COHERENT INC
Form 10-Q/A
August 17, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

Amendment No. 1

(Mark One)

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

For the Quarterly Period Ended April 2, 2005

or

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

For the transition period from to

Commission File Number: 0-5255

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 ý No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ý No o

The number of shares outstanding of registrant s common stock, par value $.01 per share, at May 3, 2005 was 30,789,822 shares.

EXPLANATORY NOTE

This Quarterly Report on Form 10-Q/A (Form 10-Q/A) is being filed as Amendment No. 1 to our Quarterly Report on Form 10-Q for the quarterly period ended April 2, 2005, which was filed with the Securities and Exchange Commission (SEC) on May 17, 2005 (the Original Filing). We are filing this Amendment No. 1 to correct the pro forma amounts reported for stock based compensation determined under the fair value based method for the three and six month periods ended April 2, 2005. This correction had no impact on our consolidated balance sheets, results of operations or cash flows for any of the periods presented. For a more detailed description of the restatement, see Restatements in Note 15 of the Notes to Condensed Consolidated Financial Statements.

This Form 10-Q/A amends and restates Item 1. Financial Statements, Item 2. Management s Discussion and Analysis of Results of Operations and Financial Condition and Item 4. Controls and Procedures of Part I of the Original Filing, as amended, solely as a result of, and to reflect, the restatement. Pursuant to the rules of the SEC, we have included currently-dated certifications from our principal executive officer and principal financial officer, as required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002. The certifications of our principal executive officer and our principal financial officer are attached to this form 10-Q/A as Exhibits 31.1, 31.2, 32.1 and 32.2.

Except for the amended information described above, this Form 10-Q/A continues to describe conditions as of the date of the Original Filing, and we have not updated the disclosures contained herein to reflect events that have occurred subsequent to that date. Other events occurring after the date of the Original Filing or other information necessary to reflect subsequent events have been disclosed in reports filed with the SEC subsequent to the Original Filing.

COHERENT, INC.

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PART I. FINANCIAL INFORMATION

Item I. Financial Statements

COHERENT, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited; in thousands, except per share data)

	Three Months Ended		Six Months Ended	
	April 2, 2005	**April 3, 2004 (as restated, see note 15)**	**April 2, 2005**	**April 3, 2004 (as restated, see note 15)**
Net sales	**$ 131,175**	$ 125,808	**$ 257,197**	$ 233,759
Cost of sales	**72,688**	74,269	**147,173**	140,919
Gross profit	**58,487**	51,539	**110,024**	92,840
Operating expenses:				
Research and development	**14,175**	15,593	**28,476**	30,710
Selling, general and administrative	**28,765**	29,517	**57,137**	56,968
Restructuring, impairment and other charges (recoveries)	**(40)**		**260**	237
Intangibles amortization	**1,528**	1,770	**3,021**	3,699
Total operating expenses	**44,428**	46,880	**88,894**	91,614
Income from operations	**14,059**	4,659	**21,130**	1,226
Other income (expense):				
Interest and dividend income	**1,081**	618	**2,048**	1,338
Interest expense	**(483)**	(795)	**(1,370)**	(1,643)
Foreign exchange gain	**311**	420	**242**	817
Other net	**(119)**	165	**777**	2,161
Total other income, net	**790**	408	**1,697**	2,673
Income from continuing operations before income taxes and minority interest	**14,849**	5,067	**22,827**	3,899
Provision (benefit) for income taxes	**(4,728)**	2,418	**(1,958)**	1,359
Income from continuing operations before minority interest	**19,577**	2,649	**24,785**	2,540
Minority interest in subsidiaries losses		145	**180**	478
Income from continuing operations	**19,577**	2,794	**24,965**	3,018
Discontinued operations, net of income taxes of $145		218		218
Net income	**$ 19,577**	$ 3,012	**$ 24,965**	$ 3,236
Net income per basic share:				
Income from continuing operations	**$ 0.64**	$ 0.09	**$ 0.82**	$ 0.10
Income from discontinued operations, net of income taxes		0.01		0.01
Net income	**$ 0.64**	$ 0.10	**$ 0.82**	$ 0.11
Net income per diluted share:				

Income from continuing operations	**$**	**0.63**	$	0.09	**$**	**0.81**	$	0.10
Income from discontinued operations, net of income taxes				0.01				0.01
Net income	**$**	**0.63**	$	0.10	**$**	**0.81**	$	0.11
Shares used in computation								
Basic		**30,628**		30,121		**30,555**		30,061
Diluted		**31,112**		30,551		**30,991**		30,442

See Accompanying Notes to Condensed Consolidated Financial Statements

COHERENT, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited; in thousands, except par value)

	April 2, 2005	October 2, 2004
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 99,002**	$ 87,659
Restricted cash, cash equivalents and short-term investments	**15,411**	15,343
Short-term investments	**113,493**	83,075
Accounts receivable net of allowances of $4,365 and $3,745, respectively	**90,301**	96,825
Inventories	**108,907**	104,698
Prepaid expenses and other assets	**19,541**	19,350
Deferred tax assets	**36,413**	43,222
Total current assets	**483,068**	450,172
Property and equipment, net	**162,455**	166,054
Restricted cash, cash equivalents and short-term investments	**16,545**	23,580
Goodwill	**58,612**	53,104
Intangible assets, net	**33,693**	35,454
Other assets	**43,669**	28,962
	$ 798,042	$ 757,326
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current portion of long-term obligations	**$ 13,360**	$ 13,700
Accounts payable	**17,226**	17,648
Income taxes payable	**7,997**	9,603
Other current liabilities	**66,589**	63,578
Total current liabilities	**105,172**	104,529
Long-term obligations	**13,961**	14,215
Other long-term liabilities	**52,613**	49,128
Minority interest in subsidiaries		5,402
Commitments and contingencies (Note 10)		
Stockholder s equity:		
Common stock, par value $.01:		
Authorized 500,000 shares		
Outstanding 30,766 shares and 30,392 shares, respectively	**306**	302
Additional paid-in capital	**316,516**	308,236
Notes receivable from stock sales	**(689)**	(758)
Accumulated other comprehensive income	**45,442**	36,516
Retained earnings	**264,721**	239,756
Total stockholders equity	**626,296**	584,052
	$ 798,042	$ 757,326

See Accompanying Notes to Condensed Consolidated Financial Statements.

COHERENT, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited; in thousands)

	Six Months Ended	
	April 2, 2005	**April 3, 2004 (as restated, see note 15)**
Cash flows from continuing operating activities:		
Income from continuing operations	**$ 24,965**	$ 3,018
Adjustments to reconcile income from continuing operations to net cash provided by continuing operating activities:		
Depreciation and amortization	**14,413**	15,306
Intangible assets amortization	**3,021**	3,699
Deferred income taxes	**(2,794)**	7,312
Other	**659**	423
Changes in operating assets and liabilities:		
Accounts receivable	**8,513**	(14,503)
Inventories	**(3,270)**	(1,302)
Prepaid expenses and other assets	**(1,609)**	2,102
Other assets	**655**	(616)
Accounts payable	**(735)**	2,746
Income taxes payable	**93**	19,649
Other current liabilities	**3,500**	(5,342)
Other long-term liabilities	**1,293**	(585)
Net cash provided by continuing operating activities	**48,704**	31,907
Cash flows from continuing investing activities:		
Decrease in restricted cash, cash equivalents and short-term investments	**8,411**	616
Purchases of property and equipment	**(7,945)**	(33,474)
Proceeds from dispositions of property and equipment and assets held for sale	**214**	1,234
Acquisition of businesses and minority interests, net of cash acquired	**(12,129)**	(2,471)
Consolidation of Picometrix under FIN 46R		251
Purchases of available-for-sale securities	**(196,211)**	(146,514)
Proceeds from sales and maturities of available-for-sale securities	**165,793**	146,622
Premiums paid on life insurance	**(1,184)**	(366)
Distributions from deferred compensation plan arrangements		408
Other net	**(554)**	(407)
Net cash used in continuing investing activities	**(43,605)**	(34,101)
Cash flows from continuing financing activities:		
Long-term debt payments	**(745)**	(771)
Cash overdrafts increase (decrease)	**(520)**	2,829
Sales of shares under employee stock plans	**7,285**	4,441
Collection of notes receivable from stock sales	**69**	
Net cash provided by continuing financing activities	**6,089**	6,499
Net cash provided by discontinued operating activities		218
Effect of exchange rate changes on cash and cash equivalents	**155**	2,006
Net increase in cash and cash equivalents	**11,343**	6,529
Cash and cash equivalents, beginning of period	**87,659**	76,541
Cash and cash equivalents, end of period	**$ 99,002**	$ 83,070
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		

Interest	**$**	**1,143**	$	1,643
Income taxes	**$**	**3,140**	$	4,466
Cash received during the period for:				
Income taxes	**$**	**2,074**	$	27,869
Noncash investing and financing activities:				
Tax benefit from stock option exercises	**$**	**958**	$	495

See Accompanying Notes to Condensed Consolidated Financial Statements

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 generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations. These interim condensed consolidated financial statements and notes should be read in conjunction with our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K/A for the fiscal year ended October 2, 2004, as amended. All adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

Stock-Based Compensation

As permitted under Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (SFAS 123), we have elected to account for stock-based compensation awards issued to employees using the intrinsic value measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees (APB 25). Accordingly, no compensation expense has been recorded for stock options granted with exercise prices greater than or equal to the fair value of the underlying common stock at the option grant date.

SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure, an Amendment of FASB Statement No. 123 (SFAS 148) amends the disclosure requirements of SFAS 123 to require more prominent disclosures in both annual and interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS 123 requires the disclosure of pro forma net income and earnings per share as if we had adopted the fair value method. Under SFAS 123, the fair value of stock-based awards to employees is calculated through the use of option pricing models, even though such models were developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differ from our stock option awards. These models also require subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated values. For purposes of estimating the effect of SFAS 123 on our net income the fair value of our options was estimated at the grant date using the Black-Scholes option pricing model with the following weighted average assumptions:

Employee Stock Option Plans		Employee Stock Purchase Plans	
Three Months Ended	**Six Months Ended**	**Three Months Ended**	**Six Months Ended**

	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004
Expected life in years	4.2	4.4	4.0	4.4	0.5	0.5	0.5	0.5
Expected volatility	49.5%	74.1%	50.1%	74.1%	37.5%	44.5%	38.2%	44.7%
Risk-free interest rate	4.1%	2.8%	3.7%	2.8%	2.2%	1.3%	2.1%	1.3%
Expected dividends	none	none	none	none	none	none	none	none

Our calculations are based on a single option valuation approach and forfeitures are recognized as they occur. During the periods presented, we recorded no compensation expense under APB 25. The following table illustrates the effect on our net income and earnings per share had we applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation (in thousands, except per share data):

	Three Months Ended		Six Months Ended	
	April 2, 2005 (as restated, see note 15)	April 3, 2004	April 2, 2005 (as restated, see note 15)	April 3, 2004
Net income, as reported	$ 19,577	$ 3,012	$ 24,965	$ 3,236
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards, net of income taxes	2,961	2,532	6,883	669
Pro forma net income	$ 16,616	$ 480	$ 18,082	$ 2,567
Earnings per share:				
Basic as reported	$ 0.64	$ 0.10	$ 0.82	$ 0.11
Basic pro forma	$ 0.54	$ 0.02	$ 0.59	$ 0.09
Diluted as reported	$ 0.63	$ 0.10	$ 0.81	$ 0.11
Diluted pro forma	$ 0.53	$ 0.02	$ 0.58	$ 0.08

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R). SFAS 123R eliminates the alternative of applying the intrinsic value measurement provisions of APB 25 to stock compensation awards issued to employees. Rather, the new standard requires enterprises to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award, known as the requisite service period (usually the vesting period). On April 14, 2005, the Securities and Exchange Commission (SEC) announced the adoption of a rule that defers the required effective date of SFAS 123R. The SEC rule provides that SFAS 123R is now effective for registrants as of the beginning of their first fiscal year beginning after June 15, 2005.

We have not yet quantified the effects of the adoption of SFAS 123R, but it is expected that the new standard may result in significant stock-based compensation expense. The pro forma effects on net income and earnings per share if we had applied the fair value recognition provisions of original SFAS 123 on stock compensation awards (rather than applying the intrinsic value measurement provisions of APB 25) are disclosed above. Although such pro forma effects of applying original SFAS 123 may be indicative of the effects of adopting SFAS 123R, the provisions of these two statements differ in some important aspects. The actual effects of adopting SFAS 123R will be dependent on numerous factors including, but not limited to, the valuation model chosen by us to value stock-based awards; the assumed award forfeiture rate; the accounting policies adopted concerning the method of recognizing the fair value of awards over the requisite service period; and the transition method (as described below) chosen for adopting SFAS 123R.

SFAS 123R will be effective for our fiscal quarter beginning October 2, 2005, and allows for the use of the Modified Prospective Application Method. Under this method, SFAS 123R is applied to new awards and to awards modified, repurchased, or cancelled after the effective date. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered (such as unvested options) that are outstanding as of the date of adoption shall be recognized as the remaining requisite services are rendered. The compensation cost relating to unvested awards at the date of adoption shall be based on the grant-date fair value of those awards as calculated for pro forma disclosures under the original SFAS 123. In addition, companies may use the Modified Retrospective Application Method. This method may be applied to all prior years for which the original SFAS 123 was effective or only to prior interim periods in the year of initial adoption. If the Modified Retrospective Application Method is applied, financial statements for prior periods shall be adjusted to give effect to the fair-value-based method of accounting for awards on a consistent basis with the pro forma disclosures required for those periods under the original SFAS 123. We have not yet determined which method we will apply upon our adoption of SFAS 123R.

2. ACQUISITIONS

On June 3, 2003, we initiated a tender offer to purchase the 5,250,000 (39.62%) outstanding shares of our Lambda Physik subsidiary owned by other shareholders (the minority interest) for approximately $10.50 per share. Through the end of fiscal 2004, we had purchased a total of 4,588,500 outstanding shares for approximately $49.0 million, resulting in a total ownership percentage of 95.01% (inclusive of shares previously owned). During the six months ended April 2, 2005, we acquired the remaining 661,500 outstanding shares for approximately $11.8 million, resulting in our full ownership of Lambda Physik.

The difference between the purchase price of the minority interest of $12.2 million (including acquisition costs of $0.4 million) and the related carrying value of $6.3 million was recorded as an adjustment of the carrying value of the assets of Lambda Physik (the step acquisition adjustment). The step acquisition adjustment was recorded based on the proportion of the remaining minority interest acquired and was accounted for as follows (in thousands):

Reduction in carrying value of minority interest acquired	$	6,267
Tangible assets		133
Goodwill		4,970
Deferred tax liabilities		(808)
Intangible assets:		
Existing technology		1,085
Trade name		367
Backlog		161
Other		13
Total	$	12,188

At April 2, 2005, we had $1.4 million remaining in an escrow account that will be applied towards remaining close out costs for the acquisition and is included in non-current restricted cash, cash equivalents and short-term investments on our condensed consolidated balance sheet (see Note 6).

3. SIGNIFICANT EVENTS

In December 2004, our Lambda Physik subsidiary decided to discontinue future product development and investments in the semiconductor lithography market. As a result, during the six months ended April 2, 2005, we recognized a charge of $2.7 million (net of minority interest of $0.1 million) primarily related to recognizing write-downs of excessive and obsolete inventories, exiting certain purchase commitments and charges related to government grants. Of the $2.7 million charge, $2.2 million was classified as cost of sales; $0.2 million was classified as research and development; $0.1 million was classified as selling, general and administrative; and $0.2 million was classified as other expense.

4. RECENT ACCOUNTING STANDARDS

In November 2004, the Financial Accounting Standards Board issued SFAS No. 151, Inventory Costs (SFAS 151), an amendment of Accounting Research Bulletin No. 43, Chapter 4. SFAS 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material. SFAS 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not believe that the adoption of SFAS 151 will have a material effect on our results of operations or consolidated financial position.

In March 2005, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143 (FIN 47). FIN 47 clarifies that conditional asset retirement obligations meet the definition of liabilities and should be recognized when incurred if their fair values can be reasonably estimated. The Interpretation is effective no later than December 31, 2005 and the cumulative effect of initially applying FIN 47 will be recognized as a change in accounting principle. We are in the process of evaluating the expected effect of FIN 47 on our consolidated financial statements.

5. REVENUE RECOGNITION

We recognize revenue when all four revenue recognition criteria have been met: persuasive evidence of an arrangement exists, the product has been delivered or the service has been rendered, the price is fixed or determinable and collection is probable. Revenue from product sales is recorded when all of the foregoing conditions are met and risk of loss and title passes to the customer. Our products typically include a one-year warranty and the estimated cost of product warranty claims (based on historical experience) is recorded at the time the sale is recognized. Sales to customers are generally not subject to any price protection or return rights.

The vast majority of our sales are made to original equipment manufacturers (OEMs), distributors, resellers and end-users in the non-scientific market. Sales made to these customers do not require installation of the products by us and are not subject to other post-delivery obligations, except in occasional instances where we have agreed to perform installation or provide training. In those instances, we defer revenue related to installation services or training until these services have been rendered. We allocate revenue from multiple element arrangements to the various elements based upon relative fair values, which is determined based on the price charged for each deliverable on a standalone basis, except for certain products sold in the scientific market for which the fair value of installation is determined based on third party evidence of fair value.

Our sales to distributors, resellers and end-user customers typically do not have customer acceptance provisions and only certain of our sales to OEM customers have customer acceptance provisions. Customer acceptance is generally limited to performance under our published product specifications. For the few product sales that have customer acceptance provisions because of higher than published specifications, (1) the products are tested and accepted by the customer at our site or by the customer s acceptance of the results of our testing program prior to shipment to the customer, or (2) the revenue is deferred until customer acceptance occurs.

Sales to end-users in the scientific market typically require installation and, thus, involve post-delivery obligations, however our post-delivery installation obligations are not essential to the functionality of our products. We defer revenue related to installation services until completion of these services.

For most products, training is not provided and, thus, no post-delivery training obligation exists. However, when training is provided to our customers, it is typically priced separately and is recognized as revenue after these services have been provided.

6. 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. Marketable short-term investments in debt and equity securities are classified and accounted for as available-for-sale securities and are valued based on quoted market prices. Investments classified as available-for-sale are reported at fair value with unrealized gains and losses, net of related tax, 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):

	April 2, 2005			
	Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash and cash equivalents	$ 110,811	$	$	$ 110,811
Less: restricted cash and cash equivalents				(11,809)
				$ 99,002
Short-term investments:				
Available-for-sale securities:				
Commercial paper	$ 5,780	$ 1	$	$ 5,781
Certificates of deposit	900	13		913
U.S. government and agency obligations	70,367	519	(156)	70,730
State and municipal obligations	34,857	383	(73)	35,167
Corporate notes and obligations	20,958	185	(94)	21,049
Total short-term investments	$ 132,862	$ 1,101	$ (323)	133,640
Less: restricted short term-investments				(20,147)
				$ 113,493

	October 2, 2004			
	Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash and cash equivalents	$ 96,567	$	$	$ 96,567
Less: restricted cash and cash equivalents				(8,908)
				$ 87,659
Short-term investments:				
Available-for-sale securities:				
Commercial paper	$ 4,838	$	$ (1)	$ 4,837
Certificates of deposit	1,150	5	(1)	1,154
U.S. government and agency obligations	71,440	134	(5)	71,569
State and municipal obligations	22,742	153	(47)	22,848
Corporate notes and obligations	12,665	49	(32)	12,682
Total short-term investments	$ 112,835	$ 341	$ (86)	113,090
Less: restricted short term-investments				(30,015)
				$ 83,075

At April 2, 2005, $1.4 million of cash and cash equivalents were restricted for remaining close out costs related to the purchase of the shares of Lambda Physik (see Note 2), $10.2 million were restricted pursuant to our Star notes agreement (see Note 9) and $0.2 million were restricted for other purposes. In addition, $20.2 million of short-term investments were restricted pursuant to our Star notes agreement. At October 2, 2004,

$8.4 million of cash and cash equivalents were restricted for the purchase of the remaining outstanding shares of Lambda Physik, $0.4 million were restricted pursuant to our Star notes agreement and $0.1 million were restricted for other purposes. Additionally, at October 2, 2004, $30.0 million of short-term investments were restricted pursuant to our Star notes agreement.

The amortized cost and estimated fair value of available-for-sale investments in debt securities at April 2, 2005 and October 2, 2004, classified as short-term investments (including restricted amounts) on our condensed consolidated balance sheets were as follows (in thousands):

	April 2, 2005		October 2, 2004	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in less than 1 year	$ 100,991	$ 101,707	$ 101,708	$ 101,979
Due in 1 to 5 years	31,169	31,230	10,282	10,265
Due in 5 to 10 years				
Due beyond 10 years	702	703	845	846
Total investments in available-for-sale debt securities	$ 132,862	$ 133,640	$ 112,835	$ 113,090

In the first six months of fiscal 2005, we received proceeds totaling $11.0 million from the sale of available-for-sale securities and realized gross losses of $0.1 million. In the first six months of fiscal 2004, we received proceeds totaling $30.0 million from the sale of available-for-sale securities and realized gross gains and gross losses of $0.1 million and $0.1 million, respectively.

7. GOODWILL AND OTHER INTANGIBLE ASSETS

The carrying amount of goodwill attributable to each reporting segment is as follows (in thousands):

	April 2, 2005	October 2, 2004
Electro-Optics	$ 35,427	$ 35,270
Lambda Physik	23,185	17,834
Total	$ 58,612	$ 53,104

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

	April 2, 2005			October 2, 2004		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Existing technology	$ 37,491	$ 11,898	$ 25,593	$ 36,746	$ 10,018	$ 26,728
Patents	9,386	4,270	5,116	9,005	3,699	5,306
Licenses	4,261	4,261		4,261	4,047	214
Drawings	1,263	1,009	254	1,214	850	364
Order backlog	2,222	2,157	65	1,990	1,990	
Customer lists	2,093	1,114	979	2,106	992	1,114
Trade name	1,776	481	1,295	1,608	417	1,191
Non-compete agreement	928	537	391	911	374	537
Total	$ 59,420	$ 25,727	$ 33,693	$ 57,841	$ 22,387	$ 35,454

Amortization expense for intangible assets for the three and six months ended April 2, 2005 were $1.5 million and $3.0 million, respectively. At April 2, 2005, estimated amortization expense for the remainder of fiscal 2005, the next five succeeding fiscal years and all years thereafter are as follows (in thousands):

		Estimated Amortization Expense
2005 (remainder)	$	2,932
2006		5,392
2007		4,960
2008		4,801
2009		4,562
2010		3,573
Thereafter		7,473
Total	$	33,693

8. BALANCE SHEET DETAILS:

Inventories are as follows (in thousands):

	April 2, 2005	October 2, 2004
Purchased parts and assemblies	$ 25,221	$ 28,097
Work-in-process	50,088	44,070
Finished goods	33,598	32,531
Inventories	$ 108,907	$ 104,698

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

	April 2, 2005	October 2, 2004
Prepaid expenses and other	$ 18,381	$ 16,812
Prepaid and refundable income taxes	1,160	2,538
Total prepaid expenses and other assets	$ 19,541	$ 19,350

Other assets consist of the following (in thousands):

	April 2, 2005	October 2, 2004
Deferred tax assets	$ 20,206	$ 6,644
Assets related to deferred compensation arrangements	18,010	17,095
Other assets	5,453	5,223
Total other assets	$ 43,669	$ 28,962

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

	April 2, 2005	October 2, 2004
Accrued payroll and benefits	$ 22,889	$ 26,532
Accrued expenses and other	18,967	14,130
Reserve for warranty	11,875	10,638
Customer deposits	4,720	4,488
Deferred income	4,518	3,838
Accrued restructuring charges	3,620	3,952
Total other current liabilities	$ 66,589	$ 63,578

We provide warranties on certain of our product sales (generally one year) and allowances for estimated warranty costs are recorded during the period of sale. The determination of such allowances 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. If actual return rates and/or repair and replacement costs differ significantly from our estimates, adjustments to recognize additional cost of sales may be required in future periods.

Components of the reserve for warranty costs during the first six months of fiscal 2005 and 2004 were as follows (in thousands):

	April 2, 2005	April 3, 2004
Beginning balance	$ 10,638	$ 10,242
Additions related to current period sales	7,126	11,580
Warranty costs incurred in the current period	(6,154)	(10,289)
Adjustments to accruals related to prior period sales	265	(116)
Ending balance	$ 11,875	$ 11,417

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

	April 2, 2005	October 2, 2004
Deferred compensation	$ 22,179	$ 20,500
Deferred tax liabilities	22,320	21,223
Deferred income	3,152	2,930
Environmental remediation costs	409	431
Other long-term liabilities	4,553	4,044
Total other long-term liabilities	$ 52,613	$ 49,128

9. CURRENT AND LONG TERM OBLIGATIONS

At April 2, 2005 and October 2, 2004, our current and long-term obligations primarily consisted of our notes payable to finance our acquisition of Star Medical (Star notes). The Star notes agreement requires that we place cash and short-term investment balances in an amount equal to 120% of the principal balance in a restricted collateral account. At April 2, 2005, $15.2 million of current and $15.2 million of non-current restricted cash, cash equivalents and short-term investments were related to the Star notes (see Note 6).

10. COMMITMENTS AND CONTINGENCIES

Certain claims and lawsuits have been filed or are pending against us. In the opinion of management, all such matters have been adequately provided for, are without merit, or are of such kind that if disposed of unfavorably, would not have a material adverse effect on our consolidated financial position or results of operations.

11. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income, net of income taxes, are as follows (in thousands):

	Three Months Ended		Six Months Ended	
	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004
Net income	$ 19,577	$ 3,012	$ 24,965	$ 3,236
Translation adjustment	(6,762)	(648)	9,134	14,622
Net loss on derivative instruments	(47)	(14)	(28)	(12)
Changes in unrealized gain (loss) on available-for-sale securities	(108)	51	(180)	71
Total comprehensive income	$ 12,660	$ 2,401	$ 33,891	$ 17,917

The following summarizes activity in accumulated other comprehensive income (loss) related to derivatives, net of income taxes, held by us (in thousands):

Balance, September 27, 2003	$	(128)
Changes in fair value of derivatives		(14)
Net losses reclassified from OCI		2
Balance, April 3, 2004	$	(140)
Balance, October 2, 2004	$	(122)
Changes in fair value of derivatives		
Net losses reclassified from OCI		(28)
Balance, April 2, 2005	$	(150)

Accumulated other comprehensive income (net of tax) at April 2, 2005 is comprised of accumulated translation adjustments of $45.9 million, net loss on derivative instruments of $0.2 million and unrealized loss on available-for-sale securities of $0.3 million, respectively. Accumulated other comprehensive income (net of tax) at October 2, 2004 is comprised of accumulated translation adjustments of $36.7 million, net loss on derivative instruments of $0.1 million and unrealized loss on available-for-sale securities of $0.1 million, respectively.

12. EARNINGS PER SHARE

Basic earnings per share is computed based on the weighted average number of shares outstanding during the period. Diluted earnings per share is computed based on the weighted average number of shares outstanding during the period increased by the effect of dilutive stock options and stock purchase contracts using the treasury stock method and shares issuable under the Productivity Incentive Plan.

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

	Three Months Ended		Six Months Ended	
	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004
Weighted average shares outstanding basic	30,628	30,121	30,555	30,061
Common stock equivalents	449	402	404	357
Employee stock purchase plan equivalents	35	28	32	24
Weighted average shares and equivalents diluted	31,112	30,551	30,991	30,442
Income from continuing operations for basic and diluted earnings per share computation	$ 19,577	$ 2,794	$ 24,965	$ 3,018
Income from continuing operations per share basic	$ 0.64	$ 0.09	$ 0.82	$ 0.10
Income from continuing operations per share diluted	$ 0.63	$ 0.09	$ 0.81	$ 0.10

A total of 2,623,000 and 3,067,000 potentially dilutive securities have been excluded from the dilutive share calculation for the three months ended April 2, 2005 and April 3, 2004, respectively, as their effect was anti-dilutive. A total of 2,709,000 and 3,192,000 anti-diluted weighted shares have been excluded from the dilutive share calculation for the six months ended April 2, 2005 and April 3, 2004, respectively, as their effect was anti-dilutive.

13. INCOME TAXES

During the second quarter of fiscal 2005, we recorded a reduction of $10.2 million of valuation allowance on Lambda Physik s deferred tax assets as we believe that it is more likely than not that we will be able to realize these assets. In accordance with SFAS No. 109 Accounting for Income Taxes, $0.6 million of the reversal was applied against goodwill recognized from the final step acquisition (see Note 2). The remaining $9.6 million of the reversal was recorded as a tax benefit during the quarter ended April, 2, 2005.

14. SEGMENT INFORMATION

We are organized around two separately managed segments: Electro-Optics and Lambda Physik, which we have identified as operating segments. Our Electro-Optics segment focuses on markets such as semiconductor and related manufacturing, materials processing, OEM laser components and instrumentation, scientific research and government programs, and graphic arts and display. Our Lambda Physik segment focuses on markets including lasers for the production of thin film transistors (TFT) used in flat panel displays, ink jet printers, automotive, environmental research, scientific research, medical OEMs, materials processing and micro-machining applications.

Our Chief Executive Officer and Chief Financial Officer have been identified as the chief operating decision makers (CODMs) for SFAS 131, Disclosures about Segments of an Enterprise and Related Information purposes as they assess the performance of the business units and decide how to allocate resources to the business units. Pretax income from continuing operations is the measure of profit and loss that our CODMs use to assess performance and make decisions. Pretax income from continuing operations represents the sales less the cost of sales and direct operating expenses incurred within the operating segments. In addition, our corporate expenses, except for depreciation of corporate assets and general legal expenses, are allocated to the operating segments and are included in the results below. Corporate expenses not allocated to the groups (depreciation of corporate assets and general legal expenses) are included in Corporate and Other in the reconciliation of operating results. Furthermore, interest expense, interest income and gains and losses on our deferred compensation plan assets are included in Corporate and Other in the reconciliation of operating results.

	Three Months Ended		Six Months Ended	
	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004
		(in thousands)		
Net sales:				
Electro-Optics	$ 105,383	$ 103,946	$ 206,282	$ 194,569
Lambda Physik	25,792	21,862	50,915	39,190
Total net sales	$ 131,175	$ 125,808	$ 257,197	$ 233,759
Intersegment net sales:				
Electro-Optics	$	$ 84	$ 7	$ 89
Lambda Physik	1,019	268	1,408	338
Total intersegment sales	$ 1,019	$ 352	$ 1,415	$ 427
Income from continuing operations before income taxes, including tax-effected minority interest:				
Electro-Optics	$ 12,719	$ 8,244	$ 22,730	$ 11,389
Lambda Physik	1,916	(3,490)	(2,025)	(9,173)
Corporate and other	214	458	2,302	2,161
Total income from continuing operations before income taxes, including tax-effected minority interest	$ 14,849	$ 5,212	$ 23,007	$ 4,377

15. RESTATEMENTS

Deferred Compensation Plans

Subsequent to the issuance of our condensed consolidated financial statements for the three and six months ended April 3, 2004, we identified errors in the accounting for our deferred compensation plans. In 1999, we amended our non-qualified deferred compensation plan (Plan) and introduced a new investment structure whereby the then existing and future contributions to the Plan were funded in Company-owned life insurance contracts. Since the change in investment structure to Company-owned life insurance contracts, we accounted for the Plan by recording the participants balances as a liability equal to the obligation to the participants and the related asset investments in the equivalent amount. As a result of a review of the accounting for the Plan in connection with a change to a new third-party administrator, we determined that the asset investments should have been recorded at the cash surrender value of the insurance contracts. Further, life insurance premiums loads, policy fees, and cost of insurance that were paid from the asset investments and gains and losses from the asset investments for this and one other deferred compensation plan should have been recorded as components of other income or expenses; and increases in the obligation to the participants should have been recorded as operating expenses.

As a result, the accompanying condensed consolidated financial statements for the three and six month periods ended April 3, 2004 have been restated from the amounts previously reported to correct these errors.

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The following is a summary of the significant effects of the restatement:

	Three Months Ended April 3, 2004			Six Months Ended April 3, 2004		
	As Previously Reported	Adjustments	As Restated	As Previously Reported	Adjustments	As Restated
	(in thousands, except per share data)					
Condensed Consolidated Statements of Operations Data						
Cost of sales	$ 74,235	$ 34	$ 74,269	$ 140,752	$ 167	$ 140,919
Gross profit	51,573	(34)	51,539	93,007	(167)	92,840
Research and development	15,538	55	15,593	30,459	251	30,710
Selling, general and administrative	29,132	385	29,517	55,090	1,878	56,968
Total operating expense	46,440	440	46,880	89,485	2,129	91,614
Income from operations	5,133	(474)	4,659	3,522	(2,296)	1,226
Other-net	(69)	234	165	80	2,081	2,161
Total other income (expense), net	174	234	408	592	2,081	2,673
Income from continuing operations before income taxes and minority interest	5,307	(240)	5,067	4,114	(215)	3,899
Provision (benefit) for income taxes	2,567	(149)	2,418	2,013	(654)	1,359
Income from continuing operations before minority interest	2,740	(91)	2,649	2,101	439	2,540
Income from continuing operations	2,885	(91)	2,794	2,579	439	3,018
Net income	3,103	(91)	3,012	2,797	$ 439	3,236
Net Income Per Share						
Basic:						
Income from continuing operations	$ 0.09	$	$ 0.09	$ 0.08	$ 0.02	$ 0.10
Net income	$ 0.10	$	$ 0.10	$ 0.09	$ 0.02	$ 0.11
Diluted:						
Income from continuing operations	$ 0.09	$	$ 0.09	$ 0.08	$ 0.02	$ 0.10
Net income	$ 0.10	$	$ 0.10	$ 0.09	$ 0.02	$ 0.11

Tax Effect on Pro Forma Stock-Based Compensation Disclosures

Subsequent to the issuance of our condensed consolidated financial statements for the quarter ended April 2, 2005, we determined that the tax effect on stock-based compensation determined under the fair value method had been calculated incorrectly for the three and six month periods ended April 2, 2005. Accordingly, such pro forma amounts presented have been restated (see Note 1). For the three month period ended April 2, 2005, the correction of the error increased pro forma stock-based compensation expense, net of tax, by $0.8 million to $2.9 million from $2.1 million, as previously reported, and decreased pro forma net income by $0.8 million to $16.6 million from $17.4 million, as previously reported. For the six month period ended April 2, 2005, the effect was to increase pro forma stock-based compensation expense, net of tax, by $2.4 million to $6.8 million from $4.4 million, as previously reported, and decreased pro forma net income by $2.4 million to $18.1 million from $20.5 million, as previously reported. For the three months ended April 2, 2005 basic and diluted pro forma earnings per share each decreased by $0.03 from $0.57 and $0.56 per share, as previously reported, to $0.54 and $0.53 per share, respectively. For the six months ended April 2, 2005 basic and diluted pro forma earnings per share each decreased by $0.08 from $0.67 and $0.66 per share, as previously reported, to $0.59 and $0.58 per share, respectively.

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

FORWARD-LOOKING STATEMENTS

This 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 on Form 10-Q/A, other than statements of historical fact, are forward-looking statements. These statements are generally accompanied by words such as may, will, could, would, should, expect, plan, anticipate, rely, believe, estimate, predict, intend, potential, continue, forecast or the neg comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. Our actual results may differ significantly from those projected in the forward-looking statements in this report. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in this section and those set forth below in the section titled Forward-Looking Information is Subject to Risk and Uncertainty.

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 and market lasers, laser-based systems, precision optics 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 have two reportable business segments: Electro-Optics and Lambda Physik, both of which work with customers to provide cost-effective photonics-based solutions. Our Electro-Optics segment focuses on markets such as semiconductor and related manufacturing, materials processing, original equipment manufacturer (OEM) laser components and instrumentation, scientific research and government programs and graphic arts and display. Lambda Physik AG (Lambda Physik), our wholly-owned subsidiary with headquarters located in Göttingen, Germany, focuses on markets using lasers for the production of thin-film transistors (TFT) used in flat panel displays, ink jet printers, automotive, environmental research, scientific research, medical OEMs, materials processing and micro-machining applications.

We were originally incorporated in California on May 26, 1966 and reincorporated in Delaware on October 1, 1990.

As discussed in Note 15 to the condensed consolidated financial statements included at Item I, we have restated our condensed consolidated financial statements for the three and six month periods ended April 3, 2004 to correct the accounting for our deferred compensation plans. We have also corrected our calculation of the tax effect on stock-based compensation determined under the fair value method for the three and six month periods ended April 2, 2005. All information included in this Management s Discussion and Analysis of Results of Operations and Financial Condition has been correspondingly corrected to give effect to such restatements.

FUTURE TRENDS

Microelectronics

After several years of process development, lasers are now used in mass production applications and the industry is benefiting in the form of enhanced performance and increased productivity. We experienced a strong recovery across all segments during fiscal 2004. We anticipate future demands in the advanced packaging market will steadily shift towards the use of ultraviolet laser-based tools, as they are capable of producing sub-50 micron features that are critical for next generation chip-scale and wafer-level packages.

Graphic arts and display

The graphic arts and display market experienced a migration in technologies towards the use of direct diode laser systems as these systems have been adopted at a much faster rate during fiscal 2004. As we continue to move into fiscal 2005 and years beyond, we anticipate a number of our newer products such as a version of our *Paladin* laser and new diode laser technology will gain more traction in the marketplace.

Our Advanced Engineering Unit has built a prototype Red, Green and Blue (RGB) laser engine for rear projection television based on our patented OPS technology. The RGB laser system delivers suitable power and is comparable in size to the lamps currently used in rear projection televisions. Alpha units of the RGB laser engine have been delivered to commercial customers for evaluation. We anticipate partnering with consumer electronics manufacturers to refine the package and evolve the technology to demonstrate acceptable lifetimes and to outsource the manufacturing of the RGB laser engine.

Materials processing

Anticipated drivers for expansion in the materials processing market include providing aggressive gains in cost-of-ownership for products and continuing increased expansion into geographical areas. The market for materials processing in Asian countries drove much of the growth in the first half of fiscal 2004, but has since stabilized, primarily due to foreign monetary policies established to slow economic growth. We anticipate growth to resume once the effects of these policies are felt and active measures to stimulate the economy begin to arise.

The market for laser material processing will continue to expand by providing cost effective manufacturing solutions for cutting, joining, marking and engraving of non-metal materials. One of the largest growth areas for us remains the Asian countries particularly in the production of capital equipment for apparel and leather goods.

Scientific research and government programs

We anticipate modest growth rates in the scientific research market for fiscal 2005 with applications in ultrashort pulses and in bio-research being the drivers of this anticipated growth.

OEM components and instrumentation

The instrumentation market has seen a migration from the use of mature laser technologies, mainly ion lasers, to new technologies, primarily based on solid state and semiconductors. Using our solid state lasers and patented OPS technology we are able to both assist and stimulate this transition. Furthermore, this trend is helping in the development of new applications such as security and clinical diagnostics. These applications are likely to require an increased number of lasers, however, the majority of these activities are still in the research and development stage and we expect only moderate impacts on the laser industry in fiscal 2005, with increases anticipated in future years. Nevertheless, we anticipate future opportunities in microscopy, lab-on chip and DNA sequencing based on our continuous product enhancements and evolving market developments.

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 distinctive 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.

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 that are industry leaders and to work together with these customers to design and develop innovative product systems and solutions as they develop new technologies.

Develop and acquire new technologies 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.

Emphasize supply chain management We will continue to focus on operational efficiency through an emphasis on supply chain management with the explicit intent of improving gross margins and increasing inventory turns.

Focus on long-term improvement of Return on Invested Capital We will continue to focus on long-term improvement of return on invested capital.

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 pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). The preparation of these 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 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 and accounting for income taxes.

Revenue Recognition

We recognize revenue when all four revenue recognition criteria have been met: persuasive evidence of an arrangement exists, the product has been delivered or the service has been rendered, the price is fixed or determinable and collection is probable. Revenue from product sales is recorded when all of the foregoing conditions are met and risk of loss and title passes to the customer. Our products typically include a one-year warranty and the estimated cost of product warranty claims (based on historical experience) is recorded at the time the sale is recognized. Sales to customers are generally not subject to any price protection or return rights.

The vast majority of our sales are made to original equipment manufacturers (OEMs), distributors, resellers and end-users in the non-scientific market. Sales made to these customers do not require installation of the products by us and are not subject to other post-delivery obligations, except in occasional instances where we have agreed to perform installation or provide training. In those instances, we defer revenue related to installation services or training until these services have been rendered. We allocate revenue from multiple element arrangements to the various elements based upon relative fair values, which is determined based on the price charged for each deliverable on a standalone basis, except for certain products sold in the scientific market for which the fair value of installation is determined based on third party evidence of fair value.

Our sales to distributors, resellers and end-user customers typically do not have customer acceptance provisions and only certain of our sales to OEM customers have customer acceptance provisions. Customer acceptance is generally limited to performance under our published product specifications. For the few product sales that have customer acceptance provisions because of higher than published specifications, (1) the products are tested and accepted by the customer at our site or by the customer s acceptance of the results of our testing program prior to shipment to the customer, or (2) the revenue is deferred until customer acceptance occurs.

Sales to end-users in the scientific market typically require installation and, thus, involve post-delivery obligations, however our post-delivery installation obligations are not essential to the functionality of our products. We defer revenue related to installation services until completion of these services.

For most products, training is not provided and, thus, no post-delivery training obligation exists. However, when training is provided to our customers, it is typically priced separately and is recognized as revenue after these services have been provided**.**

Long-lived Assets

We evaluate long-lived assets whenever events or changes in business circumstances or our planned use of assets indicate that their carrying amounts may not be fully recoverable or that their useful lives are no longer appropriate. Reviews are performed to determine whether the carrying values of assets are impaired based on comparison to either the discounted expected future cash flows (in the case of goodwill) or to the undiscounted expected future cash flows (for all other long-lived assets). If the comparison indicates that impairment exists, the impaired asset is written down to its fair value. Significant management judgment is required in the forecast of future operating results that are used in the preparation of expected discounted and undiscounted cash flows.

At April 2, 2005, we had $92.3 million of goodwill and purchased intangible assets on our condensed consolidated balance sheet. As no impairment indicators were present during the second quarter of fiscal 2005, we believe this value remains recoverable based on the discounted estimated future cash flows of the associated products and technologies.

At April 2, 2005, we had $162.5 million of property and equipment on our condensed consolidated balance sheet.

It is reasonably possible that the estimates of anticipated future net revenue, the remaining estimated economic life of the products and technologies, or both, could differ from those used to assess the recoverability of these assets. In that event, additional impairment charges or shortened useful lives of certain long-lived assets could be required.

Inventory Valuation

We record our inventory at the lower of cost (computed on a first-in, first-out basis) or market. We write-down our inventory to its estimated market value based on assumptions about future demand and market conditions. Inventory write-downs are generally recorded within guidelines set by management when the inventory for a device exceeds 12 months of its demand and when individual parts have been in inventory for greater than 12 months. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required which could materially affect our future results of operations. We write-down our demo inventory by amortizing the cost of demo inventory over a two-year period from the fourth month after it is placed in service. During the first quarter of fiscal 2005, we recorded $1.6 million (net of minority interest of $0.1 million) of inventory write-downs related to our decision to discontinue future product development and investments in the semiconductor lithography market within our Lambda Physik subsidiary. Due to rapidly changing forecasts and orders, additional write-downs for excess or obsolete inventory, while not currently expected, could be required in the future. Differences between actual results and previous estimates of excess and obsolete inventory could materially affect our future results of operations.

Warranty Reserves

We provide warranties on certain of our product sales (generally one year) and allowances for estimated warranty costs are recorded at the time of sale. The determination of such allowances 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. If actual return rates and/or repair and replacement costs differ significantly from our estimates, adjustments to recognize additional cost of sales may be required in future periods.

Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income tax provision (benefit) in each of the jurisdictions in which we operate. This process involves us estimating our current income tax provision (benefit) together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets.

We record a valuation allowance to reduce our deferred tax assets to an amount that more likely than not will be realized. While we have considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of our net recorded amount, an adjustment to the allowance for the deferred tax asset would increase income in the period such determination was made. Likewise, should we determine that we would not be able to realize all or part of our net deferred tax asset in the future, an adjustment to the allowance for the deferred tax asset would be charged to income in the period such determination was made.

During the second quarter of fiscal 2005, our valuation allowance on deferred tax assets at Lambda Physik decreased by $10.2 million as we now believe that it is more likely than not that we will be able to realize these assets.

Federal income taxes have not been provided for on a portion of the unremitted earnings of foreign subsidiaries either because such earnings are intended to be permanently reinvested or because foreign tax credits are available to offset any planned distributions of such earnings.

KEY PERFORMANCE INDICATORS

The following is a summary of some of the quantitative performance indicators (as defined below) that may be used to assess our results of operations and financial condition (dollars in thousands):

	Three Months Ended			
	April 2, 2005	April 3, 2004	Change	% Change
Bookings - Electro-Optics	$ 100,033	$ 109,095	$ (9,062)	(8.3)%
Bookings - Lambda Physik	$ 29,317	$ 28,269	$ 1,048	3.7%
Net Sales - Electro-Optics	$ 105,383	$ 103,946	$ 1,437	1.4%
Net Sales - Lambda Physik	$ 25,792	$ 21,862	$ 3,930	18.0%
Gross Profit as a % of Net Sales - Electro-Optics	46.8%	42.8%	4.0%	9.3%
Gross Profit as a % of Net Sales - Lambda Physik	35.6%	32.2%	3.4%	10.4%
Research and Development as a % of Net Sales	10.8%	12.4%	(1.6)%	(12.9)%
Income from Continuing Operations Before Income Taxes and Minority Interest	$ 14,849	$ 5,067	$ 9,782	193.1%
Cash from Continuing Operations	$ 18,414	$ 6,637	$ 11,777	177.4%
DSO in Inventories	74.7	76.1	(1.4)	(1.8)%
DSO in Receivables	62.0	65.7	(3.7)	(5.6)%
Capital Spending as a % of Net Sales	2.8%	4.6%	(1.8)%	(39.3)%

	Six Months Ended			
	April 2, 2005	April 3, 2004	Change	% Change
Bookings - Electro-Optics	$ 197,053	$ 215,786	$ (18,733)	(8.7)%
Bookings - Lambda Physik	$ 60,880	$ 48,404	$ 12,476	25.8%
Net Sales - Electro-Optics	$ 206,282	$ 194,569	$ 11,713	6.0%
Net Sales - Lambda Physik	$ 50,915	$ 39,190	$ 11,725	29.9%
Gross Profit as a % of Net Sales - Electro-Optics	46.3%	42.6%	3.7%	8.6%
Gross Profit as a % of Net Sales - Lambda Physik	28.8%	25.6%	3.1%	12.2%
Research and Development as a % of Net Sales	11.1%	13.1%	(2.1)%	(15.7)%
Income from Continuing Operations Before Income Taxes and Minority Interest	$ 22,827	$ 3,899	$ 18,928	485.5%
Cash from Continuing Operations	$ 48,704	$ 31,907	$ 16,797	52.6%
Capital Spending as a % of Net Sales	3.1%	14.3%	(11.2)%	(78.4)%

Definitions and analysis of these performance indicators are as follows:

Bookings

Bookings represent orders expected to be shipped within 12 months. Bookings are generally cancelable without substantial penalty and, historically, we generally have not experienced a significant rate of cancellation. Bookings for a period are calculated by adding current period net sales to the increase or decrease in ending backlog during the period.

In our Electro-Optics segment, second fiscal quarter bookings decreased 8.3% and bookings for the six months ended April 2, 2005 decreased 8.7% from the same periods one year ago. Decreases in the microelectronics, OEM components and instrumentation, materials processing and scientific and government programs markets were partially offset by increases in the graphic arts and display market.

Although microelectronics bookings have decreased from the comparable periods in the prior year, they still continue to be strong as a direct result of our prior investment decisions. Today, a significant portion of our revenue is derived from sales to customers investing in emerging manufacturing technologies. This has allowed us to withstand recent downturns in capacity-driven demand. During the second fiscal quarter, there was improved activity in the wafer inspection and metrology arenas for both leading edge and legacy products, as fab utilization continues to climb. There was also resurgence for lasers used in photomask tools, both for semiconductors and flat panel displays as the market was pushed towards next generation devices to support shrinking feature sizes. Bookings for ultraviolet lasers used in printed circuit board (PCB) direct write were strong, presumably reflecting increasing demand for high resolution PCB s. There is a push to extend the direct write technology to other PCB formats, although this will require a different cost structure for the tool and laser. We are currently testing concepts for this purpose. Microvia drilling, which utilizes both carbon dioxide and ultraviolet lasers, is also picking up as inventories and microvia PCB pricing seems to have bottomed out.

Bookings in the OEM components and instrumentation market decreased in the second fiscal quarter from the same period a year ago after coming off two successive quarters of growth. Our instrumentation business remains healthy as our Sapphire and Compass products continue to dominate this market. Emerging applications in HIV screening, live imaging microscopy and automated hematology hold future promise. Orders from medical OEM customers were weaker following inventory build-up in the preceding quarter. Similarly, bookings from laser OEMs were down sequentially after several annual buys were placed in the first quarter of fiscal 2005.

Bookings in the materials processing market decreased compared to the same prior year periods primarily due to the unusually high level of bookings in the second quarter of fiscal 2004. This is our third successive quarter of increasing demand, which was evident in several end markets, including textiles and marking and engraving. We believe an additional increase in demand was created when, earlier this year, the World Trade Organization lifted quotas on Chinese-made apparel, thereby creating demand for more processing capacity. We are also seeing a slight shift away from locally made carbon dioxide lasers in China towards commercial grade products. It is far too early to call this a trend, but it is a development worth watching as we estimate more than 10,000 domestic carbon dioxide lasers are sold in China each year. In the longer term, we remain concerned about energy prices and interest rates given their historical impact on this market.

Bookings in the scientific and government programs market decreased from the periods one year ago, but remained solid. We again experienced strong demand from the biological imaging market, which is consistent with our previous predictions. We posted the second highest-ever order rate for our Chameleon products. Our amplifier business was mixed as orders for standard products were in-line with expectations and stiff price competition from European suppliers led us to pass on some custom laser business. We set a record-high for orders of our Evolution laser, which has emerged as the standard for pumping amplifiers, including those from other vendors. On a geographic basis, the U.S. market recovered from its first quarter sluggishness and Asia remained on track. European bookings in the second fiscal quarter were disappointing and were due mostly to funding delays.

Bookings in the graphic arts and display market increased from the same prior year periods, driven by several applications. We have experienced an increase in demand for Paladin solid-state ultraviolet lasers used in newspaper printing. The main customer benefits are print speed and lower operating costs. Our penetration into the professional film finishing and digital film writing areas continues to gain momentum with new placements of our Sapphire series lasers. While green lasers used in computer-to-plate printing have nearly completely succumbed to diode lasers, there is a substantial installed based of legacy systems, which drove a moderately sizeable order for service stock. We have run a number of demonstrations of our previously announced RGB laser emitter for the consumer and commercial display market. Based upon feedback, we appear to be on target in terms of fit, form and function. Not surprisingly, lifetime and cost have rapidly emerged as key success factors. We are continuing to evolve the technology for this and other markets while we explore various manufacturing models.

In our Lambda Physik segment, second fiscal quarter bookings increased 3.7%, with increases in the lithography market partially offset by slight decreases in the industrial and scientific and medical markets. Year-to-date bookings increased 25.8%, with increases in the industrial and lithography markets partially offset by decreases in the scientific and medical market.

The industrial market dominated the current quarter order stream for the Lambda Physik segment, although second fiscal quarter orders were down slightly from the strong orders in the same quarter in the prior year. More than half of the industrial bookings came from a large order for lasers used in low-temperature poly-silicon (LTPS) annealing. Despite recent reports of excess capacity in the flat panel display (FPD) market, this large order helps demonstrate that LTPS continues to gain share against amorphous silicon. In fact, one recent report suggested that LTPS panels would account for 30% of the FPD market by 2008, versus its current 9% share.

Lithography bookings increased from the prior year periods and should remain mostly service-related. We will continue to support our installed base, but have discontinued future investments in lithography. We are also exploring options to sell Lambda Physik s interest in Xtreme Technologies, its joint venture with Jenoptik to develop extreme ultra-violet (EUV) light sources.

SciMed bookings grew slightly due to strong increases in our OptexPro lasers which have gained traction with customers in the medical OEM and scientific markets, partially offset by some unusually high scientific orders in the second quarter of fiscal 2004.

Net Sales

Net sales include sales of lasers, laser-based systems, precision optics, related accessories and service contracts. Net sales for the second fiscal quarter increased 1.4% in our Electro-Optics segment and 18.0% in our Lambda Physik segment from the same quarter one year ago. Net sales for the first six months of fiscal 2005 increased 6.0% in our Electro-Optics segment and 29.9% in our Lambda Physik segment from the same period one year ago. For a more complete description of the reasons for changes in net sales, we refer you to the Results of Operations section of this Form 10-Q/A.

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 second fiscal quarter increased from 42.8% to 46.8% in our Electro-Optics segment and increased from 32.2% to 35.6% in our Lambda Physik segment from the same quarter one year ago. Gross profit percentage in the first six months of fiscal 2005 increased from 42.6% to 46.3% in our Electro-Optics segment and increased from 25.6% to 28.8% in our Lambda Physik segment from the same period one year ago. For a more complete description of the reasons for changes in gross profit percentage, we refer you to the Results of Operations section of this Form 10-Q/A.

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 spending to be an important indicator in managing our business as investing in new technologies is a key to future growth. R&D percentage decreased from 12.4% to 10.8% in the second fiscal quarter and decreased from 13.1% to 11.1% for the six months ended April 2, 2005 from the same quarter and year-to-date periods, respectively, one year ago. For a more complete description of the reasons for changes in R&D percentage, refer to the Results of Operations section of this Form 10-Q/A.

Net Cash Provided by Operating Activities

Net cash provided by continuing operating activities shown on our Condensed Consolidated Statements of Cash Flows primarily represents the excess of cash collected from billings to our customers and other receipts, including tax refunds, over cash paid to our vendors for expenses and inventory purchases to run our business. This amount represents cash generated by current operations to pay for equipment, technology, and other investing activities, to repay debt, fund acquisitions and for other financing purposes. We believe this is an important performance indicator since cash generation over the long term is essential to maintaining a healthy business and providing funds to help fuel growth. We believe generating consistent cash from operations is an indication that our products are achieving a high level of customer satisfaction and we are appropriately monitoring our expenses and inventory levels. For a more complete description of the components of cash flows from continuing operating activities, we refer you to the Condensed Consolidated Statements of Cash Flows in this Form 10-Q/A and the Changes in Financial Condition section of this Form 10-Q/A.

Daily Sales Outstanding in Inventories

We calculate daily sales outstanding (DSO) in inventories as net inventories at the end of the period divided by net sales of the period and then multiplied by the number of days in the period, using 90 days for quarters. This indicates how well we are managing our inventory levels, with lower DSO in inventories resulting in more cash flow available. The more money we have tied up in inventory, the less money we have available for research and development, acquisitions, expansions, marketing and other activities to grow our business. Our DSO in inventories for the second quarter of fiscal 2005 decreased 1.4 days from the same quarter one year ago primarily due to Lambda s write-off of lithography inventory and better management of inventory levels in relation to sales volumes in both segments, partially offset by Electro-Optics increase due to a combination of a build-up of safety stock for some key components and increased inventory levels to improve customer service.

Daily Sales Outstanding in Receivables

We calculate daily 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. This indicates how well we are managing our collection of receivables, with lower DSO in receivables resulting in more cash flow available. The more money we have tied up in receivables, the less money we have available for research and development, acquisitions, expansions, marketing and other activities to grow our business. Our DSO in receivables for the second quarter of fiscal 2005 decreased 3.7 days from the same quarter one year ago. The improvement in DSO is primarily due to a lower volume of receivables with longer terms in our Lambda segment, as well as improved collections.

Capital Spending as a Percentage of Net Sales

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. This indicates the extent to which we are expanding or modernizing our operations, including investments in technology. Management monitors capital spending levels as this assists management in measuring our cash flows, net of capital expenditures. Our capital spending percentage decreased from 4.6% to 2.8% compared to the same quarter one year ago primarily due to lower spending for information technology and manufacturing equipment. Our capital spending percentage decreased from 14.3% to 3.1% for the first six months of fiscal 2005 compared to the same year-to-date period one year ago primarily due to our purchase of our previously leased facility in Santa Clara, California, in the first quarter of fiscal 2004 and lower spending on information technology. We anticipate that capital spending for fiscal 2005 will be approximately 4% to 5% of net sales.

SIGNIFICANT EVENTS

On June 3, 2003, we initiated a tender offer to purchase the 5,250,000 (39.62%) outstanding shares of our Lambda Physik subsidiary owned by other shareholders (the minority interest) for approximately $10.50 per share. Through the end of fiscal 2004, we had purchased a total of 4,588,500 outstanding shares for approximately $49.0 million, resulting in a total ownership percentage of 95.01% (inclusive of shares previously owned). During the second quarter of fiscal 2005, we acquired the remaining 661,500 outstanding shares for approximately $11.8 million, resulting in our full ownership of Lambda Physik.

In December 2004, our Lambda Physik subsidiary decided to discontinue future product development and investments in the semiconductor lithography market. As a result, during the six months ended April 2, 2005, we recognized a charge of $2.7 million (net of minority interest of $0.1 million) primarily related to recognizing write-downs of excessive and obsolete inventories, exiting certain purchase commitments and charges related to government grants. We anticipate this decision will also result in re-deployment of a portion of Lambda s lithography future R&D dollars into the most promising growth areas of Lambda Physik s Industrial and Scientific/Medical markets.

During the second quarter of fiscal 2005, we recorded a reduction of $10.2 million of valuation allowance on Lambda Physik s deferred tax assets as we believe that it is more likely than not that we will be able to realize these assets.

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:

	Three Months Ended		Six Months Ended	
	April 2, 2005	April 3, 2004	April 2, 2005	April 3, 2004
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	55.4%	59.0%	57.2%	60.3%
Gross profit	44.6%	41.0%	42.8%	39.7%

Operating expenses:				
Research and development	10.8%	12.4%	11.1%	13.1%
Selling, general and administrative	21.9%	23.5%	22.2%	24.4%
Restructuring, impairment and other charges	0.0%	0.0%	0.1%	0.1%
Intangibles amortization	1.2%	1.4%	1.2%	1.6%
Total operating expenses	33.9%	37.3%	34.6%	39.2%
Income from operations	10.7%	3.7%	8.2%	0.5%
Other income (expense):				
Interest and dividend income	0.8%	0.5%	0.8%	0.6%
Interest expense	(0.4)%	(0.6)%	(0.5)%	(0.7)%
Foreign exchange gain	0.2%	0.3%	0.1%	0.3%
Other net	(0.1)%	0.1%	0.3%	0.9%
Total other income (expense), net	0.6%	0.3%	0.7%	1.1%
Income from continuing operations before income taxes and minority interest	11.3%	4.0%	8.9%	1.7%
Provision (benefit) for income taxes	(3.6)%	1.9%	(0.8)%	0.6%
Income from continuing operations before minority interest	14.9%	2.1%	9.6%	1.1%
Minority interest in subsidiaries losses		0.1%	0.1%	0.2%
Income from continuing operations	14.9%	2.2%	9.7%	1.3%
Discontinued operations, net of tax	0.0%	0.2%	0.0%	0.1%
Net income	14.9%	2.4%	9.7%	1.4%

Net income for the second quarter of fiscal 2005 was $19.6 million ($0.63 per diluted share) including a tax benefit from the reversal of a deferred tax valuation allowance of $9.6 million related to our Lambda Physik segment (tax benefit) and a favorable adjustment of $0.3 million related to our Lambda Physik segment s first quarter of fiscal 2005 decision to discontinue future lithography investments. For the same quarter in the prior year, net income from continuing operations was $2.8 million ($0.09 per share). Net income for the first six months of fiscal 2005 was $25.0 million ($0.81 per diluted share) including a tax benefit from the reversal of a deferred tax valuation allowance of $9.6 million related to our Lambda Physik segment and a tax benefit of $0.5 million related to federal tax law changes enacted in the first quarter of fiscal 2005, partially offset by a charge of $2.7 million related to our decision to discontinue future lithography investments. For the same six months in the prior year, net income from continuing operations was $3.0 million ($0.10 per share). The increase in net income for the quarter is primarily due to the current quarter s tax benefit, higher gross margins as a percentage of sales, higher sales volumes and lower R&D expenses. Year-to-date, the increase in net income is primarily due to the current quarter s tax benefit, higher sales volumes, higher gross margins as a percentage of sales and lower R&D expenses, partially offset by the charges related to our decision to discontinue future lithography investments.

NET SALES:

	Three Months Ended					
	April 2, 2005			April 3, 2004		
		Amount	Percentage of total net sales		Amount	Percentage of total net sales
	(dollars in thousands)					
Consolidated:						
Domestic	$	44,141	33.7%	$	47,147	37.5%
Foreign		87,034	66.3%		78,661	62.5%
Total	$	131,175	100.0%	$	125,808	100.0%
Electro-Optics:						
Domestic	$	40,045	30.6%	$	44,704	35.5%
Foreign		65,338	49.8%		59,242	47.1%
Total	$	105,383	80.4%	$	103,946	82.6%
Lambda Physik:						
Domestic	$	4,096	3.1%	$	2,443	2.0%
Foreign		21,696	16.5%		19,419	15.4%
Total	$	25,792	19.6%	$	21,862	17.4%

	Six Months Ended					
	April 2, 2005			April 3, 2004		
		Amount	Percentage of total net sales		Amount	Percentage of total net sales
	(dollars in thousands)					
Consolidated:						
Domestic	$	89,070	34.6%	$	91,292	39.1%
Foreign		168,127	65.4%		142,467	60.9%
Total	$	257,197	100.0%	$	233,759	100.0%
Electro-Optics:						
Domestic	$	81,394	31.6%	$	85,950	36.8%
Foreign		124,888	48.6%		108,619	46.4%
Total	$	206,282	80.2%	$	194,569	83.2%
Lambda Physik:						
Domestic	$	7,676	3.0%	$	5,342	2.3%
Foreign		43,239	16.8%		33,848	14.5%
Total	$	50,915	19.8%	$	39,190	16.8%

Consolidated

Net sales for the second fiscal quarter and the six months ended April 2, 2005 increased $5.4 million, or 4%, and $23.4 million, or 10%, respectively, from the same periods one year ago. Increases in both periods were a result of increased sales volumes in both segments. During the second quarter of fiscal 2005, domestic sales decreased $3.0 million, or 6%, while foreign sales increased $8.4 million, or 11%. During the six months ended April 2, 2005, domestic sales decreased $2.2 million, or 2%, while foreign sales increased $25.7 million, or 18%. We anticipate that consolidated net sales in the third quarter of fiscal 2005 will be consistent with net sales of the second quarter of fiscal 2005.

Electro-Optics

Electro-Optics net sales increased $1.4 million, or 1%, and $11.7 million, or 6%, for the second fiscal quarter and six months ended April 2, 2005, respectively, compared to the corresponding prior year periods. Domestic sales decreased $4.7 million, or 10%, and foreign sales increased $6.1 million, or 10%, during the second quarter of fiscal 2005 compared to the same quarter one year ago. Domestic sales decreased $4.6 million, or 5%, and foreign sales increased $16.3 million, or 15%, during the first six months of fiscal 2005 compared to the same period one year ago.

The second quarter increase was primarily due to the strengthening of the Euro and Yen against the U.S. dollar ($1.9 million) and increases in the OEM components and instrumentation and materials processing markets, partially offset by decreases in the microelectronics and graphic arts and display markets. OEM components and instrumentation application sales increased $1.4 million, or 6%, primarily due to increased thermal imaging and medical shipments. Materials processing application sales increased $1.3 million, or 10%, primarily due to higher shipments for marking, engraving and textile processing applications. Microelectronics market application net sales decreased $0.8 million, or 3%, due to softness in the advanced packaging and interconnect business in Asia and materials processing market, partially offset by strong semiconductor application shipments. Sales in the graphic arts and display applications decreased $0.5 million, or 7%, primarily due to lower shipments for reprographic applications. The year-to-date increase is primarily due to an increase in the microelectronics market, the strengthening of the Euro and Yen against the U.S. dollar ($5.1 million) and increases in the markets for OEM components and instrumentation, materials processing and scientific research and government programs, partially offset by decreases in the graphic arts and display market. Microelectronics market application net sales increased $6.8 million, or 15%, due to improving fundamentals in the consumer electronics markets. OEM components and instrumentation application sales increased $3.5 million, or 7%, primarily due to increased thermal imaging shipments. Materials processing application sales increased $3.0 million, or 11%, primarily due to higher shipments for marking, engraving and textile processing applications. Net sales within the scientific research and government programs lines of business improved by $0.9 million, or 1%, primarily as a result of increased sales from custom scientific products. Sales in the graphic arts and display applications decreased $2.5 million, or 17%, primarily due to lower shipments for reprographic applications. Although we continue to have a sizeable backlog of orders, current market conditions make it difficult to predict future orders.

Lambda Physik

Lambda Physik net sales increased $3.9 million, or 18%, and $11.7 million, or 30%, for the second fiscal quarter and six months ended April 2, 2005, respectively, compared to the corresponding prior year periods. Domestic sales increased $1.6

million, or 68%, and foreign sales increased $2.3 million, or 12%, during the second quarter of fiscal 2005 compared to the same quarter one year ago. Domestic sales increased $2.3 million, or 44%, and foreign sales increased $9.4 million, or 28%, during the first six months of fiscal 2005 compared to the same period one year ago.

Net sales increased in the second quarter of fiscal 2005 primarily due to higher sales volumes of $3.6 million, or 28%, in the industrial market resulting from increases in flat panel display, ink jet systems and service business. For the first six months of fiscal 2005, net sales increased primarily due to higher sales volumes of $11.2 million, or 55%, in the industrial market due to increases in flat panel display, ink jet systems and service business. The second quarter and first six months of fiscal 2005 include the favorable impact of the strengthening of the Euro and Yen against the U.S. dollar ($0.5 million and $1.5 million, respectively).

GROSS PROFIT

Consolidated

The consolidated gross profit rate increased to 44.6% from 41.0% in the second fiscal quarter and increased to 42.8% from 39.7% for the six months ended April 2, 2005, compared to the same periods one year ago.

The second fiscal quarter increase in gross profit rate was primarily due to changes in product mix (1.8%) with higher margins on Lambda Physik s lithography service business, higher margin product mix within Electro-Optics scientific products, higher sales of higher margin Electro-Optics diode-pumped products and higher sales of higher margin Lambda Physik medical OEM products; more effective leveraging of manufacturing overhead (1.2%) due to higher sales volumes and non-recurring customer-funded manufacturing engineering spending in the Electro-Optics segment; more favorable variances (0.9%) due to the sale of previously scrapped semiconductor-related inventory in the Electro-Optics segment; and lower warranty costs due to improving quality (0.8%); partially offset by higher write-downs of slow-moving inventory (0.8%) in our Lambda Physik segment.

The year-to-date increase in gross profit rate was primarily due to more favorable variances (2.2%) due to the sale of previously scrapped semiconductor-related inventory and improved yields in the Electro-Optics segment; more effective leveraging of manufacturing overhead (2.0%) due to higher sales volumes and non-recurring customer-funded manufacturing engineering spending in the Electro-Optics segment; and lower warranty costs due to improving quality (0.7%); partially offset by the first quarter of fiscal 2005 lithography charge for write-downs of excess and obsolete inventories, charges related to government grants and exiting certain purchase commitments (0.9%); and higher other costs (0.6%) due to higher royalty expense and higher inventory write-downs in our Electro-Optics segment.

Our consolidated gross profit rates have been and will continue to be affected by a variety of factors including foreign and domestic sales mix, manufacturing efficiencies, excess and obsolete inventory write downs, warranty costs, pricing by competitors or suppliers, new product introductions, production volume, customization and reconfiguration of systems, foreign currency fluctuations and field service margins. We anticipate that consolidated gross margins for the third quarter of fiscal 2005 will be in the range of 44% to 45%.

Electro-Optics

The gross profit rate increased to 46.8% from 42.8% in the second fiscal quarter and increased to 46.3% from 42.6% for the six months ended April 2, 2005, compared to the same periods one year ago. The second fiscal quarter increase was primarily due to more effective leveraging of manufacturing overhead (1.5%) due to higher sales volumes and non-recurring customer-funded manufacturing engineering spending; higher product margins (1.1%) primarily due to higher margin product mix within scientific and higher sales of higher margin diode-pumped products; and more favorable variances (1.1%) due to the sale of previously scrapped semiconductor-related inventory. The year-to-date increase was primarily due to more favorable variances (2.8%) due to the sale of previously scrapped semiconductor-related inventory and improved yields; and more effective leveraging of manufacturing overhead (2.5%) due to higher sales volumes and non-recurring customer-funded manufacturing engineering spending; partially offset by lower product margins (1.1%) primarily due to higher sales of lower margin diode-pumped products, partially offset by lower sales of lower margin scientific products; and higher other costs (0.8%) due to higher royalty expense and higher inventory provisions.

Lambda Physik

The gross profit rate increased to 35.6% from 32.2% in the second fiscal quarter and increased to 28.8% from 25.6% for the six months ended April 2, 2005, compared to the same periods one year ago. The second fiscal quarter increase was primarily due to increased product margins (4.6%) due to higher margins on lithography service business and higher sales of higher margin medical OEM products and lower warranty costs (3.0%) due to improving quality. The increases were partially offset by higher write-downs for slow-moving inventory (4.2%). The year-to-date increase was primarily due to higher margins on lithography service business and higher sales of higher margin medical OEM products (4.2%), lower warranty costs due to improving quality (2.9%) and lower losses on service contracts (1.1%), partially offset by the current year lithography charge for write-downs of excess and obsolete inventories, charges related to government grants and exiting certain purchase commitments (4.4%) and the impact of a large EUV shipment at distributor margins (0.9%) in the first quarter of fiscal 2005.

OPERATING EXPENSES:

	Three Months Ended			
	April 2, 2005		April 3, 2004	
	Amount	Percentage of total net sales	Amount	Percentage of total net sales
	(dollars in thousands)			
Research and development	$ 14,175	10.8%	$ 15,593	12.4%
Selling, general and administrative	28,765	21.9%	29,517	23.5%
Restructuring, impairment and other charges	(40)	0.0%		
Intangibles amortization	1,528	1.2%	1,770	1.4%
Total operating expenses	$ 44,428	33.9%	$ 46,880	37.3%

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	Six Months Ended			
	April 2, 2005		April 3, 2004	
	Amount	Percentage of total net sales	Amount	Percentage of total net sales
	(dollars in thousands)			
Research and development	$ 28,451	11.1%	$ 30,710	13.1%
Selling, general and administrative	57,203	22.2%	56,968	24.4%
Restructuring, impairment and other charges	260	0.1%	237	0.1%
Intangibles amortization	3,021	1.2%	3,699	1.6%
Total operating expenses	$ 88,935	34.6%	$ 91,614	39.2%

Research and development (R&D) expenses decreased $1.4 million, or 9%, and $2.2 million, or 7%, in the fiscal quarter and six months ended April 2, 2005 compared to the comparable periods one year ago. As a percentage of net sales, R&D expense decreased to 10.8% from 12.4% in the second fiscal quarter and decreased to 11.1% from 13.1% in the six months ended April 2, 2005 as compared to the corresponding amounts in the prior year. The second fiscal quarter decrease was primarily due to the completion of Lambda s 193nm lithography program during the first fiscal quarter of 2005 ($2.0 million), higher net reimbursements ($1.1M) for development projects in our Electro-Optics segment and lower spending than in the prior year period to improve product reliability and expand specifications in our Lambda Physik segment ($0.9 million), partially offset by increased project spending on supplies and labor in our Electro-Optics segment ($1.8 million) primarily for optically pumped and individually addressable semiconductor laser bar products and the impact of the strengthening of the Euro and Yen against the U.S. dollar ($0.4 million). The year-to-date decrease was primarily due to the completion of Lambda Physik s 193nm lithography program during the first fiscal quarter of 2005 ($2.5 million), higher net reimbursements ($2.3M) for development projects in our Electro-Optics segment and lower spending than in the prior year period to improve product reliability and expand specifications in our Lambda Physik segment ($2.0 million), partially offset by increased project spending on supplies and labor in our Electro-Optics segment ($3.4 million) primarily for optically pumped and individually addressable semiconductor laser bar, diode-pumped and laser diode module products and the impact of the strengthening of the Euro and Yen against the U.S. dollar ($1.1 million). We anticipate R&D expenses to be in the range of 11.0% to 11.5% of net sales in the third quarter of fiscal 2005.

Selling, general and administrative (SG&A) expenses in the second fiscal quarter of 2005 decreased $0.8 million, or 3%, from the comparable fiscal quarter one year ago, and as a percentage of net sales decreased to 21.9% from 23.5%. Year-to-date, selling, general and administrative (SG&A) expenses increased $0.2 million, or less than 1%, from the comparable period one year ago, but as a percentage of net sales decreased to 22.2% from 24.4%. The second fiscal quarter decrease was primarily due to reduced charges attributable from deferred compensation plan liabilities ($0.6 million), lower medical insurance claims under our self-insured programs ($0.4 million) and the weakening of the Euro and Yen against the U.S. dollar ($0.2 million), partially offset by higher consulting and depreciation expense related to our investments in information technology systems ($0.5 million). The year-to-date increase was primarily due to higher consulting and depreciation expense related to our investments in information technology systems ($1.1 million) and the strengthening of the Euro and Yen against the U.S. dollar ($0.5 million), partially offset by lower medical insurance claims under our self-insured programs ($0.9 million) and reduced charges attributable from deferred compensation plan liabilities ($0.5 million). We anticipate SG&A expenses to be in the range of 23.0% to 23.5% of net sales in the third quarter of fiscal 2005.

Our restructuring, impairment and other charges during the three months and six months ended April 2, 2005 and the six months ended April 3, 2004 were due to adjustments to the estimated contractual obligation for lease and other facility costs of a previously vacated building, net of sublease income.

Amortization of intangible assets decreased $0.2 million, or 14%, and $0.7 million, or 18%, in the fiscal quarter and six months ended April 2, 2005 compared to the comparable periods one year ago. The decrease was due to the completion of amortization of certain intangibles related to our Positive Light acquisition and to technology sold in the second quarter of fiscal 2004.

OTHER INCOME (EXPENSE)

Other income, net of other expense, increased $0.4 million during the second quarter of fiscal 2005 and decreased $1.0 million in the six months ended April 2, 2005 compared to the comparable periods one year ago. The second quarter increase was primarily due to higher interest income ($0.5 million) as a result of higher returns and higher cash balances, lower losses recognized on our share of the losses of Lambda Physik s Xtreme joint venture ($0.5 million) and lower interest expense ($0.3 million) due to principal payments made on our Star notes, partially offset by lower investment gains, net of expenses, associated with our deferred compensation plans ($0.7 million). The year-to-date decrease was primarily due to lower investment gains, net of expenses, associated with our deferred compensation plans ($1.2 million) and $0.6 million less favorable foreign currency exchange net gains, partially offset by higher interest income ($0.7 million) as a result of higher returns and higher cash balances and lower losses recognized on our share of the losses of Lambda Physik s Xtreme joint venture ($0.3 million). Lambda Physik is currently exploring options to sell its interest in the Xtreme joint venture.

INCOME TAXES

The effective tax rate on income before minority interest for the second quarter of fiscal 2005 of (31.8%) was lower than the statutory rate of 35.0% primarily due to a benefit of $9.6 million related to the reversal of deferred tax valuation allowances at Lambda Physik. The effective tax rate on income before minority interest for the six months ended April 2, 2005 of (8.6%) was lower than the statutory rate of 35.0% primarily due to due to a benefit of $9.6 million related to the reversal of deferred tax valuation allowances at Lambda Physik and benefits from R&D tax credits, including benefits of federal tax law changes enacted in the first quarter of fiscal 2005.

The effective tax rate on income from continuing operations before minority interest for the second quarter of fiscal 2004 of 47.7% was higher than the statutory rate of 35.0% primarily due to valuation allowance provisions related to losses at Lambda Physik partially offset by benefits from R&D tax credits. The effective tax rate on income from continuing operations before minority interest for the six months ended April 3, 2004 of 34.9% was lower than the statutory rate of 35.0% primarily due to valuation allowance provisions related to losses at Lambda Physik partially offset by benefits from R&D tax credits.

MINORITY INTEREST IN SUBSIDIARIES (EARNINGS) LOSSES

Minority interest in subsidiaries losses decreased $0.1 million and $0.3 million for the second quarter and first six months of fiscal 2005, respectively, compared to the same periods in the prior year due to lower net losses incurred by Lambda Physik and the completion of the purchase of the remaining shares of Lambda Physik in the second quarter of fiscal 2005. As a result of the completion of the purchase, there will be no minority interest in earnings or losses of Lambda Physik in future periods.

FINANCIAL CONDITION

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Historically, our primary source of cash has been provided through operations. Other sources of cash include proceeds received from the sale of stock through public offerings and employee stock option and purchase plans, as well as through debt borrowings. Our historical uses of cash have primarily been for capital expenditures, acquisitions of businesses and payments of principal and interest on outstanding debt obligations. Supplemental information pertaining 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 notes thereto:

	Six Months Ended	
	April 2, 2005	April 3, 2004
	(in thousands)	
Net cash provided by operating activities	$ 48,704	$ 31,907
Sales of shares under employee stock plans	7,285	4,441
Purchases of property and equipment	(7,945)	(33,474)
Acquisition of businesses, net of cash acquired	(12,129)	(2,471)
Net payments on debt borrowings	(745)	(771)

Net cash provided by operating activities increased by $16.8 million to $48.7 million for the six months ended April 2, 2005 compared to $31.9 million for the same period one year ago. The increase was primarily due to current year-to-date operating earnings and higher cash flows from accounts receivable, partially offset by higher income tax refunds received in fiscal 2004. We believe that our cash flow provided by operating activities will be adequate to cover our current working capital needs, debt service requirements 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. We continue to follow our strategy to further strengthen our financial position by primarily using available cash flow to fund operations and to reduce the amount of debt we have outstanding.

We intend to continue pursuing acquisition opportunities at prices 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 unrestricted cash balances, cash flows from operations, additional borrowings or 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 from time to time and the willingness of potential sellers to accept it as full or partial payment.

Additional sources of cash available to us were a multi-currency line of credit and bank credit facilities totaling $39.0 million as of April 2, 2005, of which $28.9 million was unused and available. These credit facilities were used in Europe during the six months ended April 2, 2005. Our domestic lines of credit include a $12.5 million unsecured revolving account from Union Bank of California, which expires January 31, 2007. No amounts have been drawn upon our domestic lines of credit as of April 2, 2005.

Our ratio of current assets to current liabilities was 4.6:1 at April 2, 2005 compared to 4.3:1 at October 2, 2004. The increase in our ratio from October 2, 2004 to April 2, 2005 is primarily due to increases in cash and cash equivalents and short-term investments, partially offset by decreases in accounts receivable and current deferred tax assets. Our cash position, working capital and debt obligations are as follows:

		April 2, 2005		**October 2, 2004**
		(in thousands)		
Cash and cash equivalents	$	99,002	$	87,659
Working capital		377,896		345,643
Total debt obligations		27,321		27,915

Debt Obligations and Restricted Cash, Cash Equivalents and Short-term Investments

At April 2, 2005, our current and long-term debt obligations primarily consisted of our notes payable to finance our acquisition of Star Medical (Star notes). The Star notes agreement requires that we place cash and short-term investment balances in an amount equal to 120% of the principal balance in a restricted collateral account. At April 2, 2005, $15.2 million of current and $15.2 million of non-current restricted cash, cash equivalents and short-term investments were related to the Star notes (see Note 9 in our Notes to Condensed Consolidated Financial Statements).

Our $12.5 million unsecured revolving account from Union Bank of California agreement is subject to standard covenants related to financial ratios and profitability. At April 2, 2005, we were in compliance with these covenants.

As part of our tender offer to purchase the remaining outstanding shares of our Lambda Physik subsidiary, we were required by local regulations to have funds available for the offer in an account located in Germany. As of April 2, 2005, we had $1.4 million restricted for close out costs related to the purchase of the shares of Lambda Physik that is included in non-current restricted cash, cash equivalents and short-term investments on our condensed consolidated balance sheets. We purchased the remaining shares of Lambda Physik during the second fiscal quarter of 2005.

Contractual Obligations and Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements as defined by Regulation S-K. Information regarding our long-term debt payments, operating lease payments, capital lease payments and long-term purchase commitments is provided in Item 7 Management s Discussion and Analysis of Results of Operations and Financial Condition of our Annual Report on Form 10-K/A for the fiscal year ended October 2, 2004, as amended. There have been no material changes in contractual obligations since October 2, 2004. Information regarding our other financial commitments at April 2, 2005 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 six months ended April 2, 2005 was $48.7 million, which included net income of $25.0 million, depreciation and amortization of $17.4 million, cash provided by operating assets and liabilities of $8.4 million and other items aggregating $0.7 million, partially offset by decreases in net deferred tax assets of $2.8 million.

Cash used for investing activities during the six months ended April 2, 2005 of $43.6 million included $30.4 million, net, used to purchase available-for-sale securities, $12.1 million used to purchase the remaining shares of Lambda Physik, $7.9 million used to acquire property and equipment, $1.2 million used to pay premiums on life insurance and other items aggregating $0.6 million, partially offset by a $8.4 million decrease in restricted cash for the purchase of the remaining shares of Lambda Physik and $0.2 million provided by proceeds from the dispositions of property and equipment.

Cash provided by financing activities during the six months ended April 2, 2005 of $6.1 million included $7.3 million generated from our employee stock purchase and stock option plans, partially offset by net debt repayments of $0.7 million and a decrease in cash overdraft of $0.5 million.

Changes in exchange rates during the six months ended April 2, 2005 provided $0.2 million, primarily due to the strengthening of the Euro and Japanese Yen in relation to the U.S. dollar.

RECENT ACCOUNTING STANDARDS

In November 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 151, Inventory Costs (SFAS 151), an amendment of Accounting Research Bulletin No. 43, Chapter 4. SFAS 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material. SFAS 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not believe that the adoption of SFAS 151 will have a material effect on our results of operations or consolidated financial position.

On December 16, 2004, the FASB issued SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R). SFAS 123R eliminates the alternative of applying the intrinsic value measurement provisions of APB 25 to stock compensation awards issued to employees. Rather, the new standard requires enterprises to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award, known as the requisite service period (usually the vesting period). On April 14, 2005, the Securities and Exchange Commission (SEC) announced the adoption of a rule that defers the required effective date of SFAS 123R. The SEC rule provides that SFAS 123R is now effective for registrants as of the beginning of the first fiscal year beginning after June 15, 2005.

We have not yet quantified the effects of the adoption of SFAS 123R, but it is expected that the new standard may result in significant stock-based compensation expense. The pro forma effects on net income and earnings per share as if we had applied the fair value recognition provisions of original SFAS 123 on stock compensation awards (rather than applying the intrinsic value measurement provisions of APB 25) are in our Notes to Condensed Consolidated Financial Statements (see Note 1). Although the pro forma effects of applying original SFAS 123 may be indicative of the effects of adopting SFAS 123R, the provisions of these two statements differ in some important aspects. The actual effects of adopting SFAS 123R will be dependent on numerous factors including, but not limited to, the valuation model chosen by us to value stock-based awards; the assumed award forfeiture rate; the accounting policies adopted concerning the method of recognizing the fair value of awards over the requisite service period; and the transition method (as described below) chosen for adopting SFAS 123R.

SFAS 123R will be effective for our fiscal quarter beginning October 2, 2005, and allows for the use of the Modified Prospective Application Method. Under this method, SFAS 123R is applied to new awards and to awards modified, repurchased, or cancelled after the effective date. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered (such as unvested options) that are outstanding as of the date of adoption shall be recognized as the remaining requisite services are rendered. The compensation cost relating to unvested awards at the date of adoption shall be based on the grant-date fair value of those awards as calculated for pro forma disclosures under the original SFAS 123. In addition, companies may use the Modified Retrospective Application Method. This method may be applied to all prior years for which the original SFAS 123 was effective or only to prior interim periods in the year of initial adoption. If the Modified Retrospective Application Method is applied, financial statements for prior periods shall be adjusted to give effect to the fair-value-based method of accounting for awards on a consistent basis with the pro forma disclosures required for those periods under the original SFAS 123. We have not yet determined which method we will apply upon our adoption of SFAS 123R.

In March 2005, the FASB issued FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143 (FIN 47). FIN 47 clarifies that conditional asset retirement obligations meet the definition of liabilities and should be recognized when incurred if their fair values can be reasonably estimated. The Interpretation is effective no later than December 31, 2005 and the cumulative effect of initially applying FIN 47 will be recognized as a change in accounting principle. We are in the process of evaluating the expected effect of FIN 47 on our consolidated financial statements.

FORWARD-LOOKING INFORMATION IS SUBJECT TO RISK AND UNCERTAINTY

This quarterly report on Form 10-Q/A contains forward-looking statements. These forward-looking statements include, without limitation, statements regarding:

- net sales;
- results of operations;
- gross profits;
- research and development projects and expenses;
- selling, general and administrative expenses;
- bookings;
- average selling price;
- amount of restructuring, impairment and other charges;
- capital expenditures;
- warranty reserves;
- legal proceedings;
- claims against third parties for infringement of our proprietary rights;
- liquidity and sufficiency of existing cash, cash equivalents and short-term investments for near-term requirements;
- development and acquisition of new technology and intellectual property;
- write-downs for excess or obsolete inventory;
- competitors and competitive pressures;
- growth of applications for our products and increase of market share;
- obtain components and materials in a timely manner;
- identify alternative sources of supply for components;
- achieve adequate manufacturing yields;

impact of recent acquisitions;

improvement of operating results in Lambda Physik;

growth in the semiconductor industry;

compliance with environmental regulations;

leveraging of our technology portfolio and application engineering;

optimize our leadership position in existing markets;

collaborative customer and industry relationships;

development and acquisition of new technologies;

emphasis on supply chain management;

growth of direct digital imaging applications;

use of financial market instruments;

simplifications of our foreign legal structure and reduction of our presences in certain countries; and

focus on long-term improvement of return on invested capital.

You can identify these and other forward-looking statements by use of the words such as may, will, could, would, should, expects, anticipates, relies, believes, estimates, predicts, intends, potential, continue, or the negative of such terms, or other compara terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements.

Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth above in Management s Discussion and Analysis of Results of Operations and Financial Condition and under the heading Risk Factors. All forward-looking statements included in this 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.

BUSINESS ENVIRONMENT AND INDUSTRY TRENDS

Risks Related to our Business

We may experience quarterly and annual fluctuations in our net sales and operating results in the future, which may result in volatility in our stock price.

Our net sales and operating results may vary significantly from quarter to quarter and from year to year in the future. A number of factors, many of which are outside of our control, may cause these variations, including:

general economic uncertainties;

fluctuations in demand for, and sales of, our products or prolonged downturns in the industries that we serve;

ability of our suppliers to produce and deliver components and parts, including sole or limited source components, in a timely manner, in the quantity and quality desired and at the prices we have budgeted;

timing or cancellation of customer orders and shipment scheduling;

fluctuations in our product mix;

foreign currency fluctuations;

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

our ability to develop, introduce, manufacture and ship new and enhanced products in a timely manner without defects;

rate of market acceptance of our new products;

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;

level of capital spending of our customers;

potential obsolescence of our inventory; and

costs related to acquisitions of technology or businesses.

In addition, we often recognize a substantial portion of our sales in the last month of the quarter. 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, 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 common 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. There has not always been a direct correlation between this volatility and the performance of particular companies subject to these stock price fluctuations. These factors, as well as general economic and political conditions or investors concerns regarding the credibility of corporate financial statements and the accounting profession, may have a material adverse affect on the market price of our stock in the future.

We are exposed to risks associated with worldwide economic slowdowns and related uncertainties.

Concerns about consumer and investor confidence, volatile corporate profits and reduced capital spending, and international conflicts and terrorist and military activity could cause a slowdown in customer orders or cause customer order cancellations. In addition, political and social turmoil related to international conflicts and terrorist acts may put further pressure on economic conditions in the United States and abroad. Unstable political, social and economic conditions make it difficult for our customers, our suppliers and us to accurately forecast and plan future business activities. In particular, it is difficult to develop and implement strategy, sustainable business models and efficient operations, as well as effectively manage supply chain relationships. If such conditions persist, our business, financial condition and results of operations could suffer.

We depend on sole source or limited source suppliers for some of the key components and materials, including exotic materials 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. Some of these suppliers are relatively small private companies that may discontinue their operations at any time. We typically purchase our components and materials through purchase orders and we have no guaranteed supply arrangement with any of these suppliers. 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. 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. 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, would impair our ability to meet scheduled product deliveries to our customers and could cause customers to cancel orders.

We rely exclusively on our own production capability to manufacture certain strategic components, optics and optical systems, 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 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.

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

Our future success depends on the continued growth of the markets for lasers, laser systems, precision optics 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 the 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 historically been the industry s high quality, high priced supplier of laser systems. We have, in the past, experienced decreases in the average selling prices of some of our products. We anticipate that as competing products become more widely available, the average selling price of our products may decrease. If we are unable to offset the anticipated decrease in our average selling prices 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 our products. Furthermore, as average selling prices 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 average selling prices 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 new technologies or products that replace them or render them obsolete.

During the six months ended April 2, 2005, our research and development expenses were 11% of net sales. Over the last three fiscal years, our research and development expenses have been approximately 13% of net sales. 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 effectively transfer production processes, 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 sales that could harm our financial condition and results of operations.

For the six months ended April 2, 2005, 65% of net sales were derived from customers outside of the United States. For fiscal years 2004, 2003 and 2002, 61%, 61% and 60%, respectively, of our net sales were derived from customers outside of the Untied States. We anticipate that foreign sales will continue to account for a significant portion of our revenues in the foreseeable future. The global economic slowdown has already had and could continue to have a negative effect on various foreign markets in which we operate. This may cause us to simplify our foreign legal entity structure and reduce our presence in certain countries, which may negatively affect the overall level of business in such countries. A portion of our foreign sales occurs through our foreign sales subsidiaries and the remainder of our foreign sales result from exports to foreign distributors, resellers and customers. Our foreign operations and sales are subject to a number of risks, including:

longer accounts receivable collection periods;

the impact of recessions 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; and

preference for locally produced products.

We are also subject to the risks of fluctuating foreign 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. For additional discussion about our foreign currency risks, see Item 7A Quantitative and Qualitative Disclosures About Market Risk.

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

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. We cannot assure you that our patent applications will be approved, that any patents that may be issued will protect our intellectual property or that any issued patents will not 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.

We could become subject to litigation regarding intellectual property rights, which could seriously harm our business.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. 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. 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, our business may be seriously harmed. We do not have insurance to cover potential claims of this type.

We may, in the future, initiate claims or litigation against third parties for infringement of our proprietary rights to protect these rights or to determine the scope and validity of our proprietary rights or the proprietary rights of competitors. These claims could result in costly litigation and the diversion of our technical and management personnel.

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 future success depends upon the continued services of our executive officers and other key engineering, sales, marketing, manufacturing and support personnel. None of our key employees, except for employees associated with recent acquisitions in the United States, are bound by an employment agreement for any specific term and these personnel may terminate their employment at any time.

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.

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

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 customer s 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 revenue to offset those 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 companies, including Newport Corporation s Spectra-Physics Lasers business unit; Excel Technology, Inc., JDS Uniphase Corp. and Rofin-Sinar Technologies, Inc; and. 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 that have more cash reserves 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 competitors 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 market 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. As a result of the foregoing factors, we expect that competitive pressures may result in price reductions, reduced margins and loss of market share.

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 revenues.

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 technical complexity of our products, 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 such yields or product reliability, our business, operating results, financial condition and customer relationships would be adversely affected. We provide warranties on certain of our product sales, and allowances for estimated warranty costs are recorded during the period of sale. The determination of such allowances 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. If actual return rates and/or repair and replacement costs differ significantly from our estimates, adjustments to recognize additional cost of sales may be required in future periods.

Our customers may discover defects in our products after the products have been fully deployed and operated under 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;
- 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.

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

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 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, some of our suppliers may need at least six 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 and operating results.

Our increased reliance on contract manufacturing may adversely impact our financial results and operations.

We have changed our manufacturing strategy to increase sourcing from contract manufacturers. Our ability to resume internal manufacturing operations for those products has been 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. The inability of any contract manufacturer to meet our cost, quality, performance and availability standards could adversely impact our financial condition or results of operations. 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.

We may not achieve the expected benefits of integration with Lambda Physik.

We are in the process of reviewing the operational efficiency of Lambda Physik s operations and expect to achieve efficiencies by integrating some of Lambda Physik s operations and information technology systems into other Coherent operations. However, integrating the operations of Lambda Physik into our operations is a complex, time consuming and expensive process. The complexity of the technologies and operations being integrated and the disparate corporate cultures being combined may increase the difficulty of integration. Management s focus on the integration of operations may divert attention from our day-to-day business and may disrupt key research and development, marketing or sales efforts. In addition, it is common in the technology industry for aggressive competitors to attract customers and recruit key employees away from companies during the integration phase of an acquisition.

The inability to continue to reduce expenses and contain our costs could harm our operating results.

We are continuing efforts to reduce our expense structure. Additional measures to contain costs and reduce expenses may be undertaken if revenues and market conditions do not continue to improve. A number of factors could preclude us from successfully bringing costs and expenses in line with our revenues, such as our inability to accurately forecast business activities or deterioration of our revenues. If we are unable to continue to reduce expenses and contain our costs, this could harm our operating results.

If we fail to manage our growth effectively, our business could be disrupted, which could 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. We continue to expand the scope of our operations domestically and internationally. The growth in sales, combined with the challenges of managing geographically-dispersed operations, has placed, and our anticipated growth in future operations will continue to place, a significant strain on our management systems and resources. The failure to effectively manage our growth could disrupt our business and harm our operating results.

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 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;
- incur debt;
- assume liabilities; or
- incur expenses related to in-process research and development, impairment of goodwill and amortization.

These purchases also involve numerous risks, including:

- problems combining the acquired operations, technologies or products;
- unanticipated costs or liabilities;
- diversion of management s attention from our core businesses;
- adverse effects on existing business relationships with suppliers and customers; and
- potential loss of key employees, particularly those of the purchased organizations.

We cannot assure you that we will be able to successfully integrate any businesses, products, technologies or personnel that we might acquire in the future, which may harm our business.

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 Tampere, Finland site and 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.

The adoption of certain environmental regulations will require us to redesign some of our products if we are to continue to be able to sell them in Europe.

The European Union has enacted The Restriction on Hazardous Substances in Electronic Equipment (ROHS) and Waste Electrical and Electronic Equipment (WEEE) directives that will require us to redesign some of our products if we are to continue selling them in Europe. These directives come into force August 13, 2005 and July 1, 2006, respectively. We have launched a major program to bring our products into compliance with ROHS and WEEE, but there can be no guarantee that we will be successful. Failure to comply can result in the inability to sell non-compliant products into Europe, a market currently accounting for approximately one-third of our revenues, which would have a material adverse affect on our business and financial results.

Private companies outside of Europe, most notably in Japan, are undertaking similar green initiatives. Noncompliance would result in similar risks.

If our facilities were to experience catastrophic loss, our operations would be seriously harmed.

Our facilities could be subject to a catastrophic loss from fire, flood, earthquake 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 at any of our facilities could disrupt our operations, delay production, shipments and revenue 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.

Provisions of our charter documents, Delaware law, our Common Shares Rights Plan 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;

limiting the ability of our stockholders to act by written consent; 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 and years of service to us. 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.

Our common shares rights agreement permits the holders of rights to purchase shares of our common stock to exercise the stock purchase rights following an acquisition of or merger by us with another corporation or entity, following a sale of 50% or more of our consolidated assets or earning power, or the acquisition by an individual or entity of 20% or more of our common stock. Our successor or acquirer is required to assume all of our obligations and duties under the common shares rights agreement, including in certain circumstances the issuance of shares of its capital stock upon exercise of the stock purchase rights. The existence of our common shares rights agreement may have the effect of delaying, deferring or preventing a change of control and, as a consequence, may discourage potential acquirers from making tender offers for our shares.

Our financial results will be affected by changes in the accounting rules governing the recognition of stock-based compensation expense

Currently, we measure compensation expense for our employee stock compensation plans under the intrinsic value method of accounting prescribed by APB Opinion No. 25, Accounting for Stock Issued to Employees (APB 25). Under this method, no compensation expense has been recorded for stock options granted with exercise prices greater than or equal to the fair value of the underlying common stock at the option grant date. In accordance with SFAS No. 123, Accounting for Stock-Based Compensation, we provide disclosures of our operating results as if we had applied the fair value method of accounting (pro-forma basis). Beginning in the second quarter of fiscal 2003, we provided such disclosures in our Quarterly Reports on Form 10-Q in accordance with SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure. Had we accounted for our compensation expense under the fair value method of accounting prescribed by SFAS No. 123, the charges would have been significantly higher ($3.0 million and $6.9 million in the quarter and six months ended April 2, 2005, respectively, and $14.4 million, $17.6 million and $19.0 million in fiscal 2004, 2003 and 2002, respectively) than the intrinsic value method currently being used.

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R). SFAS 123R eliminates the alternative of applying the intrinsic value measurement provisions of APB 25 to stock compensation awards issued to employees. Rather, the new standard requires companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award, known as the requisite service period (usually the vesting period).

Although such pro forma effects of applying original SFAS 123 may be indicative of the effects of adopting SFAS 123R, the provisions of these two statements differ in some important aspects. The actual effects of adopting SFAS 123R will be dependent on numerous factors including, but not limited to, the valuation model chosen by us to value stock-based awards; the assumed award forfeiture rate; the accounting policies adopted concerning the method of recognizing the fair value of awards over the requisite service period; and the transition method chosen for adopting SFAS 123R.

Beginning in the first quarter of fiscal 2006, when these changes are expected to be implemented, we and other companies will be required to measure compensation expense using the fair value method, which will adversely affect our results of operations by decreasing our earnings by the additional amount of such stock option charges.

Failure to maintain effective internal controls over financial reporting could have a material adverse effect on our business, operating results and stock price.

Beginning with our annual report for our fiscal year ended October 1, 2005, Section 404 of the Sarbanes-Oxley Act of 2002 will require us to include a report by our management on our internal controls over financial reporting. Such report must contain an assessment by management of the effectiveness of our internal controls over financial reporting as of the end of our fiscal year and a statement as to whether or not such internal controls are effective. Such report must also contain a statement that our independent auditors have issued an attestation report on management s assessment of such internal controls.

In order to achieve timely compliance with Section 404, in fiscal 2003 we began a process to document and evaluate our internal controls over financial reporting. Our efforts to comply with Section 404 have resulted in, and are likely to continue to result in, significant costs, the commitment of time and operational resources and the diversion of management s attention. If our management identifies one or more material weaknesses in our internal controls over financial reporting, we will be unable to assert such internal controls are effective. If we are unable to assert that our internal controls over financial reporting are effective as of October 1, 2005 (or if our independent auditors are unable to attest that our management s report is fairly stated or they are unable to express an opinion on our management s evaluation or on the effectiveness of our internal controls), our business may be harmed. Market perception of our financial condition and the trading price of our stock may be adversely affected and customer perception of our business may suffer.

Risks related to our industry

Our market is unpredictable and characterized by rapid technological changes and evolving standards, 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 market is subject to rapid change, it is difficult to predict its potential size or future growth rate. Our success in generating revenues in this market 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, laser systems and precision optics; and

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

For the quarter and six months ended April 2, 2005, our research and development costs were $14.2 million (11% of net sales) and $28.5 million (11% of net sales), respectively. For our fiscal years 2004, 2003 and 2002, our research and development costs were $62.7 million, $51.0 million and $52.4 million, or 13% net sales for each respective fiscal year. 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. Our failure to address rapid technological changes in our markets could adversely affect our business and results of operations.

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

Our net sales depend in part on the demand for our products by semiconductor equipment companies. The semiconductor market has 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 this market severely limits our ability to predict our business prospects or financial results in this market.

During industry downturns, our revenues from this market will 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 this market, 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 this market 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.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk disclosures

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

Interest rate sensitivity

A portion of our investment portfolio is composed of 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 and uniformly by 10% from levels at April 2, 2005, the fair value of the portfolio, based on quoted market prices, would decline by an immaterial amount. 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 April 2, 2005, the fair value of our available-for-sale debt securities was $140.6 million, $13.6 million of which was classified as cash and equivalents, $106.8 million was classified as short-term investments and $20.2 million was classified as restricted cash, cash equivalents and short-term investments on our condensed consolidated balance sheet at April 2, 2005.

At April 2, 2005, we had fixed rate long-term debt of approximately $26.2 million, and a hypothetical 10% increase in interest rates would not have a material impact on the fair market value of this debt, based on pricing models using current interest rates. We do not hedge any interest rate exposures.

Foreign currency exchange risk

We maintain operations in various countries outside of the United States and foreign subsidiaries that manufacture and sell our products in various global markets. A majority of our sales are transacted in U.S. dollars. However, we do generate revenues in other currencies, primarily the Euro and Yen. As a result, our earnings and cash flows are exposed to fluctuations in foreign currency exchange rates. We attempt to limit these exposures through financial market instruments. We utilize hedging instruments, primarily forward contracts with maturities of twelve 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.

We do not anticipate any material adverse effect on our 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.

A hypothetical 10% appreciation of the forward adjusted U.S. dollar to April 2, 2005 market rates would increase the unrealized value of our forward contracts by $0.9 million. Conversely, a hypothetical 10% depreciation of the forward adjusted U.S. dollar to April 2, 2005 market rates would decrease the unrealized value of our forward contracts by $1.1 million.

The following table provides information about our foreign exchange forward contracts at April 2, 2005. The table presents the value of the contracts in U.S. dollars at the contract exchange rate as of the contract maturity date, the weighted average contractual foreign currency exchange rates and fair value. The U.S. notional fair value represents the contracted amount valued at April 2, 2005 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. Notional Fair Value
Fair Value Hedges:			
Euro	1.3104	$ (30,719)	$ (30,340)
British Pound Sterling	1.8671	1,400	1,409
Japanese Yen	103.9537	18,168	17,653
Canadian Dollar	1.2185	927	931

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Item 4. CONTROLS AND PROCEDURES

Controls Evaluation and Related CEO and CFO Certifications

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 the end of the period covered by this Quarterly Report. The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO) and has allowed us to make conclusions, as set forth below, regarding the state of our disclosure controls and procedures.

Disclosure Controls and Procedures

Our disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms. Our disclosure controls and procedures are also designed to ensure that such information is accumulated and communicated to our management, including the CEO and CFO, to allow timely decisions regarding required disclosure. Our disclosure controls include components of our internal control over financial reporting, which consists of control processes designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles in the U.S. To the extent that components of our internal control over financial reporting are included within our disclosure controls, they are included in the scope of our quarterly controls evaluation.

Limitations on the Effectiveness of Controls

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system will be attained. Furthermore, 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 a cost-effective control system, no evaluation of controls can provide absolute assurance that all misstatements due to error or fraud, if any, may occur and not be detected on a timely basis. These inherent limitations include the possibility that judgments in decision-making can be faulty and that breakdowns can occur because of errors or mistakes. Our disclosure controls and procedures can also be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Furthermore, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

Scope of the Controls Evaluation

The evaluation of our disclosure controls and procedures included a review of the controls objectives and design, our implementation of the controls and the effect of the controls on the information generated for use in this Quarterly Report. During the evaluation of our controls and procedures, we looked to identify data errors, control problems or acts of fraud and confirm that appropriate corrective action (including process improvements) was being undertaken. This evaluation is performed on a quarterly basis so that the conclusions of management, including the

CEO and CFO, concerning the effectiveness of the disclosure controls and procedures can be reported in our Quarterly Reports on Form 10-Q and to supplement our disclosures made in our Annual Report on Form 10-K. The overall goal of the evaluation activity is to monitor our disclosure controls and procedures, and to modify them as necessary. We intend to maintain our disclosure controls and procedures as a dynamic system that changes as conditions warrant.

Conclusions

Based upon the evaluation of the effectiveness of our disclosure controls and procedures, our CEO and CFO have concluded that as of the end of the period covered by this Quarterly Report, our disclosure controls and procedures were effective to provide reasonable assurance that material information required to be included in our Exchange Act reports, including this Quarterly Report on Form 10-Q/A is made known to management, including the CEO and CFO, on a timely basis and is recorded, processed, summarized and reported within the time periods prescribed by SEC rules and forms.

In coming to the conclusion that our disclosure controls and procedures were effective as of April 2, 2005, our CEO and CFO considered, among other things, the control deficiency related to the accounting for our deferred compensation plans and the control deficiency related to the error in the calculation of the tax effect on pro forma stock-based compensation, which resulted in the need to amend our Form 10Q to restate our previously issued financial statements as disclosed in Note 15 of Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q/A and our pro forma Stock-Based Compensation footnote related thereto for the three and six month periods ended April 2, 2005. We reviewed and analyzed the Securities and Exchange Commission s Staff Accounting Bulletin (SAB) No. 99 Materiality and Accounting Principles Board Opinion No. 28 Interim Financial Reporting paragraph 29. We then took into consideration that the restatement for the correction of the accounting for our deferred compensation plans (i) did not have a material impact on the financial statements of prior interim or annual periods taken as a whole; (ii) did not have a material cumulative impact to the financial statements of prior interim or annual periods; (iii) was based solely on our determination that the cumulative impact of the error, if recorded in the period discovered, would have been material to that period s reported net income; and that the restatement for the correction of the error in the calculation of the tax effect on pro forma stock-based compensation had no impact to any of our consolidated Statements of Operations, Balance Sheet, or Statement of Cash Flows for the periods affected.

Changes in Internal Controls Over Financial Reporting

During the quarter ended April 2, 2005, we effected a material change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) with the implementation of additional review procedures over the accounting for our deferred compensation plans. The additional review procedures were implemented to remediate the internal control deficiency that led to the restatement.

Following the period covered by this report, we added additional review and reconciliation procedures for the calculation of the tax effect on pro forma stock-based compensation.

PART II. OTHER INFORMATION

ITEM 6. Exhibits

2.1* Agreement and Plan of Merger. (Previously filed as Exhibit 2.1 to Form 10-K for the fiscal year ended September 29, 1990).

3.1* Restated and Amended Certificate of Incorporation. (Previously filed as Exhibit 3.1 to Form 10-K for the fiscal year ended September 29, 1990).

3.2* Certificate of Amendment of Restated and Amended Certificate of Incorporation of Coherent, Inc. (Previously filed as Exhibit 3.2 to Form 10-K for the fiscal year ended September 28, 2002).

3.3* Bylaws of Coherent, Inc, as amended (Previously filed as Exhibit 3.2 to Form 10-K for the fiscal year ended September 29, 1990).

4.1* Amended and Restated Common Shares Rights Agreement dated November 2, 1989 between Coherent and the Bank of Boston. (Previously filed as Exhibit 4.1 to Form 8-K filed on November 3, 1989).

4.2* Agreement of Substitution and Amendment of Common Shares Rights Agreement dated September 8, 2004 between Coherent and American Stock Transfer & Trust Company. (Previously filed as Exhibit 4.1 to Form 10-K/A Amendment No. 2 for the fiscal year ended October 2, 2004).

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.

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

COHERENT, INC.

SIGNATURES

Pursuant to the requirements of the Securities and 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)	
August 17, 2005	/s/:	JOHN R. AMBROSEO John R. Ambroseo President and Chief Executive Officer (Principal Executive Officer)
August 17, 2005	/s/:	HELENE SIMONET Helene Simonet Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)