NATIONAL INSTRUMENTS CORP /DE/
Form 10-Q
November 09, 2007

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended: September 30, 2007 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

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 [ ]

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

Large accelerated filer [X] Accelerated filer [ ] Non-accelerated filer [ ]
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

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

Class	**Outstanding at November 8, 2007**
Common Stock - $0.01 par value	79,605,323

NATIONAL INSTRUMENTS CORPORATION

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

NATIONAL INSTRUMENTS CORPORATION

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	September 30, 2007	December 31, 2006
Assets	(unaudited)	
Current assets:		
Cash and cash equivalents	$ 183,471	$ 100,287

	September 30, 2007	December 31, 2006
Short-term investments	92,628	150,190
Accounts receivable, net	121,291	117,235
Inventories, net	77,313	77,138
Prepaid expenses and other current assets	25,846	11,393
Deferred income tax, net	20,922	20,851
Total current assets	521,471	477,094
Property and equipment, net	148,702	145,425
Goodwill, net	53,970	53,343
Intangible assets, net	42,200	40,065
Other long-term assets	7,047	5,293
Total assets	$ 773,390	$ 721,220
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 39,875	$ 32,001
Accrued compensation	25,881	20,912
Deferred revenue	29,982	22,208
Accrued expenses and other liabilities	11,318	12,871
Other taxes payable	15,907	11,527
Total current liabilities	122,963	99,519
Deferred income taxes	20,473	20,472
Other long-term liabilities	9,314	4,643
Total liabilities	152,750	124,634
Commitments and contingencies		
Stockholders' equity:		
Preferred stock: par value $0.01; 5,000,000 shares authorized;none issued and outstanding		
Common Stock: par value $0.01; 180,000,000 shares authorized; 79,362,327 and 79,883,837 shares issuedand outstanding, respectively	794	799
Additional paid-in capital	86,734	109,851
Retained earnings	525,686	483,437
Accumulated other comprehensive income	7,426	2,499
Total stockholders' equity	620,640	596,586
Total liabilities and stockholders' equity	$ 773,390	$ 721,220

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

NATIONAL INSTRUMENTS CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006

	Three Months Ended September 30,		Nine Months Ended September 30,	
Net sales	$ 184,426	$ 164,079	$ 535,565	$ 478,954
Cost of sales	46,219	42,431	132,439	124,788
Gross profit	138,207	121,648	403,126	354,166
Operating expenses:				
Sales and marketing	66,116	58,479	194,974	172,459
Research and development	31,891	27,742	91,652	83,121
General and administrative	15,644	13,060	45,643	39,482
Total operating expenses	113,651	99,281	332,269	295,062
Operating income	24,556	22,367	70,857	59,104
Other income (expense):				
Interest income	2,613	1,964	7,056	4,898
Net foreign exchange gain	98	432	628	195
Other income (expense), net	14	(29)	(138)	78
Income before income taxes	27,281	24,734	78,403	64,275
Provision for income taxes	5,741	6,083	17,063	16,001
Net income	$ 21,540	$ 18,651	$ 61,340	$ 48,274
Basic earnings per share	$ 0.27	$ 0.23	$ 0.77	$ 0.61
Weighted average shares outstanding-basic	79,226	79,637	79,471	79,436
Diluted earnings per share	$ 0.27	$ 0.23	$ 0.76	$ 0.59
Weighted average shares outstanding-diluted	80,874	81,274	80,986	81,504
Dividends declared per share	$ 0.10	$ 0.06	$ 0.24	$ 0.18

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

NATIONAL INSTRUMENTS CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)
(unaudited)

	Nine Months Ended September 30,	
	2007	2006
Cash flow from operating activities:		
Net income	$ 61,340	$ 48,274
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	27,964	25,263
Stock-based compensation	13,051	10,773

	Nine Months Ended September 30,	
(Benefit from) deferred income taxes	(360)	(934)
Tax benefit from stock option plans	(2,391)	(3,025)
Changes in operating assets and liabilities:		
Accounts receivable, net	(4,056)	(7,596)
Inventories	(175)	(16,688)
Prepaid expenses and other assets	(14,186)	(2,966)
Accounts payable	7,874	(32)
Deferred revenue	7,774	3,072
Taxes and other liabilities	16,797	15,245
Net cash provided by operating activities	113,632	71,386
Cash flow from investing activities:		
Capital expenditures	(18,109)	(10,841)
Capitalization of internally developed software	(7,736)	(6,276)
Additions to other intangibles	(4,962)	(1,726)
Purchases of short-term investments	(62,968)	(157,746)
Sales and maturities of short-term investments	120,530	107,642
Net cash provided by (used in) investing activities	26,755	(68,947)
Cash flow from financing activities:		
Proceeds from issuance of common stock	27,454	22,835
Repurchase of common stock	(67,957)	(16,519)
Dividends paid	(19,091)	(14,267)
Tax benefit from stock option plans	2,391	3,025
Net cash used in financing activities	(57,203)	(4,926)
Changes in cash and cash equivalents	83,184	(2,487)
Cash and cash equivalents at beginning of period	100,287	55,864
Cash and cash equivalents at end of period	$ 183,471	$ 53,377

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

NATIONAL INSTRUMENTS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 Basis of Presentation

The accompanying unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2006, included in our annual report on Form 10-K filed with the Securities and Exchange Commission. In our opinion, the accompanying consolidated financial statements reflect all adjustments (consisting only of normal recurring items) considered necessary to present fairly our financial position at September 30, 2007 and December 31, 2006, and the results of our operations for the three-month and nine-month periods ended September 30, 2007 and 2006, and the cash flows for the nine-month periods ended September 30, 2007 and 2006. Operating results for the three-month and nine-month periods ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

NOTE 2 Earnings Per Share

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

computed using the treasury stock method.

The reconciliation of the denominators used to calculate basic EPS and diluted EPS for the three-month and nine-month periods ended September 30, 2007 and 2006, respectively, are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	(unaudited)		(unaudited)	
	2007	2006	2007	2006
Weighted average shares outstanding-basic	79,226	79,637	79,471	79,436
Plus: Common share equivalents				
Stock options, restricted stock units	1,648	1,637	1,515	2,068
Weighted average shares outstanding-diluted	80,874	81,274	80,986	81,504

Stock options to acquire 1,198,000 and 4,001,000 shares for the three months ended September 30, 2007 and 2006, respectively, and 2,450,000 and 3,276,000 shares for the nine months ended September 30, 2007 and 2006, respectively, were excluded in the computations of diluted EPS because the effect of including the stock options would have been anti-dilutive.

NOTE 3 Inventories

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

	September 30, 2007	December 31, 2006
	(unaudited)	
Raw materials	$ 38,001	$ 38,270
Work-in-process	3,199	4,321
Finished goods	36,113	34,547
	$ 77,313	$ 77,138

NOTE 4 Intangibles

Intangibles at September 30, 2007 and December 31, 2006 are as follows:

	September 30, 2007			December 31, 2006		
	(unaudited)					
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Capitalized software development costs	$ 65,306	$ (48,284)	$ 17,022	$ 57,571	$ (41,791)	$ 15,780
Acquired technology	20,966	(12,179)	8,787	20,814	(9,734)	11,080
Patents	14,180	(3,608)	10,572	12,928	(3,076)	9,852
Other	10,089	(4,270)	5,819	6,452	(3,099)	3,353
	$ 110,541	$ (68,341)	$ 42,200	$ 97,765	$ (57,700)	$ 40,065

Software development costs capitalized for the three months ended September 30, 2007 and 2006 were $1.7 million and $2.3 million, respectively, and related amortization was $2.2 million and $2.0 million, respectively. Software development costs capitalized for the nine

months ended September 30, 2007 and 2006 were $7.7 million and $6.3 million, respectively, and related amortization was $6.5 million and $7.1 million, respectively. Amortization of capitalized software development costs is computed on an individual product basis for those products available for market and is recognized based on the products estimated economic life, generally three years. Patents are amortized using the straight-line method over their estimated period of benefit, generally ten to seventeen years. Total intangible assets amortization expenses were $3.6 million and $3.2 million for the three months ended September 30, 2007 and 2006, respectively, and were $10.5 million and $10.7 million for the nine months ended September 30, 2007 and 2006, respectively.

Acquired core technology and intangible assets are amortized over their useful lives, which range from three to eight years. Amortization expense for intangible assets acquired was approximately $798,000 and $805,000 for the three months ended September 30, 2007 and 2006, respectively, of which approximately $678,000 and $682,000 was recorded in cost of sales for the three months ended September 30, 2007 and 2006, respectively, and approximately $120,000 and $123,000 was recorded in operating expenses for the three months ended September 30, 2007 and 2006, respectively. The estimated amortization expense of intangible assets acquired for the current fiscal year and in future years will be recorded in the consolidated statements of income as follows (in thousands):

Fiscal Year	Cost of Sales	Acquisition related costs and amortization, net	Total
2007	$ 2,689	$ 450	$ 3,139
2008	2,532	412	2,944
2009	2,259	338	2,597
2010	1,725	177	1,902
Thereafter	1,166	271	1,437
Total	$ 10,371	$ 1,648	$ 12,019

NOTE 5 Goodwill

The carrying amount of goodwill for 2007 is as follows:

	Amount (in thousands)
Balance as of December 31, 2006	$ 53,343
Acquisitions/purchase accounting adjustments	
Divestitures	
Foreign currency translation impact	627
Balance as of September 30, 2007	$ 53,970

The excess purchase price over the fair value of assets acquired is recorded as goodwill. In accordance with SFAS 142, *Goodwill and Other Intangible Assets*, goodwill is tested for impairment on an annual basis, and between annual tests if indicators of potential impairment exist, using a fair-value-based approach. Our annual impairment test was performed on February 28, 2007. No impairment of goodwill was identified. Goodwill is deductible for tax purposes.

NOTE 6 Income Taxes

In July 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation ("FIN") 48, *Accounting for Uncertainty in Income Taxes - an interpretation of Statement of Financial Accounting Standards ("SFAS") 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements and prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. We adopted FIN 48 on January 1, 2007, as required. The cumulative effect of adopting FIN 48 was $96,000, which was recorded as a reduction in beginning retained earnings upon adoption, as required. We recognized no material adjustment to the liability for unrecognized income tax benefits. We had $4.6 million of unrecognized tax benefits at January 1, 2007 and $6.8 million at September 30, 2007, all of which would affect our effective income tax rate if recognized. None of our unrecognized income tax benefits are expected to significantly decrease or increase within the next twelve months. Our continuing policy is to recognize interest and penalties related to income tax matters in income tax expense. As of September 30, 2007, we have approximately

$343,000 accrued for interest related to uncertain tax positions. The tax years 2000 through 2006 remain open to examination by the major taxing jurisdictions to which we are subject.

NOTE 7 Comprehensive Income

Our comprehensive income is comprised of net income, foreign currency translation and unrealized gains and losses on forward and option contracts and securities available for sale. Comprehensive income for the three-month and nine-month periods ended September 30, 2007 and 2006 was as follows (in thousands):

	Three Months Ended September 30, (unaudited)		Nine Months Ended September 30, (unaudited)	
	2007	2006	2007	2006
Comprehensive income:				
Net income	$ 21,540	$ 18,651	$ 61,340	$ 48,274
Foreign currency translation gains (losses)	3,557	(346)	4,896	3,436
Unrealized gains (losses) on derivative instruments	(331)	355	(190)	(291)
Unrealized gains (losses) on securities available for sale	200	207	219	6
Total comprehensive income	$ 24,966	$ 18,867	$ 66,265	$ 51,425

NOTE 8 Stock-Based Compensation Plans

Stock option plans

Our stockholders approved the 1994 Incentive Stock Option Plan (the 1994 Plan) on May 9, 1994. At the time of approval, 9,112,500 shares of our common stock were reserved for issuance under this plan. In 1997, an additional 7,087,500 shares of our common stock were reserved for issuance under this plan, and an additional 750,000 shares were reserved for issuance under this plan in 2004. The 1994 Plan terminated in May 2005, except with respect to outstanding awards previously granted thereunder. Awards under the plan were either incentive stock options within the meaning of Section 422 of the Internal Revenue Code or nonqualified options. The right to purchase shares vests over a five to ten-year period, beginning on the date of grant. Vesting of ten year awards may accelerate based on the Company s previous year s earnings and growth but shares cannot accelerate to vest over a period of less than five years. Stock options must be exercised within ten years from date of grant. Stock options were issued at the market price at the grant date. As part of the requirements of SFAS 123R, the Company is required to estimate potential forfeitures of stock grants and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods.

Transactions under all stock option plans are summarized as follows:

	Number of shares under option	Weighted average Exercise price
Outstanding at December 31, 2006	6,914,673	$ 22.49
Exercised	(1,228,843)	29.17
Canceled	(99,542)	27.39
Granted	0	0
Outstanding at September 30, 2007	5,586,288	$ 24.16

The aggregate intrinsic value of stock options at exercise, represented in the table above, was $18.0 million for the nine months ended September 30, 2007. Total unrecognized stock-based compensation expense related to non-vested stock options was approximately $13.1 million as of September 30, 2007, related to approximately 1,040,000 shares with a per share weighted average fair value of $16.15. We anticipate this expense to be recognized over a weighted average period of approximately 3.5 years.

Outstanding and Exercisable by Price Range
As of September 30, 2007

	Options Outstanding			Options Exercisable	
Range of Exercise prices	**Number outstanding as of 09/30/2007**	**Weighted average remaining contractual life**	**Weighted average exercise price**	**Number exercisable as of 09/30/2007**	**Weighted average exercise price**
$ 11.3333 $ 20.8333	1,509,625	2.15	$ 15.5373	1,378,144	$ 15.1658
$ 21.0417 $ 27.9467	1,756,286	4.15	$ 22.3955	1,370,566	$ 22.3900
$ 28.3933 $ 29.8500	929,396	6.47	$ 29.7693	515,676	$ 29.7563
$ 30.5100 $ 32.0833	1,334,014	2.64	$ 31.9308	1,235,879	$ 31.9400
$ 32.4700 $ 34.3750	56,967	4.52	$ 33.3877	46,572	$ 33.5239
$ 11.3333 $ 34.3750	5,586,288	3.64	$ 24.1581	4,546,837	$ 23.7456

The weighted average remaining contractual life of options exercisable as of September 30, 2007 was 3.25 years. The aggregate intrinsic value of options outstanding as of September 30, 2007 was $56.8 million. The aggregate intrinsic value of options currently exercisable as of September 30, 2007 was $48.1 million. No options were granted in the nine months ended September 30, 2007 as our incentive option plan terminated in May 2005.

Restricted stock plan

Our stockholders approved the 2005 Incentive Plan on May 10, 2005. At the time of approval, 2,700,000 shares of our common stock were reserved for issuance under this plan, as well as the number of shares which had been reserved, but not issued under the 1994 Plan (our stock option plan which terminated in May 2005), and any shares that returned to the 1994 Plan as a result of termination of options or repurchase of shares issued under such plan. The 2005 Plan, administered by the Compensation Committee of the Board of Directors, provides for granting of incentive awards in the form of restricted stock units to directors, executive officers and employees of the Company and its subsidiaries. Awards vest over a three, five or ten-year period, beginning on the date of grant. Vesting of ten year awards may accelerate based on the Company s previous year s earnings and growth but ten year awards cannot accelerate to vest over a period of less than five years. Shares available for grant at September 30, 2007 were 3,094,735. As part of the requirements of SFAS 123R, we are required to estimate potential forfeitures of restricted stock units and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods.

Transactions under the restricted stock plan are summarized as follows:

	RSUs	
	Number of RSUs	**Weighted Average Grant Price**
Balance at December 31, 2006	1,324,933	$ 26.77
Granted	767,655	27.62
Vested	(209,303)	27.85
Canceled	(58,284)	27.57
Balance at September 30, 2007	1,825,001	$ 26.73

Total unrecognized stock-based compensation expense related to non-vested restricted stock units was approximately $46.0 million as of September 30, 2007, related to 1,825,001 shares with a per share fair value of $34.33. We anticipate this expense to be recognized over a weighted average period of approximately 6.7 years.

Employee stock purchase plan

Our employee stock purchase plan permits substantially all domestic employees and employees of designated subsidiaries to acquire our common stock at a purchase price of 85% of the lower of the market price at the beginning or the end of the participation period. On December 21, 2005, our Compensation Committee amended the periods to be quarterly beginning on November 1, February 1, May 1 and August 1 of each year. The initial period commenced on April 1, 2006 and ended on July 31, 2006. Employees may designate up to 15% of their compensation for the purchase of common stock. The aggregate number of shares of common stock reserved for future employee purchases was 3,402,738 shares at September 30, 2007. In May 2007, our shareholders approved an additional 3,000,000 shares to be reserved under this plan. The number of shares issued under this plan for the nine month period ended September 30, 2007 was 420,571. The weighted average fair value of the employees purchase rights was $23.94 and was estimated using the Black-Scholes model with the following assumptions:

	2007
Dividend expense yield	0.2%
Expected life	3 months
Expected volatility	23.9%
Risk-free interest rate	5.1%

Authorized Preferred Stock and Preferred Stock Purchase Rights Plan

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

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

NOTE 9 Commitments and Contingencies

We offer a one-year limited warranty on most hardware products, which is included in the sales price of many of our products. Provision is made for estimated future warranty costs at the time of sale pursuant to SFAS 5, *Accounting for Contingencies*, for the estimated costs that may be incurred under the basic limited warranty. Our estimate is based on historical experience and product sales during this period.

The warranty reserve for the nine-month periods ended September 30, 2007 and 2006, respectively, was as follows (in thousands):

	Nine Months Ended September 30, (unaudited)	
	2007	2006
Balance at the beginning of the period	$ 867	$ 915
Accruals for warranties issued during the period	1,206	1,190
Settlements made (in cash or in kind) during the period	(1,323)	(1,190)
Balance at the end of the period	$ 750	$ 915

As of September 30, 2007, we have outstanding guarantees for payment of foreign operating leases, customs and foreign grants totaling approximately $4.3 million.

As of September 30, 2007, we have non-cancelable purchase commitments with various suppliers of customized inventory and inventory components totaling approximately $6.8 million over the next twelve months.

NOTE 10 Segment Information

While we sell our products to many different markets, management has chosen to organize the Company by geographic areas, and as a result has determined that we have one operating segment. Substantially all of the depreciation and amortization is recorded in the Americas. Net sales, operating income, identifiable assets and interest income ,classified by the major geographic areas in which we operate, are as follows (in thousands):

	Three Months Ended September 30, (unaudited)		Nine Months Ended September 30, (unaudited)	
	2007	2006	2007	2006
Net sales:				
Americas:				
Unaffiliated customer sales	$ 86,271	$ 80,637	$ 248,127	$ 233,841
Geographic transfers	25,033	30,833	85,066	92,642
	$ 111,304	$ 111,470	$ 333,193	$ 326,483
Europe:				
Unaffiliated customer sales	$ 52,041	$ 43,488	$ 160,070	$ 135,963
Geographic transfers	41,184	36,914	117,781	113,546
	$ 93,225	$ 80,402	$ 277,851	$ 249,509
Asia Pacific:				
Unaffiliated customer sales	$ 46,114	$ 39,954	$ 127,368	$ 109,150
Eliminations	(66,217)	(67,747)	(202,847)	(206,188)
	$ 184,426	$ 164,079	$ 535,565	$ 478,954

	Three Months Ended September 30, (unaudited)		Nine Months Ended September 30, (unaudited)	
	2007	2006	2007	2006
Operating income:				
Americas	$ 20,129	$ 18,339	$ 57,039	$ 49,041
Europe	19,847	15,956	61,124	52,330
Asia Pacific	16,471	15,814	44,346	40,854
Unallocated:				
Research and development expenses	(31,891)	(27,742)	(91,652)	(83,121)
	$ 24,556	$ 22,367	$ 70,857	$ 59,104

	Nine Months Ended September 30, (unaudited)	
	2007	2006
Interest income:		

	Nine Months Ended September 30,	
Americas	$ 3,854	$ 4,761
Europe	3,071	110
Asia Pacific	131	27
	$ 7,056	$ 4,898

	September 30, 2007	December 31, 2006
	(unaudited)	
Identifiable assets:		
Americas	$ 412,633	$ 476,027
Europe	281,693	188,388
Asia Pacific	79,064	56,805
	$ 773,390	$ 721,220

Total sales outside the United States for the three months and nine months ended September 30, 2007 were $106.4 million and $316.8 million, respectively, and for the three months and nine months ended September 30, 2006 were $90.1 million and $267.4 million, respectively.

NOTE 11 Recent Issued Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) 48, *Accounting for Uncertainty in Income Taxes an interpretation of Statement of Financial Accounting Standards (SFAS) 109*. This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. This interpretation is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 on January 1, 2007, as required. The adoption of FIN 48 did not have a significant impact on our financial position or results of operations. (See Note 6 of Notes to Consolidated Financial Statements).

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. This standard defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America, and expands disclosure about fair value measurements. This pronouncement applies under other accounting standards that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurement. This statement is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We will be required to adopt SFAS 157 in the first quarter of fiscal year 2008. We are currently evaluating the requirements of SFAS 157 and have not yet determined the impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement 115.* This standard permits an entity to measure many financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis. This statement is effective for fiscal years beginning after November 15, 2007. We will be required to adopt SFAS 159 in the first quarter of fiscal year 2008. We are currently evaluating the requirements of SFAS 159 and have not yet determined the impact on our consolidated financial statements.

NOTE 12 Litigation

We filed a patent infringement action on January 25, 2001 in the U.S. District Court, Eastern District of Texas (Marshall Division) claiming that The MathWorks, Inc. (MathWorks) infringed certain of our U.S. patents. On January 30, 2003, a jury found infringement by MathWorks of three of the patents involved and awarded us specified damages. On June 23, 2003, the District Court entered final judgment in favor of us and entered an injunction against MathWorks sale of its Simulink and related products and stayed the injunction pending appeal. Upon appeal, the judgment and the injunction were affirmed by the U.S. Court of Appeals for the Federal Circuit (September 3, 2004). Subsequently the stay of injunction was lifted by the District Court. In November 2004, the final judgment amount of $7.4 million which had been held in escrow pending appeal was released to us.

An action was filed by MathWorks against us on September 22, 2004, in the U.S. District Court, Eastern District of Texas (Marshall Division), claiming that on that day MathWorks had released modified versions of its Simulink and related products, and seeking a declaratory judgment that the modified products do not infringe the three patents adjudged infringed in the District Court s decision of June 23, 2003, (and affirmed by the Court of Appeals on September 3, 2004). On November 2, 2004, MathWorks served the complaint on us. We filed an answer to MathWorks declaratory judgment complaint, denying MathWorks claims of non-infringement and alleging our own affirmative defenses. On January 5, 2005, the Court denied a contempt motion by us to enjoin the modified Simulink products under the injunction in effect from the first case. On January 7, 2005, we amended our answer to include counterclaims that MathWorks modified products are infringing three of our patents, and requested unspecified damages and an injunction. MathWorks filed its reply to our counterclaims on February 7, 2005, denying the counterclaims and alleging affirmative defenses. On March 2, 2005, we filed a notice of appeal regarding the Court s denial of the contempt motion. On March 15, 2005, the Court stayed MathWorks declaratory judgment action, pending a decision on the appeal by the Court of Appeals for the Federal Circuit. On February 9, 2006, the Court of Appeals for the Federal Circuit affirmed the District Court s January 2005 order. On November 22, 2006, the District Court lifted the stay. The case schedule has yet to be set in this action. During the fourth quarter of 2004, we accrued $4 million related to our probable loss from this contingency, which consists entirely of anticipated patent defense costs that are probable of being incurred. In the fourth quarter of 2006, we accrued an additional $600,000 related to this contingency. There were not any charges against this accrual during the third quarter of 2007. We have charged a total of $611,000 against this accrual through September 30, 2007.

NOTE 13 Subsequent Event

On October 24, 2007, the Company s Board of Directors declared a quarterly cash dividend of $0.10 per common share, payable on December 3, 2007 to shareholders of record on November 12, 2007.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Any statements contained herein regarding our future financial performance or operations (including, without limitation, statements to the effect that we believe, expect, plan, may, will, project, continue, or estima variations thereof or comparable terminology or the negative thereof) should be considered forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of a number of important factors including those set forth under the heading Risk Factors beginning on page 21, and the discussion below. Readers are also encouraged to refer to the documents regularly filed by us with the Securities and Exchange Commission, including our Annual Report on Form 10-K for further discussion of our business and the risks attendant thereto.

Overview

National Instruments designs, develops, manufactures and markets instrumentation and automation software and hardware for general commercial, industrial and scientific applications. We offer hundreds of products used to create virtual instrumentation systems for measurement and automation. We have identified a large and diverse market for design, control and test applications. Our products are used in a variety of applications from research and development to production testing, monitoring and industrial control. We sell to a large number of customers in a wide variety of industries. No single customer accounted for more than 4% and 3% of our sales in the three and nine months ended September 30, 2007, respectively, or 3% of our sales in the years 2006, 2005 or 2004.

The key strategies that our management focuses on in running the business are the following:

Expanding our broad customer base:

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

Maintaining a high level of customer satisfaction:

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

Leveraging external and internal technology:

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

We sell into the test and measurement (T&M) and the industrial automation (IA) industries and as such are subject to the economic and industry forces which drive those markets. It has been our experience that the performance of these industries and our performance is impacted by general trends in industrial production for the global economy and by the specific performance of certain vertical markets that are intensive consumers of measurement technologies. Examples of these markets are semiconductor capital equipment, telecom, defense, aerospace, automotive and others. In assessing our business, our management considers the trends in the Global Purchasing Managers Index (published by JP Morgan), global industrial production as well as industry reports on the specific vertical industries mentioned earlier.

We distribute our software and hardware products primarily through a direct sales organization. We also use independent distributors, OEMs, VARs, system integrators and consultants to market our products. We have sales offices in the United States and sales offices and distributors in key international markets. Sales outside of the Americas accounted for approximately 53% and 51% of our revenues in the three month periods ended September 30, 2007 and 2006, respectively. The vast majority of our foreign sales are denominated in the customers local currency, which exposes us to the effects of changes in foreign-currency exchange rates. We expect that a significant portion of our total revenues will continue to be derived from international sales. See Note 10 of Notes to Consolidated Financial Statements for details concerning the geographic breakdown of our net sales, operating income, interest income, and identifiable assets.

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

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

We have been profitable in every year since 1990. However, there can be no assurance that our net sales will grow or that we will remain profitable in future periods. As a result, we believe historical results of operations should not be relied upon as indications of future performance.

Results of Operations

The following table sets forth, for the periods indicated, the percentage of net sales represented by certain items reflected in our consolidated statements of income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
Net sales:				
Americas	46.8%	49.1%	46.3%	48.8%
Europe	28.2	26.5	29.9	28.4
Asia Pacific	25.0	24.4	23.8	22.8
Consolidated net sales	100.0	100.0	100.0	100.0
Cost of sales	25.1	25.9	24.7	26.1
Gross profit	74.9	74.1	75.3	73.9

	Three Months Ended September 30,		Nine Months Ended September 30,	
Operating expenses:				
Sales and marketing	35.8	35.6	36.4	36.0
Research and development	17.3	16.9	17.1	17.4
General and administrative	8.5	8.0	8.5	8.2
Total operating expenses	61.6	60.5	62.0	61.6
Operating income	13.3	13.6	13.2	12.3
Other income (expense):				
Interest income	1.4	1.2	1.3	1.1
Net foreign exchange gain	0.1	0.3	0.1	0.0
Other income, net	0.0	0.0	0.0	0.0
Income before income taxes	14.8	15.1	14.6	13.4
Provision for income taxes	3.1	3.7	3.2	3.3
Net income	11.7%	11.4%	11.4%	10.1%

Net Sales. Consolidated net sales increased by $20.3 million or 12.4% for the three months ended September 30, 2007 to $184.4 million from $164.1 million for the three months ended September 30, 2006, and increased $56.6 million or 11.8% to $535.6 million for the nine months ended September 30, 2007 from $479.0 million for the comparable period in the prior year. The increases in sales for the three and nine months ended September 30, 2007 were primarily attributable to the introduction of new and upgraded products, an increased market acceptance of our virtual instrumentation and graphical system design products, which constitutes the vast majority of our product portfolios, in all regions and the strengthening of the euro. This increase in sales was offset slightly by the decrease in sales of our instrument control products. Sales in the Americas in the third quarter of 2007 increased by 7% from the third quarter of 2006 and sales in the Americas for the nine months ended September 30, 2007 increased by 6% from the nine months ended September 30, 2006.

Sales outside of the Americas, as a percentage of consolidated sales for the quarter ended September 30, 2007, increased to 53.2% from 50.9% over the comparable 2006 period as a result of a stronger euro and faster sales growth outside of the Americas. Sales outside of the Americas as a percentage of consolidated sales for the nine months ended September 30, 2007 increased to 53.7% from 51.2% over the comparable 2006 period due to a stronger euro and faster sales growth outside of the Americas. Compared to the corresponding periods in 2006, our European sales increased by 20% to $52.0 million for the three months ended September 30, 2007 and increased by 18% to $160.0 million for the nine months ended September 30, 2007. Sales in Asia Pacific increased by 15% to $46.1 million for the three months ended September 30, 2007 compared to the same period in 2006 and increased 17% to $127.4 million for the nine months ended September 30, 2007 compared to the same period in 2006. We expect sales outside of the Americas to continue to represent a significant portion of our revenue. We intend to continue to expand our international operations by increasing our presence in existing markets, adding a presence in some new geographical markets and continuing the use of distributors to sell our products in some countries.

Almost all sales made by our direct sales offices in Europe and Asia Pacific are denominated in local currencies, and accordingly, the U.S. dollar equivalent of these sales is affected by changes in foreign currency exchange rates. Between the third quarter of 2006 and the third quarter of 2007, net of hedging results, the change in exchange rates had the effect of increasing our consolidated sales by 2.3%; increasing European sales by 6.5% and increasing sales in Asia Pacific by 1.3%. For 2007 year-to-date sales, net of hedging results, the change in exchange rates had the effect of increasing our consolidated sales by 3%. Since most of our international operating expenses are also incurred in local currencies, the change in exchange rates had the effect of increasing operating expenses by $1.5 million, or 1.4%, for the three months ended September 30, 2007 and increasing operating expenses by $5.1 million, or 1.6%, for the nine months ended September 30, 2007 compared to the comparable prior year periods.

Gross Profit. As a percentage of sales, gross profit increased to 74.9% for the third quarter of 2007 from 74.1% for the third quarter of 2006 and increased to 75.3% for the first nine months of 2007 from 73.9% for the comparable period a year ago. The higher margin in the third quarter of 2007 compared to the 2006 period is attributable to the net impact of favorable foreign currency exchange rates, the favorable impact of higher sales volume, as well as improved product margins resulting from both price increases and cost reductions on certain products, offset by the unfavorable impact of increased stock-based compensation, and the unfavorable impact of costs incurred to transition our Austin, Texas distribution activities to Hungary. The higher margin in the first nine months of 2007 compared to the comparable prior year period is attributable to favorable foreign currency exchange rates, the favorable impact of higher sales volume and improved product margins resulting from both price increases and cost reductions on certain products offset by the unfavorable impact of increased stock-based compensation. There can be no assurance that we will maintain our historical margins. We believe our current manufacturing capacity is adequate to meet current needs.

Sales and Marketing. Sales and marketing expenses for the third quarter of 2007 increased to $66.1 million, a 13.1% increase, compared to the third quarter of 2006 and increased 13.1% to $195.0 million for the first nine months of 2007 from the comparable 2006 period. The increases in sales and marketing expenses in the three months and in the nine months ended September 30, 2007 from the comparable prior year periods were attributable to increases in sales and marketing personnel costs due to the increase in sales and marketing personnel as well as increases in stock-based compensation and the increase in variable compensation from higher sales volume. As a percentage of net sales, sales and marketing expenses were 35.8% and 35.6% for the three months ended September 30, 2007 and 2006, respectively, and 36.4% and 36.0% for the nine months ended September 30, 2007 and 2006, respectively. We expect sales and marketing expenses in future periods to increase in absolute dollars, and to fluctuate as a percentage of sales based on recruiting, marketing and advertising campaign costs associated with major new product releases and entry into new market areas, investment in web sales and marketing efforts, increasing product demonstration costs and the timing of domestic and international conferences and trade shows.

Research and Development. Research and development expenses increased to $31.9 million for the three months ended September 30, 2007, a 15.0% increase, compared to $27.7 million for the three months ended September 30, 2006, and increased 10.3% to $91.7 million for the nine months ended September 30, 2007 from the comparable 2006 period. The increases in research and development costs in the three months and nine month periods ended September 30, 2007 compared to the comparable prior year periods were primarily due to increases in personnel costs from the hiring of additional product development engineers as well as increases in stock-based compensation. We plan to continue making a significant investment in research and development in order to remain competitive and support revenue growth.

We capitalize software development costs in accordance with Statements of Financial Accounting Standards (SFAS) 86, *Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*. We amortize such costs over the related product s estimated economic useful life, generally three years, beginning when a product becomes available for general release. Software amortization expense included in cost of goods sold totaled $2.2 million and $2.0 million for the three months ended September 30, 2007 and 2006, respectively, and $6.5 million and $7.1 million during the nine months ended September 30, 2007 and 2006, respectively. Internally developed software costs capitalized were $1.7 million and $2.3 million for the three months ended September 30, 2007 and 2006, respectively, and $7.7 million and $6.3 million for the first nine months of 2007 and 2006, respectively.

General and Administrative. General and administrative expenses increased to $15.6 million for the three months ended September 30, 2007, a 19.9% increase, compared to $13.1 million for the three months ended September 30, 2006, and increased 15.6% to $45.6 million for the nine months ended September 30, 2007 from the comparable 2006 period. As a percentage of net sales, general and administrative expenses increased to 8.5% for the three months ended September 30, 2007 from 8.0% for the third quarter of 2006. During the first nine months of 2007, general and administrative expenses increased as a percentage of sales to 8.5% from 8.2% for the comparable prior year period. The increases in general and administrative expenses for the three months and nine months ended September 30, 2007 from comparable prior year periods were primarily attributable to increases in personnel costs due to the increase in general and administrative personnel and increases in stock-based compensation as well as severance and lease termination costs incurred as a result of the restructuring of our Dublin, Ireland operations and increased patent litigation costs. We expect that general and administrative expenses in future periods will fluctuate in absolute amounts and as a percentage of revenue.

Interest Income. Interest income in the third quarter of 2007 increased to $2.6 million from $2.0 million in the third quarter of 2006, and increased to $7.1 million for the first nine months of 2007 from $4.9 million for the comparable 2006 period. The increases in interest income for the quarter and nine months ended September 30, 2007 were primarily due to increased invested funds. The primary source of interest income is from the investment of our cash and short-term investments. Net cash provided by operating activities totaled $113.6 million and $71.4 million in the nine month periods ended September 30, 2007 and 2006, respectively.

Net Foreign Exchange Gain (Loss). We experienced net foreign exchange gains of $98,000 in the third quarter of 2007 compared to gains of $432,000 in the third quarter of 2006. Net foreign exchange gains of $628,000 were recognized for the first nine months of 2007 compared to gains of $195,000 for the first nine months of 2006. These results are attributable to movements between the U.S. dollar and the local currencies in countries in which our sales subsidiaries are located. We recognize the local currency as the functional currency in virtually all of our international subsidiaries.

We utilize foreign currency forward contracts to hedge a majority of our foreign currency-denominated receivables in order to reduce our exposure to significant foreign currency fluctuations. We typically limit the duration of our receivables foreign currency forward contracts to approximately 90 days.

We also utilize foreign currency forward contracts and have in the past and may in the future use foreign currency purchased option contracts in order to reduce our exposure to fluctuations in future foreign currency cash flows. We purchase these contracts for up to 100% of our forecasted exposures in selected currencies (primarily the euro, yen and pound sterling) and limit the duration of these contracts to 40 months or less. Our foreign currency purchased option contracts are purchased at-the-money or out-of-the-money. As a result, our hedging activities only partially address our risks in foreign currency transactions, and there can be no assurance that this strategy will be successful. We do not invest in contracts for speculative purposes. Our hedging strategy reduced our foreign exchange gains by $960,000 and $1.2 million in the three months and nine months ended September 30, 2007, respectively, and reduced our foreign exchange losses by $443,000 in the three months ended September 30, 2006, and reduced our foreign exchange gains by $633,000 in the nine months ended September 30, 2006.

Provision for Income Taxes. Our provision for income taxes reflects an effective tax rate of 21% and 22% for the three and nine months ended September 30, 2007, respectively, and 25% for the three and nine months ended September 30, 2006. For the nine months ended September 30, 2006, our effective tax rate was lower than the U.S. federal statutory rate of 35% primarily as a result of the extraterritorial income exclusion, tax-exempt interest and reduced tax rates in certain foreign jurisdictions. For the nine months ended September 30, 2007, our effective tax rate is lower than the U.S. federal statutory rate of 35% primarily as a result of the research tax credit, tax exempt interest and reduced tax rates in certain foreign jurisdictions. The decreases in our tax rate in the three and nine months ended September 30, 2007 from the comparable prior year periods are due to increased profits in foreign jurisdictions with the reduced income tax rates.

Liquidity and Capital Resources

We currently finance our operations and capital expenditures through cash flow from operations. At September 30, 2007, we had working capital of approximately $398.5 million compared to $377.6 million at December 31, 2006. The increase in working capital was partially due to an increase in prepaid expenses and other current assets that was primarily the result of annual maintenance and insurance renewals. Net cash provided by operating activities for the nine month periods ended September 30, 2007 and 2006 totaled $113.6 million and $71.4 million, respectively.

Accounts receivable increased to $121.3 million at September 30, 2007 from $117.2 million at December 31, 2006. Days sales outstanding remained flat at 59 at September 30, 2007 compared to September 30, 2006. Consolidated inventory balances increased to $77.3 million at September 30, 2007 from $77.1 million at December 31, 2006. Inventory turns increased to 2.4 for the quarter ended September 30, 2007 from turns of 2.1 for the quarter ended September 30, 2006. Cash used in the first nine months of 2007 for the purchase of property and equipment totaled $18.1 million, for the capitalization of internally developed software costs totaled $7.7 million, and for additions to other intangibles totaled $5.0 million. Cash used in the first nine months of 2006 for the purchase of property and equipment totaled $10.8 million, for the capitalization of internally developed software costs totaled $6.3 million, and for additions to other intangibles totaled $1.7 million.

Cash provided by the issuance of common stock totaled $27.5 million and $22.8 million for the first nine months of 2007 and 2006, respectively. The issuance of common stock was to employees under our Employee Stock Purchase Plan, our 1994 Incentive Plan, and our 2005 Incentive Plan. Cash used for the repurchase of common stock totaled $68.0 million and $16.5 million for the first nine months of 2007 and 2006, respectively. Cash used for the payment of dividends totaled $19.1 million and $14.3 million for the first nine months of 2007 and 2006, respectively.

We currently expect to fund expenditures for capital requirements as well as liquidity needs created by changes in working capital from a combination of available cash and short-term investment balances and internally generated funds. As of each of September 30, 2007 and 2006, we had no debt outstanding. We believe that our cash flow from operations and existing cash balances and short-term investments will be sufficient to meet our cash requirements for at least the next twelve months. Cash requirements for periods beyond the next twelve months will depend on our profitability, our ability to manage working capital requirements and our rate of growth.

Financial Risk Management

Our international sales are subject to inherent risks, including fluctuations in local economies; difficulties in staffing and managing foreign operations; greater difficulty in accounts receivable collection; costs and risks of localizing products for foreign countries; unexpected changes in regulatory requirements, tariffs and other trade barriers; difficulties in the repatriation of earnings and burdens of complying with a wide variety of foreign laws. The vast majority of our sales outside of North America are denominated in local currencies, and accordingly, we are subject to the risks associated with fluctuations in currency rates. In particular, increases in the value of the dollar against foreign currencies decrease the U.S. dollar value of foreign sales requiring that we either increase our price in the local currency, which could render our product prices noncompetitive, or suffer reduced revenues and gross margins as measured in U.S. dollars. These dynamics have adversely affected our revenue growth in international markets in previous years. Our foreign currency hedging program includes both foreign currency forward and purchased option contracts to reduce the effect of exchange rate fluctuations. However, our hedging program will not eliminate all of our foreign exchange risks. (See Net Foreign Exchange Gain (Loss)).

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. While we adjust for excess and obsolete inventories and we monitor the valuation of our inventories, there can be no assurance that our valuation adjustments will be sufficient.

Off-Balance Sheet Arrangements. We have no debt or off-balance sheet debt. As of September 30, 2007, we have contractual purchase commitments with various suppliers of general components and customized inventory components of approximately $6.8 million. As of September 30, 2007, we have outstanding guarantees for payment of foreign operating leases, customs and foreign grants totaling approximately $4.3 million. (See Note 9 of Notes to Consolidated Financial Statements). As of September 30, 2007, we did not have any relationships with any unconsolidated entities or financial partnerships, such as entities often referred to as structured finance entities, which would have been

established for the purpose of facilitating off-balance sheet arrangements. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we were engaged in such relationships.

Market Risk

We are exposed to a variety of risks, including foreign currency fluctuations and changes in the market value of our investments. In the normal course of business, we employ established policies and procedures to manage our exposure to fluctuations in foreign currency values and changes in the market value of our investments.

Foreign Currency Hedging Activities. Our objective in managing our exposure to foreign currency exchange rate fluctuations is to reduce the impact of adverse fluctuations in such exchange rates on our earnings and cash flow. Accordingly, we utilize purchased foreign currency option contracts and forward contracts to hedge our exposure on anticipated transactions and firm commitments. The principal currencies hedged are the euro, British pound and Japanese yen. We monitor our foreign exchange exposures regularly to ensure the overall effectiveness of our foreign currency hedge positions. However, there can be no assurance that our foreign currency hedging activities will substantially offset the impact of fluctuations in currency exchange rates on our results of operations and financial position. Based on the foreign exchange instruments outstanding at September 30, 2007, an adverse change (defined as 20% in the Asian currencies and 10% in all other currencies) in exchange rates would result in a decline in the aggregate fair market value of all of our instruments outstanding of approximately $10.7 million. However, as we utilize foreign currency instruments for hedging anticipated and firmly committed transactions, we believe that a loss in fair value for those instruments will be substantially offset by increases in the value of the underlying exposure.

Short-term Investments. The fair value of our investments in marketable securities at September 30, 2007 was $92.6 million. Investments with maturities beyond one year are classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations. Our investment policy is to manage our investment portfolio to preserve principal and liquidity while maximizing the return on our investment portfolio through the full investment of available funds. We diversify our marketable securities portfolio by investing in multiple types of investment-grade securities. Our investment portfolio is primarily invested in securities with at least an investment grade rating to minimize interest rate and credit risk as well as to provide for an immediate source of funds. Based on our investment portfolio and interest rates at September 30, 2007, a 100 basis point increase or decrease in interest rates would result in a decrease or increase of approximately $463,000 in the fair value of our investment portfolio. Although changes in interest rates may affect the fair value of our investment portfolio and cause unrealized gains or losses, such gains or losses would not be realized unless the investments are sold.

Recent Issued Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) 48, *Accounting for Uncertainty in Income Taxes an interpretation of Statement of Financial Accounting Standards (SFAS) 109*. This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. This interpretation is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 on January 1, 2007, as required. The adoption of FIN 48 did not have a significant impact on our financial position or results of operations. (See Note 6 of Notes to Consolidated Financial Statements).

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. This standard defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America, and expands disclosure about fair value measurements. This pronouncement applies under other accounting standards that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurement. This statement is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We will be required to adopt SFAS 157 in the first quarter of fiscal year 2008. We are currently evaluating the requirements of SFAS 157 and have not yet determined the impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement 115.* This standard permits an entity to measure many financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis. This statement is effective for fiscal years beginning after November 15, 2007. We will be required to adopt SFAS 159 in the first quarter of fiscal year 2008. We are currently evaluating the requirements of SFAS 159 and have not yet determined the impact on our consolidated financial statements.

Item 3. ***Quantitative and Qualitative Disclosures About Market Risk***

Response to this item is included in Item 2 Management s Discussion and Analysis of Financial Conditions and Results of Operations Market Risk above.

Item 4. ***Controls and Procedures***

Our Chief Executive Officer and Chief Financial Officer, based on the evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended) required by paragraph (b) of Rule 13a-15 or Rule 15d-15, as of September 30, 2007, have concluded that our disclosure controls and procedures were effective to ensure the timely collection, evaluation and disclosure of information relating to us that would potentially be subject to disclosure under the Securities Exchange Act of 1934, as amended, and the rules and regulations promulgated thereunder. We continue to enhance our internal control over financial reporting by adding resources in key functional areas with the goal of monitoring our operations at the level of documentation, segregation of duties, and systems security necessary, as well as transactional control procedures required under the Auditing Standard No. 5 issued by the Public Company Accounting Oversight Board, which recently replaced Auditing Standard No. 2. We discuss and disclose these matters to the audit committee of our board of directors and to our auditors. During the quarter ended September 30, 2007, there was no change in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of the Rule 13a-15 or Rule 15d-15 that has materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We filed a patent infringement action on January 25, 2001 in the U.S. District Court, Eastern District of Texas (Marshall Division) claiming that The MathWorks, Inc. (MathWorks) infringed certain of our U.S. patents. On January 30, 2003, a jury found infringement by MathWorks of three of the patents involved and awarded us specified damages. On June 23, 2003, the District Court entered final judgment in favor of us and entered an injunction against MathWorks sale of its Simulink and related products and stayed the injunction pending appeal. Upon appeal, the judgment and the injunction were affirmed by the U.S. Court of Appeals for the Federal Circuit (September 3, 2004). Subsequently the stay of injunction was lifted by the District Court. In November 2004, the final judgment amount of $7.4 million which had been held in escrow pending appeal was released to us.

An action was filed by MathWorks against us on September 22, 2004, in the U.S. District Court, Eastern District of Texas (Marshall Division), claiming that on that day MathWorks had released modified versions of its Simulink and related products, and seeking a declaratory judgment that the modified products do not infringe the three patents adjudged infringed in the District Court s decision of June 23, 2003, (and affirmed by the Court of Appeals on September 3, 2004). On November 2, 2004, MathWorks served the complaint on us. We filed an answer to MathWorks declaratory judgment complaint, denying MathWorks claims of non-infringement and alleging our own affirmative defenses. On January 5, 2005, the Court denied a contempt motion by us to enjoin the modified Simulink products under the injunction in effect from the first case. On January 7, 2005, we amended our answer to include counterclaims that MathWorks modified products are infringing three of our patents, and requested unspecified damages and an injunction. MathWorks filed its reply to our counterclaims on February 7, 2005, denying the counterclaims and alleging affirmative defenses. On March 2, 2005, we filed a notice of appeal regarding the Court s denial of the contempt motion. On March 15, 2005, the Court stayed MathWorks declaratory judgment action, pending a decision on the appeal by the Court of Appeals for the Federal Circuit. On February 9, 2006, the Court of Appeals for the Federal Circuit affirmed the District Court s January 2005 order. On November 22, 2006, the District Court lifted its stay. The case schedule has yet to be set in this action. During the fourth quarter of 2004, we accrued $4 million related to our probable loss from this contingency, which consists entirely of anticipated patent defense costs that are probable of being incurred. In the fourth quarter of 2006, we accrued an additional $600,000 related to this contingency. There were not any charges against this accrual during the third quarter of 2007. We have charged a total of $611,000 against this accrual through September 30, 2007.

ITEM 1A. RISK FACTORS

U.S./Global Economic Change Will Impact Our Future Business. As has occurred in the past, the markets in which we do business could again experience the negative effects of a slowdown in the U.S., and/or Global economies. The worsening of the U.S. or Global economies could result in reduced purchasing and capital spending in any of our markets which could have a material adverse effect on our operating results. Our business could also be subject to or impacted by acts of terrorism and/or the effects that war or continued U.S. military action would have on the U.S. and/or Global economies. Our business could also be impacted by public health concerns, natural disasters, disruptions to public or commercial transportation systems, political instability or similar events which result in increased difficulty or higher costs for the export of products into affected regions, the import of components used in our products from affected regions, and/or the effects the event has on the economy in regions in which we do business.

We Have Established a Budget and Variations From Such Budget Will Affect Our Financial Results. We have established an operating budget for 2007. Our budget was established based on the estimated revenue from forecasted sales of our products which is based on economic conditions in the markets in which we do business as well as the timing and volume of our new products and the expected penetration of both new and existing products in the marketplace. Our spending for the remainder of the year could exceed our budget due to a number of factors, including:

- additional marketing costs for new product introductions and/or for conferences and tradeshows;
- increased costs from hiring more product development engineers or other personnel;
- additional costs related to acquisitions, if any;
- increased manufacturing costs resulting from component supply shortages and/or component price fluctuations; and/or,
- additional expenses related to intellectual property litigation.

Any future decreased demand for our products could result in decreased revenue and could require us to revise our budget and reduce expenditures. Exceeding our established operating budget or failing to reduce expenditures in response to any decrease in revenue could have a material adverse effect on our operating results.

We May Experience Component Shortages. As has occurred in the past and as may be expected to occur in the future, supply shortages of components used in our products, including sole source components, can result in significant additional costs and inefficiencies in manufacturing. If we are unsuccessful in resolving any such component shortages in a timely manner, we will experience a significant impact on the timing of revenue, a possible loss of revenue, and/or an increase in manufacturing costs, any of which would have a material adverse impact on our operating results.

Our Business is Dependent on Key Suppliers. Our manufacturing processes use large volumes of high-quality components and subassemblies supplied by outside sources. Several of these components are available through sole or limited sources. Sole-source components purchased include custom application-specific integrated circuits (ASICs), chassis and other components. We have in the past experienced delays and quality problems in connection with sole-source components, and there can be no assurance that these problems will not recur in the future. Accordingly, our failure to receive sole-source components from suppliers could result in a material adverse effect on our revenues and operating results.

Our Quarterly Results are Subject to Fluctuations Due to Various Factors. 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 mix of products sold;
- the availability and pricing of components from third parties (especially sole sources);
- pricing of our products;
- fluctuations in foreign currency exchange rates;
- the timing, cost or outcome of intellectual property litigation;
- the difficulty in maintaining margins, including the higher margins traditionally achieved in international sales; and,
- changes in pricing policies by us, our competitors or suppliers.

Specifically, if the local currencies in which we sell weaken against the U.S. dollar, and if the local sales prices cannot be raised due to competitive pressures, we will experience a deterioration of our gross and net profit margins. If the U.S. dollar strengthens in the future, it could have a material adverse effect on our gross and net profit margins.

As has occurred in the past and as may be expected to occur in the future, our new software products or new operating systems of third parties on which our products are based often contain bugs or errors that can result in reduced sales and/or cause our support costs to increase, either of which could have a material adverse impact on our operating results. Furthermore, we have significant revenues from customers in industries such as semiconductors, automated test equipment, telecommunications, aerospace, defense and automotive which are cyclical in nature. Downturns in these industries could have a material adverse effect on our operating results.

In recent years, our revenues have been characterized by seasonality, with revenues typically being relatively constant in the second and third quarters, growing in the fourth quarter and declining from the fourth quarter of the year to the first quarter of the following year. This historical trend may be affected in the future by the economic impact of larger orders as well as the timing of new product introductions and/or acquisitions, if any. We believe the seasonality of our revenue results from the international mix of our revenue and the variability of the budgeting and purchasing cycles of our customers throughout each international region. In addition, 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.

Our Success Depends on New Product Introductions and Market Acceptance of Our Products. The market for our products is characterized by rapid technological change, evolving industry standards, changes in customer needs and frequent new product introductions, and is therefore highly dependent upon timely product innovation. Our success is dependent on our ability to successfully develop and introduce new and enhanced products on a timely basis to replace declining revenues from older products, and on increasing penetration in domestic and international markets. In the past, we have experienced significant delays between the announcement and the commercial availability of new products. Any significant delay in releasing new products could have a material adverse effect on the ultimate success of a product and other related products and could impede continued sales of predecessor products, any of which could have a material adverse effect on our operating results. There can be no assurance that we will be able to introduce new products in accordance with announced release dates, that new products will achieve market acceptance or that any such acceptance will be sustained for any significant period. Failure of new products to achieve or sustain market acceptance could have a material adverse effect on our operating results. Moreover, there can be no assurance that our international sales will continue at existing levels or grow in accordance with our efforts to increase foreign market penetration.

We are Subject to Risks Associated with Our Web Site. We devote resources to maintain our Web site as a key marketing, sales and support tool and expect to continue to do so in the future. However, there can be no assurance that we will be successful in our attempt to leverage the Web to increase sales. We host our Web site internally. Any failure to successfully maintain our Web site or any significant downtime or outages affecting our Web site could have a significant adverse impact on our operating results.

We Operate in Intensely Competitive Markets. 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 expect to face further competition from new market entrants in the future. A key competitor is Agilent Technologies Inc. (Agilent). Agilent offers its own line of instrument controllers, and also offers hardware and software products that provide solutions that directly compete with our virtual instrumentation products. 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:

- new product introductions by competitors;
- product pricing;
- quality and performance;
- success in developing new products;
- adequate manufacturing capacity and supply of components and materials;
- efficiency of manufacturing operations;
- effectiveness of sales and marketing resources and strategies;
- strategic relationships with other suppliers;
- timing of our new product introductions;
- protection of our products by effective use of intellectual property laws;
- the outcome of any material intellectual property litigation;
- general market and economic conditions; and,
- government actions throughout the world.

There can be no assurance that we will be able to compete successfully in the future.

We Rely on Management Information Systems and any Disruptions in Such Systems Would Adversely Affect Us. We rely on two primary regional centers for our management information systems and on multiple systems in some branches not covered by our two regional centers. As with any information system, unforeseen issues may arise that could affect our ability to receive adequate, accurate and timely financial information, which in turn could inhibit effective and timely decisions. Furthermore, it is possible that one or both of our two regional information systems could experience a complete or partial shutdown. If such a shutdown occurred, it could impact our product shipments and revenues, as order processing and product distribution are heavily dependent on the integrated management information systems in each region. Accordingly, our operating results in such periods would be adversely impacted. We are working to maintain reliable regional management information systems to control costs and improve our ability to deliver our products in our markets worldwide. No assurances can be given that our efforts will be successful. The failure to receive adequate, accurate and timely financial information could inhibit our ability to make effective and timely decisions.

During the third quarter of 2007, we continued to devote resources to the implementation of systems to support the shipment of products from our manufacturing facility and warehouse in Hungary directly to customers worldwide, and to the continued development of our web offerings. There can be no assurance that we will not experience difficulties with these new systems. Difficulties with these new systems may interrupt our normal operations, including our ability to provide quotes, process orders, ship products, provide services and support to our customers, bill and track our customers, fulfill contractual obligations and otherwise run our business. Any disruption occurring with these systems may have a material adverse effect on our operating results. During the remainder of 2007, we plan to continue to devote significant resources to the implementation of systems that support shipment of product from our manufacturing facility and warehouse in Hungary directly to our customers worldwide, and to the continued development of our web offerings. Any failure to successfully implement these initiatives could have a material adverse effect on our operating results.

We are Subject to Risks Associated with Our Centralization of Inventory and Distribution. We are devoting considerable resources to centralizing our distribution to a limited number of shipping points. Currently, shipments to our European customers are sourced from our warehouse facility in Debrecen, Hungary. Shipments to almost all customers in the Americas were previously sourced from our warehouse in Austin, Texas. Since July 2007, our Austin distribution operation has been transferred to Debrecen, Hungary. Shipments to most of our customers in Asia are currently made out of local inventory managed by our branch operations in those countries. Our planned centralization of inventory and distribution to a limited number of shipping points is subject to inherent risks, including:

- burdens of complying with additional and/or more complex VAT and customs regulations;
-

severe concentration of inventory increasing the impact associated with fire or other natural disasters to customer order fulfillment;
- lack of complete visibility of centralized inventory due to multiple information systems; and
- potential for month-end cut-off error due to time zone differences between our information systems.

No assurance can be given that our efforts will be successful. Any difficulties with the centralization of distribution or delays in the implementation of the systems or processes to support this centralized distribution could result in interruption of our normal operation, including our ability to process orders and ship products to our customers. Any failure or delay in successfully centralizing our inventory in and distribution from our facility in Hungary could have a materially adverse effect on our operating results.

We are Subject to Various Risks Associated with International Operations and Foreign Economies. Our international sales are subject to inherent risks, including;

- fluctuations in local economies;
- fluctuations in foreign currencies relative to the U.S. dollar;
- difficulties in staffing and managing foreign operations;
- greater difficulty in accounts receivable collection;
- costs and risks of localizing products for foreign countries;
- unexpected changes in regulatory requirements;
- tariffs and other trade barriers;
- difficulties in the repatriation of earnings; and,
- the burdens of complying with a wide variety of foreign laws.

In many foreign countries, particularly in those with developing economies, it is common to engage in business practices that are prohibited by United States regulations applicable to us such as the Foreign Corrupt Practices Act. Although we implement policies and procedures designed to ensure compliance with these laws, there can be no assurance that all of our employees, contractors and agents, including those based in or from countries where practices which violate such United States laws may be customary, will not take actions in violation of our policies. Any violation of foreign or United States laws by our employees, contractors or agents, even if such violation is prohibited by our policies, could have a material adverse effect on our business. We must also comply with various import and export regulations. The application of these various regulations depends on the classification of our products which can change over time as such regulations are modified or interpreted. As a result, even if we are currently in compliance with applicable regulations, there can be no assurance that we will not have to incur additional cost or take additional compliance actions in the future. Failure to comply with these regulations could result in fines and/or termination of import and export privileges, which could have a material adverse effect on our operating results. Additionally, the regulatory environment in some countries is very restrictive as their governments try to protect their local economy and value of their local currency against the U.S. dollar. Sales made by our international direct sales offices are denominated in local currencies, and accordingly, the U.S. dollar equivalent of these sales is affected by changes in the foreign currency exchange rates. Net of hedging results, the change in exchange rates had the effect of increasing our consolidated sales by 3% in the third quarter of 2007 compared to the third quarter of 2006. Since most of our international operating expenses are also incurred in local currencies, the change in exchange rates had the effect of increasing our operating expenses by $1.5 million for the quarter ended September 30, 2007 compared to the comparable prior year period. If the U.S. dollar weakens in the future, it could result in our having to reduce prices locally in order for our products to remain competitive in the local marketplace. If the U.S. dollar strengthens in the future, and we are unable to successfully raise our international selling prices, it could have a material adverse effect on our operating results.

A Substantial Majority of Our Manufacturing Capacity is Located in Hungary. Our Hungarian manufacturing facility sources a substantial majority of our sales. Currently, we are continuing to develop and implement information systems to support the operation of this facility. In the third quarter of 2007, we continued to implement systems and processes that support the direct shipment of product orders to our customers worldwide from our manufacturing facility in Hungary and will continue to do so over the foreseeable future. In order to better insure timely shipment of products to our customers we will maintain the vast majority of our inventory at our Hungary manufacturing facility. In addition to being subject to the risks of maintaining such a concentrated global inventory, this facility and its operation are also subject to risks associated with doing business internationally, including:

- difficulty in managing manufacturing operations in a foreign country;
- difficulty in achieving or maintaining product quality;
- interruption to transportation flows for delivery of components to us and finished goods to our customers, and
- changes in the country's political or economical conditions.

No assurance can be given that our efforts will be successful. Accordingly, a failure to deal with these factors could result in interruption in the facility s operation or delays in expanding its capacity, either of which could have a material adverse effect on our operating results.

Our Income Tax Rate is Affected by Tax Benefits in Hungary. As a result of certain foreign investment incentives available under Hungarian law, the profit from our Hungarian operation is currently subject to a reduced income tax rate. These benefits may not be available in the future due to changes in Hungary s political condition and/or tax laws. The reduction or elimination of these foreign investment incentives would result in the reduction or elimination of certain tax benefits thereby increasing our future effective income tax rate, which could have a material adverse effect on our operating results.

We received a substantial income tax benefit from the extraterritorial income exemption (ETI) under U.S. law. The ETI rules provided that a percentage of the profits from products and intangibles exported from the U.S. were exempt from U.S. tax. Effective December 31, 2006, this benefit is no longer available as the ETI was repealed by the American Jobs Creation Act of 2004. The repeal of the ETI has increased our effective income tax rate. However, the effect of the repeal of the ETI has been offset by the effects of the increased benefit from the deduction for income from qualified domestic production activities and increased profits in certain foreign jurisdictions with reduced income tax rates.

Our Product Revenues are Dependent on Certain Industries. Sales of our products are dependent on customers in certain industries, particularly the telecommunications, semiconductor, automotive, automated test equipment, defense and aerospace industries. As experienced in the past, and as may be expected to occur in the future, downturns characterized by diminished product demand in any one or more of these industries could result in decreased sales, which could have a material adverse effect on our operating results.

Our Reported Financial Results May be Adversely Affected by Changes in Accounting Principles Generally Accepted in the United States. We prepare our financial statements in conformity with accounting principles generally accepted in the U.S. These accounting principles are subject to interpretation by the Financial Accounting Standards Board, the American Institute of Certified Public Accountants, the Securities and Exchange Commission and various bodies formed to interpret and create appropriate accounting policies. A change in these policies or interpretations could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change. For example, beginning in the first quarter of fiscal 2006, with the adoption of SFAS 123(R), we now record a charge to earnings for employee stock option grants for all stock options unvested at December 31, 2005. This accounting pronouncement has had a material negative impact on our financial results. Technology companies generally, and our company specifically, have in the past relied on stock options as a major component of our employee compensation packages. Because we are required to expense options, we have changed our equity compensation program to no longer grant options but instead grant restricted stock units. Furthermore, because we are required to expense options, we may be less likely to sustain profitability in the future.

Our Business Depends on Our Proprietary Rights and We are Subject to Intellectual Property Litigation. Our success depends on our ability to obtain and maintain patents and other proprietary rights relative to the technologies used in our principal products. Despite our efforts to protect our proprietary rights, unauthorized parties may have in the past infringed or violated certain of our intellectual property rights. We from time to time engage in litigation to protect our intellectual property rights. In monitoring and policing our intellectual property rights, we have been and may be required to spend significant resources. We from time to time may be notified that we are infringing certain patent or intellectual property rights of others. There can be no assurance that any existing intellectual property litigation or any intellectual property litigation initiated in the future, will not cause significant litigation expense, liability, injunction against some of our products, and a diversion of management s attention, any of which may have a material adverse effect on our operating results.

Compliance With Sections 302 and 404 of the Sarbanes-Oxley Act of 2002 is Costly and Challenging. As required by Section 302 of the Sarbanes-Oxley Act of 2002, this Form 10-Q contains management s certification of adequate disclosure controls and procedures as of September 30, 2007. Our most recent report on Form 10-K contained a report by our management on our internal control over financial reporting including an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2006. Our most recent report on Form 10-K also contained an attestation and report by our auditors with respect to management s assessment of the effectiveness of internal control over financial reporting under Section 404. While these assessments and reports did not reveal any material weaknesses in our internal control over financial reporting, compliance with Sections 302 and 404 is required for each future fiscal year end. We expect that the ongoing compliance with Sections 302 and 404 will continue to be both very costly and very challenging and there can be no assurance that material weaknesses will not be identified in future periods. Any adverse results from such ongoing compliance efforts could result in a loss of investor confidence in our financial reports and have an adverse effect on our stock price.

Our Business Depends on the Continued Service of Key Management and Technical Personnel. Our success depends upon the continued contributions of our key management, sales, marketing, research and development and operational personnel, including Dr. Truchard, our Chairman and Chief Executive Officer, and other members of senior management and key technical personnel. We have no agreements providing for the employment of any of our key employees for any fixed term and our key employees may voluntarily terminate their employment with us at any time. The loss of the services of one or more of our key employees in the future could have a material adverse effect on our operating results. We also believe our future success will depend upon our ability to attract and retain additional highly skilled management, technical, marketing, research and development, and operational personnel with experience in managing large and rapidly changing companies, as well as training, motivating and supervising employees. As a result of the impact that the adoption of SFAS 123R in our first quarter of 2006 has had on our results of operations, we have changed our equity compensation program. We now grant fewer equity instruments and the type of equity instrument is restricted stock units rather than stock options, which may make it more difficult for us to attract or retain qualified management and technical personnel, which could have an adverse effect on our operating results. In addition, the recruiting environment for software engineering, sales and other technical professionals is very competitive. Competition for qualified software engineers is particularly intense and is likely to result in increased personnel costs. Our failure to attract or retain qualified software engineers could have an adverse effect on our operating results. We also recruit and employ foreign nationals to achieve our hiring goals primarily for engineering and software positions. There can be no guarantee that we will continue to be able to recruit foreign nationals at the current rate. There can be no assurance that we will be successful in retaining our existing key personnel or attracting and retaining additional key personnel. Failure to attract and retain a sufficient number of our key personnel could have a material adverse effect on our operating results.

Our Manufacturing Operations are Subject to a Variety of Environmental Regulations and Costs. We must comply with many different governmental regulations related to the use, storage, discharge and disposal of toxic, volatile or otherwise hazardous chemicals used in our manufacturing operations in the U.S. and in Hungary. Although we believe that our activities conform to presently applicable environmental regulations, our failure to comply with present or future regulations could result in the imposition of fines, suspension of production or a cessation of operations. Any such environmental regulations could require us to acquire costly equipment or to incur other significant expenses to comply with such regulations. Any failure by us to control the use of or adequately restrict the discharge of hazardous substances could subject us to future liabilities.

Our Acquisitions are Subject to a Number of Related Costs and Challenges. We have from time to time acquired, and may in the future acquire, 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 may 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 two 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. The inability of our management to successfully integrate any future acquisition could harm our business. Some of the existing products previously sold by some of the entities we have acquired are of 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 transaction.

Provisions in Our Charter Documents and Delaware Law and Our Stockholder Rights Plan May Delay or Prevent an Acquisition of Us. Our certificate of incorporation and bylaws and Delaware law contain provisions that could make it more difficult for a third party to acquire us without the consent of our Board of Directors. These provisions include a classified Board of Directors, prohibition of stockholder action by written consent, prohibition of stockholders to call special meetings and the requirement that the holders of at least 80% of our shares approve any business combination not otherwise approved by two-thirds of the Board of Directors. Delaware law also imposes some restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock. In addition, our Board of Directors has the right to issue preferred stock without stockholder approval, which could be used to dilute the stock ownership of a potential hostile acquirer. Our Board of Directors adopted a new stockholders rights plan on January 21, 2004, pursuant to which we declared a dividend of one right for each share of our common stock outstanding as of May 10, 2004. This rights plan replaced a similar rights plan that had been in effect since our initial public offering in 1995. Unless redeemed by us prior to the time the rights are exercised, upon the occurrence of certain events, the rights will entitle the holders to receive upon exercise thereof shares of our preferred stock, or shares of an acquiring entity, having a value equal to twice the then-current exercise price of the right. The issuance of the rights could have the effect of delaying or preventing a change of control of us.

We Are Subject to the Risk of Product Liability Claims. Our products are designed to provide information upon which users may rely. Our products are also used in real time applications requiring extremely rapid and continuous processing and constant feedback. Such applications give rise to the risk that failure or interruption of the system or application could result in economic damage or bodily harm. We attempt to assure the quality and accuracy of the processes contained in our products, and to limit our product liability exposure through contractual limitations on liability, limited warranties, express disclaimers and warnings as well as disclaimers contained in our shrink wrap license agreements with end-users. If our products contain errors that produce incorrect results on which users rely, or cause failure or interruption of systems or processes, customer acceptance of our products could be adversely affected. Further, we could be subject to liability claims that could have a material adverse effect on our operating results or financial position. Although we maintain liability insurance for product liability matters, there can be no assurance that such insurance or the contractual limitations used by us to limit our liability will be sufficient to cover or limit any claims which may occur.

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

The following table provides information as of September 30, 2007 with respect to the shares of common stock repurchased by National Instruments during the third quarter of 2007.

Period	Total number of shares	Average price paid per share	Total number of shares purchased as part of a publicly announced plan or program	Maximum number of shares that may yet be purchased under the plan or program
July 1, 2007 to July 31, 2007		$		3,000,000
August 1, 2007 to August 31, 2007				3,000,000
				3,000,000

Period	Total number of shares	Average price paid per share	Total number of shares purchased as part of a publicly announced plan or program	Maximum number of shares that may yet be purchased under the plan or program
September 1, 2007 to September 30, 2007				
Total		$		

For the past several years, we have maintained various stock repurchase programs. In July 2007, our board of directors approved a new share repurchase plan that increased the aggregate number of shares of common stock that we are authorized to repurchase from 639,270 to 3.0 million. Our repurchase plan does not have an expiration date.

ITEM 5. OTHER INFORMATION

From time to time our directors, executive officers and other insiders may adopt stock trading plans pursuant to Rule 10b5-1(c) promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Jeffrey L. Kodosky and James J. Truchard have made periodic sales of our stock pursuant to such plans.

ITEM 6. EXHIBITS

3.1(2)	Certificate of Incorporation, as amended, of the Company.
3.2(2)	Amended and Restated Bylaws of the Company.
3.3(4)	Certificate of Designation of Rights, Preferences and Privileges of Series A Participating Preferred Stock of the Company.
4.1(1)	Specimen of Common Stock certificate of the Company.
4.2(3)	Rights Agreement dated as of January 21, 2004, between the Company and EquiServe Trust Company, N.A.
10.1(1)	Form of Indemnification Agreement.
10.2(5)	1994 Incentive Plan, as amended.*
10.3(11)	1994 Employee Stock Purchase Plan, as amended.*
10.4(6)	Long-Term Incentive Program.*
10.5(7)	2005 Incentive Plan.*
10.6(8)	National Instruments Corporation's Annual Incentive Program.*
10.7(9)	2007 Annual Incentive Program Goals and Awards for the Named Executive Officers.*
10.8(10)	Form of Restricted Stock Unit Award Agreement (Non-Employee Director).*
10.9(10)	Form of Restricted Stock Unit Award Agreement (Performance Vesting).*
10.10(10)	Form of Restricted Stock Unit Award Agreement (Current Employee).*
10.11(10)	Form of Restricted Stock Unit Award Agreement (Newly Hired Employee).*
31.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	

Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) Incorporated by reference to the Company's Registration Statement on Form S-1 (Reg. No. 33-88386) declared effective March 13, 1995.

(2) Incorporated by reference to the same-numbered exhibit filed with the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2003.

(3) Incorporated by reference to the same-numbered exhibit filed with the Company's Form 8-K filed on January 28, 2004.

(4) Incorporated by reference to exhibit 4.1 filed with the Company's Form 8-K on January 28, 2004.

(5) Incorporated by reference to the same-numbered exhibit filed with the Company's Form 10-Q on August 5, 2004.

(6) Incorporated by reference to the same-numbered exhibit filed with the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2004.

(7) Incorporated by reference to exhibit A of the Company's Proxy Statement dated and filed on April 4, 2005.

(8) Incorporated by reference to exhibit 10.1 filed with the Company's Form 8-K filed on June 27, 2006.

(9) Incorporated by reference to exhibit 99.1 filed with the Company's Form 8-K filed on March 27, 2007.

(10) Incorporated by reference to the same-numbered exhibit filed with the Company's Form 10-Q on August 2, 2006.

(11) Incorporated by reference to Appendix A of the Company's Proxy Statement dated and filed on April 2, 2007.

* Management Contract or Compensatory Plan or Arrangement.

SIGNATURE

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.

NATIONAL INSTRUMENTS CORPORATION
Registrant

BY: /s/ Alex Davern
Alex Davern
Chief Financial Officer and Treasurer
(principal financial and accounting officer)

Dated: November 8, 2007