

COGNEX CORP  
Form 10-Q  
May 02, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

*(Mark One)*

☐ Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
for the quarterly period ended April 3, 2011  
or

☐ Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
for the transition period from \_\_\_\_\_ to \_\_\_\_\_

**Commission File Number 001-34218**

**COGNEX CORPORATION**

*(Exact name of registrant as specified in its charter)*

**Massachusetts**

*(State or other jurisdiction of  
incorporation or organization)*

**04-2713778**

*(I.R.S. Employer Identification No.)*

**One Vision Drive**

**Natick, Massachusetts 01760-2059**

**(508) 650-3000**

*(Address, including zip code, and telephone number,  
including  
area code, of principal executive offices)*

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

Yes ☐ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting  
company ☐

*(Do not check if a smaller  
reporting company)*

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

As of April 3, 2011, there were 41,513,499 shares of Common Stock, \$.002 par value, of the registrant outstanding.

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**COGNEX CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share amounts)

|   | Quarter Ended    |                  |
|---|------------------|------------------|
|   | April 3,<br>2011 | April 4,<br>2010 |
|   | (unaudited)      |                  |
| Revenue   |                  |                  |
| Product   | \$ 68,877        | \$ 54,613        |
| Service   | 5,517            | 4,354            |
|   | <b>74,394</b>    | 58,967           |
| Cost of revenue   |                  |                  |
| Product   | 15,099           | 12,911           |
| Service   | 3,284            | 3,030            |
|   | <b>18,383</b>    | 15,941           |
| Gross margin  |                  |                  |
| Product   | 53,778           | 41,702           |
| Service   | 2,233            | 1,324            |
|   | <b>56,011</b>    | 43,026           |
| Research, development, and engineering expenses                   | 9,482            | 8,103            |
| Selling, general, and administrative expenses                     | 29,161           | 23,622           |
| Restructuring charges   |                  | 49               |
| Operating income  | <b>17,368</b>    | 11,252           |
| Foreign currency loss   | (59)             | (165)            |
| Investment income   | 605              | 257              |
| Other expense   | (205)            | (246)            |
| Income before income tax expense                                  | <b>17,709</b>    | 11,098           |
| Income tax expense  | <b>4,073</b>     | 2,553            |
| Net income  | <b>\$ 13,636</b> | \$ 8,545         |
| Earnings per weighted-average common and common-equivalent share: |                  |                  |
| Basic   | \$ 0.33          | \$ 0.22          |
| Diluted   | \$ 0.32          | \$ 0.22          |

Weighted-average common and common-equivalent shares outstanding:

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|                                 |                |         |
|---------------------------------|----------------|---------|
| Basic                           | <b>41,336</b>  | 39,667  |
| Diluted                         | <b>42,286</b>  | 39,683  |
| Cash dividends per common share | <b>\$ 0.08</b> | \$ 0.05 |

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

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**COGNEX CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands)

|  | <b>April 3,<br/>2011<br/>(unaudited)</b> | December<br>31,<br>2010 |
|--|--|-------------------------|
| <b>ASSETS</b>  |  |                         |
| Current assets:  |  |                         |
| Cash and cash equivalents  | \$ 37,014                                | \$ 33,203               |
| Short-term investments   | 170,342                                  | 147,823                 |
| Accounts receivable, less reserves of \$1,244 and \$1,235 in 2011 and 2010, respectively | 42,124                                   | 45,901                  |
| Inventories  | 27,262                                   | 22,717                  |
| Deferred income taxes  | 6,312                                    | 6,302                   |
| Prepaid expenses and other current assets  | 20,569                                   | 23,059                  |
| <br>Total current assets   | <br>303,623                              | <br>279,005             |
| <br>Long-term investments  | <br>109,069                              | <br>102,055             |
| Property, plant, and equipment, net  | 30,063                                   | 29,596                  |
| Deferred income taxes  | 15,720                                   | 15,555                  |
| Intangible assets, net   | 22,084                                   | 23,130                  |
| Goodwill   | 82,524                                   | 82,204                  |
| Other assets   | 1,567                                    | 1,559                   |
|  | \$ 564,650                               | \$ 533,104              |
| <br><b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |  |                         |
| Current liabilities:   |  |                         |
| Accounts payable   | \$ 8,078                                 | \$ 7,153                |
| Accrued expenses   | 23,938                                   | 29,346                  |
| Accrued income taxes   | 10,107                                   | 7,771                   |
| Deferred revenue and customer deposits   | 11,573                                   | 10,162                  |
| <br>Total current liabilities  | <br>53,696                               | <br>54,432              |
| <br>Reserve for income taxes   | <br>5,528                                | <br>5,361               |
| <br>Commitments and contingencies (Note 7)   |  |                         |
| <br>Shareholders' equity:  |  |                         |
|  | 83                                       | 82                      |

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Common stock, \$.002 par value Authorized: 140,000 shares, issued: 41,513  
and 41,065 shares in 2011 and 2010, respectively

|  |                |         |
|--|----------------|---------|
| Additional paid-in capital                       | <b>115,368</b> | 102,620 |
| Retained earnings                                | <b>390,146</b> | 379,826 |
| Accumulated other comprehensive loss, net of tax | <b>(171)</b>   | (9,217) |

|                            |                |         |
|----------------------------|----------------|---------|
| Total shareholders' equity | <b>505,426</b> | 473,311 |
|----------------------------|----------------|---------|

|  |                   |            |
|--|-------------------|------------|
|  | <b>\$ 564,650</b> | \$ 533,104 |
|--|-------------------|------------|

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



Table of Contents**COGNEX CORPORATION****CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME**

(In thousands)

|   | Common Stock |           | Additional      | Retained   | Accumulated<br>Other |                      | Total                |
|---|--------------|-----------|-----------------|------------|----------------------|----------------------|----------------------|
|   | Shares       | Par Value | Paid-in Capital | Earnings   | Comprehensive Loss   | Comprehensive Income | Shareholders' Equity |
| Balance as of December 31, 2010   | 41,065       | \$ 82     | \$ 102,620      | \$ 379,826 | \$ (9,217)           |                      | \$ 473,311           |
| Issuance of common stock under stock option plans                         | 448          | 1         | 9,516           |            |                      |                      | 9,517                |
| Stock-based compensation expense  |              |           | 2,352           |            |                      |                      | 2,352                |
| Excess tax benefit from stock option exercises                            |              |           | 880             |            |                      |                      | 880                  |
| Payment of dividends  |              |           |                 | (3,316)    |                      |                      | (3,316)              |
| Comprehensive income:   |              |           |                 |            |                      |                      |                      |
| Net income  |              |           |                 | 13,636     |                      | \$ 13,636            | 13,636               |
| Net unrealized loss on available-for-sale investments, net of tax of \$53 |              |           |                 |            | (558)                | (558)                | (558)                |
| Foreign currency translation adjustment, net of tax of \$327              |              |           |                 |            | 9,604                | 9,604                | 9,604                |
| Comprehensive income  |              |           |                 |            |                      | \$ 22,682            |                      |

Balance as of  
April 3, 2011  
(unaudited)

**41,513   \$   83   \$   115,368   \$ 390,146   \$   (171)   \$   505,426**

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

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**COGNEX CORPORATION**  
**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**  
(In thousands)

|   | <b>Quarter Ended</b>     |                          |
|---|--------------------------|--------------------------|
|   | <b>April 3,<br/>2011</b> | <b>April 4,<br/>2010</b> |
|   | <b>(unaudited)</b>       |                          |
| Cash flows from operating activities:   |                          |                          |
| Net income  | \$ 13,636                | \$ 8,545                 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                          |                          |
| Stock-based compensation expenses   | 2,352                    | (33)                     |
| Depreciation of property, plant, and equipment                                    | 1,296                    | 1,145                    |
| Amortization of intangible assets   | 1,079                    | 1,235                    |
| Amortization of premiums/discounts on investments                                 | 1,462                    | 420                      |
| Tax effect of stock option exercises  | (880)                    | (37)                     |
| Change in deferred income taxes   | (472)                    | (312)                    |
| Change in operating assets and liabilities  | 2,310                    | (1,252)                  |
| <br>Net cash provided by operating activities                                     | <br><b>20,783</b>        | <br>9,711                |
| <br>Cash flows from investing activities:   |                          |                          |
| Purchases of investments  | (64,270)                 | (16,694)                 |
| Maturities and sales of investments   | 40,096                   | 9,890                    |
| Purchases of property, plant, and equipment                                       | (1,577)                  | (1,081)                  |
| Cash received related to disposition  |                          | 315                      |
| <br>Net cash used in investing activities   | <br><b>(25,751)</b>      | <br>(7,570)              |
| <br>Cash flows from financing activities:   |                          |                          |
| Issuance of common stock under stock option plans                                 | 9,517                    | 120                      |
| Stock option buyback  |                          | (83)                     |
| Payment of dividends  | (3,316)                  | (1,983)                  |
| Tax effect of stock option exercises  | 880                      | 37                       |
| <br>Net cash provided by (used in) financing activities                           | <br><b>7,081</b>         | <br>(1,909)              |
| <br>Effect of foreign exchange rate changes on cash                               | <br><b>1,698</b>         | <br>(5,399)              |
| <br>Net increase (decrease) in cash and cash equivalents                          | <br><b>3,811</b>         | <br>(5,167)              |
| Cash and cash equivalents at beginning of period                                  | <b>33,203</b>            | 119,831                  |
| <br>Cash and cash equivalents at end of period                                    | <br><b>\$ 37,014</b>     | <br>\$ 114,664           |

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



**Table of Contents****COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****NOTE 1: Summary of Significant Accounting Policies**

As permitted by the rules of the Securities and Exchange Commission applicable to Quarterly Reports on Form 10-Q, these notes are condensed and do not contain all disclosures required by generally accepted accounting principles. Reference should be made to the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

In the opinion of the management of Cognex Corporation (the Company), the accompanying consolidated unaudited financial statements contain all adjustments, consisting of normal, recurring adjustments necessary to present fairly the Company's financial position as of April 3, 2011, and the results of its operations for the quarters ended April 3, 2011 and April 4, 2010, and changes in shareholders' equity and cash flows for the periods presented.

The results disclosed in the Consolidated Statements of Operations for the quarter ended April 3, 2011 are not necessarily indicative of the results to be expected for the full year.

**NOTE 2: Fair Value Measurements****Financial Assets that are Measured at Fair Value on a Recurring Basis**

The following table summarizes the financial assets measured at fair value on a recurring basis as of April 3, 2011 (in thousands):

|                            | <b>Quoted Prices in<br/>Active Markets<br/>for<br/>Identical Assets<br/>(Level 1)</b> | <b>Significant<br/>Other<br/>Observable<br/>Inputs (Level<br/>2)</b> |
|----------------------------|---|--|
| Assets:                    |   |  |
| Money market instruments   | \$ 7,325  | \$   |
| Treasury bills             |   | 10,385   |
| Municipal bonds            |   | 111,143  |
| Corporate bonds            |   | 80,580   |
| Agency bonds               |   | 40,568   |
| Sovereign bonds            |   | 24,232   |
| Covered bonds              |   | 6,570  |
| Currency forward contracts | 212   |  |

The majority of the Company's investments are reported at fair value based upon model-driven valuations in which all significant inputs are observable or can be derived from or corroborated by observable market data for substantially the full term of the asset, and are therefore classified as Level 2 investments. These investments are priced daily by a large, third-party pricing service. The service maintains regular contact with market makers, brokers, dealers, and analysts to gather information on market movement, direction, trends, and other specific data. They use this information to structure yield curves for various types of debt securities and arrive at the current day's valuations. The Company's money market instruments are reported at fair value based upon the daily market price for identical assets in active markets, and are therefore classified as Level 1. The Company did not record an other-than-temporary impairment of investments in the quarter ended April 3, 2011.

The Company's forward contracts are reported at fair value based upon quoted U.S. Dollar foreign currency exchange rates, and are therefore classified as Level 1.

**Financial Assets that are Measured at Fair Value on a Non-recurring Basis**

The Company has an interest in a limited partnership, which is accounted for using the cost method and is measured at fair value on a non-recurring basis. The fair value of the Company's limited partnership interest is based upon valuations of the partnership's investments as determined by the General Partner. Publicly-traded investments in active markets are reported at the market closing price less a discount, as appropriate, to reflect restricted marketability. Fair

value for private investments for which observable

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market prices in active markets do not exist is based upon the best information available including the value of a recent financing, reference to observable valuation measures for comparable companies (such as revenue multiples), public or private transactions (such as the sale of a comparable company), and valuations for publicly-traded comparable companies. The amount determined to be fair value also incorporates the General Partner's own judgment and close familiarity with the business activities of each portfolio company. Management monitors the carrying value of this investment compared to its fair value to determine if an other-than-temporary impairment has occurred. If a decline in fair value is considered to be other-than-temporary, an impairment charge would be recorded to reduce the carrying value of the asset to its fair value. The portfolio consists of securities of public and private companies, and consequently, inputs used in the fair value calculation are classified as Level 3. The Company did not record an other-than-temporary impairment of this asset in the quarter ended April 3, 2011.

**Non-financial Assets that are Measured at Fair Value on a Non-recurring Basis**

Non-financial assets such as goodwill, intangible assets, and property, plant, and equipment are measured at fair value only when an impairment loss is recognized. The Company did not record an impairment charge related to these assets in the quarter ended April 3, 2011.

**NOTE 3: Cash, Cash Equivalents, and Investments**

Cash, cash equivalents, and investments consisted of the following (in thousands):

|  | <b>April 3,<br/>2011</b> | <b>December<br/>31,<br/>2010</b> |
|--|--------------------------|----------------------------------|
| Cash   | <b>\$ 29,689</b>         | <b>\$ 26,650</b>                 |
| Money market instruments                                       | <b>7,325</b>             | <b>6,553</b>                     |
| Cash and cash equivalents                                      | <b>37,014</b>            | <b>33,203</b>                    |
| Treasury bills   | <b>10,385</b>            | <b>2,494</b>                     |
| Municipal bonds  | <b>75,928</b>            | <b>75,457</b>                    |
| Corporate bonds  | <b>48,706</b>            | <b>34,543</b>                    |
| Agency bonds   | <b>21,232</b>            | <b>15,979</b>                    |
| Sovereign bonds  | <b>14,091</b>            | <b>19,350</b>                    |
| Short-term investments   | <b>170,342</b>           | <b>147,823</b>                   |
| Municipal bonds  | <b>35,215</b>            | <b>34,794</b>                    |
| Corporate bonds  | <b>31,874</b>            | <b>36,762</b>                    |
| Agency bonds   | <b>19,336</b>            | <b>21,025</b>                    |
| Sovereign bonds  | <b>10,141</b>            |                                  |
| Covered bonds  | <b>6,570</b>             | <b>3,541</b>                     |
| Limited partnership interest (accounted for using cost method) | <b>5,933</b>             | <b>5,933</b>                     |
| Long-term investments  | <b>109,069</b>           | <b>102,055</b>                   |
|  | <b>\$ 316,425</b>        | <b>\$ 283,081</b>                |

The Company's portfolio consists of treasury bills, municipal bonds, corporate bonds, agency bonds, sovereign bonds, and covered bonds. Treasury bills consist of debt securities issued by the U.S. government; municipal bonds consist of debt securities issued by state and local government entities; corporate bonds consist of debt securities issued by both international and domestic companies; agency bonds consist of domestic or foreign obligations of government agencies and government sponsored enterprises that have government backing; sovereign bonds consist of direct debt issued by international governments (Germany and the Netherlands as of April 3, 2011); and covered bonds consist of debt securities backed by governments, mortgages, or public sector loans.

The following table summarizes the Company's available-for-sale investments as of April 3, 2011 (in thousands):

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**COGNEX CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

|                 | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value     |
|-----------------|-------------------|------------------------------|-------------------------------|-------------------|
| Short-term:     |                   |                              |                               |                   |
| Treasury bills  | \$ 10,380         | \$ 5                         | \$                            | \$ 10,385         |
| Municipal bonds | 75,888            | 46                           | (6)                           | 75,928            |
| Corporate bonds | 48,793            | 9                            | (96)                          | 48,706            |
| Agency bonds    | 21,267            | 10                           | (45)                          | 21,232            |
| Sovereign bonds | 14,105            |                              | (14)                          | 14,091            |
| Long-term:      |                   |                              |                               |                   |
| Municipal bonds | 35,192            | 65                           | (42)                          | 35,215            |
| Corporate bonds | 32,467            |                              | (593)                         | 31,874            |
| Agency bonds    | 19,515            | 28                           | (207)                         | 19,336            |
| Sovereign bonds | 10,207            |                              | (66)                          | 10,141            |
| Covered bonds   | 6,649             |                              | (79)                          | 6,570             |
|                 | <b>\$ 274,463</b> | <b>\$ 163</b>                | <b>\$ (1,148)</b>             | <b>\$ 273,478</b> |

The following table summarizes the Company's gross unrealized losses and fair value for available-for-sale investments in an unrealized loss position as of April 3, 2011 (in thousands):

|                 | Fair Value        | Unrealized<br>Losses |
|-----------------|-------------------|----------------------|
| Municipal bonds | \$ 29,034         | \$ (48)              |
| Corporate bonds | 74,716            | (689)                |
| Agency bonds    | 28,769            | (252)                |
| Sovereign bonds | 24,232            | (80)                 |
| Covered bonds   | 6,570             | (79)                 |
|                 | <b>\$ 163,321</b> | <b>\$ (1,148)</b>    |

As of April 3, 2011, the Company did not recognize an other-than-temporary impairment as these investments have been in a continuous unrealized loss position for less than twelve months and the Company has the ability and intent to hold these investments to maturity or until the investment's amortized cost basis has been recovered. The Company recorded gross realized gains and gross realized losses on the sale of debt securities totaling \$9,000 and \$14,000, respectively, in the first quarter of 2011.

The following table presents the effective maturity dates of the Company's available-for-sale investments as of April 3, 2011 (in thousands):

|                 | <1 Year   | 1-2<br>Years | 2-3<br>Years | 3-4<br>Years | Total     |
|-----------------|-----------|--------------|--------------|--------------|-----------|
| Treasury bills  | \$ 10,385 | \$           | \$           | \$           | \$ 10,385 |
| Municipal bonds | 75,928    | 27,362       | 6,855        | 998          | 111,143   |
| Corporate bonds | 48,706    | 15,362       | 16,512       |              | 80,580    |

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|                 |                   |                  |                  |                 |                   |
|-----------------|-------------------|------------------|------------------|-----------------|-------------------|
| Agency bonds    | 21,232            | 12,060           | 7,276            |                 | 40,568            |
| Sovereign bonds | 14,091            | 4,401            | 1,482            | 4,258           | 24,232            |
| Covered bonds   |                   | 4,723            | 1,847            |                 | 6,570             |
|                 | <b>\$ 170,342</b> | <b>\$ 63,908</b> | <b>\$ 33,972</b> | <b>\$ 5,256</b> | <b>\$ 273,478</b> |

In June 2000, the Company became a Limited Partner in Venrock Associates III, L.P. (Venrock), a venture capital fund. A Director of the Company was a General Partner of Venrock Associates through December 31, 2009. The Company has committed to a total investment in the limited partnership of up to \$20,500,000, with an expiration date of December 31, 2013. As of April 3, 2011, the Company contributed \$19,886,000 to the partnership. The remaining commitment of \$614,000 can be called by Venrock at any time before December 31, 2013. Distributions are received and contributions are requested at the discretion of Venrock's management.

Table of Contents**COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****NOTE 4: Inventories**

Inventories consisted of the following (in thousands):

|                 | <b>April 3,<br/>2011</b> | December<br>31,<br>2010 |
|-----------------|--------------------------|-------------------------|
| Raw materials   | <b>\$ 17,563</b>         | \$ 14,791               |
| Work-in-process | <b>2,752</b>             | 2,051                   |
| Finished goods  | <b>6,947</b>             | 5,875                   |
|                 | <b>\$ 27,262</b>         | \$ 22,717               |

**NOTE 5: Intangible Assets and Goodwill**

The change in the carrying value of goodwill during the period (\$320,000) is wholly attributable to fluctuations in foreign currency exchange rates, as a portion of this asset is recorded on the books of the Company's Irish subsidiary. The Company evaluates the possible impairment of goodwill and other intangible assets whenever events or circumstances indicate that the carrying value of these assets may not be recoverable. No triggering event occurred in the quarter ended April 3, 2011 that would indicate a potential impairment of goodwill or other intangible assets. However, the Company continues to monitor market conditions, and changes in market conditions could result in an impairment of goodwill or other intangible assets in a future period.

**NOTE 6: Warranty Obligations**

The Company warrants its hardware products to be free from defects in material and workmanship for periods primarily ranging from six months to two years from the time of sale based upon the product being purchased and the terms of the customer arrangement. Warranty obligations are evaluated and recorded at the time of sale since it is probable that customers will make claims under warranties related to products that have been sold and the amount of these claims can be reasonably estimated based upon historical costs to fulfill claims. Obligations may also be recorded subsequent to the time of sale whenever specific events or circumstances impacting product quality become known that would not have been taken into account using historical data. Warranty obligations are included in

Accrued expenses on the Consolidated Balance Sheets.

The changes in the warranty obligation were as follows (in thousands):

|  |                 |
|--|-----------------|
| Balance as of December 31, 2010                    | \$ 1,985        |
| Provisions for warranties issued during the period | 475             |
| Fulfillment of warranty obligations                | (385)           |
| Foreign exchange rate changes                      | 96              |
| Balance as of April 3, 2011                        | <b>\$ 2,171</b> |

**NOTE 7: Contingencies**

In May 2008, the Company filed a complaint against MvTec Software GmbH, MvTec LLC, and Fuji America Corporation in the United States District Court for the District of Massachusetts alleging infringement of certain patents owned by the Company. In April 2009 and again in June 2009, Defendant MvTec Software GmbH filed re-examination requests of the patents-at-issue with the United States Patent and Trademark Office. This matter is ongoing.

**Table of Contents****COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

In May 2009, the Company pre-filed a complaint with the United States International Trade Commission (ITC) pursuant to Section 337 of the Tariff Act of 1930, as amended, 19 U.S.C. §1337, against MvTec Software GmbH, MvTec LLC, Fuji America, and several other respondents alleging unfair methods of competition and unfair acts in the unlawful importation into the United States, sale for importation, or sale within the United States after importation. By this filing, the Company requested the ITC to investigate the Company's contention that certain machine vision software, machine vision systems, and products containing the same infringe, and respondents directly infringe and/or actively induce and/or contribute to the infringement in the United States, of one or more of the Company's U.S. patents. In July 2009, the ITC issued an order that it would institute an investigation based upon the Company's assertions. In September 2009, the Company reached a settlement with two of the respondents, and in December 2009, the Company reached a settlement with five additional respondents. In March 2010, the Company reached a settlement with respondent Fuji Machine Manufacturing Co., Ltd. and its subsidiary Fuji America Corporation. These settlements did not have a material impact on the Company's financial results. An ITC hearing was held in May 2010. In July 2010, the Administrative Law Judge issued an initial determination finding two of the Company's patents invalid and that respondents did not infringe the patents-at-issue. In September 2010, the Commission issued a notice that it would review the initial determination of the Administrative Law Judge. The ITC issued its Final Determination in November 2010 in which it determined to modify-in-part and affirm-in-part the Administrative Law Judge's determination, and terminate the investigation with a finding of no violation of Section 337 of the Tariff Act of 1930 (as amended 19 U.S.C. §1337). The Company has filed an appeal of the decision with the United States Court of Appeals for the Federal Circuit.

The Company cannot predict the outcome of the above-referenced pending matters and an adverse resolution of these lawsuits could have a material adverse effect on the Company's financial position, liquidity, results of operations, and/or indemnification obligations. In addition, various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened on behalf of or against the Company. While we cannot predict the outcome of these incidental matters, we believe that any liability arising from them will not have a material adverse effect on our financial position, liquidity, or results of operations.

**NOTE 8: Indemnification Provisions**

Except as limited by Massachusetts law, the by-laws of the Company require it to indemnify certain current or former directors, officers, and employees of the Company against expenses incurred by them in connection with each proceeding in which he or she is involved as a result of serving or having served in certain capacities. Indemnification is not available with respect to a proceeding as to which it has been adjudicated that the person did not act in good faith in the reasonable belief that the action was in the best interests of the Company. The maximum potential amount of future payments the Company could be required to make under these provisions is unlimited. The Company has never incurred significant costs related to these indemnification provisions. As a result, the Company believes the estimated fair value of these provisions is minimal.

In the ordinary course of business, the Company may accept standard limited indemnification provisions in connection with the sale of its products, whereby it indemnifies its customers for certain direct damages incurred in connection with third-party patent or other intellectual property infringement claims with respect to the use of the Company's products. The term of these indemnification provisions generally coincides with the customer's use of the Company's products. The maximum potential amount of future payments the Company could be required to make under these provisions is generally subject to fixed monetary limits. The Company has never incurred significant costs to defend lawsuits or settle claims related to these indemnification provisions. As a result, the Company believes the estimated fair value of these provisions is minimal.

In the ordinary course of business, the Company also accepts limited indemnification provisions from time to time, whereby it indemnifies customers for certain direct damages incurred in connection with bodily injury and property damage arising from the installation of the Company's products. The term of these indemnification provisions generally coincides with the period of installation. The maximum potential amount of future payments the Company could be required to make under these provisions is generally limited and is likely recoverable under the Company's

insurance policies. As a result of this coverage,

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and the fact that the Company has never incurred significant costs to defend lawsuits or settle claims related to these indemnification provisions, the Company believes the estimated fair value of these provisions is minimal.

**NOTE 9: Derivative Instruments**

The Company is exposed to certain risks relating to its ongoing business operations including foreign currency exchange rate risk and interest rate risk. The Company does not currently manage its interest rate risk with derivative instruments; however, foreign currency exchange rate risk is currently mitigated with derivative instruments. The Company uses derivative instruments to provide an economic hedge against its transactional currency/functional currency exchange rate exposures. Forward contracts on currencies are entered into to manage the transactional currency/functional currency exposure of the Company's Irish subsidiary's accounts receivable denominated in U.S. dollars and intercompany receivables denominated in Japanese Yen. These forward contracts are used to minimize foreign currency gains or losses, as the gains or losses on these contracts are intended to offset the losses or gains on the underlying exposures.

These forward contracts do not qualify for hedge accounting. Both the underlying exposures and the forward contracts are recorded at fair value on the Consolidated Balance Sheets and changes in fair value are reported as Foreign currency loss on the Consolidated Statements of Operations. The Company recorded net foreign currency losses of \$59,000 and \$165,000 as of April 3, 2011 and April 4, 2010, respectively.

As of April 3, 2011, the Company had the following outstanding forward contracts that were entered into to mitigate foreign currency exchange rate risk:

| <b>Currency</b>  | <b>Amount</b>            |
|--|--------------------------|
| Japanese Yen/Euro  | 225,000,000 Japanese Yen |
| U.S. Dollar/Euro   | 12,150,000 U.S. Dollars  |
| Information regarding the fair value of the forward contracts outstanding as of April 3, 2011 and December 31, 2010 was as follows (in thousands): |                          |

|   | <b>Asset Derivatives</b> |                          | <b>Liability Derivatives</b> |                          |
|---|--------------------------|--------------------------|------------------------------|--------------------------|
|   | <b>Fair Value</b>        |                          | <b>Fair Value</b>            |                          |
| <b>Balance Sheet</b>                      | <b>April 3, 2011</b>     | <b>December 31, 2010</b> | <b>Balance Sheet</b>         | <b>April 3, 2011</b>     |
| <b>Location</b>                           |                          |                          | <b>Location</b>              | <b>December 31, 2010</b> |
| Prepaid expenses and other current assets | \$ 212                   | \$ 83                    | Accrued expenses             | \$ 125                   |

Information regarding the effect of the forward contracts, net of the underlying exposure, on the Consolidated Statements of Operations for the quarter ended April 3, 2011 and April 4, 2010 were as follows (in thousands):

| <b>Location of Gain Recognized</b> | <b>Amount of Gain Recognized in</b>        |
|------------------------------------|--|
|                                    | <b>Income on Derivatives Quarter ended</b> |

|                            | <b>in</b>          |                 |                      |
|----------------------------|--------------------|-----------------|----------------------|
|                            | <b>Income</b>      |                 |                      |
|                            | <b>on</b>          |                 |                      |
|                            | <b>Derivatives</b> | <b>April 3,</b> | <b>April 4, 2010</b> |
|                            | Foreign            | <b>2011</b>     |                      |
|                            | currency           |                 |                      |
|                            | gain               |                 |                      |
| Currency forward contracts |                    | \$ 2            | \$ 67                |
|                            |                    | 10              |                      |

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Table of Contents**COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****NOTE 10: Stock-Based Compensation**

The Company's share-based payments that result in compensation expense consist solely of stock option grants. As of April 3, 2011, the Company had 7,102,350 shares available for grant under two stock option plans: the 2001 General Stock Option Plan (5,609,990) and the 2007 Stock Option and Incentive Plan (1,492,360). Each of these plans expires ten years from the date the plan was approved. The 2001 General Stock Option Plan will expire in December of 2011. Generally, stock options are granted with an exercise price equal to the market value of the Company's common stock at the grant date, vest over four years based upon continuous service, and expire ten years from the grant date.

The following table summarizes the Company's stock option activity for the quarter ended April 3, 2011:

|                                     | <b>Shares<br/>(in<br/>thousands)</b> | <b>Weighted-<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted-<br/>Average<br/>Remaining<br/>Contractual<br/>Term (in<br/>years)</b> | <b>Aggregate<br/>Intrinsic<br/>Value<br/>(in<br/>thousands)</b> |
|-------------------------------------|--------------------------------------|---|--|---|
| Outstanding as of December 31, 2010 | 4,318                                | \$ 20.05  |  |   |
| Granted                             | 857                                  | 29.98   |  |   |
| Exercised                           | (449)                                | 21.20   |  |   |
| Forfeited or expired                | (3)                                  | 19.33   |  |   |
| Outstanding as of April 3, 2011     | <b>4,723</b>                         | <b>\$ 21.74</b>                                     | <b>7.2</b>   | <b>\$ 33,201</b>  |
| Exercisable as of April 3, 2011     | <b>1,974</b>                         | <b>\$ 20.60</b>                                     | <b>4.9</b>   | <b>\$ 15,489</b>  |

The fair values of stock options granted in each quarter presented were estimated using the following weighted-average assumptions:

|                          | <b>Quarter Ended</b>         |                          |
|--------------------------|------------------------------|--------------------------|
|                          | <b>April<br/>3,<br/>2011</b> | <b>April 4,<br/>2010</b> |
| Risk-free rate           | <b>3.6%</b>                  | 3.7%                     |
| Expected dividend yield  | <b>1.0%</b>                  | 1.0%                     |
| Expected volatility      | <b>42%</b>                   | 43%                      |
| Expected term (in years) | <b>5.4</b>                   | 5.3                      |

Risk-free rate

The risk-free rate was based upon a treasury instrument whose term was consistent with the contractual term of the option.

Expected dividend yield

The current dividend yield was calculated by annualizing the cash dividend declared by the Company's Board of Directors for the current quarter and dividing that result by the closing stock price on the grant date. The current dividend yield was then adjusted to reflect the Company's expectations relative to future dividend declarations.

Expected volatility

The expected volatility was based upon a combination of historical volatility of the Company's common stock over the contractual term of the option and implied volatility for traded options of the Company's stock.



Expected term

The expected term was derived from the binomial lattice model from the impact of events that trigger exercises over time.

The weighted-average grant-date fair values of stock options granted during the quarter ended April 3, 2011 and April 4, 2010 were \$11.75 and \$7.67, respectively.

**Table of Contents****COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

The Company stratifies its employee population into two groups: one consisting of senior management and another consisting of all other employees. The Company currently expects that approximately 66% of its stock options granted to senior management and 68% of its options granted to all other employees will actually vest. Therefore, the Company currently applies an estimated forfeiture rate of 13% to all unvested options for senior management and a rate of 14% for all other employees. The Company revised its estimated forfeiture rates in the first quarter of 2011, and the cumulative effect of this change resulted in a reduction in compensation expense of approximately \$80,000. The total stock-based compensation expense and the related income tax benefit recognized for the quarter ended April 3, 2011 were \$2,352,000 and \$791,000, respectively. For the quarter ended April 4, 2010, the Company recorded a net benefit from stock options of \$33,000 and related tax expense of \$20,000. No compensation expense was capitalized as of April 3, 2011 or December 31, 2010.

The following table details the stock-based compensation expense by caption for each quarter presented on the Consolidated Statements of Operations (in thousands):

|  | <b>Quarter Ended</b> |                      |
|--|----------------------|----------------------|
|  | <b>April 3, 2011</b> | <b>April 4, 2010</b> |
| Product cost of revenue                | \$ 165               | \$ 58                |
| Service cost of revenue                | 70                   | 1                    |
| Research, development, and engineering | 809                  | 251                  |
| Selling, general, and administrative   | 1,308                | (343)                |
|  | <b>\$ 2,352</b>      | <b>\$ (33)</b>       |

The total intrinsic values of stock options exercised for the quarter ended April 3, 2011 and April 4, 2010 were \$4,668,000 and \$13,000, respectively. The total fair values of stock options vested for the quarter ended April 3, 2011 and April 4, 2010 were \$7,002,000 and \$7,937,000, respectively.

As of April 3, 2011, total unrecognized compensation expense related to non-vested stock options was \$11,191,000, which is expected to be recognized over a weighted-average period of 1.9 years.

**NOTE 11: Stock Repurchase Program**

In April 2008, the Company's Board of Directors authorized the repurchase of up to \$50,000,000 of the Company's common stock. As of April 3, 2011, the Company had repurchased a total of 1,038,797 shares at a cost of \$20,000,000 under this program. The Company did not purchase any shares under this program during the quarter ended April 3, 2011. The Company may repurchase shares under this program in future periods depending upon a variety of factors, including, among other things, stock price levels, share availability, and cash reserve requirements.

**NOTE 12: Taxes**

A reconciliation of the United States federal statutory corporate tax rate to the Company's effective tax rate was as follows:

|  | <b>Quarter Ended</b> |                      |
|--|----------------------|----------------------|
|  | <b>April 3, 2011</b> | <b>April 4, 2010</b> |
| Income tax at federal statutory rate       | 35%                  | 35%                  |
| State income taxes, net of federal benefit | 1                    | 1                    |
| Foreign tax rate differential              | (13)                 | (13)                 |

|                      |            |     |
|----------------------|------------|-----|
| Income tax provision | <b>23%</b> | 23% |
|----------------------|------------|-----|

The Company's effective tax rate was 23% in both the first quarter of 2011 and 2010. There were no discrete tax events in the quarters ended April 3, 2011 or April 4, 2010.

Table of Contents**COGNEX CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

During the quarter ended April 3, 2011, the Company recorded a \$149,000 increase in liabilities, net of deferred tax benefit, for uncertain tax positions that were recorded as income tax expense. Estimated interest and penalties included in these amounts totaled \$20,000.

The Company's reserve for income taxes, including gross interest and penalties of \$1,209,000, was \$5,528,000 as of April 3, 2011. All of the Company's liabilities for uncertain tax positions are classified as non-current as of April 3, 2011. If the Company's tax positions were sustained or the statutes of limitations related to certain positions expired, these reserves would be released and income tax expense would be reduced in a future period. As a result of the expiration of certain statutes of limitation, there is a potential that \$490,000 of these reserves could be released within the next twelve months, which would decrease income tax expense.

The Company has defined its major tax jurisdictions as the United States, Ireland, China, and Japan, and within the United States, Massachusetts and California. The tax years 2007 through 2010 remain open to examination by various taxing authorities in the jurisdictions in which the Company operates.

The Company is currently negotiating an Advanced Pricing Agreement (APA) with Japan that will cover tax years 2006 through 2012. The Company believes it is adequately reserved for these open years. No formal agreement has been reached between the Tax Authorities in Ireland and Japan as of the date of this filing.

**NOTE 13: Weighted-Average Shares**

Weighted-average shares were calculated as follows (in thousands):

|  | <b>Quarter Ended</b>     |                          |
|--|--------------------------|--------------------------|
|  | <b>April 3,<br/>2011</b> | <b>April 4,<br/>2010</b> |
| Basic weighted-average common shares outstanding                 | <b>41,336</b>            | 39,667                   |
| Effect of dilutive stock options                                 | <b>950</b>               | 16                       |
| Weighted-average common and common-equivalent shares outstanding | <b>42,286</b>            | 39,683                   |

Stock options to purchase 539,569 and 4,498,540 shares of common stock, on a weighted-average basis, were outstanding for the quarters ended April 3, 2011 and April 4, 2010, respectively, but were not included in the calculation of diluted net income per share because they were anti-dilutive.

**NOTE 14: Segment Information**

The Company has two reportable segments: the Modular Vision Systems Division (MVSD) and the Surface Inspection Systems Division (SISD). MVSD develops, manufactures, and markets modular vision systems that are used to control the manufacture of discrete items by locating, identifying, inspecting, and measuring them during the manufacturing process. SISD develops, manufactures, and markets surface inspection vision systems that are used to inspect surfaces of materials processed in a continuous fashion, such as metals, papers, non-wovens, plastics, and glass, to ensure there are no flaws or defects on the surfaces. Segments are determined based upon the way that management organizes its business for making operating decisions and assessing performance. The Company evaluates segment performance based upon income or loss from operations, excluding stock-based compensation expense.

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The following table summarizes information about the segments (in thousands):

|                             | <b>MVSD</b>      | <b>SISD</b>     | <b>Reconciling<br/>Items</b> | <b>Consolidated</b> |
|-----------------------------|------------------|-----------------|------------------------------|---------------------|
| Quarter Ended April 3, 2011 |                  |                 |                              |                     |
| Product revenue             | <b>\$ 62,817</b> | <b>\$ 6,060</b> | <b>\$</b>                    | <b>\$ 68,877</b>    |
| Service revenue             | <b>1,969</b>     | <b>3,548</b>    |                              | <b>5,517</b>        |
| Operating income            | <b>22,027</b>    | <b>997</b>      | <b>(5,656)</b>               | <b>17,368</b>       |
| Quarter Ended April 4, 2010 |                  |                 |                              |                     |
| Product revenue             | \$ 49,660        | \$ 4,953        | \$                           | \$ 54,613           |
| Service revenue             | 1,497            | 2,857           |                              | 4,354               |
| Operating income (loss)     | 15,445           | (328)           | (3,865)                      | 11,252              |

Reconciling items consist of stock-based compensation expense and unallocated corporate expenses, which primarily include corporate headquarters costs, professional fees, and patent infringement litigation. Additional asset information by segment is not produced internally for use by the chief operating decision maker, and therefore, is not presented. Additional asset information is not provided because cash and investments are commingled and the divisions share assets and resources in a number of locations around the world.

**NOTE 15: Dividends**

On February 10, 2011, the Company announced that the Board of Directors declared a cash dividend of \$0.08 per share. The dividend was paid on March 18, 2011 to all shareholders of record at the close of business on March 4, 2011.

On May 2, 2011, the Company's Board of Directors declared a cash dividend of \$0.09 per share. The dividend is payable on June 17, 2011 to all shareholders of record at the close of business on June 3, 2011.

**Table of Contents****ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Forward-Looking Statements**

Certain statements made in this report, as well as oral statements made by the Company from time to time, constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Readers can identify these forward-looking statements by our use of the words expects, anticipates, estimates, believes, projects, intends, plans, will, could, should, and similar words and other statements of a similar sense. These statements are based upon our current estimates and expectations as to prospective events and circumstances, which may or may not be in our control and as to which there can be no firm assurances given. These forward-looking statements, which include statements regarding business and market trends, future financial performance, customer order rates, and growth and strategic plans, involve known and unknown risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include: (1) current and future conditions in the global economy; (2) the cyclical nature of the semiconductor and electronics industries; (3) the inability to penetrate new markets; (4) the inability to achieve significant international revenue; (5) fluctuations in foreign currency exchange rates; (6) the loss of a large customer; (7) the inability to attract and retain skilled employees; (8) the reliance upon key suppliers to manufacture and deliver critical components for our products; (9) the failure to effectively manage product transitions or accurately forecast customer demand; (10) the inability to design and manufacture high-quality products; (11) the technological obsolescence of current products and the inability to develop new products; (12) the failure to properly manage the distribution of products and services; (13) the inability to protect our proprietary technology and intellectual property; (14) our involvement in time-consuming and costly litigation; (15) the impact of competitive pressures; (16) the challenges in integrating and achieving expected results from acquired businesses; (17) potential impairment charges with respect to our investments or for acquired intangible assets or goodwill; and (18) exposure to additional tax liabilities. The foregoing list should not be construed as exhaustive and we encourage readers to refer to the detailed discussion of risk factors included in Part I Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010. The Company cautions readers not to place undue reliance upon any such forward-looking statements, which speak only as of the date made. The Company disclaims any obligation to subsequently revise forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date such statements are made.

**Executive Overview**

Cognex Corporation is a leading worldwide provider of machine vision products that capture and analyze visual information in order to automate tasks, primarily in manufacturing processes, where vision is required. Our Modular Vision Systems Division (MVSD) specializes in machine vision systems that are used to automate the manufacture of discrete items, while our Surface Inspection Systems Division (SISD) specializes in machine vision systems that are used to inspect the surfaces of materials processed in a continuous fashion.

In addition to product revenue derived from the sale of machine vision systems, the Company also generates revenue by providing maintenance and support, training, consulting, and installation services to its customers. Our customers can be classified into three primary markets: factory automation, semiconductor and electronics capital equipment, and surface inspection.

Factory automation customers purchase Cognex vision products and incorporate them into their manufacturing processes. Virtually every manufacturer can achieve better quality and manufacturing efficiency by using machine vision, and therefore, this segment includes a broad base of customers across a variety of industries, including automotive, consumer electronics, food and beverage, health and beauty, medical devices, packaging, pharmaceutical, and solar. The factory automation market also includes customers who purchase Cognex vision products for use outside of the assembly process, such as using ID products in logistics automation for package sorting and distribution. Sales to factory automation customers represented approximately 70% of total revenue in the first quarter of 2011.

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Semiconductor and electronics capital equipment manufacturers purchase Cognex vision products and integrate them into the automation equipment that they manufacture and then sell to their customers to either make semiconductor chips or assemble printed circuit boards. Demand from these capital equipment manufacturers has historically been highly cyclical, with periods of investment followed by downturn. Sales to semiconductor and electronics capital equipment manufacturers represented approximately 17% of total revenue in the first quarter of 2011.

Surface inspection customers are manufacturers of materials processed in a continuous fashion, such as metals, paper, non-wovens, plastics, and glass. These customers need sophisticated machine vision to detect, classify, and analyze defects on the surfaces of those materials as they are being processed at high speeds. Surface inspection sales represented approximately 13% of total revenue in the first quarter of 2011.

Revenue for the first quarter of 2011 totaled \$74,394,000, representing an increase of \$15,427,000 from the same period in the prior year. The higher revenue contributed to a gross margin of 75% of revenue in the first quarter of 2011, compared to 73% of revenue in the same period in 2010. Operating expenses increased by \$5,539,000 over the prior year's first quarter due primarily to expenses associated with increased headcount in strategic areas and higher stock-based compensation expense. As a result, the Company was able to generate an operating profit of \$17,368,000, or 23% of revenue, in the first quarter of 2011, compared to an operating profit of \$11,252,000, or 19% of revenue, in the first quarter of 2010.

## **Results of Operations**

### **Revenue**

Revenue for the first quarter of 2011 increased by \$15,427,000, or 26%, from the first quarter of 2010 due to higher sales in all three of the Company's primary markets.

### ***Factory Automation Market***

Sales to manufacturing customers in the factory automation area, which are included in the Company's MVSD segment, represented 70% of total revenue in the first quarter of 2011 compared to 71% in the first quarter of 2010. Sales to these customers increased by \$10,383,000, or 25%, from the first quarter of 2010. The largest dollar increases were experienced in the Americas and Europe, where the Company has a broad base of factory automation customers, while the largest percentage increase was experienced in Southeast Asia, where the Company has expanded its sales and support infrastructure, particularly in China, in order to access more of the machine vision market in this high-potential growth region. Although factory automation revenue in Japan was lower in the first quarter of 2011 compared to the prior year, the decline was largely attributed to shipments that were pushed from March to April at customers' requests after the March 1<sup>st</sup> earthquake that hit this region. Although the increase in factory automation revenue was noted across all major product lines, the largest percentage increase came from the ID Products business, where the Company has made significant product investments for the manufacturing sector that we currently serve, as well as for the logistics market that we hope to penetrate with DataMan® 500 that was introduced early in the first quarter of 2011.

Sales to factory automation customers decreased by \$8,495,000, or 14%, from the fourth quarter of 2010. Revenue in the fourth quarter of 2010 included \$6,500,000 related to an arrangement with a single customer for which the work was performed over the prior four years, but revenue was deferred until the final obligation was completed in the fourth quarter of 2010. Excluding the recognition of this revenue in the fourth quarter of 2010, sales to these customers decreased by \$1,995,000, or 4%, from the prior quarter. A small decrease in revenue from the fourth quarter to the first quarter is not unusual for the factory automation business, as many customers consume their remaining annual capital budgets during the last quarter of the year. Management expects total factory automation revenue to grow in the second quarter of 2011 as compared to the first quarter, despite uncertainty surrounding the market in Japan, as the aftermath of the March earthquake continues to unfold.

### ***Semiconductor and Electronics Capital Equipment Market***

Sales to customers who make automation equipment for the semiconductor and electronics industries, which are included in the Company's MVSD segment, represented 17% of total revenue in the first quarter





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of 2011 compared to 16% in the first quarter of 2010. Sales to these customers increased by \$3,246,000, or 35%, from the first quarter of 2010. Geographically, revenue increased most significantly in Japan and Southeast Asia, where many of the Company's semiconductor and electronics capital equipment customers are located. Although sales to these customers increased by \$1,094,000, or 10%, from the fourth quarter of 2010, the semiconductor and electronics capital equipment market has historically been highly cyclical and management has limited visibility regarding future order levels from these customers.

*Surface Inspection Market*

Sales to surface inspection customers, which comprise the Company's SISD segment, represented 13% of total revenue in both the first quarter of 2011 and 2010. Revenue from these customers increased by \$1,798,000, or 23%, from the first quarter of 2010 due to both higher product and service revenue. Sales to the metal and non-woven industries were significantly higher than in the first quarter of 2010. Revenue decreased by \$3,125,000, or 25%, from the fourth quarter of 2010, which was a record revenue quarter for the division. The revenue reported each quarter can vary depending upon the timing of customer orders, system deliveries, and installations, as well as the impact of revenue deferrals.

*Product Revenue*

Product revenue increased by \$14,264,000, or 26%, from the first quarter of 2010 due to a higher volume of vision systems sold, primarily to customers in factory automation and the semiconductor and electronics capital equipment markets. The impact of the higher volume was partially offset by lower average selling prices, as the Company introduced new products at lower price points.

*Service Revenue*

Service revenue, which is derived from the sale of maintenance and support, education, consulting, and installation services increased by \$1,163,000, or 27%, from the first quarter of 2010 primarily due to higher revenue from SISD installation services and maintenance support contracts, as well as higher revenue from MVSD consulting services. Service revenue was consistent as a percentage of total revenue at 7% in both the first quarter of 2011 and 2010.

Gross Margin

Gross margin as a percentage of revenue was 75% for the first quarter of 2011 compared to 73% for the first quarter of 2010. This increase was primarily due to higher MVSD product margins.

*MVSD Margin*

MVSD gross margin as a percentage of revenue was 80% for the first quarter of 2011 compared to 78% for the first quarter of 2010. The increase in MVSD margin was primarily due to manufacturing efficiencies achieved from higher revenue levels, as certain fixed manufacturing costs were spread over a higher revenue base.

*SISD Margin*

SISD gross margin as a percentage of revenue was 46% for the first quarter of 2011 compared to 40% for the first quarter of 2010. The increase in SISD margin was primarily due to improved margins from installation services, as well as improved product margins resulting from increased sales to the metal and non-woven industries, which carry higher margins than sales to the paper industry.

*Product Margin*

Product gross margin as a percentage of revenue was 78% for the first quarter of 2011 compared to 76% for the first quarter of 2010. This increase was primarily due to higher MVSD product margins as described above.

**Table of Contents***Service Margin*

Service gross margin as a percentage of revenue was 40% for the first quarter of 2011 compared to 30% for the first quarter of 2010. The increase in service margin was primarily due to improved margins from SISD installation services.

**Operating Expenses***Research, Development, and Engineering Expenses*

Research, development, and engineering (RD&E) expenses for the first quarter of 2011 increased \$1,379,000, or 17%, from the prior year. MVSD RD&E expenses increased by \$1,461,000, or 20%, and SISD RD&E expenses decreased \$82,000, or 9%.

The table below details the \$1,461,000 net increase in MVSD RD&E expenses in the first quarter of 2011:

|                                  |                     |
|----------------------------------|---------------------|
| MVSD RD&E balance in Q1 2010     | \$ 7,232            |
| Personnel-related costs          | 834                 |
| Stock-based compensation expense | 571                 |
| Other                            | 56                  |
| <br>MVSD RD&E balance in Q1 2011 | <br><b>\$ 8,693</b> |

Over the past few quarters, the Company has increased RD&E headcount in strategic areas, resulting in higher personnel-related costs, such as salaries, fringe benefits, and recruiting expense. The majority of the headcount increase was in lower-cost regions, such as Hungary. In addition, the Company recorded increased stock-based compensation expense due to the timing of the annual stock option grant, which occurred in the first quarter of 2011 as compared to the second quarter of 2010.

The decrease in SISD RD&E expenses in the first quarter of 2011 was primarily due to a change in personnel mix, resulting in savings in salaries, fringe benefits, company bonus expense, and stock-based compensation expense (\$122,000). These savings were partially offset by increased materials costs related to product development efforts (\$59,000).

RD&E expenses as a percentage of revenue were 13% in the first quarter of 2011 and 14% in the first quarter of 2010. We believe that a continued commitment to RD&E activities is essential in order to maintain or achieve product leadership with our existing products and to provide innovative new product offerings, and therefore, we expect to continue to make RD&E investments in the future in strategic areas, such as the ID products business and further development of a Vision System on a Chip. In addition, we consider our ability to accelerate time to market for new products critical to our revenue growth. Although we target our RD&E spending to be between 10% and 15% of revenue, this percentage is impacted by revenue levels.

*Selling, General, and Administrative Expenses*

Selling, general, and administrative (SG&A) expenses for the first quarter of 2011 increased by \$5,539,000, or 23%, from the prior year. MVSD SG&A expenses increased \$5,373,000, or 32%, while SISD SG&A expenses increased \$215,000, or 8%. Corporate expenses that are not allocated to either division decreased by \$49,000, or 1%.

The table below details the \$5,373,000 net increase in MVSD SG&A expenses in the first quarter of 2011:

|  |                      |
|--|----------------------|
| MVSD SG&A expenses in Q1 2010          | \$ 16,914            |
| Personnel-related costs                | 2,432                |
| Stock-based compensation expense       | 1,055                |
| Marketing and promotional expenses     | 712                  |
| Foreign currency exchange rate changes | 384                  |
| Sales demonstration equipment          | 213                  |
| Other                                  | 577                  |
| <br>MVSD SG&A expenses in Q1 2011      | <br><b>\$ 22,287</b> |



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Over the past few quarters, the Company has increased SG&A headcount in strategic areas, resulting in higher personnel-related costs, such as salaries, fringe benefits, recruiting, commissions, and travel expense. The majority of the headcount increase was in lower-cost regions, such as China. In addition, the Company recorded increased stock-based compensation expense due to the timing of the annual stock option grant, which occurred in the first quarter of 2011 as compared to the second quarter of 2010. Furthermore, stock-based compensation expense in the first quarter of 2010 included a high level of credits related to forfeited options. Other increases included higher spending on marketing and promotional activities intended to grow factory automation revenue, the unfavorable impact of changes in foreign currency exchange rates, primarily the Japanese Yen, and higher spending on sales demonstration equipment as a result of new product offerings.

The increase in SISA SG&A expenses was primarily due to increased bad debt expenses (\$102,000), higher stock-based compensation expense due to the timing of the annual stock option grant (\$56,000), and the unfavorable impact of changes in foreign currency exchange rates, primarily the Japanese Yen (\$39,000).

The decrease in corporate expenses was due to lower legal fees primarily related to patent infringement actions (\$1,362,000). These savings were partially offset by increased stock-based compensation and related option valuation fees due to the timing of the annual stock option grant (\$582,000), costs associated with the Company's 30<sup>th</sup> Anniversary parties held in the first quarter of 2011 (\$480,000), the timing of audit and proxy fees (\$148,000), and increased company bonus accruals related to employees assigned to the Company's corporate departments (\$138,000).

**Nonoperating Income (Expense)**

The Company recorded a foreign currency loss of \$59,000 in the first quarter of 2011 compared to a loss of \$165,000 for the first quarter of 2010. The foreign currency losses in each period resulted primarily from the revaluation and settlement of accounts receivable and intercompany balances that are reported in one currency and collected in another. Although the foreign currency exposure of accounts receivable is largely mitigated through the use of forward contracts, this program depends upon forecasts of sales and collections, and therefore, gains or losses on the underlying receivables may not perfectly offset losses or gains on the contracts.

Investment income for the first quarter of 2011 increased \$348,000, or 135%, from the first quarter of 2010, due to increased investment of the Company's excess cash. Beginning in the second quarter of 2010, the Board of Directors approved a change to the Company's investment policy to allow management to invest excess cash accumulated in the Company's international entities in debt securities. This change in policy has also resulted in increased investment income compared to the first quarter of 2010.

The Company recorded other expense of \$205,000 in the first quarter of 2011 compared to other expense of \$246,000 in the first quarter of 2010. Other income (expense) includes rental income, net of associated expenses, from leasing buildings adjacent to the Company's corporate headquarters. A portion of this space is currently unoccupied.

**Income Tax Expense**

The Company's effective tax rate was 23% in both the first quarter of 2011 and 2010. There were no discrete tax events in either period.

**Liquidity and Capital Resources**

The Company has historically been able to generate positive cash flow from operations, which has funded its operating activities and other cash requirements and has resulted in an accumulated cash, cash equivalent, and investment balance of \$316,425,000 as of April 3, 2011. The Company has established guidelines relative to credit ratings, diversification, and maturities of its investments that maintain liquidity.

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The Company's cash requirements during the first quarter of 2011 were met with its existing cash balances, cash from investment maturities, positive cash flows from operations, and the proceeds from stock option exercises. Cash requirements primarily consisted of operating activities, purchases of investments, capital expenditures, and the payment of dividends. During the first quarter of 2011, the Company paid out approximately \$7,000,000 in company bonuses related to fiscal year 2010, and also made further working capital investments in inventories to support higher anticipated business volumes. Capital expenditures for the first quarter of 2011 totaled \$1,577,000 and consisted primarily of expenditures for computer hardware and manufacturing test equipment for new product introductions. In June 2000, the Company became a Limited Partner in Venrock Associates III, L.P. (Venrock), a venture capital fund. The Company has committed to a total investment in the limited partnership of up to \$20,500,000, with the commitment period expiring on December 31, 2013. The Company does not have the right to withdraw from the partnership prior to December 31, 2013. As of April 3, 2011, the Company had contributed \$19,886,000 to the partnership. No contributions were made and no distributions were received in the first quarter of 2011. The remaining commitment of \$614,000 can be called by Venrock in any period through December 31, 2013.

Beginning in the third quarter of 2003, the Company's Board of Directors has declared and paid a cash dividend in each quarter, including a dividend of \$0.08 per share that amounted to \$3,316,000 in the first quarter of 2011. Future dividends will be declared at the discretion of the Company's Board of Directors and will depend upon such factors as the Board deems relevant including, among other things, the Company's ability to generate positive cash flows from operations.

In April 2008, the Company's Board of Directors authorized the repurchase of up to \$50,000,000 of the Company's common stock. As of April 3, 2011, the Company had repurchased 1,038,797 shares at a cost of \$20,000,000 under this program. The Company did not purchase any shares under this program during the first quarter of 2011. The Company may repurchase shares under this program in future periods depending upon a variety of factors, including, among other things, the stock price level, share availability, and cash reserve requirements.

The Company believes that its existing cash, cash equivalent, and investment balances, together with cash flow from operations, will be sufficient to meet its operating, investing, and financing activities for the next twelve months. As of April 3, 2011, the Company had approximately \$310,492,000 in either cash or investments that could be converted into cash. In addition, Cognex has no long-term debt and does not anticipate needing debt financing in the near future. We believe that our strong cash position has put us in a relatively good position with respect to our longer-term liquidity needs.

### **ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes to the Company's exposures to market risk since December 31, 2010.

### **ITEM 4: CONTROLS AND PROCEDURES**

As required by Rules 13a-15 and 15d-15 of the Securities Exchange Act of 1934, the Company has evaluated, with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, the effectiveness of its disclosure controls and procedures (as defined in such rules) as of the end of the period covered by this report. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer concluded that such disclosure controls and procedures were effective as of that date. From time to time, the Company reviews its disclosure controls and procedures, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that the Company's systems evolve with its business. There was no change in the Company's internal control over financial reporting that occurred during the quarter ended April 3, 2011 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents****PART II: OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

In May 2008, the Company filed a complaint against MvTec Software GmbH, MvTec LLC, and Fuji America Corporation in the United States District Court for the District of Massachusetts alleging infringement of certain patents owned by the Company. In April 2009 and again in June 2009, Defendant MvTec Software GmbH filed re-examination requests of the patents-at-issue with the United States Patent and Trademark Office. This matter is ongoing.

In May 2009, the Company pre-filed a complaint with the United States International Trade Commission (ITC) pursuant to Section 337 of the Tariff Act of 1930, as amended, 19 U.S.C. §1337, against MvTec Software GmbH, MvTec LLC, Fuji America, and several other respondents alleging unfair methods of competition and unfair acts in the unlawful importation into the United States, sale for importation, or sale within the United States after importation. By this filing, the Company requested the ITC to investigate the Company's contention that certain machine vision software, machine vision systems, and products containing the same infringe, and respondents directly infringe and/or actively induce and/or contribute to the infringement in the United States, of one or more of the Company's U.S. patents. In July 2009, the ITC issued an order that it would institute an investigation based upon the Company's assertions. In September 2009, the Company reached a settlement with two of the respondents, and in December 2009, the Company reached a settlement with five additional respondents. In March 2010, the Company reached a settlement with respondent Fuji Machine Manufacturing Co., Ltd. and its subsidiary Fuji America Corporation. These settlements did not have a material impact on the Company's financial results. An ITC hearing was held in May 2010. In July 2010, the Administrative Law Judge issued an initial determination finding two of the Company's patents invalid and that respondents did not infringe the patents-at-issue. In September 2010, the Commission issued a notice that it would review the initial determination of the Administrative Law Judge. The ITC issued its Final Determination in November 2010 in which it determined to modify-in-part and affirm-in-part the Administrative Law Judge's determination, and terminate the investigation with a finding of no violation of Section 337 of the Tariff Act of 1930 (as amended 19 U.S.C. §1337). The Company has filed an appeal of the decision with the United States Court of Appeals for the Federal Circuit.

The Company cannot predict the outcome of the above-referenced pending matters and an adverse resolution of these lawsuits could have a material adverse effect on the Company's financial position, liquidity, results of operations, and/or indemnification obligations. In addition, various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened on behalf of or against the Company. While we cannot predict the outcome of these incidental matters, we believe that any liability arising from them will not have a material adverse effect on our financial position, liquidity, or results of operations.

**ITEM 1A. RISK FACTORS**

For a complete list of factors that could affect the Company's business, results of operations, and financial condition, see the risk factors discussion provided in Part I Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010. The language below has been added to an existing risk factor previously defined on Form 10-K to address the current risks associated with international sales.

**Economic, political, and other risks associated with international sales and operations could adversely affect our business and operating results.**

On March 11, 2011, a large earthquake hit the northeast region of Japan. The majority of our customers located in Japan are outside of the affected areas. Certain customers requested that orders totaling approximately \$800,000, originally scheduled for March shipment, be pushed to April. The remaining orders that were on the backlog at the time of

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the earthquake, and any new orders, were fulfilled from our Cork, Ireland distribution center. Our Koriyama, Japan distribution center suspended shipments for approximately five weeks, but began shipping product again in April. Cognex does not manufacture in Japan.

Our key suppliers located in Japan have told us that they are up and running, subject to power outages. Cognex has a policy of maintaining strategic inventory reserves of critical components. We have taken action to secure additional reserves of Japanese-manufactured critical parts, such as imagers. For this reason, we do not expect significant supply disruption as result of the earthquake. There is uncertainty, however, regarding how demand from our customers will be impacted in the second quarter and beyond, as the aftermath of this disaster continues to unfold through layers of the supply chain.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table sets forth information with respect to purchases by the Company of shares of its Common Stock during the periods indicated.

|                                |   |   | <b>Total<br/>Number of<br/>Shares<br/>Purchased<br/>as<br/>Part of<br/>Publicly<br/>Announced<br/>Plans or<br/>Programs<br/>(1)</b> | <b>Approximate<br/>Dollar Value<br/>of<br/>Shares that<br/>May Yet Be<br/>Purchased<br/>Under the<br/>Plans or<br/>Programs</b> |
|--------------------------------|---|---|---|---|
|                                | <b>Total<br/>Number<br/>of<br/>Shares<br/>Purchased</b> | <b>Average<br/>Price<br/>Paid<br/>per<br/>Share</b> |   |   |
| January 1 - January 30, 2011   |   |   |   | \$ 30,000,000   |
| January 31 - February 27, 2011 |   |   |   | \$ 30,000,000   |
| February 28 - April 3, 2011    |   |   |   | \$ 30,000,000   |
| Total                          |   |   |   | \$ 30,000,000   |

(1) In April 2008, the Company's Board of Directors authorized the repurchase of up to \$50,000,000 of the Company's common stock.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None

**ITEM 4. REMOVED AND RESERVED****ITEM 5. OTHER INFORMATION**

None

**ITEM 6. EXHIBITS**

31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934\*

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934\*

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002\*\*

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002\*\*





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101 xBRL (Extensible Business Reporting Language)

The following materials from Cognex Corporation's Quarterly Report on Form 10-Q for the period ended April 3, 2011, formatted in xBRL: (i) Consolidated Statements of Operations for the quarter ended April 3, 2011; (ii) Consolidated Balance Sheets as of April 3, 2011 and December 31, 2010; (iii) Consolidated Statement of Shareholders' Equity and Comprehensive Income for the quarter ended April 3, 2011; (iv) Consolidated Condensed Statements of Cash Flows for the quarter ended April 3, 2011; and (v) Notes to Consolidated Financial Statements.

\* Filed herewith

\*\* Furnished herewith

\*\*\* Pursuant to Rule 406T of Regulation S-T, the xBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: May 2, 2011

COGNEX CORPORATION

By: /s/ Robert J. Willett  
Robert J. Willett  
President and Chief Executive Officer  
(duly authorized officer, principal  
executive officer)

By: /s/ Richard A. Morin  
Richard A. Morin  
Executive Vice President of Finance and  
Chief Financial Officer  
(duly authorized officer, principal  
financial and accounting officer)

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