

IPG PHOTONICS CORP  
Form 10-Q  
May 11, 2009

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**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 March 31, 2009**

**OR**

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

**Commission File Number 001-33155**

**IPG PHOTONICS CORPORATION**

**(Exact name of registrant as specified in its charter)**

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

**04-3444218  
(I.R.S. Employer  
Identification Number)**

**50 Old Webster Road, Oxford, Massachusetts  
(Address of principal executive offices)**

**01540  
(Zip code)**

**(508) 373-1100**

**(Registrant's telephone number, including area code)**

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  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

As of May 7, 2009, there were 45,369,925 shares of the registrant's common stock issued and outstanding.



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**PART I FINANCIAL INFORMATION**  
**ITEM 1. UNAUDITED INTERIM FINANCIAL STATEMENTS**  
**IPG PHOTONICS CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

|  | <b>March 31,<br/>2009</b>                                      | <b>December<br/>31,<br/>2008</b> |
|--|--|----------------------------------|
|  | <b>(In thousands, except share and<br/>per<br/>share date)</b> |                                  |
| <b>ASSETS</b>  |  |                                  |
| <b>CURRENT ASSETS:</b>   |  |                                  |
| Cash and cash equivalents  | \$ 71,601  | \$ 51,283                        |
| Accounts receivable, net   | 29,740   | 41,842                           |
| Inventories, net   | 66,445   | 72,555                           |
| Income taxes receivable  | 1,585  | 1,968                            |
| Prepaid expenses and other current assets  | 6,265  | 7,200                            |
| Deferred income taxes  | 8,042  | 6,175                            |
| <br>   |  |                                  |
| Total current assets   | 183,678  | 181,023                          |
| DEFERRED INCOME TAXES  | 2,765  | 2,400                            |
| PROPERTY, PLANT AND EQUIPMENT, Net   | 112,865  | 114,492                          |
| OTHER ASSETS   | 14,497   | 15,303                           |
| <br>   |  |                                  |
| <b>TOTAL</b>   | <b>\$ 313,805</b>  | <b>\$ 313,218</b>                |
| <br><b>LIABILITIES AND STOCKHOLDERS EQUITY</b>   |  |                                  |
| <b>CURRENT LIABILITIES:</b>  |  |                                  |
| Revolving line-of-credit facilities  | \$ 29,760  | \$ 19,769                        |
| Current portion of long-term debt  | 1,333  | 1,333                            |
| Accounts payable   | 5,029  | 7,739                            |
| Accrued expenses and other liabilities   | 17,507   | 17,988                           |
| Deferred income taxes  | 337  | 1,690                            |
| Income taxes payable   | 2,364  | 507                              |
| <br>   |  |                                  |
| Total current liabilities  | 56,330   | 49,026                           |
| <br>   |  |                                  |
| DEFERRED INCOME TAXES AND OTHER LONG-TERM<br>LIABILITIES   | 2,089  | 2,896                            |
| <br>   |  |                                  |
| LONG-TERM DEBT   | 17,649   | 17,997                           |
| <br>   |  |                                  |
| COMMITMENTS AND CONTINGENCIES  |  |                                  |
| IPG PHOTONICS CORPORATION STOCKHOLDERS EQUITY:   |  |                                  |
| Common stock, \$0.0001 par value, 175,000,000 shares authorized;<br>45,352,033 shares issued and outstanding at March 31, 2009; 44,965,960<br>shares issued and outstanding at December 31, 2008 | 5  | 4                                |

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|  |            |            |
|--|------------|------------|
| Additional paid-in capital                           | 288,209    | 283,217    |
| Accumulated deficit                                  | (52,572)   | (53,843)   |
| Accumulated other comprehensive income               | 1,886      | 8,794      |
| Total IPG Photonics Corporation stockholders' equity | 237,528    | 238,172    |
| NONCONTROLLING INTERESTS                             | 209        | 5,127      |
| Total equity   | 237,737    | 243,299    |
| TOTAL  | \$ 313,805 | \$ 313,218 |

See notes to consolidated financial statements.

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**IPG PHOTONICS CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

|   | <b>Three Months Ended<br/>March 31,</b>          |             |
|---|--|-------------|
|   | <b>2009</b>                                      | <b>2008</b> |
|   | <b>(In thousands, except per share<br/>data)</b> |             |
| NET SALES   | \$ 45,408  | \$ 52,876   |
| COST OF SALES   | 29,547   | 28,476      |
| GROSS PROFIT  | 15,861   | 24,400      |
| OPERATING EXPENSES:   |  |             |
| Sales and marketing   | 3,189  | 3,147       |
| Research and development  | 4,142  | 2,874       |
| General and administrative  | 4,990  | 6,412       |
| Loss (gain) on foreign exchange                                     | 1,515  | (573)       |
| Total operating expenses  | 13,836   | 11,860      |
| OPERATING INCOME  | 2,025  | 12,540      |
| OTHER (EXPENSE) INCOME, NET:  |  |             |
| Interest expense  | (390)  | (95)        |
| Other (expense) income, net   | (148)  | 47          |
| Total other expense   | (538)  | (48)        |
| INCOME BEFORE PROVISION FOR INCOME TAXES                            | 1,487  | 12,492      |
| PROVISION FOR INCOME TAXES  | (461)  | (3,997)     |
| NET INCOME  | 1,026  | 8,495       |
| LESS: NET (LOSS) INCOME ATTRIBUTABLE TO<br>NONCONTROLLING INTERESTS | (245)  | 346         |
| NET INCOME ATTRIBUTABLE TO IPG PHOTONICS CORPORATION                | \$ 1,271   | \$ 8,149    |
| NET INCOME ATTRIBUTABLE TO IPG PHOTONICS CORPORATION<br>PER SHARE:  |  |             |
| Basic   | \$ 0.03  | \$ 0.18     |
| Diluted   | \$ 0.03  | \$ 0.18     |
| WEIGHTED-AVERAGE SHARES OUTSTANDING:                                |  |             |
| Basic   | 45,094   | 44,095      |
| Diluted   | 46,152   | 46,041      |

See notes to consolidated financial statements.

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**IPG PHOTONICS CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

|   | <b>Three Months Ended</b> |                  |
|---|---------------------------|------------------|
|   | <b>March 31,</b>          |                  |
|   | <b>2009</b>               | <b>2008</b>      |
|   | <b>(In thousands)</b>     |                  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                           |                  |
| Net income  | \$ 1,026                  | \$ 8,495         |
| Adjustments to reconcile net income to net cash provided by operating activities: |                           |                  |
| Depreciation and amortization   | 4,380                     | 3,609            |
| Deferred income taxes   | (4,174)                   | (2,032)          |
| Stock-based compensation  | 635                       | 387              |
| Unrealized losses (gains) on foreign currency transactions                        | 1,513                     | (353)            |
| Other   | (31)                      | 130              |
| Provisions for inventory, warranty and bad debt                                   | 3,728                     | 1,710            |
| Changes in assets and liabilities that provided (used) cash:                      |                           |                  |
| Accounts receivable   | 10,281                    | (2,188)          |
| Inventories   | 859                       | (7,298)          |
| Prepaid expenses and other current assets   | (1,626)                   | 618              |
| Accounts payable  | (1,156)                   | 798              |
| Accrued expenses and other liabilities  | (697)                     | (649)            |
| Income and other taxes payable  | 2,772                     | 2,132            |
| Net cash provided by operating activities   | 17,510                    | 5,359            |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                           |                  |
| Purchases of property, plant, equipment and intangible assets                     | (4,686)                   | (12,962)         |
| Proceeds from sale of marketable securities                                       |                           | 4,450            |
| Other   | 22                        | 59               |
| Net cash used in investing activities   | (4,664)                   | (8,453)          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                      |                           |                  |
| Proceeds from line-of-credit facilities   | 13,528                    | 5,926            |
| Payments on line-of-credit facilities   | (3,298)                   | (2,585)          |
| Purchases of noncontrolling interests   | (455)                     |                  |
| Principal payments on long-term borrowings  | (344)                     |                  |
| Exercise of employee stock options and related tax benefit from exercise          | 137                       | 310              |
| Net cash provided by financing activities   | 9,568                     | 3,651            |
| <b>EFFECT OF CHANGES IN EXCHANGE RATES ON CASH AND CASH EQUIVALENTS</b>           |                           |                  |
|   | (2,096)                   | 169              |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>                                  | <b>20,318</b>             | <b>726</b>       |
| <b>CASH AND CASH EQUIVALENTS</b> Beginning of period                              | <b>51,283</b>             | <b>37,972</b>    |
| <b>CASH AND CASH EQUIVALENTS</b> End of period                                    | <b>\$ 71,601</b>          | <b>\$ 38,698</b> |



SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

|   |          |          |
|---|----------|----------|
| Cash paid for interest  | \$ 403   | \$ 108   |
| Income taxes paid   | \$ 2,795 | \$ 2,915 |
| Non-cash transactions:  |          |          |
| Additions to property, plant and equipment included in accounts payable | \$ 365   | \$ 1,556 |
| Purchases of noncontrolling interests in exchange for Common Stock      | \$ 2,191 | \$       |
| See notes to consolidated financial statements.                         |          |          |

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**IPG PHOTONICS CORPORATION**  
**CONSOLIDATED STATEMENTS OF EQUITY**

|   | <b>Three Months Ended March 31,</b>                    |                |             |                |
|---|--|----------------|-------------|----------------|
|   | <b>2009</b>  |                | <b>2008</b> |                |
|   | <b>(In thousands, except share and per share data)</b> |                |             |                |
|   | Shares   | Amount         | Shares      | Amount         |
| <b>COMMON STOCK</b>   |  |                |             |                |
| Balance, beginning of year                                  | 44,965,960   | \$ 4           | 44,012,341  | \$ 4           |
| Common stock issued in purchase of noncontrolling interests | 293,146  | 1              |             |                |
| Exercise of stock options                                   | 92,927   |                | 193,994     |                |
| Balance, end of period                                      | 45,352,033   | 5              | 44,206,335  | 4              |
| <b>ADDITIONAL PAID-IN CAPITAL</b>                           |  |                |             |                |
| Balance, beginning of year                                  |  | 283,217        |             | 275,506        |
| Common stock issued in purchase of noncontrolling interests |  | 2,190          |             |                |
| Discount on purchase of noncontrolling interests            |  | 2,028          |             |                |
| Exercise of stock options                                   |  | 139            |             | 310            |
| Stock-based compensation                                    |  | 635            |             | 387            |
| Balance, end of period                                      |  | 288,209        |             | 276,203        |
| <b>ACCUMULATED DEFICIT</b>                                  |  |                |             |                |
| Balance, beginning of year                                  |  | (53,843)       |             | (90,497)       |
| Net income attributable to IPG Photonics Corporation        |  | 1,271          |             | 8,149          |
| Balance, end of period                                      |  | (52,572)       |             | (82,348)       |
| <b>ACCUMULATED OTHER COMPREHENSIVE INCOME</b>               |  |                |             |                |
| Balance, beginning of year                                  |  | 8,794          |             | 15,167         |
| Translation adjustments                                     |  | (5,893)        |             | 6,375          |
| Unrealized loss on derivatives, net of tax                  |  | (1,015)        |             |                |
| Balance, end of period                                      |  | 1,886          |             | 21,542         |
| <b>TOTAL IPG PHONTONICS CORPORATION STOCKHOLDERS EQUITY</b> |  | <b>237,528</b> |             | <b>215,401</b> |

| NONCONTROLLING INTERESTS                                   |            |            |
|--|------------|------------|
| Balance, beginning of year                                 | 5,127      | 4,455      |
| Net (loss) income attributable to noncontrolling interests | (245)      | 346        |
| Purchase of noncontrolling interests                       | (2,645)    |            |
| Discount on purchase of noncontrolling interests           | (2,028)    |            |
| Balance, end of period                                     | 209        | 4,801      |
| <br>   |            |            |
| TOTAL EQUITY   | \$ 237,737 | \$ 220,202 |

See notes to consolidated financial statements.

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**IPG PHOTONICS CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. BASIS OF PRESENTATION**

The accompanying unaudited interim consolidated financial statements have been prepared by IPG Photonics Corporation, or IPG, we, our, or the Company. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission. The consolidated financial statements include our accounts and those of our subsidiaries. All intercompany balances have been eliminated in consolidation. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in our annual report on Form 10-K for the year ended December 31, 2008.

Effective January 1, 2009, we adopted Statement of Financial Accounting Standards (SFAS) No. 160, *Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51* (SFAS No. 160). SFAS No. 160 was retrospectively applied, and

clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements,

requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest,

establishes standards for accounting for changes in a parent's ownership interest in a subsidiary, and

requires expanded disclosures that clearly identify and distinguish between interests of the parent's owners and the interests of the noncontrolling owners of a subsidiary.

The calculation of earnings per share continues to be based on income amounts attributable to the parent. SFAS No. 160 was effective for the Company beginning January 1, 2009. The changes in presentation prescribed by SFAS No. 160 are incorporated in the accompanying Consolidated Balance Sheets, Consolidated Statements of Operations, Consolidated Statements of Cash Flows and Consolidated Statements of Equity.

In the opinion of our management, the unaudited financial information for the interim periods presented reflects all adjustments necessary for a fair presentation of our financial position, results of operations and cash flows. The results reported in these consolidated financial statements are not necessarily indicative of results that may be expected for the entire year.

**2. RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS No. 141 (revised 2007)). SFAS No. 141 (revised 2007) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. This standard also requires the fair value measurement of certain other assets and liabilities related to the acquisition such as contingencies and research and development. SFAS No. 141 (revised 2007) was required to be applied prospectively beginning January 1, 2009 and has not had a material effect on our financial statements.

In March 2008, the FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities* (SFAS 161). SFAS 161 applies to all derivative instruments and non-derivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 37 and 42 of SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*, (SFAS 133), and related hedged items accounted for under SFAS 133. SFAS 161 requires additional disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related

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hedged items are accounted for under SFAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, results of operations, and cash flows. SFAS 161 was effective for the Company beginning January 1, 2009. The disclosures prescribed by SFAS 161 are included in Note 7 of these Notes to Consolidated Financial Statements.

**3. INVENTORIES**

Inventories consist of the following (in thousands):

|                              | <b>March 31,<br/>2009</b> | <b>December<br/>31,<br/>2008</b> |
|------------------------------|---------------------------|----------------------------------|
| Components and raw materials | \$ 25,073                 | \$ 27,482                        |
| Work-in-process              | 26,719                    | 28,653                           |
| Finished goods               | 14,653                    | 16,420                           |
| <br>                         |                           |                                  |
| Total                        | \$ 66,445                 | \$ 72,555                        |

The Company recorded inventory provisions totaling \$2,743,000 and \$733,000 for the three months ended March 31, 2009 and 2008, respectively. These provisions were recorded as a result of changes in market prices of certain components, the realizable value of those inventories through finished product sales and uncertainties related to the recoverability of the value of inventories due to technological changes and excess quantities. These provisions are reported as a reduction to components and raw materials and finished goods.

**4. FINANCING ARRANGEMENTS**

The Company's borrowings under existing financing arrangements consist of the following (in thousands):

|                                      | <b>March 31,<br/>2009</b> | <b>December<br/>31,<br/>2008</b> |
|--------------------------------------|---------------------------|----------------------------------|
| Revolving Line-of-Credit Facilities: |                           |                                  |
| Euro Credit and Overdraft Facilities | \$ 1,213                  | \$ 670                           |
| U.S. Line of Credit                  | 28,547                    | 19,099                           |
| <br>                                 |                           |                                  |
| Total                                | \$ 29,760                 | \$ 19,769                        |
| <br>                                 |                           |                                  |
| Term Debt:                           |                           |                                  |
| U.S. Long-Term Note                  | 18,982                    | 19,330                           |
| Less current portion                 | (1,333)                   | (1,333)                          |
| <br>                                 |                           |                                  |
| Total long-term debt                 | \$ 17,649                 | \$ 17,997                        |

**5. NET INCOME ATTRIBUTABLE TO IPG PHOTONICS CORPORATION PER SHARE**

The following table sets forth the computation of diluted net income attributable to IPG Photonics Corporation per share (in thousands, except per share data):

| <b>Three Months<br/>Ended March 31,<br/>2009</b> |  | <b>2008</b> |
|--|--|-------------|
|--|--|-------------|

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|  |          |          |
|--|----------|----------|
| Net income attributable to IPG Photonics Corporation                   | \$ 1,271 | \$ 8,149 |
| Weighted average shares  | 45,094   | 44,095   |
| Dilutive effect of common stock equivalents                            | 1,058    | 1,946    |
| Diluted weighted average common shares                                 | 46,152   | 46,041   |
| Basic net income attributable to IPG Photonics Corporation per share   | \$ 0.03  | \$ 0.18  |
| Diluted net income attributable to IPG Photonics Corporation per share | \$ 0.03  | \$ 0.18  |

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The computation of diluted weighted average common shares excludes 1,399,000 and 66,000 shares for the three months ended March 31, 2009 and 2008, respectively, because the effect on net income attributable to IPG Photonics Corporation per share would have been anti-dilutive.

**6. COMPREHENSIVE INCOME**

Total comprehensive income and its components were as follows (in thousands):

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2009</b>                             | <b>2008</b> |
| Net income attributable to IPG Photonics Corporation | \$ 1,271                                | \$ 8,149    |
| Other comprehensive income:                          |   |             |
| Unrealized loss on derivatives, net of tax           | 31                                      |             |
| Foreign currency translation adjustment              | (6,939)                                 | 6,375       |
| Comprehensive income                                 | \$ (5,637)                              | \$ 14,524   |

**7. DERIVATIVE FINANCIAL INSTRUMENTS**

On January 1, 2009, we adopted SFAS No. 161, which requires enhanced disclosures regarding an entity's derivative and hedging activities as provided below.

Our primary market exposures are to interest rates and foreign exchange rates. We use certain derivative financial instruments to help manage these exposures. We execute these instruments with financial institutions we judge to be credit-worthy and the majority are denominated in currencies of major industrial countries. We do not hold or issue derivative financial instruments for trading or speculative purposes.

We recognize all derivative financial instruments as either assets or liabilities at fair value in the consolidated balance sheet. We have used foreign currency forward contracts as cash flow hedges of forecasted intercompany settlements denominated in foreign currencies. We have no outstanding foreign currency forward contracts. We have an interest rate swap that is classified as a cash flow hedge of our variable rate debt.

*Cash flow hedges* - Our cash flow hedge is an interest rate swap under which we agree to pay fixed rates of interest. We have no derivatives that are not accounted for as a hedging instrument. The fair value amounts in the consolidated balance sheet at March 31, 2009 were (in thousands):

|                    | <b>Asset Derivatives</b>      |                   | <b>Liability Derivatives</b>                          |                   |
|--------------------|-------------------------------|-------------------|---|-------------------|
|                    | <b>Balance Sheet Location</b> | <b>Fair Value</b> | <b>Balance Sheet Location</b>                         | <b>Fair Value</b> |
| Interest rate swap | Other Assets                  | \$                | Deferred income taxes and other long-term liabilities | \$ 1,628          |
| Total              |                               | \$                |   | \$ 1,628          |

The derivative gains and losses in the consolidated statement of operations for the three months ended March 31, 2009, related to our interest rate swap contract was as follows (in thousands):

| <b>Derivatives in Cash Flow</b> | <b>Pretax Loss<br/>Recognized in<br/>Other<br/>Comprehensive</b> | <b>Pretax Loss on<br/>Effective<br/>Portion of<br/>Derivative</b>    | <b>Ineffective Portion of<br/>Gain on<br/>Derivative and<br/>Amount Excluded<br/>from Effectiveness<br/>Testing</b> |  |
|---------------------------------|--|--|---|--|
| <b>Hedging Relationships</b>    | <b>Income on<br/>Effective Portion<br/>of</b>                    | <b>Reclassified from<br/>Accumulated<br/>Other<br/>Comprehensive</b> | <b>Loss</b>   |  |
|                                 | <b>Derivative<br/>Amount</b>                                     | <b>Location</b>  | <b>Amount</b>   | <b>Recognized in Income<br/>Location</b> |
|                                 |  |  | <b>Amount</b>   | <b>Amount</b>                            |
| Interest Rate Swap              | \$ 49  |  | \$  | \$                                       |
|                                 | 9  |  |   |  |

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The notional amount of the outstanding interest rate swap was \$18,982,000. We made no adjustments to the fair value of this derivative as a result of evaluating counterparty risk.

**8. FAIR VALUE MEASUREMENTS**

Effective January 1, 2009, we adopted SFAS No. 157, *Fair Value Measurements* ( SFAS No. 157 ) for our nonfinancial assets and nonfinancial liabilities measured on a non-recurring basis. We adopted SFAS No. 157 for financial assets and liabilities in 2008. The adoption of SFAS No. 157 did not have a material impact on our fair value measurements.

The following tables present our assets and liabilities that are measured at fair value on a recurring basis as of March 31, 2009 and December 31, 2008, and are categorized using the fair value hierarchy. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value. Level 1 refers to fair values determined based on quoted prices in active markets for identical assets. Level 2 refers to fair values estimated using significant other observable inputs, and Level 3 includes fair values estimated using significant non-observable inputs.

|                          | <b>Fair Value Measurements at<br/>March 31, 2009</b> |                  |                   |                 |
|--------------------------|--|------------------|-------------------|-----------------|
|                          | <b>Total</b>   | <b>Level 1</b>   | <b>Level 2</b>    | <b>Level 3</b>  |
| <b>Assets</b>            |  |                  |                   |                 |
| Money market funds       | \$ 9,027   | \$ 9,027         | \$                | \$              |
| Treasury Bills           | 30,664   | 30,664           |                   |                 |
| Auction Rate Securities  | 1,309  |                  |                   | 1,309           |
| <b>Total assets</b>      | <b>\$ 41,000</b>                                     | <b>\$ 39,691</b> | <b>\$</b>         | <b>\$ 1,309</b> |
| <b>Liabilities</b>       |  |                  |                   |                 |
| Interest Rate Swap       | \$ (1,638)   | \$               | \$ (1,638)        | \$              |
| <b>Total liabilities</b> | <b>\$ (1,638)</b>                                    | <b>\$</b>        | <b>\$ (1,638)</b> | <b>\$</b>       |

|                          | <b>Fair Value Measurements at<br/>December 31, 2008</b> |                  |                   |                 |
|--------------------------|---|------------------|-------------------|-----------------|
|                          | <b>Total</b>  | <b>Level 1</b>   | <b>Level 2</b>    | <b>Level 3</b>  |
| <b>Assets</b>            |   |                  |                   |                 |
| Money market funds       | \$ 22,560   | \$ 22,560        | \$                | \$              |
| Treasury Bills           | 9,090   | 9,090            |                   |                 |
| Auction Rate Securities  | 1,309   |                  |                   | 1,309           |
| <b>Total assets</b>      | <b>\$ 32,959</b>  | <b>\$ 31,650</b> | <b>\$</b>         | <b>\$ 1,309</b> |
| <b>Liabilities</b>       |   |                  |                   |                 |
| Interest Rate Swap       | \$ (1,667)  | \$               | \$ (1,667)        | \$              |
| <b>Total liabilities</b> | <b>\$ (1,667)</b>                                       | <b>\$</b>        | <b>\$ (1,667)</b> | <b>\$</b>       |



**Table of Contents****9. INTANGIBLE ASSETS**

|                                | <b>March<br/>31,<br/>2009</b> | <b>December<br/>31,<br/>2008</b> |
|--------------------------------|-------------------------------|----------------------------------|
| (In thousands)                 |                               |                                  |
| Amortizable intangible assets  |                               |                                  |
| Patents                        | \$ 3,650                      | \$ 3,650                         |
| Customer relationships         | 1,574                         | 1,655                            |
| Other identifiable intangibles | 437                           | 544                              |
|                                | 5,661                         | 5,849                            |
| Accumulated amortization       | (959)                         | (737)                            |
|                                | \$ 4,702                      | \$ 5,112                         |

The estimated future amortization expense for intangibles as of March 31, 2009 is as follows (in thousands):

| <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012</b> | <b>2013</b> | <b>Thereafter</b> |
|-------------|-------------|-------------|-------------|-------------|-------------------|
| \$1,047     | \$1,183     | \$1,183     | \$924       | \$292       | \$ 73             |

**10. PRODUCT WARRANTIES**

The company typically provides one to three-year parts and service warranties on lasers and amplifiers. Most of the sales offices provide support to customers in their respective geographic areas. Warranty reserves have generally been sufficient to cover product warranty repair and replacement costs. The following table summarizes product warranty activity recorded during the three months ended March 31, 2009 and 2008 (in thousands).

|   | <b>2009</b> | <b>2008</b> |
|---|-------------|-------------|
| Beginning balance January 1             | \$ 3,224    | \$ 1,986    |
| Additions for current year deliveries   | 603         | 831         |
| Reductions for payments made            | (389)       | (436)       |
| Impact of foreign currency rate changes | (94)        | 65          |
| Ending balance March 31                 | \$ 3,344    | \$ 2,446    |

**11. COMMITMENTS AND CONTINGENCIES**

In November 2006, the Company was sued for patent infringement relating to certain products, including but not limited to fiber lasers and fiber amplifiers. The plaintiff has made a complaint for damages of over \$10 million, treble damages for alleged willful infringement and injunctive relief. The case has been stayed until the termination of a pending patent re-examination.

In February 2008, the Company was sued for patent infringement relating to two product lines used in medical laser applications. The plaintiff has filed a complaint for unspecified damages, treble damages for alleged willful infringement and injunctive relief. The patent asserted in the lawsuit expired in April 2007. The case has been stayed until October 2009 in connection with a patent reexamination.

The Company believes it has meritorious defenses and intends to vigorously contest the claims. No loss is deemed probable at March 31, 2009 and no amounts have been accrued in respect of these contingencies.

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*You should read the following discussion in conjunction with our consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q. This discussion contains forward looking statements that are based on management's current expectations, estimates and projections about our business and operations. Our actual results may differ materially from those currently anticipated and expressed in such forward-looking statements. See Cautionary Statement Regarding Forward-Looking Statements.*

**Overview**

We develop and manufacture a broad line of high-performance fiber lasers, fiber amplifiers and diode lasers for diverse applications in numerous markets. Our diverse lines of low, mid and high-power lasers and amplifiers are used in materials processing, advanced, communications and medical applications. We sell our products globally to original equipment manufacturers, or OEMs, system integrators and end users. We market our products internationally primarily through our direct sales force and also through agreements with independent sales representatives and distributors.

We are vertically integrated such that we design and manufacture all key components used in our finished products, from semiconductor diodes to optical fiber preforms, finished fiber lasers and amplifiers. Since our formation in 1990, we have been focused on developing and manufacturing high-power fiber lasers and amplifiers.

**Factors and Trends That Affect Our Operations and Financial Results**

In reading our financial statements, you should be aware of the following factors and trends that our management believes are important in understanding our financial performance.

*Net sales.* Our net sales have historically fluctuated from quarter to quarter. The increase or decrease in sales from a prior quarter can be affected by the timing of orders received from customers, the shipment, installation and acceptance of products at our customers' facilities, the mix of OEM orders and one-time orders for products with large purchase prices, and seasonal factors such as the purchasing patterns and levels of activity throughout the year in the regions where we operate. Historically, our net sales have been higher in the second half of the year than in the first half of the year. Furthermore, net sales can be affected by the time taken to qualify our products for use in new applications in the end markets that we serve. The adoption of our products by a new customer or qualification in a new application can lead to an increase in net sales for a period, which may then slow until we further penetrate new markets or obtain new customers. Our net sales can also be affected from quarter to quarter by the general level of worldwide economic activity, including economic expansion or contraction, and expenditures on capital equipment. In general, increases in worldwide economic activity have a positive effect on our sales and decreases in economic activity have a negative effect on our sales.

*Gross margin.* Our total gross margin in any period can be affected by total net sales in any period, product mix, that is, the percentage of our revenue in that period that is attributable to higher or lower-power products, production volumes, and by other factors, some of which are not under our control. Our product mix affects our margins because the selling price per watt is higher for low and mid-power devices than for high-power devices. The overall cost of high-power lasers may be partially offset by improved absorption of fixed overhead costs associated with sales of larger volumes of higher-power products.

Due to the fact that we have high fixed costs, our costs are difficult to adjust in response to changes in demand. In addition, our fixed costs will increase as we expand our capacity. Gross margins generally improve when greater absorption of fixed overhead costs is associated with an increase in sales. In addition, absorption of fixed costs can benefit gross margins due to an increase in production that is not sold and placed into inventory. Gross margins generally decline if production volumes are lower as a result of a decrease in sales or inventory because the absorption of fixed manufacturing costs will be reduced. If both sales and inventory decrease in the same period the decline in gross margin may be magnified if we cannot reduce fixed costs or chose not to reduce fixed costs to match the decrease in the level of production. We also regularly review our inventory for items that are slow-moving, have been rendered obsolete or determined to be excess. If we experience a decline in sales that reduces absorption of our fixed costs, or if we have production issues or inventory write-downs, our gross margins will be negatively affected.

*Sales and marketing expense.* We expect to continue to expand our worldwide direct sales organization, build and expand applications centers, hire additional personnel involved in marketing in our existing and new geographic locations, increase the number of units used for demonstration purposes and otherwise increase expenditures on sales and marketing activities in order to support the growth in our net sales. As such, we expect that our sales and marketing expenses will increase in the aggregate.

*Research and development expense.* We plan to continue to invest in research and development to improve our existing components and products and develop new components and products. We plan to increase the personnel involved in research and development and

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expect to increase other research and development expenses. As such, we expect that our research and development expenses will increase in the aggregate.

*General and administrative expense.* We expect our general and administrative expenses to increase moderately as we continue to invest in systems and resources to support our worldwide operations. Legal expenses vary from quarter to quarter based upon the stage of litigation, including patent re-examinations and termination of litigation stays but could increase in response to any future litigation or due to a change in status of current intellectual property matters. The timing and amount of legal expenses may vary substantially from quarter to quarter.

*Major customers.* We have historically depended on a few customers for a large percentage of our annual net sales. The composition of this group can change from year to year. Net sales derived from our five largest customers as a percentage of our annual net sales were 29% in 2006, 20% in 2007, 17% in 2008, and 15% for the three months ended March 31, 2009. We seek to add new customers and to expand our relationships with existing customers. We anticipate that the composition of our net sales to our significant customers will continue to change. If any of our significant customers were to substantially reduce their purchases from us, our results would be adversely affected.

**Results of Operations for the three months ended March 31, 2009 compared to the three months ended March 31, 2008**

*Overview.* The worldwide economic downturn negatively affected our results of operations for the three months ended March 31, 2009. With uncertain end market demand, we will continue to focus on controlling costs and reducing inventories in order to maximize cash flow. At the same time, we plan to continue to build on our technology by investing in new sales and application personnel and R&D for new products. We anticipate that economic conditions will continue to have a negative effect on our financial results in the second quarter of 2009 as we experience continued weakness across many of our end markets, especially in materials processing.

*Net sales.* Net sales decreased by \$7.5 million, or 14.1%, to \$45.4 million for the three months ended March 31, 2009 from \$52.9 million for the three months ended March 31, 2008. This decrease was attributable to lower sales of fiber lasers in materials processing applications, where net sales decreased by \$9.4 million or 21.3% and communications applications, where net sales decreased by \$0.3 million or 9.0%, offset by increases in sales of advanced applications, where net sales increased by \$1.8 million, or 34.7%, and medical applications, where net sales increased by \$0.4 million, or 78.4%. The decrease in materials processing applications resulted from decreased sales of pulsed lasers and low-power lasers used in marking, engraving and printing applications. The decrease in pulsed laser sales was partially off-set by an increase in sales of high power laser for materials processing. The decrease in communications applications sales resulted primarily from decreased sales of amplifiers and high power amplifiers. The increase in sales of advanced applications was due to higher sales of high power lasers used in government and defense research. We estimate that if exchange rates had been approximately the same as one year ago our first quarter 2009 sales would have been \$2.1 million higher.

*Cost of sales and gross margin.* Cost of sales increased by \$1.0 million, or 3.8%, to \$29.5 million for the three months ended March 31, 2009 from \$28.5 million for the three months ended March 31, 2008. Our gross margin decreased to 34.9% for the three months ended March 31, 2009 from 46.1% for the three months ended March 31, 2008. The decrease in gross margin was the result of less favorable absorption of our fixed manufacturing costs due to a decline in sales volume and reduction of inventory as well as an increase in charges related to inventory write-downs. These increases were offset by a reduction in manufacturing expenses in the period primarily related to reduced salaries and benefits expense and other manufacturing supplies. Expenses related to inventory reserves and other valuation adjustments increased by \$2.0 million to \$2.7 million or 6.0% of sales for the three months ended March 31, 2009 as compared to 1.5% of sales for the three months ended March 31, 2008. We estimate that if exchange rates had been approximately the same as one year ago our first quarter 2009 gross profit would have been \$0.5 million higher.

*Sales and marketing expense.* Sales and marketing expense increased by \$0.1 million, or 1.3%, to \$3.2 million for the three months ended March 31, 2009 from \$3.1 million for the three months ended March 31, 2008, primarily as a result of an increase of \$0.2 million in contractor, advertising and travel expenses offset by a \$0.1 million decrease in selling expenses related to decreased depreciation of units used for demonstration purposes. As a percentage of sales, sales and marketing expense increased to 7.0% for the three months ended March 31, 2009 from 6.0% for the three

months ended March 31, 2008. As we continue to expand our worldwide sales organization, we expect expenditures on sales and marketing to continue to increase in the aggregate although the near term increases will be more moderate. We estimate that if exchange rates had been approximately the same as one year ago our first quarter 2009 sales and marketing expense would have been \$0.2 million higher.

*Research and development expense.* Research and development expense increased by \$1.2 million, or 44.2%, to \$4.1 million for the three months ended March 31, 2009 from \$2.9 million for the three months ended March 31, 2008. This increase was primarily due to an increase of \$0.6 million in material costs and \$0.3 million in personnel costs. Research and development activity continues to focus on

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enhancing the performance of our internally manufactured components, refining production processes to improve manufacturing yields and the development of new products operating at different wavelengths and at higher output powers and new complimentary accessories used with our products. As a percentage of sales, research and development expense increased to 9.1% for the three months ended March 31, 2009 from 5.4% for the three months ended March 31, 2008. We estimate that if exchange rates had been approximately the same as one year ago our first quarter 2009 research and development expenses would have been \$0.4 million higher.

*General and administrative expense.* General and administrative expense decreased by \$1.4 million, or 22.2%, to \$5.0 million for the three months ended March 31, 2009 from \$6.4 million for the three months ended March 31, 2008, primarily due to a decrease of \$1.2 million in patent litigation defense fees and a \$0.6 million decrease in personnel and contractor expenses partially offset by \$0.4 million increase in reserves for bad debts. Expenses for patent litigation defense were higher for the three months ended March 31, 2008 due to activity in one patent litigation and a new patent litigation brought against the Company. As a percentage of sales, general and administrative expense decreased to 11.0% for the three months ended March 31, 2009 from 12.1%. We estimate that if exchange rates had been approximately the same as one year ago our first quarter 2009 general and administrative expenses would have been \$0.4 million higher.

*Loss (gain) on foreign exchange.* Loss (gain) on foreign exchange increased by \$2.1 million to a loss of \$1.5 million for the three months ended March 31, 2009 from a gain of \$0.6 million for the three months ended March 31, 2008 and was primarily attributable to the depreciation of the Russian Ruble and Euro against the U.S. Dollar.

*Interest expense.* Interest expense, net was \$0.4 million for the three months ended March 31, 2009 compared to \$0.1 million for the three months ended March 31, 2008. The change in interest expense resulted from higher interest expense due to increased utilization of credit lines.

*Provision for income taxes.* Provision for income taxes decreased by \$3.5 million to \$0.5 million for the three months ended March 31, 2009 from \$4.0 million for the three months ended March 31, 2008, representing an effective tax rate of 31.0% for the three months ended March 31, 2009 as compared to an effective tax rate of 32.0% for the three months ended March 31, 2008. The decrease in the effective tax rate is primarily due to changes in distribution of income among tax jurisdictions subject to differing tax rates.

*Net income attributable to IPG Photonics Corporation.* Net income attributable to IPG Photonics Corporation decreased by \$6.9 million to \$1.3 million for the three months ended March 31, 2009 from \$8.1 million for the three months ended March 31, 2008. Net income attributable to IPG Photonics Corporation as a percentage of our net sales decreased by 12.6 percentage points to 2.8% for the three months ended March 31, 2009 from 15.4% for the three months ended March 31, 2008 due to the factors described above.

**Liquidity and Capital Resources**

Our principal sources of liquidity as of March 31, 2009 consisted of cash and cash equivalents of \$71.6 million, unused credit lines and overdraft facilities of \$29.2 million and working capital (excluding cash) of \$55.7 million. This compares to cash and cash equivalents of \$51.3 million, unused overdraft facilities of \$40.9 million and working capital (excluding cash) of \$80.7 million as of December 31, 2008. The increase in cash and cash equivalents of \$20.3 million from December 31, 2008 relates primarily to cash provided by operating activities during the first quarter of 2009 of \$17.5 million and net proceeds from our credit lines of \$10.3 million, partially offset by capital expenditures and the acquisition of noncontrolling interests totaling \$5.1 million and the negative effect of foreign exchange on cash and cash equivalents of \$2.1 million.

We held approximately \$1.3 million in auction-rate securities (ARSs) at March 31, 2009 all of which is included in other long-term assets. Our investments in ARSs at March 31, 2009 consisted solely of taxable municipal debt securities. None of the ARSs in our portfolio are collateralized debt obligations (CDOs) or mortgage-backed securities.

As a result of continued auction failures, we continue to hold the ARSs not subject to redemption and the issuers are required to pay interest on the ARSs at the maximum contractual rate. As these auction failures have affected our ability to access these funds in the near term, we have classified these as long-term available for sale securities. Additionally, we have assessed the fair value of these instruments and have identified an other-than-temporary decline



in their market value related to the lack of liquidity. As a result, we carry these ARSs at approximately 86% of their face value and recorded a charge totaling \$191,000 during 2008. These ARSs are insured and are rated A2 and AA by Moody's and Standard & Poor's, respectively. If the credit rating of the issuer of the ARSs were to deteriorate, we may be required to further adjust the carrying value of these investments by recording additional impairment charges. Based on our ability to access our cash, our expected operating cash flows and our available credit lines, we do not expect that the

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current lack of liquidity in our investments in ARSs will have a material impact on our overall liquidity, financial condition or results of operations.

Our long-term debt consists of a \$19.0 million secured variable-rate note described in Note 4 to our consolidated financial statements which matures in August 2013. The note is secured by a mortgage on real estate and buildings in Massachusetts. We expect that the existing cash and marketable securities, our cash flows from operations and our existing lines of credit will be sufficient to meet our liquidity and capital needs for the foreseeable future. Our future long-term capital requirements will depend on many factors including our rate of net sales growth, the timing and extent of spending to support development efforts, the expansion of our sales and marketing activities, the timing and introductions of new products, the need to ensure access to adequate manufacturing capacity and the continuing market acceptance of our products. We have made no arrangements to obtain additional financing, and there is no assurance that such additional financing, if required or desired, will be available in amounts or on terms acceptable to us, if at all.

The following table details our line-of-credit facilities as of March 31, 2009:

| <b>Description</b>                 | <b>Available Principal</b>         | <b>Interest Rate</b>  | <b>Maturity</b>                  | <b>Security</b>  |
|------------------------------------|------------------------------------|---|----------------------------------|--|
| U.S. Revolving Line of Credit      | Up to \$35 million                 | LIBOR plus 0.8% to 1.2%, depending on the Company's performance | July 2011                        | Unsecured  |
| Euro Credit Facility (Germany) (1) | Euro 15.0 million (\$19.8 million) | Euribor + 1.0% or EONIA + 1.5%                                  | June 2010                        | Unsecured, guaranteed by parent company                  |
| Euro Overdraft Facilities          | Euro 3.2 million (\$4.2 million)   | 3.90%-6.95%   | Between July 2009 and March 2010 | Common pool of assets of German and Italian subsidiaries |

(1) \$4.0 million of this credit facility is available to our Russian subsidiary and \$1.3 million is available to our Italian subsidiary

The Company is required to meet certain financial covenants associated with its U.S. revolving line of credit and long term debt facilities. These covenants, tested quarterly, include a debt service coverage ratio and a funded debt to earnings before interest, taxes, depreciation and amortization ( EBITDA ) ratio. The debt service coverage covenant requires that we maintain a trailing twelve month ratio of cash flow to debt service that is greater than 1.5:1. Debt service is defined as required principal and interest payments during the period. Cash flow is defined as EBITDA less unfunded capital expenditures. For trailing twelve month periods until June 2010, up to \$15.0 million of our capital expenditures are treated as being funded from the proceeds of our initial public offering. The funded debt to EBITDA covenant requires that the sum of all indebtedness for borrowed money on a consolidated basis shall be less than two

times our trailing twelve months EBITDA. We were in compliance with all such financial covenants as of March 31, 2009.

The financial covenants in our loan documents may cause us to not take or to delay investments and actions that we might otherwise undertake because of limits on capital expenditures and amounts that we can borrow or lease. In the event that we do not comply with any one of these covenants, we would be in default under the loan agreement or loan agreements, which may result in acceleration of the debt, cross-defaults on other debt or a reduction in available liquidity, any of which could harm our results of operations and financial condition.

*Operating activities.* Net cash provided by operating activities in the three months ended March 31, 2009 increased by \$12.1 million to \$17.5 million from \$5.4 million in the three months ended March 31, 2008. The increase in cash provided by operating activities in the first quarter of 2009 compared to the first quarter of 2008 primarily resulted from:

A decrease in accounts receivable of \$10.3 million compared to an increase of \$2.2 million;

A decrease in inventory of \$0.9 million compared to an increase of inventory of \$7.3 million; partially offset by

A decrease in cash provided by net income after adding back non-cash charges of \$4.9 million.

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Given our vertical integration, rigorous and time-consuming testing procedures for both internally manufactured and externally purchased components and the lead time required to manufacture components used in our finished product, the rate at which we turn inventory has historically been low when compared to our cost of sales. We do not expect this to change significantly in the future and believe that we will have to maintain a relatively high level of inventory compared to our cost of sales. As a result, we continue to expect to have a significant amount of working capital invested in inventory and for changes in our level of inventory to lead to an increase in cash generated from our operations when it is sold or a decrease in cash generated from our operations at times when the amount of inventory is increasing. A reduction in our level of net sales or the rate of growth of our net sales from their current levels would mean that the rate at which we are able to convert our inventory into accounts receivable would decrease.

*Investing activities.* Net cash used in investing activities was \$4.7 million and \$8.5 million in the three months ended March 31, 2009 and 2008, respectively. The cash used in investing activities in the first quarter of 2009 was related to \$4.7 million of capital expenditures on property, plant and equipment. The cash used in investing activities in the first quarter of 2008 was primarily related to capital expenditures on property, plant and equipment of \$13.0 million. In 2009 and 2008, capital expenditures in the United States, Germany, and Russia related to facilities and equipment for diode wafer growth, burn-in test stations and packaging as well as new fiber assembly and component production facilities. We expect capital expenditures, excluding intangible assets, in the range of \$13 million to \$15 million for the year ended December 31, 2009. The timing and extent of any capital expenditures in and between periods can have a significant effect on our cash flow. Many of the capital expenditure projects that we undertake have long lead times and are difficult to cancel or defer, with the result that it would be difficult to defer such committed capital expenditures to a later period.

*Financing activities.* Net cash provided by financing activities was \$9.6 million in the three months ended March 31, 2009 as compared \$3.7 million in the three months ended March 31, 2008. The cash provided by financing activities in 2009 was primarily related to the net proceeds of \$10.2 million from the use of our credit lines, partially offset by cash used to purchase noncontrolling interests of \$0.4 million. The cash provided by financing activities in 2008 was primarily related to the net proceeds of \$3.3 million from the use of our credit lines. The increase in net drawings on credit lines in 2009 was primarily related to a plan to increase cash liquidity in response to economic uncertainties present during the three months ended March 31, 2009.

**Cautionary Statement Regarding Forward-Looking Statements**

This Quarterly Report on Form 10-Q 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, and we intend that such forward-looking statements be subject to the safe harbors created thereby. For this purpose, any statements contained in this Quarterly Report on Form 10-Q except for historical information are forward-looking statements. Without limiting the generality of the foregoing, words such as may, will, expect, believe, anticipate, intend, estimate, or continue or the negative or other variations thereof or comparable terminology are intended to identify forward-looking statements. In addition, any statements that refer to projections of our future financial performance, trends in our businesses, or other characterizations of future events or circumstances are forward-looking statements.

The forward-looking statements included herein are based on current expectations of our management based on available information and involve a number of risks and uncertainties, all of which are difficult or impossible to accurately predict and many of which are beyond our control. As such, our actual results may differ significantly from those expressed in any forward-looking statements. Factors that may cause or contribute to such differences include, but are not limited to, those discussed in more detail in Item 1, *Business* and Item 1A, *Risk Factors* of Part I of our Annual Report on Form 10-K for the period ended December 31, 2008. Readers should carefully review these risks, as well as the additional risks described in other documents we file from time to time with the Securities and Exchange Commission. In light of the significant risks and uncertainties inherent in the forward-looking information included herein, the inclusion of such information should not be regarded as a representation by us or any other person that such results will be achieved, and readers are cautioned not to rely on such forward-looking information. We undertake no obligation to revise the forward-looking statements contained herein to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

**Recent Accounting Pronouncements**

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* ( SFAS No. 141 (revised 2007) ), and SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements-an amendment of ARB No. 51* ( SFAS No. 160 ).

SFAS No. 141 (revised 2007) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. This standard also requires the fair value measurement of certain other assets and liabilities related to the

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acquisition such as contingencies and research and development. SFAS No. 141 (revised 2007) was required to be applied prospectively beginning January 1, 2009 and did not have a material effect on our financial statements.

SFAS No. 160 requires that a noncontrolling interest in a subsidiary be reported as a component of stockholders equity in the consolidated financial statements. Consolidated net income should include the net income for both the parent and the noncontrolling interest with disclosure of both amounts on the consolidated statement of income. The calculation of earnings per share will continue to be based on income amounts attributable to the parent. SFAS No. 160 was effective for the Company beginning January 1, 2009. The changes in presentation prescribed by SFAS No. 160 have been incorporated in the accompanying Consolidated Balance Sheets, Consolidated Statements of Operations, Consolidated Statements of Cash Flows and Consolidated Statements of Equity.

In March 2008, the FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities* ( SFAS 161 ). SFAS 161 applies to all derivative instruments and non-derivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 37 and 42 of SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*, ( SFAS 133 ), and related hedged items accounted for under SFAS 133. SFAS 161 requires additional disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, results of operations, and cash flows. SFAS 161 is effective for the Company beginning January 1, 2009. The disclosures prescribed by SFAS 161 have been included in the accompanying Notes to Consolidated Financial Statements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risk in the ordinary course of business, which consists primarily of interest rate risk associated with our cash and cash equivalents and our debt and foreign exchange rate risk.

*Interest rate risk.* Our investments have limited exposure to market risk. To minimize this risk, we maintain a portfolio of cash, cash equivalents and short-term investments, consisting primarily of bank deposits, money market funds and short-term government funds. The interest rates are variable and fluctuate with current market conditions. Because of the short-term nature of these instruments, a sudden change in market interest rates would not be expected to have a material impact on our financial condition or results of operations.

Our exposure to market risk also relates to the increase or decrease in the amount of interest expense we must pay on our bank debt and borrowings on our bank credit facilities. The interest rate on our existing bank debt is currently fixed except for our U.S. revolving line of credit and our Euro credit facility. The rates on our Euro overdraft facilities in Germany and Italy and our Japanese Yen overdraft facility are fixed for twelve-month periods. Approximately 39% of our outstanding debt had a fixed rate of interest as of March 31, 2009. We do not believe that a 10% change in market interest rates would have a material impact on our financial position or results of operations.

*Exchange rates.* Due to our international operations, a significant portion of our net sales, cost of sales and operating expenses are denominated in currencies other than the U.S. dollar, principally the Euro, the Japanese Yen and the Russian Ruble. As a result, our international operations give rise to transactional market risk associated with exchange rate movements of the U.S. dollar, the Euro, the Japanese Yen and the Russian Ruble. Gains and losses on foreign exchange transactions totaled a \$1.5 million loss, and a \$0.6 million gain for the three months ended March 31, 2009 and 2008, respectively. Management believes that the use of foreign currency financial instruments reduces the risks of certain foreign currency transactions, however, these instruments provide only limited protection. We will continue to analyze our exposure to currency exchange rate fluctuations and may engage in additional financial hedging techniques in the future to attempt to minimize the effect of these potential fluctuations. Exchange rate fluctuations may adversely affect our financial results in the future. No foreign currency derivative instruments were outstanding at March 31, 2009.

**ITEM 4. CONTROLS AND PROCEDURES****Evaluation of Disclosure Controls and Procedures**

Under the supervision of our chief executive officer and our chief financial officer, our management has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this Quarterly Report on Form 10-Q (the Evaluation Date). Based upon that evaluation, our

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executive officer and our chief financial officer have concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective.

**Changes in Internal Controls**

There was no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) promulgated under the Exchange Act) that occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

From time to time, we are party to various legal proceedings and other disputes incidental to our business. There have been no material developments in the first quarter of 2009 with respect to those proceedings previously reported in our Annual Report on Form 10-K for the year ended December 31, 2008.

**ITEM 1A. RISK FACTORS**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2008, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

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

During the three months ended March 31, 2009, we have sold and issued 293,146 unregistered shares of common stock as payment of the purchase price for the 31.6% minority interest in NTO IRE-Polus that we did not previously own. NTO- IRE-Polus is now 99.9% owned by us. The aggregate purchase price was \$6,117,973. The sales of securities described above were deemed to be exempt from registration pursuant to Section 4(2) of the Securities Act and Regulation D promulgated thereunder as transactions by an issuer not involving a public offering. Each of these sales was to accredited investors, as such term is defined in Rule 501 of Regulation D. Each of the recipients of securities in the transactions deemed to be exempt from registration pursuant to Section 4(2) of the Securities Act received written disclosures that the securities had not been registered under the Securities Act and that any resale must be made pursuant to a registration or an available exemption from such registration. None of the sales of the securities described above involved the use of an underwriter, and no commissions were paid in connection with the sale of any of the securities that we issued. The sales of these securities were made without general solicitation or advertising.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

(a) Exhibits



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**Exhibit**

| <b>No.</b> | <b>Description</b>  |
|------------|---|
| 31.1       | Certification of Chief Executive Officer pursuant to Rule 13a-14(a)                           |
| 31.2       | Certification of Chief Financial Officer pursuant to Rule 13a-14(a)                           |
| 32         | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 1350 |

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

**IPG PHOTONICS CORPORATION**

Date: May 11, 2009

By: /s/ Valentin P. Gapontsev  
Valentin P. Gapontsev  
Chairman and Chief Executive Officer  
(Principal Executive Officer)

Date: May 11, 2009

By: /s/ Timothy P.V. Mammen  
Timothy P.V. Mammen  
Vice President and Chief Financial  
Officer  
(Principal Financial Officer)

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