash provided by operating activities was approximately $2.8 million for the year ended December 31, 1995. Net cash used in operating activities was approximately $1.9 million and $9.2 million for the years ended December 31, 1996 and 1997, respectively. The net cash used in operating activities in 1997

was the result of the net loss adjusted for noncash expenses including depreciation, amortization, deferred income taxes and write-off of acquired in-process research and development and the changes in certain assets and liabilities, net of the effect of the acquisition of IPC. The significant net changes in assets and liabilities that used cash in operations include increases in accounts receivable and inventories and decreases in accounts payable and customer deposits. The net increase in accounts receivable in 1997 of approximately $4.4 million is attributable to the decrease in customer deposits, which represent advance payments from customers and the 6% increase in revenues in the fourth quarter of 1997 compared to the same period in 1996. The net increase in inventories in 1997 of approximately $7.1 million is attributable to lower than anticipated system sales in the fourth quarter of 1997 and additional inventories to support the Company's current and anticipated revenue from existing and new product lines and to service the growing installed base of systems. The net decrease in customer deposits in 1997 of approximately $3.3 million is the result of the timing, volume and size of customer orders.

Net cash used in investing activities was approximately $659,000, $3.2 million and $10.8 million for the years ended December 31, 1995, 1996 and 1997, respectively. Investment activity consisted primarily of capital expenditures related to the acquisition of computer equipment, office furniture, and other capital equipment required to support the expansion and growth of the business. In addition, in 1997 the marketable securities increased $9.3 million, net of sales and maturities of $9.0 million and the Company acquired approximately $665,000 of cash, net of transaction costs, related to the acquisition of IPC.

Net cash provided by financing activities was approximately $3.2 million and $22.3 million for the years ended December 31, 1995 and 1996, respectively. Net cash used in financing activities was approximately $454,000 for the year ended December 31,1997. In 1995, the cash provided by financing activities included $4.0 million received in connection with the issuance of the Series B Convertible Redeemable Preferred Stock, partially offset by a $795,000 cash outlay related to loans to stockholders. In 1996, the cash provided by financing activities consisted primarily of net proceeds of $24.1 million from the initial public offering of the Company's common stock in November 1996 offset by the purchase of $2.0 million of treasury stock. In 1997, the cash used in financing represented repayment of IPC's line of credit of approximately $700,000 and payment of loans to related parties of approximately $437,000, offset by $683,000 received in connection with the issuance of common stock pursuant to both the exercise of stock options and purchases under the employee stock purchase plan.

The Company has a $6.0 million revolving line of credit with a bank which expires in September 1998. Borrowings under the line of credit are secured by substantially all of the Company's assets. Loans made under the revolving line of credit will bear interest at a rate per annum equal to, at the Company's option, the bank's base rate or LIBOR, plus an applicable margin. The loan agreement relating to the line of credit requires that the Company provide the bank with certain periodic financial reports and comply with certain financial ratios. As of December 31, 1997, the Company had not borrowed against the line.

The Company believes that existing funds together with available borrowings under the line of credit agreement are adequate to satisfy its working capital and capital expenditure requirements for the foreseeable future.

The Company also believes that "Year 2000" conversion costs will not be significant. The Company's business and operating systems were installed in 1996 and necessary Year 2000 conversion requirements will be achieved through routine upgrades and maintenance to these systems. These upgrades are expected to be completed by the end of 1998.

The Company had no material capital expenditure commitments as of December 31, 1997.

NEW ACCOUNTING PRONOUNCEMENTS

In February 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 128, "Earnings Per Share" (SFAS 128) which changes the method of calculating earnings per share. SFAS 128 requires the presentation of "basic" earnings per share and "diluted" earnings per share. Basic earnings per share is computed by dividing the net income available to common shareholders by the weighted average number of shares outstanding. For purposes of calculating diluted earnings per share the denominator includes both the weighted average number of shares of common stock outstanding and potential common stock, such as stock options. Earnings per share for all periods presented have been restated to comply with SFAS 128.

In February 1998, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 98 (SAB 98), which supersedes SAB 83 and provides new guidance for the calculation of earnings per share in an initial public offering. SAB 98 is effective upon a Company's adoption of SFAS 128 and impacts the Company's calculation of earnings per share for fiscal periods prior to the Company's initial public offering in November 1996, and for the year ended December 31, 1996. Earnings per share amounts for these periods have been restated to comply with SAB 98.

In October 1997, the Accounting Standards Executive Committee of the American

Institute of Certified Public Accountants (AcSEC) issued Statement of Position 97-2 "Software Revenue Recognition" (SOP 97-2), which will become effective with respect to all reporting periods subsequent to January 1, 1998. Management does not expect SOP 97-2 to have a material effect on the Company's results of operations as the Company's revenue recognition policy is substantially consistent with the provisions of SOP 97-2.

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130) and Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" (SFAS 131). SFAS 130 establishes standards for reporting of comprehensive income and its components in the consolidated financial statements. SFAS 131 establishes standards for reporting information on operating segments in interim and annual financial statements. Both SFAS 130 and SFAS 131 will become effective for the Company beginning in 1998 and will require additional financial statement disclosures only.

EFFECTS OF INFLATION

Management believes that financial results have not been significantly impacted by inflation and price changes.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Company's Financial Statements and Schedules, together with the auditors' reports thereon, appear at pages F-1 through F-12, and S-1 through S-2, respectively, of this Form 10-K.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information concerning the directors of the Registrant is hereby incorporated by reference from the information contained under the heading " Election of Directors" in the Registrant's definitive proxy statement related to the Registrant's 1997 Annual Meeting of Stockholders which will be filed with the Commission within 120 days after the close of the fiscal year (the "Definitive Proxy Statement").

Certain information concerning directors and executive officers of the Registrant is hereby incorporated by reference to the information contained under the heading "Occupations of Directors and Executive Officers" in the Registrant's Definitive Proxy Statement.

ITEM 11. EXECUTIVE COMPENSATION

Information concerning executive compensation is hereby incorporated by reference to the information contained under the heading "Compensation and Other Information Concerning Directors and Officers" in the Definitive Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGMENT

Information concerning security ownership of certain beneficial owners and management is hereby incorporated by reference to the information contained under the heading "Securities Ownership of Certain Beneficial Owners and Management" in the Definitive Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information concerning certain relationships and related transactions is hereby incorporated by reference to the information contained under the heading "Certain Relationships and Related Transactions" in the Definitive Proxy Statement.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a)(1) INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

The following Consolidated Financial Statements of the Registrant are filed as part of this report:

	Page
Report of Independent Accountants	F-1
Consolidated Balance Sheet as of December 31, 1996 and 1997	F-2
Consolidated Statement of Operations for the years ended December 31, 1995, 1996 and 1997	F-3
Consolidated Statement of Stockholders' Equity for the years ended December 31, 1995, 1996 and 1997	F-4
Consolidated Statement of Cash Flows for the years ended December 31, 1995, 1996 and 1997	F-5
Notes to Consolidated Financial Statements	F-6

(a)(2) INDEX TO FINANCIAL STATEMENT SCHEDULES

The following Financial Statement Schedule of the Registrant is filed as part of this report:

	Page
Schedule I - Report of Independent Accountants on Financial Statement Schedule	S-1
Schedule II - Valuation and Qualifying Accounts and Reserves	S-2

Schedules not listed above have been omitted because the information requested to be set forth therein is not applicable or is shown in the accompanying Consolidated Financial Statements or notes thereto.

(a) (3) INDEX TO EXHIBITS

See attached Exhibit Index of this Annual Report on Form 10-K.

(b) REPORTS ON FORM 8-K

On December 10, 1997 the Company filed a current report on Form 8-K announcing that the Company had acquired all of the outstanding stock of IPC Interactive Pte. Ltd. pursuant to a Stock Purchase Agreement by and among the Company and the parties listed therein.

(c) EXHIBITS

The Company hereby files as part of this Form 10-K the Exhibits listed in Item 14(a)(3) above. Exhibits which are incorporated herein by reference can be inspected and copied at the public reference facilities maintained by the Securities and Exchange Commission (the "Commission"), 450 Fifth Street, N.W., Washington, D.C., 20549 and at the Commission's regional offices located at Seven World Trade Center, 13th Floor, New York, New York 10048, and at the Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of such material can also be obtained from the Public Reference Section of the Commission, 450 Fifth Street, N.W., Washington, D.C., 20549, at prescribed rates. In addition the Company is required to file electronic versions of certain of these documents with the Commission through the Commission's Electronic Data Gathering, Analysis and Retrieval (EDGAR) system. The Commission maintains a World Wide Web site at http://www.sec.gov that contains the report, proxy and information statements and other information regarding registrants that file electronically with the Commission. The Common Stock of the Company is traded on the Nasdaq National Market. Reports and other information concerning the Company may be inspected at the National Association of Securities Dealers, Inc. 1735 K Street, N.W., Washington, D.C. 20006.

(d) FINANCIAL STATEMENT SCHEDULES

The Company hereby files as part of this Form 10-K the consolidated financial statements schedules listed in Item 14(a)(2) above, which are attached hereto.

SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) of the Securities Exchange Act of 1934, SeaChange International, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: MARCH 31, 1998

SEACHANGE INTERNATIONAL, INC.

by: /s/ William C. Styslinger, III

William C. Styslinger, III
President, Chief Executive Officer,
Chairman of the Board and Director.

POWER OF ATTORNEY AND SIGNATURES

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints William C. Styslinger, III and Edward J. McGrath, jointly and severally, his attorney-in-fact, each with the power of substitution, for him in any and all capacities, to sign any amendments to this Report on Form 10-K and to file same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

SIGNATURE	TITLE(S)	DATE
/s/ William C. Styslinger, III William C. Styslinger, III	President, Chief Executive Officer, Chairman of the Board and Director (Principal Executive Officer)	March 31, 1998
/s/ Joseph S. Tibbetts, Jr. Joseph S. Tibbetts, Jr.	Vice President, Finance and Administration, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)	March 31, 1998
/s/ Martin R. Hoffmann Martin R. Hoffmann	Director	March 31, 1998
/s/ Edward J. McGrath Edward J. McGrath	Director	March 31, 1998
/s/ Paul Saunders Paul Saunders	Director	March 31, 1998
/s/ Carmine Vona Carmine Vona	Director	March 31, 1998

EXHIBIT INDEX

EXHIBIT NO.	DESCRIPTION	PAGE
3.1	Amended and Restated Certification of Incorporation (incorporated by reference to the Registrant's Annual Report on Form 10-K filed March 28, 1997).	
3.2	Amended and Restated By-laws of the Company (incorporated by reference to the Registrant's Annual Report on Form 10-K filed March 28, 1997).	
4.1 (1)	Form of Stock Restriction Agreement (incorporated by reference to Exhibit 4.3 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).	
4.2 (1)	Form of Stock Restriction Agreement Admendment (incorporated by reference to Exhibit 4.4 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).	
10.1 (1)	Amended and Restated 1995 Stock Option Plan (incorporated by reference to Exhibit 10.1 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).	
10.2 (1)	1996 Non-Employee Director Stock Option Plan (incorporated by reference to Exhibit 10.2 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).	
10.3	Lease Agreement dated March 10, 1995 between Thomas B. O'Brien, Trustee of Jelric Realty Trust u/d/t dated 9/18/68 and the Company (incorporated by reference to Exhibit 10.3 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).	
10.4	Sublease Agreement dated March 19, 1996 between IPL Systems, Inc.	

	and the Company (incorporated by reference to Exhibit 10.4 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.5	Indenture of Lease dated October 1, 1995 between Alden T. Greenwood and the Company (incorporated by reference to Exhibit 10.5 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.6 (1)	Letter Agreement dated as of June 12, 1996 between Joseph S. Tibbetts, Jr. And the Company (incorporated by reference to Exhibit 10.6 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.7	License Agreement dated May 30, 1996 between Summit Software Systems, Inc. and the Company (incorporated by reference to Exhibit 10.7 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.8	Loan and Security Agreement, dated September 25, 1996, between the Company and BayBank, N.A. (incorporated by reference to Exhibit 10.8 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.9	Working Capital Line of Credit-Master Note dated September 25, 1996, between the Company and BayBank, N.A. (incorporated by reference to Exhibit 10.9 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.10	Equipment Line of Credit-Master Note dated September 25, 1996, between the Company and BayBank, N.A. (incorporated by reference to Exhibit 10.10 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.11	Sales and Marketing Representative Agreement dated October 11, 1996, between the Company and Media Power S.n.c. (incorporated by reference to Exhibit 10.11 to the Registrant's Registration Statement on Form S-1, Registration No. 333-12233).
10.12*	Second Amendment To Loan and Security Agreement, dated September 24, 1997 between the Company and BankBoston, N.A.
10.13	Stock Purchase Agreement, dated December 10, 1997, by and among the Company, IPC Interactive Pte. Ltd. and the shareholders of IPC Interactive Pte. Ltd. (incorporated by reference to the Exhibits to the Company's Report on Form 8-K dated December 10, 1997).
10.14	Registration Rights Agreement, dated December 10, 1997, by and among the Company, IPC Interactive Pte. Ltd. and the shareholders of IPC Interactive Pte. Ltd. (incorporated by reference to

</TABLE>

	the Exhibits to the Company's Report on Form 8-K dated December 10, 1997).
10.15	Escrow Agreement, dated December 10, 1997, by and among the Company, IPC Interactive Pte. Ltd., the shareholders of IPC Interactive Pte. Ltd. and State Street Bank and Trust Company (incorporated by reference to the Exhibits to the Company's Report on Form 8-K dated December 10, 1997).
11.1	Statement re: computation of earnings per share.
21.1*	Subsidiaries of the Company.
23.1*	Consent of Price Waterhouse LLP.
27.1*	Financial Data Schedule (For SEC Edgar Filing Only; Intentionally Omitted).

- -------------

* Filed herewith.

(1) Indicates a management contract or any compensatory plan or arrangement.

SEACHANGE INTERNATIONAL, INC.

REPORT OF INDEPENDENT ACCOUNTANTS ON
FINANCIAL STATEMENT SCHEDULE

To the Board of Directors of SeaChange International, Inc.

Our audits of the consolidated financial statements referred to in our report

dated January 22, 1998 appearing on page F-1 of this Form 10-K also include an audit of the Financial Statement Schedule listed in Item 14(a) of this Form 10-K. In our opinion, this Financial Statement Schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

PRICE WATERHOUSE LLP

Boston, Massachusetts
January 22, 1998

Schedule II

SEACHANGE INTERNATIONAL, INC.

VALUATION OF QUALIFYING ACCOUNTS AND RESERVES

<TABLE>
<CAPTION>

	Balance at beginning of period	Charged to costs and expenses	Deductions and write-offs	Other	Balance at end of period
<S>	<C>	<C>	<C>	<C>	<C>
Allowance for Doubtful Accounts:					
Year ended December 31, 1995	$ --	$ 40,000	$ --	$ --	$ 40,000
Year ended December 31, 1996	$ 40,000	$ 133,000	$ --	$ --	$ 173,000
Year ended December 31, 1997	$173,000	$ 485,000	$ (174,000)	$ 75,000	$ 559,000
Inventory Valuation Allowance:					
Year ended December 31, 1995	$ --	$ 56,200	$ --	$ --	$ 56,200
Year ended December 31, 1996	$ 56,200	$ 693,800	$ --	$ --	$ 750,000
Year ended December 31, 1997	$750,000	$1,730,000	$(1,076,000)	$100,000	$1,504,000

</TABLE>

Exhibit 10.12

SECOND AMENDMENT TO LOAN
AND SECURITY AGREEMENT

This Second Amendment to Loan and Security Agreement is entered into on this 24th day of September, 1997 by and between SeaChange International, Inc., a Delaware corporation with its principal address at 124 Acton Street, Maynard, Massachusetts (hereinafter, the "Borrower"), and BankBoston, N.A., successor by merger with BayBank, N.A., a national banking association, with offices located at 100 Federal Street, Boston, Massachusetts (hereinafter, the "Lender"), in consideration of the mutual covenants contained herein and the benefits to be derived herefrom.

WITNESSETH:

WHEREAS, pursuant to the terms of a Loan and Security Agreement dated September 25, 1996 by and between the Borrower and Lender, as amended by a certain First Amendment to Loan and Security Agreement dated March 30, 1997 (as amended, the "Loan Agreement"), the Lender agreed to establish a Working Capital Line (as defined in the Loan Agreement) in the Borrower's favor in the amount of the Borrower's Availability (as defined in the Loan Agreement); and

WHEREAS, the Borrower has requested that the Lender agree to modify the Loan Agreement by extending the Working Capital Line Maturity Date (as defined in the Loan Agreement) by an additional twelve (12) months.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Borrower and the Lender hereby agree as follows:

1. The Loan Agreement is hereby amended by deleting the following text appearing in Section 12-1 of the Loan Agreement:

"(a) The Working Capital Line shall be terminated upon the sooner of (the "WORKING CAPITAL LINE MATURITY DATE"):

(i) the entry of any order for relief with respect to the Borrower under the Bankruptcy Code; or

(ii) at the Lender's option, upon or after the occurrence of an Event of Default, as defined hereunder; or

(iii) September 24, 1997."

and by substituting therefor the following:

"(a) The Working Capital Line shall be terminated upon the sooner of (the "WORKING CAPITAL LINE MATURITY DATE"):

(i) the entry of any order for relief with respect to the Borrower under the Bankruptcy Code; or

(ii) at the Lender's option, upon or after the occurrence of an Event of Default, as defined hereunder; or

(iii) September 24, 1998."

2. The Loan Agreement is hereby amended by deleting the following text appearing in Section 11-1 of the Loan Agreement:

"If to the Lender: BayBank, N.A.
7 New England Executive Park
Burlington, Massachusetts 01803
Attention: Stephen C. Buzzell
Vice President"

and by substituting therefor the following:

"If to the Lender: BankBoston, N.A.
100 Federal Street
Boston, Massachusetts 02110
Attention: Stephen C. Buzzell
Vice President"

3. The Borrower hereby ratifies, confirms and reaffirms, all and singular the terms and conditions of any and all documents, instruments and/or agreements executed and/or delivered by the Borrower to the Lender in connection with the loan arrangement evidenced by the Loan Agreement.

4. The Borrower acknowledges, confirms and agrees that it has no offsets, defenses or counterclaims against the Lender with respect to any of the Liabilities (as defined in the Loan Agreement) or other obligations due and owing to the Lender, and to the extent that the Borrower has or had any such offsets, defenses, or counterclaims, the Borrower hereby specifically WAIVES and RELEASES any and all rights to such offsets, defenses and counterclaims.

Except as amended hereby, all terms and conditions of the Loan Agreement shall remain in full force and effect and are hereby ratified and confirmed.

("BORROWER")
SEACHANGE INTERNATIONAL, INC.

By: /s/ Joseph S. Tibbetts, Jr.

Name: Joseph S. Tibbetts, Jr.

Title: Vice President, Finance & Administration, CFO and Treasurer

("LENDER")
BANKBOSTON, N.A.

By: /s/ Stephen C. Buzzell

Name: Stephen C. Buzzell

Title: Vice President

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF SEACHANGE INTERNATIONAL, INC.

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of operations, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of SeaChange International, Inc. and its subsidiaries at December 31, 1996 and 1997 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles. 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 of these statements in accordance with generally accepted auditing standards 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 audits provide a reasonable basis for the opinion expressed above.

/s/ Price Waterhouse LLP

Price Waterhouse LLP
Boston, Massachusetts
January 22, 1998

- ---------------------------------

CONSOLIDATED BALANCE SHEET
(IN THOUSANDS, EXCEPT SHARE DATA)

<TABLE>
<CAPTION>

	December 31, 1996	December 31, 1997
<S>	<C>	<C>
ASSETS		
Current assets:		
Cash and cash equivalents	$23,394	$ 2,973
Marketable securities	--	9,310
Accounts receivable, net of allowance for doubtful accounts of $173 at December 31, 1996 and $559 at December 31, 1997	7,426	12,535
Inventories	9,153	13,713
Prepaid expenses	250	2,336
Deferred income taxes	575	1,091
Total current assets	40,798	41,958
Property and equipment, net	4,705	8,303
Other assets	532	81
Goodwill and intangibles, net	--	1,608
	$46,035	$51,950
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 7,305	$ 8,765
Accrued expenses	1,809	2,718
Customer deposits	2,899	2,049
Deferred revenue	2,192	3,851
Income taxes payable	--	85
Total current liabilities	14,205	17,468
Commitments (Note 10)		
STOCKHOLDERS' EQUITY		
Common stock, $.01 par value; 50,000,000 shares authorized; 12,859,234 shares and 13,593,594 shares issued at December 31, 1996 and 1997, respectively	129	136
Additional paid-in capital	26,167	31,218
Retained earnings	5,534	3,114
Treasury stock, none and 9,000 shares at December 31, 1996 and 1997, respectively	--	--
Cumulative translation adjustment	--	14
Total stockholders' equity	31,830	34,482
	$46,035	$51,950

</TABLE>

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

- ---

CONSOLIDATED STATEMENT OF OPERATIONS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
<TABLE>
<CAPTION>

	Year Ended December 31,		
	1995	1996	1997
<S>	<C>	<C>	<C>
REVENUES			
Systems	$ 21,999	$ 45,745	$ 60,414
Services	1,204	3,521	7,473
	23,203	49,266	67,887
COSTS OF REVENUES			
Systems	14,917	27,133	34,740
Services	1,641	4,030	7,607
	16,558	31,163	42,347
Gross profit	6,645	18,103	25,540
OPERATING EXPENSES			
Research and development	2,367	5,393	11,758
Selling and marketing	1,609	4,254	6,049
General and administrative	858	2,064	3,744
Write-off of acquired in-process research and development	--	--	5,290
	4,834	11,711	26,841
Income (loss) from operations	1,811	6,392	(1,301)
Interest income, net	113	353	657
Income (loss) before income taxes	1,924	6,745	(644)
Provision for income taxes	713	2,483	1,776
Net income (loss)	$ 1,211	$ 4,262	$(2,420)
Basic earnings (loss) per share	$ .33	$ .82	$ (.24)
Diluted earnings (loss) per share	$ .11	$ .36	$ (.24)
Shares used in calculating:			
Basic earnings per share	3,654,088	5,187,993	10,276,711
Diluted earnings per share	11,121,157	11,745,866	10,276,711

</TABLE>

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

- --

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(IN THOUSANDS, EXCEPT SHARE DATA)
<TABLE>
<CAPTION>

	Series A convertible preferred stock		Common stock		
	Number of shares	Amount	Number of shares	Par value	Additional paid-in capital
<S>	<C>	<C>	<C>	<C>	<C>
Balance at December 31, 1994	11,808	$ --	9,309,615	$ 93	$ 367
Sale of common stock	--	--	316,125	3	7
Loans to stockholders	--	--	--	--	--
Net income	--	--	--	--	--
Balance at December 31, 1995	11,808	--	9,625,740	96	374
Purchase of treasury stock	--	--	--	--	--
Sale of common stock, net of stock issuance costs	--	--	1,810,000	18	24,052
Conversion of preferred stock into common stock	(11,808)	--	2,260,856	23	3,985
Issuance of common stock pursuant to to exercise of stock options	--	--	9,223	--	9
Compensation expense associated with stock issuance	--	--	--	--	126
Issuance of common					

stock pursuant to purchased research and development	--	--	9,615	--	144
Retirement of treasury stock	--	--	(856,200)	(8)	(2,523)
Net income	--	--	--	--	--
Balance at December 31, 1996	--	--	12,859,234	129	26,167
Purchase of treasury stock	--	--	(9,000)	--	--
Compensation expense associated with stock issuance	--	--	--	--	45
of common stock pursuant to exercise of stock options	--	--	88,999	1	203
Issuance of common stock in connection with employee stock purchase plan	--	--	29,361	--	479
Issuance of common stock in connection with acquisition of IPC Interactive Pte. Ltd.	--	--	625,000	6	4,324
Translation adjustment	--	--	--	--	--
Net loss	--	--	--	--	--
Balance at December 31, 1997	--	$ --	13,593,594	$ 136	$31,218

<CAPTION>

	Retained earnings and currency translation adjustment	Treasury stock	Notes receivable from stockholders	Total stockholders' equity
<S>	<C>	<C>	<C>	<C>
Balance at December 31, 1994	$ 61	$ (4)	$ --	$ 517
Sale of common stock	--	--	--	10
Loans to stockholders	--	--	(795)	(795)
Net income	1,211	--	--	1,211
Balance at December 31, 1995	1,272	(4)	(795)	943
Purchase of treasury stock	--	(2,527)	795	(1,732)
Sale of common stock, net of stock issuance costs	--	--	--	24,070
Conversion of preferred stock into common stock	--	--	--	4,008
Issuance of common stock pursuant to to exercise of stock options	--	--	--	9
Compensation expense associated with stock issuance	--	--	--	126
Issuance of common stock pursuant to purchased research and development	--	--	--	144
Retirement of treasury stock	--	2,531	--	--
Net income	4,262	--	--	4,262
Balance at December 31, 1996	5,534	--	--	31,830
Purchase of treasury stock	--	--	--	--
Compensation expense associated with stock issuance	--	--	--	45
of common stock pursuant to exercise of stock options	--	--	--	204
Issuance of common stock in connection with employee stock purchase plan	--	--	--	479
Issuance of common stock in connection with acquisition of IPC Interactive Pte. Ltd.	--	--	--	4,330
Translation adjustment	14	--	--	14
Net loss	(2,420)	--	--	(2,420)
Balance at December 31, 1997	$ 3,128	$ --	$ --	$ 34,482

</TABLE>

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

- ---

CONSOLIDATED STATEMENT OF CASH FLOWS
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS (IN THOUSANDS)

<TABLE>
<CAPTION>

<S>	Year Ended December 31, 1995 <C>	1996 <C>	1997 <C>
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income (loss)	$ 1,211	$ 4,262	$(2,420)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	230	1,436	2,802
Inventory valuation allowance	56	694	1,730
Compensation expense associated with stock and stock options	--	126	45
Write-off of acquired in-process research and development	--	--	5,290
Research and development expense associated with common stock issuance	--	144	--
Deferred income taxes	(85)	(424)	(516)
Changes in assets and liabilities, net of the effect of the acquisition of IPC Interactive Pte. Ltd.:			
Accounts receivable	(2,035)	(4,091)	(4,381)
Inventories	(2,280)	(9,134)	(7,069)
Prepaid expenses and other assets	(15)	(468)	(1,470)
Accounts payable	2,069	4,165	(1,164)
Accrued expenses	1,693	(126)	(109)
Customer deposits	700	817	(3,260)
Deferred revenue	615	1,425	1,273
Income taxes payable	599	(720)	85
Net cash provided by (used in) operating activities	2,758	(1,894)	(9,164)
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of software	--	(450)	--
Purchases of property and equipment	(659)	(2,792)	(2,158)
Proceeds from sale and maturity of marketable securities	--	--	8,966
Purchases of marketable securities	--	--	(18,276)
Cash acquired related to the acquisition of IPC Interactive Pte. Ltd., net of transaction costs	--	--	665
Net cash used in investing activities	(659)	(3,242)	(10,803)
CASH FLOWS FROM FINANCING ACTIVITIES			
Repayment of notes payable	(8)	--	--
Repayment of line of credit	--	--	(700)
Proceeds from sale of convertible preferred stock, net	4,008	--	--
Proceeds from sale of common stock, net	10	24,079	683
Purchase of treasury stock	--	(2,023)	--
Payment of loans to related parties	--	--	(437)
(Loans to) repayments from stockholders	(795)	290	--
Net cash provided by (used in) financing activities	3,215	22,346	(454)
Net increase (decrease) in cash and cash equivalents	5,314	17,210	(20,421)
Cash and cash equivalents, beginning of year	870	6,184	23,394
Cash and cash equivalents, end of year	$ 6,184	$23,394	$ 2,973

</TABLE>

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

- ---

CONSOLIDATED STATEMENT OF CASH FLOWS
INCREASE(DECREASE) IN CASH AND CASH EQUIVALENTS (IN THOUSANDS)
(CONTINUED)

<TABLE>
<CAPTION>

<S>	Year Ended December 31, 1995 <C>	1996 <C>	1997 <C>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Income taxes paid	$180	$3,854	$ 1,691
SUPPLEMENTAL DISCLOSURE OF NONCASH ACTIVITY			
Receipt of computer equipment in lieu of cash payment of accounts receivable from customer	$ 75	$ --	$ --
Transfer of items originally classified as inventories to fixed assets	$576	$1,726	$ 1,829
Purchase of treasury stock in lieu of cash payment of notes receivable from stockholders	$ --	$ 505	$ --

Acquisition of all of the outstanding shares of IPC Interactive Pte. Ltd. (Note 3)	
Fair value of assets acquired (including intangible assets and in-process research and development)	$12,396
Fair value of common shares issued	(4,330)
Transaction costs	(475)
Liabilities assumed	$ 7,591

</TABLE>

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 | NATURE OF BUSINESS

The Company develops computer systems to digitally manage, store and distribute video. Through December 31, 1997, substantially all of the Company's revenues were derived from the sale of digital video insertion systems, movie systems and related services to cable television operators and telecommunications companies in the United States and internationally.

On December 10, 1997, the Company acquired all of the outstanding capital stock of IPC Interactive Pte. Ltd. ("IPC"). IPC, together with the Company's centralized video server platform, provides interactive television network systems to the hospitality and commercial property markets. Additionally, IPC deploys and operates its interactive network television systems at customer locations and charges fees for providing services and content, primarily movies.

2 | SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Significant accounting policies followed in the preparation of the accompanying consolidated financial statements are as follows:

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

REVENUE RECOGNITION

Revenues from the sales of systems are recognized upon shipment provided that there are no uncertainties regarding customer acceptance and collection of the related receivables is probable. If such uncertainties exist, such as performance criteria beyond the Company's standard terms and conditions, revenue is recognized upon customer acceptance. Installation and training revenue is deferred and recognized as these services are performed. Revenue from technical support and maintenance contracts is deferred and recognized ratably over the period of the related agreements, generally twelve months, if billed in advance. Customer deposits represent advance payments from customers for systems. Revenue from content fees, primarily movies, are recognized in the period earned based on noncancelable agreements.

CONCENTRATION OF CREDIT RISK, SIGNIFICANT CUSTOMERS AND EXPORT SALES

Financial instruments which potentially expose the Company to concentrations of credit risk include trade accounts receivable and marketable securities. To minimize this risk, the Company evaluates customers' financial condition and requires advance payments from certain of its customers. At December 31, 1996 and 1997, the Company had an allowance for doubtful accounts of $173,000 and $559,000, respectively, to provide for potential credit losses and such losses to date have not exceeded management's expectations. The Company invests its excess cash in marketable securities, primarily municipal securities with strong credit ratings.

For the years ended December 31, 1995, 1996 and 1997, certain customers accounted for more than 10% of the Company's revenues. Individual customers accounted for 29%, 29%, 16% and 12% of revenues in 1995; 29%, 17%, 13% and 12% in 1996; and 24%, 18% and 10% in 1997.

Sales to international customers accounted for 12% of total revenues in the year ended December 31, 1997. In 1997, international sales to significant geographic areas were approximately $2,696,000 in North and South America, $4,211,000 in Europe and $1,125,000 in the rest of the world.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

CASH AND CASH EQUIVALENTS

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. The Company invests its excess cash in money market funds, municipal securities and corporate debt securities that are subject to minimal credit and market risk. Cash equivalents are classified as available-for-sale and are carried at market value, and any unrealized gains or losses are recorded as a part of stockholders' equity.

PROPERTY AND EQUIPMENT

Property and equipment consist of office and computer equipment, leasehold improvements, demonstration equipment, deployed assets and spare components and assemblies used to service the Company's installed base. Demonstration equipment consists of systems manufactured by the Company for use in marketing and selling. Property and equipment are recorded at cost and depreciated using the straight-line method over their estimated useful lives. Leasehold improvements are amortized over the shorter of their estimated useful lives or the term of the respective leases by use of the straight-line method. Deployed assets consist primarily of hardware owned and operated by the Company and installed at customer locations. Deployed assets are depreciated over the life of the related service agreements ranging from 2 to 5 years. Maintenance and repair costs are expensed as incurred.

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INVENTORIES

Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out (FIFO) method. Inventories consist primarily of components and subassemblies and finished products held for sale. Rapid technological change and new product introductions and enhancements could result in excess or obsolete inventory. To minimize this risk, the Company evaluates inventory levels and expected usage on a periodic basis and records valuation allowances as required.

The Company is dependent upon certain vendors for the manufacture of significant components of its digital advertising insertion system and its movie systems. If these vendors were to become unwilling or unable to continue to manufacture these products in required volumes, the Company would have to identify and qualify acceptable alternative vendors. The inability to develop alternative sources, if required in the future, could result in delays or reductions in product shipments.

GOODWILL AND INTANGIBLE ASSETS

Goodwill and assembled workforce acquired in connection with the acquisition of IPC (Note 3) are amortized on a straight-line basis over five to seven years. Software acquired in connection with the acquisition is amortized over the greater of the amount computed using (a) the ratio that current gross revenues for related products bear to total current and anticipated future gross revenues for that product or (b) on a straight-line basis over the remaining estimated life of three years.

RESEARCH AND DEVELOPMENT AND SOFTWARE DEVELOPMENT COSTS

Costs incurred in the research and development of the Company's products are expensed as incurred, except for certain software development costs. Costs associated with the development of computer software are expensed prior to establishing technological feasibility and capitalized thereafter until the product is released for sale. Software development costs eligible for capitalization to date have not been material to the Company's financial statements. Costs associated with acquired software rights are capitalized if technological feasibility of the software has been established.

STOCK COMPENSATION

Employee stock awards under the Company's compensation plans are accounted for in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25). In January 1996, the Company adopted the disclosure requirements of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS 123). Nonemployee stock awards are accounted for in accordance with SFAS 123.

FOREIGN CURRENCY TRANSLATION

The Company has determined that the functional currency of its foreign subsidiaries is the local currency. Accordingly, assets and liabilities are translated to U.S. dollars at current exchange rates as of each balance sheet date. Income and expense items are translated using average exchange rates during the year. Cumulative currency translation adjustments are presented as a separate component of stockholders' equity. Transaction gains and losses and unrealized gains and losses on intercompany receivables have not been material to date.

ADVERTISING COSTS

Advertising costs are charged to expense as incurred. Advertising costs were $174,000, $328,000 and $659,000 for the years ended December 31, 1995, 1996 and 1997, respectively.

EARNINGS PER SHARE

Statement of Financial Accounting Standards No. 128, "Earnings Per Share" (SFAS 128), became effective for financial statements issued for fiscal periods ending after December 15, 1997 and requires restatement of all prior period earnings per share data. SFAS 128 replaced Accounting Principles Board Opinion No. 15 and requires the presentation of "basic" earnings per share and "diluted" earnings per share. Basic earnings per share is computed by dividing income available to common shareholders by the weighted average shares of common stock outstanding during the period. For the purposes of calculating diluted earnings per share the denominator includes both the weighted average number of shares of common stock outstanding during the period and the weighted average number of potential common stock, such as stock options and restricted stock.

In addition, on February 3, 1998 the Securities and Exchange Commission issued Staff Accounting Bulletin (SAB) No. 98, which supersedes SAB No. 83, includes new guidance with respect to historical earnings per share computations in an initial public offering and is effective upon a company's adoption of SFAS 128. Pursuant to SAB No. 98, nominal issuances of common stock during the period January 1, 1995 through the effective date of the initial public offering would be included in computing basic earnings per share as if outstanding for all periods presented. In computing diluted earnings per share for such periods, nominal issuances of common stock and potential common stock would be included as if outstanding for all periods presented. During the period January 1, 1995 through the effective date of the initial public offering, the Company had no nominal issuance of any common stock or potential common stock as defined by SAB No. 98.

The Company adopted SFAS 128 and SAB No. 98 in the fourth quarter of 1997 and has restated earnings per share for all periods presented, as required.

For the year ended December 31, 1997, potential common stock of 468,311 common shares issuable upon the exercise of stock options and 2,661,825 shares of unvested restricted common stock are antidilutive because the Company recorded a net loss for the year and therefore have been excluded from the diluted earnings per share computation.

- --

Below is a summary of the shares used in calculating basic and diluted earnings per share for the years indicated:

<TABLE>
<CAPTION>

<S>	Year Ended December 31, 1995 <C>	1996 <C>	1997 <C>
Weighted average number of shares outstanding	3,654,088	5,187,993	10,276,711
Shares attributable to Series A redeemable convertible preferred stock	1,771,200	1,476,000	--
Shares attributable to Series B redeemable convertible preferred stock	170,582	568,607	--
Shares attributable to unvested restricted common stock	5,471,500	4,109,925	--
Dilutive stock options	53,787	403,341	--
Shares used in calculating diluted earnings per share	11,121,157	11,745,866	10,276,711

</TABLE>

NEW ACCOUNTING PRONOUNCEMENTS

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130) and Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" (SFAS 131). SFAS 130 establishes standards for reporting comprehensive income and its components in the consolidated financial statements. SFAS 131 establishes standards for reporting information on operating segments in interim and annual financial statements. SFAS 130 and SFAS 131 require disclosure only and will have no impact on the Company's consolidated financial position or results of operations.

In October 1997, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants (AcSEC) issued Statement of Position 97-2, "Software Revenue Recognition" (SOP 97-2), which will become effective on January 1, 1988. Management does not expect SOP 97-2 to have a material effect on the Company's results of operations as the Company's revenue recognition policy is substantially consistent with the provisions of SOP 97-2.

3 | ACQUISITION

On December 10, 1997, the Company exchanged 625,000 shares of its common stock

for all of the outstanding capital stock of IPC. IPC provides interactive television network systems to the hospitality and commercial property markets. The total purchase price, including transaction costs, was $4,805,000. The acquisition was accounted for under the purchase method. Accordingly, the purchase price was allocated to the estimated fair value of the acquired assets and liabilities based upon an independent appraisal. A portion of the purchase price was allocated to in-process research and development, resulting in an immediate charge to the Company's operations of $5,290,000 at the date of acquisition. The amount allocated to in-process research and development represented technology which had not reached technological feasability and had no alternative future use. The appraisal also valued intangibles, including assembled workforce and software. Goodwill and intangibles, net of related accumulated amortization of $27,000, at December 31, 1997 totaled $1,608,000. The consolidated results of operations include the operating results of IPC from the date of acquisition.

The purchase price was allocated to the acquired assets and liabilities as follows:

Tangible assets	$ 5,471,000
Assumed liabilities	(7,591,000)
Intangible assets:	
In-process research and development	$ 5,290,000
Software	850,000
Assembled workforce	280,000
Goodwill	505,000
	$ 4,805,000

Included in assumed liabilities were a line of credit of $700,000 and notes payable to related parties of $437,000. The notes payable to related parties were due to two companies owned by new shareholders as a result of the acquisition. The Company paid these assumed liabilities in full and cancelled the line of credit prior to December 31, 1997.

The Company has renamed IPC to GuestServe Networks.

The following unaudited pro forma data summarizes the consolidated results of the Company and IPC as if the acquisition had occurred on February 1, 1996 (inception of IPC) and excludes the $5,290,000 charge for in-process research and development. The unaudited pro forma information is not necessarily indicative either of results of operations that would have occurred had the purchase been made at the beginning of the periods presented, or of future results of operations of the combined companies.

	Pro forma for the year ended December 31, 1996 (unaudited)	1997 (unaudited)
Revenues	$60,372,000	$75,573,000
Net income (loss)	$ 1,085,000	$(3,403,000)
Basic earnings (loss) per share	$ .19	$ (.31)
Diluted earnings (loss) per share	$ .09	$ (.31)

4 | CONSOLIDATED BALANCE SHEET DETAIL
Cash equivalents and marketable securities consist of the following:

	December 31, 1996	1997
Cash equivalents:		
Money market funds	$ 297,000	$ 506,000
Municipal securities	12,600,000	1,550,000
Corporate debt securities	9,485,000	--
	22,382,000	2,056,000
Marketable securities:		
Municipal securities	--	9,310,000
	$22,382,000	$11,366,000

Marketable securities are classified as available-for-sale securities and are carried at fair market value, which approximates amortized cost. The

contractual maturities of all available-for-sale securities classified as cash equivalents are less than three months. Gross unrealized gains and losses on securities for the years ended December 31, 1996 and 1997, the cost of which is based upon the specific identification method, were not significant.

Inventories consist of the following:
<TABLE>
<CAPTION>

	December 31, 1996	December 31, 1997
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Components and assemblies	$6,524,000	$11,932,000
Finished products	2,629,000	1,781,000
	$9,153,000	$13,713,000

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Property and equipment consist of the following:
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	Estimated useful life (years)	December 31, 1996	December 31, 1997
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Office furniture and equipment	5	$ 432,000	$ 1,332,000
Computer and demonstration equipment	3	4,571,000	8,140,000
Deployed assets	3	-	497,000
Service and spare components	5	1,050,000	2,000,000
Leasehold improvements	1-3	107,000	304,000
		6,160,000	12,273,000
Less - Accumulated depreciation		1,455,000	3,970,000
		$ 4,705,000	$ 8,303,000

</TABLE>

Depreciation expense was $230,000, $1,246,000 and $2,515,000 for the years ended December 31, 1995, 1996 and 1997 respectively.

- ---

Accrued expenses consist of the following:
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	December 31, 1996	December 31, 1997
<S>	<C>	<C>
Accrued software license fees	$ 367,000	$ 630,000
Accrued sales and use taxes	608,000	338,000
Other accrued expenses	834,000	1,750,000
	$1,809,000	$2,718,000

</TABLE>

5 | INCOME TAXES

The components of the provision for income taxes are as follows:
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	Year ended December 31, 1995	1996	1997
<S>	<C>	<C>	<C>
Current provision:			
Federal	$652,000	$2,346,000	$1,920,000
State	146,000	561,000	371,000
	798,000	2,907,000	2,291,000
Deferred benefit:			
Federal	(65,000)	(324,000)	(394,000)
State	(20,000)	(100,000)	(121,000)
	(85,000)	(424,000)	(515,000)
	$713,000	$2,483,000	$1,776,000

</TABLE>

The components of deferred income taxes are as follows:
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	December 31,	
	1996	1997
Deferred tax assets:		
Inventories	$366,000	$ 769,000
Allowance for doubtful accounts	66,000	209,000
Deferred revenue	118,000	96,000
Software	122,000	176,000
Acquired net operating loss carryforward and basis differences	--	3,361,000
	672,000	4,611,000
Valuation allowance	--	(3,361,000)
Total deferred tax assets	672,000	1,250,000
Deferred tax liabilities:		
Property and equipment	83,000	157,000
Other	14,000	2,000
Total deferred tax liabilities	97,000	159,000
Net deferred income taxes	$575,000	$ 1,091,000

</TABLE>

Deferred income taxes reflect the tax impact of temporary differences between the amount of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws and regulations. Under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" the benefit associated with future deductible temporary differences is recognized if it is more likely than not that the benefit will be realized.

The valuation allowance of $3,361,000 relates to net operating loss carryforwards and tax basis differences acquired in the Company's purchase of IPC. These acquired deferred tax assets may only be utilized to offset future taxable income attributable to IPC. In addition, the recognition of these deferred tax assets are subject to Internal Revenue Code change in ownership rules which may limit the amount that can be utilized to offset future taxable income. The Company believes that the valuation allowance is appropriate given the weight of objective evidence, including the historical operating results of IPC. Any tax benefits subsequently recognized related to these assets will first reduce the remaining balance in goodwill and then other acquired intangible assets.

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Based on the weight of available evidence, the Company believes its remaining deferred tax assets will be realizable. The amount of the deferred tax asset considered realizable is subject to change based on future events. The Company will assess the need for the valuation allowance at each balance sheet date based on all available evidence.

At December 31, 1997, the Company had federal and state net operating loss carryforwards of approximately $5,980,000 which expire at various dates through 2012 and foreign net operating loss carryforwards of approximately $1,436,000 which do not expire.

The income tax provision computed using the federal statutory income tax rate differs from the Company's effective tax rate primarily due to the following:

<TABLE>
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	Year ended December 31,		
	1995	1996	1997
Statutory U.S. federal tax rate	$654,000	$2,293,000	$ (91,000)
State taxes, net of federal tax benefits	85,000	304,000	165,000
Other	--	--	145,000
Research and development tax credits	(54,000)	(135,000)	(334,000)
Foreign Sales Corporation exempt income	--	(20,000)	--
Nondeductible expenses, including write-off of acquired in-process research and development in 1997	28,000	41,000	1,891,000
	$713,000	$2,483,000	$1,776,000

</TABLE>

The Company's effective tax rates were 37.1% and 36.8% in 1995 and 1996, respectively. The Company's effective tax rate for 1997 was significantly impacted by the write-off of the acquired in-process research and development which, due to the tax-free nature of the transaction to IPC stockholders, is not deductible for tax purposes by the Company. Accordingly, in 1997 the Company recorded a tax provision of $1,776,000 despite a book pre-tax operating loss.

6 | CONVERTIBLE PREFERRED STOCK

SERIES B CONVERTIBLE PREFERRED STOCK

In October and November 1995, the Company sold 650,487 shares of Series B Redeemable Convertible Preferred Stock for $4,008,000, net of issuance costs of $86,000.

CONVERSION

Upon closing of the initial public offering in November 1996, the convertible preferred stock automatically converted into a total of 2,260,856 shares of common stock.

STOCK AUTHORIZATION

The Board of Directors is authorized to issue from time to time up to an aggregate of 5,000,000 shares of preferred stock, in one or more series. Each such series of preferred stock shall have the number of shares, designations, preferences, voting powers, qualifications and special or relative rights or privileges to be determined by the Board of Directors, including dividend rights, voting rights, redemption rights and sinking fund provisions, liquidation preferences, conversion rights and preemptive rights.

7 | COMMON STOCK

INITIAL PUBLIC OFFERING

On November 5, 1996, the Company sold 1,810,000 shares of common stock to the public in the Company's initial public offering at a price of $15.00 per share. Proceeds to the Company, net of offering expenses, amounted to $24,070,000.

STOCK SPLITS

Effective August 3, 1995, the Company's Board of Directors approved a 100-for-1 stock split of the Company's common stock. On September 6, 1996, the Board of Directors authorized a 3-for-2 stock split of the Company's common stock, which became effective on October 30, 1996. All shares of common stock, common stock options, preferred stock conversion ratios and per share amounts included in the accompanying consolidated financial statements have been adjusted to give retroactive effect to the stock splits for all years presented.

RESTRICTION AGREEMENTS

Certain common shares are subject to stock restriction and repurchase agreements under which the Company may repurchase unvested common shares at the original issuance price and vested common shares at fair value upon termination of a business relationship with the Company. Common shares subject to these agreements vest ratably over a five-year period and, at December 31, 1997, 2,109,300 of such shares are unvested.

TREASURY STOCK

In January 1996, the Company repurchased 431,250 shares of its common stock and 1,286 shares of Series A Stock from certain employees and directors of the Company. Of the common stock repurchased, 21,750 shares were held by the stockholders for less than six months from the time the shares became vested. Accordingly, compensation expense was recorded for the difference between the repurchase price and the original purchase price paid by the stockholders. Compensation expense recorded as a result of this transaction was $91,000. In December 1996, the Board of Directors voted to retire all shares of treasury stock held at December 31, 1996.

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In 1997, the Company repurchased 9,000 shares of its common stock from an employee of the Company. The shares were held for less than six months from the time the shares became vested. Accordingly, compensation expense was recorded for the difference between the repurchase price and the original purchase price paid by the stockholder. Compensation expense recorded as a result of this transaction was $45,000.

NOTES RECEIVABLE FROM STOCKHOLDERS

Interest on the principal amount outstanding of the notes receivable from stockholders accrued at a rate of 5.9% per annum. These loans were secured by common stock held by the noteholders and, consequently, the loans are reflected as an offset to stockholders' equity at December 31, 1995. In January 1996, the notes were settled in connection with the repurchase by the Company of the common shares and Series A preferred shares noted above.

RESERVED SHARES

At December 31, 1997, the Company had 2,152,417 shares of common stock reserved for issuance upon the exercise of common stock options and the purchase of stock under the Employee Stock Purchase Plan.

8 | STOCK PLANS

EMPLOYEE STOCK PURCHASE PLAN

In September 1996, the Company's Board of Directors adopted and the stockholders approved an employee stock purchase plan (the "Stock Purchase Plan"), effective January 1, 1997, which provides for the issuance of a maximum of 300,000 shares of common stock to participating employees who meet eligibility requirements. Employees who would immediately after the grant own 5% or more of the total combined voting power or value of the Company's stock and directors or who are not employees of the Company may not participate in the Stock Purchase Plan. The purchase price of the stock is 85% of the lesser of the market price of the common stock on the first or last business day of each six-month plan period. During 1997, 29,361 shares were issued under the Stock Purchase Plan.

1995 STOCK OPTION PLAN

The 1995 Stock Option Plan (the "1995 Stock Option Plan") provides for the grant of incentive stock options and nonqualified stock options for the purchase of up to an aggregate of 1,950,000 shares of the Company's common stock by officers, employees, consultants and directors of the Company. The Board of Directors is responsible for administration of the 1995 Stock Option Plan. The Board of Directors determines the term of each option, option exercise price, number of shares for which each option is granted and the rate at which each option is exercisable. Options generally vest ratably over five years. The Company may not grant an employee incentive stock options with a fair value in excess of $100,000 that are first exercisable during any one calendar year.

Incentive stock options may be granted to employees at an exercise price per share of not less than the fair value per common share on the date of the grant (not less than 110% of the fair value in the case of holders of more than 10% of the Company's voting stock). Nonqualified stock options may be granted to any officer, employee, director or consultant at an exercise price per share as determined by the Company's Board of Directors.

Options granted under the 1995 Stock Option Plan generally expire ten years from the date of the grant (five years for incentive stock options granted to holders of more than 10% of the Company's voting stock).

DIRECTOR STOCK OPTION PLAN

In June 1996, the Company's Board of Directors adopted and the stockholders approved a director stock option plan (the "Director Option Plan") which provides for the grant of options to full-time directors of the Company to purchase a maximum of 30,000 shares of common stock. Under the Director Option Plan, participating directors receive an option to purchase 3,375 shares of common stock. Options granted under the Director Option Plan vest as to 33-1/3% of the shares underlying the option immediately upon the date of the grant, and vest as to an additional 8-1/3% of the shares underlying the option at the end of each of the next 8 quarters, provided that the optionee remains a director. Directors will also receive, on each three-year anniversary of such director's option grant date, an additional option to purchase 3,375 shares of common stock, provided that such director continues to serve on the Board of Directors. All options granted under the Director Option Plan have an exercise price equal to the fair value of the common stock on the date of grant and a term of ten years from the date of grant.

- --

Transactions under the 1995 Stock Option Plan and the Director Option Plan during the years ended December 31, 1995, 1996 and 1997 are summarized as follows:
<TABLE>
<CAPTION>

	Year ended December 31,					
	1995		1996		1997	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Outstanding at beginning of period	327,120	$ .92	327,120	$ .92	739,334	$ 5.87
Granted	--	--	472,510	$8.79	585,536	$18.03
Exercised	--	--	(9,223)	$ .85	(88,999)	$ 2.30
Cancelled	--	--	(51,073)	$2.22	(92,814)	$17.81
Outstanding at end of period	327,120	$ .92	739,334	$5.87	1,143,057	$11.40
Options exercisable at period end	--		115,224		205,198	
Weighted average fair value of options granted during the period		$ .32		$4.33		$11.00

</TABLE>

The following table summarizes information about employee and director stock options outstanding at December 31, 1997:

<TABLE>

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Range of exercise prices	Options outstanding at December 31, 1997 Weighted average remaining contractual life (years)	Number outstanding	Weighted average exercise price
$ .50	7.65	78,753	$ 0.50
$ 1.23 to 1.36	5.61	134,773	$ 1.29
$ 4.20 to 5.00	8.10	74,700	$ 4.42
$ 6.67 to 9.38	9.01	401,275	$ 7.76
$10.19 to 15.00	9.43	125,213	$11.94
$15.50 to 22.00	9.30	172,018	$19.73
$24.63 to 33.75	8.98	156,325	$28.69
		1,143,057	

<CAPTION>

Range of exercise prices	Options exercisable at December 31, 1997 Number exercisable	Weighted average exercise price
$ .50	26,783	$ 0.50
$ 1.23 to 1.36	44,435	$ 1.30
$ 4.20 to 5.00	21,391	$ 4.50
$ 6.67 to 9.38	94,919	$ 7.32
$10.19 to 15.00	10,402	$12.39
$15.50 to 22.00	4,378	$17.16
$24.63 to 33.75	2,890	$33.06
	205,198	

</TABLE>

The Company applies APB 25 in accounting for employee stock awards. Compensation expense of $0, $126,000 and $45,000 have been recorded for the years ended December 31, 1995, 1996 and 1997, respectively. Had compensation expense for the Company's employee stock plans been determined based on the fair value at the grant dates, as prescribed in SFAS 123, the Company's net income (loss) and net income (loss) per share would have been as follows:

<TABLE>
<CAPTION>

	Year ended December 31, 1995	1996	1997
Net income (loss)			
As reported	$1,211,000	$4,262,000	$(2,420,000)
Pro forma	$1,208,000	$4,205,000	$(3,290,000)
Basic earnings (loss) per share			
As reported	$ .33	$ .82	$ (.24)
Pro forma	$ .33	$ .81	$ (.32)
Diluted earnings (loss) per share			
As reported	$ .11	$ .36	$ (.24)
Pro forma	$ .11	$ .36	$ (.32)

</TABLE>

For options granted prior to the Company's initial filing of its Registration Statement on Form S-1 on September 18, 1996, the fair value of each option grant was estimated on the date of grant using the minimum value method. The fair value of each option granted subsequent to the initial filing was estimated on the date of grant assuming a weighted average volatility factor of 67%. Additional weighted average assumptions used for grants during the years ended December 31, 1995, 1996 and 1997 included: dividend yield of 0.0% for all periods; risk-free interest rates of 5.89% to 6.00% for options granted during the year ended December 31, 1995, 5.36% to 6.49% for options granted during the year ended December 31, 1996 and 5.70% to 6.75% for options granted during the year ended December 31, 1997; and an expected option term of 5 years for all periods.

Because additional option grants are expected to be made each year, the above pro forma disclosures are not representative of pro forma effects of reported net income for future years.

9 | LINE OF CREDIT

The Company has a $6.0 million revolving line of credit which expires in September 1998. Borrowings under the line of credit are secured by substantially

all of the Company's assets. Loans made under the revolving line of credit will bear interest at a rate per annum equal to, at the Company's option, the bank's base rate or LIBOR, plus an applicable margin. The loan agreement relating to the line of credit requires that the Company provide the bank with certain periodic financial reports and comply with certain financial ratios. As of December 31, 1997, the Company had not borrowed against the line of credit.

10 | COMMITMENTS

The Company leases its operating facilities and certain office equipment under noncancelable operating leases which expire at various dates. Rental expense under operating leases was approximately $154,000, $251,000 and $542,000 for the years ended December 31, 1995, 1996 and 1997, respectively. Future minimum lease payments as of December 31, 1997 are as follows:

Year ended December 31, 1998	$ 806,000
1999	645,000
2000	588,000
2001	360,000
2002	65,000
	$2,464,000

The Company had noncancelable purchase commitments for inventories of approximately $1,000,000 at December 31, 1997.

11 | EMPLOYEE BENEFIT PLAN

The Company sponsors a 401(k) retirement savings plan (the "Plan"). Participation in the Plan is available to full-time employees who meet eligibility requirements. Eligible employees may contribute up to 15% of their annual salary, subject to certain limitations. The Company matches contributions up to 25% of the first 6% of compensation contributed by the employee to the Plan. During 1997, the Company contributed $68,000 to the Plan. Prior to 1997, the Company did not make contributions to the Plan.

Exhibit 21.1

SeaChange International, Inc.
List of Significant Subsidiaries

Subsidiary Name	Jurisdiction of Incorporation
IPC Interactive, Pte. Ltd.	Singapore
GuestServe Networks, Inc.(1)	Delaware

(1) A wholly owned subsidiary of IPC Interactive, Pte. Ltd.

Exhibit 23.1

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-17379) of SeaChange International, Inc. of our report dated January 22, 1998 appearing on page F-1 of this Form 10-K. We also consent to the incorporation by reference of our report on the Financial Statement Schedule, which appears on page S-1 of this Form 10-K.

PRICE WATERHOUSE LLP

Boston, Massachusetts
March 31, 1998

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