COHERENT INC
Form 10-Q
February 04, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

S QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended December 27, 2014

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: 001-33962

COHERENT, INC.

Delaware	94-1622541
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

5100 Patrick Henry Drive, Santa Clara, California 95054
(Address of principal executive offices) (Zip Code)
Registrant’s telephone number, including area code: (408) 764-4000

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 S 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 S 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 definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer S	Accelerated filer £
Non-accelerated filer £ (do not check if a smaller reporting company)	Smaller reporting company £

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes £ No S

The number of shares outstanding of registrant's common stock, par value $.01 per share, on January 30, 2015 was 24,731,941.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements included in or incorporated by reference in this quarterly report, other than statements of historical fact, are forward-looking statements. These statements are generally accompanied by words such as “trend,” “may,” “will,” “could,” “would,” “should,” “expect,” “plan,” “anticipate,” “rely,” “believe,” “estimate,” “predict,” “intend,” “potential,” “continue,” "outlook," “forecast” or the negative of or other comparable terminology, including without limitation statements made under “Our Strategy,” discussions regarding our bookings and in “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. Actual results of Coherent, Inc. (referred to herein as the Company, we, our or Coherent) may differ significantly from those anticipated in these forward-looking statements as a result of various factors, including those discussed in the sections captioned “Our Strategy,” “Risk Factors,” “Key Performance Indicators,” as well as any other cautionary language in this quarterly report. All forward-looking statements included in the document are based on information available to us on the date hereof. We undertake no obligation to update these forward-looking statements as a result of events or circumstances or to reflect the occurrence of unanticipated events or non-occurrence of anticipated events.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

COHERENT, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited; in thousands, except per share data)

	Three Months Ended	
	December 27, 2014	December 28, 2013
Net sales	$200,615	$193,556
Cost of sales	118,296	116,010
Gross profit	82,319	77,546
Operating expenses:		
Research and development	19,173	20,937
Selling, general and administrative	38,141	39,891
Amortization of intangible assets	696	934
Total operating expenses	58,010	61,762
Income from operations	24,309	15,784
Other income (expense):		
Interest income	96	59
Interest expense	(11)	(23)
Other—net	(770)	(256)
Total other expense, net	(685)	(220)
Income before income taxes	23,624	15,564
Provision for income taxes	6,194	3,861
Net income	$17,430	$11,703
Net income per share:		
Basic	$0.70	$0.48
Diluted	$0.69	$0.47
Shares used in computation:		
Basic	24,936	24,542
Diluted	25,197	24,915

See Accompanying Notes to Condensed Consolidated Financial Statements.

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COHERENT, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited; in thousands)

	Three Months Ended	
	December 27, 2014	December 28, 2013
Net income	$17,430	$11,703
Other comprehensive income (loss): (1)		
Translation adjustment, net of taxes (2)	(14,519)	1,148
Net gain on derivative instruments, net of taxes (3)	375	—
Changes in unrealized losses on available-for-sale securities, net of taxes (4)	(73)	(11)
Other comprehensive income (loss), net of taxes	(14,217)	1,137
Comprehensive income	$3,213	$12,840

(1) Reclassification adjustments were not significant during the three months ended December 27, 2014 and December 28, 2013.

(2) Tax expense (benefit) of $(752) and $1,186 was provided on translation adjustments during the three months ended December 27, 2014 and December 28, 2013, respectively.

(3) Tax expense of $217 was provided on net gain (loss) on derivative instruments during the three months ended December 27, 2014.

(4) Tax expense (benefit) on changes in unrealized gains (losses) on available-for-sale securities was insignificant.

See Accompanying Notes to Condensed Consolidated Financial Statements.

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COHERENT, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited; in thousands, except par value data)

	December 27, 2014	September 27, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$129,420	$91,217
Short-term investments	193,531	227,058
Accounts receivable—net of allowances of $1,090 and $1,155, respectively	130,461	137,324
Inventories	161,993	170,483
Prepaid expenses and other assets	34,021	27,839
Deferred tax assets	23,765	27,134
Total current assets	673,191	681,055
Property and equipment, net	103,978	107,424
Goodwill	106,602	109,513
Intangible assets, net	28,481	31,666
Other assets	65,755	69,717
Total assets	$978,007	$999,375
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$27,040	$32,784
Income taxes payable	1,262	2,029
Other current liabilities	87,856	82,506
Total current liabilities	116,158	117,319
Other long-term liabilities	54,223	62,407
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Common stock, par value $.01 per share:		
Authorized—500,000 shares		
Outstanding—24,865 shares and 24,950 shares, respectively	248	248
Additional paid-in capital	168,806	184,042
Accumulated other comprehensive income	20,465	34,682
Retained earnings	618,107	600,677
Total stockholders' equity	807,626	819,649
Total liabilities and stockholders' equity	$978,007	$999,375

See Accompanying Notes to Condensed Consolidated Financial Statements.

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COHERENT, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; in thousands)

	Three Months Ended	
	December 27, 2014	December 28, 2013
Cash flows from operating activities:		
Net income	$17,430	$11,703
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,210	6,699
Amortization of intangible assets	2,180	2,445
Deferred income taxes	6,988	(1,621)
Stock-based compensation	4,390	4,868
Other non-cash (income) expense	360	(32)
Changes in assets and liabilities, net of effect of acquisitions:		
Accounts receivable	2,760	19,754
Inventories	4,715	(2,297)
Prepaid expenses and other assets	(8,650)	(9,256)
Other assets	(658)	(2,118)
Accounts payable	(5,358)	(5,658)
Income taxes payable/receivable	(7,277)	(4,361)
Other current liabilities	7,145	5,250
Other long-term liabilities	816	3,301
Net cash provided by operating activities	31,051	28,677
Cash flows from investing activities:		
Purchases of property and equipment	(5,138)	(6,792)
Proceeds from dispositions of property and equipment	568	182
Purchases of available-for-sale securities	(43,780)	(47,224)
Proceeds from sales and maturities of available-for-sale securities	77,370	51,605
Net cash provided by (used in) investing activities	29,020	(2,229)
Cash flows from financing activities:		
Short-term borrowings	11,542	21,154
Repayments of short-term borrowings	(11,542)	(21,154)
Net change in capital lease obligations	—	(2)
Repurchase of common stock	(17,298)	—
Issuance of common stock under employee stock option and purchase plans	3,437	6,810
Net settlement of restricted common stock	(5,200)	(7,658)
Net cash used in financing activities	(19,061)	(850)
Effect of exchange rate changes on cash and cash equivalents	(2,807)	2,333
Net increase in cash and cash equivalents	38,203	27,931
Cash and cash equivalents, beginning of period	91,217	110,444
Cash and cash equivalents, end of period	$129,420	$138,375

See Accompanying Notes to Condensed Consolidated Financial Statements.

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COHERENT, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted pursuant to such rules and regulations. These interim condensed consolidated financial statements and notes thereto should be read in conjunction with the Coherent, Inc. (referred to herein as the "Company," "we," "our," "us" or "Coherent") condensed consolidated financial statements and notes thereto filed on Form 10-K for the fiscal year ended September 27, 2014. In the opinion of management, all adjustments necessary for a fair presentation of financial condition and results of operation as of and for the periods presented have been made and include only normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year or any other interim periods. Our fiscal year ends on the Saturday closest to September 30 and our first fiscal quarters include 13 weeks of operations in each fiscal year presented. Fiscal year 2015 includes 53 weeks and fiscal 2014 includes 52 weeks.

2. RECENT ACCOUNTING STANDARDS

Adoption of New Accounting Pronouncements

In July 2013, the FASB issued amended guidance that resolves the diversity in practice for the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This new accounting guidance requires the netting of unrecognized tax benefits ("UTBs") against a deferred tax asset for a loss or other carryforward that would apply in settlement of the uncertain tax positions. Under the new standard, UTBs will be netted against all available same-jurisdiction losses or other tax carryforwards that would be utilized, rather than only against carryforwards that are created by the UTBs. The new standard requires prospective adoption but allows retrospective adoption for all periods presented. We have adopted the FASB's amended guidance prospectively for our fiscal year beginning September 28, 2014 in accordance with the new standard. As a result of this adoption, both long-term income taxes payable and noncurrent deferred tax assets decreased by approximately $7.9 million on our condensed consolidated balance sheet as of December 27, 2014.

Recently Issued Accounting Pronouncement

In May 2014, the FASB amended the Accounting Standards Codification and created a new Topic 606, Revenue from Contracts with Customers. The new guidance establishes a single comprehensive contract-based model for entities to use in accounting for revenue arising from contracts with customers. The new model significantly changes existing GAAP, requires substantial judgment in its application, and will generally require companies to make more disclosures about revenue. The core principle of the amendment is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the new guidance, an entity will (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the contract's performance obligations; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. The new standard provides for two alternative implementation methods. The first is to apply the new standard retrospectively to each prior reporting period presented. This method does allow the use of certain practical expedients. The second method is to apply the new standard retrospectively in the year of initial adoption and record a cumulative effect adjustment for the impact of adjusting contracts open at the

date of adoption. Under this transition method, we would apply this guidance retrospectively only to contracts that are not completed contracts at the date of initial application. We would then recognize the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings. This method also requires us to disclose comparative information for the year of adoption. We will adopt the FASB's amended guidance for our fiscal year beginning October 1, 2017; early adoption is not permitted. We are currently evaluating the new guidance and have not determined the impact this standard may have on our financial statements nor have we decided upon the method of adoption.

3. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

We measure our cash equivalents and marketable securities at fair value. The fair values of our financial assets and liabilities are determined using quoted market prices of identical assets or quoted market prices of similar assets from active markets. Level 1 valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets. Level 2 valuations are obtained from quoted market prices in active markets involving similar assets; these instruments, which mature within two years and are issued by counterparties with high credit ratings, include U.S. Treasury and international government obligations, investment-grade corporate bonds, certificates of deposit and commercial paper. Level 3 valuations would be based on unobservable inputs to a valuation model and include our own data about assumptions market participants would use in pricing the asset or liability based on the best information available under the circumstances. As of December 27, 2014 and September 27, 2014, we did not have any assets or liabilities valued based on Level 3 valuations.

Financial assets and liabilities measured at fair value as of December 27, 2014 and September 27, 2014 are summarized below (in thousands):

	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs
	December 27, 2014		September 27, 2014	
	(Level 1)	(Level 2)	(Level 1)	(Level 2)
Money market fund deposits(1)	$14,516	$—	$5,975	$—
Certificates of deposit(1)	—	37,396	—	12,084
U.S. and international government obligations(3)(8)	—	141,456	—	150,088
Corporate notes and obligations(2)(8)	—	52,853	—	52,987
Commercial paper(4)(8)	—	7,999	—	25,383
Equity Securities (5)	—	130	—	—
Foreign currency contracts(6)(9)	—	(1,316)	—	(1,830)
Mutual funds — Deferred comp and supplemental plan(7)(10)	15,225	—	15,000	—

(1) Included in cash and cash equivalents on the Condensed Consolidated Balance Sheet. The carrying amounts approximate fair value due to the short-term maturities of the cash equivalents.

(2) Included in short-term investments on the Condensed Consolidated Balance Sheet.

(3) December 27, 2014: $8,905 recorded in cash and cash equivalents and $132,551 recorded in short-term investments on the Condensed Consolidated Balance Sheet.

September 27, 2014: Included in short-term investments on the Condensed Consolidated Balance Sheet.

(4) December 27, 2014: Included in short-term investments on the Condensed Consolidated Balance Sheet.

September 27, 2014: Includes $1,400 recorded in cash and cash equivalents and $23,983 recorded in short-term investments on the Condensed Consolidated Balance Sheet.

(5) December 27, 2014: Includes $2 recorded in cash and cash equivalents and $128 recorded in short-term investments on the Condensed Consolidated Balance Sheet.

(6) December 27, 2014: Includes $398 and $360 recorded in prepaid expenses and other assets on the Condensed Consolidated Balance Sheet for non-designated forward contracts and cash flow contracts, respectively. Includes $1,414 and $660 recorded in other current liabilities on the Condensed Consolidated Balance Sheet for non-designated forward contracts and cash flow contracts, respectively. (See Note 4).

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September 27, 2014: Includes $303 and $63 recorded in prepaid expenses and other assets on the Condensed Consolidated Balance Sheet for non-designated forward contracts and cash flow contracts, respectively. Includes $1,246 and $950 both recorded in other current liabilities on the Condensed Consolidated Balance Sheet for non-designated forward contracts and cash flow contracts, respectively. (See Note 4).

(7) December 27, 2014: Includes $1,560 recorded in prepaid expenses and other assets and $13,665 recorded in other assets on the Condensed Consolidated Balance Sheet.

September 27, 2014: Includes $1,515 recorded in prepaid expenses and other assets and $13,485 recorded in other assets on the Condensed Consolidated Balance Sheet.

(8) Valuations are based upon quoted market prices in active markets involving similar assets. The market inputs used to value these instruments generally consist of market yields, reported trades, broker/dealer quotes or alternative pricing sources with reasonable levels of price transparency. Pricing sources include industry standard data providers, security master files from large financial institutions, and other third party sources which are input into a distribution-curve-based algorithm to determine a daily market value. This creates a “consensus price” or a weighted average price for each security.

(9) The principal market in which we execute our foreign currency contracts is the institutional market in an over-the-counter environment with a relatively high level of price transparency. The market participants usually are large commercial banks. Our foreign currency contracts’ valuation inputs are based on quoted prices and quoted pricing intervals from public data sources and do not involve management judgment.

(10) The fair value of mutual funds is determined based on quoted market prices. Securities traded on a national exchange are stated at the last reported sales price on the day of valuation; other securities traded in over-the-counter market and listed securities for which no sale was reported on that date are stated as the last quoted bid price.

4. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

All derivatives, whether designated in hedging relationships or not, are recorded on the Condensed Consolidated Balance Sheet at fair value. We enter into foreign exchange forwards to minimize the risks of foreign currency fluctuation of specific assets and liabilities on the balance sheet; these are not designated as hedging instruments. Our derivative contracts do not contain any credit risk related contingent features and do not require collateral or other security to be furnished by us or the counterparties.

We maintain operations in various countries outside of the United States and have foreign subsidiaries that manufacture and sell our products in various global markets. The majority of our sales are transacted in U.S. dollars. However, we do generate revenues in other currencies, primarily the Euro, Japanese Yen (JPY), Korean Won and Chinese Renminbi (RMB). As a result, our earnings, cash flows and cash balances are exposed to fluctuations in foreign currency exchange rates. We attempt to limit these exposures through financial market instruments. We utilize derivative instruments, primarily forward contracts with maturities of four months or less, to manage our exposure associated with anticipated cash flows and net asset and liability positions denominated in foreign currencies. Gains and losses on the forward contracts are mitigated by gains and losses on the underlying instruments. We do not use derivative financial instruments for speculative or trading purposes. If a financial counterparty to any of our hedging arrangements experiences financial difficulties or is otherwise unable to honor the terms of the foreign currency hedge, we may experience material financial losses.

For derivative instruments that are not designated as hedging instruments, gains and losses are recognized in other income (expense).

Cash flow hedges related to anticipated transactions are designated and documented at the inception of the hedge when we enter into contracts for specific future transactions. Cash flow hedges are evaluated for effectiveness quarterly. The effective portion of the gain or loss on these hedges is reported as a component of Other Comprehensive Income ("OCI") in stockholder's equity and is reclassified into earnings when the underlying transaction affects earnings. The majority of the after-tax net income or loss related to derivative instruments included in OCI at December 27, 2014 is expected to be reclassified into earnings within 12 months. Changes in the fair value of currency forward contracts due to changes in time value are excluded from the assessment of effectiveness and recognized in other income (expense) as incurred. We classify the cash flows from the foreign exchange forward contracts that are accounted for as cash flow hedges in the same section

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as the underlying item, primarily within cash flows from operating activities since we do not designate our cash flow hedges as investing or financing activities.

The outstanding notional contract and fair value amounts of non-designated hedge contracts, with maximum maturity of four months, are as follows (in thousands):

	U.S. Notional Contract Value		U.S. Fair Value	
	December 27, 2014	September 27, 2014	December 27, 2014	September 27, 2014
Euro currency hedge contracts				
Purchase	$48,113	$31,926	$(1,240)	$(1,153)
Sell	$(2,624)	$—	$(12)	$—
Japanese Yen currency hedge contracts				
Purchase	$307	$471	$—	(3)
Sell	$(8,369)	$(15,084)	$368	$169
Korean Won currency hedge contracts				
Sell	$(4,235)	$(2,991)	$(68)	$72
Chinese RMB currency hedge contracts				
Sell	$(9,035)	$(15,678)	$(57)	$(56)
Other foreign currency hedge contracts				
Purchase	$2,445	$1,899	$(25)	$(35)
Sell	$(5,447)	$(3,515)	$18	$63

The outstanding notional contract and fair value amounts of designated cash flow hedge contracts, with maximum maturity of twelve months, are as follows (in thousands):

	U.S. Notional Contract Value		U.S. Fair Value	
	December 27, 2014	September 27, 2014	December 27, 2014	September 27, 2014
Euro currency hedge contracts				
Purchase	$5,574	$11,149	$(660)	$(950)
Japanese Yen currency hedge contracts				
Sell	$(5,859)	$(12,091)	$360	$63

We have entered into certain derivative forward contracts to sell Japanese Yen and buy Euro to hedge revenue exposures related to our photonics-based solutions in Asia. In order to facilitate the hedge, we transact with counterparties in the US directly and then allocate the hedge contracts to our affiliates through a back-to-back relationship with our German subsidiary. The German subsidiary designates these hedge contracts as cash flow hedges under ASC 815

The fair value of our derivative instruments are included in prepaid expenses and other assets and in other current liabilities in our Condensed Consolidated Balance Sheets (see Note 3); such amounts were not material as of December 27, 2014 and September 27, 2014.

The locations and amounts of designated and non-designated derivative instruments' gains and losses in the condensed consolidated financial statements for the indicated periods were as follows (in thousands):

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	Location in financial statements	Three Months Ended December 27, 2014	December 28, 2013
Derivatives designated as hedging instruments			
Gains(losses) in AOCI on derivatives (effective portion), after tax	AOCI	$ 375	$ —
Gains(losses) reclassified from AOCI into income (effective portion)	Revenue	$ 300	$ —
Gains(losses) reclassified from AOCI into income (effective portion)	Cost of sales	$ (614)	$ —
Gains(losses) recognized in income on derivatives (ineffective portion and amount excluded from effectiveness testing)	Other income(expense)	$ 35	$ —
Derivatives not designated as hedging instruments			
Gains(losses) recognized in income	Other income(expense)	$ (712)	$ (38)

The amounts that will be reclassified from AOCI to earnings will generally be offset by the recognition of the hedged transactions (e.g., anticipated cost of sales) in earnings, thereby achieving the realization of prices contemplated by the underlying risk management strategies and will vary from the expected amounts presented above as a result of changes in foreign exchange rates.

To mitigate credit risk in derivative transactions, we enter into master netting arrangements that allow each counterparty in the arrangements to net settle amounts of multiple and separate derivative transactions under certain conditions. We present the fair value of derivative assets and liabilities within our condensed consolidated balance sheet on a gross basis even when derivative transactions are subject to master netting arrangements and may otherwise qualify for net presentation. Our derivative contracts do not contain any credit risk related contingent features and do not require collateral or other security to be furnished by us or the counterparties.

Offsetting of Financial Assets/Liabilities under Master Netting Agreements with Derivative Counterparties as of December 27, 2014 and September 27, 2014 (in thousands):

				Gross Amounts Not Offset in the Condensed Consolidated Balance Sheets		
	Gross Amounts of Recognized Derivative	Gross Amounts Offset in the Condensed	Net Amounts of Derivative Assets Presented in	Financial Instruments (1)	Cash Collateral Received	Net Amounts

	Assets	Consolidated Balance Sheets	the Condensed Consolidated Balance Sheets			
As of December 27, 2014:						
Foreign exchange contracts	$758	$—	$758	$(88)	$—	670
As of September 27, 2014:						
Foreign exchange contracts	$367	$—	$367	$(367)	$—	$—

(1) The balances at December 27, 2014 and September 27, 2014 were related to derivative liabilities which are allowed to be net settled against derivative assets in accordance with the master netting agreements.

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	Gross Amounts of Recognized Derivative Liabilities	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts of Derivative Liabilities Presented in the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset in the Condensed Consolidated Balance Sheets		
				Financial Instruments (1)	Cash Collateral Paid	Net Amounts
As of December 27, 2014:						
Foreign exchange contracts	$(2,074)	$—	$(2,074)	$88	$—	(1,986)
As of September 27, 2014:						
Foreign exchange contracts	$(2,197)	$—	$(2,197)	$367	$—	$(1,830)

(1) The balances at December 27, 2014 and September 27, 2014 were related to derivative assets which are allowed to be net settled against derivative liabilities in accordance with the master netting agreements.

5. SHORT-TERM INVESTMENTS

We consider all highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents. Investments classified as available-for-sale are reported at fair value with unrealized gains and losses, net of related income taxes, recorded as a separate component of other comprehensive income ("OCI") in stockholders' equity until realized. Interest and amortization of premiums and discounts for debt securities are included in interest income. Gains and losses on securities sold are determined based on the specific identification method and are included in other income (expense).

Cash, cash equivalents and short-term investments consist of the following (in thousands):

	December 27, 2014			
	Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash and cash equivalents	$129,415	$6	$(1)	$129,420
Short-term investments:				
Available-for-sale securities:				
Commercial paper	$7,999	$—	$—	$7,999
U.S. Treasury and agency obligations	131,888	732	(69)	132,551
Equity Securities	99	29	—	128
Corporate notes and obligations	52,617	319	(83)	52,853
Total short-term investments	$192,603	$1,080	$(152)	$193,531

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	September 27, 2014			
	Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash and cash equivalents	$91,217	$—	$—	$91,217
Short-term investments:				
Available-for-sale securities:				
Commercial paper	$23,983	$—	$—	$23,983
U.S. Treasury and agency obligations	149,260	831	(3)	150,088
Corporate notes and obligations	52,834	195	(42)	52,987
Total short-term investments	$226,077	$1,026	$(45)	$227,058

None of the unrealized losses as of December 27, 2014 or September 27, 2014 were considered to be other-than-temporary impairments.

The amortized cost and estimated fair value of available-for-sale investments in debt securities as of December 27, 2014 and September 27, 2014, classified as short-term investments on our condensed consolidated balance sheet were as follows (in thousands):

	December 27, 2014		September 27, 2014	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Investments in available-for-sale debt securities due in less than one year	$152,248	$ 153,139	$178,329	$ 179,223
Investments in available-for-sale debt securities due in one to five years [(1)]	$40,256	$ 40,264	$47,748	$ 47,835

(1) Classified as short-term investments because these securities are highly liquid and can be sold at any time.

During the three months ended December 27, 2014, we received proceeds totaling $29.6 million from the sale of available-for-sale securities and realized gross gains of less than $0.1 million. During the three months ended December 28, 2013, we received proceeds totaling $7.0 million from the sale of available-for-sale securities and realized gross gains of less than $0.1 million.

6. GOODWILL AND INTANGIBLE ASSETS

Goodwill is tested for impairment on an annual basis and between annual tests if events or circumstances indicate that an impairment loss may have occurred, and we write down these assets when impaired. We perform our annual impairment tests during the fourth quarter of each fiscal year using the opening balance sheet as of the first day of the fourth quarter, with any resulting impairment recorded in the fourth quarter of the fiscal year.

During the three months ended December 27, 2014, we noted no indications of impairment or triggering events to cause us to review goodwill for potential impairment. We will conduct our annual goodwill testing during the fourth fiscal quarter.

The changes in the carrying amount of goodwill by segment for the period from September 27, 2014 to December 27, 2014 are as follows (in thousands):

	Specialty Lasers and	Commercial Lasers and	Total

	Systems	Components	
Balance as of September 27, 2014	$103,150	$6,363	$109,513
Additions	—	—	—
Translation adjustments and other	(2,911)	—	(2,911)
Balance as of December 27, 2014	$100,239	$6,363	$106,602

Components of our amortizable intangible assets are as follows (in thousands):

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	December 27, 2014			September 27, 2014		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Existing technology	$80,063	$(58,792)	$21,271	$81,551	$(57,827)	$23,724
Customer lists	16,238	(9,508)	6,730	16,632	(9,199)	7,433
Trade name	421	(349)	72	431	(346)	85
In-process research & development	408	—	408	424	—	424
Total	$97,130	$(68,649)	$28,481	$99,038	$(67,372)	$31,666

** For accounting purposes, when an intangible asset is fully amortized, it is removed from the disclosure schedule.

Amortization expense for intangible assets for the three months ended December 27, 2014 and December 28, 2013 was $2.2 million and $2.4 million, respectively, which includes $1.7 million and $1.9 million, respectively, for amortization of existing technology.

At December 27, 2014, estimated amortization expense for the remainder of fiscal 2015, the next five succeeding fiscal years and all fiscal years thereafter are as follows (in thousands):

	Estimated Amortization Expense
2015 (remainder)	$6,438
2016	8,210
2017	7,086
2018	4,170
2019	2,232
2020	201
Thereafter	144
Total	$28,481

7. BALANCE SHEET DETAILS

Inventories consist of the following (in thousands):

	December 27, 2014	September 27, 2014
Purchased parts and assemblies	$49,454	$51,091
Work-in-process	65,238	70,486
Finished goods	47,301	48,906
Total inventories	$161,993	$170,483

Prepaid expenses and other assets consist of the following (in thousands):

	December 27, 2014	September 27, 2014
Prepaid and refundable income taxes	$8,887	$11,001
Other taxes receivable	11,068	5,184
Prepaid expenses and other	14,066	11,654
Total prepaid expenses and other assets	$34,021	$27,839

Other assets consist of the following (in thousands):

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	December 27, 2014	September 27, 2014
Assets related to deferred compensation arrangements	$26,888	$26,484
Deferred tax assets	33,289	37,616
Other assets	5,578	5,617
Total other assets	$65,755	$69,717

Other current liabilities consist of the following (in thousands):

	December 27, 2014	September 27, 2014
Accrued payroll and benefits	$28,986	$29,228
Deferred income	15,668	15,536
Warranty Reserve	16,604	16,961
Accrued expenses and other	13,411	13,410
Other taxes payable	9,057	5,036
Customer deposits	4,130	2,335
Total other current liabilities	$87,856	$82,506

We provide warranties on the majority of our product sales and reserves for estimated warranty costs are recorded during the period of sale. The determination of such reserves requires us to make estimates of product return rates and expected costs to repair or replace the products under warranty. We currently establish warranty reserves based on historical warranty costs for each product line. The weighted average warranty period covered is approximately 15 months. If actual return rates and/or repair and replacement costs differ significantly from our estimates, adjustments to cost of sales may be required in future periods.

Components of the reserve for warranty costs during the first three months of fiscal 2015 and 2014 were as follows (in thousands):

	Three Months Ended	
	December 27, 2014	December 28, 2013
Beginning balance	$16,961	$18,508
Additions related to current period sales	5,608	6,708
Warranty costs incurred in the current period	(5,135)	(6,815)
Adjustments to accruals related to foreign exchange and other	(830)	—
Ending balance	$16,604	$18,401

Other long-term liabilities consist of the following (in thousands):

	December 27, 2014	September 27, 2014
Long-term taxes payable	$7,864	$15,776
Deferred compensation	28,402	27,858
Deferred tax liabilities	6,046	6,511
Deferred income	3,229	3,448
Asset retirement obligations liability	2,151	2,222
Other long-term liabilities	6,531	6,592
Total other long-term liabilities	$54,223	$62,407

8. SHORT-TERM BORROWINGS

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We have several lines of credit which allow us to borrow in the applicable local currency. We have a total of $13.7 million of unsecured foreign lines of credit as of December 27, 2014. At December 27, 2014, we had used $3.0 million of these available foreign lines of credit as guarantees. These credit facilities were used in Europe, Japan and China during the first quarter of fiscal 2015. In addition, our domestic line of credit consists of a $50.0 million unsecured revolving credit account with Union Bank of California. The agreement will expire on May 31, 2017. The line of credit is subject to covenants related to financial ratios and tangible net worth with which we are currently in compliance. No amounts have been drawn upon our domestic line of credit as of December 27, 2014.

9. STOCK-BASED COMPENSATION

Fair Value of Stock-based compensation

We recognize compensation expense for all share based payment awards based on the fair value of such awards. The expense is recognized on a straight-line basis over the respective requisite service period of the awards.

Determining Fair Value

The fair values of shares purchased under the Employee Stock Purchase Plan ("ESPP") for the three months ended December 27, 2014 and December 28, 2013, respectively, were estimated using the following weighted-average assumptions:

	Employee Stock Purchase Plan Three Months Ended			
	December 27, 2014		December 28, 2013	
Expected life in years	0.5		0.5	
Expected volatility	24.8	%	24.8	%
Risk-free interest rate	0.1	%	0.1	%
Expected dividend yield	—	%	—	%
Weighted average fair value per share	$13.97		$13.49	

There were no stock options granted during the three months ended December 27, 2014 and December 28, 2013.

Restricted stock awards and restricted stock units are typically subject to vesting restrictions—either time-based or performance-based market conditions for vesting. Until restricted stock vests, shares (including those issuable upon vesting of the applicable restricted stock unit) are subject to forfeiture if employment terminates prior to the release of restrictions and cannot be transferred.

- The service based restricted stock awards generally vest three years from the date of grant.
- The service based restricted stock unit awards are generally subject to annual vesting over three years from the date of grant.
- The market-based performance restricted stock unit award grants are generally either subject to annual vesting over three years from the date of grant or subject to a single vest measurement three years from the date of grant, depending upon achievement of performance measurements based on the performance of the Company's Total Shareholder Returns (as defined in the plan) compared with the performance of the Russell 2000 Index.

We grant market-based performance restricted stock unit award grants to officers and certain employees. The performance stock unit agreements provide for the award of performance stock units with each unit representing the right to receive one share of our common stock to be issued after the applicable award period. The final number of units awarded for this grant will be determined as of the vesting dates, based upon our total shareholder return over the

performance period compared to the Russell 2000 Index and could range from a minimum of no units to a maximum of twice the target award. The weighted average fair value for these performance units was determined using a Monte Carlo simulation model incorporating the following weighted average assumptions:

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	Three Months Ended			
	December 27, 2014		December 28, 2013	
Risk-free interest rate	0.96	%	0.62	%
Volatility	28.7	%	36.9	%
Weighted average fair value	$70.57		$77.10	

We recognize the estimated cost of these awards, as determined under the simulation model, over the related service period, with no adjustment in future periods based upon the actual shareholder return over the performance period.

Stock-Based Compensation Expense

The following table shows total stock-based compensation expense and related tax benefits included in the condensed consolidated statements of operations for the three months ended December 27, 2014 and December 28, 2013 (in thousands):

	Three Months Ended			
	December 27, 2014		December 28, 2013	
Cost of sales	$597		$538	
Research and development	330		522	
Selling, general and administrative	3,463		3,808	
Income tax benefit	(430	)	(1,339	)
	$3,960		$3,529	

During the three months ended December 27, 2014, $0.7 million was capitalized into inventory for all stock plans, $0.6 million was amortized to cost of sales and $0.8 million remained in inventory at December 27, 2014. During the three months ended December 28, 2013, $0.7 million was capitalized into inventory for all stock plans, $0.5 million was amortized to cost of sales and $0.8 million remained in inventory at December 28, 2013. Management has made an estimate of expected forfeitures and is recognizing compensation costs only for those equity awards expected to vest.

At December 27, 2014, the total compensation cost related to unvested stock-based awards granted to employees under the Company's stock plans but not yet recognized was approximately $27.7 million, net of estimated forfeitures of $1.0 million. This cost will be amortized on a straight-line basis over a weighted-average period of approximately 1.8 years and will be adjusted for subsequent changes in estimated forfeitures.

At December 27, 2014, total compensation cost related to options to purchase common shares under the ESPP but not yet recognized was approximately $0.6 million, which will be recognized over the six month offering period.

The stock option exercise tax benefits reported in the statement of cash flows results from the excess tax benefits arising from tax deductions in excess of the stock-based compensation cost recognized, determined on a grant-by-grant basis. During the first three months of fiscal 2015 and fiscal 2014, we have not generated any excess tax benefits as cash flows from financing activities.

Stock Options & Awards Activity

The following is a summary of option activity for our Stock Option Plans (in thousands, except per share amounts and weighted average remaining contractual term in years):

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	Number of Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
Outstanding at September 27, 2014	107	$29.20		
Granted	—	—		
Exercised	(4)	23.16		
Forfeitures	—	—		
Expirations	—	—		
Outstanding at December 27, 2014	103	$29.46	3.8 years	$3,395
Vested and expected to vest at December 27, 2014	103	$29.46	3.8 years	$3,395
Exercisable at December 27, 2014	103	$29.46	3.8 years	$3,395

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying options and the quoted price of our common stock for in-the money options. The aggregate intrinsic value of options exercised under the Company's stock plans for the three months ended December 27, 2014 and December 28, 2013 were $0.2 million and $5.8 million, respectively, determined as of the date of option exercise.

The following table summarizes the activity of our time based and market- performance based restricted stock units for the first three months of fiscal 2015 (number of shares in thousands):

	Time Based Restricted Stock Units		Market-Based Performance Restricted Stock Units	
	Number of Shares(1)	Weighted Average Grant Date Fair Value	Number of Shares(2)	Weighted Average Grant Date Fair Value
Nonvested stock at September 27, 2014	390	$58.66	229	$61.46
Granted	214	64.82	51	70.57
Vested	(194)	51.99	(38)	53.46
Forfeited	(2)	60.81	(43)	53.46
Nonvested stock at December 27, 2014	408	$65.07	199	$67.09

(1)Service-based restricted stock vested during each fiscal year.
(2)Performance-based awards and units included at 100% of target goal; under the terms of the awards, the recipient may earn between 0% and 200% of the award.

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10. COMMITMENTS AND CONTINGENCIES

We are subject to legal claims and litigation arising in the ordinary course of business, such as product liability, employment or intellectual property claims, including, but not limited to, the matter described below. On May 14, 2013, IMRA America ("Imra") filed a complaint for patent infringement against two of the Company's subsidiaries in the Regional Court of Düsseldorf, Germany, captioned In re IMRA America Inc. versus Coherent Kaiserslautern GmbH et. al. 4b O 38/13. The complaint alleges that the use of certain of the Company's lasers infringes upon EP Patent No. 754,103, entitled "Method For Controlling Configuration of Laser Induced Breakdown and Ablation," issued November 5, 1997. The patent is owned by the University of Michigan and licensed to Imra. The complaint seeks unspecified compensatory damages, the cost of court proceedings and seeks to permanently enjoin the Company from infringing the patent in the future. Management has made an accrual of the amount which is reasonably estimable and probable with respect to this matter and has determined, based on its current knowledge, that the amount or range of reasonably possible losses in excess of the amounts already accrued is not reasonably estimable. Although we do not expect that such legal claims and litigation will ultimately have a material adverse effect on our condensed consolidated financial position, results of operations or cash flows, an adverse result in one or more matters could negatively affect our results in the period in which they occur.

The United States and many foreign governments impose tariffs and duties on the import and export of certain products we sell. From time to time our duty calculations and payments are audited by government agencies. We are currently under audit in South Korea for customs duties and value added tax for the period March 2009 to March 2014. At this time, management has not made an accrual of an amount related to this matter since it has determined that such accrual is neither probable nor reasonably estimable. Although we do not expect that the audit will ultimately have a material adverse effect on our condensed consolidated financial position, results of operations or cash flows, an adverse result in this matter could negatively affect our results in the period in which they occur.

11. STOCK REPURCHASE

On July 25, 2014, the Board of Directors authorized a buyback program whereby we are authorized to repurchase up to $25.0 million of our common stock from time to time through July 31, 2015. During the first quarter of fiscal 2015, we repurchased and retired 300,441 shares of outstanding common stock at an average price of $57.55 per share for a total of $17.3 million, excluding expenses. During the month of January of fiscal 2015, we repurchased and retired 133,673 shares of outstanding common stock under this plan at an average price of $57.66 per share for a total of $7.7 million.

12. EARNINGS PER SHARE

Basic earnings per share is computed based on the weighted average number of shares outstanding during the period, excluding unvested restricted stock. Diluted earnings per share is computed based on the weighted average number of shares outstanding during the period increased by the effect of dilutive employee stock awards, including stock options, restricted stock awards and stock purchase plan contracts, using the treasury stock method.

The following table presents information necessary to calculate basic and diluted earnings per share (in thousands, except per share data):

	Three Months Ended	
	December 27, 2014	December 28, 2013
Weighted average shares outstanding —basic	24,936	24,542

Dilutive effect of employee stock awards	261	373
Weighted average shares outstanding—diluted	25,197	24,915
Net income	$17,430	$11,703
Net income per basic share	$0.70	$0.48
Net income per diluted share	$0.69	$0.47

A total of 159,618 and 29,916 potentially dilutive securities have been excluded from the diluted share calculation for the three months ended December 27, 2014 and December 28, 2013, respectively, as their effect was anti-dilutive.

13. OTHER INCOME (EXPENSE)

Other income (expense) is as follows (in thousands):

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	Three Months Ended	
	December 27, 2014	December 28, 2013
Foreign exchange loss	$(1,161)	$(2,124)
Gain on deferred compensation investments, net	384	1,877
Other—net	7	(9)
Other expense, net	$(770)	$(256)

14. INCOME TAXES

Income tax expense includes a provision for federal, state and foreign taxes based on the annual estimated effective tax rate applicable to us and our subsidiaries, adjusted for items which are considered discrete to the period. Our effective tax rate for the three months ended December 27, 2014 was 26.2%. Our effective tax rate for the three months ended December 27, 2014 was lower than the statutory rate of 35.0% primarily due to differences related to the benefit of income subject to foreign tax rates that are lower than U.S. statutory tax rates including Korea and Singapore tax exemptions, the benefit of foreign tax credits and the benefit of the federal research and development tax credits including renewal of the federal research and development tax credits for fiscal 2014. These amounts are partially offset by deemed dividend inclusions under the Subpart F tax rules, stock-based compensation not deductible for tax purposes and limitations on the deductibility of compensation under IRC Section 162(m).

Determining the consolidated provision for income taxes, income tax liabilities and deferred tax assets and liabilities involves judgment. We calculate and provide for income taxes in each of the tax jurisdictions in which we operate, which involves estimating current tax exposures as well as making judgments regarding the recoverability of deferred tax assets in each jurisdiction. The estimates used could differ from actual results, which may have a significant impact on operating results in future periods.

We are subject to taxation and file income tax returns in the U.S. federal jurisdiction and in many state and foreign jurisdictions. For U.S. federal income tax purposes, all years prior to 2011 are closed. In our major foreign jurisdictions and our major state jurisdictions, the years prior to 2006 and 2010, respectively, are closed to examination. Earlier years in our various jurisdictions may remain open for adjustment to the extent that we have tax attribute carryforwards from those years. In December 2011 and January 2012, three of our German subsidiaries received notices of tax audits for the fiscal years 2006 through 2010. In fiscal year 2013, we received a preliminary assessment for two of the German subsidiaries and the amount is immaterial; the audit for the other German subsidiary is currently in process.

Management believes that it has adequately provided for any adjustments that may result from tax examinations. We regularly engage in discussions and negotiations with tax authorities regarding tax matters in various jurisdictions. It is reasonably possible that certain foreign tax matters may be concluded in the next 12 months.

The Tax Increase Prevention Act of 2014 (“the Act”), was enacted on December 19, 2014. Under the Act, the federal research and development tax credit was retroactively extended for amounts paid or incurred after December 31, 2013 through December 31, 2014. The effects of the change in the tax law are recognized in our first quarter of fiscal 2015, which is the quarter that the law was enacted. Accordingly, prior year research and development tax credits of approximately $1.3 million less appropriate reserves are recognized in the first quarter of fiscal 2015.

15. SEGMENT INFORMATION

We are organized into two reportable operating segments: Specialty Lasers and Systems ("SLS") and Commercial Lasers and Components ("CLC"). This segmentation reflects the go-to-market strategies for various products and

markets. While both segments work to deliver cost-effective solutions, SLS develops and manufactures configurable, advanced-performance products largely serving the microelectronics, scientific research and government programs and OEM components and instrumentation markets. The size and complexity of many of our SLS products require service to be performed at the customer site by factory-trained field service engineers. CLC focuses on higher volume products that are offered in set configurations. The product architectures are designed for easy exchange at the point of use such that product service and repairs are based upon advanced replacement and depot (i.e., factory) repair. CLC's primary markets include materials processing, OEM components and instrumentation and microelectronics.

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We have identified SLS and CLC as operating segments for which discrete financial information is available. Both units have dedicated engineering, manufacturing, product business management and product line management functions. Occasionally, a small portion of our outside revenue is attributable to projects and recently developed products for which a segment has not yet been determined. The associated direct and indirect costs are presented in the category of Corporate and other, along with other corporate costs as described below.

Our Chief Executive Officer has been identified as the chief operating decision maker (CODM) as he assesses the performance of the segments and decides how to allocate resources to the segments. Income from operations is the measure of profit and loss that our CODM uses to assess performance and make decisions. As assets are not a measure used to assess the performance of the company by the CODM, asset information is not tracked or compiled by segment and is not available to be reported in our disclosures. Income from operations represents the net sales less the cost of sales and direct operating expenses incurred within the operating segments as well as allocated expenses such as shared sales and manufacturing costs. We do not allocate to our operating segments certain operating expenses which we manage separately at the corporate level. These unallocated costs include stock-based compensation and corporate functions (certain research and development, management, finance, legal and human resources) and are included in the results below under Corporate and other in the reconciliation of operating results. Management does not consider unallocated Corporate and other costs in its measurement of segment performance.

The following table provides net sales and income from operations for our operating segments (in thousands):

	Three Months Ended	
	December 27, 2014	December 28, 2013
Net sales:		
Specialty Laser Systems	$145,091	$136,823
Commercial Lasers and Components	55,524	56,733
Total net sales	$200,615	$193,556
Income from operations:		
Specialty Laser Systems	$34,554	$28,632
Commercial Lasers and Components	703	306
Corporate and other	(10,948)	(13,154)
Total income from operations	$24,309	$15,784

The following table provides a reconciliation of our total income from operations to net income (in thousands):

Reconciliation of Income From Operations to Net Income	Three Months Ended	
	December 27, 2014	December 28, 2013
Total income from operations	$24,309	$15,784
Total other income, net	(685)	(220)
Income before income taxes	23,624	15,564
Provision for income taxes	6,194	3,861
Net Income	$17,430	$11,703

Major Customers

We had one major customer during the three months ended December 27, 2014 who accounted for 18.6% and 13.8% of consolidated revenue during the three months ended December 27, 2014 and the three months ended December 28, 2013, respectively. The customer purchased primarily from our SLS segment.

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We had one major customer who accounted for 18.3% and 15.2% of accounts receivable at December 27, 2014 and September 27, 2014, respectively. There was one additional major customer who accounted for 11.6% of accounts receivable at September 27, 2014. Both customers purchased primarily from our SLS segment.

16. SUBSEQUENT EVENT

On January 21, 2015, our board of directors authorized an additional stock repurchase program to repurchase up to $25.0 million of the Company's outstanding common stock from time to time through January 31, 2016.

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

COMPANY OVERVIEW

BUSINESS BACKGROUND

We are one of the world’s leading suppliers of photonics-based solutions in a broad range of commercial and scientific research applications. We design, manufacture, service and market lasers and related accessories for a diverse group of customers. Since
inception in 1966, we have grown through internal expansion and through strategic acquisitions of complementary businesses, technologies, intellectual property, manufacturing processes and product offerings.

We are organized into two operating segments: Specialty Lasers and Systems (“SLS”) and Commercial Lasers and Components (“CLC”). This segmentation reflects the go-to-market strategies for various products and markets. While both segments deliver cost-effective photonics solutions, SLS develops and manufactures configurable, advanced performance products largely serving the microelectronics, scientific research and government programs and OEM components and instrumentation markets. The size and complexity of many of the SLS products require service to be performed at the customer site by factory trained field service engineers. CLC focuses on higher volume products that are offered in set configurations. The product architectures are designed for easy exchange at the point of use such that substantially all product service and repairs are based upon advanced replacement and depot (i.e., factory) repair. CLC’s primary markets include materials processing, original equipment manufacturer (“OEM”) components and instrumentation and microelectronics.

Income (loss) from operations is the measure of profit and loss that our chief operating decision maker (“CODM”) uses to assess performance and make decisions. Income (loss) from operations represents the sales less the cost of sales and direct operating expenses incurred within the operating segments as well as allocated expenses such as shared sales and manufacturing costs. We do not allocate to our operating segments certain operating expenses, which we manage separately at the corporate level. These unallocated costs include stock-based compensation and corporate functions (certain advanced research and development, management, finance, legal and human resources) and are included in Corporate and other. Management does not consider unallocated Corporate and other costs in its measurement of segment performance.

MARKET APPLICATIONS

Our products address a broad range of applications that we group into the following markets: Microelectronics, Materials Processing, OEM Components and Instrumentation and Scientific Research and Government Programs.

OUR STRATEGY

We strive to develop innovative and proprietary products and solutions that meet the needs of our customers and that are based on our core expertise in lasers and optical technologies. In pursuit of our strategy, we intend to:

- Leverage our technology portfolio and application engineering to lead the proliferation of photonics into broader markets—We will continue to identify opportunities in which our technology portfolio and application engineering can be used to offer innovative solutions and gain access to new markets. We plan to utilize our expertise to increase our market share in the mid to high power material processing applications.

- Optimize our leadership position in existing markets—There are a number of markets where we have historically been at the forefront of technological development and product deployment and from which we have derived a substantial portion of our revenues. We plan to optimize our financial returns from these markets.
- Maintain and develop additional strong collaborative customer and industry relationships—We believe that the Coherent brand name and reputation for product quality, technical performance and customer satisfaction will help us to further develop our loyal customer base. We plan to maintain our current customer relationships and develop new ones with customers who are industry leaders and work together with these customers to design and develop innovative product systems and solutions as they develop new technologies.

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- Develop and acquire new technologies and market share—We will continue to enhance our market position through our existing technologies and develop new technologies through our internal research and development efforts, as well as through the acquisition of additional complementary technologies, intellectual property, manufacturing processes and product offerings.
- Streamline our manufacturing structure and improve our cost structure—We will focus on optimizing the mix of products that we manufacture internally and externally. We will utilize vertical integration where our internal manufacturing process is considered proprietary and seek to leverage external sources when the capabilities and cost structure are well developed and on a path towards commoditization.
- Focus on long-term improvement of adjusted EBITDA, in dollars and as a percentage of net sales—We define adjusted EBITDA as operating income adjusted for depreciation, amortization, stock-based compensation, major restructuring costs and certain other non-operating income and expense items. Key initiatives to reach our goals for EBITDA improvements include utilization of our Asian manufacturing locations, rationalizing our supply chain and continued leveraging of our infrastructure.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America and pursuant to the rules and regulations of the SEC. The preparation of these condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. We have identified the following as the items that require the most significant judgment and often involve complex estimation: revenue recognition, accounting for long-lived assets (including goodwill and intangible assets), inventory valuation, warranty reserves, stock-based compensation and accounting for income taxes. See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for our fiscal year ended September 27, 2014.

KEY PERFORMANCE INDICATORS

Below is a summary of some of the quantitative performance indicators (as defined below) that are evaluated by management to assess our financial performance. Some of the indicators are non-GAAP measures and should not be considered as an alternative to any other measure for determining operating performance or liquidity that is calculated in accordance with generally accepted accounting principles.

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	Three Months Ended December 27, 2014	December 28, 2013	Change	% Change
	(Dollars in thousands)			
Bookings	$162,524	$201,462	$(38,938)	(19.3)%
Book-to-bill ratio	0.81	1.04	(0.23)	(22.1)%
Net sales—Specialty Lasers and Systems	$145,091	$136,823	$8,268	6.0%
Net sales—Commercial Lasers and Components	$55,524	$56,733	$(1,209)	(2.1)%
Gross profit as a percentage of net sales—Specialty Lasers and Systems	44.0%	43.1%	0.9%	2.1%
Gross profit as a percentage of net sales—Commercial Lasers and Components	34.7%	34.1%	0.6%	1.8%
Research and development as a percentage of net sales	9.6%	10.8%	(1.2)%	(11.1)%
Income before income taxes	$23,624	$15,564	$8,060	51.8%
Net cash provided by operating activities	$31,051	$28,677	$2,374	8.3%
Days sales outstanding in receivables	58.5	53.8	4.7	8.7%
Annualized first quarter inventory turns	2.9	2.7	0.2	7.4%
Capital spending as a percentage of net sales	2.6%	3.5%	(0.9)%	(25.7)%
Net income as a percentage of net sales	8.7%	6.0%	2.7%	45.0%
Adjusted EBITDA as a percentage of net sales	18.7%	16.4%	2.3%	14.0%

Definitions and analysis of these performance indicators are as follows:

Bookings and Book-to-Bill Ratio

Bookings represent orders received during the current period for products and services to be provided pursuant to service contracts. While we generally have not experienced a significant rate of cancellation, bookings are generally cancelable by our customers without substantial penalty and, therefore, we cannot assure all bookings will be converted to net sales.

The book-to-bill ratio is calculated as quarterly bookings divided by quarterly net sales. This is an indication of the strength of our business but can sometimes be impacted by a single large order. A ratio of greater than 1.0 indicates that demand for our products is greater than what we supply in the quarter whereas a ratio of less than 1.0 indicates that demand for our products is less than what we supply in the quarter.

Bookings decreased 19.3% in the first quarter of fiscal 2015 compared to the same quarter one year ago, with decreases in all four markets led by a significant decrease in the OEM components and instrumentation market. Compared to the fourth quarter of fiscal 2014, bookings decreased 11.0% with decreases in the OEM components and instrumentation, materials processing and microelectronics markets partially offset by an increase in the scientific and government programs market. The book-to-bill ratio was 0.81 in the first quarter of fiscal 2015. Bookings in the first quarter of fiscal 2015 were lower due to the timing of orders placed by customers following large, multi-quarter bookings in the second half of fiscal 2014.

Microelectronics

Microelectronics bookings decreased 10% compared to the same quarter one year ago and decreased 7% from bookings in the fourth quarter of fiscal 2014. The book-to-bill ratio for the first quarter of fiscal 2015 was 0.73.

Flat panel display orders in the first quarter of fiscal 2015 decreased 36% both from orders in the first and fourth quarters of fiscal 2014 due to timing of order placement by customers as we had record bookings in the first three quarters of fiscal 2014, as well as reduced service bookings as customers manage their inventory levels. We expect continued fluctuations in order volumes on a quarterly basis. The drivers for flat panel display are unchanged and include higher smartphone share, larger screen sizes, lower display unit costs and the emergence of flexible displays. We believe these factors favor larger format annealing systems in excess of one meter. In addition, flexible displays have enabled wearable devices and may be poised for a role in automotive applications, such as in digital instrument panels. We shipped the first Triple Vyper™ Linebeam 1500

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system in the first quarter of fiscal 2015. We are planning to ship the remaining two systems in the order during fiscal 2015, pursuant to the customer's requested delivery schedule.
Orders in the advanced packaging (API) market increased 38% from orders in the first quarter of fiscal 2014 and 2% from orders in the fourth quarter of fiscal 2014. We expect bookings in the API market to increase over the course of fiscal 2015. We have broadened our customer set in microvia applications with greater emphasis on Chinese and Korean integrators. We believe this strategy will be beneficial in areas like flip-chip packaging. Additionally, the laser direct imaging market has posted good utilization numbers supporting service demand, slow capacity expansion and a shift to UV diode based imagers for the lower end of the market.
Orders from semiconductor capital equipment OEMs decreased 3% from the first quarter of fiscal 2014 but increased 35% from the fourth quarter of fiscal 2014. Industry trade groups project a record-setting year for capital expenditure investment. While we have seen a very modest increase in orders, we are starting to receive longer-term scheduling inquiries. These requests have historically correlated with an upturn in orders, but we believe it is too early to increase manufacturing levels.
Micro materials processing using short pulse lasers is the most dynamic part of microelectronics, with much of the business tied to consumer electronics, predominantly mobile devices, and is very project driven. We are actively engaged on a number of projects where our newer products like the Rapid NX, Avia NX, and Monaco offer process and performance advantages to the customer.
Materials Processing

Materials processing orders decreased 17% compared to the same quarter one year ago and decreased 22% from the fourth quarter of fiscal 2014. The book-to-bill ratio for the first quarter of fiscal 2015 was 0.83. First quarter of fiscal 2015 orders were lower following an exceptionally strong fourth quarter of fiscal 2014 as well as exhibiting some seasonal effects. Nonetheless, demand for our new J-Series CO_2 lasers was strong with high sequential and year-over-year growth. We also released a redesigned laser manufacturing workstation, the META™ 10C, equipped with a kilowatt CO_2 laser for the job shop market. The metal cutting market is very active. At the Fabtech tradeshow, some of the larger integrators were showing early homegrown fiber lasers or discussing plans to introduce them, driven by desires of differentiation and cost control. If successful, the trend will drive more top-down and bottom-up vertical integration. The additive manufacturing market is also showing positive trends which resulted in orders for CO_2 and UV lasers in polymer processes; this market also appears to be driving demand for mid-power (500W-1kW) fiber lasers and direct diode systems.

OEM Components and Instrumentation

OEM Components and Instrumentation orders decreased 41% compared to the same quarter one year ago and decreased 21% from the fourth quarter of fiscal 2014. The book-to-bill ratio for the first quarter of fiscal 2015 was 0.77.

Orders for medical OEM products were 65% lower in the first quarter of fiscal 2015 compared to the same quarter one year ago and 48% lower than orders in the fourth quarter of fiscal 2014. The decreases predominantly reflect the timing of large medical OEM orders, rather than easing of demand in medical applications as medical OEM customers report stable to increasing demand. We have also launched a new product for the cataract market that supports a broader procedure window which is relevant because research shows not all cataracts are treated similarly. The more stubborn variety of cataracts occurs in populations closer to the equator due to increased sun exposure. Ability to vary the laser performance, as our new product does, allows for process optimization.
Instrumentation orders decreased 27% compared to the first quarter of fiscal 2014 but increased 11% compared to the fourth quarter of fiscal 2014. The growth was skewed towards emerging customers in China, North America and Europe for cytometry and sequencing applications.
Scientific and Government Programs

Scientific and government programs orders decreased 9% compared to the same quarter one year ago but increased 2% from the fourth quarter of fiscal 2014. The book-to-bill for the first quarter of fiscal 2015 was 1.11.

While overall research funding remains flat, there were some notable market and regional factors during the first quarter of fiscal 2015. The increase in life sciences research in Asia is continuing and led to record Chameleon™ orders from the region. Combined with traditional physical sciences, Asia also produced record scientific orders, with activity especially strong in China and Korea. North America and Europe were in-line with expectations and Japan orders were up modestly.

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The biological imaging market continues to be the largest opportunity in the research market. Our Chameleon product line is a key contributor in this area and we recently released the newest version at the Neuroscience Conference in November 2014. The Chameleon Discovery is a different architect than earlier Ti:Sapphire-based Chameleons and is an Ytterbium laser with a tunable optical parametric oscillator (OPO) to provide very broad tuning with leading power performance. The combination allows investigators to target reagents and reactions not easily accessible with Ti:Sapphire. While we have offered OPOs with earlier versions of Chameleon, they were purchased from a vendor. The unit paired with Discovery is a Coherent-developed device, which should be beneficial to costs.

Net Sales

Net sales include sales of lasers, laser tools, related accessories and service. Net sales for the first fiscal quarter increased 6.0% in our SLS segment from the same quarter one year ago and decreased 2.1% in our CLC segment from the same quarter one year ago. For a description of the reasons for changes in net sales refer to the “Results of Operations” section of this quarterly report.

Gross Profit as a Percentage of Net Sales

Gross profit as a percentage of net sales (“gross profit percentage”) is calculated as gross profit for the period divided by net sales for the period. Gross profit percentage in the first quarter increased from 43.1% to 44.0% in our SLS segment and increased from 34.1% to 34.7% in our CLC segment from the same quarter one year ago. For a description of the reasons for changes in gross profit refer to the “Results of Operations” section of this quarterly report.

Research and Development as a Percentage of Net Sales

Research and development as a percentage of net sales (“R&D percentage”) is calculated as research and development expense for the period divided by net sales for the period. Management considers R&D percentage to be an important indicator in managing our business as investing in new technologies is a key to future growth. R&D percentage decreased to 9.6% from 10.8% in our first fiscal quarter compared to the same period one year ago. For a description of the reasons for changes in R&D spending refer to the “Results of Operations” section of this quarterly report.

Net Cash Provided by Operating Activities

Net cash provided by operating activities as reflected on our Condensed Consolidated Statements of Cash Flows primarily represents the excess of cash collected from billings to our customers and other receipts over cash paid to our vendors for expenses and inventory purchases to run our business. We believe that cash flows from operations is an important performance indicator because cash generation over the long term is essential to maintaining a healthy business and providing funds to help fuel growth. For a description of the reasons for changes in Net Cash Provided by Operating Activities refer to the “Liquidity and Capital Resources” section of this quarterly report.

Days Sales Outstanding in Receivables

We calculate days sales outstanding (“DSO”) in receivables as net receivables at the end of the period divided by net sales during the period and then multiplied by the number of days in the period, using 90 days for quarters. DSO in receivables indicates how well we are managing our collection of receivables, with lower DSO in receivables resulting in higher working capital availability. The more money we have tied up in receivables, the less money we have available for research and development, acquisitions, expansion, marketing and other activities to grow our business. Our DSO in receivables for the first quarter of fiscal 2015 increased 4.7 days from the same quarter one year ago primarily due to a higher concentration of sales in the last month of the fiscal quarter and timing of collections, particularly in Europe.

Annualized First Quarter Inventory Turns

We calculate annualized first quarter inventory turns as the cost of sales during the first quarter annualized and divided by net inventories at the end of the first quarter. This indicates how well we are managing our inventory levels, with higher inventory turns resulting in more working capital availability and a higher return on our investments in inventory. The more money we have tied up in inventory, the less money we have available for research and development, acquisitions, expansion, marketing and other activities to grow our business. Our annualized inventory turns for the first quarter of fiscal 2015 increased by 0.2 turns from the same quarter one year ago primarily due to the impact of lower levels of service inventory.

Capital Spending as a Percentage of Net Sales

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Capital spending as a percentage of net sales (“capital spending percentage”) is calculated as capital expenditures for the period divided by net sales for the period. Capital spending percentage indicates the extent to which we are expanding or improving our operations, including investments in technology and equipment. Management monitors capital spending levels as this assists management in measuring our cash flows, net of capital expenditures. Our capital spending percentage decreased to 2.6% from 3.5% for the first quarter of fiscal 2015 compared to the same period one year ago primarily due to lower purchases of production-related assets to support new product introductions.

Adjusted EBITDA as a Percentage of Net Sales

We define adjusted EBITDA as operating income adjusted for depreciation, amortization, stock-based compensation, major restructuring costs and certain other non-operating income and expense items. Key initiatives to reach our goals for EBITDA improvements include utilization of our Asian manufacturing locations, rationalizing our supply chain and continued leveraging of our infrastructure.

We utilize a number of different financial measures, both GAAP and non-GAAP, such as adjusted EBITDA as a percentage of net sales, in analyzing and assessing our overall business performance, for making operating decisions and for forecasting and planning future periods. We consider the use of non-GAAP financial measures helpful in assessing our current financial performance and ongoing operations. While we use non-GAAP financial measures as a tool to enhance our understanding of certain aspects of our financial performance, we do not consider these measures to be a substitute for, or superior to, the information provided by GAAP financial measures. We provide adjusted EBITDA in order to enhance investors' understanding of our ongoing operations. This measure is used by some investors when assessing our performance.

Below is the reconciliation of our net income as a percentage of net sales to our adjusted EBITDA as a percentage of net sales:

	Three Months Ended			
	December 27, 2014		December 28, 2013	
Net income as a percentage of net sales	8.7	%	6.0	%
Income tax expense	3.1	%	2.0	%
Interest and other (income) expense, net	0.6	%	1.1	%
Depreciation and amortization	4.1	%	4.8	%
Stock based compensation	2.2	%	2.5	%
Adjusted EBITDA as a percentage of net sales	18.7	%	16.4	%

SIGNIFICANT EVENTS

Stock Repurchases

On July 25, 2014, the Board of Directors authorized a buyback program whereby we were authorized to repurchase up to $25.0 million of our common stock from time to time through July 31, 2015. During the first quarter of fiscal 2015, we repurchased and retired 300,441 shares of outstanding common stock under this plan at an average price of $57.55 per share for a total of $17.3 million. During the month of January 2015, we repurchased and retired 133,673 shares of outstanding common stock under this plan at an average price of $57.66 per share for a total of $7.7 million, which concluded this program. For information regarding our new buyback program, please see Note 16 "Subsequent Event" to our condensed consolidated financial statements.

RESULTS OF OPERATIONS

CONSOLIDATED SUMMARY

The following table sets forth, for the periods indicated, the percentage of total net sales represented by the line items reflected in our condensed consolidated statements of operations:

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	Three Months Ended December 27, 2014		December 28, 2013	
Net sales	100.0	%	100.0	%
Cost of sales	59.0	%	59.9	%
Gross profit	41.0	%	40.1	%
Operating expenses:				
Research and development	9.6	%	10.8	%
Selling, general and administrative	19.0	%	20.6	%
Amortization of intangible assets	0.3	%	0.5	%
Total operating expenses	28.9	%	31.9	%
Income from operations	12.1	%	8.2	%
Other income (expense), net	(0.3	)%	(0.2	)%
Income before income taxes	11.8	%	8.0	%
Provision for income taxes	3.1	%	2.0	%
Net income	8.7	%	6.0	%

Net income for the first quarter of fiscal 2015 was $17.4 million ($0.69 per diluted share) including $4.0 million of after-tax stock-based compensation expense, $1.6 million after-tax amortization of intangible assets and a benefit of $1.1 million related to the renewal of the federal research and development tax credits for fiscal 2014. Net income for the first quarter of fiscal 2014 was $11.7 million ($0.47 per diluted share) including $3.5 million of after-tax stock-based compensation expense and $1.8 million amortization of intangible assets.

NET SALES

Market Application

The following tables set forth, for the periods indicated, the amount of net sales and their relative percentages of total net sales by market application (dollars in thousands):

	Three Months Ended December 27, 2014			December 28, 2013		
	Amount	Percentage of total net sales		Amount	Percentage of total net sales	
Consolidated:						
Microelectronics	$99,311	49.5	%	$92,303	47.7	%
OEM components and instrumentation	41,289	20.6	%	40,003	20.7	%
Materials processing	28,758	14.3	%	27,970	14.4	%
Scientific and government programs	31,257	15.6	%	33,280	17.2	%
Total	$200,615	100.0	%	$193,556	100.0	%

Net sales for the first quarter of fiscal 2015 increased by $7.1 million, or 4%, compared to the first quarter of fiscal 2014. Sales increases in the microelectronics, OEM components and instrumentation and materials processing markets were partially offset by decreases in the scientific and government programs market.

The increase in the microelectronics market of $7.0 million, or 8%, was due to higher shipments of flat panel display annealing systems net of lower flat panel display tube replacement sales partially offset by lower shipments for semiconductor and advanced packaging applications. The increase in the OEM components and instrumentation market of $1.3 million, or 3%, was due primarily to higher shipments for medical applications partially offset by

lower shipments for bio-instrumentation and military applications. Sales in the materials processing market increased $0.8 million, or 3%, primarily due to higher shipments of non-metal cutting and automotive manufacturing applications. Sales in the scientific and government programs market decreased $2.0 million, or 6%, primarily due to the timing of shipments to customers in Europe, particularly compared to the record level of shipments in the fourth quarter of fiscal 2014.

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Backlog represents orders which we expect to be shipped within 12 months and the current portion of service contracts. Orders used to compute backlog are generally cancelable and subject to rescheduling by our customers without substantial penalties. Historically, we have not experienced a significant rate of cancellation or rescheduling outside the 12 month period, though we cannot guarantee that the rate of cancellations or rescheduling will not increase in the future. We have a backlog of orders shippable within 12 months of $295.9 million at December 27, 2014, including a significant concentration in the flat panel display market (34%) for customers which are primarily in Asia.

The timing for shipments of our higher average selling price excimer products in the flat panel display market have historically fluctuated and are in the future expected to fluctuate from quarter-to-quarter due to customer scheduling, our ability to manufacture these products and/or availability of supplies. As a result, the timing to convert orders for these products to net sales will likely fluctuate from quarter-to-quarter.

Segments

We are organized into two reportable operating segments: Specialty Lasers and Systems (“SLS”) and Commercial Lasers and Components (“CLC”). SLS develops and manufactures configurable, advanced-performance products largely serving the microelectronics, scientific research and government programs and OEM components and instrumentation markets. CLC focuses on higher volume products that are offered in set configurations. CLC’s primary markets include materials processing, OEM components and instrumentation and microelectronics.

The following tables set forth, for the periods indicated, the amount of net sales and their relative percentages of total net sales by segment (dollars in thousands):

	Three Months Ended				
	December 27, 2014			December 28, 2013		
	Amount	Percentage of total net sales		Amount	Percentage of total net sales	
Consolidated:						
Specialty Lasers and Systems (SLS)	$145,091	72.3	%	$136,823	70.7	%
Commercial Lasers and Components (CLC)	55,524	27.7	%	56,733	29.3	%
Total	$200,615	100.0	%	$193,556	100.0	%

Net sales for the first quarter of fiscal 2015 increased by $7.1 million, or 4%, compared to the first quarter of fiscal 2014, with increases of $8.3 million, or 6%, in our SLS segment and decreases of $1.2 million, or 2%, in our CLC segment.

The increase in our SLS segment sales was primarily due to higher shipments of flat panel display annealing systems partially offset by lower shipments for semiconductor applications and scientific and government research programs. The decrease in our CLC segment sales was primarily due to lower advanced packaging application sales partially offset by higher medical application sales.

GROSS PROFIT

Consolidated

Our gross profit rate increased to 41.0% in the first quarter of fiscal 2015 from 40.1% in the first quarter of fiscal 2014. The increase in the gross profit rate was primarily due to lower other costs (0.9%) primarily due to improved

inventory management, lower duty and freight charges and lower warranty costs (0.8%) partially offset by unfavorable product margins (0.8%) resulting from a less favorable product mix, unfavorable yields and the impact of lower volumes in certain business units net of the favorable impact from foreign currency fluctuations.

Our gross profit rate has been and will continue to be affected by a variety of factors including market mix, pricing on volume orders, our ability to manufacture advanced and more complex products, manufacturing efficiencies, excess and obsolete inventory write-downs, warranty costs, amortization of intangibles, pricing by competitors or suppliers, new product introductions, production volume, customization and reconfiguration of systems, commodity prices and foreign currency fluctuations, particularly the recent weakening of the Euro and Japanese Yen.

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Specialty Lasers and Systems

The gross profit rate in our SLS segment increased to 44.0% in the first quarter of fiscal 2015 from 43.1% in the first quarter of fiscal 2014 primarily due to lower warranty costs (0.9%) due to fewer warranty events, lower other costs (0.6%) primarily due to improved inventory management and lower duty costs resulting from more favorable regional mix as well as lower intangibles amortization (0.1%). These improvements were partially offset by unfavorable product costs (0.7%) due to a less favorable product mix within the microelectronics and scientific markets partially offset by the favorable impact from foreign currency fluctuations.

Commercial Lasers and Components

The gross profit rate in our CLC segment increased to 34.7% in the first quarter of fiscal 2015 from 34.1% in the first quarter of fiscal 2014 primarily due to lower other costs (1.6%) from improved inventory management and lower warranty costs (0.6%) as a result of fewer warranty events. These improvements were partially offset by unfavorable product costs (1.6%) resulting from unfavorable yields and higher manufacturing costs primarily due to lower volumes in several business units.
OPERATING EXPENSES:

	Three Months Ended					
	December 27, 2014			December 28, 2013		
	Amount	Percentage of total net sales		Amount	Percentage of total net sales	
	(Dollars in thousands)					
Research and development	$19,173	9.6	%	$20,937	10.8	%
Selling, general and administrative	38,141	19.0	%	39,891	20.6	%
Amortization of intangible assets	696	0.3	%	934	0.5	%
Total operating expenses	$58,010	28.9	%	$61,762	31.9	%

Research and development

Research and development expenses decreased $1.8 million, or 8%, during the first fiscal quarter ended December 27, 2014 compared to the same quarter one year ago. The decrease was primarily due to $1.4 million lower project spending as a result of higher customer reimbursements for development projects and lower spending on various projects and the impact of foreign exchange rates ($0.4 million). These customer reimbursements are expected to be at a lower rate beginning in our second fiscal quarter. Other variable spending increases were offset by lower charges for increases in deferred compensation plan liabilities and lower stock-based compensation expense. On a segment basis as compared to the prior year period, SLS research and development spending decreased $1.0 million primarily due to lower project spending as a result of higher customer reimbursements for development projects and the impact of foreign exchange rates partially offset by higher other variable spending. CLC spending decreased $0.3 million primarily due to lower project spending. Corporate and other spending decreased $0.5 million primarily due to lower charges for increases in deferred compensation plan liabilities and lower stock-based compensation expense.

Selling, general and administrative

Selling, general and administrative expenses decreased $1.8 million or 4%, during the first fiscal quarter ended December 27, 2014 compared to the same quarter one year ago. The decrease was primarily due to $1.4 million lower charges for increases in deferred compensation plan liabilities with the related income for increases in deferred compensation plan assets recorded in other income (expense), the favorable impact of foreign exchange rates ($1.0 million), $0.4 million lower stock-based compensation expense and $0.3 million lower other net variable spending

partially offset by $1.3 million higher payroll spending primarily due to higher salaries, benefits and variable compensation. On a segment basis as compared to the prior year period, SLS segment expenses were flat with higher headcount related spending offset by the favorable impact of foreign exchange rates. CLC spending was flat with higher headcount related spending offset by lower other variable spending. Spending for Corporate and other decreased $1.8 million primarily due to lower charges for deferred compensation plan liabilities and lower stock-based compensation expense.

Amortization of intangible assets

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Amortization of intangible assets decreased $0.2 million during the first three months of fiscal 2015 compared to the same period one year ago primarily due to the completion of amortization in fiscal 2014 of certain intangibles from prior acquisitions.

OTHER INCOME (EXPENSE) — NET

Other income (expense), net, decreased $0.5 million during the three months ended December 27, 2014 compared to the same period one year ago. The decrease was primarily due to lower gains on our deferred compensation plan assets net of expenses ($1.5 million) partially offset by lower net foreign exchange losses ($1.0 million) due to less significant movement in certain foreign currencies in the first quarter of fiscal 2015 as compared to the first quarter of fiscal 2014.

INCOME TAXES

The effective tax rate on income before income taxes for the first quarter of fiscal 2015 of 26.2% was lower than the statutory rate of 35.0% primarily due to differences related to the benefit of income subject to foreign tax rates that are lower than U.S. statutory tax rates including Korea and Singapore tax exemptions, the benefit of foreign tax credits and the benefit of the federal research and development tax credits including renewal of the federal research and development tax credits for fiscal 2014. These amounts are partially offset by deemed dividend inclusions under the Subpart F tax rules, stock-based compensation not deductible for tax purposes and limitations on the deductibility of compensation under IRC Section 162(m).

The effective tax rate on income before income taxes for the first quarter of fiscal 2014 of 24.8% was lower than the statutory rate of 35.0% primarily due to differences related to the benefit of income subject to foreign tax rates that are lower than U.S. statutory tax rates, including Korea and Singapore tax exemptions and the benefit of foreign tax credits. These amounts are partially offset by deemed dividend inclusions under the Subpart F tax rules, stock-based compensation not deductible for tax purposes and limitations on the deductibility of compensation under IRC Section 162(m).

LIQUIDITY AND CAPITAL RESOURCES

At December 27, 2014, we had assets classified as cash and cash equivalents and short-term investments, in an aggregate amount of $323.0 million, compared to $318.3 million at September 27, 2014. At December 27, 2014, approximately $225.5 million of this cash and securities was held in certain of our foreign subsidiaries, $91.1 million of which was denominated in currencies other than the U.S. dollar, primarily the Euro. We currently have approximately $224.1 million of cash held by foreign subsidiaries where we intend to permanently reinvest our accumulated earnings in these entities and our current plans do not demonstrate a need for these funds to support our domestic operations. If, however, a portion of these funds were needed for and distributed to our operations in the United States, we would be subject to additional U.S. income taxes and foreign withholding taxes. The amount of the taxes due would depend on the amount and manner of repatriation, as well as the location from where the funds are repatriated. We actively monitor the third-party depository institutions that hold these assets, primarily focusing on the safety of principal and secondarily maximizing yield on these assets. We diversify our cash and cash equivalents and investments among various financial institutions, money market funds and sovereign debt in order to reduce our exposure should any one of these financial institutions or financial instruments fail or encounter difficulties. To date, we have not experienced any material loss or lack of access to our invested cash, cash equivalents or short-term investments. However, we can provide no assurances that access to our invested cash, cash equivalents or short-term investments will not be impacted by adverse conditions in the financial markets.

In the fourth quarter of fiscal 2014, we converted $62.7 million of cash and securities held in certain of our foreign subsidiaries to U.S. dollars and invested those funds within a European subsidiary whose functional currency is the U.S. dollar. At December 27, 2014, this subsidiary had $127.6 million of U.S. dollar denominated investments primarily in U.S. Treasury Securities, Corporate Notes and Commercial Paper. Accordingly, there is no translation expense arising from this entity holding U.S. dollar denominated investments. The converted funds are not intended to be repatriated to the U.S. and no U.S. tax was triggered on the transfer of these funds to the European subsidiary. See ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK below for more information about risks and trends related to foreign currencies.

Sources and Uses of Cash

Historically, our primary source of cash has been provided by operations. Other sources of cash in the past three fiscal years include proceeds received from the sale of our stock through our employee stock option and purchase plans. Our historical uses of cash have primarily been for the repurchase of our common stock, capital expenditures, acquisitions of businesses and technologies and the payment of a special cash dividend in the first quarter of fiscal 2013. Supplemental information pertaining

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to our historical sources and uses of cash is presented as follows and should be read in conjunction with our condensed consolidated statements of cash flows and the notes to our condensed consolidated financial statements:

	Three Months Ended	
	December 27, 2014	December 28, 2013
	(in thousands)	
Net cash provided by operating activities	$31,051	$28,677
Sales of shares under employee stock plans	3,437	6,810
Repurchase of common stock	(17,298)	—
Capital expenditures	(5,138)	(6,792)

Net cash provided by operating activities increased by $2.4 million for the first three months of fiscal 2015 compared to the same period one year ago. The increase in cash provided by operating activities was primarily due to higher net income, higher cash flows from timing of inventory purchases as well as net changes in deferred taxes and taxes payable partially offset by lower cash flows from timing of accounts receivable collections. We believe that our existing cash, cash equivalents and short term investments combined with cash to be provided by operating activities will be adequate to cover our working capital needs and planned capital expenditures for at least the next 12 months to the extent such items are known or are reasonably determinable based on current business and market conditions. However, we may elect to finance certain of our capital expenditure requirements through borrowings under our bank credit facilities or other sources of capital. We continue to follow our strategy to further strengthen our financial position by using available cash flow to fund operations.

We intend to continue pursuing acquisition opportunities at valuations we believe are reasonable based upon market conditions. However, we cannot accurately predict the timing, size and success of our acquisition efforts or our associated potential capital commitments. Furthermore, we cannot assure you that we will be able to acquire businesses on terms acceptable to us. We expect to fund future acquisitions through existing cash balances and cash flows from operations. If required, we will look for additional borrowings or consider the issuance of securities. The extent to which we will be willing or able to use our common stock to make acquisitions will depend on its market value at the time and the willingness of potential sellers to accept it as full or partial payment.

On July 25, 2014, the Board of Directors authorized a buyback program whereby we were authorized to repurchase up to $25.0 million of our common stock from time to time through July 31, 2015. During the first quarter of fiscal 2015, we repurchased and retired 300,441 shares of outstanding common stock at an average price of $57.55 per share for a total of $17.3 million, excluding expenses. During the month of January of fiscal 2015, we repurchased and retired 133,673 shares of outstanding common stock under this plan at an average price of $57.66 per share for a total of $7.7 million, excluding expenses, which concluded this plan.

On January 21, 2015, our Board of Directors authorized a buyback program authorizing the Company to repurchase up to $25 million of our common stock from time to time through January 31, 2016. See Note 16 "Subsequent Events".

Additional sources of cash available to us were domestic and international currency lines of credit and bank credit facilities totaling $63.7 million as of December 27, 2014, of which $60.7 million was unused and available. These unsecured credit facilities were used in Europe and Japan during the first three months of fiscal 2015. Our domestic line of credit consists of a $50.0 million unsecured revolving credit account with Union Bank of California, which expires on May 31, 2017 and is subject to covenants related to financial ratios and tangible net worth and we were in compliance with these covenants at December 27, 2014. No amounts were outstanding on our domestic line of credit and $3.0 million of the international currency lines has been used as guarantees as of December 27, 2014.

Our ratio of current assets to current liabilities was unchanged at 5.8:1 at both December 27, 2014 and September 27, 2014. Our cash and cash equivalents, short-term investments, working capital and debt obligations are as follows:

	December 27, 2014	September 27, 2014
	(in thousands)	
Cash and cash equivalents	$129,420	$91,217
Short-term investments	193,531	227,058
Working capital	557,033	563,736

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Contractual Obligations and Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements as defined under Regulation S-K of the Securities Act of 1933. Information regarding our long-term debt payments, operating lease payments, asset retirement obligations, purchase commitments with suppliers and purchase obligations is provided in Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of our Annual Report on Form 10-K for the fiscal year ended September 27, 2014. There have been no material changes in contractual obligations outside of the ordinary course of business since September 27, 2014. Information regarding our other financial commitments at December 27, 2014 is provided in the notes to the condensed consolidated financial statements in this filing.

Changes in Financial Condition

Cash provided by operating activities during the first three months of fiscal 2015 was $31.1 million, which included net income of $17.4 million, depreciation and amortization of $8.4 million, decreases in net deferred tax assets of $7.0 million, stock-based compensation expense of $4.4 million and $0.4 million other partially offset by cash used by operating assets and liabilities of $6.5 million. Cash provided by operating activities during the first three months of fiscal 2014 was $28.7 million, which included net income of $11.7 million, depreciation and amortization of $9.1 million, stock-based compensation expense of $4.9 million and cash provided by operating assets and liabilities of $4.6 million partially offset by $1.6 million other.

Cash provided by investing activities during the first three months of fiscal 2015 was $29.0 million, which included $33.6 million net sales of available-for-sale securities partially offset by $4.6 million net used to acquire property and equipment and improve buildings. Cash used in investing activities during the first three months of fiscal 2014 was $2.2 million, which included $6.6 million net used to acquire property and equipment and improve buildings partially offset by $4.4 million net sales of available-for-sale securities.

Cash used by financing activities during the first three months of fiscal 2015 was $19.1 million, which included $17.3 million repurchases of our common stock and $5.2 million net settlement of restricted stock partially offset by $3.4 million generated from our employee stock option and stock purchase plans. Cash used by financing activities during the first three months of fiscal 2014 was $0.9 million, which included $7.7 million net settlement of restricted stock partially offset by $6.8 million generated from our employee stock option and stock purchase plans.

Changes in exchange rates during the first three months of fiscal 2015 decreased our cash balances by $2.8 million. Changes in exchange rates during the first three months of fiscal 2014 increased our cash balances by $2.3 million.

RECENT ACCOUNTING STANDARDS

See Note 2. “Recent Accounting Standards” in the Notes to Condensed Consolidated Financial Statements for a full description of recent accounting pronouncements, including the respective dates of adoption or expected adoption and effects on our condensed consolidated financial position, results of operations and cash flows.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk disclosures

We are exposed to market risk related to changes in interest rates and foreign currency exchange rates. We do not use derivative financial instruments for speculative or trading purposes.

Interest rate sensitivity

A portion of our investment portfolio is composed of fixed income securities. These securities are subject to interest rate risk and will fall in value if market interest rates increase. If market interest rates were to increase immediately (whether due to changes in overall market rates or credit worthiness of the issuers of our individual securities) and uniformly by 10% from levels at December 27, 2014, the fair value of the portfolio, based on quoted market prices in active markets involving similar assets, would decline by an immaterial amount due to their short-term maturities. We have the ability to generally hold our fixed income investments until maturity and therefore we would not expect our operating results or cash flows to be affected to any significant degree by the effect of a sudden change in market interest rates on our securities portfolio. If necessary, we may sell short-term investments prior to maturity to meet our liquidity needs.

At December 27, 2014, the fair value of our available-for-sale debt securities was $193.5 million, all of which were classified as short-term investments. Gross unrealized gains and losses on available-for-sale debt securities were $1.1 million and $0.2 million, respectively, at December 27, 2014.

Foreign currency exchange risk

We maintain operations in various countries outside of the United States and have foreign subsidiaries that manufacture and sell our products in various global markets. The majority of our sales are transacted in U.S. dollars. However, we do generate revenues in other currencies, primarily the Euro, the Japanese Yen, the Korean Won and the Chinese Renminbi. Additionally we have operations in different countries around the world with costs incurred in other local currencies, such as British Pound Sterling, Singapore Dollars and Malaysian Ringgit. As a result, our earnings, cash flows and cash balances are exposed to fluctuations in foreign currency exchange rates. For example, we have significant manufacturing operations in Europe so that a weakening Euro is advantageous to the Company’s financial results. We attempt to limit these exposures through financial market instruments. We utilize derivative instruments, primarily forward contracts with maturities of three months or less, to manage our exposure associated with anticipated cash flows and net asset and liability positions denominated in foreign currencies. Gains and losses on the forward contracts are mitigated by gains and losses on the underlying instruments. We do not use derivative financial instruments for trading purposes.

On occasion, we enter into currency forward exchange contracts to hedge specific anticipated foreign currency denominated transactions generally expected to occur within the next 12 months. These cash flow hedges are designated for hedge accounting treatment and gains and losses on these contracts are recorded in accumulated other comprehensive income in stockholder's equity and reclassified into earnings at the time that the related transactions being hedged are recognized in earnings. See Note 4 "Derivative Instruments and Hedging Activities".

We do not anticipate any material adverse effect on our condensed consolidated financial position, results of operations or cash flows resulting from the use of these instruments. There can be no assurance that these strategies will be effective or that transaction losses can be minimized or forecasted accurately. While we model currency valuations and fluctuations, these may not ultimately be accurate. If a financial counterparty to any of our hedging arrangements experiences financial difficulties or is otherwise unable to honor the terms of the foreign currency

hedge, we may experience material financial losses. In the current economic environment, the risk of failure of a financial party remains high.

At December 27, 2014, approximately $225.5 million of our cash, cash equivalents and short-term investments were held outside the U.S. in certain of our foreign operations, $91.1 million of which was denominated in currencies other than the U.S. dollar.

A hypothetical 10% change in foreign currency rates on our forward contracts would not have a material impact on our results of operations, cash flows or financial position.

The following table provides information about our foreign exchange forward contracts at December 27, 2014. The table presents the weighted average contractual foreign currency exchange rates, the value of the contracts in U.S. dollars at the

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contract exchange rate as of the contract maturity date and fair value. The U.S. fair value represents the fair value of the contracts valued at December 27, 2014 rates.

Forward contracts to sell (buy) foreign currencies for U.S. dollars (in thousands, except contract rates):

	Average Contract Rate	U.S. Notional Contract Value	U.S. Fair Value
Non-Designated - For US Dollars:			
Euro	1.2612	$(45,489)	$1,252
Japanese Yen	117.5378	$896	$(19)
British Pound	1.5666	$4,809	$(14)
Korean Won	1,113.8100	$4,235	$68
Chinese Renminbi	6.1500	$9,035	$57
Singapore Dollar	1.3062	$(2,445)	$25
Malaysian Ringgit	3.4700	$638	$(4)
Non-Designated - For Euros:			
Japanese Yen	112.7346	$7,166	$(349)
Designated - For US Dollars:			
Euro	1.3935	$(5,574)	$660
Designated - For Euros:			
Japanese Yen	111.2099	$5,859	$(360)

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ITEM 4. CONTROLS AND PROCEDURES

Management's Evaluation of Disclosure Controls and Procedures

We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as of December 27, 2014 ("Evaluation Date"). The controls evaluation was conducted under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective in providing reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934, as amended, is (i) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended December 27, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations over Internal Control

Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles ("GAAP"). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Our internal control over financial reporting includes those policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our internal controls will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of internal controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Also, any evaluation of the effectiveness of controls in future periods are subject to the risk that those internal controls may become inadequate because of changes in business conditions, or that the degree of compliance with the policies or

procedures may deteriorate.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information with respect to this item may be found in Note 10 to our condensed consolidated financial statements in Part I, Item 1 of this report and is incorporated herein by reference.

ITEM 1A. RISK FACTORS

You should carefully consider the followings risks when considering an investment in our Common Stock. These risks could materially affect our business, results of operations or financial condition, cause the trading price of our Common Stock to decline materially or cause our actual results to differ materially from those expected or those expressed in any forward-looking statements made by us. These risks are not exclusive, and additional risks to which we are subject include, but are not limited to, the factors mentioned under “Forward-Looking Statements” and the risk of our businesses described elsewhere in this annual report. Additionally, these risks and uncertainties described herein are not the only ones facing us. Other events that we do not currently anticipate or that we currently deem immaterial also may affect our business, results of operations or financial condition.

BUSINESS ENVIRONMENT AND INDUSTRY TRENDS

Our operating results, including net sales, net income (loss) and adjusted EBITDA in dollars and as a percentage of net sales, as well as our stock price have varied in the past, and our future operating results will continue to be subject to quarterly and annual fluctuations based upon numerous factors, including those discussed in this Item 1A and throughout this report. Our stock price will continue to be subject to daily variations as well. Our future operating results and stock price may not follow any past trends or meet our guidance and expectations.

Our net sales and operating results, such as adjusted EBITDA percentage, net income (loss) and operating expenses, and our stock price have varied in the past and may vary significantly from quarter to quarter and from year to year in the future. We believe a number of factors, many of which are outside of our control, could cause these variations and make them difficult to predict, including:

- general economic uncertainties in the macroeconomic and local economies facing us, our customers and the markets we serve;
- fluctuations in demand for our products or downturns in the industries that we serve;
- the ability of our suppliers, both internal and external, to produce and deliver components and parts, including sole or limited source components, in a timely manner, in the quantity, quality and prices desired;
- the timing of receipt and conversion of bookings to net sales;
- the concentration of a significant amount of our backlog, and resultant net sales, with a few customers;
- cancellation of customer orders and rescheduling of shipments;
- fluctuations in our product mix;
- the ability of our customers' other suppliers to provide sufficient material to support our customers' products;

- currency fluctuations and stability, in particular the Euro, the Japanese Yen, the Korean Won, the Chinese Renminbi and the US dollar as compared to other currencies;

- commodity pricing;

- introductions of new products and product enhancements by our competitors, entry of new competitors into our markets, pricing pressures and other competitive factors;

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- our ability to develop, introduce, manufacture and ship new and enhanced products in a timely manner without defects;
- our ability to manage our capacity and that of our suppliers;
- our reliance on contract manufacturing;
- the rate of market acceptance of our new products;
- the ability of our customers to pay for our products;
- expenses associated with acquisition-related activities;
- seasonal sales trends;
- access to applicable credit markets by us, our customers and their end customers;
- delays or reductions in customer purchases of our products in anticipation of the introduction of new and enhanced products by us or our competitors;
- our ability to control expenses;
- the level of capital spending of our customers;
- potential excess and/or obsolescence of our inventory;
- costs and timing of adhering to current and developing governmental regulations and reviews relating to our products and business;
- costs related to acquisitions of technology or businesses;
- impairment of goodwill, intangible assets and other long-lived assets;
- our ability to meet our expectations and forecasts and those of public market analysts and investors;
- the availability of research funding by governments with regard to our customers in the scientific business, such as universities;
- continued government spending on defense-related projects where we are a subcontractor;
- maintenance of supply relating to products sold to the government on terms which we would prefer not to accept;
- changes in policy, interpretations, or challenges to the allowability of costs incurred under government cost accounting standards;
- damage to our reputation as a result of coverage in social media, Internet blogs or other media outlets;
- managing our and other parties' compliance with contracts in multiple languages and jurisdictions;

- managing our internal and third party sales representatives and distributors, including compliance with all applicable laws;
- impact of government economic policies on macroeconomic conditions;
- costs and expenses from litigation;
- costs associated with designing around or payment of licensing fees associated with issued patents in our fields of business;

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- government support of alternative energy industries, such as solar;
- the future impact of legislation, rulemaking, and changes in accounting, tax, defense procurement, or export policies; and
- distraction of management related to acquisition or divestment activities.

In addition, we often recognize a substantial portion of our sales in the last month of our fiscal quarters. Our expenses for any given quarter are typically based on expected sales and if sales are below expectations in any given quarter, the adverse impact of the shortfall on our operating results may be magnified by our inability to adjust spending quickly enough to compensate for the shortfall. We also base our manufacturing on our forecasted product mix for the quarter. If the actual product mix varies significantly from our forecast, we may not be able to fill some orders during that quarter, which would result in delays in the shipment of our products. Accordingly, variations in timing of sales, particularly for our higher priced, higher margin products, can cause significant fluctuations in quarterly operating results.

Due to these and other factors, such as varying product mix, we believe that quarter-to-quarter and year-to-year comparisons of our historical operating results may not be meaningful. You should not rely on our results for any quarter or year as an indication of our future performance. Our operating results in future quarters and years may be below public market analysts' or investors' expectations, which would likely cause the price of our stock to fall. In addition, over the past several years, the stock market has experienced extreme price and volume fluctuations that have affected the stock prices of many technology companies both in and outside our industry. There has not always been a direct correlation between this volatility and the performance of particular companies subject to these stock price fluctuations. Further, over the last twelve months, equity markets around the world have significantly fluctuated across most sectors. These factors, as well as general economic and political conditions or investors' concerns regarding the credibility of corporate financial statements, may have a material adverse effect on the market price of our stock in the future.

We depend on sole source or limited source suppliers, both internal and external, for some of our key components and materials, including exotic materials, certain cutting-edge optics and crystals, in our products, which make us susceptible to supply shortages or price fluctuations that could adversely affect our business.

We currently purchase several key components and materials used in the manufacture of our products from sole source or limited source suppliers, both internal and external. Our failure to timely receive these key components and materials, such as the large optics used in our flat panel display manufacturing applications, could cause delays in the shipment of our products. Some of these suppliers are relatively small private companies that may discontinue their operations at any time and which may be particularly susceptible to prevailing economic conditions. Some of our suppliers are located in regions which may be susceptible to natural disasters, such as the flooding in Thailand and the earthquake, tsunami and resulting nuclear disaster in Japan and severe flooding and power loss in the Eastern part of the United States in recent years. We typically purchase our components and materials through purchase orders or agreed upon terms and conditions and we do not have guaranteed supply arrangements with many of these suppliers. Some of our products, particularly in the flat panel display industry, require designs and specifications which are at the cutting-edge of available technologies. Our and our customers' designs and specifications frequently change to meet rapidly evolving market demands. Accordingly certain of our products require components and supplies which may be technologically difficult and unpredictable to manufacture. These characteristics further pressure the timely delivery of such components. We may fail to obtain these supplies in a timely manner in the future. We may experience difficulty identifying alternative sources of supply for certain components used in our products and may have to incur expenses and management distraction in assisting our current and future suppliers to meet our and our customers' technical requirements. We would experience further delays while identifying, evaluating and testing the

products of these potential alternative suppliers. Furthermore, financial or other difficulties faced by these suppliers or significant changes in demand for these components or materials could limit their availability. We continue to consolidate our supply base and move supplier locations. When we transition locations we may increase our inventory of such products as a “safety stock” during the transition, which may cause the amount of inventory reflected on our balance sheet to increase. Additionally, many of our customers rely on sole source suppliers. In the event of a disruption of our customers' supply chain, orders from our customers could decrease or be delayed.

Any interruption or delay in the supply of any of these components or materials, or the inability to obtain these components and materials from alternate sources at acceptable prices and within a reasonable amount of time, or our failure to properly manage these moves, would impair our ability to meet scheduled product deliveries to our customers and could cause customers to cancel orders. We have historically relied exclusively on our own production capability to manufacture certain strategic components, crystals, semiconductor lasers, lasers and laser-based systems. Because we manufacture, package and test these components, products and systems at our own facilities, and such components, products and systems are not readily available

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from other sources, any interruption in manufacturing would adversely affect our business. In addition, our failure to achieve adequate manufacturing yields of these items at our manufacturing facilities may materially and adversely affect our operating results and financial condition.

We participate in the microelectronics market, which requires significant research and development expenses to develop and maintain products and a failure to achieve market acceptance for our products could have a significant negative impact on our business and results of operations.

The microelectronics market is characterized by rapid technological change, frequent product introductions, the volatility of product supply and demand, changing customer requirements and evolving industry standards. The nature of this market requires significant research and development expenses to participate, with substantial resources invested in advance of material sales of our products to our customers in this market. Additionally, our product offerings may become obsolete given the frequent introduction of alternative technologies. In the event either our customers' or our products fail to gain market acceptance, or the microelectronics market fails to grow, it would likely have a significant negative effect on our business and results of operations.

We participate in the flat panel display market, which has a relatively limited number of end customer manufacturers. Our backlog, timing of net sales and results of operations could be negatively impacted in the event our customers reschedule orders.

In the flat panel display market, there are a relatively limited number of manufacturers who are the end customers for our annealing products. In each of our last three fiscal years, Advanced Process Systems Corporation, an integrator in the flat panel display market, has contributed more than 10% of our revenue. Given macroeconomic conditions, varying consumer demand and technical process limitations at manufacturers, our customers may seek to reschedule or cancel orders. Challenges in meeting evolving technological requirements for these complex products by us and our suppliers could also result in delays in shipments, rescheduled or canceled orders by our customers. This could negatively impact our backlog, timing of net sales and results of operations.

As of December 27, 2014, flat panel display systems represented 34% of our backlog. Given our backlog includes these higher average selling price flat panel display systems, any delays or cancellation of shipments could have a material adverse effect on our financial results.

Some of our laser systems are complex in design and may contain defects that are not detected until deployed by our customers, which could increase our costs and reduce our net sales.

Lasers and laser systems are inherently complex in design and require ongoing regular maintenance. The manufacture of our lasers, laser products and systems involves a highly complex and precise process. As a result of the technological complexity of our products, in particular the flat panel annealing systems, changes in our or our suppliers' manufacturing processes or the inadvertent use of defective materials by us or our suppliers could result in a material adverse effect on our ability to achieve acceptable manufacturing yields and product reliability. To the extent that we do not achieve and maintain our projected yields or product reliability, our business, operating results, financial condition and customer relationships would be adversely affected. We provide warranties on a majority of our product sales, and reserves for estimated warranty costs are recorded during the period of sale. The determination of such reserves requires us to make estimates of failure rates and expected costs to repair or replace the products under warranty. We typically establish warranty reserves based on historical warranty costs for each product line. If actual return rates and/or repair and replacement costs differ significantly from our estimates, adjustments to cost of sales may be required in future periods which could have an adverse effect on our results of operations.

Our customers may discover defects in our products after the products have been fully deployed and operated under the end user's peak stress conditions. In addition, some of our products are combined with products from other vendors, which may contain defects. As a result, should problems occur, it may be difficult to identify the source of the problem. If we are unable to identify and fix defects or other problems, we could experience, among other things:

- loss of customers or orders;
- increased costs of product returns and warranty expenses;
- damage to our brand reputation;
- failure to attract new customers or achieve market acceptance;

- diversion of development and engineering resources; and
- legal actions by our customers and/or their end users.

The occurrence of any one or more of the foregoing factors could seriously harm our business, financial condition and results of operations.

Continued volatility in the semiconductor manufacturing and advanced packaging markets could adversely affect our business, financial condition and results of operations.

A portion of our net sales in the microelectronics market depends on the demand for our products by semiconductor equipment and advanced packaging applications companies. These markets have historically been characterized by sudden and severe cyclical variations in product supply and demand, which have often severely affected the demand for semiconductor manufacturing equipment, including laser-based tools and systems. The timing, severity and duration of these market cycles are difficult to predict, and we may not be able to respond effectively to these cycles. The continuing uncertainty in these markets severely limits our ability to predict our business prospects or financial results in these markets.

During industry downturns, our net sales from these markets may decline suddenly and significantly. Our ability to rapidly and effectively reduce our cost structure in response to such downturns is limited by the fixed nature of many of our expenses in the near term and by our need to continue our investment in next-generation product technology and to support and service our products. In addition, due to the relatively long manufacturing lead times for some of the systems and subsystems we sell to these markets, we may incur expenditures or purchase raw materials or components for products we cannot sell. Accordingly, downturns in the semiconductor capital equipment market may materially harm our operating results. Conversely, when upturns in these markets occur, we must be able to rapidly and effectively increase our manufacturing capacity to meet increases in customer demand that may be extremely rapid, and if we fail to do so we may lose business to our competitors and our relationships with our customers may be harmed.

We are exposed to risks associated with worldwide economic conditions and related uncertainties which could negatively impact demand for our products and results of operations.

Volatility and disruption in the capital and credit markets, depressed consumer confidence, government economic policies, negative economic conditions, volatile corporate profits and reduced capital spending could negatively impact demand for our products. In particular, it is difficult to develop and implement strategy, sustainable business models and efficient operations, as well as effectively manage supply chain relationships in the face of such conditions, including uncertainty regarding the ability of some of our suppliers to continue operations and provide us with uninterrupted supply flow. Our ability to maintain our research and development investments in our broad product offerings may be adversely impacted in the event that our sales decline and do not increase in the future. Spending and the timing thereof by consumers and businesses have a significant impact on our results and, where such spending is delayed or canceled, it could have a material negative impact on our operating results. The current global economic conditions remain uncertain and challenging. Weakness in our end markets could negatively impact our net sales, gross margin and operating expenses, and consequently have a material adverse effect on our business, financial condition and results of operations.

Recent uncertainty in global fiscal policy has likely had an adverse impact on global financial markets and overall economic activity. Should this uncertain financial policy recur, it would likely negatively impact global economic

activity. Any weakness in global economies would also likely have negative repercussions on U.S. and global credit and financial markets, and further exacerbate sovereign debt concerns in the European Union. All of these factors would likely adversely impact the global demand for our products and the performance of our investments, and would likely have a material adverse effect on our business, results of operations and financial condition.

The financial turmoil which recently affected the banking system and financial markets continues to negatively impact financial institutions and has resulted in tighter credit markets, and lower levels of liquidity in some financial markets. There could be a number of follow-on effects from the tightened credit environment on our business, including the insolvency of key suppliers or their inability to obtain credit to finance development and/or manufacture products resulting in product delays; inability of customers to obtain credit to finance purchases of our products and/or customer insolvencies; and failure of financial institutions negatively impacting our treasury functions. In the event our customers are unable to obtain credit or otherwise pay for our shipped products it could significantly impact our ability to collect on our outstanding accounts receivable. Other income and expense also could vary materially from expectations depending on gains or losses realized on the sale or exchange of financial instruments; impairment charges resulting from revaluations of debt and equity securities and other investments;

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interest rates; cash balances; and changes in fair value of derivative instruments. Volatility in the financial markets and any overall economic uncertainty increase the risk that the actual amounts realized in the future on our financial instruments could differ significantly from the fair values currently assigned to them. Uncertainty about current global economic conditions could also continue to increase the volatility of our stock price.

In addition, political and social turmoil related to international conflicts, terrorist acts and civil unrest may put further pressure on economic conditions in the United States and abroad. Unstable economic, political and social conditions make it difficult for our customers, our suppliers and us to accurately forecast and plan future business activities. If such conditions persist, our business, financial condition and results of operations could suffer. Additionally, unstable economic conditions can provide significant pressures and burdens on individuals, which could cause them to engage in inappropriate business conduct.

Our cash and cash equivalents and short-term investments are managed through various banks around the world and volatility in the capital and credit market conditions could cause financial institutions to fail or materially harm service levels provided by such banks, both of which could have an adverse impact on our ability to timely access funds.

World capital and credit markets have been and may continue to experience volatility and disruption. In some cases, the markets have exerted downward pressure on stock prices and credit capacity for certain issuers, as well as pressured the solvency of some financial institutions. These financial institutions, including banks, have had difficulty timely performing regular services and in some cases have failed or otherwise been largely taken over by governments. We maintain our cash, cash equivalents and short-term investments with a number of financial institutions around the world. Should some or all of these financial institutions fail or otherwise be unable to timely perform requested services, we would likely have a limited ability to timely access our cash deposited with such institutions, or, in extreme circumstances the failure of such institutions could cause us to be unable to access cash for the foreseeable future. If we are unable to quickly access our funds when we need them, we may need to increase the use of our existing credit lines or access more expensive credit, if available. If we are unable to access our cash or if we access existing or additional credit or are unable to access additional credit, it could have a negative impact on our operations, including our reported net income.

We are exposed to credit risk and fluctuations in the market values of our investment portfolio.

Although we have not recognized any material losses on our cash, cash equivalents and short-term investments, future declines in their market values could have a material adverse effect on our financial condition and operating results. Given the global nature of our business, we have investments both domestically and internationally. There has recently been growing pressure on the creditworthiness of sovereign nations, particularly in Europe where a significant portion of our cash, cash equivalents and short-term investments are invested, which results in corresponding pressure on the valuation of the securities issued by such nations. Additionally, our overall investment portfolio is often concentrated in certificates of deposit and money market funds. We maintain a mix of government-issued securities. Credit ratings and pricing of these investments can be negatively impacted by liquidity, credit deterioration or losses, financial results, or other factors. Additionally, liquidity issues or political actions by sovereign nations could result in decreased values for our investments in certain government securities. As a result, the value or liquidity of our cash, cash equivalents and short-term investments could decline or become materially impaired, which could have a material adverse effect on our financial condition and operating results. See “Item 3. Quantitative and Qualitative Disclosures about Market Risk.”

Our future success depends on our ability to increase our sales volumes and decrease our costs to offset potential declines in the average selling prices (“ASPs”) of our products and, if we are unable to realize greater sales volumes and lower costs, our operating results may suffer.

Our ability to increase our sales volume and our future success depends on the continued growth of the markets for lasers, laser systems and related accessories, as well as our ability to identify in advance emerging markets for laser-based systems. We cannot assure you that we will be able to successfully identify on a timely basis new high-growth markets in the future. Moreover, we cannot assure you that new markets will develop for our products or our customers' products, or that our technology or pricing will enable such markets to develop. Future demand for our products is uncertain and will depend to a great degree on continued technological development and the introduction of new or enhanced products. If this does not continue, sales of our products may decline and our business will be harmed.

We have in the past experienced decreases in the ASPs of some of our products. As competing products become more widely available, the ASPs of our products may decrease. If we are unable to offset any decrease in our ASPs by increasing our sales volumes, our net sales will decline. In addition, to maintain our gross margins, we must continue to reduce the cost of manufacturing our products while maintaining their high quality. From time to time, our products, like many complex technological products, may fail in greater frequency than anticipated. This can lead to further charges, which can result in

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higher costs, lower gross margins and lower operating results. Furthermore, as ASPs of our current products decline, we must develop and introduce new products and product enhancements with higher margins. If we cannot maintain our gross margins, our operating results could be seriously harmed, particularly if the ASPs of our products decrease significantly.

Our future success depends on our ability to develop and successfully introduce new and enhanced products that meet the needs of our customers.

Our current products address a broad range of commercial and scientific research applications in the photonics markets. We cannot assure you that the market for these applications will continue to generate significant or consistent demand for our products. Demand for our products could be significantly diminished by disrupting technologies or products that replace them or render them obsolete. Furthermore, the new and enhanced products in certain markets generally continue to be smaller in size and have lower ASPs, and therefore, we have to sell more units to maintain revenue levels. Accordingly, we must continue to invest in research and development in order to develop competitive products.

Our future success depends on our ability to anticipate our customers' needs and develop products that address those needs. Introduction of new products and product enhancements will require that we effectively transfer production processes from research and development to manufacturing and coordinate our efforts with those of our suppliers to achieve volume production rapidly. If we fail to transfer production processes effectively, develop product enhancements or introduce new products in sufficient quantities to meet the needs of our customers as scheduled, our net sales may be reduced and our business may be harmed.

We face risks associated with our foreign operations and sales that could harm our financial condition and results of operations.

For the three months ended December 27, 2014, 73% of our net sales were derived from customers outside of the United States. For fiscal 2014, fiscal 2013 and fiscal 2012, 74%, 77% and 76%, respectively, of our net sales were derived from customers outside of the United States. We anticipate that foreign sales, particularly in Asia, will continue to account for a significant portion of our net sales in the foreseeable future.

A global economic slowdown or a natural disaster could have a negative effect on various foreign markets in which we operate, such as the earthquake, tsunami and resulting nuclear disaster in Japan and the flooding in Thailand in recent years. Such a slowdown may cause us to reduce our presence in certain countries, which may negatively affect the overall level of business in such countries. Our foreign sales are primarily through our direct sales force. Additionally, some foreign sales are made through foreign distributors and resellers. Our foreign operations and sales are subject to a number of risks, including:

- longer accounts receivable collection periods;

- the impact of recessions and other economic conditions in economies outside the United States;

- unexpected changes in regulatory requirements;

- certification requirements;

- environmental regulations;

- reduced protection for intellectual property rights in some countries;

- potentially adverse tax consequences;
- political and economic instability;
- import/export regulations, tariffs and trade barriers;
- compliance with applicable United States and foreign anti-corruption laws;
- cultural and management differences;
- reliance in some jurisdictions on third party sales channel partners;

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- preference for locally produced products; and

- shipping and other logistics complications.

Our business could also be impacted by international conflicts, terrorist and military activity, civil unrest and pandemic illness which could cause a slowdown in customer orders or cause customer order cancellations.

We are also subject to the risks of fluctuating foreign currency exchange rates, which could materially adversely affect the sales price of our products in foreign markets, as well as the costs and expenses of our foreign subsidiaries. While we use forward exchange contracts and other risk management techniques to hedge our foreign currency exposure, we remain exposed to the economic risks of foreign currency fluctuations.

We may not be able to protect our proprietary technology which could adversely affect our competitive advantage.

Maintenance of intellectual property rights and the protection thereof is important to our business. We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. Our patent applications may not be approved, any patents that may be issued may not sufficiently protect our intellectual property and any issued patents may be challenged by third parties. Other parties may independently develop similar or competing technology or design around any patents that may be issued to us. We cannot be certain that the steps we have taken will prevent the misappropriation of our intellectual property, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. Further, we may be required to enforce our intellectual property or other proprietary rights through litigation, which, regardless of success, could result in substantial costs and diversion of management's attention. Additionally, there may be existing patents of which we are unaware that could be pertinent to our business and it is not possible for us to know whether there are patent applications pending that our products might infringe upon since these applications are often not publicly available until a patent is issued or published.

We may, in the future, be subject to claims or litigation from third parties, for claims of infringement of their proprietary rights or to determine the scope and validity of our proprietary rights or the proprietary rights of competitors or other rights holders. These claims could result in costly litigation and the diversion of our technical and management personnel. Adverse resolution of litigation may harm our operating results or financial condition.

In recent years, there has been significant litigation in the United States and around the world involving patents and other intellectual property rights. This has been seen in our industry, for example in the recently concluded patent-related litigation between IMRA America, Inc. ("Imra") and IPG Photonics Corporation and in Imra's recently brought litigation against two of our German subsidiaries. From time to time, like many other technology companies, we have received communications from other parties asserting the existence of patent rights, copyrights, trademark rights or other intellectual property rights which such third parties believe may cover certain of our products, processes, technologies or information. In the future, we may be a party to litigation to protect our intellectual property or as a result of an alleged infringement of others' intellectual property whether through direct claims or by way of indemnification claims of our customers, as, in some cases, we contractually agree to indemnify our customers against third-party infringement claims relating to our products. These claims and any resulting lawsuit, if successful, could subject us to significant liability for damages or invalidation of our proprietary rights. These lawsuits, regardless of their success, would likely be time-consuming and expensive to resolve and would divert management time and attention. Any potential intellectual property litigation could also force us to do one or more of the following:

- stop manufacturing, selling or using our products that use the infringed intellectual property;

-

obtain from the owner of the infringed intellectual property right a license to sell or use the relevant technology, although such license may not be available on reasonable terms, or at all; or

- redesign the products that use the technology.

If we are forced to take any of these actions or are otherwise a party to lawsuits of this nature, we may incur significant losses and our business may be seriously harmed. We do not have insurance to cover potential claims of this type.

If our goodwill or intangible assets become impaired, we may be required to record a significant charge to earnings.

Under accounting principles generally accepted in the United States, we review our intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Goodwill is required to be tested for impairment at least annually. Factors that may be considered in determining whether a change in circumstances indicating that

the carrying value of our goodwill or other intangible assets may not be recoverable include declines in our stock price and market capitalization or future cash flows projections. We recorded a charge during the fourth quarter of fiscal 2012 related to the impairment of intangibles in our SLS operating segment relating to the decision to discontinue the legacy Hypertronics products. A decline in our stock price, or any other adverse change in market conditions, particularly if such change has the effect of changing one of the critical assumptions or estimates we used to calculate the estimated fair value of our reporting units, could result in a change to the estimation of fair value that could result in an impairment charge. Any such material charges, whether related to goodwill or purchased intangible assets, may have a material negative impact on our financial and operating results.

We depend on skilled personnel to operate our business effectively in a rapidly changing market, and if we are unable to retain existing or hire additional personnel when needed, our ability to develop and sell our products could be harmed.

Our ability to continue to attract and retain highly skilled personnel will be a critical factor in determining whether we will be successful in the future. Recruiting and retaining highly skilled personnel in certain functions continues to be difficult. At certain locations where we operate, the cost of living is extremely high and it may be difficult to retain key employees and management at a reasonable cost. We may not be successful in attracting, assimilating or retaining qualified personnel to fulfill our current or future needs. Our failure to attract additional employees and retain our existing employees could adversely affect our growth and our business.

Our future success depends upon the continued services of our executive officers and other key engineering, sales, marketing, manufacturing and support personnel, any of whom may leave, which could harm our business and our results of operations.

The long sales cycles for our products may cause us to incur significant expenses without offsetting net sales.

Customers often view the purchase of our products as a significant and strategic decision. As a result, customers typically expend significant effort in evaluating, testing and qualifying our products before making a decision to purchase them, resulting in a lengthy initial sales cycle. While our customers are evaluating our products and before they place an order with us, we may incur substantial sales and marketing and research and development expenses to customize our products to the customers' needs. We may also expend significant management efforts, increase manufacturing capacity and order long lead-time components or materials prior to receiving an order. Even after this evaluation process, a potential customer may not purchase our products. As a result, these long sales cycles may cause us to incur significant expenses without ever receiving net sales to offset such expenses.

The markets in which we sell our products are intensely competitive and increased competition could cause reduced sales levels, reduced gross margins or the loss of market share.

Competition in the various photonics markets in which we provide products is very intense. We compete against a number of large public and private companies, including CVI Melles Griot, GSI Group, Inc., IPG Photonics Corporation, JDS Uniphase Corporation, Newport Corporation, Rofin-Sinar Technologies, Inc., and Trumpf GmbH, as well as other smaller companies. Some of our competitors are large companies that have significant financial, technical, marketing and other resources. These competitors may be able to devote greater resources than we can to the development, promotion, sale and support of their products. Some of our competitors are much better positioned than we are to acquire other companies in order to gain new technologies or products that may displace our product lines. Any of these acquisitions could give our competitors a strategic advantage. Any business combinations or mergers among our competitors, forming larger companies with greater resources, could result in increased competition, price reductions, reduced margins or loss of market share, any of which could materially and adversely affect our business, results of operations and financial condition.

Additional competitors may enter the markets in which we serve, both foreign and domestic, and we are likely to compete with new companies in the future. We may encounter potential customers that, due to existing relationships with our competitors, are committed to the products offered by these competitors. Further, our current or potential customers may determine to develop and produce products for their own use which are competitive to our products. As a result of the foregoing factors, we expect that competitive pressures may result in price reductions, reduced margins, loss of sales and loss of market share. In addition, in markets where there are a limited number of customers, competition is particularly intense.

If we fail to accurately forecast component and material requirements for our products, we could incur additional costs and incur significant delays in shipments, which could result in a loss of customers.

We use rolling forecasts based on anticipated product orders and material requirements planning systems to determine our product requirements. It is very important that we accurately predict both the demand for our products and the lead times

required to obtain the necessary components and materials. We depend on our suppliers for most of our product components and materials. Lead times for components and materials that we order vary significantly and depend on factors including the specific supplier requirements, the size of the order, contract terms and current market demand for components. For substantial increases in our sales levels of certain products, some of our suppliers may need at least nine months lead-time. If we overestimate our component and material requirements, we may have excess inventory, which would increase our costs. If we underestimate our component and material requirements, we may have inadequate inventory, which could interrupt and delay delivery of our products to our customers. Any of these occurrences would negatively impact our net sales, business or operating results.

Our reliance on contract manufacturing and outsourcing may adversely impact our financial results and operations due to our decreased control over the performance and timing of certain aspects of our manufacturing.

Our manufacturing strategy includes partnering with contract manufacturers to outsource non-core subassemblies and less complex turnkey products, including some performed at international sites located in Asia and Eastern Europe. Additionally, we have outsourced the manufacture of certain of our optics components to certain third parties. Our ability to resume internal manufacturing operations for certain products and components in a timely manner may be eliminated. The cost, quality, performance and availability of contract manufacturing operations are and will be essential to the successful production and sale of many of our products. Our financial condition or results of operation could be adversely impacted if any contract manufacturer or other supplier is unable for any reason, including as a result of the impact of worldwide economic conditions, to meet our cost, quality, performance, and availability standards. We may not be able to provide contract manufacturers with product volumes that are high enough to achieve sufficient cost savings. If shipments fall below forecasted levels, we may incur increased costs or be required to take ownership of the inventory. Also, our ability to control the quality of products produced by contract manufacturers may be limited and quality issues may not be resolved in a timely manner, which could adversely impact our financial condition or results of operations.

If we fail to effectively manage our growth or, alternatively, our spending during downturns, our business could be disrupted, which could harm our operating results.

Growth in sales, combined with the challenges of managing geographically dispersed operations, can place a significant strain on our management systems and resources, and our anticipated growth in future operations could continue to place such a strain. The failure to effectively manage our growth could disrupt our business and harm our operating results. Our ability to successfully offer our products and implement our business plan in evolving markets requires an effective planning and management process. In economic downturns, we must effectively manage our spending and operations to ensure our competitive position during the downturn, as well as our future opportunities when the economy improves, remain intact. The failure to effectively manage our spending and operations could disrupt our business and harm our operating results.

Historically, acquisitions have been an important element of our strategy. However, we may not find suitable acquisition candidates in the future and we may not be able to successfully integrate and manage acquired businesses. Any acquisitions we make could disrupt our business and harm our financial condition.

We have in the past made strategic acquisitions of other corporations and entities, as well as asset purchases, and we continue to evaluate potential strategic acquisitions of complementary companies, products and technologies. In the event of any future acquisitions, we could:

- issue stock that would dilute our current stockholders' percentage ownership;
- pay cash that would decrease our working capital;

- incur debt;
- assume liabilities; or
- incur expenses related to impairment of goodwill and amortization.

Acquisitions also involve numerous risks, including:

- problems combining the acquired operations, systems, technologies or products;
- an inability to realize expected operating efficiencies or product integration benefits;

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- difficulties in coordinating and integrating geographically separated personnel, organizations, systems and facilities;
- difficulties integrating business cultures;
- unanticipated costs or liabilities, including the costs associated with improving the internal controls of the acquired company;
- diversion of management's attention from our core businesses;
- adverse effects on existing business relationships with suppliers and customers;
- potential loss of key employees, particularly those of the purchased organizations;
- incurring unforeseen obligations or liabilities in connection with acquisitions; and
- the failure to complete acquisitions even after signing definitive agreements which, among other things, would result in the expensing of potentially significant professional fees and other charges in the period in which the acquisition or negotiations are terminated.

We cannot assure you that we will be able to successfully identify appropriate acquisition candidates, to integrate any businesses, products, technologies or personnel that we might acquire in the future or achieve the anticipated benefits of such transactions, which may harm our business.

We are exposed to lawsuits in the normal course of business which could have a material adverse effect on our business, operating results, or financial condition.

We are exposed to lawsuits in the normal course of our business, including product liability claims, if personal injury, death or commercial losses occur from the use of our products. While we typically maintain business insurance, including directors' and officers' policies, litigation can be expensive, lengthy, and disruptive to normal business operations, including the potential impact of indemnification obligations for individuals named in any such lawsuits. We may not, however, be able to secure insurance coverage on terms acceptable to us in the future. Moreover, the results of complex legal proceedings are difficult to predict. An unfavorable resolution of a particular lawsuit, including a recall or redesign of products if ultimately determined to be defective, could have a material adverse effect on our business, operating results, or financial condition.

We use standard laboratory and manufacturing materials that could be considered hazardous and we could be liable for any damage or liability resulting from accidental environmental contamination or injury.

Although most of our products do not incorporate hazardous or toxic materials and chemicals, some of the gases used in our excimer lasers and some of the liquid dyes used in some of our scientific laser products are highly toxic. In addition, our operations involve the use of standard laboratory and manufacturing materials that could be considered hazardous. Also, if a facility fire were to occur at our Sunnyvale, California site and were to spread to a reactor used to grow semiconductor wafers, it could release highly toxic emissions. We believe that our safety procedures for handling and disposing of such materials comply with all federal, state and offshore regulations and standards. However, the risk of accidental environmental contamination or injury from such materials cannot be entirely eliminated. In the event of such an accident involving such materials, we could be liable for damages and such liability could exceed the amount of our liability insurance coverage and the resources of our business which could have an adverse effect on our financial results or our business as a whole.

Compliance or the failure to comply with current and future environmental regulations could cause us significant expense.

We are subject to a variety of federal, state, local and foreign environmental regulations relating to the use, storage, discharge and disposal of hazardous chemicals used during our manufacturing process or requiring design changes or recycling of products we manufacture. If we fail to comply with any present and future regulations, we could be subject to future liabilities, the suspension of production or a prohibition on the sale of products we manufacture. In addition, such regulations could restrict our ability to expand our facilities or could require us to acquire costly equipment, or to incur other significant expenses to comply with environmental regulations, including expenses associated with the recall of any non-compliant product and the management of historical waste.

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From time to time new regulations are enacted, and it is difficult to anticipate how such regulations will be implemented and enforced. We continue to evaluate the necessary steps for compliance with regulations as they are enacted. These regulations include, for example, the Registration, Evaluation, Authorization and Restriction of Chemical substances (“REACH”), the Restriction on the Use of Certain Hazardous Substances in Electrical and Electronic Equipment Directive (“RoHS”) and the Waste Electrical and Electronic Equipment Directive (“WEEE”) enacted in the European Union which regulate the use of certain hazardous substances in, and require the collection, reuse and recycling of waste from, certain products we manufacture. This and similar legislation that has been or is in the process of being enacted in Japan, China, Korea and various states of the United States may require us to re-design our products to ensure compliance with the applicable standards, for example by requiring the use of different types of materials. These redesigns or alternative materials may detrimentally impact the performance of our products, add greater testing lead-times for product introductions or have other similar effects. We believe we comply with all such legislation where our products are sold and we will continue to monitor these laws and the regulations being adopted under them to determine our responsibilities. In addition, we are monitoring legislation relating to the reduction of carbon emissions from industrial operations to determine whether we may be required to incur any additional material costs or expenses associated with our operations. We are not currently aware of any such material costs or expenses. The SEC has promulgated rules requiring disclosure regarding the use of certain “conflict minerals” mined from the Democratic Republic of Congo and adjoining countries and procedures regarding a manufacturer's efforts to prevent the sourcing of such minerals. The implementation of such rules has required us to incur additional expense and internal resources and may continue to do so in the future, particularly in the event that only a limited pool of suppliers are available to certify that products are free from “conflict minerals.” Our failure to comply with any of the foregoing regulatory requirements or contractual obligations could result in our being directly or indirectly liable for costs, fines or penalties and third-party claims, and could jeopardize our ability to conduct business in the United States and foreign countries.

Our and our customers' operations would be seriously harmed if our logistics or facilities or those of our suppliers, our customers' suppliers or our contract manufacturers were to experience catastrophic loss.

Our and our customers' operations, logistics and facilities and those of our suppliers and contract manufacturers could be subject to a catastrophic loss from fire, flood, earthquake, volcanic eruption, work stoppages, power outages, acts of war, pandemic illnesses, energy shortages, theft of assets, other natural disasters or terrorist activity. A substantial portion of our research and development activities, manufacturing, our corporate headquarters and other critical business operations are located near major earthquake faults in Santa Clara, California, an area with a history of seismic events. Any such loss or detrimental impact to any of our operations, logistics or facilities could disrupt our operations, delay production, shipments and net sales and result in large expenses to repair or replace the facility. While we have obtained insurance to cover most potential losses, after reviewing the costs and limitations associated with earthquake insurance, we have decided not to procure such insurance. We believe that this decision is consistent with decisions reached by numerous other companies located nearby. We cannot assure you that our existing insurance coverage will be adequate against all other possible losses.

Difficulties with our enterprise resource planning (“ERP”) system and other parts of our global information technology system could harm our business and results of operation. If our network security measures are breached and unauthorized access is obtained to a customer's data or our data or our information technology systems, we may incur significant legal and financial exposure and liabilities.

Like many modern multinational corporations, we maintain a global information technology system, including software products licensed from third parties. Any system, network or Internet failures, misuse by system users, the hacking into or disruption caused by the unauthorized access by third parties or loss of license rights could disrupt our ability to timely and accurately manufacture and ship products or to report our financial information in compliance with the timelines mandated by the SEC. Any such failure, misuse, hacking, disruptions or loss would likely cause a diversion of management's attention from the underlying business and could harm our operations. In addition, a significant failure of our global information technology system could adversely affect our ability to complete an

evaluation of our internal controls and attestation activities pursuant to Section 404 of the Sarbanes-Oxley Act of 2002.

As part of our day-to-day business, we store our data and certain data about our customers in our global information technology system. While our system is designed with access security, if a third party gains unauthorized access to our data, including any regarding our customers, such a security breach could expose us to a risk of loss of this information, loss of business, litigation and possible liability. These security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, employee error, malfeasance or otherwise. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our customers' data or our data, including our intellectual property and other confidential business information, or our information technology systems. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. Any security breach could result in a loss of

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confidence by our customers, damage our reputation, disrupt our business, lead to legal liability and negatively impact our future sales.

Changes in tax rates, tax liabilities or tax accounting rules could affect future results.

As a global company, we are subject to taxation in the United States and various other countries and jurisdictions. Significant judgment is required to determine worldwide tax liabilities. Our future tax rates could be affected by changes in the composition of earnings in countries or states with differing tax rates, changes in the valuation of our deferred tax assets and liabilities, or changes in the tax laws or the interpretation of such tax laws, including the Base Erosion Profit Shifting ("BEPS") project being conducted by the Organization for Economic Co-operation and Development ("OECD"). In addition, we are subject to regular examination of our income tax returns by the Internal Revenue Service ("IRS") and other tax authorities. From time to time the United States, foreign and state governments make substantive changes to tax rules and the application of rules to companies, including various announcements from the United States government potentially impacting our ability to defer taxes on international earnings. We regularly assess the likelihood of favorable or unfavorable outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. Although we believe our tax estimates are reasonable, there can be no assurance that any final determination will not be materially different than the treatment reflected in our historical income tax provisions and accruals, which could materially and adversely affect our operating results and financial condition.

Changing laws, regulations and standards relating to corporate governance and public disclosure may create uncertainty regarding compliance matters.

Federal securities laws, rules and regulations, as well as the rules and regulations of self-regulatory organizations such as NASDAQ and the NYSE, require companies to maintain extensive corporate governance measures, impose comprehensive reporting and disclosure requirements, set strict independence and financial expertise standards for audit and other committee members and impose civil and criminal penalties for companies and their chief executive officers, chief financial officers and directors for securities law violations. These laws, rules and regulations have increased and will continue to increase the scope, complexity and cost of our corporate governance, reporting and disclosure practices, which could harm our results of operations and divert management's attention from business operations. Changing laws, regulations and standards relating to corporate governance and public disclosure may create uncertainty regarding compliance matters. New or changed laws, regulations and standards are subject to varying interpretations in many cases. As a result, their application in practice may evolve over time. We are committed to maintaining high standards of ethics, corporate governance and public disclosure. Complying with evolving interpretations of new or changed legal requirements may cause us to incur higher costs as we revise current practices, policies and procedures, and may divert management time and attention from revenue generating to compliance activities. If our efforts to comply with new or changed laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to practice, our reputation may also be harmed.

Governmental regulations, including duties, affecting the import or export of products could negatively affect our net sales.

The United States and many foreign governments impose tariffs and duties on the import and export of products, including some of those which we sell. In particular, given our worldwide operations, we pay duties on certain products when they are imported into the United States for repair work as well as on certain of our products which are manufactured by our foreign subsidiaries. These products can be subject to a duty on the product value. Additionally, the United States and various foreign governments have imposed tariffs, controls, export license requirements and restrictions on the import or export of some technologies, especially encryption technology. From time to time, government agencies have proposed additional regulation of encryption technology, such as requiring the escrow and

governmental recovery of private encryption keys. Governmental regulation of encryption technology and regulation of imports or exports, or our failure to obtain required import or export approval for our products, could harm our international and domestic sales and adversely affect our net sales. From time to time our duty calculations and payments are audited by government agencies. For example, we are currently under audit in South Korea for customs duties and value-added-tax for the period March 2009 to March 2014. In the event of an adverse audit result, we could be liable for additional payments, duties, taxes and penalties, any of which could have a material adverse effect on our business or financial position, results of operations, or cash flows.

In addition, compliance with the directives of the Directorate of Defense Trade Controls (“DDTC”) may result in substantial expenses and diversion of management. Any failure to adequately address the directives of DDTC could result in civil fines or suspension or loss of our export privileges, any of which could have a material adverse effect on our business or financial position, results of operations, or cash flows.

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Our market is unpredictable and characterized by rapid technological changes and evolving standards demanding a significant investment in research and development, and, if we fail to address changing market conditions, our business and operating results will be harmed.

The photonics industry is characterized by extensive research and development, rapid technological change, frequent new product introductions, changes in customer requirements and evolving industry standards. Because this industry is subject to rapid change, it is difficult to predict its potential size or future growth rate. Our success in generating net sales in this industry will depend on, among other things:

- maintaining and enhancing our relationships with our customers;

- the education of potential end-user customers about the benefits of lasers and laser systems; and

- our ability to accurately predict and develop our products to meet industry standards.

For the three months ended December 27, 2014, our research and development costs were $19.2 million (9.6% of net sales). For our fiscal years 2014, 2013 and 2012, our research and development costs were $79.1 million (10.0% of net sales), $82.8 million (10.2% of net sales) and $78.3 million (10.2% of net sales), respectively. We cannot assure you that our expenditures for research and development will result in the introduction of new products or, if such products are introduced, that those products will achieve sufficient market acceptance or to generate sales to offset the costs of development. Our failure to address rapid technological changes in our markets could adversely affect our business and results of operations.

Failure to maintain effective internal controls may cause a loss of investor confidence in the reliability of our financial statements or to cause us to delay filing our periodic reports with the SEC and adversely affect our stock price.

The SEC, as directed by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring public companies to include a report of management on internal control over financial reporting in their annual reports on Form 10-K that contain an assessment by management of the effectiveness of our internal control over financial reporting. In addition, our independent registered public accounting firm must attest to and report on the effectiveness of our internal control over financial reporting. Although we test our internal control over financial reporting in order to ensure compliance with the Section 404 requirements, our failure to maintain adequate internal controls over financial reporting could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements or a delay in our ability to timely file our periodic reports with the SEC, which ultimately could negatively impact our stock price.

Provisions of our charter documents and Delaware law, and our Change-of-Control Severance Plan may have anti-takeover effects that could prevent or delay a change in control.

Provisions of our certificate of incorporation and bylaws may discourage, delay or prevent a merger or acquisition or make removal of incumbent directors or officers more difficult. These provisions may discourage takeover attempts and bids for our common stock at a premium over the market price. These provisions include:

- the ability of our Board of Directors to alter our bylaws without stockholder approval;

- limiting the ability of stockholders to call special meetings; and

- establishing advance notice requirements for nominations for election to our Board of Directors or for proposing matters that can be acted on by stockholders at stockholder meetings.

We are subject to Section 203 of the Delaware General Corporation Law, which prohibits a publicly-held Delaware corporation from engaging in a merger, asset or stock sale or other transaction with an interested stockholder for a period of three years following the date such person became an interested stockholder, unless prior approval of our board of directors is obtained or as otherwise provided. These provisions of Delaware law also may discourage, delay or prevent someone from acquiring or merging with us without obtaining the prior approval of our board of directors, which may cause the market price of our common stock to decline. In addition, we have adopted a change of control severance plan, which provides for the payment of a cash severance benefit to each eligible employee based on the employee's position. If a change of control occurs, our successor or acquirer will be required to assume and agree to perform all of our obligations under the change of control severance plan which may discourage potential acquirers or result in a lower stock price.

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

There were no sales of unregistered securities during the first quarter of fiscal 2015. Stock repurchases during the three months ended December 27, 2014 were as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value that May Yet Be Purchased Under the Plans or Programs (1)
September 28, 2014 - October 25, 2014	—	$—	—	25,000,000
October 26, 2014 - November 22, 2014	58,974	$55.99	58,974	21,698,040
November 23, 2014 - December 27, 2014	241,467	$57.94	241,467	7,708,218
Total	300,441	$57.55	300,441	7,708,218

(1) On July 25, 2014, we announced that the Board of Directors authorized a buyback program whereby we are authorized to repurchase up to $25.0 million of our common stock from time to time through July 31, 2015. On January 21, 2015, our board of directors authorized an additional stock repurchase program to repurchase up to $25.0 million of the Company's outstanding common stock from time to time through January 31, 2016.

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ITEM 6. EXHIBITS

Exhibit No.	Description
10.1‡ **	Fiscal 2015 Variable Compensation Plan Payout Scale
10.2‡	Fiscal 2014 Variable Compensation Plan Payout Scale
10.3+ ‡	Change of Control Severance Plan (Previously filed as Exhibit 10.1 to Form 8-K filed on December 17, 2014)
10.4‡	Form of PRSU Award Terms
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 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. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

+ These exhibits were previously filed with the Commission as indicated and are incorporated herein by reference.

‡ Identifies management contract or compensatory plans or arrangements required to be filed as an exhibit.

* In accordance with Rule 406T of Regulation S-T, the information in these exhibits is furnished and deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Exchange Act of 1934, and otherwise is not subject to liability under these sections.

** Portions of this exhibit are redacted and confidential treatment has been requested with the Securities and Exchange Commission.

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COHERENT, INC.

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.

Coherent, Inc.
(Registrant)

Date: February 4, 2015

/s/: JOHN R. AMBROSEO
John R. Ambroseo
President and Chief Executive Officer
(Principal Executive Officer)

Date: February 4, 2015

/s/: HELENE SIMONET
Helene Simonet
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

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10.4‡	Form of PRSU Award Terms
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 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. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

+	These exhibits were previously filed with the Commission as indicated and are incorporated herein by reference.
‡	Identifies management contract or compensatory plans or arrangements required to be filed as an exhibit.
*	In accordance with Rule 406T of Regulation S-T, the information in these exhibits is furnished and deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Exchange Act of 1934, and otherwise is not subject to liability under these sections.
**	Portions of this exhibit are redacted and confidential treatment has been requested with the Securities and Exchange Commission.

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