

NEWPORT CORP
Form 10-Q
November 12, 2009

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended October 3, 2009

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: 000-01649

NEWPORT CORPORATION

(Exact name of registrant as specified in its charter)

Nevada

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

94-0849175

(IRS Employer Identification No.)

1791 Deere Avenue, Irvine, California 92606

(Address of principal executive offices) (Zip Code)

(949) 863-3144

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Yes No

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

Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting

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company)

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

Yes No

As of October 31, 2009, 36,236,303 shares of the registrant's sole class of common stock were outstanding.

**NEWPORT CORPORATION
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PART I FINANCIAL INFORMATION**Item 1. Financial Statements**

NEWPORT CORPORATION
Consolidated Statements of Operations
(In thousands, except per share data)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Net sales	\$ 88,317	\$ 105,026	\$ 265,394	\$ 337,933
Cost of sales	53,097	65,424	163,764	204,923
Gross profit	35,220	39,602	101,630	133,010
Selling, general and administrative expenses	27,942	28,205	82,140	88,088
Research and development expense	9,339	11,340	27,704	35,125
Loss on disposal of diode laser assets and related costs	285		4,355	
Operating income (loss)	(2,346)	57	(12,569)	9,797
Recovery (write-down) of note receivable and other amounts related to previously discontinued operations, net	200	743	192	(6,317)
Interest and other expense, net	(2,024)	(2,100)	(6,339)	(5,261)
Loss before income taxes	(4,170)	(1,300)	(18,716)	(1,781)
Income tax (benefit) provision	(652)	1,086	(1,237)	2,144
Net loss	\$ (3,518)	\$ (2,386)	\$ (17,479)	\$ (3,925)
Net loss per share:				
Basic	\$ (0.10)	\$ (0.07)	\$ (0.48)	\$ (0.11)
Diluted	\$ (0.10)	\$ (0.07)	\$ (0.48)	\$ (0.11)
Shares used in per share calculations:				
Basic	36,214	36,078	36,150	36,208
Diluted	36,214	36,078	36,150	36,208

See accompanying notes.

NEWPORT CORPORATION
Consolidated Balance Sheets
(In thousands, except share and per share data)
(Unaudited)

	October 3, 2009	January 3, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 88,623	\$ 74,874
Marketable securities	61,422	73,546
Accounts receivable, net of allowance for doubtful accounts of \$2,568 and \$1,642 as of October 3, 2009 and January 3, 2009, respectively	64,501	75,258
Notes receivable, net	2,345	6,610
Inventories	96,683	98,833
Deferred income taxes	13,060	13,456
Prepaid expenses and other current assets	14,892	10,740
 Total current assets	 341,526	 353,317
 Property and equipment, net	 53,585	 60,245
Goodwill	69,932	68,540
Deferred income taxes	1,920	2,555
Intangible assets, net	29,359	26,696
Investments and other assets	13,295	13,550
	\$ 509,617	\$ 524,903
 LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Short-term obligations	\$ 9,909	\$ 14,089
Accounts payable	22,289	24,636
Accrued payroll and related expenses	19,088	21,827
Accrued expenses and other current liabilities	30,284	29,258
 Total current liabilities	 81,570	 89,810
 Long-term debt	 138,928	 135,478
Obligations under capital leases, less current portion	1,289	1,220
Accrued pension liabilities	11,216	10,652
Other liabilities	22,309	22,546
 Commitments and contingencies		
 Stockholders' equity:		
Common stock, par value \$0.1167 per share, 200,000,000 shares authorized; 36,236,303 and 36,048,634 shares issued and outstanding as of October 3, 2009 and January 3, 2009, respectively	 4,229	 4,207

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Capital in excess of par value	409,250	407,047
Accumulated other comprehensive income	10,653	6,291
Accumulated deficit	(169,827)	(152,348)
Total stockholders' equity	254,305	265,197
	\$ 509,617	\$ 524,903

See accompanying notes.

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NEWPORT CORPORATION
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine Months Ended	
	October	September
	3,	27,
	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (17,479)	\$ (3,925)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	14,910	16,024
Amortization of discount on convertible subordinated notes	3,416	3,929
Write-down of note receivable and other amounts related to previously discontinued operations		7,061
Provision for losses on inventories	8,102	4,372
Stock-based compensation expense	1,703	1,506
Provision for doubtful accounts, net	686	106
Loss on disposal of diode laser assets	3,765	
Loss on disposal of property and equipment	5	519
Deferred income taxes, net	(192)	1,237
Increase (decrease) in cash, net of acquisition and divestiture, due to changes in:		
Accounts and notes receivable	16,316	5,613
Inventories	(9,489)	3,789
Prepaid expenses and other assets	(3,679)	(1,126)
Accounts payable	(3,257)	(9,597)
Accrued payroll and related expenses	(2,998)	(1,188)
Accrued expenses and other liabilities	(239)	3,275
Other long-term liabilities	1,619	38
Net cash provided by operating activities	13,189	31,633
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(7,580)	(16,126)
Acquisition of business	(3,000)	
Purchase of marketable securities	(18,994)	(47,923)
Proceeds from the sale of marketable securities	33,010	30,616
Net cash provided by (used in) investing activities	3,436	(33,433)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term debt		2,828
Borrowings (repayments) of long-term debt and obligations under capital leases, net	80	(48)
Repayments of short-term obligations, net	(4,336)	(1,627)
Proceeds from the issuance of common stock under employee plans	522	1,582
Purchases of common stock		(12,822)

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Net cash used in financing activities	(3,734)	(10,087)
Impact of foreign exchange rate changes on cash balances	858	100
Net increase (decrease) in cash and cash equivalents	13,749	(11,787)
Cash and cash equivalents at beginning of period	74,874	88,737
Cash and cash equivalents at end of period	\$ 88,623	\$ 76,950
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 3,938	\$ 4,844
Income taxes, net	\$ 1,294	\$ 759

See accompanying notes.

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NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of Newport Corporation and its wholly owned subsidiaries (collectively referred to as the Company) and have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions of Form 10-Q and Rule 10-01 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal and recurring accruals) considered necessary for a fair presentation have been included. All intercompany transactions and balances have been eliminated in consolidation.

The accompanying consolidated financial statements do not include certain footnotes and financial presentations normally required under generally accepted accounting principles (GAAP) and, therefore, should be read in conjunction with the consolidated financial statements and related notes contained in the Company's Annual Report on Form 10-K for the year ended January 3, 2009. The results for the interim periods are not necessarily indicative of the results the Company will have for the full year ending January 2, 2010. The January 3, 2009 balances reported herein are derived from the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended January 3, 2009.

The Company has reviewed events and transactions that have occurred from October 3, 2009 through November 12, 2009, the date of issuance of the accompanying financial statements, and determined that no events or transactions have occurred subsequent to October 3, 2009 that require recognition or disclosure in the financial statements.

Certain prior period amounts have been reclassified to reflect the Company's retrospective implementation of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 470-20 (formerly known as FSP APB 14-1). See Note 10 for additional detail.

NOTE 2 RECENT ACCOUNTING PRONOUNCEMENTS

In August 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-05, *Measuring Liabilities at Fair Value*, which amends the guidance in ASC 820, *Fair Value Measurements and Disclosures*, to provide guidance on fair value measurement of liabilities. If a quoted price in an active market is not available for an identical liability, ASU 2009-05 requires companies to compute fair value by using quoted prices for an identical liability when traded as an asset, quoted prices for similar liabilities when traded as an asset or another valuation technique that is consistent with the guidance in ASC 820. ASU 2009-05 will be effective for interim and annual periods beginning after its issuance and is not expected to have a material impact on the Company's financial position or results of operations. In October 2009, the FASB issued ASU No. 2009-13, *Multiple-Deliverable Revenue Arrangements - a consensus of the FASB Emerging Issues Task Force*, which amends the guidance in ASC 605, *Revenue Recognition*. ASU 2009-13 eliminates the residual method of accounting for revenue on undelivered products and, instead, requires companies to allocate revenue to each of the deliverable products based on its relative selling price. In addition, this ASU expands the disclosure requirements surrounding multiple-deliverable arrangements. ASU 2009-13 will be effective for revenue arrangements entered into for fiscal years beginning on or after June 15, 2010. The Company is currently evaluating the impact that ASU 2009-13 will have on its financial position and results of operations.

NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

NOTE 3 MARKETABLE SECURITIES

All marketable securities were classified as available for sale and were recorded at market value using the specific identification method, and unrealized gains and losses are reflected in *accumulated other comprehensive income* in the accompanying consolidated balance sheets. The aggregate fair value of available for sale securities and aggregate amount of unrealized gains and losses for available for sale securities at October 3, 2009 were as follows:

(In thousands)	Aggregate Fair Value	Aggregate Amount of Unrealized	
		Gains	Losses
U.S. government and agency debt securities	\$ 18,555	\$ 474	\$
Corporate debt securities	6,256	2	(126)
Equity securities	24,930	248	
Asset-backed securities	7,284	177	(240)
Certificates of deposit	4,397	1	(1)
	\$ 61,422	\$ 902	\$ (367)

**Marketable Securities In Cumulative
Unrealized Loss Positions**

(In thousands)	Less Than 12 Months		More Than 12 Months	
	Aggregate Fair Value	Unrealized Loss	Aggregate Fair Value	Unrealized Loss
Corporate debt securities	\$	\$	\$ 3,304	\$ (126)
Asset-backed securities			90	(240)
Certificates of deposit			546	(1)
	\$	\$	\$ 3,940	\$ (367)

The aggregate fair value of available for sale securities and aggregate amount of unrealized gains and losses for available for sale securities at January 3, 2009 were as follows:

(In thousands)	Aggregate Fair Value	Aggregate Amount of Unrealized	
		Gains	Losses
U.S. government and agency debt securities	\$ 21,516	\$ 419	\$ (4)
Corporate debt securities	18,819	26	(588)
Equity securities	22,054	154	
Asset-backed securities	10,504		(938)
Certificates of deposit	653	1	
	\$ 73,546	\$ 600	\$ (1,530)

	Marketable Securities In Cumulative Unrealized Loss Positions			
	Less Than 12 Months		More Than 12 Months	
	Aggregate Fair Value	Unrealized Loss	Aggregate Fair Value	Unrealized Loss
(In thousands)				
U.S. government and agency debt securities	\$ 1,090	\$ (1)	\$ 172	\$ (3)
Corporate debt securities	5,962	(249)	8,187	(340)
Asset-backed securities	7,361	(498)	3,144	(439)
	\$ 14,413	\$ (748)	\$ 11,503	\$ (782)

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NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

The contractual maturities of debt securities and certificates of deposit were as follows:

(In thousands)	October 3, 2009
0 1 Year	\$ 21,476
1 2 Years	6,118
2 3 Years	1,129
3 5 Years	5,237
5 10 Years	2,532
More than 10 years	2,532
	\$ 36,492

The gross realized gains and losses on sales of available for sale securities were as follows:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Gross realized gains	\$	\$	\$ 4	\$ 121
Gross realized losses	(1)	(3)	(2)	(3)
	\$ (1)	\$ (3)	\$ 2	\$ 118

NOTE 4 FAIR VALUE MEASUREMENTS

The Company's financial instruments include cash and cash equivalents, marketable securities, short-term obligations and long-term debt. The carrying amount of cash and cash equivalents and short-term obligations approximates fair value due to the short-term maturities of these instruments. The fair value of marketable securities was estimated based on quoted market prices. The fair value of the Company's long-term debt was estimated based on the current rates for similar issues or on the current rates offered to the Company for debt of similar remaining maturities.

The estimated fair values of the Company's financial instruments were as follows:

(In thousands)	October 3, 2009		January 3, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$ 88,623	\$ 88,623	\$ 74,874	\$ 74,874
Marketable securities	\$ 61,422	\$ 61,422	\$ 73,546	\$ 73,546
Pension assets not owned by plan	\$ 9,154	\$ 9,154	\$ 6,614	\$ 6,614
Short-term obligations	\$ 9,909	\$ 9,909	\$ 14,089	\$ 14,089
Long-term debt	\$ 138,928	\$ 139,290	\$ 135,478	\$ 117,967

ASC 820-10 requires that for any assets and liabilities stated at fair value on a recurring basis in the Company's financial statements, the fair value of such assets and liabilities be measured based on the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company's assets measured at fair value on a recurring basis are categorized in the table below based upon their level within the fair value hierarchy.

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(In thousands)	Fair Value Measurements at Reporting Date Using			
Description	October 3, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Marketable securities:				
U.S. government and agency debt securities	\$ 18,555	\$ 18,555	\$	\$
Corporate debt securities	6,256	6,256		
Equity securities	24,930	24,930		
Asset-backed securities	7,284	3,871	3,413	
Certificates of deposit	4,397	3,746	651	
	61,422	57,358	4,064	
Pension assets not owned by plan	9,154	9,154		
	\$ 70,576	\$ 66,512	\$ 4,064	\$

NOTE 5 ACQUISITIONS AND DIVESTITURES

On July 4, 2009, the Company completed an asset exchange transaction with Oclaro, Inc. (Oclaro), pursuant to which the Company acquired certain assets and assumed certain liabilities related to Oclaro's New Focus business, and sold certain assets and transferred certain liabilities related to its diode laser operations based in Tucson, Arizona to Oclaro. The acquisition of the New Focus business expands the Company's current product offerings to include a number of new high-performance products, including opto-electronics, high-resolution actuators, opto-mechanics, tunable lasers, and custom-engineered solutions designed for original equipment manufacturers (OEMs).

The fair value of the New Focus business on the acquisition date was \$14.1 million, and the purchase price was paid by the transfer to Oclaro of the Company's diode laser assets and liabilities, which had a fair value of \$11.1 million, and the payment of \$3.0 million in cash. The Company incurred \$0.2 million in acquisition related expenses, which have been expensed as incurred and are included in *selling, general and administrative expenses* in the accompanying statements of operations.

Below is a summary of the purchase price, assets acquired and liabilities assumed:

(In thousands)	
Assets acquired and liabilities assumed:	
Current assets	\$ 8,930
Goodwill	1,392
Purchased intangible assets	4,830
Other assets	1,247
Current liabilities	(2,299)

\$ 14,100

The \$1.4 million in goodwill has been allocated to the Company's Photonics and Precision Technologies (PPT) Division and will be deductible for tax purposes, as this was an asset acquisition.

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Notes to Consolidated Financial Statements
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The actual net sales and net income of the New Focus business from July 4, 2009, the closing date of the acquisition, that were included in the Company's consolidated statement of operations for the three and nine months ended October 3, 2009 and September 27, 2008 are set forth in the table below. Also set forth in the table below are the net sales and net loss of the Company during such periods, including the results of the New Focus business as though the acquisition had occurred at the beginning of both periods presented. This supplemental pro forma financial information is presented for information purposes only and is not necessarily indicative of the results of operations that would have been achieved if the acquisition had occurred as of the beginning of each reporting period.

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Actual:				
Net sales	\$ 5,374	\$	\$ 5,374	\$
Net income	\$ 1,213	\$	\$ 1,213	\$
Supplemental pro forma information:				
Net sales	\$88,317	\$ 112,787	\$278,147	\$362,793
Net loss	\$ (3,518)	\$ (4,903)	\$ (21,888)	\$ (3,662)

The Company's diode laser assets had a net book value of \$14.9 million, which resulted in a loss of \$4.4 million after considering the fair value of these assets of \$11.1 million and selling costs of \$0.6 million. This loss has been included in continuing operations under *loss on disposal of diode laser assets and related costs* in the Company's consolidated statements of operations. These assets had previously been included in the Company's Lasers Division. Below is a summary of the assets and liabilities disposed of:

(In thousands)	
Assets and liabilities disposed of:	
Current assets	\$ 11,043
Other assets	5,106
Current liabilities	(1,284)
	\$ 14,865

NOTE 6 SUPPLEMENTAL BALANCE SHEET INFORMATION

Inventories

Inventories were as follows:

(In thousands)	October 3, 2009	January 3, 2009
Raw materials and purchased parts	\$ 82,101	\$ 84,472
Work in process	10,161	7,624
Finished goods	36,144	33,422
	128,406	125,518
Allowance for excess and obsolete inventory	(31,723)	(26,685)
	\$ 96,683	\$ 98,833

Accrued Warranty Obligations

Unless otherwise stated in the Company's product literature or in its agreements with customers, products sold by the Company's PPT Division generally carry a one-year warranty from the original invoice date on all product materials and workmanship, other than filters, gratings and crystals products, which generally carry a 90 day

NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

warranty. Products of this division sold to OEM customers generally carry longer warranties, typically 15 to 19 months. Products sold by the Company's Lasers Division carry warranties that vary by product and product component, but that generally range from 90 days to two years. In certain cases, such warranties for Lasers Division products are limited by either a set calendar period or a maximum amount of usage of the product, whichever occurs first. Defective products will be either repaired or replaced, generally at the Company's option, upon meeting certain criteria. The Company accrues a provision for the estimated costs that may be incurred for warranties relating to a product (based on historical experience) as a component of cost of sales at the time revenue for that product is recognized. Accrued warranty obligations are included in *accrued expenses and other current liabilities* in the accompanying consolidated balance sheets.

The activity in accrued warranty obligations was as follows:

(In thousands)	Nine Months Ended	
	October 3, 2009	September 27, 2008
Balance at beginning of year	\$ 5,978	\$ 5,847
Additions charged to cost of sales	3,215	5,208
Warranty claims	(4,465)	(4,761)
Balance at end of period	\$ 4,728	\$ 6,294

Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities were as follows:

(In thousands)	October 3, 2009	January 3, 2009
Deferred revenue	\$ 14,193	\$ 11,813
Accrued warranty obligations	4,728	5,978
Accrued pension benefits	2,516	1,999
Other	8,847	9,468
	\$ 30,284	\$ 29,258

Accumulated Other Comprehensive Income

Accumulated other comprehensive income consisted of the following:

(In thousands)	October 3, 2009	January 3, 2009
Cumulative foreign currency translation gains	\$ 10,263	\$ 6,884
Unrecognized net pension gains	55	58
Unrealized gains (losses) on marketable securities	335	(651)
	\$ 10,653	\$ 6,291

NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

NOTE 7 INTANGIBLE ASSETS

Intangible assets were as follows:

(In thousands)	October 3, 2009	January 3, 2009
Intangible assets subject to amortization:		
Developed technology, net of accumulated amortization of \$3,815 and \$3,210 as of October 3, 2009 and January 3, 2009, respectively	\$ 5,985	\$ 3,990
Customer relationships, net of accumulated amortization of \$10,171 and \$8,694 as of October 3, 2009 and January 3, 2009, respectively	9,929	10,806
Other, net of accumulated amortization of \$85 and \$0 as of October 3, 2009 and January 3, 2009	945	
	16,859	14,796
Intangible assets not subject to amortization:		
Trademarks and trade names	12,500	11,900
Intangible assets, net	\$ 29,359	\$ 26,696

Amortization expense related to intangible assets totaled \$0.8 million and \$2.2 million for the three and nine months ended October 3, 2009, respectively, and \$1.0 million and \$3.0 million for the three and nine months ended September 27, 2008, respectively. Developed technology and customer relationships are amortized over 10 years. Other intangible assets include acquired backlog, which is amortized over one year, and in-process research and development, which will not be amortized until the technology is completed. Estimated aggregate amortization expense for future fiscal years is as follows:

(In thousands)	Estimated Aggregate Amortization Expense
2009 (remaining)	\$ 833
2010	3,160
2011	2,990
2012	2,990
2013	2,990
Thereafter	3,206
	\$ 16,169

The Company has excluded \$690,000 of amortization expense related to in-process research and development from the table above, as it is uncertain when the technology will be completed and when the amortization will begin.

NEWPORT CORPORATION
Notes to Consolidated Financial Statements
October 3, 2009

NOTE 8 INTEREST AND OTHER EXPENSE, NET

Interest and other expense, net, was as follows:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Interest and dividend income	\$ 538	\$ 1,006	\$ 1,609	\$ 3,070
Interest expense	(2,366)	(2,829)	(7,136)	(8,281)
Bank and portfolio asset management fees	(158)	(149)	(483)	(441)
Other, net	(38)	(128)	(329)	391
	\$ (2,024)	\$ (2,100)	\$ (6,339)	\$ (5,261)

NOTE 9 STOCK-BASED COMPENSATION

During the nine months ended October 3, 2009, the Company granted 1.2 million restricted stock units and 1.0 million stock appreciation rights with weighted average grant date fair values of \$4.18 and \$1.64, respectively.

The total stock-based compensation expense included in the Company's consolidated statements of operations was as follows:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Cost of sales	\$ 39	\$ 36	\$ 98	\$ 198
Selling, general and administrative expenses	530	(195)	1,442	1,044
Research and development expense	53	61	163	264
	\$ 622	\$ (98)	\$ 1,703	\$ 1,506

In the three months ended September 27, 2008, the Company determined that the performance goals applicable to certain of its outstanding stock-based awards, for which it previously recognized compensation expense, would not be achieved and, therefore, reversed the amount of compensation expense previously recognized for such awards.

At October 3, 2009, the total compensation cost related to unvested stock-based awards granted to employees, officers and directors under the Company's stock-based benefit plans that had not yet been recognized was \$3.9 million (net of estimated forfeitures of \$1.3 million). This amount excludes compensation expense associated with awards that are subject to performance conditions that the Company does not expect will vest. This future compensation expense will be amortized, using the straight-line method for time-based awards and the graded vesting method for performance-based awards, over a weighted-average period of 1.6 years. The actual compensation expense that the Company will recognize in the future related to stock-based awards will be adjusted for subsequent forfeitures and will be adjusted based on the Company's determination as to the extent to which performance conditions applicable to any stock-based awards will be achieved. At October 3, 2009, there were 1.2 million performance-based restricted stock units outstanding with a weighted-average grant date fair value of \$11.15 per share that were not expected to vest.

At October 3, 2009, 2.6 million stock options with a weighted average exercise price of \$20.45 per share, intrinsic value of \$0.3 million and remaining contractual term of 3.0 years were vested or expected to vest and exercisable.

NOTE 10 DEBT AND LINES OF CREDIT

In February 2007, the Company issued \$175 million in convertible subordinated notes. The notes are subordinated to all of the Company's existing and future senior indebtedness, mature on February 15, 2012 and bear interest at a rate of 2.5% per year, payable in cash semiannually in arrears on February 15 and August 15 of each year. During the fourth quarter of 2008, the Company extinguished \$28 million of these notes.

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Holders may convert their notes based on a conversion rate of 41.5861 shares of the Company's common stock per \$1,000 principal amount of notes (equal to an initial conversion price of approximately \$24.05 per share) under certain circumstances. Upon conversion, in lieu of shares of the common stock, for each \$1,000 principal amount of notes, a holder will receive an amount in cash equal to the lesser of (i) \$1,000 or (ii) the conversion value, determined in the manner set forth in the indenture. If the conversion value exceeds \$1,000, the Company will also deliver, at its election, cash or common stock or a combination of cash and common stock with respect to the remaining common stock deliverable upon conversion. As of October 3, 2009, the conversion value was less than the principal amount of the notes.

During the first quarter of 2009, the Company adopted ASC 470-20, which requires the liability and equity components of convertible debt instruments to be separately accounted for in a manner that reflects the non-convertible debt borrowing rate for interest expense recognition. In addition, direct issuance costs associated with the convertible debt instruments are required to be allocated to the liability and equity components in proportion to the allocation of proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. These provisions have been applied retrospectively upon adoption. In accordance with ASC 470-20, the Company has recorded a debt discount of \$27.5 million and a deferred tax liability of \$10.6 million and has allocated \$0.9 million of issuance costs to the equity component. Such amounts were calculated using an income approach and assumed a non-convertible debt borrowing rate of 6.25%, which is also the effective interest rate used to calculate interest expense. Due to the valuation allowance maintained by the Company against its deferred tax assets, the recording of the deferred tax liability resulted in a reduction to this valuation allowance rather than in a reduction in capital in excess of par value. Upon the adoption of ASC 470-20, the amortization of the debt discount resulted in an increase in non-cash interest expense of \$4.2 million and \$4.9 million for the Company's fiscal years 2008 and 2007, respectively. The cumulative effect of adopting ASC 470-20 was an increase in stockholders' equity of \$14.6 million as of January 3, 2009. The Company's consolidated statements of operations for the three and nine months ended September 27, 2008 have been retrospectively adjusted compared with previously reported amounts as follows:

(In thousands)	Three Months Ended September 27, 2008	Nine Months Ended September 27, 2008
Additional non-cash interest expense	\$ 1,321	\$ 3,929
Reduction in amortization of debt issuance costs	(70)	(206)
Retrospective increase in net loss	\$ 1,251	\$ 3,723
Change to basic earnings per share	\$ (0.03)	\$ (0.10)
Change to diluted earnings per share	\$ (0.03)	\$ (0.10)

At October 3, 2009, the Company had \$147.0 million in convertible subordinated notes outstanding with a carrying value of \$135.6 million, net of \$11.4 million in unamortized debt discount, which is included in *long-term debt* in the accompanying consolidated balance sheets. At January 3, 2009, the Company had \$147.0 million in convertible subordinated notes outstanding with a carrying value of \$132.2 million, net of \$14.8 million in unamortized debt discount. At October 3, 2009 and January 3, 2009, the carrying value of the equity component was \$26.6 million, net of \$0.9 million of equity issuance costs. At October 3, 2009 and January 3, 2009, debt issuance costs of \$2.0 million

and \$2.6 million, respectively, net of accumulated amortization, were included in other long-term assets in *investments and other assets*. The remaining debt issuance costs and unamortized debt discount are being amortized through February 15, 2012 using the effective interest method.

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Interest cost on the convertible subordinated notes consisted of the following components:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Contractual interest	\$ 919	\$ 1,094	\$ 2,756	\$ 3,281
Amortization of debt discount	1,148	1,321	3,416	3,929
Interest cost on convertible subordinated notes	\$ 2,067	\$ 2,415	\$ 6,172	\$ 7,210

During June 2008, the Company issued 300 million yen (\$3.3 million at October 3, 2009) in private placement bonds through a Japanese bank. These bonds bear interest at a rate of 1.55% per year, payable in cash semiannually in arrears on June 30 and December 31 of each year. The bonds mature on June 30, 2011. The bonds are included in *long-term debt* in the accompanying consolidated balance sheets.

At October 3, 2009, the Company had a total of three lines of credit, including one domestic revolving line of credit and two revolving lines of credit with Japanese banks. Additionally, the Company has agreements with two Japanese banks under which it sells trade notes receivable with recourse.

The Company's domestic revolving line of credit has a total credit limit of \$5.0 million and expires December 1, 2009. Certain cash equivalents held at this lending institution collateralize this line of credit, which bears interest at either the prevailing London Interbank Offered Rate (LIBOR) (0.24% at October 3, 2009) plus 1.00% or the British Bankers Association LIBOR Daily Floating Rate (0.20% at October 3, 2009) plus 1.00%, at the Company's option, and carries an unused line fee of 0.25% per year. At October 3, 2009, there were no balances outstanding under this line of credit, with \$3.7 million available, after considering outstanding letters of credit totaling \$1.3 million.

The two revolving lines of credit with Japanese banks totaled 1.1 billion yen (\$12.2 million at October 3, 2009) and expire as follows: \$8.9 million on November 30, 2009 and \$3.3 million on May 31, 2010. The \$8.9 million line of credit bears interest at the prevailing bank rate and the \$3.3 million line of credit bears interest at LIBOR plus 1.75%. Certain cash equivalents held by the lending institution's U.S. affiliate collateralize the \$3.3 million line of credit. At October 3, 2009, the Company had \$7.9 million outstanding and \$4.3 million available for borrowing under these lines of credit. Amounts outstanding are included in *short-term obligations* in the accompanying consolidated balance sheets. The Company has agreements with two Japanese banks under which it sells trade notes receivable with recourse. These agreements allow the Company to sell receivables totaling up to 550 million yen (\$6.1 million at October 3, 2009), have no expiration dates and bear interest at the prevailing bank rate. At October 3, 2009, the Company had \$2.0 million outstanding and \$4.1 million available for the sale of notes receivable under these agreements. Amounts outstanding under these agreements are included in *short-term obligations* in the accompanying consolidated balance sheets, as the sale of these receivables has not met the criteria for sale treatment in accordance with ASC 860-30, *Transfers and Servicing - Secured Borrowing and Collateral*. As of October 3, 2009, the weighted average effective interest rate on all of the Company's Japanese borrowings, including the private placement bonds, was 2.5%.

Total long-term debt was as follows:

(In thousands)	October 3, 2009	January 3, 2009
	\$ 3,340	\$ 3,307

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Japanese private placement bonds due June 2011, interest at 1.55% payable semi-annually		
Convertible notes due February 2012, interest at 2.5% payable semi-annually	135,588	132,171
Total long-term debt	\$ 138,928	\$ 135,478

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NOTE 11 NET LOSS PER SHARE

The following table sets forth the computation of basic and diluted net loss per share:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Net loss	\$ (3,518)	\$ (2,386)	\$ (17,479)	\$ (3,925)
Shares:				
Weighted average shares outstanding basic	36,214	36,078	36,150	36,208
Dilutive potential common shares, using treasury stock method				
Weighted average shares outstanding diluted	36,214	36,078	36,150	36,208
Net loss per share:				
Basic	\$ (0.10)	\$ (0.07)	\$ (0.48)	\$ (0.11)
Diluted	\$ (0.10)	\$ (0.07)	\$ (0.48)	\$ (0.11)

For the three and nine months ended October 3, 2009, 156,000 and 120,000 dilutive shares, respectively, and for the three and nine months ended September 27, 2008, 68,000 and 100,000 dilutive shares, respectively, were excluded from the computation of diluted net loss per share, as their inclusion would have had an antidilutive effect due to the Company incurring a loss in each period. In addition, for the three and nine months ended October 3, 2009, 2,532,000 and 2,614,000 stock options, respectively, and for the three and nine months ended September 27, 2008, 2,694,000 and 2,541,000 stock options, respectively, were excluded from the computation of dilutive shares, as their exercise price exceeded the average market price of the Company's common stock, which would have resulted in an antidilutive effect. For the three and nine months ended October 3, 2009 and for the three and nine months ended September 27, 2008, 3.3 million and 1.7 million performance-based awards, respectively, were excluded from the computation of diluted net income per share, as the performance criteria for their vesting had not been met. For the three and nine months ended October 3, 2009 and September 27, 2008, the Company's convertible subordinated notes had no impact on diluted net loss per share as the average price of the Company's common stock during those periods was below \$24.05, and the convertible subordinated notes, if converted, would require only cash settlement.

NOTE 12 INCOME TAXES

The Company has maintained a valuation allowance against substantially all of its gross deferred tax assets pursuant to ASC 740-10, *Income Taxes*, due to the uncertainty as to the timing and ultimate realization of those assets. As a result, until such valuation allowance is reversed, the U.S. tax provision relating to future earnings will be offset substantially by a reduction in the valuation allowance. Accordingly, current and future tax expense will consist of taxes in certain foreign jurisdictions, required state income taxes, the federal alternative minimum tax and the impact of discrete items.

The Company will continue to monitor actual results, refine forecasted data and assess the need for retaining a valuation allowance against the U.S. and certain foreign gross deferred tax assets. In the event it is determined that a valuation allowance is no longer required, substantially all of the reversal will be recorded as a discrete item in the appropriate period. As of October 3, 2009, the Company's valuation allowance was \$59.7 million.

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NOTE 13 COMPREHENSIVE LOSS

The components of comprehensive loss, net of related tax, were as follows:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Net loss	\$ (3,518)	\$ (2,386)	\$ (17,479)	\$ (3,925)
Foreign currency translation gains (losses)	2,416	(4,772)	3,380	781
Unrecognized net pension gains (losses)	16	1	(3)	24
Unrealized gains (losses) on marketable securities	(93)	(511)	985	(652)
	\$ (1,179)	\$ (7,668)	\$ (13,117)	\$ (3,772)

NOTE 14 STOCKHOLDERS EQUITY TRANSACTIONS

In May 2008, the Board of Directors of the Company approved a share repurchase program, authorizing the purchase of up to 4.0 million shares of the Company's common stock. Purchases may be made under this program from time to time in the open market or in privately negotiated transactions, and the timing and amount of the purchases will be based on factors including the Company's share price, cash balances, expected cash requirements and general business and market conditions. No purchases were made under this program during the first nine months of 2009. As of October 3, 2009, 3.9 million shares remained available for purchase under the program.

NOTE 15 DEFINED BENEFIT PENSION PLANS

Several of the Company's non-U.S. subsidiaries have defined benefit pension plans covering substantially all full-time employees at those subsidiaries. Some of the plans are unfunded, as permitted under the plans and applicable laws. For financial reporting purposes, the calculation of net periodic pension costs is based upon a number of actuarial assumptions, including a discount rate for plan obligations, an assumed rate of return on pension plan assets and an assumed rate of compensation increase for employees covered by the plan. All of these assumptions are based upon management's judgment, considering all known trends and uncertainties. Actual results that differ from these assumptions would impact future expense recognition and the cash funding requirements of the Company's pension plans.

Net periodic benefit costs for the plans in aggregate included the following components:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Service cost	\$ 148	\$ 143	\$ 436	\$ 438
Interest cost on benefit obligation	163	172	466	523
Expected return on plan assets	(32)	(40)	(92)	(123)
Net loss	(8)		(22)	
	\$ 271	\$ 275	\$ 788	\$ 838

NOTE 16 BUSINESS SEGMENT INFORMATION

The operating segments reported below are the segments of the Company for which separate financial information is available and for which operating results are evaluated regularly by the Chief Executive Officer, who is the chief

operating decision maker, in deciding how to allocate resources and in assessing performance. The Company develops, manufactures and markets its products within two distinct business segments, its Lasers Division and its PPT Division.

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The Company measured operating income (loss) reported for each business segment, which included only those costs that were directly attributable to the operations of that segment, and excluded certain unallocated operating expenses and other charges and gains, interest and other expense, net, and income taxes.

(In thousands)	Lasers	Photonics and Precision Technologies	Total
Three months ended October 3, 2009:			
Sales to external customers	\$ 34,601	\$ 53,716	\$ 88,317
Segment income	\$ 459	\$ 6,375	\$ 6,834
Three months ended September 27, 2008:			
Sales to external customers	\$ 44,847	\$ 60,179	\$ 105,026
Segment income (loss)	\$ (2,218)	\$ 8,935	\$ 6,717
Nine months ended October 3, 2009:			
Sales to external customers	\$ 107,555	\$ 157,839	\$ 265,394
Segment income (loss)	\$ (8,336)	\$ 19,907	\$ 11,571
Nine months ended September 27, 2008:			
Sales to external customers	\$ 142,212	\$ 195,721	\$ 337,933
Segment income (loss)	\$ (4,143)	\$ 33,367	\$ 29,224

The segment loss reported for the Company's Lasers Division for the three and nine months ended October 3, 2009 includes a loss on the disposal of diode laser assets and related costs of \$0.3 million and \$4.4 million, respectively. The following reconciles segment income to consolidated loss before income taxes:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Segment income	\$ 6,834	\$ 6,717	\$ 11,571	\$ 29,224
Unallocated operating expenses	(9,180)	(6,660)	(24,140)	(19,427)
Recovery (write-down) of note receivable and other amounts related to previously discontinued operations, net	200	743	192	(6,317)
Interest and other expense, net	(2,024)	(2,100)	(6,339)	(5,261)
	\$ (4,170)	\$ (1,300)	\$ (18,716)	\$ (1,781)

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our unaudited consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and in conjunction with our Annual Report on Form 10-K for the year ended January 3, 2009. This discussion contains descriptions of our expectations regarding future trends affecting our business. These forward-looking statements and other forward-looking statements made elsewhere in this report are made in reliance upon safe harbor provisions in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Words such as may, will, expect, believe, anticipate, intend, could, continue or the negative or other variations thereof or comparable terminology are intended to identify forward-looking statements. In addition, any statements that refer to projections of our future financial performance or condition, trends in our business, or other characterizations of future events or circumstances are forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of several factors, including, but not limited to those factors set forth and discussed elsewhere in this Quarterly Report on Form 10-Q and in Item 1 (Business) and Item 1A (Risk Factors) of Part I, and Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations) of Part II, of our Annual Report on Form 10-K for the year ended January 3, 2009. In light of the significant uncertainties inherent in the forward-looking information included in this report, the inclusion of this information should not be regarded as a representation by us or any other person that our objectives or plans will be achieved and readers are cautioned not to place undue reliance on such forward-looking information. We undertake no obligation to update or revise these forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

We are a global supplier of advanced technology products and systems, including lasers, photonics instrumentation, sub-micron positioning systems, vibration isolation, optical components and subsystems and advanced automated manufacturing systems. Our products are used worldwide in industries including scientific research, microelectronics, aerospace and defense/security, life and health sciences and industrial manufacturing. We operate within two distinct business segments, our Lasers Division and our Photonics and Precision Technologies (PPT) Division. Both of our divisions offer a broad array of products and services to original equipment manufacturer (OEM) and end-user customers across a wide range of applications and markets.

The following is a discussion and analysis of certain factors that have affected our results of operations and financial condition during the periods included in the accompanying consolidated financial statements.

Critical Accounting Policies and Estimates

The preparation of these financial statements requires our management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We evaluate these estimates and assumptions on an ongoing basis. We base our estimates on our historical experience and on various other factors which we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities and the amounts of certain expenses that are not readily apparent from other sources. The accounting policies that involve the most significant judgments, assumptions and estimates used in the preparation of our financial statements are those related to revenue recognition, allowances for doubtful accounts, pension liabilities, inventory reserves, warranty obligations, asset impairment, income taxes and stock-based compensation expense. The judgments, assumptions and estimates used in these areas by their nature involve risks and uncertainties, and in the event that any of them prove to be inaccurate in any material respect, it could have a material adverse effect on our reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. A summary of these critical accounting policies is included in Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations) of Part II, of our Annual Report on Form 10-K for the fiscal year ended January 3, 2009. There have been no material changes to the critical accounting policies disclosed in our Annual Report on Form 10-K.

Acquisitions and Divestitures

On July 4, 2009, we completed an asset exchange transaction with Oclaro, Inc. (Oclaro), pursuant to which we acquired certain assets and assumed certain liabilities related to Oclaro's New Focus business, and we sold certain assets and transferred certain liabilities related to our diode laser operations based in Tucson, Arizona to Oclaro. The New Focus business expands our current product offerings to include a number of new high-performance products, including opto-electronics, high-resolution actuators, opto-mechanics, tunable lasers, and custom-engineered solutions designed for OEMs.

The fair value of the New Focus business on the acquisition date was \$14.1 million and the purchase price was paid by the transfer to Oclaro of our diode laser assets and liabilities, which had a fair value of \$11.1 million, and the payment of \$3.0 million in cash. We incurred \$0.2 million in acquisition related expenses, which have been expensed as incurred and are included in *selling, general and administrative expenses* in the accompanying statements of operations.

Below is a summary of the purchase price, assets acquired and liabilities assumed:

(In thousands)

Assets acquired and liabilities assumed:

Current assets	\$ 8,930
Goodwill	1,392
Purchased intangible assets	4,830
Other assets	1,247
Current liabilities	(2,299)
	\$ 14,100

Our diode laser assets had a net book value of \$14.9 million, which resulted in a loss of \$4.4 million after considering the fair value of these assets of \$11.1 million and selling costs of \$0.6 million. This loss has been included in continuing operations under *loss on disposal of diode laser assets and related costs* in our consolidated statements of operations. These assets had previously been included in our Lasers Division.

Adoption of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 470-20 (formerly known as FSP APB 14-1)

During the first quarter of 2009, we adopted ASC 470-20, *Debt - Debt with Conversion and Other Options*, which requires the liability and equity components of convertible debt instruments to be separately accounted for in a manner that reflects the non-convertible debt borrowing rate for interest expense recognition. In addition, direct issuance costs associated with the convertible debt instruments are required to be allocated to the liability and equity components in proportion to the allocation of proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. These provisions have been applied retrospectively upon adoption. In accordance with ASC 470-20, we have recorded a debt discount of \$27.5 million and a deferred tax liability of \$10.6 million and have allocated \$0.9 million of issuance costs to the equity component. Such amounts were calculated using an income approach and assumed a non-convertible debt borrowing rate of 6.25%, which is also the effective interest rate used to calculate interest expense. Due to the valuation allowance maintained against our deferred tax assets, the recording of the deferred tax liability resulted in a reduction to this valuation allowance rather than in a reduction in capital in excess of par value. Upon the adoption of ASC 470-20, the amortization of the debt discount resulted in an increase in non-cash interest expense of \$4.2 million and \$4.9 million for our fiscal years 2008 and 2007, respectively. The cumulative effect of adopting ASC 470-20 was an increase in stockholders' equity of \$14.6 million as of January 3, 2009. Our consolidated statements of operations for the three and nine months ended September 27, 2008 have been retrospectively adjusted compared with previously reported amounts as follows:

(In thousands)	Three Months Ended September 27, 2008	Nine Months Ended September 27, 2008
Additional non-cash interest expense	\$ 1,321	\$ 3,929
Reduction in amortization of debt issuance costs	(70)	(206)
Retrospective increase in net loss	\$ 1,251	\$ 3,723
Change to basic earnings per share	\$ (0.03)	\$ (0.10)
Change to diluted earnings per share	\$ (0.03)	\$ (0.10)

Stock-Based Compensation

During the nine months ended October 3, 2009, we granted 1.2 million restricted stock units and 1.0 million stock appreciation rights with weighted average grant date fair values of \$4.18 and \$1.64, respectively.

The total stock-based compensation expense included in our consolidated statements of operations was as follows:

(In thousands)	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Cost of sales	\$ 39	\$ 36	\$ 98	\$ 198
Selling, general and administrative expenses	530	(195)	1,442	1,044
Research and development expense	53	61	163	264
	\$ 622	\$ (98)	\$ 1,703	\$ 1,506

In the three months ended September 27, 2008, we determined that the performance goals applicable to certain of our outstanding stock-based awards, for which we previously recognized compensation expense, would not be achieved, and we therefore reversed the amount of compensation expense we previously recognized for such awards.

Results of Operations for the Three and Nine Months Ended October 3, 2009 and September 27, 2008

The following table presents our results of operations for the periods indicated as a percentage of net sales:

	Percentage of Net Sales			
	Three Months Ended		Nine Months Ended	
	October 3, 2009	September 27, 2008	October 3, 2009	September 27, 2008
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	60.1	62.3	61.7	60.6
Gross profit	39.9	37.7	38.3	39.4
Selling, general and administrative expenses	31.6	26.9	31.0	26.1
Research and development expense	10.6	10.8	10.4	10.4
Loss on disposal of diode laser assets and related costs	0.3		1.6	
Operating income (loss)	(2.6)	(0.0)	(4.7)	2.9
Recovery (write-down) of note receivable and other amounts related to previously discontinued operations, net	0.2	0.7	0.1	(1.9)
Interest and other expense, net	(2.3)	(2.0)	(2.5)	(1.6)
Loss before income taxes	(4.7)	(1.3)	(7.1)	(0.6)
Income tax (benefit) provision	(0.7)	1.0	(0.5)	0.6
Net loss	(4.0)%	(2.3)%	(6.6)%	(1.2)%

In the following discussion regarding our net sales, certain prior period amounts have been reclassified between end markets to conform to the current period presentation.

Net Sales

Net sales for the three months ended October 3, 2009 decreased by \$16.7 million, or 15.9%, compared with the corresponding period in 2008. Net sales for the nine months ended October 3, 2009 decreased \$72.5 million, or 21.5%, compared with the corresponding period in 2008. For the three months ended October 3, 2009, net sales by our Lasers Division decreased \$10.2 million, or 22.8%, and net sales by our PPT Division decreased \$6.5 million, or 10.7%, compared with the prior year period. For the nine months ended October 3, 2009, net sales by our Lasers Division decreased \$34.6 million, or 24.4%, and net sales by our PPT Division decreased \$37.9 million, or 19.4%, compared with the prior year period. We experienced decreases in net sales during the three and nine months ended October 3, 2009 compared with the corresponding periods of 2008 in all of our end markets, other than sales to the scientific research end market in the third quarter of 2009, which were approximately the same as the prior year period. These decreases resulted primarily from continued poor worldwide macroeconomic conditions and the ongoing cyclical downturn in the semiconductor equipment industry.

Net sales to the scientific research, aerospace and defense/security markets for the three months ended October 3, 2009 were approximately equal to our net sales to these markets in the same period in 2008. Net sales to these markets for the nine months ended October 3, 2009 decreased \$4.8 million, or 4.5%, compared with the same period in 2008.

In the third quarter of 2009, we experienced lower sales to these markets in our existing businesses compared with the

same period in 2008, which were offset by the addition of sales to these markets by the New Focus business following its acquisition on July 4, 2009. The decrease in sales to these markets during the nine months ended October 3, 2009 compared with the prior year period was due primarily to decreased sales to research customers, including universities, resulting from lower funding from governmental entities, corporations and private foundations, and decreased sales to defense contractor customers, offset in part by additional sales from the New Focus business. Generally, our net sales to these markets by each of our divisions may fluctuate from period to period due to changes in overall research and defense spending levels and the timing of large sales relating to major research and aerospace/defense programs and, in some cases, these fluctuations may be offsetting between our divisions or between such periods.

Net sales to the microelectronics market for the three months ended October 3, 2009 decreased \$10.6 million, or 34.8%, compared with the same period in 2008. Net sales to this market for the nine months ended October 3, 2009 decreased \$44.6 million, or 42.6%, compared with the same period in 2008. The decrease in sales to this market during the three and nine months ended October 3, 2009 compared with the same periods in 2008 was due primarily to a significant decline in sales to our semiconductor manufacturing equipment customers as a result of the severe cyclical downturn in that industry, as well as lower sales of laser-based disk texturing systems, offset in part by the addition of sales from the New Focus Business.

Net sales to the life and health sciences market for the three months ended October 3, 2009 decreased \$1.6 million, or 7.0%, compared with the same period in 2008. Net sales to this market for the nine months ended October 3, 2009 decreased \$1.8 million, or 2.7%, compared with the same period in 2008. The decrease in sales to this market for the three month period in 2009 compared with the same period in 2008 was due primarily to the divestiture of our diode laser operations at the end of the second quarter of 2009. The decrease for the nine month period in 2009 was due to the divestiture of our diode laser operations and to decreased sales of products for bioinstrumentation applications and for cosmetic and other elective treatment applications, offset in part by higher sales of products for bioimaging applications, compared with the same period in 2008.

Net sales to our industrial manufacturing and other end markets for the three months ended October 3, 2009 decreased \$4.5 million, or 25.5%, compared with the same period in 2008. Net sales to these markets for the nine months ended October 3, 2009 decreased \$21.3 million, or 36.9%, compared with the same period in 2008. The decrease in sales to this market during the three and nine months ended October 3, 2009 compared with the same periods in 2008 was due primarily to the continued poor macroeconomic climate worldwide.

Geographically, net sales were as follows:

(In thousands)	Three Months Ended		Decrease	Percentage Decrease
	October 3, 2009	September 27, 2008		
United States	\$ 43,658	\$ 50,869	\$ (7,211)	(14.2)%
Europe	21,804	27,165	(5,361)	(19.7)
Pacific Rim	18,845	21,872	(3,027)	(13.8)
Other	4,010	5,120	(1,110)	(21.7)
	\$ 88,317	\$ 105,026	\$ (16,709)	(15.9)%

(In thousands)	Nine Months Ended		Decrease	Percentage Decrease
	October 3, 2009	September 27, 2008		
United States	\$ 122,935	\$ 157,249	\$ (34,314)	(21.8)%
Europe	69,041	86,982	(17,941)	(20.6)
Pacific Rim	58,421	78,207	(19,786)	(25.3)
Other	14,997	15,495	(498)	(3.2)
	\$ 265,394	\$ 337,933	\$ (72,539)	(21.5)%

The decrease in sales to customers in the United States and Europe during the three and nine months ended October 3, 2009 compared with the corresponding periods in 2008 was due primarily to lower sales to our semiconductor manufacturing equipment and industrial manufacturing customers. The decrease in sales to customers in the Pacific Rim during the three and nine months ended October 3, 2009 compared with the corresponding periods in 2008 was

due primarily to lower sales to our semiconductor manufacturing equipment customers and lower sales of laser-based disk texturing systems.

Gross Margin

Gross margin was 39.9% and 37.7% for the three months ended October 3, 2009 and September 27, 2008, respectively. The increase in gross margin for the current year period was due primarily to the divestiture of our diode laser operations and the impact of our cost reduction actions.

Gross margin was 38.3% and 39.4% for the nine months ended October 3, 2009 and September 27, 2008, respectively. The decrease in gross margin for the nine month period was due primarily to lower overhead absorption resulting from decreased sales and increased inventory reserves, offset in part by lower personnel costs resulting from headcount reductions, improved operating efficiencies at certain facilities as a result of our cost reduction actions and the divestiture of our diode laser operations.

Selling, General and Administrative (SG&A) Expenses

SG&A expenses totaled \$27.9 million, or 31.6% of net sales, and \$28.2 million, or 26.9% of net sales, for the three months ended October 3, 2009 and September 27, 2008, respectively. The decrease in SG&A expenses in absolute dollars in the current year period was due primarily to decreases in professional fees, salary costs, utilities expenses and travel expenses, offset in part by increased incentive compensation costs.

SG&A expenses totaled \$82.1 million, or 31.0% of net sales, and \$88.1 million, or 26.1% of net sales, for the nine months ended October 3, 2009 and September 27, 2008, respectively. The decrease in SG&A expenses in absolute dollars in the current year period was due primarily to decreases in professional fees, travel expenses, personnel costs, shipping costs and advertising costs, offset in part by increased bad debt expense.

In general, we expect that SG&A expense will vary as a percentage of sales in the future based on our sales level in any given period. Because the majority of our SG&A expense is fixed in the short term, changes in SG&A expense will likely not be in proportion to changes in net sales.

Research and Development (R&D) Expense

R&D expense totaled \$9.3 million, or 10.6% of net sales, and \$11.3 million, or 10.8% of net sales, for the three months ended October 3, 2009 and September 27, 2008, respectively. The decrease in R&D expense in the current year period was due primarily to decreased personnel costs in our Lasers Division.

R&D expense totaled \$27.7 million, or 10.4% of net sales, and \$35.1 million, or 10.4% of net sales, for the nine months ended October 3, 2009 and September 27, 2008, respectively. The decrease in R&D expense in absolute dollars in the current year period was due to decreased spending in both our PPT Division and our Lasers Division. The decreased R&D expense in our PPT Division was due primarily to lower spending related to solar cell manufacturing applications, as the design and development of certain products was completed during 2008. The decreased R&D expense in our Lasers Division was due primarily to decreased personnel costs.

We believe that the continued development and advancement of our key products and technologies is critical to our success, and we intend to continue to invest in key R&D initiatives, while working to ensure that the efforts are focused and the resources are deployed efficiently. In general, we expect that R&D expense as a percentage of net sales will vary in the future based on our sales level in any given period. Because of our commitment to continued product development, and because the majority of our R&D expense is fixed in the short term, changes in R&D expense will likely not be in proportion to changes in net sales.

Interest and Other Expense, Net

Interest and other expense, net totaled \$2.0 million and \$2.1 million for the three months ended October 3, 2009 and September 27, 2008, respectively. The improvement in the current year period compared with the 2008 period resulted from a decrease in interest expense due to the extinguishment of \$28 million of our convertible subordinated notes in the fourth quarter of 2008, offset in part by a decrease in interest income earned due to lower interest rates during the current year period.

Interest and other expense, net totaled \$6.3 million and \$5.3 million for the nine months ended October 3, 2009 and September 27, 2008, respectively. Interest expense declined compared with the prior year period due to the extinguishment of \$28 million of our convertible subordinated notes in the fourth quarter of 2008, but this was more than offset by a decrease in interest income earned due to lower interest rates and by an increase in other expense due to currency fluctuations.

Income Taxes

Our effective tax rate for the three months ended October 3, 2009 and September 27, 2008 was a benefit of 15.6% and expense of (83.5)%, respectively. Our effective tax rate for the nine months ended October 3, 2009 and September 27, 2008 was a benefit of 6.6% and an expense of (120.4)%, respectively. The effective tax rate for the three and nine months ended October 3, 2009 reflects income tax expense applicable to certain foreign jurisdictions, income tax benefit for losses incurred in certain foreign jurisdictions, state taxes and refundable research tax credits, offset in part by an allocation of tax expense to other comprehensive income.

Under ASC 740-270, *Income Taxes - Interim Reporting*, we are required to adjust our effective tax rate each quarter to be consistent with the estimated annual effective tax rate and interim period tax. We are also required to record the tax impact of certain unusual or infrequently occurring discrete items, including changes in judgment about valuation allowances and effects of changes in tax laws or rates, in the interim period in which they occur. In addition, jurisdictions for which we have projected losses for the year, or a year-to-date loss, where no tax benefit can be recognized, are excluded from the calculation of the estimated annual effective tax rate. The impact of such an exclusion could result in a higher or lower effective tax rate during a particular quarter, based upon the mix and timing of actual earnings compared with annual projections.

We have maintained a valuation allowance against substantially all of our gross deferred tax assets pursuant to ASC 740-10, *Income Taxes*, due to the uncertainty as to the timing and ultimate realization of those assets. As a result, until such valuation allowance is reversed, the U.S. tax provision relating to future earnings will be offset substantially by a reduction in the valuation allowance. Accordingly, current and future tax expense will consist of taxes in certain foreign jurisdictions, required state income taxes, the federal alternative minimum tax and the impact of discrete items.

As of October 3, 2009, our valuation allowance was \$59.7 million. We will continue to monitor our actual results, refine forecasted data and assess the need for retaining a valuation allowance against a portion of our gross deferred tax assets. In the event it is determined that a valuation allowance is no longer required, substantially all of the reversal will be recorded as a discrete item in the appropriate period.

Liquidity and Capital Resources

Our cash and cash equivalents and marketable securities balances increased to a total of \$150.0 million as of October 3, 2009 from \$148.4 million as of January 3, 2009. This increase was attributable primarily to cash generated from operations, offset in part by capital expenditures primarily related to facility consolidation activities, and cash used in financing activities and in connection with our asset exchange transaction with Oclaro.

Net cash provided by our operating activities of \$13.2 million for the nine months ended October 3, 2009 was attributable primarily to cash provided by our operations and increased collections of accounts and notes receivable, offset in part by purchases of inventory and the timing of payables and other expenses.

Net cash provided by investing activities of \$3.4 million for the nine months ended October 3, 2009 was attributable to net sales of marketable securities of \$14.0 million, offset in part by purchases of property and equipment of \$7.6 million and the \$3.0 million cash payment related to our asset exchange transaction with Oclaro.

Net cash used in financing activities of \$3.7 million for the nine months ended October 3, 2009 was attributable primarily to the repayment of short-term borrowings of \$4.3 million, offset in part by \$0.5 million received as consideration for the issuance of common stock in connection with exercises of stock options and purchases of common stock under our employee stock purchase plan.

During June 2008, we issued 300 million yen (\$3.3 million at October 3, 2009) in private placement bonds through a Japanese bank. These bonds bear interest at a rate of 1.55% per year, payable in cash semiannually in arrears on June 30 and December 31 of each year. The bonds mature on June 30, 2011. The bonds are included in *long-term debt* in the accompanying consolidated balance sheets.

At October 3, 2009, we had a total of three lines of credit, including one domestic revolving line of credit and two revolving lines of credit with Japanese banks. In addition, we had two other agreements with Japanese banks under which we sell trade notes receivable with recourse.

Our domestic revolving line of credit has a total credit limit of \$5.0 million and expires on December 1, 2009. Certain cash equivalents held at this lending institution collateralize this line of credit, which bears interest at either the prevailing London Interbank Offered Rate (LIBOR) (0.24% at October 3, 2009) plus 1.00% or the British Bankers Association LIBOR Daily Floating Rate (0.20% at October 3, 2009) plus 1.00%, at our option, and carries an unused line fee of 0.25% per year. At October 3, 2009, there were no balances outstanding under this line of credit, with \$3.7 million available, after considering outstanding letters of credit totaling \$1.3 million.

Our two revolving lines of credit with Japanese banks totaled 1.1 billion yen (\$12.2 million at October 3, 2009) and expire as follows: \$8.9 million on November 30, 2009 and \$3.3 million on May 31, 2010. The \$8.9 million line of credit bears interest at the prevailing bank rate and the \$3.3 million line of credit bears interest at LIBOR plus 1.75%. Certain cash equivalents held by the lending institution's U.S. affiliate collateralize the \$3.3 million line of credit. At October 3, 2009, we had \$7.9 million outstanding and \$4.3 million available for borrowing under these lines of credit. Amounts outstanding under these revolving lines of credit are included in *short-term obligations* in the accompanying consolidated balance sheets. Our two other agreements with Japanese banks, under which we sell trade notes receivable with recourse, totaled 550 million yen (\$6.1 million at October 3, 2009), have no expiration dates and bear interest at the bank's prevailing rate. At October 3, 2009, we had \$2.0 million outstanding and \$4.1 million available for the sale of notes receivable under these agreements. Amounts outstanding under these agreements are included in *short-term obligations* in the accompanying consolidated balance sheets. As of October 3, 2009, the weighted average effective interest rate on all of our Japanese borrowings, including the private placement bonds, was 2.45%.

In May 2008, our Board of Directors approved a share repurchase program, authorizing the purchase of up to 4.0 million shares of our common stock. Purchases may be made under this program from time to time in the open market or in privately negotiated transactions, and the timing and amount of the purchases will be based on factors including our share price, cash balances, expected cash requirements and general business and market conditions. No purchases were made under this program during the first nine months of 2009. As of October 3, 2009, 3.9 million shares remained available for purchase under the program.

During the fourth quarter of 2009, we expect to use \$2 million to \$5 million of cash for capital expenditures, primarily related to the relocation of our Lasers Division to a new facility, an upgrade of our domestic telecommunications system and the relocation of our manufacturing operations in Wuxi, China.

We believe our current working capital position, together with our expected future cash flows from operations, will be adequate to fund our operations in the ordinary course of business, anticipated capital expenditures, debt payment requirements and other contractual obligations for at least the next twelve months. However, this belief is based upon many assumptions and is subject to numerous risks including those discussed in Item 1A (Risk Factors) of Part I of our Annual Report on Form 10-K for the year ended January 3, 2009, and there can be no assurance that we will not require additional funding in the future.

Except for the aforementioned capital expenditures, we have no present agreements or commitments with respect to any material acquisitions of other businesses, products, product rights or technologies or any other material capital expenditures. However, we will continue to evaluate acquisitions of and/or investments in products, technologies, capital equipment or improvements or companies that complement our business and may make such acquisitions and/or investments in the future. Accordingly, we may need to obtain additional sources of capital in the future to finance any such acquisitions and/or investments. We may not be able to obtain such financing on commercially reasonable terms, if at all. Due to the ongoing global economic crisis, we believe it may be difficult to obtain additional financing if needed. Even if we are able to obtain additional financing, it may contain undue restrictions on our operations, in the case of debt financing, or cause substantial dilution for our stockholders, in the case of equity

financing.

Recent Accounting Pronouncements

In August 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-05, *Measuring Liabilities at Fair Value*, which amends the guidance in ASC 820, *Fair Value Measurements and Disclosures*, to provide guidance on fair value measurement of liabilities. If a quoted price in an active market is not available for an identical liability, ASU 2009-05 requires companies to compute fair value by using quoted prices for an identical liability when traded as an asset, quoted prices for similar liabilities when traded as an asset or another valuation technique that is consistent with the guidance in ASC 820. ASU 2009-05 was effective for interim and annual periods beginning after its issuance and did not have a material impact on our financial position or results of operations.

In October 2009, the FASB issued ASU No. 2009-13, *Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force*, which amends the guidance in ASC 605, *Revenue Recognition*. ASU 2009-13 eliminates the residual method of accounting for revenue on undelivered products and instead, requires companies to allocate revenue to each of the deliverable products based on their relative selling price. In addition, this ASU expands the disclosure requirements surrounding multiple-deliverable arrangements. ASU 2009-13 will be effective for revenue arrangements entered into for fiscal years beginning on or after June 15, 2010. We are currently evaluating the impact that ASU 2009-13 will have on our financial position and results of operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The principal market risks (i.e., the risk of loss arising from adverse changes in market rates and prices) to which we are exposed are foreign currency exchange rates, which may generate translation and transaction gains and losses, and changes in interest rates.

Foreign Currency Risk

Operating in international markets sometimes involves exposure to volatile movements in currency exchange rates. The economic impact of currency exchange rate movements on our operating results is complex because such changes are often linked to variability in real growth, inflation, interest rates, governmental actions and other factors. These changes, if material, may cause us to adjust our financing and operating strategies. Consequently, isolating the effect of changes in currency does not incorporate these other important economic factors.

From time to time we use forward exchange contracts to mitigate the risks associated with certain foreign currency transactions entered into in the ordinary course of business, primarily foreign currency denominated receivables and payables. We do not engage in currency speculation. The forward exchange contracts generally require us to exchange U.S. dollars for foreign currencies at maturity, at rates agreed to at the inception of the contracts. If the counterparties to the exchange contracts (typically highly rated banks) do not fulfill their obligations to deliver the contracted currencies, we could be at risk for any currency related fluctuations. Transaction gains and losses are included in our current net loss in our statements of operations. Net foreign exchange gains and losses were not material to our reported results of operations for the three and nine months ended October 3, 2009. There were no forward exchange contracts outstanding at October 3, 2009.

As currency exchange rates change, translation of the statements of operations of international operations into U.S. dollars affects the year-over-year comparability of operating results. We do not generally hedge translation risks because cash flows from international operations are generally reinvested locally. We do not enter into hedges to minimize volatility of reported earnings because we do not believe it is justified by the exposure or the cost. Changes in currency exchange rates that would have the largest impact on translating our future international operating income include the euro and Japanese yen. We estimate that a 10% change in foreign exchange rates would not have had a material effect on our reported net loss for the three and nine months ended October 3, 2009. We believe that this quantitative measure has inherent limitations because, as discussed in the first paragraph of this section, it does not take into account any governmental actions or changes in either customer purchasing patterns or our financing and operating strategies.

Interest Rate Risk

The interest rates we pay on certain of our debt instruments are subject to interest rate risk. Our collateralized line of credit bears interest at either the prevailing London Interbank Offered Rate (LIBOR) plus 1.00% or the British Bankers Association LIBOR Daily Floating Rate plus 1.00%, at our option. Our \$3.3 million revolving line of credit with a Japanese bank bears interest at LIBOR plus 1.75%. Our other revolving line of credit and other credit agreements with Japanese banks bear interest at the lending bank's prevailing rate. Our convertible subordinated notes and private placement bonds bear interest at a fixed rate of 2.5% and 1.55% per year, respectively, and are not impacted by changes in interest rates. Our cash and marketable securities, which totaled \$150.0 million at October 3, 2009, are sensitive to changes in the general level of U.S. interest rates. In addition, certain assets related to our pension plans that are not owned by such plans, which totaled \$9.2 million at October 3, 2009, are sensitive to interest rates and economic conditions in Europe. We estimate that a 10% change in the interest rate earned on our cash and marketable securities or a 10% change in interest rates payable on our lines of credit would not have had a material effect on our net loss for the three and nine months ended October 3, 2009.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and our Chief Financial Officer, after evaluating our disclosure controls and procedures (as defined in Securities Exchange Act of 1934 (the Exchange Act) Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-Q (the Evaluation Date), have concluded that as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our chief executive officer and chief financial officer where appropriate, to allow timely decisions regarding required disclosure.

(b) Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. We continue to enhance our internal control over financial reporting, primarily by evaluating and enhancing our process and control documentation, in connection with our ongoing efforts to meet the requirements of Section 404 of the Sarbanes-Oxley Act of 2002. We discuss with and disclose these matters to the Audit Committee of our Board of Directors and our independent registered public accounting firm.

PART II OTHER INFORMATION

Item 1A. Risk Factors

Our Annual Report on Form 10-K for the year ended January 3, 2009 contains a full discussion of the risks associated with our business. There have been no material changes to the risks described in our Annual Report on Form 10-K.

Item 6. Exhibits

Exhibit Number	Description of Exhibit
31.1	Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 (the Exchange Act).
31.2	Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act.
32.1	Certification pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Exchange Act and 18 U.S.C. Section 1350.
32.2	Certification pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Exchange Act and 18 U.S.C. Section 1350.

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.

Dated: November 12, 2009

NEWPORT CORPORATION

By: */s/ Charles F. Cargile*
Charles F. Cargile,
Senior Vice President, Chief Financial
Officer and Treasurer (Principal
Financial Officer and Duly Authorized
Officer)

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