

NATIONAL INSTRUMENTS CORP /DE/  
Form 10-Q  
July 29, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended: June 30, 2011 or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 0-25426

NATIONAL INSTRUMENTS CORPORATION  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or  
organization)

74-1871327  
(I.R.S. Employer Identification Number)

11500 North MoPac Expressway  
Austin, Texas  
(address of principal executive offices)

78759  
(zip code)

Registrant's telephone number, including area code: (512) 338-9119  
\_\_\_\_\_

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer   
Smaller reporting company

Non-accelerated filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 27, 2011
Common Stock - \$0.01 par value	120,133,668

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## NATIONAL INSTRUMENTS CORPORATION

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## PART I - FINANCIAL INFORMATION

## ITEM 1. Financial Statements

NATIONAL INSTRUMENTS CORPORATION  
CONSOLIDATED BALANCE SHEETS  
(in thousands, except per share data)

	June 30, 2011 (unaudited)	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	\$207,367	\$219,447
Short-term investments	112,341	131,215
Accounts receivable, net	148,939	127,214
Inventories, net	141,571	117,765
Prepaid expenses and other current assets	42,007	36,239
Deferred income taxes, net	13,919	18,838
Total current assets	666,144	650,718
Property and equipment, net	171,506	160,410
Goodwill	132,011	70,278
Intangible assets, net	93,971	52,816
Other long-term assets	25,938	25,460
Total assets	\$1,089,570	\$959,682
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$36,475	\$33,544
Accrued compensation	34,135	27,734
Deferred revenue	80,172	71,650
Accrued expenses and other liabilities	20,156	16,538
Other taxes payable	19,478	16,846
Total current liabilities	190,416	166,312
Deferred income taxes	37,476	29,477
Liability for uncertain tax positions	18,016	14,953
Other long-term liabilities	17,201	4,395
Total liabilities	263,109	215,137
Commitments and contingencies		
Stockholders' equity:		
Preferred stock: par value \$0.01; 5,000,000 shares authorized; none issued and outstanding	-	-
Common stock: par value \$0.01; 180,000,000 shares authorized; 120,130,355 and 117,904,976 shares issued and outstanding, respectively	1,201	1,179
Additional paid-in capital	447,407	407,713

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Retained earnings	369,512	336,363
A c c u m u l a t e d o t h e r c o m p r e h e n s i v e i n c o m e (loss)	8,341	(710 )
Total stockholders' equity	826,461	744,545
Total liabilities and stockholders' equity	\$1,089,570	\$959,682

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

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NATIONAL INSTRUMENTS CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(in thousands, except per share data)  
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Net sales:				
Product	\$233,141	\$194,830	\$451,751	\$370,225
S o f t w a r e				
maintenance	20,143	16,887	39,383	32,583
Total net sales	253,284	211,717	491,134	402,808
Cost of sales:				
Product	\$54,803	\$47,176	\$105,761	\$89,438
S o f t w a r e				
maintenance	1,083	1,463	2,601	2,443
Total cost of sales	55,886	48,639	108,362	91,881
Gross profit	197,398	163,078	382,772	310,927
Operating expenses:				
Sales and marketing	\$96,197	\$79,231	\$183,352	\$153,672
R e s e a r c h a n d				
development	47,027	36,395	89,895	74,941
G e n e r a l a n d				
administrative	21,232	16,969	40,071	32,309
Total operating expenses	164,456	132,595	313,318	260,922
Operating income	32,942	30,483	69,454	50,005
Other income (expense):				
Interest income	\$344	\$371	\$685	\$671
N e t f o r e i g n e x c h a n g e				
(loss)	(486 )	(2,203 )	(709 )	(2,901 )
O t h e r i n c o m e ( l o s s ) ,				
net	(571 )	462	(125 )	810
Income before income taxes	32,229	29,113	69,305	48,585
P r o v i s i o n f o r i n c o m e				
taxes	5,681	4,511	12,296	5,630
Net income	\$26,548	\$24,602	\$57,009	\$42,955
Basic earnings per share	\$0.22	\$0.21	\$0.48	\$0.37
Weighted average shares outstanding - basic	119,736	116,898	119,218	116,485

Diluted earnings per share	\$0.22	\$0.21	\$0.47	\$0.36
Weighted average shares outstanding - diluted	121,161	118,488	120,810	118,128
D i v i d e n d s   d e c l a r e d   p e r share	\$0.10	\$0.09	\$0.20	\$0.18

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

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NATIONAL INSTRUMENTS CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands)  
(unaudited)

	Six Months Ended June 30,	
	2011	2010
Cash flow from operating activities:		
Net income	\$57,009	\$42,955
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	23,390	18,988
Stock-based compensation	10,296	9,459
Tax expense from deferred income taxes	2,770	3,774
Tax (benefit) expense from stock option plans	(5,035 )	579
Changes in operating assets and liabilities:		
Accounts receivable	(13,841 )	(6,803 )
Inventories	(21,393 )	(9,163 )
Prepaid expenses and other assets	2,186	(18,740 )
Accounts payable	937	4,953
Deferred revenue	7,051	7,205
Taxes and other liabilities	9,926	18,513
Net cash provided by operating activities	73,296	71,720
Cash flow from investing activities:		
Capital expenditures	(23,053 )	(10,015 )
Capitalization of internally developed software	(9,391 )	(11,021 )
Additions to other intangibles	(1,756 )	(1,690 )
Acquisition, net of cash received	(73,558 )	(2,191 )
Purchases of short-term investments	(54,097 )	(85,199 )
Sales and maturities of short-term investments	73,915	41,538
Net cash (used by) investing activities	(87,940 )	(68,578 )
Cash flow from financing activities:		
Proceeds from issuance of common stock	21,389	32,550
Repurchase of common stock	-	(30,935 )

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Dividends paid	(23,860 )	(20,225 )
Tax benefit (expense) from stock option plans	5,035	(579 )
Net cash provided by (used by) financing activities	2,564	(19,189 )
Net change in cash and cash equivalents	(12,080 )	(16,047 )
Cash and cash equivalents at beginning of period	219,447	201,465
Cash and cash equivalents at end of period	\$207,367	\$185,418

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

NATIONAL INSTRUMENTS CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Basis of presentation

The accompanying unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2010, included in our annual report on Form 10-K, filed with the Securities and Exchange Commission. In our opinion, the accompanying consolidated financial statements reflect all adjustments (consisting only of normal recurring items) considered necessary to present fairly our financial position at June 30, 2011 and December 31, 2010, and the results of our operations for the three month and six month periods ended June 30, 2011 and June 30, 2010 and the cash flows for the six month periods ended June 30, 2011 and June 30, 2010. Operating results for the three-month and six-month periods ended June 30, 2011, are not necessarily indicative of the results that may be expected for the year ending December 31, 2011.

Note 2 – Earnings per share

Basic earnings per share (“EPS”) is computed by dividing net income by the weighted average number of common shares outstanding during each period. Diluted EPS is computed by dividing net income by the weighted average number of common shares and common share equivalents outstanding (if dilutive) during each period. The number of common share equivalents, which include stock options and restricted stock units, is computed using the treasury stock method.

The reconciliation of the denominators used to calculate basic EPS and diluted EPS for the three month and six month periods ended June 30, 2011 and 2010, respectively, are as follows (in thousands):

	Three Months Ended June 30, (unaudited)		Six Months Ended June 30, (unaudited)	
	2011	2010	2011	2010
Weighted average shares outstanding-basic	119,736	116,898	119,218	116,485
Plus: Common share equivalents				
Stock options, restricted stock units	1,425	1,590	1,592	1,643
Weighted average shares outstanding-diluted	121,161	118,488	120,810	118,128

Stock options to acquire 823,500 shares and 405,000 shares for the three month periods ended June 30, 2011 and 2010, respectively, and 415,700 shares and 427,500 shares for the six month periods ended June 30, 2011 and 2010, respectively, were excluded in the computations of diluted EPS because the effect of including the stock options would have been anti-dilutive.

On January 21, 2011, our Board of Directors declared a 3 for 2 stock split which was effected as a stock dividend, and paid on February 21, 2011, to stockholders of record on February 4, 2011. All per share data and numbers of common shares, where appropriate, have been retroactively adjusted to reflect the stock split.

Note 3 – Cash, cash equivalents and short-term investments

The following table summarizes unrealized gains and losses related to our cash, cash equivalents and short-term investments designated as available-for-sale (in thousands):

	As of June 30, 2011 (unaudited)				
	Adjusted Cost	Gross Unrealized Gain	Gross Unrealized Loss	Cumulative Translation Adjustment	Fair Value
Cash	\$99,798	\$-	\$-	\$-	\$99,798
M o n e y m a r k e t accounts	107,569	-	-	-	107,569
Municipal bonds	19,255	28	-	-	19,283
Corporate bonds	51,418	45	(28 )	-	51,435
U.S. treasuries and agencies	3,005	5	-	-	3,010
Foreign government bonds	36,038	-	(188 )	(633 )	35,217
Time deposits	3,396	-	-	-	3,396
Cash, Cash equivalents and short-term investments	\$320,479	\$78	\$(216 )	\$(633 )	\$319,708

	As of December 31, 2010				
	Adjusted Cost	Gross Unrealized Gain	Gross Unrealized Loss	Cumulative Translation Adjustment	Fair Value
Cash	\$86,344	\$-	\$-	\$-	\$86,344
M o n e y m a r k e t accounts	133,103	-	-	-	133,103
Municipal bonds	16,843	18	-	-	16,861
Corporate bonds	56,141	38	(69 )	-	56,110
U.S. treasuries and agencies	23,142	13	(20 )	-	23,135
Foreign government bonds	36,010	89	(32 )	(3,410 )	32,657
Time deposits	2,452	-	-	-	2,452
Cash, Cash equivalents and short-term investments	\$354,035	\$158	\$(121 )	\$(3,410 )	\$350,662

The following table summarizes the contractual maturities of our investments designated as available-for-sale (in thousands):

	As of June 30, 2011 (Unaudited)	
	Adjusted Cost	Fair Value
Due in less than 1 year	\$75,559	\$75,181
Due in 1 to 5 years	37,553	37,160
Total short-term investments	\$113,112	\$112,341
	Adjusted Cost	Fair Value
Due in less than 1 year		
Municipal bonds	\$13,925	\$13,939
Corporate bonds	36,820	36,839
U.S. treasuries and agencies	3,005	3,010
Foreign government bonds	18,413	17,997
Time deposits	3,396	3,396
Total short-term investments	\$75,559	\$75,181

	Adjusted Cost	Fair Value
Due in 1 to 5 years		
Municipal bonds	\$5,330	\$5,344
Corporate bonds	14,598	14,596
Foreign government bonds	17,625	17,220
Total short-term investments	\$37,553	\$37,160

#### Note 4 – Fair value measurements

We define fair value to be the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, we consider the principal or most liquid market and assumptions that market participants would use when pricing the asset or liability.

We follow a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The three values of the fair value hierarchy are the following:

Level 1 – Quoted prices in active markets for identical assets or liabilities

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly

Level 3 – Inputs that are not based on observable market data

Assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands):

Description	Fair Value Measurements at Reporting Date Using (Unaudited)			
	June 30, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
Money Market Funds	\$107,569	\$107,569	\$-	\$ -
Short-term investments available for sale:				
Municipal bonds	19,283	19,283	-	-
Corporate bonds	51,435	51,435	-	-
U.S. treasuries and agencies	3,010	3,010	-	-
Foreign government bonds	35,217	35,217	-	-
Time deposits	3,396	3,396	-	-
Derivatives	4,787	-	4,787	-
Total Assets	\$224,697	\$219,910	\$4,787	\$ -
<b>Liabilities</b>				
Derivatives	\$(3,312)	\$-	\$(3,312)	\$ -



We have operations in over 40 countries. Sales outside of the Americas accounted for 59% and 57% of our revenues during the three month periods ended June 30, 2011 and 2010, respectively, and 59% and 58% of our revenues during the six month periods ended June 30, 2011 and 2010, respectively. Our activities expose us to a variety of market risks, including the effects of changes in foreign currency exchange rates. These financial risks are monitored and managed by us as an integral part of our overall risk management program.

We maintain a foreign currency risk management strategy that uses derivative instruments (foreign currency forward and purchased option contracts) to help protect our earnings and cash flows from fluctuations caused by the volatility in currency exchange rates. Movements in foreign currency exchange rates pose a risk to our operations and competitive position, since exchange rate changes may affect our profitability and cash flow, and the business or pricing strategies of our non-U.S. based competitors.

The vast majority of our foreign sales are denominated in the customers' local currency. We purchase foreign currency forward and option contracts as hedges of forecasted sales that are denominated in foreign currencies and as hedges of foreign currency denominated receivables. These contracts are entered into to help protect against the risk that the eventual dollar-net-cash inflows resulting from such sales or firm commitments will be adversely affected by changes in exchange rates. We also purchase foreign currency forward contracts as hedges of forecasted expenses that are denominated in foreign currencies. These contracts are entered into to help protect against the risk that the eventual dollar-net-cash outflows resulting from foreign currency operating and cost of revenue expenses will be adversely affected by changes in exchange rates.

We designate foreign currency forward and purchased option contracts as cash flow hedges of forecasted revenues or forecasted expenses. In addition, we hedge our foreign currency denominated balance sheet exposures using foreign currency forward contracts that are not designated as hedging instruments. None of our derivative instruments contain a credit-risk-related contingent feature.

#### Cash flow hedges

To help protect against the reduction in value caused by a fluctuation in foreign currency exchange rates of forecasted foreign currency cash flows resulting from international sales over the next one to two years, we have instituted a foreign currency cash flow hedging program. We hedge portions of our forecasted revenue and forecasted expenses denominated in foreign currencies with forward and purchased option contracts. For forward contracts, when the dollar strengthens significantly against the foreign currencies, the change in the present value of future foreign currency cash flows may be offset by the change in the fair value of the forward contracts designated as hedges. For option contracts, when the dollar strengthens significantly against the foreign currencies, the change in the present value of future foreign currency cash flows may be offset by the change in the fair value of the option contracts net of the premium paid designated as hedges. Our foreign currency purchased option contracts are purchased "at-the-money" or "out-of-the-money". We purchase foreign currency forward and option contracts for up to 100% of our forecasted exposures in selected currencies (primarily in Euro, Japanese yen, British pound sterling and Hungarian forint) and limit the duration of these contracts to 40 months or less.

For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of accumulated other comprehensive income ("OCI") and reclassified into earnings in the same line item (net sales, operating expenses, or cost of sales) associated with the forecasted transaction and in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings or expenses during the current period and are classified as a component of "net foreign exchange gain (loss)". Hedge effectiveness of foreign currency forwards and purchased option contracts designated as cash flow hedges are measured by comparing the hedging instrument's cumulative change in fair value from inception to maturity to the forecasted transaction's terminal value.

We held forward contracts with a notional amount of \$13.6 million dollar equivalent of Euro, \$3.1 million dollar equivalent of British pound sterling, \$27.2 million dollar equivalent of Japanese yen, and \$23.1 million dollar equivalent of Hungarian forint at June 30, 2011. These contracts are for terms of up to 24 months. At December 31, 2010, we held forward contracts with a notional amount of \$28.3 million dollar equivalent of Euro, \$6.0 million dollar equivalent of British pound sterling, \$18.4 million dollar equivalent of Japanese yen, and \$33.4 million dollar equivalent of Hungarian forint.

We did not have any purchased option contracts at June 30, 2011. At June 30, 2010, we held purchased option contracts with a notional amount of \$14.8 million dollar equivalent of Euro.

At June 30, 2011, we expect to reclassify \$2.5 million of losses on derivative instruments from accumulated other comprehensive income to net sales during the next twelve months when the hedged international sales occur, \$2.2 million of gains on derivative instruments from accumulated OCI to cost of sales when the cost of sales are incurred and \$1.0 million of gains on derivative instruments from accumulated OCI to operating expenses during the next twelve months when the hedged operating expenses occur. Expected amounts are based on derivative valuations at June 30, 2011. Actual results may vary as a result of changes in the corresponding exchange rate subsequent to this date.

We did not record any ineffectiveness from our hedges during the six months ended June 30, 2011.

#### Other Derivatives

Other derivatives not designated as hedging instruments consist primarily of foreign currency forward contracts that we use to hedge our foreign denominated net receivable or net payable positions to protect against the change in value caused by a fluctuation in foreign currency exchange rates. We typically attempt to hedge up to 90% of our outstanding foreign denominated net receivables or net payables and typically limit the duration of these foreign currency forward contracts to approximately 120 days. The gain or loss on the derivatives as well as the offsetting gain or loss on the hedge item attributable to the hedged risk is recognized in current earnings under the line item "net foreign exchange gain (loss)". As of June 30, 2011 and December 31, 2010, we held foreign currency forward contracts with a notional amount of \$45.2 million and \$41.3 million, respectively.

The following tables present the fair value of derivative instruments on our Consolidated Balance Sheets and the effect of derivative instruments on our Consolidated Statements of Income.

#### Fair Values of Derivative Instruments (in thousands):

	Asset Derivatives			
	June 30, 2011 (Unaudited)		December 31, 2010	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange contracts - ST forwards	Prepaid expenses and other current assets	\$3,296	Prepaid expenses and other current assets	\$1,104
Foreign exchange contracts - LT forwards	Other long-term assets	1,359	Other long-term assets	490
Total derivatives designated as hedging instruments		\$4,655		\$1,594



## Derivatives not designated as hedging instruments

Foreign exchange contracts - ST forwards	Prepaid expenses and other current assets	\$ 132	Prepaid expenses and other current assets	\$ 731
Total derivatives not designated as hedging instruments		\$ 132		\$ 731
Total derivatives		\$4,787		\$2,325

## Liability Derivatives

June 30, 2011  
(Unaudited)

December 31, 2010

	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange contracts - ST forwards	Accrued expenses and other liabilities	\$(2,633 )	Accrued expenses and other liabilities	\$(2,677 )
Foreign exchange contracts - LT forwards	Other long-term liabilities	(7 )	Other long-term liabilities	-
Total derivatives designated as hedging instruments		\$(2,640 )		\$(2,677 )
Derivatives not designated as hedging instruments				
Foreign exchange contracts - ST forwards	Accrued expenses and other liabilities	\$(672 )	Accrued expenses and other liabilities	\$(1,056 )
Total derivatives not designated as hedging instruments		\$(672 )		\$(1,056 )
Total derivatives		\$(3,312 )		\$(3,733 )

Effect of derivative instruments on our Consolidated Statements of Income for the three month periods ended June 30, 2011 and 2010, respectively (in thousands):

	June 30, 2011 (Unaudited)			
	Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)
Derivatives in Cash Flow Hedging Relationship	\$(71 )	Net sales	\$(983 )	\$-

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Foreign exchange contracts - forwards and options				Net foreign exchange gain (loss)	
Foreign exchange contracts - forwards and options	326	Cost of sales	376	Net foreign exchange gain (loss)	-
Foreign exchange contracts - forwards and options	55	Operating expenses	277	Net foreign exchange gain (loss)	-
Total	\$ 310		\$ (330 )		\$ -

June 30, 2010  
(Unaudited)

Derivatives in Cash Flow Hedging Relationship	Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Recognized into Income (Effective Portion)	Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)
Foreign exchange contracts - forwards and options	\$ 229	Net sales	\$ 2,012	Net foreign exchange gain (loss)	\$ -
Foreign exchange contracts - forwards and options	(3,319 )	Cost of sales	642	Net foreign exchange gain (loss)	-
Foreign exchange contracts - forwards and options	(1,509 )	Operating expenses	219	Net foreign exchange gain (loss)	-
Total	\$ (4,599 )		\$ 2,873		\$ -

Derivatives not Designated as Hedging Instruments	Location of Gain (Loss) Recognized in Income	Amount of Gain (Loss) Recognized in Income June 30, 2011 (Unaudited)	Amount of Gain (Loss) Recognized in Income June 30, 2010 (Unaudited)
Foreign exchange contracts - forwards	Net foreign exchange gain/(loss)	\$ (1,110 )	\$ 937
Total		\$ (1,110 )	\$ 937

Effect of derivative instruments on our Consolidated Statements of Income for the six month periods ended June 30, 2011 and 2010, respectively (in thousands):

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June 30, 2011  
(Unaudited)

Derivatives in Cash Flow Hedging Relationship	Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)
Foreign exchange contracts - forwards and options	\$ (467 )	Net sales	\$ (1,740 )	Net foreign exchange gain (loss)	\$ -
Foreign exchange contracts - forwards and options	2,480	Cost of sales	750	Net foreign exchange gain (loss)	-
Foreign exchange contracts - forwards and options	1,143	Operating expenses	422	Net foreign exchange gain (loss)	-
Total	\$ 3,156		\$ (568 )		\$ -

June 30, 2010  
(Unaudited)

Derivatives in Cash Flow Hedging Relationship	Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)
Foreign exchange contracts - forwards and options	\$ 1,744	Net sales	\$ 3,049	Net foreign exchange gain (loss)	\$ -
Foreign exchange contracts - forwards and options	(4,710 )	Cost of sales	1,411	Net foreign exchange gain (loss)	-
Foreign exchange contracts - forwards and options	(2,394 )	Operating expenses	587	Net foreign exchange gain (loss)	-
Total	\$ (5,360 )		\$ 5,047		\$ -

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Derivatives not Designated as Hedging Instruments	Location of Gain (Loss) Recognized in Income	Amount of Gain (Loss) Recognized in Income June 30, 2011 (Unaudited)	Amount of Gain (Loss) Recognized in Income June 30, 2010 (Unaudited)
Foreign exchange contracts - forwards	Net foreign exchange gain/(loss)	\$ (2,103 )	\$ 1,376
Total		\$ (2,103 )	\$ 1,376

Note 6 – Inventories

Inventories, net consist of the following (in thousands):

	June 30, 2011 (Unaudited)	December 31, 2010
Raw materials	\$ 64,871	\$ 55,218
Work-in-process	4,766	6,359
Finished goods	71,934	56,188
	\$ 141,571	\$ 117,765

Note 7 – Intangibles

Intangibles at June 30, 2011 and December 31, 2010 were as follows (in thousands):

	June 30, 2011 (Unaudited)			December 31, 2010		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Capitalized software development costs	\$ 50,284	\$ (22,767 )	\$ 27,517	\$ 40,481	\$ (16,217 )	\$ 24,264
Acquired technology	67,508	(27,564 )	39,944	35,634	(25,017 )	10,617
Patents	21,646	(6,826 )	14,820	20,790	(6,312 )	14,478
Other	23,363	(11,673 )	11,690	14,059	(10,602 )	3,457
	\$ 162,801	\$ (68,830 )	\$ 93,971	\$ 110,964	\$ (58,148 )	\$ 52,816

Capitalized software development costs for the three month periods ended June 30, 2011 and 2010, were \$5.9 million and \$8.0 million, respectively, and related amortization expense was \$3.3 million and \$2.5 million, respectively. For the six month periods ended June 30, 2011 and 2010, capitalized software development costs were \$9.8 million and \$11.5 million, respectively, and related amortization expense was \$6.6 million and \$5.1 million, respectively. For the three month periods ended June 30, 2011 and 2010, capitalized software development costs included costs related to stock based compensation of \$262,000 and \$349,000, respectively. For the six month periods ended June 30, 2011 and 2010, capitalized software development costs included costs related to stock based compensation of \$412,000 and \$511,000, respectively.

Amortization of capitalized software development costs is computed on an individual product basis for those products available for market and is recognized based on the product's estimated economic life, generally three years. Acquired

intangible assets which include acquired technology and other are amortized over their useful lives, which range from three to eight years. Patents are amortized using the straight-line method over their estimated period of benefit, generally ten to seventeen years. Total intangible assets amortization expenses were \$5.5 million and \$4.1 million for the three month periods ended June 30, 2011 and 2010, respectively, and \$10.7 million and \$8.2 million for the six month periods ended June 30, 2011 and 2010, respectively.

The overall increase in our acquired technology and other intangible assets can be attributed to the acquisition of AWR Corporation and Phase Matrix Inc. See Note 16 – Acquisitions of Notes to Consolidated Financial Statements for additional discussion related to these acquisitions.

#### Note 8 – Goodwill

The carrying amount of goodwill as of June 30, 2011, was as follows (in thousands):

	Amount
B a l a n c e a s o f D e c e m b e r 3 1 , 2 0 1 0	\$70,278
Acquisitions	61,069
Divestitures	-
F o r e i g n c u r r e n c y t r a n s l a t i o n i m p a c t	664
Balance as of June 30, 2011	\$132,011

The excess purchase price over the fair value of assets acquired is recorded as goodwill. As we have one operating segment, we allocate goodwill to one reporting unit for goodwill impairment testing. Goodwill is tested for impairment on an annual basis, and between annual tests if indicators of potential impairment exist, using a fair-value-based approach based on the market capitalization of the reporting unit. Our annual impairment test was performed as of February 28, 2011. No impairment of goodwill has been identified during the period presented. Goodwill is deductible for tax purposes in certain jurisdictions.

See Note 16 – Acquisitions of Notes to Consolidated Financial Statements for additional discussion related to current period acquisitions.

#### Note 9 – Income taxes

We account for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts. Valuation allowances are established when necessary to reduce deferred tax assets to amounts which are more likely than not to be realized.

We account for uncertainty in income taxes recognized in our financial statements using prescribed recognition thresholds and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on our tax returns. We had \$18.0 million and \$15.0 million of unrecognized tax benefits at June 30, 2011 and December 31, 2010, respectively, all of which would affect our effective income tax rate if recognized. We recorded a gross increase in unrecognized tax benefits of \$2.8 million for the six month period ended June 30, 2011. As of June 30, 2011, it is deemed reasonable that we will recognize tax benefits in the amount of \$3.6 million in the next twelve months due to the closing of open tax years. The nature of the uncertainty is related to deductions taken on returns that have not been examined by the applicable tax authority. Our continuing policy is to recognize interest and penalties related to income tax matters in income tax expense. As of June 30, 2011, we have approximately \$1.0 million accrued for interest related to uncertain tax positions. The tax years 2004 through 2010 remain open to examination by the major taxing jurisdictions to which we are subject.

Our provision for income taxes reflected an effective tax rate of 18% and 16% for the three month periods ended June 30, 2011 and 2010, respectively, and of 18% and 12% for the six month periods ended June 30, 2011 and 2010, respectively. For the three and six month periods ended June 30, 2011, our effective tax rate was lower than the U.S. federal statutory rate of 35% as a result of a tax benefit from equity awards that do not ordinarily result in a tax benefit, an enhanced deduction for certain research and development expenses, profits in foreign jurisdictions with reduced income tax rates and the U.S. federal research and development credit. For the three months ended June 30, 2010, our effective tax rate was lower than the U.S. federal statutory rate of 35% as a result of the partial release of a deferred tax asset valuation allowance, an enhanced deduction for certain research and development expenses and profits in foreign jurisdictions with reduced income tax rates. For the six months ended June 30, 2010, our effective tax rate was lower than the U.S. federal statutory rate of 35% as a result of the partial release of a deferred tax asset valuation allowance, an enhanced deduction for certain research and development expenses, profits in foreign jurisdictions with reduced income tax rates and a decrease in unrecognized tax benefits for uncertain tax positions.

Our earnings in Hungary are subject to a statutory tax rate of 19%. The difference between this rate and the statutory U.S. rate of 35% resulted in income tax benefits of \$4.0 million and \$3.5 million for the three month periods ended June 30, 2011 and 2010, respectively, and \$7.4 million and \$5.8 million for the six month periods ended June 30, 2011 and 2010, respectively. No countries other than Hungary had a significant impact on our effective tax rate. We have not entered into any advanced pricing or other agreements with the Internal Revenue Service with regard to any foreign jurisdictions.

The tax position of our Hungarian operation continues to benefit from assets created by the restructuring of our operations in Hungary in 2003. In addition, our research and development activities in Hungary continue to benefit from a tax law in Hungary that provides for an enhanced deduction for qualified research and development expenses. Partial release of the valuation allowance on assets from the restructuring and the enhanced tax deduction for research expenses resulted in income tax benefits of \$5.2 million and \$4.6 million for the three month periods ended June 30, 2011 and 2010, respectively, and \$9.9 million and \$7.7 million for the six month periods ended June 30, 2011 and 2010, respectively.

#### Note 10 – Comprehensive income

Our comprehensive income is comprised of net income, foreign currency translation, unrealized gains and losses on forward and option contracts and unrealized gains and losses on our investments designated as available for sale. Comprehensive income for the three and six month periods ended June 30, 2011 and 2010, was as follows (in thousands):

	Three Months Ended June 30, (unaudited)		Six Months Ended June 30, (unaudited)	
	2011	2010	2011	2010
Comprehensive income:				
Net income	\$26,548	\$24,602	\$57,009	\$42,955
Foreign currency translation gains (losses), net of taxes	2,148	(7,407 )	7,424	(11,369 )
Unrealized gains (losses) on derivative instruments, net of taxes	262	(3,747 )	2,631	(7,092 )
Unrealized gains (losses) on investments designated as available for sale, net of taxes	(580 )	(1,106 )	(1,004 )	771
Total comprehensive income	\$28,378	\$12,342	\$66,060	\$25,265

#### Note 11 – Stock-based compensation plans

### Stock option plans

Our stockholders approved the 1994 Incentive Stock Option Plan (the “1994 Plan”) on May 9, 1994. At the time of approval, 13,668,750 shares of our common stock were reserved for issuance under this plan. In 1997, an additional 10,631,250 shares of our common stock were reserved for issuance under this plan, and an additional 1,125,000 shares were reserved for issuance under this plan in 2004. The 1994 Plan terminated in May 2005, except with respect to outstanding awards previously granted thereunder.

Awards under the plan were either incentive stock options within the meaning of Section 422 of the Internal Revenue Code or nonqualified options. The right to purchase shares under the options vests over a five to ten-year period, beginning on the date of grant. Vesting of ten year awards may accelerate based on the Company’s previous year’s earnings and revenue growth but shares cannot accelerate to vest over a period of less than five years. Stock options must be exercised within ten years from date of grant. Stock options were issued with an exercise price which was equal to the market price of our common stock at the grant date. We estimate potential forfeitures of stock grants and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods. During the six month period ended June 30, 2011, we did not make any changes in accounting principles or methods of estimates related to the 1994 Plan.

### Restricted stock plans

Our stockholders approved our 2005 Incentive Plan (the “2005 Plan”) on May 10, 2005. At the time of approval, 4,050,000 shares of our common stock were reserved for issuance under this plan, as well as the number of shares which had been reserved but not issued under the 1994 Plan (our incentive stock option plan which terminated in May 2005), and any shares that returned to the 1994 Plan as a result of termination of options or repurchase of shares issued under such plan. The 2005 Plan, administered by the Compensation Committee of the Board of Directors, provided for granting of incentive awards in the form of restricted stock and restricted stock units (“RSUs”) to directors, executive officers and employees of the Company and its subsidiaries. Awards vest over a three, five or ten-year period, beginning on the date of grant. Vesting of ten year awards may accelerate based on the Company’s previous year’s earnings and growth but ten year awards cannot accelerate to vest over a period of less than five years. The 2005 Plan terminated on May 11, 2010, except with respect to outstanding awards previously granted thereunder. There were 3,362,304 shares of common stock that were reserved but not issued under the 1994 Plan and the 2005 Plan as of May 11, 2010.

Our stockholders approved our 2010 Incentive Plan (the “2010 Plan”) on May 11, 2010. At the time of approval, 3,000,000 shares of our common stock were reserved for issuance under this plan, as well as the 3,362,304 shares of common stock that were reserved but not issued under the 1994 Plan and the 2005 Plan as of May 11, 2010, and any shares that are returned to the 1994 Plan and the 2005 Plan as a result of forfeiture or termination of options or RSUs or repurchase of shares issued under these plans. The 2010 Plan, administered by the Compensation Committee of the Board of Directors, provides for granting of incentive awards in the form of restricted stock and RSUs to employees, directors and consultants of the Company and employees and consultants of any parent or subsidiary of the Company. Awards vest over a three, five or ten-year period, beginning on the date of grant. Vesting of ten year awards may accelerate based on the Company’s previous year’s earnings and growth but ten year awards cannot accelerate to vest over a period of less than five years. At June 30, 2011, there were 5,245,564 shares available for grant under the 2010 Plan.

We estimate potential forfeitures of RSUs and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up

adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods. During the six month period ended June 30, 2011, we did not make any changes in accounting principles or methods of estimates related to the 2010 Plan.

#### Employee stock purchase plan

Our employee stock purchase plan permits substantially all domestic employees and employees of designated subsidiaries to acquire our common stock at a purchase price of 85% of the lower of the market price at the beginning or the end of the purchase period. The plan has quarterly purchase periods generally beginning on February 1, May 1, August 1 and November 1 of each year. Employees may designate up to 15% of their compensation for the purchase of common stock under this plan. At June 30, 2011, we had 1,164,724 shares of common stock reserved for future employee purchases under this plan. During the six month period ended June 30, 2011, we issued 456,118 shares under this plan. The weighted average fair value of the employees' purchase rights for these shares was \$21.68 per share and was estimated using the Black-Scholes model. During the six month period ended June 30, 2011, we did not make any changes in accounting principles or methods of estimates related to the employee stock purchase plan.

#### Authorized Preferred Stock and Preferred Stock Purchase Rights Plan

We have 5,000,000 authorized shares of preferred stock. On January 21, 2004, our Board of Directors designated 750,000 of these shares as Series A Participating Preferred Stock in conjunction with its adoption of a Preferred Stock Rights Agreement (the "Rights Agreement") and declaration of a dividend of one preferred share purchase right (a "Right") for each share of common stock outstanding held as of May 10, 2004 or issued thereafter. Each Right will entitle its holder to purchase one one-thousandth of a share of National Instruments' Series A Participating Preferred Stock at an exercise price of \$200, subject to adjustment, under certain circumstances. The Rights Agreement was not adopted in response to any effort to acquire control of National Instruments.

The Rights only become exercisable in certain limited circumstances following the tenth day after a person or group announces acquisitions of or tender offers for 20% or more of our common stock. In addition, if an acquirer (subject to certain exclusions for certain current stockholders of National Instruments, an "Acquiring Person") obtains 20% or more of our common stock, then each Right (other than the Rights owned by an Acquiring Person or its affiliates) will entitle the holder to purchase, for the exercise price, shares of our common stock having a value equal to two times the exercise price. Under certain circumstances, our Board of Directors may redeem the Rights, in whole, but not in part, at a purchase price of \$0.01 per Right. The Rights have no voting privileges and are attached to and automatically traded with our common stock until the occurrence of specified trigger events. The Rights will expire on the earlier of May 10, 2014 or the exchange or redemption of the Rights.

There were not any shares of preferred stock issued and outstanding at June 30, 2011.

#### Note 12 – Segment information

We determine operating segments using the management approach. The management approach designates the internal organization that is used by management for making operating decisions and assessing performance as the source of our operating segments. It also requires disclosures about products and services, geographic areas and major customers.

We have defined our operating segment based on geographic regions. We sell our products in three geographic regions. Our sales to these regions share similar economic characteristics, similar product mix, similar customers, and similar distribution methods. Accordingly, we have elected to aggregate these three geographic regions into a single operating segment. Revenue from the sale of our products which are similar in nature and software maintenance are reflected as total net sales in our Consolidated Statements of Income.



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Total net sales, operating income, interest income and long-lived assets, classified by the major geographic areas in which we operate, are as follows (in thousands):

	Three Months Ended June 30, (unaudited)		Six Months Ended June 30, (unaudited)	
	2011	2010	2011	2010
Net sales:				
Americas:	\$ 103,713	\$ 90,072	\$ 201,077	\$ 169,269
Europe:	76,383	59,876	147,439	117,799
Asia Pacific:	73,188	61,769	142,618	115,740
	\$ 253,284	\$ 211,717	\$ 491,134	\$ 402,808
	Three Months Ended June 30, (unaudited)		Six Months Ended June 30, (unaudited)	
	2011	2010	2011	2010
Operating income:				
Americas	\$18,700	\$17,915	\$38,785	\$31,294
Europe	32,542	29,023	68,695	56,062
Asia Pacific	28,727	19,940	51,869	37,590
Unallocated:				
Research and development expenses	(47,027 )	(36,395 )	(89,895 )	(74,941 )
	\$32,942	\$30,483	\$69,454	\$50,005
	Three Months Ended June 30, (unaudited)		Six Months Ended June 30, (unaudited)	
	2011	2010	2011	2010
Interest income:				
Americas	\$121	\$145	\$270	\$256
Europe	195	206	353	365
Asia Pacific	28	20	62	50
	\$344	\$371	\$685	\$671
			June 30, 2011 (unaudited)	December 31, 2010
Long-lived assets:				
Americas			\$108,616	\$103,033
Europe			41,802	40,083
Asia Pacific			21,088	17,294
			\$171,506	\$160,410

Total sales outside the U. S. for the three month periods ended June 30, 2011 and 2010, were \$157.6 million and \$128.2 million, respectively, and \$306.5 million and \$247.6 million for the six month periods ended June 30, 2011 and 2010, respectively.

Note 13 – Commitments and contingencies

We offer a one-year limited warranty on most hardware products, with a two or three-year warranty on a subset of our hardware products, which is included in the sales price of many of our products. Provision is made for estimated future warranty costs at the time of the sale for the estimated costs that may be incurred under the basic limited warranty. Our estimate is based on historical experience and product sales during this period.

The warranty reserve for the six month periods ended June 30, 2011 and 2010, respectively, was as follows (in thousands):

	Six Months Ended June 30, (unaudited)	
	2011	2010
B a l a n c e a t t h e b e g i n n i n g o f t h e period	\$921	\$921
A c c r u a l s f o r w a r r a n t i e s i s s u e d d u r i n g t h e period	1,515	998
S e t t l e m e n t s m a d e ( i n c a s h o r i n k i n d ) d u r i n g t h e period	(1,192 )	(998 )
B a l a n c e a t t h e e n d o f t h e period	\$1,244	\$921

As of June 30, 2011, we have non-cancelable purchase commitments with various suppliers of customized inventory and inventory components totaling approximately \$9.1 million over the next twelve months.

As of June 30, 2011, we have outstanding guarantees for payment of customs and foreign grants totaling approximately \$4.6 million, which are generally payable over the next twelve months.

From November 1999 to May 2011, we sold products to the U.S. government under a contract with the General Services Administration ("GSA"). During such time, our sales under the contract were approximately 2% of our total sales. Our contract with GSA contains a price reduction or "most favored customer" pricing provision. We have been in discussions with GSA regarding our compliance with this pricing provision and have provided GSA with information regarding our pricing practices. GSA recently conducted an on-site review of our GSA pricing practices and has orally informed us that GSA does not agree with our previous determination of the potential non-compliance amount. GSA has not informed us of its estimate of the non-compliance amount and GSA has not made any formal demand for pricing adjustments related to our GSA contract. However, GSA may make such a demand in the future, and there can be no assurance that the amount of any such demand, if we were required to pay it, would not have a material adverse impact on our results of operations. If GSA believes that our pricing practices did not comply with the contract, GSA could conduct a formal investigation of such matter or could refer such matter to the U.S. Department of Justice for investigation, including an investigation regarding potential violations of the False Claims Act, which could result in litigation and the possible imposition of a damage remedy that includes treble damages plus civil penalties, and could also result in us being suspended or debarred from future government contracting. Due to the complexities of conducting business with GSA, the relatively small amount of revenue we realized from our GSA contract, and our belief that we can continue to sell our products to U.S. government agencies through other contracting methods, we cancelled our contract with GSA in April 2011, effective May 2011. To date, we have not experienced any material adverse impact on our results of operations as a result of the cancellation of our GSA contract.

#### Note 14 – Recently issued accounting pronouncements

In October 2009, the FASB updated FASB ASC 605, Revenue Recognition (FASB ASC 605) that amended the criteria for separating consideration in multiple-deliverable arrangements. The amendments establish a selling price

hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. The amendments will change the application of the residual method of allocation and require that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method. The relative selling price method allocates any discount in the arrangement proportionally to each deliverable on the basis of each deliverable's selling price. This update will be effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. On January 1, 2011, we adopted the accounting update as required on a prospective basis. The adoption of the amended revenue recognition rules did not change the units of accounting for our revenue transactions. It also did not significantly change how we allocated the arrangement consideration to the various units of accounting or the timing of revenue. The impact of our adoption was not material to our consolidated financial statements for the three and six month periods ended June 30, 2011. We cannot reasonably estimate the effect of adopting these standards on future financial periods as the impact will vary depending on the nature and volume of new or materially modified sales arrangements in any given period. In addition, as our, or our competitors', pricing practices and strategies evolve, we may modify our pricing practices in the future. This may result in a different allocation of revenue to the deliverables in the multiple element arrangements from the current fiscal quarter, which may change the pattern and timing of revenue recognition for these elements, but will not change the total revenue recognized for the arrangement.

In January 2010, the FASB updated FASB ASC 820, Fair Value Measurements and Disclosures (FASB ASC 820) that requires additional disclosures and clarifies existing disclosures regarding fair value measurements. The additional disclosures include (i) transfers in and out of Levels 1 and 2 and (ii) activity in Level 3 fair value measurements. The update provides amendments that clarify existing disclosures on level of disaggregation and disclosures about inputs and valuation techniques. This update is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. These disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. We adopted the update on January 1, 2010 as required and subsequently adopted on January 1, 2011, the update surrounding disclosures on Level 3 fair value measurements and concluded it did not have a material impact on our consolidated financial position or results of operations. In May 2011, the FASB updated FASB ASC 820 that resulted in common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards (IFRSs). Some of the amendments clarify the FASB's intent about the application of existing fair value measurement requirements. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments are to be applied prospectively and are effective during interim and annual periods beginning after December 15, 2011. We are currently evaluating the requirements of this update and have not yet determined the impact on our consolidated financial statements.

In June 2011, the FASB updated FASB ASC 220, Comprehensive Income (FASB ASC 220) that gives an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The update does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The update does not change the option for an entity to present components of other comprehensive income either net of related tax effects or before related tax effects, with one amount shown for the aggregate income tax expense or benefit related to the total of other comprehensive income items. The update does not affect how earnings per share is calculated or presented. The update should be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We are currently evaluating the requirements of this update and have not yet determined the impact on our consolidated financial statements.

## Note 15 – Litigation

We are not currently a party to any material litigation. However, in the ordinary course of our business, we are involved in legal actions, both as plaintiff and defendant, and could incur uninsured liability in any one or more of them. We also periodically receive notifications from various third parties related to alleged infringement of patents or intellectual property rights, commercial disputes or other matters. No assurances can be given with respect to the extent or outcome of any future litigation or dispute.

## Note 16 – Acquisitions

## AWR Corporation

On June 30, 2011, we acquired all of the outstanding shares of AWR Corporation (AWR), a privately held company that is a leading supplier of electronic design automation software for designing radio frequency and high-frequency components and systems for the semiconductor, aerospace and defense, communications and test equipment industries. The acquisition is expected to improve customer productivity through increased interoperability between upfront design and validation and production test functions. The purchase price of the acquisition was \$66 million consisting of \$54 million in cash and a three-year earn-out arrangement. We funded the purchase price from existing cash balances. The range of potential undiscounted payments that we could be required to make under the earn-out arrangement is between \$0 and \$29 million. The earn-out payments amount to a maximum of \$10 million per year for three years, and are payable if AWR achieves certain revenue and operating income targets. The fair value of the earn-out arrangement was estimated at \$12 million using the income approach, the key assumptions which included probability-weighted revenue and operating expense growth projections.

The allocation of the purchase price was determined using the preliminary fair value of assets and liabilities acquired as of June 30, 2011. The preliminary allocation of the purchase price was based upon a preliminary valuation which is subject to change within the measurement period up to one year from the acquisition date. The primary areas which are not finalized are the fair value of contingent consideration, deferred revenue, intangible assets and related deferred taxes. Our consolidated financial statements include the operating results from the date of acquisition. Pro-forma results of operations have not been presented because the effects of those operations were not material. The following table summarizes the allocation of the purchase price of AWR (in thousands):

	Amount
Net tangible assets acquired	\$10,718
Acquired core technology	25,978
Trade names	3,715
Customer relationships	1,992
Deferred tax liability	(10,351 )
Goodwill	34,343
Total	\$66,395

Goodwill is not deductible for tax purposes. Acquired core technology, trade names and customer relationships each have useful lives of 5 years from the date of acquisition.

## Phase Matrix Inc.

On May 20, 2011, we acquired all of the outstanding shares of Phase Matrix, Inc. (PMI), a privately held company that designs and manufactures radio frequency and microwave test and measurement instruments, subsystems and components. The acquisition is expected to speed our deployment of high-performance RF and wireless technologies to our production test and R&D customers. The purchase price of the acquisition was \$40.7 million consisting of \$38.9 million in cash and \$1.8 million in shares of our common stock. We funded the cash portion of the purchase

price from existing cash balances.

The allocation of the purchase price was determined using the fair value of assets and liabilities acquired as of May 20, 2011. Our consolidated financial statements include the operating results from the date of acquisition. Pro-forma results of operations have not been presented because the effects of those operations were not material. The following table summarizes the allocation of the purchase price of Phase Matrix, Inc. (in thousands):

	Amount
Net tangible assets acquired	\$5,624
Acquired core technology	4,282
I n - p r o c e s s r e s e a r c h a n d development	1,407
Non-competition agreements	333
Royalty agreements	271
Trademarks	361
Customer relationships	862
Backlog	815
Goodwill	26,725
Total	\$40,680

Goodwill is deductible for tax purposes. Acquired core technology, in process R&D, non-competition agreements, royalty agreements, trademarks, customer relationships and backlog have useful lives of 5 years, 5 years, 3 years, 8 years, 4 years, 5 years and 9 months, respectively, from the date of acquisition. These assets are also deductible for tax purposes.

#### Other acquisitions

On December 31, 2010, we acquired all of the outstanding shares of a privately-held company for \$2.3 million in net cash with an additional \$500,000 in net cash to be paid out over the next three years. The purchase price for this acquisition included net working capital of \$187,000, amortizable intangible assets of \$1.5 million, and goodwill of \$1.1 million. Our consolidated financial statements include the operating results of the acquired company from the date of acquisition.

On February 1, 2010, we acquired all of the outstanding shares of a privately-held company for \$2.2 million in net cash, \$3.0 million in shares of our common stock with the remainder to be paid in cash over the next four years. The purchase price allocation for this acquisition included net working capital of \$1.1 million, amortizable intangible assets of \$5.0 million, and goodwill of \$5.0 million. Our consolidated financial statements include the operating results of the acquired company from the date of acquisition.

For these acquisitions, goodwill is not deductible for tax purposes. Existing technology, non-competition agreements, trademarks, and customer relationships have useful lives of 5 years, 3 years, 3 years, and 5 years, respectively, from the date of acquisition. These assets are not deductible for tax purposes.

Pro forma results of operations have not been presented because the effect of these acquisitions is not material either individually or in the aggregate to our consolidated results of operations.

#### Note 17 – Subsequent events

We have evaluated subsequent events through the date the financial statements were issued.

On July 22, 2011, our Board of Directors declared a quarterly cash dividend of \$0.10 per common share, payable August 29, 2011, to shareholders of record on August 8, 2011.

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

This Quarterly Report on Form 10-Q contains 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. Any statements contained herein regarding our future financial performance or operations (including, without limitation, statements to the effect that we "believe," "expect," "plan," "may," "will," "project," "continue," or "estimate" or other variations thereof or comparable terminology or the negative thereof) should be considered forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of a number of important factors, including those set forth under the heading "Risk Factors" beginning on page 38, and the discussion below. Readers are also encouraged to refer to the documents regularly filed by us with the Securities and Exchange Commission, including our Annual Report on Form 10-K for further discussion of our business and the risks attendant thereto.

Overview

National Instruments Corporation ("we", "us" or "our") is a leading supplier of measurement and automation products that engineers and scientists use in a wide range of industries. These industries comprise a large and diverse market for design, control and test applications. We provide flexible application software and modular, multifunctional hardware that users combine with industry-standard computers, networks and third party devices to create measurement, automation and embedded systems, which we also refer to as "virtual instruments". Our approach gives customers the ability to quickly and cost-effectively design, prototype and deploy unique custom-defined solutions for their design, control and test application needs. We sell to a large number of customers in a wide variety of industries. We have been profitable in every year since 1990.

The key strategies that we focus on in running our business are the following:

Expanding our broad customer base

We strive to increase our already broad customer base by serving a large market on many computer platforms, through a global marketing and distribution network. We also seek to acquire new technologies and expertise from time to time in order to open new opportunities for our existing product portfolio.

Maintaining a high level of customer satisfaction

To maintain a high level of customer satisfaction we strive to offer innovative, modular and integrated products through a global sales and support network. We strive to maintain a high degree of backwards compatibility across different platforms in order to preserve the customer's investment in our products. In this time of intense global competition, we believe it is crucial that we continue to offer products with quality and reliability, and that our products provide cost-effective solutions for our customers.

Leveraging external and internal technology

Our product strategy is to provide superior products by leveraging generally available technology, supporting open architectures on multiple platforms and by leveraging our core technologies such as custom application specific integrated circuits ("ASICs") across multiple products.

We sell into test and measurement ("T&M") and industrial/embedded applications in a broad range of industries and as such are subject to the economic and industry forces which drive those markets. It has been our experience that the performance of these industries and our performance is impacted by general trends in industrial production for the

global economy and by the specific performance of certain vertical markets that are intensive consumers of measurement technologies. Examples of these markets are semiconductor capital equipment, telecom, defense, aerospace, automotive and others

In assessing our business, we consider the trends in the Global Purchasing Managers Index (“PMI”) published by JP Morgan, global industrial production as well as industry reports on the specific vertical industries that we target. Over the last 24 months, the PMI has reflected an expanding industrial economy by rising from a value of 50 in July 2009, to a high of 58 in February 2011, and having an average value of 55 over that time period. At June 30, 2011, the PMI was at 52 a decline from the reading of 56 at March 31, 2011. Historically, our business cycles have followed the expansion and contraction cycles in the PMI. During the six month period ended June 30, 2011, the PMI had an average value of 55. A value above 50 is indicative of expansion in the global industrial economy. We are unable to predict whether the current expansion cycle, as measured by the PMI, will be sustained throughout 2011. If this expansion is not sustained, even at moderate levels, it could have an adverse effect on the spending patterns of businesses including our current and potential customers which could adversely affect our revenues and therefore harm our business and result of operations.

We distribute our software and hardware products primarily through a direct sales organization. We also use independent distributors, OEMs, VARs, system integrators and consultants to market our products. We have sales offices in the U.S. and sales offices and distributors in key international markets. Sales outside of the Americas accounted for 59% and 57% of our revenues during the three month periods ended June 30, 2011 and 2010, respectively and 59% and 58% of our revenues during the six month periods ended June 30, 2011 and 2010, respectively. The vast majority of our foreign sales are denominated in the customers’ local currency, which exposes us to the effects of changes in foreign currency exchange rates. We expect that a significant portion of our total revenues will continue to be derived from international sales. (See Note 12 - Segment information of Notes to Consolidated Financial Statements for details concerning the geographic breakdown of our net sales, operating income, interest income and long-lived assets).

We manufacture a substantial majority of our products at our facilities in Debrecen, Hungary. Additional production primarily of low volume or newly introduced products is done in Austin, Texas. Our product manufacturing operations can be divided into four areas: electronic circuit card and module assembly; chassis and cable assembly; technical manuals and product support documentation; and software duplication. We manufacture most of the electronic circuit card assemblies and modules in-house, although subcontractors are used from time to time. We currently use a subcontractor in Asia to manufacture a significant portion of our chassis but we are steadily moving an increasing percentage of this production in-house. We manufacture some of our electronic cable assemblies in-house, but many assemblies are produced by subcontractors. We primarily subcontract our software duplication, our technical manuals and product support documentation.

We believe that our long-term growth and success depend on delivering high quality software and hardware products on a timely basis. Accordingly, we focus significant efforts on research and development. We focus our research and development efforts on enhancing existing products and developing new products that incorporate appropriate features and functionality to be competitive with respect to technology, price and performance. Our success also is dependent on our ability to obtain and maintain patents and other proprietary rights related to technologies used in our products. We have engaged in litigation and where necessary, will likely engage in future litigation to protect our intellectual property rights. In monitoring and policing our intellectual property rights, we have been and may be required to spend significant resources.

Our operating results fluctuate from period to period due to changes in global economic conditions and a number of other factors. As a result, we believe our historical results of operations should not be relied upon as indications of future performance. There can be no assurance that our net sales will grow or that we will remain profitable in future periods.



## Current business outlook

Many of the industries we serve have historically been cyclical and have experienced periodic downturns. Our customers across all industries and geographic regions demonstrated increased order patterns throughout 2010 and during the six month period ended June 30, 2011. These positive order trends are consistent with the expansion we have seen in the global industrial economy as measured by the global PMI which has ranged from 57 in January 2011 to 52 in June 2011. We have seen these positive trends across all geographic regions and across all the vertical markets that we serve although the strength of the trend varies by region and by market. We are unable to predict whether the current expansion cycle, as measured by the PMI, will be sustained throughout 2011. If this expansion cannot be sustained, it could have an adverse effect on the spending patterns of businesses including our current and potential customers which could adversely affect our revenues and therefore harm our business and result of operations. Our key strategies are to maintain a stable gross margin and to optimize our operating cost structure while maintaining strong employee productivity.

## Results of Operations

The following table sets forth, for the periods indicated, the percentage of net sales represented by certain items reflected in our Consolidated Statements of Income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(unaudited)			
Net sales:				
Americas	40.9 %	42.5 %	40.9 %	42.0 %
Europe	30.2	28.3	30.0	29.3
Asia Pacific	28.9	29.2	29.1	28.7
Consolidated net sales	100.0	100.0	100.0	100.0
Cost of sales	22.1	23.0	22.1	22.8
Gross profit	77.9	77.0	77.9	77.2
Operating expenses:				
Sales and marketing	38.0	37.4	37.3	38.2
Research and development	18.5	17.2	18.3	18.6
General and administrative	8.4	8.0	8.2	8.0
Total operating expenses	64.9	62.6	63.8	64.8
Operating income	13.0	14.4	14.1	12.4
Other income (expense):				
Interest income	0.1	0.2	0.1	0.2
Net foreign exchange gain (loss)	(0.2 )	(1.0 )	(0.1 )	(0.7 )
Other income (expense), net	(0.2 )	0.2	-	0.2
Income before income taxes	12.7	13.8	14.1	12.1
Provision for income taxes	2.2	2.2	2.5	1.4
Net income	10.5 %	11.6 %	11.6 %	10.7 %

## Results of Operations for the Three and Six Month Periods Ended June 30, 2011 and 2010

In the three month period ended June 30, 2011, we experienced continued strong revenue growth and an all time revenue record for a quarter. We were also pleased by our ability to deliver a record operating profit for a second quarter, while significantly increasing our investment in research and development and field sales.

Net Sales. Our consolidated net sales were \$253 million and \$212 million for the three month periods ended June 30, 2011 and 2010, respectively, an increase of 20%. For the same periods, product sales were \$233 million and \$195 million, respectively, an increase of 20% and software maintenance sales were \$20 million and \$17 million, respectively, an increase of 19%. Products in the areas of virtual instrumentation and graphical system design, which comprised approximately 94% of our revenue in the three month period ended June 30, 2011, saw a year-over-year revenue increase of 21%. Instrument control products, which comprised approximately 6% of our revenues in the three month period ended June 30, 2011, saw a year-over-year revenue increase of 6%. In the three month period ended June 30, 2010, products in the areas of virtual instrumentation and graphical system design comprised approximately 93% of our revenue while instrument control products comprised approximately 7% of our revenues.

For the six month periods ended June 30, 2011 and 2010, our consolidated net sales were \$491 million and \$403 million, respectively, an increase of 22%. For the same periods, product sales were \$452 million and \$370 million, respectively, an increase of 22% and software maintenance sales were \$39 million and \$33 million, respectively, an increase of 21%. Products in the areas of virtual instrumentation and graphical system design, which comprised approximately 93% of our revenue in the six month period ended June 30, 2011, saw a year-over-year revenue increase of 23%. Instrument control products, which comprised approximately 7% of our revenues in the six month period ended June 30, 2011, saw a year-over-year revenue increase of 12%. In the six month period ended June 30, 2010, products in the areas of virtual instrumentation and graphical system design comprised approximately 93% of our revenue while instrument control products comprised approximately 7% of our revenues.

Revenues from our instrument control products are the most sensitive to the cycles of the global industrial economy. Our overall revenue increases in the three and six month periods ended June 30, 2011 compared to the same periods in 2010, are attributed to increases in sales volume across all geographic regions of our business. We did not take any significant action with regard to pricing during the three and six month periods ended June 30, 2011 and 2010.

Large orders, defined as orders with a value greater than \$20,000, grew by 39%, year over year, during the three month period ended June 30, 2011 and grew by 34%, year over year, during the six month period ended June 30, 2011. During the three and six month periods ended June 30, 2011, these orders were 46% and 44%, respectively, of our total sales. During the three and six month periods ended June 30, 2010, these orders were 40% and 39%, respectively, of our total sales. Larger orders may be more sensitive to changes in the global industrial economy, may be subject to greater discount variability and may contract at a faster pace during an economic downturn.

For the three month periods ended June 30, 2011 and 2010, net sales in the Americas were \$104 million and \$90 million, respectively, an increase of 15%. For these same periods, sales in the Americas, as a percentage of consolidated sales were 41% and 43%, respectively. In Europe, net sales were \$76 million and \$60 million in 2011 and 2010, respectively, an increase of 28%. For these same periods, sales in Europe, as a percentage of consolidated sales were 30% and 28%, respectively. In Asia, net sales were \$73 million and \$62 million, respectively, an increase of 18%. For these same periods, sales in Asia, as a percentage of consolidated sales were 29% and 29%, respectively.

For the six month periods ended June 30, 2011 and 2010, net sales in the Americas were \$201 million and \$169 million, respectively, an increase of 19%. For these same periods, sales in the Americas, as a percentage of consolidated sales were 41% and 42%, respectively. In Europe, net sales were \$147 million and \$118 million in 2011 and 2010, respectively, an increase of 25%. For these same periods, sales in Europe, as a percentage of consolidated sales were 30% and 29%, respectively. In Asia, net sales were \$143 million and \$116 million, respectively, an increase of 23%. For these same periods, sales in Asia, as a percentage of consolidated sales were 29% and 29%, respectively.

We expect sales outside of the Americas to continue to represent a significant portion of our revenue. We intend to continue to expand our international operations by increasing our presence in existing markets, adding a presence in some new geographical markets and continuing the use of distributors to sell our products in some countries. We anticipate that sales growth in Asia may continue to be strong relative to the Americas and Europe and continue to

grow as a percentage of our total net sales.

Almost all of the sales made by our direct sales offices in the Americas, outside of the U.S., in Europe and in Asia Pacific are denominated in local currencies, and accordingly, the U.S. dollar equivalent of these sales is affected by changes in foreign currency exchange rates. For the three month period ended June 30, 2011, in local currency terms, our consolidated net sales increased by \$33 million or 16%, Americas sales increased by \$13 million or 14%, European sales increased by \$13 million or 23%, and sales in Asia Pacific increased by \$7 million or 12%, compared to the three month period ended June 30, 2010. During this same period, the change in exchange rates had the effect of increasing our consolidated sales by \$10 million or 5%, increasing Americas sales by \$856,000 or 1%, increasing European sales by \$4.1 million or 7%, and increasing sales in Asia Pacific by \$4.5 million or 7%.

For the six month period ended June 30, 2011, in local currency terms, our consolidated net sales increased by \$82 million or 20%, Americas sales increased by \$31 million or 18%, European sales increased by \$28 million or 24%, and sales in Asia Pacific increased by \$23 million or 20%, compared to the six month period ended June 30, 2010. During this same period, the change in exchange rates had the effect of increasing our consolidated sales by \$8 million or 2%, increasing Americas sales by \$853,000 or 0.5%, increasing European sales by \$3.1 million or 3%, and increasing sales in Asia Pacific by \$4.5 million or 4%.

To help protect against a reduction in value caused by a fluctuation in foreign currency exchange rates of forecasted foreign currency cash flows resulting from international sales, we have a foreign currency cash flow hedging program. We hedge portions of our forecasted revenue denominated in foreign currencies with forward contracts. During the three month periods ended June 30, 2011 and 2010, these hedges had the effect of decreasing our consolidated sales by \$983,000 and increasing our consolidated sales by \$2.0 million, respectively. During the six month periods ended June 30, 2011 and 2010, these hedges had the effect of decreasing our consolidated sales by \$1.7 million and increasing our consolidated sales by \$3.0 million, respectively. (See Note 5 - Derivative instruments and hedging activities of Notes to Consolidated Financial Statements for further discussion regarding our cash flow hedging program and its related impacted on our consolidated sales for 2011 and 2010).

**Gross Profit.** For the three month periods ended June 30, 2011 and 2010, gross profit was \$197 million and \$163 million, respectively, an increase of 21%. For these same periods, as a percentage of sales, gross profit was 78% and 77%, respectively. For the six month periods ended June 30, 2011 and 2010, gross profit was \$383 million and \$311 million, respectively, an increase of 23%. For these same periods, as a percentage of sales, gross profit was 78% and 77%, respectively. Our gross margins as a percentage of sales continue to benefit from our cost reduction strategies that we began implementing in 2009. This along with robust sales growth has allowed us to achieve and maintain stability in our gross margin percentage.

For the three month periods ended June 30, 2011 and 2010, the change in exchange rates had the effect of increasing our cost of sales by \$1.4 million or 3% and increasing our cost of sales by \$670,000 or 3%, respectively. For the six month periods ended June 30, 2011 and 2010, the change in exchange rates had the effect of increasing our cost of sales by \$2.6 million or 3% and increasing our cost of sales by \$1.4 million or 3%, respectively. To help protect against changes in our cost of sales caused by a fluctuation in foreign currency exchange rates of forecasted foreign currency cash flows, we have a foreign currency cash flow hedging program. We hedge portions of our forecasted costs of sales denominated in foreign currencies with forward contracts. During the three month periods ended June 30, 2011 and 2010, these hedges had the effect of decreasing our cost of sales by \$376,000 and \$642,000, respectively. During the six month periods ended June 30, 2011 and 2010, these hedges had the effect of decreasing our cost of sales by \$750,000 and \$1.4 million, respectively. (See Note 5 - Derivative instruments and hedging activities of Notes to Consolidated Financial Statements for further discussion regarding our cash flow hedging program and its related impacted on our consolidated sales for 2011 and 2010).

**Operating Expenses.** For the three month periods ended June 30, 2011 and 2010, operating expenses were \$164 million and \$133 million, respectively, an increase of 24%. This increase in our operating expenses was due to higher

personnel related expenses of \$11 million which included commissions, variable compensation and benefits, higher expenses related to marketing and outside services of \$4.8 million, higher expenses for building and equipment of \$3.1 million, higher travel related expenses of \$2.9 million and higher equity based compensation of \$1.1 million. Over the same period, the net impact of changes in foreign currency exchange rates increased our operating expense by \$6 million. The increase in personnel expenses is related to a net increase in our average headcount of 562 employees.

For the six month periods ended June 30, 2011 and 2010, operating expenses were \$313 million and \$261 million respectively, an increase of 20%. This increase in our operating expenses was due to higher personnel related expenses of \$19 million which included commissions, variable compensation and benefits as well as the fact that temporary cost cutting measures enacted in 2009 were still in place in January of 2010, higher expenses related to marketing and outside services of \$10.5 million, higher expenses for building and equipment of \$5.9 million, higher travel related expenses of \$5.5 million and higher equity based compensation of \$864,000. Over the same period, the net impact of changes in foreign currency exchange rates increased our operating expense by \$8 million. The increase in personnel expenses is related to a net increase in our average headcount of 429 employees.

As a percentage of net sales, operating expenses in the three month periods ended June 30, 2011 and 2010, were 65% and 63%, respectively. The year over year increase in our operating expenses as a percentage of sales is attributed to the fact that we grew our overall operating expenses by 24% while our net sales grew by 20%. For the six month periods ended June 30, 2011 and 2010, operating expenses as a percentage of net sales were 64% and 65%, respectively. This year over year decrease in our operating expenses as a percentage of net sales is attributed to the fact that we grew our overall operating expenses by 20% while our net sales grew by 22%.

We believe that our long-term growth and success depends on developing high quality software and hardware products and delivering those products to our customers on a timely basis. To that end, we have made investments in research and development and our field sales force a priority in 2011. In the three month and six month periods ended June 30, 2011, we increased our research and development staff by 131 and 211, respectively, or 8% and 14%, respectively, and our field sales force by 30 and 62, respectively, or 5% and 11%, respectively. During the remainder of 2011, we expect to continue our investment in these areas although we expect the rate of growth to decrease in the third and fourth quarters relative to the first half of the year.

**Operating Income.** For the three month periods ended June 30, 2011 and 2010, operating income was \$33 million and \$30 million, respectively, an increase of 8%. As a percentage of net sales, operating income was 13% and 14% respectively, in these same periods. For the six month periods ended June 30, 2011 and 2010, operating income was \$69 million and \$50 million, respectively, an increase of 39%. As a percentage of net sales, operating income was 14% and 12% respectively, in these same periods.

**Interest Income.** For the three month periods ended June 30, 2011 and 2010, interest income was \$344,000 and \$371,000, respectively, a decrease of 7%. For the six month periods ended June 30, 2011 and 2010, interest income was \$685,000 and \$671,000, respectively, an increase of 2%. We continued to see low yields for high quality investment alternatives that comply with our corporate investment policy. We do not expect yields in these types of investments to increase during the remainder of 2011.

**Net Foreign Exchange (Loss).** For the three month periods ended June 30, 2011 and 2010, net foreign exchange (loss) was \$ (486,000) and \$ (2.2) million, respectively. During the six month periods ended June 30, 2011 and 2010, net foreign exchange (loss) was \$(709,000) and \$(2.9) million, respectively. These results are attributable to movements in the foreign currency exchange rates between the U.S. dollar and foreign currencies in subsidiaries for which our functional currency is not the U.S. dollar. During the three and six month periods ended June 30, 2011, the U.S. dollar has generally declined against most of the major currencies in the markets in which we do business. Although this decline has been gradual, we cannot predict the direction or degree of future movements. In the past, we have noted that significant volatility in foreign currency exchange rates in the markets in which we do business has had a

significant impact on the revaluation of our foreign currency denominated firm commitments, on our ability to forecast our U.S. dollar equivalent revenues and expenses and on the effectiveness of our hedging programs. In the past, these dynamics have also adversely affected our revenue growth in international markets and may pose similar challenges in the future. We recognize the local currency as the functional currency in virtually all of our international subsidiaries.

We utilize foreign currency forward contracts to hedge our foreign denominated net foreign currency balance sheet positions to help protect against the change in value caused by a fluctuation in foreign currency exchange rates. We typically hedge up to 90% of our outstanding foreign denominated net receivable or payable positions and typically limit the duration of these foreign currency forward contracts to approximately 90 days. The gain or loss on these derivatives as well as the offsetting gain or loss on the hedged item attributable to the hedged risk is recognized in current earnings under the line item "Net foreign exchange gain (loss)". Our hedging strategy reduced our foreign exchange gains by \$1.1 million in the three month period ended June 30, 2011 and reduced our foreign exchange losses by \$937,000 in three month period ended June 30, 2010. Our hedging strategy reduced our foreign exchange gains by \$2.1 million in the six month period ended June 30, 2011 and reduced our foreign exchange gains by \$1.4 million in six month period ended June 30, 2010.

Provision for Income Taxes. For the three month periods ended June 30, 2011 and 2010, our provision for income taxes reflected an effective tax rate of 18% and 16%, respectively. For the six month periods ended June 30, 2011 and 2010, our provision for income taxes reflected an effective tax rate of 18% and 12%, respectively. The factors that caused our effective tax rate to change year-over-year are detailed in the table below:

	Three Months Ended June 30, 2011	Six Months Ended June 30, 2011
	(Unaudited)	
Effective tax rate for the three and six month periods ended June 30, 2010	16%	12%
Change in unrecognized tax benefits for uncertain tax positions	(1)%	2%
Decreased profits in foreign jurisdictions wi		