

COGNEX CORP  
Form 10-Q  
November 01, 2007

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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 September 30, 2007

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 0-17869

**COGNEX CORPORATION**

(Exact name of registrant as specified in its charter)

**Massachusetts**

**04-2713778**

(State or other jurisdiction of  
incorporation or organization)

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐

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 October 28, 2007, there were 43,321,700 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)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September</b>	<b>October</b>	<b>September</b>	<b>October 1,</b>
	<b>30,</b>	<b>1,</b>	<b>30,</b>	<b>2006</b>
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
	<b>(unaudited)</b>		<b>(unaudited)</b>	
Revenue				
Product	\$ 49,196	\$ 52,249	\$ 142,834	\$ 163,250
Service	5,549	5,756	17,582	16,869
	54,745	58,005	160,416	180,119
Cost of revenue				
Product (1)	11,278	12,031	36,087	38,055
Service (1)	3,340	3,416	10,933	10,695
	14,618	15,447	47,020	48,750
Gross margin				
Product	37,918	40,218	106,747	125,195
Service	2,209	2,340	6,649	6,174
	40,127	42,558	113,396	131,369
Research, development, and engineering expenses (1)	8,704	7,997	24,654	24,496
Selling, general, and administrative expenses (1)	24,303	23,414	72,870	72,470
Operating income	7,120	11,147	15,872	34,403
Foreign currency gain (loss)	353	(282)	(88)	(707)
Investment and other income	1,881	1,518	5,597	4,856
Income before income tax expense	9,354	12,383	21,381	38,552
Income tax expense	2,011	2,267	5,576	8,202
Net income	\$ 7,343	\$ 10,116	\$ 15,805	\$ 30,350

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Net income per common and common-equivalent share:

Basic	\$ 0.17	\$ 0.23	\$ 0.36	\$ 0.66
Diluted	\$ 0.17	\$ 0.22	\$ 0.36	\$ 0.64

Weighted-average common and common-equivalent shares outstanding:

Basic	43,286	44,825	43,859	45,905
Diluted	43,506	45,682	44,257	47,086

Cash dividends per common share	\$ 0.085	\$ 0.085	\$ 0.255	\$ 0.245
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(1) Amounts include stock-based compensation expense, as follows:

Product cost of revenue	\$ 138	\$ 191	\$ 450	\$ 544
Service cost of revenue	140	222	417	650
Research, development, and engineering	723	941	2,268	2,671
Selling, general, and administrative	1,723	2,121	5,110	6,071

Total stock-based compensation expense	\$ 2,724	\$ 3,475	\$ 8,245	\$ 9,936
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The accompanying notes are an integral part of these consolidated financial statements.

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

	<b>September 30, 2007 (unaudited)</b>	<b>December 31, 2006</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 107,343	\$ 87,361
Short-term investments	87,824	128,319
Accounts receivable, less reserves of \$1,280 and \$1,662 in 2007 and 2006, respectively	39,687	40,055
Inventories, net	30,048	30,583
Deferred income taxes	8,446	8,636
Prepaid expenses and other current assets	16,069	18,127
 Total current assets	 289,417	 313,081
 Long-term investments	 70,200	 50,540
Property, plant, and equipment, net	26,327	26,028
Deferred income taxes	18,959	9,002
Intangible assets, net	41,023	44,988
Goodwill	84,621	83,318
Other assets	8,384	1,694
	\$ 538,931	\$ 528,651
 <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 4,551	\$ 6,463
Accrued expenses	34,548	31,064
Accrued income taxes	5,030	1,181
Deferred revenue and customer deposits	15,184	7,726
 Total current liabilities	 59,313	 46,434
 Reserve for income taxes	 17,913	 8,367
 Commitments (Notes 3, 7, 8, 9, and 13)		
 Shareholders' equity:		
Common stock, \$.002 par value    Authorized: 140,000 shares, issued: 43,322 and 44,403 shares in 2007 and 2006, respectively	 87	 89

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Additional paid-in capital	137,377	155,136
Retained earnings	329,820	329,251
Accumulated other comprehensive loss	(5,579)	(10,626)
 Total shareholders' equity	 461,705	 473,850
	 \$ 538,931	 \$ 528,651

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

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**COGNEX CORPORATION**  
**CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY**  
(In thousands)

	Common Shares	Stock Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Comprehensive Income	Total Shareholders' Equity
Balance at December 31, 2006	44,403	\$ 89	\$ 155,136	\$ 329,251	\$ (10,626)		\$ 473,850
Issuance of common stock under stock option and stock purchase plans	349	1	6,453				6,454
Stock-based compensation expense			8,245				8,245
Excess tax benefit from stock option exercises			203				203
Repurchase of common stock	(1,430)	(3)	(32,660)				(32,663)
Payment of dividends				(11,215)			(11,215)
Reduction in retained earnings related to the adoption of FIN 48 (Note 9)				(4,021)			(4,021)
Comprehensive income:							
Net income				15,805		\$ 15,805	15,805
Losses on currency swaps, net of gains on long-term intercompany loans, net of tax of \$220					(375)	(375)	(375)
Net unrealized gain on available-for-sale investments, net of tax of \$128					218	218	218
Foreign currency translation adjustment					5,204	5,204	5,204
Comprehensive income						\$ 20,852	
	43,322	\$ 87	\$ 137,377	\$ 329,820	\$ (5,579)		\$ 461,705



Balance at  
September 30, 2007  
(unaudited)

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

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

	<b>Nine Months Ended</b>	
	<b>September 30, 2007</b>	<b>October 1, 2006</b>
	<b>(unaudited)</b>	
Cash flows from operating activities:		
Net income	\$ 15,805	\$ 30,350
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation expense	8,245	9,936
Depreciation and amortization	8,494	8,702
Provision for excess and obsolete inventory	2,627	301
Excess tax benefit from stock option exercises	(203)	(1,201)
Deferred income tax benefit	(5,566)	(5,822)
Deposit related to Japan tax audit (Note 9)	(6,336)	
Change in operating assets and liabilities	12,931	(831)
 Net cash provided by operating activities	 35,997	 41,435
 Cash flows from investing activities:		
Purchase of investments	(220,467)	(351,528)
Maturity and sale of investments	240,571	413,210
Purchase of property, plant, and equipment	(3,307)	(3,231)
Cash paid for business acquisitions, net of cash acquired	(502)	(3,188)
 Net cash provided by investing activities	 16,295	 55,263
 Cash flows from financing activities:		
Issuance of common stock under stock option and stock purchase plans	6,454	9,198
Repurchase of common stock	(32,663)	(81,296)
Payment of dividends	(11,215)	(11,267)
Excess tax benefit from stock option exercises	203	1,201
 Net cash used in financing activities	 (37,221)	 (82,164)
 Effect of foreign exchange rate changes on cash	 4,911	 2,160
 Net increase in cash and cash equivalents	 19,982	 16,694
Cash and cash equivalents at beginning of period	87,361	72,856
 Cash and cash equivalents at end of period	 \$ 107,343	 \$ 89,550

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

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**COGNEX CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**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, 2006.

In the opinion of the management of Cognex Corporation (the Company), the accompanying consolidated unaudited financial statements contain all adjustments, consisting of only normal, recurring adjustments, necessary to present fairly the Company's financial position at September 30, 2007, and the results of its operations for the three-month and nine-month periods ended September 30, 2007 and October 1, 2006, and changes in shareholders' equity and cash flows for the periods presented.

The results disclosed in the Consolidated Statements of Operations for the three-month and nine-month periods ended September 30, 2007 are not necessarily indicative of the results to be expected for the full year.

**NOTE 2: New Pronouncements****FASB Statement No. 159, The Fair Value Option for Financial Assets and Financial Liabilities**

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which provides companies with an option to report selected financial assets and liabilities at fair value. This Statement is effective for the Company's fiscal year ended December 31, 2008, although earlier adoption is permitted. The Company does not expect this Statement to have a material impact on its financial condition or results of operations.

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

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

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Cash	\$ 107,343	\$ 84,361
Cash equivalents		3,000
Cash and cash equivalents	107,343	87,361
Municipal bonds	87,824	108,332
Commercial paper		15,988
Agency notes		3,999
Short-term investments	87,824	128,319
Municipal bonds	60,777	39,594
Limited partnership interest (accounted for using cost method)	9,423	10,946
Long-term investments	70,200	50,540
	\$ 265,367	\$ 266,220



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**COGNEX CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3: Cash, Cash Equivalents, and Investments (continued)**

In June 2000, Cognex Corporation became a Limited Partner in Venrock Associates III, L.P. (Venrock), a venture capital fund. A Director of the Company is a Managing General Partner of Venrock Associates. 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, 2010.

As of September 30, 2007, the Company had contributed \$19,488,000 to the partnership. During the nine-month period ended September 30, 2007, the Company made \$1,025,000 in contributions to the partnership, and received \$2,548,000 of distributions from the partnership that were accounted for as a return of capital. No contributions were made to the partnership or distributions received from the partnership during the quarter ended September 30, 2007. At September 30, 2007, the carrying value of this investment was \$9,423,000 compared to an estimated fair value, as determined by the General Partner, of \$12,280,000.

**NOTE 4: Inventories**

Inventories consisted of the following (in thousands):

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Raw materials	\$ 15,998	\$ 16,746
Work-in-process	1,362	1,630
Finished goods	12,688	12,207
	<b>\$ 30,048</b>	<b>\$ 30,583</b>

The Company periodically reviews inventory quantities on hand and estimates excess and obsolescence exposures based upon assumptions about future demand, product transitions, and market conditions, and records reserves to reduce the carrying value of inventories to their net realizable value. In the second quarter of 2007, the Company recorded provisions for excess and obsolete MVSD inventory totaling \$2,126,000 resulting from lower actual demand than was previously estimated as part of the Company's material requirements forecasts, together with lower estimates of future demand from both semiconductor and electronics capital equipment and discrete factory automation customers. Provisions of \$303,000 and \$285,000 were also recorded in the first and third quarters of 2007, respectively.

When inventory has been written down below cost, such reduced amount is considered the new cost basis for subsequent accounting purposes. As a result, the Company may recognize a higher than normal gross margin if the reserved inventory is subsequently sold. The Company recognized benefits to cost of product revenue from the sale of reserved inventory for the three-month and nine-month periods ended September 30, 2007 of \$164,000 and \$436,000, respectively, and \$298,000 and \$902,000 for the same periods in 2006.

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**COGNEX CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4: Inventories (continued)**

The changes in the excess and obsolete inventory reserve during the nine-month period ended September 30, 2007 were as follows (in thousands):

Balance at December 31, 2006	\$ 10,822
Provisions for excess and obsolete inventory	2,714
Inventory sold to customers	(382)
Inventory sold to brokers	(2,573)
Scrap of reserved inventory	(3,059)
Foreign exchange rate changes	659
Balance at September 30, 2007	\$ 8,181

In addition to reserves against existing inventory, in 2001 the Company accrued \$1,400,000 related to inventory purchase commitments. A favorable settlement or outcome of these purchase commitments would result in a recovery of a portion of this accrual.

**NOTE 5: Intangible Assets**

Amortized intangible assets consisted of the following (in thousands):

	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Amount</b>
<b>September 30, 2007</b>			
Distribution networks	\$ 38,060	\$ 7,941	\$ 30,119
Customer contracts and relationships	13,491	5,392	8,099
Completed technologies	6,742	4,463	2,279
Other	1,434	908	526
	\$ 59,727	\$ 18,704	\$ 41,023
 <b>December 31, 2006</b>			
Distribution networks	\$ 38,060	\$ 5,477	\$ 32,583
Customer contracts and relationships	13,002	4,110	8,892
Completed technologies	6,834	4,086	