NATIONAL INSTRUMENTS CORP /DE/
Form 10-K
February 07, 2012

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

FORM 10-K

T ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended: December 31, 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	74-1871327
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
11500 North MoPac Expressway Austin, Texas	78759
(address of principal executive offices)	(zip code)

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

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $0.01 par value	The NASDAQ Stock Market, LLC

Securities registered pursuant to Section 12(g) of the Act:
Preferred Stock Purchase Rights

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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 x No o

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 x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 x Accelerated filer o Non-accelerated filer o Smaller reporting company o

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

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant at the close of business on June 30, 2011, was $2,326,245,669 based upon the last sales price reported for such date on the NASDAQ Stock Market. For purposes of this disclosure, shares of Common Stock held by persons who hold more than 5% of the outstanding shares of Common Stock and shares held by officers and directors of the registrant as of June 30, 2011, have been excluded in that such persons may be deemed to be affiliates. This determination is not necessarily conclusive.

At the close of business on February 2, 2012, registrant had outstanding 120,678,169 shares of Common Stock.

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DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates certain information by reference from the definitive proxy statement to be filed by the registrant for its Annual Meeting of Stockholders to be held on May 8, 2012 (the "Proxy Statement").

PART I

This Form 10-K 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 neg 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 11, and elsewhere in this Form 10-K. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on these forward-looking statements. We disclaim any obligation to update information contained in any forward-looking statement.

ITEM 1. BUSINESS

National Instruments Corporation ("NI", "we", "us" or "our") designs, manufactures and sells tools to engineers and scientists that accelerate productivity, innovation and discovery. Our graphical system design approach to engineering provides an integrated software and hardware platform that speeds the development of systems needing measurement and control. We believe our long-term vision and focus on technology supports the success of our customers, employees, suppliers and shareholders.

We are based in Austin, Texas and were incorporated under the laws of the State of Texas in May 1976 and were reincorporated in Delaware in June 1994. On March 13, 1995, we completed an initial public offering of our common stock. Our common stock, $0.01 par value, is quoted on the NASDAQ Stock Market under the trading symbol NATI.

Our Internet website address is http://www.ni.com. Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T are available through our Internet website as soon as reasonably practicable after we electronically file such materials with, or furnish them to, the SEC, or upon written request without charge. Our Internet website and the information contained therein or connected thereto are not intended to be incorporated into this Annual Report on Form 10-K.

Industry Background

Engineers and scientists use instruments to observe, understand and manage the real-world phenomena, events and processes related to their industries or areas of expertise. Instruments measure and control electrical signals, such as voltage, current and power, as well as temperature, pressure, speed, flow, volume, torque and vibration. Common general-purpose instruments include voltmeters, signal generators, oscilloscopes, data loggers, spectrum analyzers, cameras, and temperature and pressure monitors and controllers. Some traditional instruments are also highly application-specific, designed with fixed functionality to measure specific signals for particular vertical industries or applications. Instruments used for industrial automation applications include data loggers, strip chart recorders, programmable logic controllers ("PLCs"), and proprietary turn-key devices and/or systems designed to automate

specific vertical applications.

Measurement and automation applications can be generally categorized as test and measurement ("T&M") or industrial/embedded ("IE"). T&M applications are used to research, design, manufacture and service a wide variety of products before they go to market. IE applications are used to design, prototype and deploy machinery to produce and distribute a wide variety of products and materials.

Historically, engineers and scientists have used a variety of cost-prohibitive instruments and systems that operated independently and could be difficult to customize. Due to the limitations of these systems, adapting them to changing needs can be expensive and time-consuming, and users must often purchase multiple single-purpose instruments.

Our Approach to Measurement and Automation

National Instruments provides engineers and scientists with an integrated software and hardware platform that accelerates the design and implementation of systems that need measurement and control. Our customers use our platform to develop test, measurement, control and embedded systems throughout industry from design to production; in advanced research; and in teaching engineering and science.

Reconfigurable Platform for System Design. Our graphical system design platform integrates fundamental elements of engineering in software and hardware, giving scientists and engineers the essential elements to create and customize systems that need measurement and control. Users can scale from design to test, from small to large systems, reusing the tools and our flexible platform of Graphical System Design.

Accelerate Development. Users accelerate their development by using our highly productive LabVIEW software that integrates and abstracts the complexity of systems at multiple levels, including unprecedented visualization of system timing. The NI graphical system design platform can lower total systems cost, increase flexibility, and integrate new technology using off-the-shelf customizable hardware that meets system needs from low power to high performance.

Innovate Rapidly. The NI graphical system design platform gives customers the power to innovate rapidly. The flexibility and scalability of the platform, supported by a growing ecosystem of reusable intellectual property ("IP") and applications, gives users a strong competitive advantage in completing more projects with less time and resources. Tens of thousands of engineers successfully use the NI graphical system design platform today to innovate, discover, and invent their own solutions.

Compared with traditional solutions, we believe our products and our graphical system design platform provides the following significant benefits to our customers:

Performance and Efficiency

Our software brings the power of commercial computers, handheld devices, networks and the Internet to instrumentation and embedded devices. With features such as graphical programming, automatic code generation, graphical tools libraries, ready-to-use example programs, libraries of specific instrumentation functions, and the ability to deploy applications on a range of platforms, scientists and engineers can quickly build a system that meets individual application needs. Because the continuous performance improvement of personal computers ("PC"), Field Programmable Gate Arrays ("FPGA") and networking technologies are the core platforms for our approach, scientists and engineers can quickly realize direct performance benefits, faster execution for measurement and automation applications, shorter test times, faster automation, higher performing embedded systems and higher manufacturing throughput.

Modularity, Reusability and Reconfigurability

Our products include reusable hardware and software modules to provide considerable flexibility in configuring systems. This ability to reconfigure measurement and automation systems allows users to quickly adapt their systems to new and changing needs, eliminate duplicated programming efforts, and ultimately improve their efficiency and productivity. In addition, these features help protect both hardware and software investments against obsolescence.

Lower Total Solution Cost

National Instruments solutions offer price/performance and energy-efficiency advantages over traditional proprietary systems. Graphical System Design allows customers to equip powerful industry-standard computers, with reusable system design software and modular cost-effective hardware. In addition, these systems give engineers and scientists the flexibility and portability to adapt to changing needs, while offering a smaller form factor that occupies less space on the manufacturing floor and consumes less energy than traditional instrumentation equipment.

Products, Technology and Services

We offer an extensive line of measurement and control products to work either separately, as stand-alone products or as an integrated solution; however, customers generally purchase our software and hardware together. We believe that the flexibility, functionality and ease of use of our system design software promotes sales of our other software and hardware products.

System Design Software

For the past 25 years, National Instruments has invested in its flagship software product, LabVIEW, which the company believes is the ultimate system design software for measurement and control. LabVIEW promotes problem-solving, accelerates productivity, and empowers innovation. With LabVIEW, users program graphically and can design custom virtual instruments by connecting icons with software wires to create “block diagrams” which are natural design notations for scientists and engineers. Users can customize front panels with knobs, buttons, dials and graphs to emulate control panels of instruments or add custom graphics to visually represent the control and operation of processes.

National Instruments believes that LabVIEW is the comprehensive development environment with the unprecedented hardware integration and wide-ranging compatibility that engineers and scientists need to design and deploy measurement and control systems. The LabVIEW programming environment is graphical, with engineering-specific libraries of software functions and hardware interfaces. It also offers data analysis, visualization and sharing features. Engineers and scientists can bring their vision to life with LabVIEW, and have access to a vast ecosystem of partners and technology alliances, and a global and active user community to innovate with confidence. When customers use LabVIEW, combined with the modular hardware approach with NI Data Acquisition, CompactRIO and PCI Extensions for Instrumentation (“PXI”) platforms, they are able to quickly integrate system components and do their jobs faster, better and at a lower cost.

LabVIEW Real-Time and LabVIEW FPGA are strategic modular software add-ons. With LabVIEW Real-Time, the user can easily configure their application program to execute using a real-time operating system kernel instead of the Windows operating system, so users can easily build virtual instrument solutions for mission-critical applications. In addition, with LabVIEW Real-Time, users can easily configure their programs to operate remotely on embedded processors in PXI-based systems, on embedded processors inside CompactRIO distributed I/O systems, or on processors embedded on plug-in PC data acquisition boards. With LabVIEW FPGA, the user can configure their application to execute directly in silicon via a Field Programmable Gate Array (“FPGA”) residing on one of our reconfigurable I/O hardware products. LabVIEW FPGA allows users to build their own highly specialized, custom hardware devices for ultra high-performance requirements or for unique or proprietary measurement or control protocols.

Programming Tools

In addition to LabVIEW, National Instruments offers LabWindows/CVI and Measurement Studio as alternative programming environments. LabWindows/CVI users use the conventional, text-based programming language of C for creating test and control applications. Measurement Studio consists of measurement and automation add-on libraries and additional tools for programmers who prefer Microsoft's Visual Basic, Visual C++, Visual C#, and Visual Studio.NET development environments.

Application Software

National Instruments also offers a suite of complementary software products, including NI TestStand, NI VeriStand, NI DIAdem and NI Multisim.

NI TestStand is targeted for T&M applications in a manufacturing environment. TestStand is a test management environment for organizing, controlling, and running automated prototype, validation, and manufacturing test systems. It also generates customized test reports and integrates product and test data across the customers' enterprise and across the Internet. TestStand manages tests that are written in LabVIEW, LabWindows/CVI, Measurement Studio, C and C++, and Visual Basic, so test engineers can easily share and re-use test code throughout their organization and from one product to the next. TestStand is a key element of our strategy to broaden the reach of our application software products across the corporate enterprise.

NI VeriStand is a ready-to-use software environment for configuring real-time testing applications, including hardware-in-the-loop ("HIL") test systems. With NI VeriStand, users configure real-time I/O, stimulus profiles, data logging, alarming, and other tasks; implement control algorithms or system simulations by importing models from a variety of software environments; build test system user interfaces quickly; and add custom functionality using NI LabVIEW, NI TestStand, and other software environments.

NI DIAdem offers users configuration-based technical data management, analysis, and report generation tools to interactively mine and analyze data. DIAdem helps users make informed decisions and meet the demands of today's testing environments, which require quick access to large volumes of scattered data, consistent reporting, and data visualization.

NI Multisim equips engineers, educators, and students with powerful and innovative circuit design technology. Educators and students can take advantage of easy-to-use teaching tools to overcome the traditional hurdles in electronics education. Professional engineers can improve productivity with intuitive capture tools, interactive simulation, board layout, and design validation.

We offer volume licensing that helps customers maximize their software investment by reducing total cost of ownership and simplifying their software budgeting and purchasing.

Hardware Products and Related Driver Software

Using cutting-edge commercial technology, such as the latest processors, Analog to Digital Converters ("ADCs"), FPGAs, and PC busses, our hardware delivers modular and easy-to-use solutions for a wide range of applications – from automated test and data logging to industrial control and embedded design. Our hardware and related driver software products include data acquisition ("DAQ"), PXI chassis and controllers, image acquisition, motion control, distributed I/O, modular instruments and embedded control hardware/software, industrial communications interfaces, General Purpose Interface Bus ("GPIB") interfaces, and VME Extension for Instrumentation ("VXI") Controllers. The high level of integration among our products provides users with the flexibility to mix and match hardware components when developing custom virtual instrumentation systems.

Data Acquisition (DAQ) Hardware/Driver Software. Our DAQ hardware and driver software products are "instruments on a board" that users can combine with sensors, signal conditioning hardware and software to acquire analog data and convert it into a digital format that can be accepted by a computer. Computer-based DAQ products are typically a lower-cost solution than traditional instrumentation and exploit the processing power, display, and connectivity capabilities of industry-standard computers. Applications suitable for automation with computer-based DAQ products are widespread throughout many industries, and many systems currently using traditional instrumentation (either manual or computer-controlled) could be displaced by computer-based DAQ systems. We offer a range of computer-based DAQ products with a variety of form factors and degrees of performance. In 2006, we introduced NI CompactDAQ, a rugged, portable, USB data acquisition system designed for high-performance mixed-signal measurement systems. Since its introduction, we have expanded the CompactDAQ platform with wireless and Ethernet technologies that have extended the reach of computer-based DAQ from across the lab to around the world. Some of our latest introductions in this area include X Series DAQ which delivers state-of-the-art measurement, generation, timing and triggering on a single device.

PXI Modular Instrumentation Platform. Our PXI modular instrument platform, which was introduced in 1997, is a standard PC packaged in a small, rugged form factor with expansion slots and instrumentation extensions for timing, triggering and signal sharing. It combines mainstream PC software and PCI hardware with advanced instrumentation capabilities. In essence, PXI is an instrumentation PC with several expansion slots supporting complete system-level opportunities and delivering a much higher percentage of the overall system content using our own products. We continue to expand our PXI product offerings with new modules, which address a wide variety of measurement and automation applications. The platform is now a testing standard, with a wide array of companies developing on the platform and investing in its future through the PXI System Alliance ("PXISA"). In 2006, we introduced our first PXI Express products which provide backward software compatibility with PXI while providing advanced capabilities for high-performance instrumentation, such as RF instrumentation. Today, we have a rapidly expanding portfolio of PXI Express products that are further expanding the capabilities of this important platform.

Modular Instruments. We offer a variety of modular instrument devices used in general purpose test and communication test applications. These devices include digitizers, digital multimeters, signal generators, RF analyzers/generators, power supplies, source measurement units and switch modules that users can configure through software to meet their specific measurement tasks. Because these instruments are modular and software-defined, they can be quickly interchanged and easily repurposed to meet evolving test needs. Additionally, our modular instruments provide high-speed test execution by harnessing the power of industry-standard PC FPGAs and advanced timing and synchronization technologies. Options are available for a variety of platforms including PXI, PXI Express, PCI, PCI Express, and USB.

Machine Vision/Image Acquisition. Our machine vision platform includes a range of hardware platform options, from embedded NI Smart Cameras that integrate the sensor and processor in a single package to NI Embedded and NI Compact Vision Systems to plug-in boards for PCI and PXI systems. We offer two software options for use across the entire NI vision hardware portfolio. A user can configure a system with NI Vision Builder for Automated Inspection, an easy-to-use, stand-alone package for machine vision, or program it using the NI Vision Development Module, a comprehensive library of imaging functions. With NI Vision hardware, a user can build high-performance, PC based systems using the latest processor techniques with NI Frame Grabbers, save on cost and space by combining an image sensor and real-time embedded processors into one rugged, industrial package with NI Smart Cameras, or harness multicore performance with fanless designs, connectivity to multiple cameras and reconfigurable digital I/O with NI Vision systems.

Motion Control. By integrating flexible software with high-performance hardware, our motion control products offer a powerful solution for motion system design. From automating test equipment and research labs to controlling biomedical, packaging, and manufacturing machines, engineers use our motion products to meet a diverse set of application challenges. Our software tools for motion easily integrate with our other product lines, so users can combine motion control with image acquisition, test, measurement, data acquisition, and automation to create robust,

flexible solutions. We introduced our first line of motion control hardware, software and peripheral products in 1997.

NI RIO Hardware Platform. NI reconfigurable I/O ("RIO") hardware combined with NI LabVIEW system design software provides a commercial off-the-shelf solution to simplify development and shorten time to market when designing advanced measurement and control systems. All NI RIO hardware systems, which include products like CompactRIO, NI Single-Board RIO, R Series boards and PXI-based FlexRIO, feature a standard, high-performance architecture that combines a powerful floating-point processor, reconfigurable FPGA, and modular I/O. Engineers can program all NI RIO hardware components with NI LabVIEW, including the LabVIEW FPGA Module, to rapidly create custom timing, signal processing and control for I/O without requiring expertise in low-level hardware description languages or board-level design. NI provides a breadth of NI RIO hardware targets that provide varying degrees of performance, cost, I/O rates, and ruggedness, to meet any unique application need. NI first released NI RIO hardware in 2003 with the release of the first R Series PXI plug-in board along with the release of the first CompactRIO rugged, high-performance embedded system. To date, NI has released over 60 NI RIO FPGA-based hardware products.

Industrial Communications Interfaces. In 1995, we began shipping our first interface boards for communicating with serial devices, such as data loggers and PLCs targeted for industrial/embedded applications, and benchtop instruments, such as oscilloscopes, targeted for test and measurement applications. We offer hardware and driver software product lines for communication with industrial devices—Controller Area Network ("CAN"), DeviceNet, Foundation Fieldbus, and RS-485 and RS-232.

GPIB Interfaces/Driver Software. We began selling GPIB products in 1977 and are a leading supplier of GPIB interface boards and driver software to control traditional GPIB instruments. These traditional instruments are manufactured by a variety of third-party vendors and are used primarily in T&M applications. Our diverse portfolio of hardware and software products for GPIB instrument control is available for a wide range of computers. Our GPIB product line also includes products for controlling GPIB instruments using the computer's standard parallel, USB, Ethernet, and serial ports.

VXI Controllers//Driver Software. We are a leading supplier of VXI computer controller hardware and the accompanying NI-VXI and NI-VISA driver software. We also offer LabVIEW, LabWindows/CVI, Measurement Studio and TestStand software products for VXI systems.

Services

System Configuration and Deployment. Our trained technicians install software and hardware and configure our customers' PXI, PXI/SCXI combination, NI CompactRIO, or NI Compact FieldPoint system to their specifications.

Calibration. We provide calibration solutions, including recalibration services, manual calibration procedures, and automated calibration software. In 2011, the American Association for Laboratory Accreditation (A2LA) accredited NI Calibration Services Austin to one of the highest international calibration standards in the industry, ISO/IEC 17025:2005. National Instruments now offers 17025 calibration services for OEMs and other organizations seeking to maintain compliance with the strictest governmental, medical, transportation and electronics regulations. The new calibration service offering is ideal for companies standardizing their automated test and measurement systems on PXI modular instrumentation, which provides some of the most advanced technology for addressing the latest engineering challenges.

Warranty and Repair. We offer standard and extended warranties to help meet project life-cycle requirements and provide repair services for our products, express repair, and advance replacement services.

Customer Training Courses. We offer fee-based training classes and self-paced course kits for many of our software and hardware products. On-site courses are quoted per customer requests and we include on-line course offerings with

live teachers. We also offer programs to certify programmers and instructors for our products.

Software Maintenance

Software maintenance revenue is post-purchase contract customer support that provides the customer with unspecified upgrades and/or updates and technical support.

Markets and Applications

Our products are used across many industries in a variety of applications including research and development, simulation and modeling, product design, prototype and validation, production testing and industrial control and field and factory service and repair. We serve the following industries and applications worldwide: advanced research, automotive, automated test equipment, consumer electronics, commercial aerospace, computers and electronics, continuous process manufacturing, education, government/defense, medical research/pharmaceutical, power/energy, semiconductors, telecommunications and others.

Customers

We have a broad base of over 35,000 customers worldwide, with no customer accounting for more than 4% of our sales in 2011 and 2010 or 3% of our sales in 2009.

Marketing

Through our worldwide marketing efforts, we strive to educate engineers and scientists about the benefits of our graphical system design philosophy, products and technology, and to highlight the performance and cost advantages of our products. We also seek to present our position as a technology leader among producers of instrumentation software and hardware and to help promulgate industry standards that can benefit users of computer-based instrumentation.

We reach our intended audience through our website at ni.com as well as through the distribution of written and electronic materials including demonstration versions of our software products, participation in tradeshows and technical conferences and training and user seminars.

We actively market our products in higher education environments, and we identify many colleges, universities and trade and technical schools as key accounts. We offer special academic pricing and products to enable universities to utilize our products in their classes and laboratories. We believe our prominence in the higher education area can contribute to our future success because students gain experience using our products before they enter the work force.

Sales and Distribution

We sell 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. Sales through any one of these channels accounted for less than 5% of our total sales in 2011. Our Hungarian manufacturing facility sources a substantial majority of our sales throughout the world. We have sales offices in the U.S. and sales offices and distributors in key international markets. Sales outside of the U.S. accounted for approximately 63%, 62% and 61%, of our revenues in 2011, 2010 and 2009, respectively. 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 identifiable assets.)

We believe the ability to provide comprehensive service and support to our customers is an important factor in our business. We permit customers to return products within 30 days from receipt for a refund of the purchase price less a restocking charge. Our products are generally warranted against defects in materials and workmanship for one year from the date we ship the products to our customers. Historically, warranty costs and returns have not been material.

The marketplace for our products dictates that many of our products be shipped very quickly after an order is received. As a result, we are required to maintain significant inventories. Therefore, inventory obsolescence is a risk for us due to frequent engineering changes, shifting customer demand, the emergence of new industry standards and rapid technological advances including the introduction by us or our competitors of products embodying new technology. We strive to mitigate this risk by monitoring inventory levels against product demand and technological changes. Additionally, many of our products have interchangeable parts and many have long lives. There can be no assurance that we will be successful in these efforts in the future.

Our foreign operations are subject to certain risks set forth on page 16 under “We are Subject to Various Risks Associated with International Operations and Foreign Economies.”

See discussion regarding fluctuations in our quarterly results and seasonality in ITEM 1A, Risk Factors, “Our Revenues are Subject to Seasonal Variations.”

Competition

The markets in which we operate are characterized by intense competition from numerous competitors, some of which are divisions of large corporations having far greater resources than we have, and we may face further competition from new market entrants in the future. A key competitor is Agilent Technologies Inc. (“Agilent”). Agilent offers hardware and software products that provide solutions that directly compete with our virtual instrumentation products and has recently released its own line of PXI based hardware. Agilent is aggressively advertising and marketing products that are competitive with our products. Because of Agilent’s strong position in the instrumentation business, changes in its marketing strategy or product offerings could have a material adverse effect on our operating results.

We believe our ability to compete successfully depends on a number of factors both within and outside our control, including:

- general market and economic conditions, particularly in the Euro zone;
- success in developing new products;
- timing of our new product introductions;
- new product introductions by competitors;
- the ability of competitors to more fully leverage low cost geographies;
- the impact of foreign exchange rates on product pricing;
- product pricing;
- effectiveness of sales and marketing resources and strategies;
- adequate manufacturing capacity and supply of components and materials;
- efficiency of manufacturing operations;
- strategic relationships with our suppliers;
- quality and performance;
- protection of our products by effective use of intellectual property laws;
- the outcome of any material intellectual property litigation;
- the financial strength of our competitors;
- barriers to entry imposed by competitors with significant market power in new markets; and
- government actions throughout the world.

We currently believe that we compete effectively with respect to the foregoing factors; however, there can be no assurance that we will be able to compete successfully in the future.

Research and Development

We believe that our long-term growth and success depends on delivering high quality hardware and software products on a timely basis. We intend to 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 and price/performance characteristics.

Our research and development staff strives to build quality into our products at the design stage in an effort to reduce overall development and manufacturing costs. Our research and development staff also designs proprietary application specific integrated circuits ("ASICs"), many of which are designed for use in several of our products. The goal of our ASIC design program is to further differentiate our products from competing products, to improve manufacturability and to reduce costs. We seek to reduce our time to market for new and enhanced products by sharing our internally developed hardware and software components across multiple products.

As of December 31, 2011, we employed 1,868 people in product research and development. Our research and development expenses were $199 million, $158 million and $133 million for 2011, 2010 and 2009, respectively.

Intellectual Property

We rely on a combination of patent, trade secret, copyright and trademark law, contracts and technical measures to establish and protect our proprietary rights in our products. As of December 31, 2011, we held 610 U.S. patents (607 utility patents and 3 design patents) and 23 patents in foreign countries (22 patents registered in Europe in various countries; and 1 patent in Japan), and had 280 patent applications pending in the U.S. and foreign countries. 170 of our issued U.S. patents are software patents related to LabVIEW, and cover fundamental aspects of the graphical programming approach used in LabVIEW. Our patents expire from 2012 to 2030. The expiration of any patents in the short term is not expected to have any significant negative impact on our business. No assurance can be given that our pending patent applications will result in the issuance of patents. We also own certain registered trademarks in the United States and abroad. See further discussion regarding risks associated with our patents in ITEM 1A, Risk Factors, "Our Business Depends on Our Proprietary Rights and We are Subject to Intellectual Property Litigation."

Manufacturing and Suppliers

We manufacture a substantial majority of our products at our facilities in Debrecen, Hungary. Additional production primarily of low volume, complex 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 have used a subcontractor in Asia to manufacture a significant portion of our chassis but most of that production was moved in house during 2010. 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.

Our long term manufacturing and warehousing capacity planning contemplates a third manufacturing and warehousing facility in Penang, Malaysia. We began warehousing and distribution operations out of Penang, Malaysia via a third party logistics provider in October 2010. We began construction of our manufacturing and logistics facility in Malaysia in the third quarter of 2011.

Our manufacturing processes use large volumes of high-quality components and subassemblies supplied by outside sources in the U.S., Europe and Asia. Several of these components are available through limited sources. Limited source components purchased include custom ASICs and other RF or custom components. Any disruption of our supply of limited source components, whether resulting from business demand, quality, production or delivery problems, could adversely affect our ability to manufacture our products, which could in turn adversely affect our business and results of operations. See “Our Business is Dependent on Key Suppliers” at page 12 for additional discussion of the risks associated with limited source suppliers.

See “Our Manufacturing Operations are Subject to a Variety of Environmental Regulations and Costs” at page 17 for discussion of environmental matters as they may affect our business.

Backlog

Backlog is a measure of orders that are received but that are not shipped to customers at the end of a quarter. We typically ship products shortly following the receipt of an order. Accordingly, our backlog typically represents less than 5 days sales. Backlog should not be viewed as an indicator of our future sales.

Employees

As of December 31, 2011, we had 6,235 employees worldwide, including 1,868 in research and development, 2,854 in sales and marketing and customer support, 808 in manufacturing and 705 in administration and finance. None of our employees are represented by a labor union and we have never experienced a work stoppage. We consider our employee relations to be good. For thirteen consecutive years, from 1999 to 2011, we have been named among the 100 Best Companies to Work for in America according to FORTUNE magazine.

ITEM 1A. RISK FACTORS

Uncertain Economic Conditions Could Materially Adversely Affect Our Business and Results of Operations. Our business is sensitive to fluctuations in general economic conditions, both in the U.S. and globally. Uncertainty associated with financial markets, negative financial news, foreign currency markets, natural disasters, energy costs, budget and tax policies throughout the world's developed economies, employment levels, labor costs, healthcare costs, declining income or asset values and credit availability, could negatively impact the global industrial economy. Historically, our business cycles have generally followed the expansion and contraction cycles in the global industrial economy as measured by the PMI. The most recent reading for December 2011, showed the PMI had increased to 50.8 up from readings below 50 for the previous three months, but continues to indicate overall weakness in the global industrial economy. A reading above 50 indicates an expanding industrial economy while a reading below 50 indicates a contracting industrial economy. We are unable to predict whether the industrial economy, as measured by the PMI will strengthen or contract during 2012. If the industrial economy, as measured by the PMI, contracts or remains at a neutral reading at or around 50, indicating general weakness, 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 result of operations.

Our Revenues are Subject to Seasonal Variations. In previous years, our revenues have been characterized by seasonality, with revenues typically growing from the first quarter to the second quarter, being relatively constant from the second quarter to the third quarter, growing in the fourth quarter compared to the third quarter and declining in the first quarter of the following year from the fourth quarter of the preceding year. This historical trend has been affected and may continue to be affected in the future by broad fluctuations in the global industrial economy, the economic impact of larger orders as well as the timing of new product introductions or acquisitions, if any. The economic contraction in the Euro zone during the fourth quarter of 2011 could persist or worsen in 2012. If this instability in the Euro zone continues, worsens or negatively affects other economic regions in 2012, it may have a material adverse effect on the seasonal patterns described above as well as on our overall results of operations and profitability. Our total operating expenses have in the past tended to increase in each successive quarter and have fluctuated as a percentage of revenue based on the seasonality of our revenue.

Concentrations of Credit Risk and Uncertain Conditions in the Global Financial Markets May Adversely Affect Our Business and Result of Operations. By virtue of our holdings of cash, investment securities and foreign currency derivatives, we have exposure to many different counterparties, and routinely execute transactions with counterparties in the financial services industry, including commercial banks and investment banks. Many of these transactions expose us to credit risk in the event of a default of our counterparties. We continue to monitor the stability of the financial markets, particularly those in the European region and have taken steps to limit our direct and indirect exposure to these markets; however, we can give no assurance that we will not be negatively impacted by any adverse outcomes in those markets. There can be no assurance that any losses or impairments to the carrying value of our financial assets as a result of defaults by our counterparties, would not materially and adversely affect our business, financial position and results of operations.

Changes in the Amount of Revenue Derived from Large Orders Could Adversely Affect our Gross Margin and Could Lead to Greater Variability in our Quarterly Results. Our large order business, defined as orders with a value greater than $20,000, continues to grow as a percent of our overall business. As a percent of our overall business, larger orders reached a new high during 2011 and represented 45%, 42% and 38% of our total sales during 2011, 2010 and 2009, respectively. 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. Historically, our gross margins have been stable from period to period. To the extent that the amount of our revenue derived from larger orders increases in future periods, both in absolute dollars and as a percent of our overall business, our gross margins could experience greater volatility and see a greater negative impact from future downturns in the global industrial

economy. This dynamic may also have an adverse effect on the historical seasonal pattern of our revenues and our results of operations.

Risks or Claims Associated With the Compliance With Our Pricing Provisions of Our Previous GSA Contract Could Have a Material Adverse Impact on Our Results of Operations. 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 previous contract with GSA contained a price reduction or "most favored customer" pricing provision. For the past several months, 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 conducted an on-site review of our GSA pricing practices and orally informed us that GSA did not agree with our previous determination of the potential non-compliance amount. GSA subsequently requested that we conduct a further analysis of the non-compliance amount based upon a methodology that GSA proposed. This analysis resulted in calculated overpayments (including added interest) by GSA to us of approximately $13.1 million. GSA is reviewing the analysis and has not yet officially responded, and has not made any formal demand for pricing adjustments related to our previous 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. As a result of the foregoing, during the quarter ended September 30, 2011, we established an accrual of $13.1 million which represents the amount of the loss contingency that is reasonably estimable at this time. There can be no assurance that our actual losses will not exceed such reserve amount. Due to the complexities of conducting business with GSA, the relatively small amount of revenue we realized from our previous 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 previous GSA contract.

Our Acquisitions are Subject to a Number of Related Costs and Challenges that Could Have a Material Adverse Effect on Our Business and Results of Operations. During the second quarter of 2011, we completed the acquisitions of AWR Corporation (AWR) and Phase Matrix Inc. (PMI). We may in the future acquire additional complementary businesses, products or technologies. Achieving the anticipated benefits of an acquisition depends upon whether the integration of the acquired business, products or technology is accomplished efficiently and effectively. In addition, successful acquisitions generally require, among other things, integration of product offerings, manufacturing operations and coordination of sales and marketing and R&D efforts. These difficulties can become more challenging due to the need to coordinate geographically separated organizations, the complexities of the technologies being integrated, and the necessities of integrating personnel with disparate business backgrounds and combining different corporate cultures. The integration of operations following an acquisition also requires the dedication of management resources, which may distract attention from our day-to-day business and may disrupt key R&D, marketing or sales efforts. Our inability to successfully integrate AWR and PMI or any future acquisition could harm our business. The existing products previously sold by entities we have acquired may be of a lesser quality than our products and/or could contain errors that produce incorrect results on which users rely or cause failure or interruption of systems or processes that could subject us to liability claims that could have a material adverse effect on our operating results or financial position. Furthermore, products acquired in connection with acquisitions may not gain acceptance in our markets, and we may not achieve the anticipated or desired benefits of such transactions.

Our Quarterly Results are Subject to Fluctuations Due to Various Factors that May Adversely Affect Our Business and Result of Operations. Our quarterly operating results have fluctuated in the past and may fluctuate significantly in the future due to a number of factors, including:

- changes in the global economy or global credit markets, particularly in the Euro zone;
- adjustments to acquisition earn-out accruals;
- changes in the amount of revenue derived from large orders;
- fluctuations in foreign currency exchange rates;
- the timing, cost or outcome of any future intellectual property or commercial disputes including under our previous GSA contract;
- changes in the mix of products sold;
- the availability and pricing of components from third parties (especially limited sources);
- the difficulty in maintaining margins, including the higher margins traditionally achieved in international sales;
- changes in pricing policies by us, our competitors or suppliers;
- delays in product shipments caused by human error or other factors; and,