
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 28, 2014

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: 0-12853

ELECTRO SCIENTIFIC INDUSTRIES, INC.

Oregon
(State or other jurisdiction of incorporation
or organization)

93-0370304
(I.R.S. Employer Identification No.)

13900 N.W. Science Park Drive, Portland, Oregon
(Address of principal executive offices)

97229
(Zip Code)

Registrant's telephone number, including area code: **503-641-4141**

Registrant's web address: **www.esi.com**

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

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

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

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

The number of shares outstanding of the Registrant's Common Stock as of August 1, 2014 was 30,108,299 shares.

ELECTRO SCIENTIFIC INDUSTRIES, INC.
2015 FORM 10-Q QUARTERLY REPORT
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ELECTRO SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands)	Jun 28, 2014	Mar 29, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 82,459	\$ 68,461
Short-term investments	23,866	38,444
Trade receivables, net of allowances of \$406 and \$404	32,957	37,813
Inventories	60,398	58,902
Shipped systems pending acceptance	2,547	2,054
Deferred income taxes, net	160	161
Other current assets	4,563	4,674
Total current assets	206,950	210,509
Non-current assets:		
Non-current investments	—	3,985
Property, plant and equipment, net of accumulated depreciation of \$98,371 and \$98,333	27,086	27,930
Non-current deferred income taxes, net	811	704
Goodwill	7,889	7,889
Acquired intangible assets, net of accumulated amortization of \$18,915 and \$18,376	6,305	6,845
Other assets	12,253	12,347
Total assets	\$ 261,294	\$ 270,209
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 14,597	\$ 14,465
Accrued liabilities	21,101	20,524
Deferred income tax liability, net	170	170
Deferred revenue	12,268	10,515
Total current liabilities	48,136	45,674
Non-current liabilities:		
Income taxes payable	1,151	1,654
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, without par value; 1,000 shares authorized; no shares issued	—	—
Common stock, without par value; 100,000 shares authorized; 30,495 and 30,155 issued and outstanding	182,451	183,193
Retained earnings	28,668	39,336
Accumulated other comprehensive income, other	888	352
Total shareholders' equity	212,007	222,881
Total liabilities and shareholders' equity	\$ 261,294	\$ 270,209

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

ELECTRO SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

(In thousands, except per share amounts)	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Net sales	\$ 35,030	\$ 46,172
Cost of sales	21,795	26,786
Gross profit	13,235	19,386
Operating expenses:		
Selling, service and administration	13,100	14,547
Research, development and engineering	9,145	8,425
Gain on acquisition of Semiconductor Systems business	—	(464)
Net operating expenses	22,245	22,508
Operating loss	(9,010)	(3,122)
Non-operating income (expense):		
Interest and other income (expense), net	46	(60)
Total non-operating income (expense)	46	(60)
Loss before income taxes	(8,964)	(3,182)
(Benefit from) provision for income taxes	(713)	101
Net loss	\$ (8,251)	\$ (3,283)
Net loss per share—basic	\$ (0.27)	\$ (0.11)
Net loss per share—diluted	\$ (0.27)	\$ (0.11)
Weighted average number of shares—basic	30,353	29,745
Weighted average number of shares—diluted	30,353	29,745
Cash dividends paid per outstanding common share	\$ 0.08	\$ 0.08

ELECTRO SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)

(In thousands)	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Net loss	\$ (8,251)	\$ (3,283)
Other comprehensive loss:		
Foreign currency translation adjustment, net of taxes of \$0 and \$0	534	(99)
Accumulated other comprehensive income related to benefit plan obligation, net of taxes of \$2 and \$2	3	3
Net unrealized loss on available-for-sale securities, net of taxes of \$0, and \$0	(1)	(19)
Comprehensive loss	\$ (7,715)	\$ (3,398)

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

ELECTRO SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (8,251)	\$ (3,283)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,957	1,747
Amortization of acquired intangible assets	539	722
Share-based compensation expense	1,330	2,634
(Gain) loss on sale of property and equipment, net	(19)	37
Gain on acquisition of Semiconductor Systems business	—	(464)
Other-than-temporary impairment of cost based investments	—	—
Increase in deferred income taxes	(103)	(289)
Changes in operating accounts, net of acquisitions:		
Decrease (increase) in trade receivables, net	4,958	(2,573)
Increase in inventories	(1,609)	(2,676)
Increase in shipped systems pending acceptance	(493)	(850)
Decrease (increase) in other current assets	234	(1,441)
Increase (decrease) in accounts payable and accrued liabilities	441	(2,655)
Increase in deferred revenue	1,753	391
Net cash provided by (used in) operating activities	737	(8,700)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investments	(133,765)	(123,126)
Proceeds from sales and maturities of investments	152,328	129,015
Purchase of property, plant and equipment	(1,158)	(1,215)
Proceeds from sale of property, plant and equipment	105	—
Cash paid for business acquisitions	—	(8,000)
(Increase) decrease in other assets	(276)	239
Net cash provided by (used in) investing activities	17,234	(3,087)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash dividends paid to shareholders	(2,417)	(2,379)
Stock plan activity, net	(615)	(796)
Share repurchase settlements	(1,330)	—
Net cash used in financing activities	(4,362)	(3,175)
Effect of exchange rate changes on cash	389	(186)
NET CHANGE IN CASH AND CASH EQUIVALENTS	13,998	(15,148)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	68,461	88,913
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 82,459	\$ 73,765
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for interest	(2)	\$ —
Cash paid for income taxes	(320)	(338)
Income tax refunds received	2	2
Accrued acquisition purchase price adjustment	—	(1,600)

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

ELECTRO SCIENTIFIC INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation

These unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted in these interim statements. Accordingly, these condensed consolidated financial statements are to be read in conjunction with the financial statements and notes included in the Company's Annual Report on Form 10-K for its fiscal year ended March 29, 2014. These interim statements include all adjustments (consisting of only normal recurring adjustments and accruals) necessary for a fair presentation of results for the interim periods presented. The results for interim periods are not necessarily indicative of the results of operations for the entire year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of commitments and contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results may differ from those estimates.

Management believes that the estimates used are reasonable. Significant estimates made by management include: revenue recognition; inventory valuation; product warranty reserves; allowance for doubtful accounts; accrued restructuring costs; share-based compensation; income taxes including the valuation of deferred tax assets; fair value measurements; valuation of cost method equity investments; valuation of long-lived assets; valuation of goodwill; and valuation of acquired technology.

There have been no significant changes to the Company's significant accounting policies from those presented in Note 2 "Summary of Significant Accounting Policies" to the consolidated financial statements included in the Company's Annual Report on Form 10-K for its fiscal year ended March 29, 2014. All references to years or quarters relate to fiscal years or fiscal quarters unless otherwise noted.

2. Recent Accounting Pronouncements

Recent Accounting Pronouncements issued by the financial accounting standards board (FASB) and the SEC did not have a material impact on the Company's financial statements.

3. Share-Based Compensation

The Company recognizes expense related to the fair value of its share-based compensation awards using the Black-Scholes model to estimate the fair value of awards on the date of grant, except for unvested restricted stock unit awards which are valued at the fair value of the Company's stock on the date of award. The Company recognizes compensation expense for all share-based compensation awards on a straight-line basis over the requisite service period of the award.

Stock-settled stock appreciation rights (SARs) grant the right to receive shares of the Company's stock equivalent to the increase in stock value of a specified number of shares over a specified period of time, divided by the stock price at the time of exercise. The Company uses the Black-Scholes model to estimate the fair value of SARs. Similar to options, SARs are recorded at the fair value of the award at grant date and the expense is recognized on a straight-line basis over the requisite service period of the award.

The Company granted a total of 451,400 restricted stock unit (RSUs) awards and 230,000 SARs during the first quarter of 2015. In the same period, the Company did not grant any stock options. The Company granted 611,500 restricted stock unit awards and did not grant any SARs or stock options during the first quarter of 2014.

Share-based compensation expense was included in the Company's Condensed Consolidated Statements of Operations as follows:

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<u>(In thousands)</u>	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Cost of sales	\$ 169	\$ 185
Selling, service and administration	865	2,094
Research, development and engineering	296	355
Total share-based compensation expense	\$ 1,330	\$ 2,634

No share-based compensation costs were capitalized in the first quarter of 2015. As of June 28, 2014, the Company had \$7.4 million of total unrecognized share-based compensation costs, net of estimated forfeitures, which are expected to be recognized over a weighted average period of 2.3 years.

4. Fair Value Measurements

Financial Assets Measured at Fair Value

ASC Topic 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include the following:

- *Level 1*, defined as observable inputs such as quoted prices in active markets for identical assets or liabilities;
- *Level 2*, defined as inputs that are observable either directly or indirectly such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and other inputs that can be corroborated by observable market data; and
- *Level 3*, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

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The Company's fair value hierarchy for its financial assets measured at fair value on a recurring basis as of June 28, 2014 and March 29, 2014 was as follows (in thousands):

June 28, 2014	Level 1	Level 2	Level 3	Total
Money market securities	\$ 5,579	\$ —	\$ —	\$ 5,579
Commercial paper	—	20,344	—	20,344
Municipal bonds	—	11,515	—	11,515
Corporate Bonds	—	7,316	—	7,316
Government agencies	—	2,002	—	2,002
Forward purchase or (sale) contracts:				
Japanese Yen	—	2	—	2
New Taiwan Dollar	—	5	—	5
Korean Won	—	11	—	11
Euro	—	(5)	—	(5)
British Pound	—	(46)	—	(46)
Chinese Renminbi	—	(10)	—	(10)
March 29, 2014	Level 1	Level 2	Level 3	Total
Money market securities	\$ 9,456	\$ —	\$ —	\$ 9,456
Corporate bonds	—	17,328	—	17,328
Municipal bonds	—	12,725	—	12,725
Government agencies	—	8,037	—	8,037
Commercial paper	—	6,700	—	6,700
Forward purchase or (sale) contracts:				
Japanese Yen	—	25	—	25
New Taiwan Dollar	—	(6)	—	(6)
Korean Won	—	(44)	—	(44)
Euro	—	39	—	39
British Pound	—	(19)	—	(19)
Chinese Renminbi	—	(2)	—	(2)
Singapore Dollar	—	1	—	1

For Level 1 assets, the Company utilized quoted prices in active markets for identical assets.

For Level 2 assets, exclusive of forward contracts, the Company utilized quoted prices in active markets for similar assets. For forward contracts, spot prices at June 28, 2014 and March 29, 2014 were utilized to calculate fair values.

During the first quarter of 2015, there were no transfers between Level 1, Level 2 or Level 3 assets.

Investments

Certain information regarding the Company's investments at June 28, 2014 and March 29, 2014 was as follows (in thousands):

<u>June 28, 2014</u>	<u>Cost</u>	<u>Unrealized</u>		<u>Fair Value</u>
		<u>Gain</u>	<u>Loss</u>	
Available-for-sale securities (current):				
Commercial paper	\$ 20,344	\$ —	\$ —	\$ 20,344
Municipal Bonds	11,503	12	—	11,515
Corporate Bonds	7,314	2	—	7,316
Government agencies	2,000	2	—	2,002
	<u>\$ 41,161</u>	<u>\$ 16</u>	<u>\$ —</u>	<u>\$ 41,177</u>
<u>March 29, 2014</u>	<u>Cost</u>	<u>Unrealized</u>		<u>Fair Value</u>
		<u>Gain</u>	<u>Loss</u>	
Available-for-sale securities (current):				
Corporate Bonds	\$ 17,321	\$ 7	\$ —	\$ 17,328
Municipal Bonds	8,737	4	—	8,741
Government agencies	8,035	2	—	8,037
Commercial paper	6,700	—	—	6,700
	<u>\$ 40,793</u>	<u>\$ 13</u>	<u>\$ —</u>	<u>\$ 40,806</u>
Available-for-sale securities (non-current):				
Municipal Bonds	\$ 3,976	\$ 9	\$ —	\$ 3,985
	<u>\$ 3,976</u>	<u>\$ 9</u>	<u>\$ —</u>	<u>\$ 3,985</u>

For purposes of determining gross realized gains and losses and reclassification out of accumulated other comprehensive income, the cost of securities sold is based on specific identification. Net unrealized holding gains and losses on current available-for-sale securities included in accumulated other comprehensive income were insignificant as of June 28, 2014 and March 29, 2014.

Underlying maturities of investments at June 28, 2014 were \$41.2 million within one year.

5. Business Acquisitions

Fiscal 2014

On May 3, 2013, the Company purchased the assets related to the Semiconductor Systems business of GSI Group Inc. for a total purchase price of \$9.7 million. The acquisition provides the Company with direct access to industry-leading wafer marking, wafer trimming and circuit trimming laser systems. The purchase price was allocated to the underlying assets acquired and liabilities assumed based on their fair values and resulted in a net gain on bargain purchase of \$0.5 million. The fair value of the acquired net assets of \$10.5 million was in excess of the total purchase consideration of \$9.7 million, primarily due to the recognition of certain intangible assets. The resulting gain of \$0.8 million was partially offset by \$0.3 million of deferred tax liabilities. Analysis supporting the purchase price allocation included a valuation of assets and liabilities as of the closing date, an analysis of intangible assets and a detailed review of the opening balance sheet to determine other significant adjustments required to recognize assets and liabilities at fair value. The acquisition was an asset purchase for tax purposes.

As a result of the acquisition, the Company recorded approximately \$8.2 million of inventory, \$3.9 million of accounts receivable and other current assets, \$0.7 million of identifiable intangible assets, \$2.3 million of current liabilities, and a gain on bargain purchase of \$0.8 million. The \$0.7 million of identifiable intangible assets includes approximately \$0.5 million of backlog and \$0.2 million of developed technology. The acquired intangibles are amortized over their estimated useful lives, which range from one to three years.

In 2014, the Company also incurred approximately \$1.5 million in acquisition related costs which are included in Selling, service and administration expenses in the Condensed Consolidated Statements of Operations.

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The operating results of this purchase are included in the Company's results of operations since the date of acquisition. Pro forma financial information has not been provided for the purchase as it was not material to the Company's overall financial position.

6. Inventories

Inventories are principally valued at standard costs, which approximate the lower of cost (first-in, first-out) or market. Components of inventories were as follows:

<u>(In thousands)</u>	<u>Jun 28, 2014</u>	<u>Mar 29, 2014</u>
Raw materials and purchased parts	\$ 40,410	\$ 38,747
Work-in-process	12,272	12,914
Finished goods	7,716	7,241
	<u>\$ 60,398</u>	<u>\$ 58,902</u>

7. Other Current Assets

Other current assets consisted of the following:

<u>(In thousands)</u>	<u>Jun 28, 2014</u>	<u>Mar 29, 2014</u>
Prepaid expenses	\$ 2,432	\$ 2,601
Value added tax receivable	822	779
Other	1,309	1,294
	<u>\$ 4,563</u>	<u>\$ 4,674</u>

8. Other Assets

Other assets consisted of the following:

<u>(In thousands)</u>	<u>Jun 28, 2014</u>	<u>Mar 29, 2014</u>
Consignment and demo equipment, net	\$ 5,563	\$ 5,938
Minority equity investments	4,263	4,263
Long term deposits and other	2,427	2,146
	<u>\$ 12,253</u>	<u>\$ 12,347</u>

Minority equity investments represents the Company's investments in OmniGuide, Inc., which are accounted for as cost method investments. At each reporting period end, the Company determines whether events or circumstances have occurred that are likely to have a significant adverse effect on the fair value of the investments. If there are no identified events or circumstances that may have a significant adverse effect on the fair value of the investments, the fair value of the investments are not calculated as it is not practicable to do so.

The total carrying value of these investments was \$9.0 million at March 30, 2013 and an additional investment of \$5.0 million was made in the second quarter of 2014 for a total investment of \$14.0 million life-to-date, or a 15% interest. In the second quarter of 2014, OmniGuide, Inc., engaged in a Series F Preferred Stock round of equity financing priced below previous rounds, which was considered a triggering event and the Company recorded a \$3.6 million impairment charge on its Series D and Series E investments at that time. In the fourth quarter of 2014, further triggering events were identified due to poor operating results through the end of the year combined with decreasing cash levels. We performed an updated valuation of our investments in the fourth quarter and recorded an additional \$6.1 million impairment charge.

The Company's investment may be further impaired if OmniGuide, Inc., is unable to raise sufficient funding for operations or if business results deteriorate. The total carrying value of \$4.3 million at March 29, 2014 is included in Other assets on the Condensed Consolidated Balance Sheets.

9. Accrued Liabilities

Accrued liabilities consisted of the following:

<u>(In thousands)</u>	<u>Jun 28, 2014</u>	<u>Mar 29, 2014</u>
Payroll-related liabilities	\$ 8,325	\$ 6,889
Product warranty accrual	3,487	4,215
Professional fees payable	1,622	1,933
Pension benefit liabilities	2,045	1,912
Purchase order commitments and receipts	2,002	2,569
Customer deposits	1,341	375
Freight accrual	375	503
Income taxes payable	—	162
Restructuring costs payable	25	327
Value added taxes payable	357	332
Other	1,522	1,307
	<u>\$ 21,101</u>	<u>\$ 20,524</u>

10. Product Warranty

The following is a reconciliation of the changes in the aggregate product warranty accrual:

<u>(In thousands)</u>	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Product warranty accrual, beginning	\$ 4,215	\$ 5,411
Warranty charges incurred, net	(1,940)	(1,821)
Provision for warranty charges	1,212	1,603
Product warranty accrual, ending	<u>\$ 3,487</u>	<u>\$ 5,193</u>

Net warranty charges incurred include labor charges and costs of replacement parts for system repairs under warranty. These costs are recorded net of any estimated cost recoveries resulting from either successful repair of damaged parts or from warranties offered by the Company's suppliers for defective components. The provision for warranty charges reflects the estimate of future anticipated net warranty costs to be incurred for all products under warranty at quarter end and is recorded to cost of sales.

11. Deferred Revenue

Generally, revenue is recognized upon fulfillment of acceptance criteria at the Company's factory and title transfer which frequently occurs at the time of delivery to a common carrier. Revenue is deferred whenever title transfer is pending and/or acceptance criteria have not yet been fulfilled. Deferred revenue occurrences include sales to Japanese customers, shipments of substantially new products and shipments with custom specifications and acceptance criteria. In sales involving multiple element arrangements, the relative selling price of any undelivered elements, including installation services, is deferred until the elements are delivered and acceptance criteria are met. Revenue related to maintenance and service contracts is deferred and recognized ratably over the duration of the contracts.

The following is a reconciliation of the changes in deferred revenue:

<u>(In thousands)</u>	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Deferred revenue, beginning	\$ 10,515	\$ 10,196
Revenue deferred	11,808	6,941
Revenue recognized	(10,055)	(6,371)
Deferred revenue, ending	\$ 12,268	\$ 10,766

12. Earnings (Loss) Per Share

The following is a reconciliation of weighted average shares outstanding used in the calculation of basic and diluted earnings per share:

<u>(In thousands, except per share data)</u>	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Net loss	\$ (8,251)	\$ (3,283)
Weighted average shares used for basic earnings per share	30,353	29,745
Incremental diluted shares	—	—
Weighted average shares used for diluted earnings per share	30,353	29,745
Net loss per share:		
Net loss — basic	\$ (0.27)	\$ (0.11)
Net loss — diluted	\$ (0.27)	\$ (0.11)

Awards of options, SARs and unvested RSUs representing an additional 3.3 million and 3.4 million shares of stock for the first quarters of 2015 and 2014, respectively, were not included in the calculation of diluted net earnings per share because their effect would have been antidilutive.

13. Product and Geographic Information

Net sales by product type were as follows:

<u>(In thousands)</u>	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Interconnect & Microfabrication Group (IMG)	\$ 20,948	\$ 34,417
Semiconductor Group (SG)	10,749	5,613
Components Group (CG)	3,333	6,142
	\$ 35,030	\$ 46,172

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Net sales by geographic area, based on the location of the end user, were as follows:

(In thousands)	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Asia	\$ 24,718	\$ 37,693
Americas	6,174	6,070
Europe	4,138	2,409
	<u>\$ 35,030</u>	<u>\$ 46,172</u>

14. Restructuring and Cost Management Plans

In 2013, the Company initiated a restructuring plan to improve efficiency, transition from memory repair and other legacy products, and focus on laser microfabrication for consumer electronics, emerging technologies related to semiconductor 3D packaging, and proprietary laser technology. Although the plan is substantially complete, we will continue to wind down both our physical and legal presence in the vacated region over the year of 2015. See the Company's Form 10-K for the year ended March 29, 2014 for additional information related to restructuring and cost management plans.

In the first quarter of 2015, net restructuring costs of \$0.5 million were recognized. At June 28, 2014 and March 29, 2014, the amount of unpaid restructuring costs included in accrued liabilities was \$0.6 million and \$1.1 million, respectively.

The following table presents the amounts related to restructuring costs payable (in thousands):

Restructuring & cost management amounts payable as of March 29, 2014	\$ 1,050
Employee severance and related benefits:	
Cash payments	(455)
Restructuring & cost management amounts payable as of June 28, 2014	<u>\$ 595</u>

15. Shareholders' Equity

Share Repurchase Program

In December 2011, the Board of Directors authorized a share repurchase program totaling \$20.0 million to acquire shares of our outstanding common stock. The repurchases are to be made at management's discretion in the open market or in privately negotiated transactions in compliance with applicable securities laws and other legal requirements and are subject to market conditions, share price and other factors.

In the first quarter of 2015 the Company repurchased 207,738 shares for \$1.5 million under this authorization at an average price of \$7.01 per share, calculated inclusive of commissions and fees. Cash used to settle the repurchase transactions as of June 28, 2014 totaled \$1.3 million and is reflected as a component of cash used in financing activities on the Condensed Consolidated Statements of Cash Flows. Accrued liabilities include \$0.2 million for amounts owed on the unsettled repurchase transactions as of June 28, 2014. In 2014 the Company repurchased 19,832 shares for \$0.2 million at an average price of \$9.65 per share. The Company has repurchased a total of 227,570 shares life to date under this authorization as a part of its publicly announced plan.

There is no fixed completion date for the repurchase program. The following table provides information with respect to share repurchases by the Company during 2015 and 2014.

Fiscal Period	Total number of shares purchased	Average price paid per share	Total value of shares repurchased	Maximum value of shares that may yet be purchased under the program
June FY 2015 (06/01/2014 to 06/28/2014)	68,750	\$6.89	\$0.5 million	\$18.3 million
May FY 2015 (05/04/2014 to 05/31/2014)	138,988	\$7.07	\$1.0 million	\$18.8 million

Dividends

In December 2011, the Board of Directors adopted a dividend policy under which the Company intends to pay quarterly cash dividends. The following table summarizes the quarterly dividend declared and paid by the Company during 2015 and 2014:

Date Declared	Record Date	Payable Date	Amount per Share
May 15, 2014	May 27, 2014	June 10, 2014	\$0.08
February 13, 2014	February 27, 2014	March 13, 2014	\$0.08
November 7, 2013	November 19, 2013	December 4, 2013	\$0.08
August 8, 2013	August 19, 2013	September 3, 2013	\$0.08
May 14, 2013	June 5, 2013	June 19, 2013	\$0.08

The Company paid aggregate dividends of \$2.4 million in each of the first quarters of 2015 and 2014.

The Company currently anticipates that it will continue to pay cash dividends on a quarterly basis in the future, although the declaration, timing and amount of any future cash dividends are at the discretion of the Board of Directors and will depend on the Company's financial condition, results of operations, capital requirements, business conditions and other factors, as well as a determination that cash dividends are in the best interest of the shareholders.

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

The statements contained in this report that are not statements of historical fact, including without limitation, statements containing the words "believes," "expects," "anticipates" and similar words, constitute forward-looking statements that are subject to a number of risks and uncertainties. From time to time we may make other forward-looking statements. Investors are cautioned that such forward-looking statements are subject to an inherent risk that actual results may materially differ as a result of many factors, including the risks described in Part II, Item 1A "Risk Factors."

Overview of Business

Electro Scientific Industries, Inc. and its subsidiaries (ESI) is a leading supplier of innovative laser-based manufacturing solutions for the microtechnology industry. Our advanced laser systems enable precise structuring of micron to submicron features in components and devices which are used in a wide variety of end products in the consumer electronics, computer, semiconductor, communications and other markets. These features enable our customers to achieve functionality, or improve yield and productivity in their manufacturing processes that can be critical to their profitability. Founded in 1944, ESI is headquartered in Portland, Oregon, with global operations and subsidiaries in Asia, Canada, Europe and the United States.

Our advanced laser microfabrication systems allow microelectronics, semiconductor, and other microtechnology manufacturers to physically alter select device features during high-volume production in order to increase performance, enable functionality, alter physical characteristics or improve production yields. Laser microfabrication comprises a set of precise micron-level processes, including drilling, scribing, dicing, singulation, cutting, ablating, trimming, and precision marking on multiple types of materials. These processes require application-specific laser systems that are able to meet our customers' exacting performance and productivity requirements. Our laser-based systems improve production yields or enable improved performance for flexible and rigid high density interconnect printed circuit boards, semiconductor devices, advanced semiconductor packaging, touch-panel glass, flat panel liquid crystal displays (LCDs) and other high value components.

Additionally, we produce high-capacity test and inspection equipment that is critical to the quality control process during the production of multilayer ceramic capacitors (MLCCs). Our equipment ensures that each component meets the electrical and physical tolerances required to perform properly. Lastly, we produce systems that use photonic technology to perform precision inspection for quality control and defect identification.

Summary of Sequential Quarterly Results

The financial results for the first quarter of 2015 reflected a sequential decline in revenues to \$35.0 million from \$37.1 million in the fourth quarter of 2014, largely a result of the low order rate of approximately \$31.7 million in the fourth quarter of 2014. Total orders increased to \$47.3 million in first quarter of 2015, primarily driven by growth in flex via drilling, advanced microfabrication and to a lesser extent by growth in components and semiconductor businesses.

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Net sales were \$35.0 million in the first quarter of 2015 compared to \$37.1 million in the fourth quarter of 2014. IMG decreased due to lower microfabrication and scientific product sales, partially offset by an increase in the flex business. CG and SG sales remained substantially flat, with CG decreasing by \$0.2 million and SG increasing by \$0.5 million.

Gross profit was \$13.2 million in the first quarter of 2015 compared to a gross profit of \$3.7 million in the fourth quarter of 2014. Gross margin was 37.8% on net sales of \$35.0 million in the first quarter of 2015 compared to a gross margin of 10.1% on net sales of \$37.1 million in the fourth quarter of 2014. Gross margin rate improved primarily due to significantly lower inventory write-offs compared to the fourth quarter of 2014, but reflects the unfavorable impacts of product mix, lower volumes, and increased warranty costs in the first quarter of 2015.

Net operating expenses of \$22.2 million in the first quarter of 2015 decreased \$3.3 million from \$25.5 million in the fourth quarter of 2014, primarily due to one-time expenses associated with shipment of the initial glass cutting and semiconductor systems during the fourth quarter of 2014, lower discretionary costs and other variable expenses based on lower business volume in the first quarter of 2015.

Operating loss was \$9.0 million in the first quarter of 2015 compared to an operating loss of \$21.8 million in the fourth quarter of 2014, a change of \$12.8 million. The decrease in operating loss was primarily due to lower inventory write-offs and decreased operating expenses resulting from restructuring actions initiated in 2014.

Non-operating income was \$0.05 million in the first quarter of 2015 compared to expense of \$6.1 million in the fourth quarter of 2014. The change is primarily due to the \$6.1 million impairment against our minority equity investment in OmniGuide, Inc., recorded in the fourth quarter of 2014.

Benefit from income taxes was \$0.7 million in the first quarter of 2015 compared to a benefit of \$0.3 million in the fourth quarter of 2014, primarily due to a favorable tax ruling related to the legal settlement with All Ring.

Net loss was \$8.3 million in the first quarter of 2015 compared to a net loss of \$27.6 million in the fourth quarter of 2014.

Quarter Ended June 28, 2014 Compared to Quarter Ended June 29, 2013

Results of Operations

The following table presents results of operations data as a percentage of net sales:

	Fiscal quarter ended	
	Jun 28, 2014	Jun 29, 2013
Net sales	100.0 %	100.0 %
Cost of sales	62.2	58.0
Gross profit	37.8	42.0
Selling, service and administration	37.4	31.6
Research, development and engineering	26.1	18.2
Gain on acquisition of Semiconductor Systems business	—	(1.0)
Operating (loss) income	(25.7)	(6.8)
Interest and other income (expense), net	0.1	(0.1)
Loss before income taxes	(25.6)	(6.9)
(Benefit from) provision for income taxes	(2.1)	0.2
Net loss	(23.6)%	(7.1)%

Net Sales

The following table presents net sales information by product group:

	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Net Sales	% of Net Sales	Net Sales	% of Net Sales
(In thousands, except percentages)				
Interconnect & Microfabrication Group (IMG)	\$ 20,948	59.8%	\$ 34,417	74.5%
Semiconductor Group (SG)	10,749	30.7	5,613	12.2
Components Group (CG)	3,333	9.5	6,142	13.3
	<u>\$ 35,030</u>	<u>100.0%</u>	<u>\$ 46,172</u>	<u>100.0%</u>

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Net sales for the first quarter of 2015 decreased \$11.1 million or 24% from net sales for the first quarter of 2014. Sales in IMG and CG decreased by 39% and 46%, respectively, while SG sales increased by 92%.

IMG sales for the first quarter of 2015 decreased \$13.5 million compared to the first quarter of 2014. The decrease in IMG sales was driven by decreased demand resulting from excess capacity and increased competition in the flex product space.

SG sales for the first quarter of 2015 increased \$5.1 million compared to the first quarter of 2014. The increase was primarily driven by the sales in the Semiconductor Systems business which was acquired in early May in the first quarter of 2014.

CG sales for the first quarter of 2015 decreased \$2.8 million compared to the first quarter of 2014 due to reduced demand for MLCC systems in first quarter 2015.

The following table presents net sales information by geographic region:

<u>(In thousands, except percentages)</u>	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Net Sales	% of Net Sales	Net Sales	% of Net Sales
Asia	\$ 24,718	70.6%	\$ 37,693	81.6%
Americas	6,174	17.6	6,070	13.1
Europe	4,138	11.9	2,409	5.2
	<u>\$ 35,030</u>	<u>100.0%</u>	<u>\$ 46,172</u>	<u>100.0%</u>

Gross Profit

<u>(In thousands, except percentages)</u>	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Gross Profit	% of Net Sales	Gross Profit	% of Net Sales
Gross Profit	\$ 13,235	37.8%	\$ 19,386	42.0%

Gross profit was \$13.2 million for the first quarter of 2015, a decrease of \$6.2 million compared to the first quarter of 2014. Gross margins were 37.8% and 42.0% for the first quarters of 2015 and 2014, respectively. These decreases were driven primarily by lower IMG sales and associated higher absorption of fixed costs. To a lesser extent, margins were negatively impacted by increased warranty expenses in IMG and changes in mix within both IMG and CG, due to lower MLCC and flex sales.

Operating Expenses

<u>(In thousands, except percentages)</u>	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Expense	% of Net Sales	Expense	% of Net Sales
Selling, service and administration	\$ 13,100	37.4%	\$ 14,547	31.6%
Research, development and engineering	9,145	26.1	8,425	18.2
Gain on acquisition of Semiconductor Systems business	—	—	(464)	(1.0)
	<u>\$ 22,245</u>	<u>63.4%</u>	<u>\$ 22,508</u>	<u>48.8%</u>

Selling, Service and Administration

Selling, service and administration (SS&A) expenses primarily consist of labor and other employee-related expenses including share-based compensation expense, travel expenses, professional fees, sales commissions and facilities costs.

SS&A expenses for the first quarter of 2015 decreased \$1.4 million compared to the first quarter of 2014. This decrease was primarily attributable to decreases in share-based compensation and the impact on labor costs of restructuring actions in 2014.

Research, Development and Engineering

Research, development and engineering (RD&E) expenses are primarily comprised of labor and other employee-related expenses, professional fees, project materials costs, equipment costs and facilities costs. RD&E expenses for the first quarter of 2015 increased \$0.7 million compared to the first quarter of 2014, reflecting increases due to the inclusion of a full quarter of

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the acquired Semiconductor Systems business in 2015 and higher project development costs, partially offset by the impact of restructuring actions in 2014.

Gain on acquisition of Semiconductor Systems Business

Gain on acquisition of the Semiconductor Systems business was \$0.5 million in first quarter of 2014. This purchase resulted in a gain as the estimated fair value of the assets purchased was in excess of the total purchase consideration, primarily due to the recognition of certain intangible assets.

Non-operating Income and Expense, net

	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Non-operating Income and Expense, net	% of Net Sales	Non-operating Income and Expense, net	% of Net Sales
(In thousands, except percentages)				
Interest and other income (expense), net	\$ 46	0.1%	\$ (60)	(0.1)%

Interest and other income (expense), net, consists of net interest income and expense, market gains and losses on assets held in employees' deferred compensation accounts, realized and unrealized foreign exchange gains and losses, bank charges, investment management fees, and other miscellaneous non-operating items. The increase in other income was primarily attributable to higher net market gains on investments, partially offset by increased net foreign exchange losses.

Income Taxes

	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Income Tax Benefit	Effective Tax Rate	Income Tax Provision	Effective Tax Rate
(In thousands, except percentages)				
(Benefit from) provision for income taxes	\$ (713)	8.0%	\$ 101	(3.2)%

The income tax benefit for the first quarter of 2015 was \$0.7 million on pretax loss of \$9.0 million, an effective tax rate of 8.0%. For the first quarter of 2014, the income tax provision was \$0.1 million on pretax income of \$3.2 million, an effective rate of (3.2)%. The change in the effective tax rate is driven primarily by the change in pretax income levels, the release of the tax reserve related to the legal settlement with All Ring, and, to a lesser extent, by changes in the mix of income between foreign tax jurisdictions.

Net Loss

	Fiscal quarter ended			
	Jun 28, 2014		Jun 29, 2013	
	Net Loss	% of Net Sales	Net Loss	% of Net Sales
(In thousands, except percentages)				
Net loss	\$ (8,251)	(23.6)%	\$ (3,283)	(7.1)%

As a result of the factors discussed above, net loss for the first quarter of 2015 was \$8.3 million, or \$0.27 per basic and diluted share, compared to a net loss of \$3.3 million, or \$0.11 per basic and diluted share, for the first quarter of 2014.

Financial Condition and Liquidity

At June 28, 2014, our principal sources of liquidity were cash and cash equivalents of \$82.5 million, short-term investments of \$23.9 million and accounts receivable of \$33.0 million. At June 28, 2014, we had a current ratio of 4.30 and held no long-term debt. Working capital of \$158.8 million decreased \$6.0 million compared to the March 29, 2014 balance of \$164.8 million, substantially impacted by the payment of quarterly dividends.

In December 2011, the Board of Directors adopted a dividend policy under which we intend to pay quarterly cash dividends. The following table summarizes the quarterly dividend declared and paid by us in 2015 and 2014:

Date Declared	Record Date	Payable Date	Amount per Share
May 15, 2014	May 27, 2014	June 10, 2014	\$0.08
February 13, 2014	February 27, 2014	March 13, 2014	\$0.08
November 7, 2013	November 19, 2013	December 4, 2013	\$0.08
August 8, 2013	August 19, 2013	September 3, 2013	\$0.08
May 14, 2013	June 5, 2013	June 19, 2013	\$0.08

We paid aggregate dividends of \$2.4 million in each of the first quarters of 2015 and 2014.

We currently anticipate that we will continue to pay cash dividends on a quarterly basis in the future, although the declaration, timing and amount of any future cash dividends are at the discretion of the Board of Directors and will depend on our financial condition, results of operations, capital requirements, business conditions and other factors, as well as a determination that cash dividends are in the best interest of our shareholders.

Sources and Uses of Cash

Net cash provided by operating activities of \$0.7 million for the first quarter of 2015, was due to a \$3.9 million decrease to working capital and a \$1.3 million increase to deferred margin, partially offset by \$4.5 million of net loss adjusted for non-cash items.

Net cash provided by investing activities of \$17.2 million was the result of \$133.8 million of purchases of investments, \$1.2 million of capital expenditures from purchases of property, plant and equipment (PP&E) and \$0.3 million increase in other assets, partially offset by \$152.3 million of proceeds from sales and maturities of investments and \$0.1 million of proceeds from the sale of property. Accounts payable balance includes \$0.04 million for amounts owed on PP&E purchases as of June 28, 2014.

For the first quarter of 2015, net cash used in financing activities of \$4.4 million primarily resulted from \$2.4 million of cash dividends paid to shareholders and \$1.3 million of share repurchase settlements.

We believe that our existing cash, cash equivalents and short-term investments are adequate to fund our operations, any dividends which may be declared, our share repurchase program and contractual obligations for at least the next twelve months.

Critical Accounting Policies and Estimates

We reaffirm the "Critical Accounting Policies and Estimates" in Part II Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations reported in our Form 10-K for the year ended March 29, 2014.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes in the market risk disclosure contained in our Form 10-K for the year ended March 29, 2014.

Item 4. Controls and Procedures

Attached to this quarterly report as exhibits 31.1 and 31.2 are the certifications of our President and Chief Executive Officer (CEO) and our Chief Financial Officer (CFO) required by Section 302 of the Sarbanes-Oxley Act of 2002 (the Section 302 Certifications). This portion of our quarterly report on Form 10-Q is our disclosure of the conclusions of our management regarding the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report based on management's evaluation of those disclosure controls and procedures. This disclosure should be read in conjunction with the Section 302 Certifications for a more complete understanding of the topics presented.

Disclosure Controls and Procedures

Our management has evaluated, under the supervision and with the participation of our CEO and CFO, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (Exchange Act). Based on that evaluation, our CEO and CFO have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective in ensuring that information required to be disclosed in our Exchange Act reports is (1) recorded, processed, summarized and reported in a timely manner, and (2) accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There has been no change in our internal control over financial reporting during the first quarter of 2015 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

In the ordinary course of business, we are involved in various legal matters, either asserted or unasserted, and investigations. In the opinion of management, ultimate resolution of these matters will not have a material effect on our consolidated financial position, results of operations or cash flows.

Item 1A. Risk Factors

The statements contained in this report that are not statements of historical fact, including without limitation statements containing the words "believes," "expects" and similar words, constitute forward-looking statements that are subject to a number of risks and uncertainties. From time to time, we may make other forward-looking statements. Investors are cautioned that such forward-looking statements are subject to an inherent risk that actual results may differ materially. The following information highlights some of the factors that could cause actual results to differ materially from the results expressed or implied by our forward-looking statements. Forward-looking statements should be considered in light of these factors. Factors that may result in such variances include, but are not limited to, the following:

Risks Related to Our Competition and Customers

Volatility of Our Customers' Industries

Our business is dependent upon the capital expenditures of manufacturers of microelectronics, semiconductors, computers, wireless communications and other electronic products. The capital equipment market for microelectronics, semiconductor, and consumer electronics manufacturers has historically been characterized by sudden and severe cyclical variations in product supply and demand due to a number of factors including capacity utilization, timing of customers' new product introductions and demand for their products, inventory levels relative to demand and access to affordable capital. The timing, severity and duration of these market cycles are difficult or impossible to predict. As a result, business levels can vary significantly from quarter to quarter or year to year. Significant volatility in investment cycles in the market for microelectronics, and semiconductors used in electronic devices or in the market for consumer electronics reduce demand for our products and may materially and adversely affect our business, financial condition and results of operations. For example, starting in the second half of fiscal 2012, we experienced the negative impact of an uncertain economic environment, slower market growth and overcapacity in several of our markets, which resulted in overall lower order and revenue levels. As a result of these circumstances, our total order volume declined in 2013 compared to 2012 and continued to decline in 2014. The degree of the impact of any downturn on our business depends on a number of factors, including: the strength of the global and United States economies; the overall level of demand for consumer electronics products; the stability of global financial systems; and the overall health of the microelectronics, semiconductor, and consumer electronics industries.

Highly Competitive Markets

We face substantial competition from established competitors throughout the world, some of which have greater financial, engineering, manufacturing and marketing resources than we do. Those competitors with greater resources may, in addition to other things, be able to better withstand periodic downturns, compete more effectively on the basis of price and technology, or more quickly develop enhancements to, and new generations of, products that compete with the products we manufacture and market. New companies may enter the markets in which we compete, or industry consolidation may occur, further increasing competition in those markets. We have also experienced new entrants to our markets offering aggressive price and payments terms in an attempt to gain market share. Some competitors, particularly in China, also develop low cost products employing processes or technology developed by us. We believe that to be competitive we must continue to expend significant financial resources in order to, among other things, invest in new product development and enhancements. We may not be able to compete successfully in the future and increased competition may result in price reductions, reduced profit margins and loss of market share.

We intend to enter into existing markets that are adjacent to our current markets. In these markets we will be competing against established competitors with recognized brands, customer relationships and proven products. If we fail to compete successfully against these competitors our ability to penetrate these markets will be limited, which could have an adverse effect on our financial results.

Increased Price Pressure

We have experienced and continue to experience pricing pressure in the sale of our products, from both competitors and customers. Pricing pressures typically have become more intense during cyclical downturns when competitors seek to maintain or increase market share, reduce inventory or introduce more technologically advanced products or lower cost products. In addition, we may agree to pricing concessions or extended payment terms with our customers in connection with volume orders or to improve cost of ownership in highly competitive applications. Our business, financial condition, margins or results of operations may be materially and adversely affected by competitive pressure and intense price-based competition.

Revenues are Largely Dependent on Few Customers

We depend on a few significant customers for a large portion of our revenues. In 2014, our top ten customers accounted for approximately 41% of total net sales, with one customer, Apple, Inc., and its affiliates, accounting for approximately 15% of total net sales. We anticipate that sales of our products to a relatively small number of customers will continue to account for a significant portion of our revenues. Consolidation between customers, changes in technologies or solutions used by customers, changes in products manufactured by customers or in end-user demand for those products, selection of suppliers other than us, customer bankruptcies or customer departures from their respective industries all may result in even fewer customers accounting for a high percentage of our revenue and reduced demand from any single major customer. Also, business levels with several of our top customers are dependent on our winning new designs and features each product cycle, and there is no guarantee of future business based on past design wins. Furthermore, none of our customers have any long-term obligation to continue to buy our products or services and may therefore delay, reduce or cease ordering our products or services at any time. The cancellation, reduction or deferral of purchases of our products by even a single customer could significantly reduce our revenues in any particular quarter. For example, revenues from Apple, Inc., decreased from \$67 million or 31% of revenue in 2013 to \$27 million or 15% of revenue in 2014. If we were to lose any of our significant customers or suffer a material reduction in their purchase orders, revenue could decline and our business, financial condition and results of operations could be materially and adversely affected.

Revenues are Largely Based on the Sale of a Small Number of Product Units

We derive a substantial portion of our revenue from the sale of a relatively small number of products. Accordingly, our revenues, margins and other operating results could fluctuate significantly from quarter to quarter depending upon a variety of factors in addition to those described above, including:

- changes in the timing of orders and terms or acceptance of product shipments by our customers;
- changes in the mix of products and services that we sell;
- timing and market acceptance of our new product introductions; and
- delays or problems in the planned introduction of new products, or in the performance of any such products following delivery to customers.

As a result of these risks, we believe that quarter-to-quarter comparisons of our revenue and operating results may not be meaningful, and that these comparisons may not be an accurate indicator of our future performance.

Risks Related to Our Supply Chain and Production

Variability of Production Capacity

To meet rapidly changing demand in the industries we serve, we must effectively manage our resources and production capacity. During periods of decreasing demand for our products, we must be able to appropriately align our cost structure with prevailing market conditions and effectively manage our supply chain. Our ability to rapidly and effectively reduce our cost structure in response to such downturns is limited by the fixed nature of many of our expenses in the near term and by our need to continue our investment in next-generation product technology and to support and service our products. Conversely, when upturns occur in the markets we serve, we may have difficulty rapidly and effectively increasing our manufacturing capacity or procuring sufficient materials to meet sudden increases in customer demand that could result in the loss of business to our competitors and harm to our relationships with our customers. If we are not able to timely and appropriately adapt to changes in our business environment, our business, financial condition or results of operations may be materially and adversely affected.

Reliance on Critical Suppliers

We use a wide range of components from numerous suppliers in the manufacture of our products, including custom electronic, laser, optical and mechanical components. We generally do not have guaranteed supply arrangements with our suppliers. We seek to reduce the risk of production and service interruptions and shortages of key parts by selecting and qualifying alternative suppliers for key parts, monitoring the financial stability of key suppliers and maintaining appropriate inventories of key parts. Although we make reasonable efforts to ensure that parts are available from multiple suppliers, some key parts are available only from a single supplier or a limited group of suppliers in the short term. In addition, some of the lasers we use in our products are difficult to manufacture, and as a result we may not receive an adequate supply of lasers in a timely fashion to fill orders. Operations at our suppliers' facilities are subject to disruption or discontinuation for a variety of reasons, including changes in business relationships, competitive factors, financial difficulties, work stoppages, fire, natural disasters or other causes. Any such disruption or discontinuation to our suppliers' operations could interrupt or reduce our manufacturing activities and delay delivery of our products, any or all of which could materially and adversely affect our results of operations. In addition, when markets recover from economic downturns, there is a heightened risk that one or more of our suppliers may not be able to meet our increased demand requirements, adversely impacting our ability to fulfill orders and win business with our customers.

Utilization of Contract Manufacturers

We have arrangements with contract manufacturers to complete the manufacturing of certain of our products or product subcomponents. Any significant interruption in our contract manufacturers' ability to provide manufacturing services to us as a result of contractual disputes with us or another party, labor disruptions, financial difficulties, natural disasters, delay or interruption in the receipt of inventory, customer prioritization or other causes could result in reduced manufacturing capabilities or delayed deliveries for certain of our products, any or all of which could materially and adversely affect our results of operations.

Charges for Excess or Obsolete Inventory

One factor on which we compete is the ability to ship products on schedules required by customers. In order to facilitate timely shipping, management forecasts demand, both in type and amount of products, and these forecasts are used to determine inventory to be purchased. We also order materials based on our technology roadmap, which represents management's assessment of technology that will be utilized in new products that we develop. Certain types of inventory, including lasers and optical equipment, are particularly expensive and may only be used in the production of a single type of product. If actual demand is lower than forecast with respect to the type or amount of products actually ordered, or both, our inventory levels may increase. As a result, there is a risk that we may have to incur material charges for excess and obsolete inventory if inventory cannot be used, which would negatively affect our financial results. Also, if we alter our technology or product development strategy, we may have inventory that may not be usable under the new strategy, which may also result in material accounting charges. For example, during 2014, we recorded \$12.8 million of charges in cost of sales for inventory written off in connection with discontinued products.

Uncertainties Resulting from Conflict Minerals Regulation

On August 22, 2012, the SEC adopted a new rule requiring disclosures of specified minerals, known as conflict minerals, that are necessary to the functionality or production of products manufactured or contracted to be manufactured by companies filing public reports. The new rule requires a disclosure report to be filed annually with the SEC and this report will require companies to perform due diligence, disclose, and report whether such minerals originate from the Democratic Republic of Congo or an adjoining country. The new rule could affect sourcing at competitive prices and availability in sufficient quantities

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of certain minerals used in the manufacture of our products, including tantalum, tin, gold, and tungsten. The number of suppliers who provide conflict-free minerals may be limited. In addition, there may be material costs associated with complying with the disclosure requirements, such as costs related to determining the source of certain minerals used in our products, as well as costs of possible changes to products, processes, or sources of supply as a consequence of such verification activities. Since our supply chain is complex, we may not be able to sufficiently verify the origins of the relevant minerals used in our products through the due diligence procedures that we implement, which may harm our reputation. In addition, we may encounter challenges to satisfy those customers who require that all of the components of our products be certified as conflict-free, which could place us at a competitive disadvantage if we are unable to do so.

Risks Related to Our Organization

Operating a Global Business

International shipments accounted for 83% of net sales in 2014, with 76% of our net shipments to customers in Asia. We expect that international shipments will continue to represent a significant percentage of net sales in the future. We also have significant foreign operations, including manufacturing facilities in Singapore, research and development facilities in Canada, France and Taiwan, and sales and service offices in various countries. Under our globalization strategy, we intend to increase our foreign operations in the future. Our non-U.S. sales, purchases and operations are subject to risks inherent in conducting business abroad, many of which are outside our control, including the following:

- periodic local or geographic economic downturns and unstable political conditions;
- price and currency exchange controls;
- fluctuation in the relative values of currencies;
- difficulty in repatriating money, whether as a result of tax laws or otherwise;
- difficulties protecting intellectual property;
- compliance with labor laws and other laws governing employees;
- local labor disputes;
- shipping delays and disruptions;
- unexpected changes in trading policies, regulatory requirements, tariffs and other barriers; and
- difficulties in managing a global enterprise, including staffing, enforcing internal controls, collecting accounts receivable, and managing suppliers, distributors and representatives.

Our business and operating results could also be impacted, directly or indirectly, by natural disasters, outbreaks of infectious disease, military action, international conflicts, terrorist activities, civil unrest and associated political instability. Many of our facilities, including our Portland, Oregon headquarters, are in areas with known earthquake risk. Some of these events or circumstances may also result in heightened security concerns with respect to domestic and international travel and commerce, which may further affect our business and operating results. In particular, due to these uncertainties, we are subject to the following additional risks:

- future tightening of immigration controls may adversely affect the residence status of non-U.S. engineers and other key technical employees in our U.S. facilities or our ability to hire new non-U.S. employees in such facilities;
- more frequent instances of shipping delays;
- demand for our products may not increase or may decrease; and
- our customers or suppliers may experience financial difficulties or cease operations.

Implementation and Modification of Globalization Strategy

We are continuing to implement and expand our globalization strategy in which we are moving certain operational resources and capabilities to different countries in Asia to be closer to many of our significant customers to reduce costs and to develop low cost follow-on solutions to our products. We believe this strategy will enhance customer relationships, improve our responsiveness, reduce our manufacturing costs for certain products and allow us to compete with low cost competitors who develop systems employing processes developed by us. We opened a manufacturing facility in Singapore in the fourth quarter of 2010, which manufactures certain IMG, SG, CG and laser ablation products and is now our primary system manufacturing facility.

Our globalization strategy is subject to a variety of complexities and risks, many of which may divert a substantial amount of management's time. These risks include:

- challenges in designing facilities that can be scaled for future expansion, replicating current processes and bringing new facilities up to full operation;
- unpredictable costs, redundancy costs and cost overruns for developing facilities and acquiring equipment;
- building local management teams, technical personnel and other staff for functions that we have not previously conducted outside of the United States;

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- technical obstacles such as poor production or process yield and loss of quality control during the ramp of a new facility;
- re-qualifications and other procedures that may be required by our customers;
- our ability to bring up local suppliers to meet our quality and cycle-time needs;
- our ability to reduce costs in the United States as we add costs elsewhere;
- rapidly changing business conditions that may require plans to be changed or abandoned before they are fully implemented; and
- challenges posed by distance and by differences in language and culture.

These and other factors could delay the continuing development, expansion and implementation of our strategy, as well as impair our gross margins, delay shipments and deliveries, cause us to lose sales, require us to write off investments already made, damage our reputation and harm our business, financial condition and results of operations. If we decide to change our globalization strategy, we may incur charges for certain costs incurred.

Acquisitions and Divestitures

We may make acquisitions of, or significant investments in, other businesses with complementary products, services or technologies, such as our 2013 acquisition of Eolite Systems and 2014 acquisition of the Semiconductor Systems business from GSI Group, Inc. Acquisitions involve numerous risks, many of which are unpredictable and beyond our control, including:

- difficulties and increased costs in connection with integration of personnel, operations, technologies and products of the acquired businesses;
- implementation of our enterprise resource planning (ERP) system into the acquired company's operations;
- diversion of management's attention from other operational matters;
- the potential loss of key employees of the acquired company;
- lack of synergy or inability to realize expected synergies resulting from the acquisition;
- acquired assets becoming impaired as a result of technological advancements or worse-than-expected performance by the acquired company;
- difficulties establishing satisfactory internal controls at the acquired company;
- risks and uncertainties relating to the performance of the combined company following the transaction; and
- acquiring unanticipated liabilities for which we will not be indemnified.

Furthermore, the accounting for an acquisition could result in significant charges resulting from amortization or write-off of intangible assets we acquire. Our inability to effectively manage these risks could result in our inability to realize the anticipated benefits of an acquisition on a timely basis, or at all, and materially and adversely affect our business, financial condition and results of operations. In addition, all acquisition transaction costs must be expensed as incurred rather than capitalized, which may have a material adverse effect on our results of operations.

The means by which we finance an acquisition may also significantly affect our business or the value of the shares of our common stock. If we issue common stock to pay for an acquisition, the ownership percentage of our existing shareholders will be diluted and the value of the shares held by our existing shareholders could be reduced. If we use cash on hand to pay for an acquisition, the payment could significantly reduce the cash that would be available to fund our operations or to use for other purposes. If we borrow funds in connection with an acquisition, we would be required to use cash to service the debt and to comply with financial and other covenants.

We may from time to time also make strategic investments in development stage companies. Investments in development stage companies are subject to a high degree of risk. We could lose all or a portion of our investment in any such company or could be required to recognize an impairment charge with respect to our investment. For example, in 2014 we recognized a \$9.7 million impairment with respect to our investment in OmniGuide, Inc. based upon a reduction in the investment's estimated fair value.

Hiring and Retention of Personnel

Our continued success depends in part upon the services of our key managerial, financial and technical personnel. The loss of key personnel, or our inability to attract, assimilate and retain qualified personnel, could result in the loss of customers, inhibit our ability to operate and grow our business and otherwise have a material adverse effect on our business and results of operations. We have previously had to, and may in the future have to, impose salary reductions on employees during economic downturns in an effort to maintain our financial position. On several occasions in recent years executives and other employees have received limited or no annual bonuses due to our financial performance relative to the performance parameters in our annual bonus plans. These events may have an adverse effect on employee loyalty and may make it more difficult for us to attract and retain key personnel. Competition for qualified personnel in the industries in which we compete is intense, and we

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may not be successful in attracting and retaining qualified personnel. We may incur significant costs in our efforts to recruit and retain key personnel, which could affect our financial position and results of operations.

Our ability to retain key personnel and execute our strategy may also be adversely affected by the transition to a new CEO. In February 2014 Edward C. Grady became our President and Chief Executive Officer, replacing Nicholas Konidaris who held the position since 2004.

Need to Broaden our Marketing and Channel Capability

The laser microfabrication industry is comprised of a broad set of markets and applications and represents significant opportunities for growth. In order to access these opportunities, we need to broaden our approach from being customer-centric to being market-based. This will require the hiring, development, and application of new marketing capability and channel access. Our ability to successfully access and compete in these broader markets will be partially dependent on our development of these new skills and capabilities. Our inability to do so may harm our business and adversely affect our revenues and profitability.

Risks Related to Technology

Markets Characterized by Rapid Technological Change

The markets for our products are characterized by rapid technological change and innovation, frequent new product introductions, changes in customer requirements and evolving industry standards. Our future performance will depend on the successful development, introduction and market acceptance of new and enhanced products that address technological changes and the requirements of current and potential customers. The development of new, technologically advanced products is a complex and uncertain process, requiring high levels of innovation and highly skilled engineering and development personnel, as well as the accurate anticipation of technological and market trends. We cannot assure you that we will be able to identify, develop, manufacture, market or support new or enhanced products successfully, if at all, or on a timely basis. The introduction by us or by our competitors of new or enhanced products, or alternative technologies, may cause our customers to defer, change or cancel orders for our existing products or cease purchasing our products altogether. Further, we cannot assure that our new products will gain timely market acceptance or that we will be able to respond effectively to product announcements by competitors, technology changes or emerging industry standards. If we are unable to develop new or enhanced products to address product or technology changes or new industry standards on a timely basis or at all, or if our new or enhanced products are not accepted by the market, or if our customers adopt alternative technologies, our business, financial condition and results of operations may be adversely affected.

Need to Invest in Research and Development

Our industry is characterized by the need for continued investment in research and development. Because of intense competition in the industries in which we compete, if we were to fail to invest sufficiently in research and development, our products could become less attractive to our current and potential customers or obsolete, and our business and financial condition could be materially and adversely affected. We also will incur research and development expenses as we develop products for the adjacent markets we intend to enter. As a result of our need to maintain our spending levels in this area, our operating results could be materially harmed if our net sales decline. In addition, as a result of our emphasis on research and development and technological innovation, our operating costs may increase in the future, and research and development expenses may increase as a percentage of total operating expenses and as a percentage of net sales.

Products are Highly Complex

Our products are highly complex, and our extensive product development, manufacturing and testing processes may not be adequate to detect all defects, errors, failures and quality issues that could impact customer satisfaction or result in claims against us. As a result, we may have to replace certain components or provide remediation in response to the discovery of defects in products after they are shipped. The occurrence of any defects, errors, failures or quality issues could result in cancellation of orders, product returns, diversion of our resources, legal actions by our customers and other losses to us or to our customers. These occurrences could also result in the loss of, or delay in, market acceptance of our products, loss of sales and increased expenses and warranty costs, which would harm our business and adversely affect our revenues and profitability.

Risks Related to Legal Matters

Protection of Proprietary Rights – Generally

Our success depends significantly upon the protection of our proprietary rights. We attempt to protect our proprietary rights through patents, copyrights, trademarks, maintenance of trade secrets and other measures, including entering into confidentiality agreements. We incur substantial costs to obtain and maintain patents and to defend our intellectual property

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rights. We rely upon the laws of the United States and foreign countries where we develop, manufacture or sell our products to protect our proprietary rights. We may not be successful in protecting these proprietary rights, these rights may not provide the competitive advantages that we expect, or other parties may challenge, invalidate or circumvent these rights.

Protection of Proprietary Rights – Foreign Jurisdictions

Our efforts to protect our intellectual property may be less effective in some foreign countries where intellectual property rights are not as well protected as in the United States. Many United States companies have encountered substantial problems in protecting their proprietary rights against infringement in foreign countries. If we fail to adequately protect our intellectual property in these countries, it could be easier for our competitors to sell competing products in foreign countries, which could result in reduced sales and gross margins.

Intellectual Property Infringement Claims

Several of our competitors hold patents covering a variety of technologies, applications and methods of use similar to some of those used in our products. While we attempt in our designs to avoid patent infringement, from time to time we and our customers have received correspondence from our competitors claiming that some of our products, as used by our customers, may be infringing one or more of these patents. Competitors or others have in the past and may in the future assert infringement claims against our customers or us with respect to current or future products or uses, and these assertions may result in costly litigation or require us to obtain a license to use intellectual property rights of others. If claims of infringement are asserted against our customers, those customers may seek indemnification from us for damages or expenses they incur.

If we become subject to infringement claims, we will evaluate our position and consider the available alternatives, which may include seeking licenses to use the technology in question or defending our position. These licenses, however, may not be available on satisfactory terms or at all. If we are not able to negotiate the necessary licenses on commercially reasonable terms or successfully defend our position, our financial condition and results of operations could be materially and adversely affected.

We also defend our patent and intellectual property portfolio. We initiated litigation in 2014 against each of Humo Laboratory, LTD. in Japan and Eo Technics Co., Ltd., in South Korea for infringement of key patents. There is no assurance that this litigation will be successful, and we may incur significant legal fees to prosecute these claims.

Tax Audits and Changes in Tax Law

We are periodically under audit by United States and foreign tax authorities and may have exposure to additional tax liabilities as a result. Significant judgment is required in determining our provision for income and other tax liabilities. Although we believe our tax estimates are reasonable, the final outcome of tax audits and the impact of changes in tax laws or the interpretation of tax laws could result in material differences from what is reflected in historical income tax accruals. If additional taxes are assessed as a result of an examination, a material effect on our financial results, tax positions or cash flows could occur in the period or periods in which the determination is made.

We currently benefit from a tax incentive program in Singapore pursuant to which we pay no Singapore income tax with respect to our manufacturing income. The incentive commenced on July 1, 2006 and will continue through June 30, 2016 assuming we are able to satisfy applicable requirements. The Company has failed to meet certain of the associated requirements in the past, and has obtained a waiver for certain periods. There is no assurance we will be able to satisfy these requirements and failure to meet such requirements may lead to reduction in future or past tax benefits. The Company believes that it is more likely than not the Company will continue to receive the associated tax incentives and there is no indication that past benefits received would be rescinded.

Legal Proceedings

From time to time we are subject to various legal proceedings, including breach of contract claims and claims that involve possible infringement of patent or other intellectual property rights of third parties or by third parties. It is inherently difficult to assess the outcome of litigation matters, and there can be no assurance that we will prevail in any litigation. Any litigation could result in substantial cost and diversion of management's attention, which by itself could have a material adverse effect on our financial condition and results of operations. Further, adverse determinations in such litigation could result in loss of our property rights, subject us to significant liabilities, require us to seek licenses from others or prevent us from manufacturing or selling our products, any of which could materially adversely affect our business, financial condition, results of operations or cash flows.

Provisions Restricting Our Acquisition

Our articles of incorporation and bylaws contain provisions that could make it harder for a third party to acquire us without the consent of our Board of Directors. Our Board of Directors has also adopted a shareholder rights plan, or “poison pill,” which would significantly dilute the ownership of a hostile acquirer. In addition, the Oregon Control Share Act and the Oregon Business Combination Act limit the ability of parties who acquire a significant amount of voting stock to exercise control over us. These provisions may have the effect of lengthening the time required for a person to acquire control of us through a proxy contest or the election of a majority of our Board of Directors, may deter efforts to obtain control of us and may make it more difficult for a third party to acquire us without negotiation. These provisions may apply even if the offer may be considered beneficial by our shareholders.

Risks Related to Financial Matters

Unfavorable Currency Exchange Rate Fluctuations

Currency exchange rate fluctuations could have an adverse effect on our sales and results of operations and we could experience losses with respect to forward exchange contracts into which we may enter. Unfavorable currency fluctuations could require us to increase prices to foreign customers, which could result in lower net sales by us to those customers. Alternatively, if we do not adjust the prices for our products in response to unfavorable currency fluctuations, our results of operations could be materially and adversely affected. In addition, some of our foreign sales are denominated in the currency of the country in which these products are sold and the currency we receive in payment for such sales could be less valuable at the time of receipt as a result of exchange rate fluctuations. From time to time, we enter into forward exchange contracts to hedge the value of accounts receivable primarily denominated in euros and other currencies. However, we cannot be certain that our efforts will be adequate to protect us against significant currency fluctuations or that such efforts will not expose us to additional exchange rate risks, which could adversely affect our results of operations.

Fluctuations in Effective Tax Rate

As a global company, we are subject to taxation in the United States and numerous foreign jurisdictions. Our effective tax rate is subject to fluctuation from one period to the next because the income tax rates for each year are a function of many factors, including: (a) taxable income levels and the effects of a mix of profits (losses) earned by ESI and our subsidiaries in numerous tax jurisdictions with a broad range of income tax rates; (b) our ability to utilize deferred tax assets; (c) taxes, refunds, interest or penalties resulting from tax audits; (d) the magnitude of various credits and deductions as a percentage of total taxable income; and (e) changes in tax laws or the interpretation of such tax laws. In addition, we currently have a valuation allowance against domestic tax assets as a result of historic losses recorded in the United States. Changes in the mix of these items may cause our effective tax rate to fluctuate between periods, which could have a material adverse effect on our financial position and results of operations.

Impairment of Intangible Assets

We held a total of \$6.3 million in acquired intangible assets and \$7.9 million in goodwill at June 28, 2014. We review our acquired intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. We test goodwill for impairment using a quantitative approach at least annually or between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value below the carrying value.

We performed a review of our acquired intangible assets in the fourth quarter of 2014, including a review for impairment based on certain triggering events and no significant impairments of intangible assets were detected.

We performed our annual goodwill impairment analysis during the fourth quarter of 2014 and determined that goodwill was not impaired. If at any time management determines that an impairment exists the Company may be required to record the impairment as part of operating income, which will result in a reduction in earnings and a corresponding reduction in our net asset value in the period such impairment is identified. The assessment of whether goodwill is impaired is sensitive to stock price and the assumed control premium. A significant deterioration in either may trigger impairment. Our stock price has recently traded around or below our book value of equity, thereby placing more emphasis on the determination of a reasonable control premium.

Stock Price Volatility

The market price of our common stock has fluctuated widely. During the first quarter of 2015, our stock price fluctuated between a high of \$10.01 per share and a low of \$6.68 per share, and subsequent to the end of the fiscal quarter and prior to August 1, 2014 has been as low as \$5.98. Consequently, the current market price of our common stock may not be indicative of future market prices, and we may be unable to sustain or increase the value of an investment in our common stock. Factors affecting our stock price, many of which are outside of our control, may include:

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- variations in operating results from quarter to quarter;
- changes in earnings estimates by analysts or our failure to meet analysts' expectations;
- changes in the market price per share of our public company customers;
- market conditions in the consumer electronics, semiconductor and other industries into which we sell products;
- general economic conditions;
- political changes, hostilities or natural disasters;
- low trading volume of our common stock;
- change in our dividend policy;
- the number of analysts covering our common stock; and
- the number of firms making a market in our common stock.

In addition, the stock market has experienced significant price and volume fluctuations in recent years. These fluctuations have particularly affected the market prices of the securities of high-technology companies like ours. These market fluctuations could adversely affect the market price of our common stock.

Reduction or Cessation of Dividends

Our Board of Directors first adopted a dividend policy in December 2011. We intend to pay quarterly dividends subject to capital availability and periodic determinations by our Board of Directors that cash dividends are in the best interest of our shareholders and are in compliance with all laws and agreements applicable to the declaration and payment of cash dividends. Future dividends may be affected by, among other factors: our views on overall levels of current or projected profitability; potential future capital requirements for investments in acquisitions; funding of research and development; legal risks; stock repurchase programs; changes in federal and state income tax laws or corporate laws; and changes to our business model. Our dividend payments may change from time to time, and we cannot provide assurance that we will continue to declare dividends at all or in any particular amounts. Further, the special dividend declared by the Board of Directors in December 2012 should not be considered a recurring event. A reduction or cessation in our dividend payments could have a negative effect on our stock price.

Impairment of Investments

Our investment portfolio is primarily comprised of commercial paper, debt securities issued by U.S. governmental agencies and municipal debt securities. These investments are intended to be highly liquid and low risk. If the markets for these securities were to deteriorate for any reason, including as a result of a downgrade in the credit rating of U.S. government securities, the liquidity and value of these investments could be negatively affected, which could result in impairment charges. Any such impairment charges may have a material impact on our financial condition and results of operations.

Item 2. Share Repurchase Program

In December 2011, the Board of Directors authorized a share repurchase program totaling \$20.0 million to acquire shares of our outstanding common stock. The repurchases are to be made at management's discretion in the open market or in privately negotiated transactions in compliance with applicable securities laws and other legal requirements and are subject to market conditions, share price and other factors.

In the first quarter of 2015 the Company repurchased 207,738 shares for \$1.5 million under this authorization at an average price of \$7.01 per share, calculated inclusive of commissions and fees. Cash used to settle the repurchase transactions as of June 28, 2014 totaled \$1.3 million and is reflected as a component of cash used in financing activities on the Consolidated Statements of Cash Flows. Accrued liabilities include \$0.2 million for amounts owed on the unsettled repurchase transactions as of June 28, 2014. In 2014 the Company repurchased 19,832 shares for \$0.2 million at an average price of \$9.65 per share. The Company has repurchased a total of 227,570 shares life to date under this authorization as a part of its publicly announced plan.

There is no fixed completion date for the repurchase program. The following table provides information with respect to share repurchases by the Company during 2015 and 2014.

Fiscal Period	Total number of shares purchased	Average price paid per share	Total value of shares repurchased	Maximum value of shares that may yet be purchased under the program
June FY 2015 (06/01/2014 to 06/28/2014)	68,750	\$6.89	\$0.5 million	\$18.3 million
May FY 2015 (05/04/2014 to 05/31/2014)	138,988	\$7.07	\$1.0 million	\$18.8 million

Item 4. Mine Safety Disclosures

Not Applicable.

Item 6. Exhibits

This list is intended to constitute the exhibit index.

3.1	Third Restated Articles of Incorporation, as amended. Incorporated by reference to Exhibit 3.1 of the Company's Annual Report on Form 10-K for the fiscal year ended April 3, 2010.
3.2	2009 Amended and Restated Bylaws, as amended. Incorporated by reference to Exhibit 3.1 of the Company's Current Report on Form 8-K filed on November 9, 2012.
4.1	Rights Agreement, dated as of May 18, 2009, between Electro Scientific Industries, Inc. and Mellon Investor Services. Incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed on May 19, 2009.
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document *
101.SCH	XBRL Taxonomy Extension Schema Document *
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document *
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document *
101.LAB	XBRL Taxonomy Extension Label Linkbase Document *
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document *

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities and Exchange Act of 1934, and otherwise are not subject to liability under those sections.

**CERTIFICATION PURSUANT TO
SECTION 302(a) OF THE SARBANES-OXLEY ACT OF 2002**

I, Edward C. Grady, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Electro Scientific Industries, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 7, 2014

/s/ Edward C. Grady

Edward C. Grady

President and Chief Executive Officer

**CERTIFICATION PURSUANT TO
SECTION 302(a) OF THE SARBANES-OXLEY ACT OF 2002**

I, Paul Oldham, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Electro Scientific Industries, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 7, 2014

/s/ Paul Oldham

Paul Oldham

Vice President of Administration,

Chief Financial Officer and Corporate Secretary

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with this quarterly report on Form 10-Q of Electro Scientific Industries, Inc. (the Company) for the quarterly period ended June 28, 2014 as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Edward C. Grady, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Edward C. Grady

Edward C. Grady

President and Chief Executive Officer

August 7, 2014

This certification is made solely for the purpose of 18 U.S.C. Section 1350, and not for any other purpose. A signed original of this written statement required by Section 906 has been provided to Electro Scientific Industries, Inc. and will be retained by Electro Scientific Industries, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with this quarterly report on Form 10-Q of Electro Scientific Industries, Inc. (the Company) for the quarterly period ended June 28, 2014 as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Paul Oldham, Vice President of Administration, Chief Financial Officer, and Corporate Secretary of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Paul Oldham

Paul Oldham

Vice President of Administration,

Chief Financial Officer and Corporate Secretary

August 7, 2014

This certification is made solely for the purpose of 18 U.S.C. Section 1350, and not for any other purpose. A signed original of this written statement required by Section 906 has been provided to Electro Scientific Industries, Inc. and will be retained by Electro Scientific Industries, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

