COGNEX CORP

FORM 10-K
(Annual Report)

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

FORM 10-K

(Mark One)

☑ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2004 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 0-17869

COGNEX CORPORATION

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2713778**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

One Vision Drive
Natick, Massachusetts 01760-2059
(508) 650-3000

(Address, including zip code, and telephone number, including area code, of principal executive offices)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value $.002 per share

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes ☑ No ☐

Aggregate market value of voting stock held by non-affiliates of the registrant as of July 2, 2004: $1,557,248,000

$.002 par value common stock outstanding as of February 27, 2005: 46,269,923 shares

Documents incorporated by reference:

The registrant intends to file a Definitive Proxy Statement pursuant to Regulation 14A within 120 days of the end of the fiscal year ended December 31, 2004. Portions of such Proxy Statement are incorporated by reference in Part III of this report. Portions of the registrant's Annual Report to Shareholders for the year ended December 31, 2004 are incorporated by reference in Part I and Part II of this report.

**COGNEX CORPORATION ANNUAL REPORT ON
FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2004**

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PART I

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Federal Securities Laws. Readers can identify these forward-looking statements by the Company's use of the words "expects," "anticipates," "estimates," "believes," "projects," "intends," "plans," "will," "may," "shall," and similar words and other statements of a similar sense. The Company's future results may differ materially from current results and from those projected in the forward-looking statements as a result of known and unknown risks and uncertainties. Readers should pay particular attention to considerations described in the section captioned "Risk Factors," appearing in Part I — Item I of this Annual Report on Form 10-K.

ITEM 1. *BUSINESS*

Corporate Profile

Cognex® Corporation ("Cognex" or the "Company," each of which includes, unless the context indicates otherwise, Cognex Corporation and its subsidiaries) was incorporated in Massachusetts in 1981. Its corporate headquarters are located at One Vision Drive, Natick, Massachusetts 01760 and its telephone number is (508) 650-3000.

The Company designs, develops, manufactures, and markets machine vision systems, or computers that can "see," which are used to automate a wide range of manufacturing processes where vision is required. Machine vision is important for applications in which human vision is inadequate to meet requirements for feature size, accuracy, or speed, or in instances where substantial cost savings are obtained through the reduction of direct labor or improved product quality. Today, many types of manufacturing equipment require machine vision because of the increasing demands for speed and accuracy in manufacturing processes, as well as the decreasing feature size of items being manufactured.

The Company has two operating divisions: the Modular Vision Systems Division (MVSD), based in Natick, Massachusetts, and the Surface Inspection Systems Division (SISD), based in Alameda, California. MVSD designs, develops, manufactures, and markets modular vision systems that are used to automate the manufacture of discrete items, such as semiconductor chips, cellular phones, and light bulbs, by locating, identifying, inspecting, and measuring them during the manufacturing process. SISD designs, develops, manufactures, and markets surface inspection vision systems that are used to inspect the surfaces of materials processed in a continuous fashion, such as paper, metals, plastics, and non-wovens, to ensure there are no flaws or defects on the surfaces. Historically, MVSD has been the source of the majority of the Company's revenue, representing approximately 86% of total revenue in 2004.

What is Machine Vision?

Since the beginning of the Industrial Revolution, human vision has played an indispensable role in the process of manufacturing products. Human eyes did what no machines could do themselves: locating and positioning work, tracking the flow of parts, and inspecting output for quality and consistency. Today, however, the requirements of many manufacturing processes have surpassed the limits of human eyesight. Manufactured items often are produced too quickly or with tolerances too small to be analyzed by the human eye. In response to manufacturers' needs, "machine vision" technology emerged, providing manufacturing equipment with the gift of sight. The Company believes that virtually every manufacturer that makes products in an automated process can achieve better quality and manufacturing efficiency by using machine vision.

Machine vision systems combine cameras with intelligent software to collect images and then answer questions about these images, such as:

Question	Description	Example
GUIDANCE Where is it?	Determining the exact physical location and orientation of an object.	Determining the position of a printed circuit board so that a robot can automatically be guided to insert electronic components.
IDENTIFICATION What is it?	Identifying an object by analyzing its shape or by reading a serial number.	Identifying the serial number on an automotive airbag so that it can be tracked and processed correctly through manufacturing.
INSPECTION How good is it?	Inspecting an object for flaws or defects.	Inspecting the paper that US currency is printed on.
GAUGING What size is it?	Determining the dimensions of an object.	Determining the diameter of a bearing prior to final assembly.

Machine Vision Market

The Company's customers can be classified into three categories: semiconductor and electronics capital equipment manufacturers, discrete manufacturing customers, and surface inspection customers. Semiconductor and electronics capital equipment manufacturers purchase Cognex modular vision systems and integrate them into the capital equipment that they manufacture and then sell to their customers in the semiconductor and electronics industries that either make computer chips or make printed circuit boards containing computer chips. Although the Company sells to original equipment manufacturers (OEMs) in a number of industries, these semiconductor and electronics OEMs have historically been large consumers of the Company's products. Sales to semiconductor and electronics capital equipment manufacturers represented approximately 42% of the Company's total revenue in 2004.

The discrete manufacturing category includes a wide array of manufacturers who use machine vision for applications in a variety of industries, including the packaging, automotive, consumer electronics, food and beverage, and personal care industries. The majority of these customers are end users who purchase Cognex modular vision systems and install them directly on their production lines. Unlike OEMs and system integrators, these customers typically have limited computer programming or machine vision experience. The Company sells its products to end users through its own direct sales force, as well as through distributors and system integrators. System integrators are companies that create complete automated inspection solutions for end users. For example, they combine lighting, conveyors, robotics, machine vision, and other components to produce custom inspection systems for various applications. Sales to discrete manufacturing customers represented approximately 44% of the Company's total revenue in 2004.

The last category, surface inspection customers, includes manufacturers of materials processed in a continuous fashion, such as paper and steel. These customers need sophisticated machine vision to detect and classify defects in the surfaces of those materials as they are being processed at high speeds. Surface inspection sales represented approximately 14% of the Company's total revenue in 2004.

Business Strategy

The Company's goal is to expand its position as a leading worldwide supplier of machine vision systems for factory automation by offering a complete family of machine vision products to a broad base of manufacturers. Semiconductor and electronics equipment manufacturers have historically been large consumers of the Company's products. Over the past few years, however, the Company has diversified its customer base beyond the semiconductor and electronics capital equipment sector. Demand from these capital equipment manufacturers is highly cyclical, with periods of investment followed by temporary downturns. At its peak in 2000, sales to semiconductor and electronics capital equipment manufacturers represented approximately 61% of the Company's total revenue, compared to approximately 42% in 2004.

The Company believes that long-term, sustained revenue growth will come from a broad base of manufacturers outside of the semiconductor and electronics capital equipment manufacturer sector. Accordingly, the Company has invested in expanding its product offerings to its discrete manufacturing customers, who demand a wide range of easy-to-use products of varying capability and price, and in developing a strong worldwide sales and support infrastructure. The Company intends to continue to defend its strong position in the semiconductor and electronics capital equipment sector, while selectively expanding into new machine vision applications through the internal development of new products, as well as the acquisition of businesses and technologies.

Products

Cognex offers a full range of machine vision systems designed to meet customer needs at virtually any stage of the manufacturing process and virtually any capability/price point.

In-Sight Vision Sensors

The Company believes that it is firmly positioned in the fast-growing market for vision sensors with its In-Sight® product line. Vision sensors are machine vision systems that combine a video camera, software, vision processor, and input/output capability in a low-cost, compact, easy-to-use package. These general-purpose vision sensors are designed to be easily programmed to perform a wide range of vision tasks including part location, identification, measurement, and assembly verification.

In 2004, the Company introduced the In-Sight 5000 series, with increased processing power and a rugged, industrial-grade package that meets high standards for shock, vibration, and dust and wash-down protection.

In-Sight is sold to end users located in North America, Japan, Europe, and Southeast Asia in a wide range of general manufacturing industries, such as medical devices, automotive parts, disposable consumer goods, and electronic components.

Expert Sensors

Unlike general-purpose vision sensors that can be programmed to solve a wide variety of vision tasks, expert sensors are designed to deliver very simple, low-cost solutions for specific automation problems.

Late in 2004, the Company introduced Checker™ 101, its lowest cost and easiest-to-use vision sensor designed to detect the presence or absence of multiple product features. Performing this common vision task provides manufacturers with a reliable and cost effective way to check 100% of their products during the manufacturing process, instead of relying upon random sampling at the end of the production line. Checker is currently sold primarily in North America to end users in a wide range of general manufacturing industries, although the Company intends to market Checker worldwide. Because of its low price and ease of use, the Company expects to solve many new manufacturing problems with its Checker series of products.

The CPS-1000 is a vision sensor designed for door security; it detects and counts people as they pass through an access-controlled doorway. The CPS-1000 utilizes Cognex's existing vision software, as well as patented 2D and 3D vision technology that Cognex developed specifically for "people sensing" applications. The CPS-1000 is currently sold to OEM customers located in North America.

ID Products

The Company's ID products are designed to quickly and reliably read codes (e.g. serial numbers, bar codes, or two-dimensional codes) that have been stamped, scribed, etched, printed, or otherwise formed directly on the surfaces of manufactured goods ranging from pharmaceutical items to aircraft components to semiconductor wafers. Industrial ID, or Direct Part Marking, is an increasingly critical tool to ensure the appropriate manufacturing processes are performed in the correct sequence on the right parts. In addition, it can be used to create a history of the part from the beginning of its life to the end, and for use in supply chain management and repair.

In 2004, the Company introduced the In-Sight 5110 fixed-mount Industrial ID reader and the DataMan™ 6400 and DataMan 6500 hand-held Industrial ID readers. Each model incorporates IDMax™ software, new Data Matrix code-reading software based upon Cognex PatMax® technology. IDMax reads reliably despite degradations to the appearance of the code. In addition, the Company's In-Sight 1700 series of Wafer ID readers identifies and tracks semiconductor wafers through the manufacturing process.

ID products are sold to OEMs, system integrators, and end users located in North America, Japan, Europe, and Southeast Asia in a wide range of industries.

PC-Based Vision Systems

The Company sells a full range of PC-based vision systems that combine the power and flexibility of advanced programming with the simplicity of a graphical programming environment. These products contain the Company's most extensive library of vision software tools featuring PatMax, high-accuracy pattern location software that can locate objects that vary in size and orientation or whose appearance is degraded, and PatFlex, which enables a vision system to locate an object, feature, or pattern whose perspective has changed or whose surface is curved, warped, wrinkled, or stretched.

MVS-8000 Product Family

The MVS-8000™ family of programmable machine vision systems combines Cognex's unique algorithms with Intel's MMX instruction set. The MVS-8100 Series features PCI bus-mastering frame grabbers for high-speed image transfer from the video camera to the host PC for processing and display. The MVS-8200 Series of embedded CPU machine vision systems enables all vision processing to occur on-board, freeing the PC to perform other tasks. The MVS-8500 Series of frame grabbers are designed to support next-generation, high-speed analog cameras that use the latest progressive scan CCD sensor technology.

The MVS-8000 product family is sold primarily to OEMs located in North America, Japan, Europe, and Southeast Asia who integrate the machine vision systems into capital equipment for the semiconductor and electronics industries. These vision systems are also sold to system integrators located in North America, Japan, Europe, and Southeast Asia who integrate them into capital equipment for end users in a broad range of industries.

VisionPro Product Family

VisionPro® is an Active X-based vision system that combines Cognex machine vision technology with quick and powerful application development. These PC-based systems offer the flexibility of an advanced programming language with the simplicity of graphical prototyping, speeding time-to-market for OEMs, system integrators, and advanced manufacturing engineers. VisionPro's powerful software, combined with Cognex MVS-8100 and 8500 Series frame grabbers, provide a complete vision system to solve demanding applications.

The VisionPro product family is sold to OEMs, system integrators, and end users located in North America, Japan, Europe, and Southeast Asia in a wide range of industries.

Application Specific PC-based Vision Systems

The Company offers a variety of application-specific systems that combine Cognex PC-based hardware and software to create a solution that is tailored to the particular requirements of certain vision applications. A partial list of application-specific vision systems is as follows:

SMD 4 ™ guides the placement of surface mount devices onto printed circuit boards and other assemblies.

BGA II ™ inspects ball grid array devices for missing, misplaced, or improperly formed solder balls.

Fiducial Finder II ™ locates fiducial or alignment marks on printed circuit boards for automatic printed circuit board alignment.

DisplayInspect ® inspects the small, high-resolution displays commonly found on cellular phones, pagers, medical test instruments, and other electronic devices.

FiberInspect ™ is a machine vision system specifically designed to automatically detect and measure scratches, cracks, and spots that form during the fiber end polishing process.

TIS-8000 ™ *Tire Identification System and WIS-8000* ™ *Wheel Identification System* are high-performance identification systems for automatically identifying tires and wheels by their unique characteristics. The systems ensure the presence of correct tires or wheels at any point in the manufacturing or assembly process.

Application-specific systems are targeted to OEMs, system integrators, and end users located in North America, Japan, Europe, and Southeast Asia in a wide range of industries, depending upon the application.

Digital Cameras for PC-Based Products

The Company designs, develops, manufactures, and markets the CDC Series of digital Complementary Metal-Oxide Semiconductor (CMOS) cameras designed specifically for machine vision applications. CDC cameras are designed for use with the MVS-8100D digital frame grabber. These products, in combination with Cognex's vision software, provide a complete, tightly-integrated solution to the Company's PC-based vision customers.

Surface Inspection Systems

The SmartView® surface/web inspection system provides reliable detection, identification, and visualization of defects on products that are manufactured in a continuous process. The SmartView system provides greyscale imaging capability to visualize the defects, as well as a high-quality snapshot of the inspected surface or web. Most advanced open data access capabilities embedded into the SmartView system ensure real-time inspection control and data access between the SmartView system and other business, production, and quality systems in the mill. The SmartView system is a modular and scalable system on a Microsoft Windows-based platform that enables the Company to expand into more complex vision applications in the paper, metals, plastics, and nonwovens industries.

SmartView is sold primarily to end users located in North America, Japan, Europe, and Southeast Asia in the paper, metals, plastics, and nonwovens industries. In addition, SmartView is sold to end users located in Europe and Asia in the paper industry through an OEM relationship with Honeywell International, Inc.

Research, Development, and Engineering

The Company engages in research, development, and engineering (R, D & E) to enhance its existing products and to develop new products and functionality to meet market opportunities. In addition to internal research and development efforts, the Company intends to continue its strategy of gaining access to new technology through strategic relationships and acquisitions where appropriate. The Company considers its on-going efforts in R, D & E to be a key component of its strategy.

At December 31, 2004, the Company employed 157 professionals in R, D & E, most of whom are software developers. The Company's R, D & E expenses totaled $27,063,000, $24,719,000, and $25,630,000, or approximately 14%, 17%, and 23% of revenue, in 2004, 2003, and 2002, respectively.

Manufacturing

The Company's MVSD manufacturing organization utilizes a turnkey operation whereby the majority of component procurement, subassembly, final assembly, and initial testing are performed under agreement by third-party contract manufacturers. After the completion of initial testing, the contract manufacturers deliver the products to the Company's Natick, Massachusetts facility for final testing, quality control, and shipment to the customer. The contract manufacturers use specified components and assembly and test documentation created and controlled by the Company. From time to time, the Company will procure large quantities of end-of-life components for strategic purposes that will not be consumed within one year. Certain components are presently available only from a single source.

The Company's SISD products are manufactured at its Alameda, California facility, with the exception of the frames on which the cameras are mounted. The manufacturing process at the Alameda facility consists of system design, configuration management and control, component procurement, and subassembly. After the completion of subassembly at the Alameda facility, some of the systems are delivered to the Company's Kuopio, Finland facility where the frames are manufactured. The manufacturing process at the Kuopio facility consists of system integration with the frames, final testing, quality control, and shipment to the customer. Certain products are manufactured by third-party contract manufacturers using documentation created and controlled by the Company. Certain components are presently available only from a single source.

Sales and Service

The Company sells its MVSD and SISD products primarily through a direct sales force in North America, Japan, Europe, and Southeast Asia. In addition, the Company is developing an indirect sales channel of distributors to sell its low-cost vision sensors in the United States. The Company intends to expand this distribution network outside of the United States. At December 31, 2004, the Company's direct sales force consisted of 202 professionals, including sales and application engineers. The majority of the Company's sales force holds engineering or science degrees. Sales engineers call directly on targeted accounts and coordinate the activity of the application engineers.

Sales to customers based outside of the United States represented approximately 69% of total revenue in 2004, compared to approximately 66% in 2003 and approximately 60% in 2002. No customer accounted for greater than 10% of revenue in 2004, 2003, or 2002. Although international sales may from time to time be subject to federal technology export regulations, to date the Company has not suffered significant delays or prohibitions in sales to any of its foreign customers. Financial information about segments and geographic areas may be found in the Notes to the Consolidated Financial Statements, appearing on pages 67 and 68 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

The Company's MVSD service offerings include maintenance and support, education, and consulting services. Maintenance and support programs include hardware support programs that entitle customers to have failed product repaired, as well as software support programs that provide customers with application support and software updates on the latest software releases. Education services include a variety of product courses that are available at the Company's offices worldwide, at customer facilities, and on computer-based tutorials, video, and the Internet. The Company provides consulting services that range from a specific area of functionality to a completely integrated machine vision application.

The Company's SISD service offerings include maintenance and support and education services similar to those provided by MVSD, as well as installation services. The installation services group supervises the physical installation of the hardware at the customer location, configures the software application to detect the customer's defects, validates that the entire integrated system with the peripheral components is functioning according to the specifications, and performs operator training.

Intellectual Property

Because the Company relies on the technical expertise, creativity, and knowledge of its personnel, it utilizes patent, trademark, copyright, and trade secret protection to safeguard its competitive position. At December 31, 2004, the Company had obtained 202 patents on various innovations in the field of machine vision technology and had more than 106 patent applications pending. In addition, the Company makes use of non-disclosure agreements with customers, suppliers, employees, and consultants. The Company attempts to protect its intellectual property by restricting access to its proprietary information by a combination of technical and internal security measures. There can be no assurance, however, that any of the above measures will be adequate to protect the proprietary technology of the Company. Moreover, effective patent, trademark, copyright, and trade secret protection may be unavailable in certain foreign countries.

The Company's trademark and servicemark portfolio includes various registered marks, including but not limited to, Cognex ®, PatMax ®, VisionPro ®, In-Sight ®, DisplayInspect ®, and SmartView ®, as well as many common-law marks, including but not limited to, Checker ™ and DataMan ™. In addition, the Company has sought and obtained a number of trademark registrations outside of the United States. All third-party brand names, servicemarks, and trademarks referenced in this document are the property of their respective owners.

The Company's software products are protected by various security schemes and are primarily licensed to customers pursuant to a license agreement that restricts the use of the products to the customer's purposes, as well as imposes strict limitations on the customer's use of the Company's trade secret, proprietary, and other confidential business information to which the customer may have access. The Company has made portions of its source code available to certain customers under very limited circumstances and for restricted uses. If the source code is released to a customer, the customer is required by contract to maintain its confidentiality and, in general, to use the source code solely for internal purposes or for maintenance.

Numerous users of the Company's products have received notice of patent infringement from the Lemelson Medical, Educational, & Research Foundation, Limited Partnership (the "Partnership") alleging that their use of the Company's products infringes certain patents transferred to the Partnership by the late Jerome H. Lemelson. The Company does not believe its products infringe any valid and enforceable claims of the Partnership's patents.

As a result of continuing assertions against current and potential Cognex customers, the Company decided to initiate action against the Partnership in order to preserve its right to sell machine vision products without the threat of legal action against the Company or its customers. Accordingly, on September 23, 1998, the Company filed a complaint against the Partnership seeking a declaration that Lemelson's machine vision patents are invalid, unenforceable, and not infringed by either Cognex or by any users of Cognex products.

On January 23, 2004, the U.S. District Court of Nevada issued a court order ruling in favor of Cognex and finding that all of the Lemelson patent claims in suit are unenforcable, invalid, and not infringed by Cognex. On June 23, 2004, the Partnership filed a notice of appeal with respect to this decision with the U.S. Court of Appeals for the Federal Circuit. The matter has been fully briefed to the Court of Appeals which will likely render its decision during 2005. Cognex cannot predict the outcome of this appeal.

Compliance with Environmental Provisions

The Company's capital expenditures, earnings, and competitive position are not materially affected by compliance with federal, state, and local environmental provisions which have been enacted or adopted to regulate the distribution of materials into the environment.

Competition

The Company competes with other vendors of machine vision systems, the internal engineering efforts of the Company's current or prospective customers, and the manufacturers of image processing systems. Any of these competitors may have greater financial and other resources than the Company. Although the Company considers itself to be one of the leading machine vision companies in the world, reliable estimates of the machine vision market and the number of competitors are not available. The primary competitive factors affecting the choice of a machine vision system include vendor reputation, product functionality and performance, ease-of-use, price, and post-sales support.

Backlog

At December 31, 2004, the Company's backlog totaled $29,023,000, compared to $25,930,000 at December 31, 2003. Backlog reflects purchase orders for products scheduled for shipment primarily within three months at MVSD and within six months at SISD. The level of backlog at any particular date is not necessarily indicative of future revenue of the Company. The Company's low-cost vision sensors typically ship within one week of when the order is booked. In addition, delivery schedules may be extended and orders may be canceled at any time subject to certain cancellation penalties.

Employees

At December 31, 2004, the Company employed 662 persons, including 330 in sales, marketing, and service activities; 157 in research, development, and engineering; 61 in manufacturing and quality assurance; and 114 in information technology, finance, and administration. Of the Company's 662 employees, 242 are based outside of the United States. None of the Company's employees are represented by a labor union and the Company has experienced no work stoppages. The Company believes that its employee relations are good.

Risk Factors

Unfavorable changes in economic conditions and capital spending may negatively impact the Company's operating results.

The Company's revenue is dependent upon the capital spending trends of manufacturers in a number of industries and regions. These spending levels are, in turn, impacted by global economic conditions. The Company's operating results have been materially adversely affected in the past, and could be materially adversely affected in the future, as a result of unfavorable economic conditions and reduced capital spending by manufacturers worldwide.

Downturns in the semiconductor and electronics industries may adversely affect the Company's business.

In 2004, approximately 42% of the Company's revenue was derived from semiconductor and electronics capital equipment manufacturers. This concentration was as high as 61% in 2000. The semiconductor and electronics industries are highly cyclical and have historically experienced periodic downturns, which have often had a severe effect on demand for production equipment that incorporates the Company's products. While the Company has been successful in recent years in diversifying its business beyond OEM customers who serve the semiconductor and electronics industries, the Company is still largely dependent upon the capital expenditures in these industries, which, in turn, are dependent upon the market demand for products containing computer chips. As a result, the Company's operating results in the foreseeable future could be significantly and adversely affected by a slowdown in either of these industries.

Economic, political, and other risks associated with international sales and operations could adversely affect the Company's business and operating results.

In 2004, approximately 69% of the Company's revenue was derived from customers located outside of the United States. The Company anticipates that international sales will continue to account for a significant portion of its revenue. The Company intends to continue to expand its operations outside of the United States and may enter additional international markets, which will require significant management attention and financial resources. The Company's operations are subject to the risks inherent in international sales, including, but not limited to, various regulatory requirements, transportation delays, difficulties in staffing and managing foreign sales operations, and potentially adverse tax consequences. In addition, fluctuations in foreign currency exchange rates may render the Company's products less competitive relative to local product offerings, or could result in significant foreign currency losses if not properly hedged. The Company is also subject to the political risks inherent in international operations and their impact on the global economy, including economic disruption from acts of war or terrorism, particularly in the aftermath of the terrorist attacks of September 11, 2001. Any of these factors could have a material adverse effect on the Company's operating results.

Fluctuations in foreign exchange rates could materially affect the Company's reported results.

The Company faces exposure to adverse movements in foreign currency exchange rates as a significant portion of its revenue, expenses, assets, and liabilities are denominated in currencies other than the functional currencies of the Company or its subsidiaries. In certain instances, the Company utilizes derivative instruments to hedge against certain foreign currency fluctuations. These contracts are used to reduce the Company's risk associated with foreign currency exchange rate changes, as the gains or losses on the derivative are intended to offset the losses or gains on the underlying exposure. The Company does not engage in foreign currency speculation. The success of the Company's foreign currency risk management program depends upon forecasts of transaction activity denominated in various currencies. To the extent that these forecasts are overstated or understated during periods of currency volatility, the Company could experience unanticipated foreign currency gains or losses that could have a material impact on the Company's results of operations. In addition, the failure to identify new exposures and hedge them in a timely manner may result in material foreign currency gains or losses.

The loss of a large customer could have an adverse effect on the Company's operating results.

In 2004, the Company's top five customers accounted for approximately 15% of total revenue. In recent years, the Company's expansion into the end-user marketplace has reduced its reliance upon the revenue from any one of its larger OEM customers. Nevertheless, the loss of, or significant curtailment of purchases by, any one or more of the Company's larger customers could have a material adverse effect on the Company's operating results.

The failure of a key supplier to deliver quality product in a timely manner or the Company's inability to obtain components for its products could adversely affect the Company's operating results.

A significant portion of the Company's MVSD inventory is manufactured by a third-party contractor. The Company is dependent upon this contractor to provide quality product and meet delivery schedules. The Company engages in extensive product quality programs and processes, including actively monitoring the performance of its third-party manufacturers, however, these programs and processes may not detect all product quality issues. In addition, a variety of components used in the Company's products are only available from a single source. The announcement by a single-source supplier of a last-time component buy could result in a significant amount of inventory purchases, that in turn, could lead to an increased risk of inventory obsolescence. An interruption in, termination of, or material change in the purchase terms of any single-source components could have a material adverse effect on the Company's operating results.

The Company's business could suffer if it loses the services of, or fails to attract, key personnel.

The Company is highly dependent upon the management and leadership of Robert J. Shillman, Chief Executive Officer and Chairman of the Board of Directors of the Company, as well as other members of the Company's senior management team, including James Hoffmaster who was promoted to President of Cognex Corporation during 2004 with full responsibility for running the day-to-day operations of the Company. Although the Company has retained many experienced and qualified senior managers, the loss of certain key personnel could have a material adverse effect on the Company. The Company's continued growth and success also depends upon its ability to attract and retain skilled employees and on the ability of its officers and key employees to effectively manage the growth of the Company through the implementation of appropriate management information systems and internal controls.

Products that the Company manufactures may contain design or manufacturing defects, which could result in reduced demand, significant delays, or substantial costs.

If flaws in either the design or manufacture of the Company's products were to occur, the Company could experience a rate of failure in its products that could result in significant delays in shipment and material repair or replacement costs. While the Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its component suppliers and contract manufacturers, there can be no assurance that these actions will be sufficient to avoid a product failure rate that results in substantial delays in shipment, significant repair or replacement costs, or potential damage to the Company's reputation, any of which could have a material adverse effect on the Company's operating results.

The Company's failure to accurately forecast customer demand could result in inventory obsolescence and resulting charges.

In recent years, the Company has expanded its presence in the end-user marketplace. The Company's end-user business typically operates with a relatively short backlog and production plans are based on internal forecasts of customer demand. Due to these factors, the Company has in the past, and may again in the future, fail to accurately forecast demand, in terms of both volume and configuration for either its legacy or next-generation products. This has led to, and may again in the future lead to, an increased risk of inventory obsolescence and resulting charges.

Failure to develop new products and to respond to technological changes could result in the loss of market share and a decrease in the Company's revenues.

The market for the Company's products is characterized by rapidly changing technology. Accordingly, the Company believes that its future success will depend upon its ability to develop or acquire new products with improved price/performance and introduce them to the marketplace in a timely manner. There can be no assurance that the Company will be able to introduce and market new products successfully and respond effectively to technological changes or new product introductions by competitors. The inability to keep pace with the rapid rate of technological change in the high-technology marketplace could have a material adverse effect on the Company's operating results.

If the Company fails to successfully defend its intellectual property, its competitive position and operating results could suffer.

The Company relies heavily on its proprietary software technology and hardware designs, as well as the technical expertise, creativity, and knowledge of its personnel. Although the Company uses a variety of methods to protect its intellectual property, it relies most heavily on patent, trademark, copyright, and trade secret protection, as well as non-disclosure agreements with customers, suppliers, employees, and consultants. The Company attempts to protect its intellectual property by restricting access to its proprietary information by a combination of technical and internal security measures. There can be no assurance, however, that any of these measures will be adequate to protect the proprietary technology of the Company, that any patents issued to the Company will not be challenged, invalidated, or circumvented, or that the rights granted thereunder will provide competitive advantages to the Company. Any such adverse circumstances could have a material effect on the Company's operating results. Readers should refer to the section captioned "Intellectual Property," appearing in Part I — Item I of this Annual Report on Form 10-K.

The Company may be subject to costly litigation.

From time to time, the Company may be subject to various claims and lawsuits by competitors, customers, or other parties arising in the ordinary course of business, including lawsuits charging patent infringement. Such matters can be time-consuming, divert management's attention and resources, and cause the Company to incur significant expenses. Furthermore, there can be no assurance that the results of any of these actions will not have a material adverse effect on the Company's operating results.

Increased competition may result in decreased demand or prices for the Company's products and services.

The Company competes with other vendors of machine vision systems, the internal engineering efforts of the Company's current or prospective customers, and the manufacturers of image processing systems. Any of these competitors may have greater financial and other resources than the Company. In recent years, ease-of-use and product price have become significant competitive factors in the end-user marketplace. There can be no assurance that the Company will be able to compete successfully in the future or that the Company's investments in research and development, sales and marketing, and service activities will prove sufficient to enable the Company to maintain its competitive advantage. In addition, competitive pressures could lead to price erosion that could materially and adversely affect the Company's operating results. Readers should refer to the section captioned "Competition," appearing in Part I — Item 1 of this Annual Report on Form 10-K.

Implementation of the Company's acquisition strategy may not be successful, which could affect the Company's ability to increase its revenue or profitability.

The Company's business strategy includes selective expansion into other machine vision applications through the acquisition of businesses and technologies. Since 1995, the Company has completed nine business and technology acquisitions. The Company plans to continue to seek opportunities to expand its product line, customer base, and technical talent through acquisitions in the machine vision industry. Acquisitions involve numerous risks, including, but not limited to, diversion of management's attention from other operational matters, the inability to realize expected synergies resulting from the acquisition, failure to commercialize purchased technology, and the impairment of acquired intangible assets resulting from technological obsolescence or lower-than-expected cash flows from the acquired assets. Acquisitions are inherently risky and the inability to effectively manage these risks could have a material adverse effect on the Company's operating results.

The trading price of the Company's common stock may be volatile.

The price of the Company's common stock has historically experienced significant volatility due to fluctuations in the Company's revenue and earnings, changes in the market's expectations for the Company's growth, overall equity market conditions, conditions relating to the market for technology stocks, general economic conditions, and other factors unrelated to the Company's operations. The stock markets have experienced extreme price volatility in recent years. This volatility has had a substantial effect on the market prices of securities issued by many technology companies, often for reasons unrelated to the operating results of the specific company.

Available Information

The Company maintains a website on the World Wide Web at www.cognex.com . The Company makes available, free of charge, on its website in the section captioned "Investors – SEC Filings" its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the SEC. The Company's reports filed with, or furnished to, the SEC are also available at the SEC's website at www.sec.gov . Information contained on the Company's website is not a part of, or incorporated by reference into, this Annual Report on Form 10-K.

ITEM 2: *PROPERTIES*

In 1994, the Company purchased and renovated a 100,000 square-foot building located in Natick, Massachusetts that serves as its corporate headquarters. In 1997, the Company completed construction of a 50,000 square-foot addition to this building.

In 1995, the Company purchased an 83,000 square-foot office building adjacent to its corporate headquarters. The building is currently largely occupied with tenants who have lease agreements that expire at various dates through 2007. The Company uses a portion of the space for storage.

In 1997, the Company purchased a three and one-half acre parcel of land situated on Vision Drive, adjacent to the Company's corporate headquarters. This land is being held for future expansion.

ITEM 3: *LEGAL PROCEEDINGS*

To the Company's knowledge, there are no pending legal proceedings, other than as described in the section captioned "Intellectual Property," appearing in Part I — Item I of this Annual Report on Form 10-K, which are material to the Company. From time to time, however, the Company may be subject to various claims and lawsuits by competitors, customers, or other parties arising in the ordinary course of business, including lawsuits charging patent infringement. There can be no assurance as to the outcome of any of this litigation.

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

There were no matters submitted during the fourth quarter of the year ended December 31, 2004 to a vote of security holders through solicitation of proxies or otherwise.

ITEM 4A : *EXECUTIVE OFFICERS AND OTHER MEMBERS OF THE MANAGEMENT TEAM OF THE REGISTRANT*

The following table sets forth the names, ages, and titles of the Company's executive officers at December 31, 2004:

Name	Age	Title
Robert J. Shillman	58	Chief Executive Officer and Chairman of the Board of Directors
Patrick Alias	59	Executive Vice President and Director
James Hoffmaster	53	President and Chief Operating Officer
Richard Morin	55	Senior Vice President of Finance and Administration, Chief Financial Officer, and Treasurer

Messrs. Shillman, Alias, and Morin have been employed by the Company in their present or other capacities for no less than the past five years.

Mr. Hoffmaster joined the Company in 2001 as Chief Operating Officer and President, MVSD, and was promoted to President of Cognex Corporation in 2004. Prior to joining the Company, Mr. Hoffmaster was the Chief Executive Officer of Fibersense, a Massachusetts-based company specializing in the application of fiber optic technology to gyroscopes and other sensors. Prior to that, Mr. Hoffmaster served as President of Fisher-Rosemount Systems, a division of Emerson Electric. He holds a Masters of Computer and Information Science degree and a Bachelor of Arts degree in Economics from Cleveland State University.

Executive officers are elected annually by the Board of Directors. There are no family relationships among the directors and executive officers of the Company.

Other members of the senior management team include the following individuals:

Name	Age	Title
Eric Ceyrolle	51	President, Cognex International
Markku Jaaskelainen	50	Senior Vice President and General Manager, SISD
Marilyn Matz	51	Senior Vice President, PC Vision
E. John McGarry	48	Senior Vice President, In-Sight
Akira Nakamura	60	President, Cognex K.K.
Kris Nelson	57	Senior Vice President of Sales, North America
William Silver	51	Senior Vice President of R&D and Chief Technology Officer, MVSD
Justin Testa	52	Senior Vice President, ID Products

Messrs. Ceyrolle, Jaaskelainen, McGarry, Nelson, Silver, and Testa and Ms. Matz have been employed by the Company in their present or other capacities for no less than the past five years.

Mr. Nakamura joined the Company in 2000 after having served as President of Intergraph Japan, K.K., a worldwide provider of CAD/CAM technology. Prior to that, Mr. Nakamura spent 20 years in sales and sales management at senior levels for IBM Japan. Mr. Nakamura holds a Bachelor of Science degree in Electronic Communication from Tohoku University.

PART II

ITEM 5: ***MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES***

Information with respect to this item may be found in the sections captioned "Selected Quarterly Financial Data (Unaudited)" and "Company Information," appearing on pages 73 through 75 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

ITEM 6: ***SELECTED FINANCIAL DATA***

Information with respect to this item may be found in the section captioned "Five-Year Summary of Selected Financial Data," appearing on page 72 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

ITEM 7: ***MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

Information with respect to this item may be found in the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations," appearing on pages 25 through 41 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

ITEM 7A: ***QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK***

Information with respect to this item may be found in the section captioned "Quantitative and Qualitative Disclosures About Market Risk," appearing on pages 39 through 41 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

ITEM 8: ***FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA***

Information with respect to this item, which includes the consolidated financial statements and notes thereto, reports of independent registered public accounting firms, and supplementary data, may be found on pages 42 through 73 of the Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and is incorporated herein by reference.

ITEM 9: ***CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE***

On June 10, 2003, the Company filed a Current Report, dated June 5, 2003, on Form 8-K regarding the dismissal of PricewaterhouseCoopers LLP and the engagement of Ernst & Young LLP as their principal independent accountants.

There were no disagreements with accountants on accounting or financial disclosure during 2004 or 2003.

ITEM 9A: *CONTROLS AND PROCEDURES*

Disclosure Controls and Procedures

As required by Rules 13a-15 and 15d-15 of the Securities Exchange Act of 1934, the Company has evaluated with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, the effectiveness of its disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that such disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. From time to time, the Company reviews the disclosure controls and procedures, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that the Company's systems evolve with its business.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Management has evaluated the effectiveness of the Company's internal control over financial reporting based upon the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based upon this evaluation, management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2004.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2004 has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report which is included herein.

Changes in Internal Control over Financial Reporting

There have been no changes in the Company's internal control over financial reporting that occurred during the quarter ended December 31, 2004 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

COGNEX CORPORATION - REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROLS OVER FINANCIAL REPORTING

To The Board of Directors and Shareholders of Cognex Corporation

We have audited management's assessment, included in the accompanying Report on Internal Controls over Financial Reporting, that Cognex Corporation and subsidiaries maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Cognex Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Cognex Corporation and subsidiaries maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Cognex Corporation and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the COSO criteria **.**

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Cognex Corporation and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2004 and our report dated March 4, 2005 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 4, 2005

PART III

ITEM 10: *DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT*

Information with respect to Directors and Executive Officers of the Company required by Item 10 shall be included in the Company's definitive Proxy Statement for the Special Meeting in Lieu of the 2005 Annual Meeting of Shareholders to be held on April 21, 2005 and is incorporated herein by reference. In addition, certain information with respect to Executive Officers of the Company may be found in the section captioned "Executive Officers and Other Members of the Management Team of the Registrant," appearing in Part I — Item 4A of this Annual Report on Form 10-K.

The Company has adopted a Code of Business Conduct and Ethics covering all employees, which is available, free of charge, on the Company's website, www.cognex.com, and is included in this Annual Report on Form 10-K as Exhibit 14. The Company intends to disclose any amendments to or waivers of the Code of Business Conduct and Ethics on behalf of the Company's Chief Executive Officer, Chief Financial Officer, Controller, and persons performing similar functions on the Company's website.

ITEM 11: *EXECUTIVE COMPENSATION*

Information with respect to executive compensation required by Item 11 shall be included in the Company's definitive Proxy Statement for the Special Meeting in Lieu of the 2005 Annual Meeting of Shareholders to be held on April 21, 2005 and is incorporated herein by reference.

ITEM 12: *SECURITY OWNERSHIP AND CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS*

Information with respect to security ownership and the other matters required by Item 12 shall be included in the Company's definitive Proxy Statement for the Special Meeting in Lieu of the 2005 Annual Meeting of Shareholders to be held on April 21, 2005 and is incorporated herein by reference.

The following table provides information as of December 31, 2004 regarding shares of common stock that may be issued under the Company's existing equity compensation plans, including the 1998 Director Plan, the 1998 Stock Incentive Plan, and the 2001 General Stock Option Plan. The Company also has an Employee Stock Purchase Plan (ESPP).

	Equity Compensation Plan Information		
Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted-average exercise price of outstanding options, warrants, and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by shareholders	10,268,978(1)	$ 24.86	2,040,288(2)
Equity compensation plans not approved by shareholders	350,834(3)	21.20	7,500,000(4)
	10,619,812	$ 24.74	9,540,288

(1) Includes shares issuable upon exercise of outstanding options under the Company's 1993 Stock Option Plan, 1993 Stock Option Plan for Employee Directors, 1991 Isys Controls, Inc. Long-Term Equity Incentive Plan, 1998 Director Plan, and 1998 Stock Incentive Plan. Does not include purchase rights accruing under the ESPP because the purchase price (and therefore the number of shares to be purchased) will not be determined until the end of the purchase period.

(2) Includes shares remaining available for future issuance under the Company's 1998 Director Plan and 1998 Stock Incentive Plan. Includes 228,969 shares available for future issuance under the ESPP.

(3) Includes shares issuable upon the exercise of outstanding options under the Company's 2001 Interim General Stock Incentive Plan.

(4) Includes shares remaining available for future issuance under the Company's 2001 General Stock Option Plan.

The 2001 General Stock Option Plan was adopted by the Board of Directors on December 11, 2001 without shareholder approval. This plan provides for the granting of nonqualified stock options to any employee who is actively employed by the Company and is not an officer or director of the Company. The maximum number of shares of common stock available for grant under the plan is 7,500,000 shares. All option grants must have an exercise price per share that is no less than the fair market value per share of the Company's common stock on the grant date and must have a term that is no longer than fifteen years from the grant date. No stock options have been granted under the 2001 General Stock Option Plan.

The 2001 Interim General Stock Incentive Plan was adopted by the Board of Directors on July 17, 2001 without shareholder approval. This plan provides for the granting of nonqualified stock options to any employee who is actively employed by the Company and is not an officer or director of the Company. The maximum number of shares of common stock available for grant under the plan is 400,000 shares. All option grants have an exercise price per share that is no less than the fair market value per share of the Company's common stock on the grant date and must have a term that is no longer than fifteen years from the grant date. All 400,000 stock options have been granted under the 2001 Interim General Stock Incentive Plan.

ITEM 13: *CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS*

Information with respect to certain relationships and related transactions required by Item 13 shall be included in the Company's definitive Proxy Statement for the Special Meeting in Lieu of the 2005 Annual Meeting of Shareholders to be held on April 21, 2005 and is incorporated herein by reference.

ITEM 14: *PRINCIPAL ACCOUNTANT FEES AND SERVICES*

Information with respect to principal accountant fees and services required by Item 14 shall be included in the Company's definitive Proxy Statement for the Special Meeting in Lieu of the 2005 Annual Meeting of Shareholders to be held on April 21, 2005 and is incorporated herein by reference.

PART IV

ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(1) Financial Statements

The following consolidated financial statements of Cognex Corporation and the reports of independent public accounting firms relating thereto are included in the Company's Annual Report to Shareholders for the year ended December 31, 2004, which is attached as Exhibit 13 hereto, and are incorporated herein by reference:

Consolidated Statements of Operations for the years ended December 31, 2004, 2003, and 2002

Consolidated Balance Sheets at December 31, 2004 and 2003

Consolidated Statements of Cash Flows for the years ended December 31, 2004, 2003 and 2002

Consolidated Statements of Shareholders' Equity for the years ended December 31, 2004, 2003, and 2002

Notes to Consolidated Financial Statements

Reports of Independent Public Accounting Firms

(2) Financial Statement Schedule

Included at the end of this report are the following:

Report of Independent Registered Public Accounting Firm on the Financial Statement Schedule

Schedule II — Valuation and Qualifying Accounts

Other schedules are omitted because of the absence of conditions under which they are required or because the required information is given in the consolidated financial statements or notes thereto.

(3) Exhibits

The Exhibits filed as part of this Annual Report on Form 10-K are listed in the Exhibit Index, immediately preceding such Exhibits.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COGNEX CORPORATION

By: /s/ Robert J. Shillman

Robert J. Shillman
Chief Executive Officer and Chairman of the Board of Directors

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Robert J. Shillman Robert J. Shillman	Chief Executive Officer and Chairman of the Board of Directors (principal executive officer)	March 11, 2005
/s/ Richard Morin Richard Morin	Senior Vice President of Finance, Chief Financial Officer, and Treasurer (principal financial and accounting officer)	March 11, 2005
/s/ Patrick Alias Patrick Alias	Executive Vice President and Director	March 11, 2005
/s/ Jerald Fishman Jerald Fishman	Director	March 11, 2005
/s/ William Krivsky William Krivsky	Director	March 11, 2005
/s/ Anthony Sun Anthony Sun	Director	March 11, 2005
/s/ Reuben Wasserman Reuben Wasserman	Director	March 11, 2005

COGNEX CORPORATION - REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors and Shareholders of Cognex Corporation:

We have audited the consolidated financial statements of Cognex Corporation as of December 31, 2004 and 2003, and for the each of the two years then ended, and have issued our report thereon dated March 4, 2005 (incorporated by reference in this Annual Report (Form 10-K)). Our audits also included the financial statement schedule listed in Item 15(2) of this Annual Report (Form 10-K). This schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits.

In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 4, 2005

COGNEX CORPORATION - REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors and Shareholders of Cognex Corporation:

Our audit of the consolidated financial statements referred to in our report dated January 24, 2003 appearing in the 2004 Annual Report to Shareholders of Cognex Corporation (which report and consolidated financial statements are incorporated by reference in this Annual Report on Form 10-K) also included an audit of the financial statement schedule for the year ended December 31, 2002, listed in Item 15(2) of this Form 10-K. In our opinion, this financial statement schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

/s/ PricewaterhouseCoopers LLP

Boston, Massachusetts
January 24, 2003

COGNEX CORPORATION - SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS

Description	Balance at Beginning of Period	Additions: Charged to Costs and Expenses	Additions: Charged to Other Accounts		Deductions		Other		Balance at End of Period
		(Dollars in thousands)							
Reserve for Uncollectible Accounts:									
2004	$ 2,613	$ 150	—		$ (167)	(b)	—		$ 2,596
2003	2,207	689	—		(283)	(b)	—		2,613
2002	2,080	340	—		(213)	(b)	—		2,207
Reserve for Inventory Obsolescence:									
2004	$ 17,408	$ 375	—		$ (2,206)	(c)	$ (805)	(d)	$ 14,772
2003	20,478	914	—		(2,694)	(c)	(1,290)	(d)	17,408
2002	19,563	1,695	$ 1,506	(a)	(496)	(c)	(1,790)	(d)	20,478

(a) Settlement of inventory purchase commitments
(b) Specific write-offs
(c) Specific dispositions
(d) Sale of inventory previously reserved

EXHIBIT INDEX

EXHIBIT NUMBER	
3A	Restated Articles of Organization of Cognex Corporation effective June 27, 1989, as amended April 30, 1991, April 21, 1992, April 25, 1995, April 23, 1996, and May 8, 2000 (incorporated by reference to Exhibit 3A of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
3B	By-laws of the Company, as amended March 16, 1998 (incorporated by reference to Exhibit 3B of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
4	Specimen Certificate for Shares of Common Stock (incorporated by reference to Exhibit 4 to the Registration Statement on Form S-1 [Registration No. 33-29020])
10A	Cognex Corporation 1993 Stock Option Plan for Non-Employee Directors (incorporated by reference to Exhibit 4A to the Registration Statement on Form S-8 [Registration No. 33-81150])
10B	Cognex Corporation 1993 Stock Option Plan, as amended November 14, 1995 and February 25, 1996 (incorporated by reference to Exhibit 4A to the Registration Statement on Form S-8 [Registration No. 333-04621])
10C	1991 Isys Controls, Inc. Long-Term Equity Incentive Plan (incorporated by reference to Exhibit 4A to the Registration Statement on Form S-8 [Registration No. 333-02151])
10D	Amendment to the Cognex Corporation 1993 Stock Option Plan for Non-Employee Directors (incorporated by reference to Exhibit 10E of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
10E	Amendment to the Cognex Corporation 1993 Stock Option Plan (incorporated by reference to Exhibit 10F of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
10F	Cognex Corporation 1998 Non-Employee Director Stock Option Plan (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-8 [Registration No. 333-60807])
10G	Cognex Corporation 1998 Stock Incentive Plan (incorporated by reference to Exhibit 4.2 to the Registration Statement on Form S-8 [Registration No. 333-60807])
10H	First Amendment to the Cognex Corporation 1998 Stock Incentive Plan (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-8 [Registration No. 333-60807])
10I	Cognex Corporation 2000 Employee Stock Purchase Plan (incorporated by reference to Exhibit 4 to the Registration Statement on Form S-8 [Registration No. 333-44824])
10J	Cognex Corporation 2001 Interim General Stock Incentive Plan (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-8 [Registration No. 333-68158])
10K	Cognex Corporation 2001 General Stock Option Plan (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-8 [Registration No. 333-100709])
10L	Transition Loan Agreement between James F. Hoffmaster and Cognex Corporation, dated May 24, 2001 (incorporated by reference to Exhibit 10M of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
10M	Termination Agreement between James F. Hoffmaster and Cognex Corporation dated June 4, 2001 (incorporated by reference to Exhibit 10N of Cognex's Annual Report on Form 10-K for the year ended December 31, 2002 [File No. 0-17869])
10N	Form of Stock Option Agreement (Non-Qualified) under 1998 Stock Incentive Plan (incorporated by reference to Exhibit 10.1 of Cognex's Quarterly Report on Form 10-Q for the quarter ended October 3, 2004 [File No. 0-17869])

EXHIBIT NUMBER	
10O	Form of Stock Option Agreement (Non-Qualified) under 1998 Non-Employee Director Stock Plan (incorporated by reference to Exhibit 10.2 of Cognex's Quarterly Report on Form 10-Q for the quarter ended October 3, 2004 [File No. 0-17869])
10P	Supplemental Retirement and Deferred Compensation Plan effective April 1, 1995 *
13	Annual Report to Shareholders for the year ended December 31, 2004 (which is not deemed to be “filed” except to the extent that portions thereof are expressly incorporated by reference in this Annual Report on Form 10-K) *
14	Code of Business Conduct and Ethics as amended March 12, 2004*
21	Subsidiaries of the Registrant *
23.1	Consent of Ernst & Young LLP *
23.2	Consent of PricewaterhouseCoopers LLP *
31.1	Certification of Chief Executive Officer*
31.2	Certification of Chief Financial Officer*
32.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (CEO)**
32.2	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (CFO)**

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*   Filed herewith

** Furnished herewith

EXHIBIT 10P

COGNEX CORPORATION

SUPPLEMENTAL RETIREMENT AND DEFERRED COMPENSATION PLAN

EFFECTIVE AS OF APRIL 1, 1995

This Cognex Corporation Supplemental Retirement and Deferred Compensation Plan (the "Plan") is adopted by Cognex Corporation (the "Employer") for certain of its executive employees. The purpose of the Plan is to provide those employees with supplement retirement income and to offer those employees an opportunity to elect to defer the receipt of compensation in order to provide termination of employment and related benefits taxable pursuant to Section 451 of the Internal Revenue Code of 1986, as amended (the "Code"). The Plan is intended to be a "top-hat" plan (i.e. an unfunded deferred compensation plan maintained for a select group management or highly compensated employees) under Sections 201(2),
301(a)(3), and 401(a)(1) of the Employee Retirement Income Security Act of 1974 ("ERISA").

Accordingly, the following Plan is adopted.

ARTICLE I -- DEFINITIONS

1.1 ACCOUNT means the balance credited to a Participant's or Beneficiary's Plan account, including contribution credits and deemed income, gains, and losses (to the extend realized as determined by the Employer, in its discretion) credited thereto. A Participant's or Beneficiary's Account shall be determined as of the date of reference.

1.2 BENEFICIARY means any person or persons so designated in accordance with the provisions of Article VII.

1.3 CODE means the Internal Revenue Code of 1986 and the regulations thereunder, as amended from time to time.

1.4 COMPENSATION means the total current cash remuneration paid by the Employer to an Eligible Employee with respect to his or her service for the Employer (as determined by the Employer).

1.5 DESIGNATION DATE means the date or dates as of which a designation of deemed investment directions by an individual pursuant to Section 4.5, or any change in a prior designation of deemed investment directions by an individual pursuant to Section 4.5, shall become effective. The Designation Dates in any Plan Year shall be designated by the Employer.

1.6 EFFECTIVE DATE means the effective date of the Plan, which shall be April 1, 1995.

1.7 ELIGIBLE EMPLOYEE means, for any Plan Year (or applicable portion thereof), a person employed by the Employer who is determined by the Employer to be a member of a select group of management or highly compensated employees and who is designated by the Employer to be an Eligible Employee under the Plan. By each November 1, the Employer shall notify those individuals, if any, who will be Eligible Employees for the next Plan Year. If the Employer determines that an individual first becomes an Eligible Employee during a Plan Year, the Employer shall notify such individual of its determination and of the date during the Plan Year on which the individual shall first become an Eligible Employee.

1.8 EMPLOYER means Cognex Corporation and its successors and assigns unless otherwise herein provided, or any other corporation or business organization which, with the consent of Cognex Corporation, or its successors or assigns, assumes the Employer's obligations hereunder, or any other corporation or business organization which agrees, with the consent of Cognex Corporation, to become a party to the Plan.

1.9 ENTRY DATE with respect to an individual means the first day of the pay period following the date on which the individual first becomes an Eligible Employee.

1.10 PARTICIPANT means any person so designated in accordance with the provisions of Article II, including, where appropriate according to the context of the Plan, any former employee who is or may become (or whose Beneficiaries may become) eligible to receive a benefit under the Plan.

1.11 PARTICIPANT ENROLLMENT AND ELECTION FORM means the form on which a Participant elects to defer Compensation hereunder and on which the Participant makes certain other designations as required thereon.

1.12 PLAN means this Cognex Corporation Supplemental Retirement and Deferred Compensation Plan, as amended from time to time.

1.13 PLAN YEAR means the twelve (12) month period ending on the December 31 of each year during which the Plan is in effect.

1.14 TRUST means the trust fund established pursuant to the Plan.

1.15 TRUSTEE means the trustee named in the agreement establishing the Trust and such successor and/or additional trustees as may be named pursuant to the terms of the agreement establishing the Trust.

1.16 VALUATION DATE means the December 31 of each Plan Year and any other date that the Employer, in its sole discretion, designates as a Valuation Date.

1.17 YEAR OF SERVICE shall mean a Plan Year in which the Participant has completed at least 1,000 hours of service with the Employer.

ARTICLE II -- ELIGIBILITY AND PARTICIPATION

2.1 REQUIREMENTS. Every Eligible Employee on the Effective Date shall be eligible to become a Participant on the Effective Date. Every other Eligible Employee shall be eligible to become a Participant on the first Entry Date occurring on or after the date on which he or she becomes an Eligible Employee. No individual shall become a Participant, however, if he or she is not an Eligible Employee on the date his or her participation is to begin.

Participation in the Plan is voluntary. In order to participate, an otherwise eligible Employee must make written application in such manner as may be required by Section 3.1 and by the Employer and must agree to make Compensation Deferrals as provided in Article III.

2.2 RE-EMPLOYMENT. If a Participant whose employment with the Employer is terminated is subsequently re-employed, he or she shall become a Participant in accordance with the provisions of Section 2.1.

2.3 CHANGE OF EMPLOYMENT CATEGORY. During any period in which a Participant remains in the employ of the Employer, but ceases to be an Eligible Employee, he or she shall not be eligible to make Compensation Deferrals hereunder.

ARTICLE III -- CONTRIBUTIONS AND CREDITS

3.1 PARTICIPANT COMPENSATION DEFERRALS. In accordance with rules established by the Employer, a Participant may elect to defer Compensation which is due to be earned and which would otherwise be paid to the Participant, in a lump sum or in any fixed periodic dollar amounts designated by the Participant. Amounts so deferred will be considered a Participant's "Compensation Deferrals." Ordinarily, a Participant shall make such an election with respect to a coming twelve (12) month Plan Year during the period beginning on the November 1 and ending on the November 30 of the prior Plan Year, or during such other period established by the Employer.

Compensation Deferrals shall be made through regular payroll deductions or through an election by the Participant to defer the payment of a bonus not yet payable to him or her at the time of the election. The Participant may reduce his or her payroll deduction Compensation Deferral amount as of, and by written notice delivered to the Employer at least thirty (30) days prior to, the beginning of any regular payroll period, with such reduction being first effective for Compensation to be earned in that payroll period. Once made, a Compensation Deferral payroll deduction election shall continue in force indefinitely, until changed by the Participant on a subsequent Participant Enrollment and Election Form provided by the Employer. Compensation Deferrals shall be deducted by the Employer from the pay of a deferring Participant and shall be credited to the Account of the deferring Participant.

There shall be established and maintained by the Employer a separate Plan Account in the name of each Participant, which shall at all times be one hundred percent (100%) vested in the Participant, and to which shall be credited or debited: (a) amounts equal to the Participant's

Compensation Deferrals, and (b) amounts equal to any deemed income, gains, or losses (to the extent realized, based upon deemed fair market value of the Account's deemed assets, as determined by the Employer, in its discretion) attributable or allocable to (a). The Employer shall have the discretion to allocate such deemed income, gains, or losses among Plan Accounts pursuant to such allocation rules as the Employer deems to be reasonable and administratively practicable.

Amounts equal to the Compensation Deferrals will be paid by the Employer to the Trust with reasonable promptness after the total of such Compensation Deferrals during any month or other period has been determined.

ARTICLE IV -- ALLOCATION OF FUNDS

4.1 ALLOCATION OF DEEMED EARNINGS OR LOSSES ON ACCOUNTS. Pursuant to Section 4.5, each Participant shall have the right to direct the Employer as to how amounts in his or her Plan Account shall be deemed to be invested. In such a case, the Employer shall direct the Trustee to invest the Account maintained in the Trust on behalf of the Participant pursuant to the direction the Employer has received from that Participant. The Participant's Plan Account will be credited or debited with the increase or decrease in the realizable net asset value or credited interest, as applicable, of the designated deemed investments, as follows. As of each Valuation Date, an amount equal to the net increase or decrease in realizable net asset value or credited interest, as applicable (as determined by the employer), of each deemed investment option within the Trust since the preceding Valuation Date shall be allocated among all Participant's Accounts deemed to be invested in that investment option in accordance with the ratio which the portion of the Account of each Participant which is deemed to be invested within that investment option, determined as provided herein, bears to the aggregate of all amounts deemed to be invested that investment option.

4.2 ACCOUNTING FOR DISTRIBUTIONS. As of the date of any distribution hereunder, the distribution to a Participant or his or her Beneficiary or Beneficiaries shall be charged to such Participant's Account.

4.3 SEPARATE ACCOUNTS. A separate account under the Plan shall be established and maintained by the Employer to reflect the Account for each Participant with sub-accounts to show separately the deemed earnings and losses credited or debited to such Account and the applicable deemed investments of the Account.

4.4 INTERIM VALUATIONS. If it is determined by the Employer that the value of the Trust as of any date on which distributions are to be made differs materially from the value of the Trust on the prior Valuation Date upon which the distribution is to be based, the Employer, in its discretion, shall have the right to designate any date in the interim as a Valuation Date for the purpose of revaluing the Trust so that the Account from which the distributions being made will, prior to the distribution, reflect its share of such material difference in value.

4.5 DEEMED INVESTMENT DIRECTIONS OF PARTICIPANTS. Subject to such limitations as may from time to time be required by law, imposed by the Employer or the Trustee, or contained elsewhere in the Plan, and subject to such operating rules and procedures as may be imposed from time to time by the Employer or the Trustee, prior to and effective for each Designation Date, each Participant may communicate to the Employer a direction as to how his or her Account should be deemed to be invested among such categories as deemed investments as may be made available by the Employer hereunder. Such direction shall designate the percentage (in ten percent multiples) of each portion of the Participant's Account which is requested to be deemed to be invested in such categories as deemed investments, and shall be subject to the following rules:

(a) Any initial or subsequent deemed investment direction shall be in writing, or on a form supplied by and filed with the Employer, and shall be effective as of the next Designation Date which is at least ten (10) business days after such filing.

(b) All amounts credited to the Participant's Account shall be deemed to be invested in accordance with the then effective deemed investment direction, and as of the effective date of any new deemed investment direction, all or a portion of the Participant's Account at that date shall be reallocated among the designated deemed investment funds according to the percentages specified in the new deemed investment direction shall be filed and become effective. An election concerning deemed investment choices shall continue indefinitely as provided in the Participant's most recent Participant Enrollment and Election Form, or other form specified by the Employer.

(c) If the Employer receives an initial or revised deemed investment direction which it deems to be incomplete, unclear, or improper, the Participant's investment direction then in effect shall remain in effect (or, in the case of deficiency in an initial deemed investment direction, the Participant shall be deemed to have filed no deemed investment direction) until the next Designation Date, unless the Employer provides for, and permits the application of, corrective action prior thereto.

(d) If the Employer possesses at any time directions as to the deemed investment of less than all of a Participant's Account, the Participant shall be deemed to have directed that the undesignated portion of the Account be deemed to be invested in a money market, fixed income, or similar fund made available under the Plan as determined by the Employer in its discretion.

(e) Each Participant hereunder, as a condition to his or her participation hereunder agrees to indemnify and hold harmless the Employer and its agents and representatives from any losses or damages of any kind relating to the deemed investment of the Participant's Account hereunder.

(f) Each reference in this Section to a Participant shall be deemed to include, where applicable, a reference to a Beneficiary.

ARTICLE V -- ENTITLEMENT TO BENEFITS

5.1 TERMINATION OF EMPLOYMENT. If a Participant terminates employment with the Employer for any reason, the Participant's Plan Account at the date of termination shall be valued and payable according to the provisions of Article VI.

5.2 CHANGE OF CONTROL. If a Change of Control of the Employer occurs, the participant's Plan Account at the date of the Change of Control shall be valued and payable according to the provisions of Article VI. For purposes of this Section, a "Change of Control" shall occur when there is a purchase or other acquisition by any person, entity or group of persons, within the meaning of section 13(d) of the Securities Exchange Act of 1934 ("Act"), or any comparable successor provisions, or beneficial ownership (within the meaning of Rule 13d-3. promulgated under the Act) of 30 percent or more of either the outstanding shares of common stock or the combined voting power of Employer's then outstanding voting securities entitled to vote generally, or the approval by the stockholders of Employer of a reorganization, merger, or consolidation, in each case, with respect to which persons who were stockholders of Employer immediately prior to such reorganization, merger or consolidation do not, immediately thereafter, own more than 50 percent of the combined voting power entitled to vote generally in the election of directors of the reorganized, merged or consolidated Employer's then outstanding securities, or a liquidation or dissolution of Employer or of the sale of all or substantially all of Employer's assets.

5.3 HARDSHIP DISTRIBUTIONS. In the event of financial hardship of the Participant, as hereinafter defined, the Participant may apply to the Employer for the distribution of all or any part of his or her Account. The Employer shall consider the circumstances of each such case, and the best interests of the Participant and his or her family, and shall have the best interests of the Participant and his or her family, and shall have the right, in its sole discretion, if applicable, to allow such distribution, or, if applicable, to direct a distribution of part of the amount requested, or to refuse to allow any distribution. Upon a finding of financial hardship, the Employer shall instruct the Trustee to make the appropriate distribution to the Participant from amounts contributed to the Trust by the Employer in respect of the Participant's Account. In no event shall the aggregate amount of the distribution exceed either the full value of the Participant's Account or the amount determined by the Employer to be necessary to alleviate the Participant's financial hardship (which financial hardship may be considered to include any taxes due because of the distribution occurring because of this Section), and which is not reasonably available from other resources of the Participant. For purposes of this Section, the value of the Participant's Account shall be determined as of the date of the distribution. "Financial hardship" means (a) a severe financial hardship to the Participant resulting from a sudden and unexpected illness or accident of the Participant or of a dependent (as defined in Code Section 152(a)) of the Participant, (b) loss of the Participant's property due to casualty, or (c) other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the

Participant, each as determined to exist by the Employer. A distribution may be made under Section 5.3 only with the consent of the Employer's board of directors.

5.4 DISABILITY. In the event that the Participant incurs a Disability, as hereinafter defined, the Participant may apply to the Employer for the distribution of all or any part of his or her Account. Upon a finding of a Disability, the Employer shall instruct the Trustee to make the appropriate distribution to the Participant from amounts contributed to the Trust by the Employer in respect of the Participant's Account. For purposes of this Section 5.4, a "Disability" means a physical impairment which would be expected to prevent the Participant from performing the duties of his job with the Employer for a period of at least six months as determined by a physican which is selected by the Employer. A distribution may be made under this Section 5.4 only with the consent of the Employer's board of directors.

5.5 RETIREMENT. A Participant who has attained his or her Retirement Date, as hereinafter defined, may apply to the Employer for the distribution of all or any part of his or her Account. For purposes of this Section 5.5, "Retirement Date," shall mean the date on which the Participant has attained age fifty (50) and has completed at least five Years of Service with the Employer.

5.6 RE-EMPLOYMENT OF RECIPIENT. If a Participant receiving installment distributions pursuant to Section 6.2 is re-employed by the Employer, the remaining distributions due to the Participant shall be suspended until such time as the Participant (or his or her Beneficiary) once again becomes eligible for benefits under Article V, at which time such distribution shall commence, subject to the limitations and conditions contained in this Plan.

ARTICLE VI -- DISTRIBUTION OF BENEFITS

6.1 AMOUNT. A Participant (or his or her Beneficiary) shall become entitled to receive, on or about the date of the Participant's termination of employment with the Employer, a distribution in an aggregate amount equal to the Participant's Account, which amount, depending on (a) the performance of the deemed investments elected from time to time by the Participant, the Beneficiary, and/or the Employer, as applicable, and (b) the extent to which the investments of the Trust relating to the Participant's deemed investments under Sections 4.1 and 4.5 actually are realized by the Trust, may be less than, equal to, or greater than the aggregate amount of the Participant's Compensation Deferrals. Any payment due hereunder from the Trust which is not paid by the Trust will be paid by the Employer from its general assets.

6.2 METHOD OF PAYMENT.

(a) Cash Payments. All payments under the Plan shall be made in cash.

(b) Timing and Manner of Payment. In the case of distributions to a Participant or his or her Beneficiary by virtue of an entitlement pursuant to Section 5.1, 5.2, 5.3, or 5.4 an aggregate amount equal to the Participant's Account will be paid by the Trust or the Employer, as provided by Section 6.1, in a single lump sum. In the event a Participant becomes entitled to benefits under Section 5.5, an aggregate amount equal to the Participant's Account will be paid by the Trust or the Employer, as provided by Section 6.1, in a lump sum, on or about the date of the Participant's termination, or in annual installments made over a period elected by the Participant but not to exceed five years, provided such election is made at least 12 months prior to his Retirement Date or termination of employment. If such election is not made in accordance with the preceding sentence, the Participant's Account will be paid in a lump sum. If a Participant fails to designate properly the manner of payment of the Participant's benefit under the Plan, such payment will be in a lump sum on or about the date of the Participant's termination of employment with the Employer.

If the whole or any part of a payment hereunder by the Trust of the Employer is to be in installments, the total to be so paid shall continue to be deemed to be invested pursuant to Sections 4.1 and 4.5 under such procedures as the Employer may establish, in which case, subject to limitations of Section 6.1, any deemed income, gain, or loss attributable thereto (to the extent realized, as determined by the Employer, in its discretion) shall be reflected in the installment payments, in such equitable manner as the Employer shall determine.

6.3 DEATH BENEFITS. If a Participant dies before terminating his or her employment with the Employer and before the commencement of payments to the Participant hereunder, the Participant's Account shall be distributed in a single lump sum payment, as provided in Section 6.2, to the person or persons designated in accordance with Section 7.1.

Upon the death of a Participant after payments hereunder have begun but before he or she has received all payments to which he or she is entitled under the Plan, the remaining benefit payments shall be paid to the person or persons designated in accordance with Section 7.1, in the form of a single lump sum.

ARTICLE VII -- BENEFICIARIES; PARTICIPANT DATA

7.1 DESIGNATION OF BENEFICIARIES. Each Participant from time to time may designate any person or persons (who may be named contingently or successively) to receive such benefits as may be payable under the Plan upon or after the Participant's death, and such designation may be changed from time to time by the Participant by filing a new designation. Each designation will revoke all prior designations by the same Participant, shall be in a form prescribed by the Employer, and will be effective only when filed in writing with the Employer during the Participant's lifetime.

In the absence of a valid Beneficiary designation, or if, at the time any benefit payment is due to a Beneficiary, there is no living Beneficiary validly named by the Participant, the Employer shall pay any such benefit payment to the Participant's spouse, if then living, but otherwise to the Participant's living descendants, if any, per stripes, but, if none, to the Participant's estate. In determining the existence or identity of anyone entitled to a benefit payment, the Employer may rely conclusively upon information supplied by the Participant's personal representative, executor, or administrator. If a question arises as to the existence or identity of anyone entitled to receive a benefit payment as aforesaid, or if a dispute arises with respect to any such payment, then notwithstanding the foregoing, the Employer, in its sole discretion, may distribute such payment to the Participant's estate without liability for any tax or other consequences which might flow therefrom, or may take such other action as the Employer deems to be appropriate.

7.2 INFORMATION TO BE FURNISHED BY PARTICIPANTS AND BENEFICIARIES; INABILITY TO LOCATE PARTICIPANTS OR BENEFICIARIES. Any communication, statement, or notice addressed to a Participant or to a Beneficiary at his or her last post office address as down on the Employer's records shall be binding on the Participant or Beneficiary for all purposes of the Plan. The Employer shall not be obliged to search for any Participant or Beneficiary beyond the sending of a registered letter to such last known address. If the Employer notifies any Participant or Beneficiary that he or she is entitled to an amount under the Plan and the Participant or Beneficiary fails to claim such amount or make his or her location known to the Employer within three (3) years thereafter, then, except as otherwise required by law, if the location of one or more of the next of kin of the Participant is known to the Employer, the Employer may direct distribution of such amount to any one or more or all of such next of kin, and in such proportions as the Employer determines. If the location of none of the foregoing persons can be determined, the Employer shall have the right to direct that the amount payable shall be deemed to be a forfeiture, except that the dollar amount of the forfeiture, unadjusted for deemed gains or losses in the interim, shall be paid by the Employer if a claim for the benefit subsequently is made by the Participant or the Beneficiary to whom it was payable. If a benefit payable to an unlocated Participant or Beneficiary is subject to escheat pursuant to applicable state law, the Employer shall not be liable to any person for any payment made in accordance with such law.

ARTICLE VIII -- THE TRUST

8.1 ESTABLISHMENT OF TRUST. The Employer shall establish the Trust with the Trustee, pursuant to such terms and conditions as are set forth in the Trust agreement to be entered into between the Employer and the Trustee. The Trust is intended to be treated as a "grantor" trust under the Code, and the establishment of the Trust is not intended to cause Participants to realize current income on amounts contributed thereto, and the Trust shall be so interpreted.

ARTICLE IX -- ADMINISTRATION

9.1 ADMINISTRATIVE AUTHORITY. Except as otherwise specifically provided herein, the Employer shall have the sole responsibility for and the sole control of the operation and administration of the Plan, and shall have the power and authority to take all action and to make all decisions and interpretations which may be necessary or appropriate in order to administer and operate the Plan, including, without limiting the generality of the foregoing, the power, duty, and responsibility to:

(a) Resolve and determine all disputes or questions arising under the Plan, including the power to determine the rights of Eligible Employees, Participants, and Beneficiaries, and their respective benefits, and to remedy any ambiguities, inconsistencies, or omissions in the Plan.

(b) Adopt such rules of procedure and regulations as in its opinion may be necessary for the proper and efficient administration of the Plan and as are consistent with the Plan.

(c) Implement the Plan in accordance with its terms and the rules and regulations adopted as above.

(d) Make determinations with respect to the eligibility of any Eligible Employee as a Participant and make determinations concerning the crediting and distribution of Plan Accounts.

(e) Appoint any persons or firms, or otherwise act to secure specialized advice or assistance, as it deems necessary or desirable in connection with the administration and operation of the Plan, and the Employer shall be entitled to rely conclusively upon, and shall be fully protected in any action or omission taken by it in good faith reliance upon, the advice or opinion of such firms or persons. The Employer shall have the power and authority to delegate from time to time by written instrument all or any part of its duties, powers, or responsibilities under the Plan, both ministerial and discretionary, as it deems appropriate, to any person or committee, and in the same manner to revoke any such delegation of duties, powers, or responsibilities. Any action of such person or committee in the exercise of such delegated duties, powers, or responsibilities shall have the same force and effect for all purposes hereunder as if such action had been taken by the Employer. Further, the Employer may authorize one or more persons to execute any certificate or document on behalf of the Employer, in which event any person notified by the Employer of such authorization shall be entitled to accept and conclusively rely upon any such certificate or document executed by such person as representing action by the Employer until such third person shall have been notified of the revocation of such authority.

9.2 MUTUAL EXCLUSION OF RESPONSIBILITY. Neither the Trustee nor the Employer shall be obliged to inquire into or be responsible for any act or failure to act, or the authority therefor, on the part of the other.

9.3 UNIFORMITY OF DISCRETIONARY ACTS. Whenever in the administration or operation of the Plan discretionary actions by the Employer are required or permitted, such actions shall be consistently and uniformly applied to all persons similarly situated, and no such action shall be taken which shall discriminate in favor of any particular person or group of persons.

9.4 LITIGATION. Except as may be otherwise required by law, in any action or judicial proceeding affecting the Plan, no Participant or Beneficiary shall be entitled to any notice or service of process, and any final judgment entered in such action shall be binding on all persons interested in, or claiming under, the Plan.

9.5 PAYMENT OF ADMINISTRATION EXPENSES. All expenses incurred in the administration and operation of the Plan and the Trust, including any taxes payable by the Employer in respect of the Plan or Trust or payable by or from the Trust pursuant to its terms, shall be paid by the Employer.

9.6 CLAIMS PROCEDURE. Any person claiming a benefit under the Plan (a "Claimant") shall present the claim, in writing, to the Employer, and the Employer shall respond in writing. If the claim is denied, the written notice of denial shall state, in a manner calculated to be understood by the Claimant:

(a) The specific reason or reasons for the denial, with specific references to the Plan provisions on which the denial is based;

(b) A description of any additional material or information for the Claimant to perfect his or her claim and an explanation of why such material or information is necessary; and

(c) An explanation of the Plan's claims review procedure.

The written notice denying or granting the Claimant's claim shall be provided to the Claimant within ninety (90) days after the Employer's receipt of the claim, unless special circumstances require an extension of time for processing the claim. If such an extension is required, written notice of the extension shall be furnished by the Employer to the Claimant within the initial ninety (90) day period and in no event shall such an extension exceed a period of ninety(90) days from the end of the initial ninety (90) day period. Any extension notice shall indicate the special circumstances requiring the extension and the date on which the Employer expects to render decision on the claim. Any claim not granted or denied within the period noted above shall be deemed to have been denied.

Any Claimant whose claim is denied, or deemed to have been denied under the preceding sentences (or such Claimant's authorized representative), may, within sixty (60) days after the Claimant's receipt of notice of the denial, or after the date of the deemed denial, request a review of the denial by notice given, in writing, to the Employer. Upon such a request for review, the claim shall be reviewed by the Employer (or its designated representative), which may, but shall not be required to, grant the Claimant a hearing. In connection with the review, the Claimant may have representation, may examine pertinent documents, and may submit issues and comments in writing.

The decision on review normally shall be made within sixty (60) days of the Employer's receipt of the request for review. If an extension of time is required due to special circumstances, the Claimant shall be notified, in writing, by the Employer, and the time limit for the decision on review shall be extended to one hundred twenty (120) days. The decision on review shall be in writing and shall state, in a manner calculated to be understood by the Claimant, the specific reasons for the decision and shall include references to the relevant Plan provisions on which the decision is based. The written decision on review shall be given to the Claimant within the sixty (60) day (or, if applicable, the one hundred twenty (120) day) time limit discussed above. If the decision on review is not communicated to the Claimant within the sixty (60) day (or, if applicable, the one hundred twenty (120) day) period discussed above, the claim shall be deemed to have been denied upon review. All decisions on review shall be final and binding with respect to all concerned parties.

ARTICLE X -- AMENDMENT

10.1 RIGHT TO AMEND. The Employer, by written instrument executed by the Employer, shall have the right to amend the Plan, at any time and with respect to any provisions hereof, and all parties hereto or claiming any interest hereunder shall be bound by such amendment; provided, however, that no such amendment shall deprive a Participant or a Beneficiary of a right accrued hereunder prior to the date of the amendment.

10.2 AMENDMENTS TO ENSURE PROPER CHARACTERIZATION OF PLAN. Notwithstanding the provisions of Section 10.1, the Plan and the Trust agreement may be amended by the Employer at any time, retroactively if required, if found necessary, in the opinion of the Employer, in order to ensure that the Plan is characterized as "top-hat" plan of deferred compensation maintained for a select group of management or highly compensated employees as described under ERISA Sections 201(2), 301(a)(3), and 401(a)(1), and to conform the Plan to the provisions and requirements of any applicable law (including ERISA and the Code). No such amendment shall be considered prejudicial to any interest of a Participant or a Beneficiary hereunder.

ARTICLE XI -- TERMINATION

11.1 EMPLOYER'S RIGHT TO TERMINATE OR SUSPEND PLAN. The Employer reserves the right, at any time, to terminate the Plan and/or its obligation to make further credits to Plan accounts. The Employer also reserves the right, at any time, to suspend the operation of the Plan for a fixed or indeterminate period of time.

11.2 AUTOMATIC TERMINATION OF PLAN. The Plan, but not the Trust, automatically shall terminate upon the dissolution of the Employer, or upon its merger into or consolidation with any other corporation or business organization if there is a failure by the surviving corporation or business organization to adopt specifically and agree to continue the Plan.

11.3 SUSPENSION OF DEFERRALS. In the event of a suspension of the Plan, the Employer shall continue all aspects of the Plan, other than Compensation Deferrals under Section 3.1 during the period of the suspension, in which event payments hereunder will continue to be made during the period of the suspension in accordance with Articles V and VI.

11.4 ALLOCATION AND DISTRIBUTION. This Section shall become operative upon a complete termination of the Plan. The provisions of this Section also shall become operative in the event of a partial termination of the Plan, as determined by the Employer, but only with respect to that portion of the Plan attributable to the Participants to whom the partial termination is applicable. Upon the effective date of any such event, notwithstanding any other provisions of the Plan, no persons who were not theretofore Participants shall be eligible to become Participants, the value of the interest of all Participants and Beneficiaries shall be determined and, after deduction of estimated expenses in liquidating and, if applicable, paying Plan benefits, paid to them as soon as is practicable after such termination.

11.5 SUCCESSOR TO EMPLOYER. Any corporation or other business organization which is a successor to the Employer by reason of a consolidation, merger, or purchase of substantially all of the assets of the Employer shall have the right to become a party to the Plan by adopting the same resolution of the entity's board of directors or other appropriate governing body. If, within ninety (90) days from the effective date of such consolidation, merger, or sale of assets, such new entity does not become a party hereto, as above provided, the Plan automatically shall be terminated, and the provisions of Section 10.4 shall become operative.

ARTICLE XII -- MISCELLANEOUS

12.1 LIMITATIONS ON LIABILITY OF EMPLOYER. Neither the establishment of the Plan nor any modification thereof, not the creation of any account under the Plan, not the payment of any benefits under the Plan shall be construed as giving to any Participant or other person any legal or equitable right against the Employer, or any officer or employer thereof except as provided by law or by any Plan provision. The Employer does not in any way guarantee any Participant's Account from loss or depreciation, whether caused by poor investment performance of a deemed investment or the inability to realize upon an investment due to an insolvency affecting an investment vehicle or any other reason. In no event shall the Employer, or any successor, employee, officer, director, or stockholder of the Employer, be liable to any person on account of any claim arising by reason of the provisions of the Plan or of any instrument or instruments implementing its provisions, or for the failure of any Participant, Beneficiary, or other person to be entitled to any particular tax consequences with respect to the Plan, or any credit or distribution hereunder.

12.2 CONSTRUCTION. If any provision of the Plan is held to be illegal or void, such illegality or invalidity shall not affect the remaining provisions of the Plan, but shall be fully severable, and the Plan shall be construed and enforced as if said illegal or invalid provision had never been inserted herein. For all purposes of the Plan, where the context admits, the singular shall include the plural, and the plural shall include the singular. Headings of Articles and Sections herein are inserted only for convenience of reference and are not to be considered in the construction of the Plan. The laws of the Commonwealth of Massachusetts shall govern, control, and determine all questions of law arising with respect to the Plan and interpretation and validity of its respective provisions, except where those laws are preempted by the laws of the United States. Participation under the Plan will not give any Participant the right to be retained in the service of the Employer nor any right or claim to any benefit under the Plan unless such right or claim has specifically accrued hereunder.

12.3 SPENDTHRIFT PROVISION. No amount payable to a Participant or a Beneficiary under the Plan will, except as otherwise specifically provided by law, be subject in any manner to anticipation, alienation, attachment, garnish, sale, transfer, assignment (either at law or in equity), levy, execution, pledge, encumbrance, charge, or any other legal or equitable process, and any attempt to do so will be void; nor will any benefit be in any manner liable for or subject to the debts, contracts, liabilities, engagements, or torts of the person entitled thereto. Further (i) the withholding of taxes from Plan benefit payments, (ii) the recovery under the Plan of overpayments of benefits previously made to a Participant or Beneficiary, (iii) if applicable, the transfer of benefit rights from the Plan to another plan, or (iv) the direct deposit of benefit payments to an account in a banking institution (if not actually part of an arrangement constituting an assignment or alienation) shall not be construed as an assignment or alienation.

In the event that any Participant's or Beneficiary's benefits hereunder are garnished or attached by order of the court, the Employer may bring action or a declaratory judgment in a court of competent jurisdiction to determine the proper recipient of the benefits to be paid under the Plan. During the pendency of said action, any benefits that become payable shall be held as credits to the Participant's or Beneficiary's Account or, if the Employer prefers, paid into the court as they become payable, to be distributed by the court to the recipient as the court deems proper at close of said action.

IN WITNESS THEREOF, the Employer has caused the Plan to be executed and its seal to be affixed hereto, effective as of the 1st day of the April, 1995.

ATTEST/WITNESS	*Cognex Corporation*
/s/ JoAnn Woodyard	*By: /s/ John J. Roger Jr.*
Print Name: JoAnn Woodyard	*Print Name: John J. Roger Jr.*
	Date: June 1, 1995

[SEAL]

EXHIBIT 13

COGNEX CORPORATION: 25 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

Certain statements made in this report, as well as oral statements made by the Company from time to time, constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Readers can identify these forward-looking statements by the Company's use of the words "expects," "anticipates," "estimates," "believes," "projects," "intends," "plans," "will," "may," "shall," and similar words and other statements of a similar sense. These statements are based upon the Company's current estimates and expectations as to prospective events and circumstances, which may or may not be in the Company's control and as to which there can be no firm assurances given. These forward-looking statements involve known and unknown risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include: (1) global economic conditions that impact the capital spending trends of manufacturers in a variety of industries; (2) the cyclicality of the semiconductor and electronics industries; (3) the inability to achieve significant international revenue; (4) fluctuations in foreign exchange rates; (5) the loss of, or a significant curtailment of purchases by, any one or more principal customers; (6) the reliance upon certain sole-source suppliers to manufacture and deliver critical components for the Company's products; (7) the inability to attract and retain skilled employees; (8) the inability to design and manufacture high-quality products; (9) inaccurate forecasts of customer demand; (10) the technological obsolescence of current products and the inability to develop new products; (11) the inability to protect the Company's proprietary technology and intellectual property; (12) the Company's involvement in time-consuming and costly litigation; (13) the impact of competitive pressures; and (14) the inability to achieve expected results from acquisitions. The foregoing list should not be construed as exhaustive and the Company encourages readers to refer to the detailed discussion of risk factors included in Part I - Item 1 of the Company's Annual Report on Form 10-K. The Company cautions readers not to place undue reliance upon any such forward-looking statements, which speak only as of the date made. The Company disclaims any obligation to subsequently revise forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date such statements are made.

EXECUTIVE OVERVIEW

Cognex Corporation (the "Company") designs, develops, manufactures, and markets machine vision systems, or computers that can "see," which are used to automate a wide range of manufacturing processes where vision is required. The Company's Modular Vision Systems Division (MVSD) specializes in machine vision systems that are used to automate the manufacture of discrete items, while the Company's Surface Inspection Systems Division (SISD) specializes in machine vision systems that are used to inspect the surfaces of materials processed in a continuous fashion.

In addition to product revenue derived from the sale of machine vision systems, the Company also generates revenue by providing maintenance and support, education, consulting, and installation services to its customers. The Company's customers can be classified into three categories: semiconductor and electronics capital equipment manufacturers, discrete manufacturing customers, and surface inspection customers. Semiconductor and electronics capital equipment manufacturers purchase Cognex machine vision systems and integrate them into the capital equipment that they manufacture and then sell to their customers in the semiconductor and electronics industries that either make computer chips or make printed circuit boards containing computer chips. Although the Company sells to original equipment manufacturers (OEMs) in a number of industries, these semiconductor and electronics OEMs have historically been large consumers of the Company's products. The discrete manufacturing category includes a wide array of manufacturers who use machine vision for applications in a variety of industries, including the packaging, automotive, consumer electronics, food and beverage, and personal care industries. The majority of these customers are end users who purchase Cognex machine vision systems and install them directly on their production lines. The last category, surface inspection customers, includes manufacturers of materials processed in a continuous fashion, such as paper and steel.

Over the past few years, the Company has been successful in diversifying its customer base beyond semiconductor and electronics capital equipment manufacturers. Demand from these capital equipment manufacturers is highly cyclical, with periods of investment followed by temporary downturns. During the first half of 2004, the Company experienced an increase in orders from these customers, resulting in a 64% increase in sales to this sector for the full year 2004 over the prior year. Despite the rebound in this business, the Company generated 58% of its total revenue in 2004 from customers outside of the semiconductor and electronics capital equipment sector. Sales to customers in the discrete manufacturing category increased from the prior year by 29%, while surface inspection sales were down slightly from the prior year.

The Company's total revenue for 2004 increased 35% from the prior year to $202 million, and because the Company was able to focus increased spending in strategic areas that help drive revenue growth and in employee incentive programs, earnings increased at an even faster rate than revenue. Net income more than doubled from $0.36 per share in 2003 to $0.80 per share in 2004 and grew from 11% of revenue in 2003 to 19% of revenue in 2004.

The following table sets forth certain consolidated financial data as a percentage of revenue:

Year ended December 31,	2004	2003	2002
Revenue	100%	100%	100%
Cost of revenue	28	33	35
Gross margin	72	67	65
Research, development, and engineering expenses	14	17	23
Selling, general, and administrative expenses	35	37	51
Operating income (loss)	23	13	(9)
Nonoperating income	3	3	2
Income (loss) before taxes	26	16	(7)
Income tax provision (benefit)	7	5	(2)
Net income (loss)	19%	11%	(5)%

RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2004 COMPARED TO YEAR ENDED DECEMBER 31, 2003

REVENUE

Revenue for the year ended December 31, 2004 increased 35% to $201,957,000 from $150,092,000 for the year ended December 31, 2003. The majority of this growth came from sales to semiconductor and electronics capital equipment manufacturers, which increased $33,001,000, or 64%, from the prior year. While sales to these customers contributed most significantly to the Company's revenue growth in 2004, sales to discrete manufacturing customers also increased by $19,872,000, or 29%, from 2003. Surface inspection sales, however, decreased $1,008,000, or 3%, from the prior year. Although sales to customers outside of the semiconductor and electronics capital equipment sector grew from the prior year and represented the majority of the company's total revenue in 2004, they decreased as a percentage of total revenue to 58% in 2004 from 66% in 2003 due to the significant increase in sales to semiconductor and electronics capital equipment manufacturers. Geographically, revenue increased from the prior year in all of the Company's major regions, but most significantly in Japan, where many of the Company's semiconductor and electronics capital equipment customers are located.

Product revenue for the year ended December 31, 2004 increased 35% to $176,569,000 from $130,670,000 for the year ended December 31, 2003. The increase in product revenue was due to a higher volume of machine vision systems sold to customers in the semiconductor, electronics, automotive, and other industries. Service revenue, which is derived from the sale of maintenance and support, education, consulting, and installation services, increased 31% to $25,388,000 from $19,422,000 due principally to higher revenue generated by maintenance and support programs that are sold bundled with product offerings. Service revenue remained constant as a percentage of total revenue at 13% in both 2003 and 2004.

MVSD revenue for the year ended December 31, 2004 increased 44% to $173,889,000 from $121,016,000 for the year ended December 31, 2003. The increase in MVSD revenue was due to a higher volume of modular vision systems sold to customers in the semiconductor, electronics, automotive, and other industries. Although surface inspection orders increased from the prior year, the timing of shipments and installations resulted in a 3% decline in SISD revenue to $28,068,000 in 2004 from $29,076,000 in 2003. As a result of the increase in MVSD revenue, SISD revenue decreased as a percentage of total revenue to 14% in 2004 compared to 19% in 2003.

GROSS MARGIN

Gross margin as a percentage of revenue was 72% for 2004 compared to 67% for 2003. The increase in gross margin was primarily due to the impact of the higher sales volume without a proportional increase in manufacturing overhead costs, as well as a greater percentage of total revenue from the sale of modular vision systems, which have higher margins than the sale of services and surface inspection systems.

Product gross margin as a percentage of revenue was 76% for 2004 compared to 71% for 2003. The increase in product margin was primarily due to the increased sales volume, as well as the shift in product mix to higher-margin modular vision systems. Service gross margin as a percentage of revenue was 43% for 2004 compared to 37% for 2003. Many of the Company's products are sold with bundled maintenance and support programs for which the revenue is recognized over the program period. The increasing volume of product sales in 2003 and 2004 has resulted in higher service revenue derived from these maintenance and support programs. Although service costs increased to support the additional revenue, the increase in revenue was greater than the increase in costs.

MVSD gross margin as a percentage of revenue was 76% for 2004 compared to 71% for 2003. The increase in MVSD margin was primarily due to the higher sales volume of modular vision systems. SISD gross margin as a percentage of revenue was 45% for 2004 compared to 48% for 2003. The decrease in SISD margin was due principally to the impact of the lower revenue, while costs increased slightly.

OPERATING EXPENSES

Research, development, and engineering (R,D&E) expenses for the year ended December 31, 2004 increased 9% to $27,063,000 from $24,719,000 for the year ended December 31, 2003. MVSD R,D&E expenses increased $2,156,000, or 10%, from the prior year primarily due to higher personnel-related costs, including the additional engineering personnel resulting from the acquisition of the machine vision business of Gavitec AG on December 1, 2003 and the accrual of company bonuses for 2004. SISD R,D&E expenses increased $188,000, or 7%, from the prior year due principally to the accrual of company bonuses for 2004.

Selling, general, and administrative (S,G&A) expenses for the year ended December 31, 2004 increased 27% to $70,674,000 from $55,724,000 for the year ended December 31, 2003. MVSD S,G&A expenses increased $11,577,000, or 27%, from the prior year, while SISD S,G&A expenses increased $1,031,000, or 14%, from 2003. Corporate expenses that are not allocated to a division increased $2,342,000, or 41%, from the prior year. The increase in MVSD expenses was primarily due to the hiring of additional sales personnel and increased marketing spending to grow the Company's base of discrete manufacturing customers, higher commissions related to the increased sales volume, and the accrual of company bonuses for 2004, as well as the unfavorable impact of foreign exchange rates on the Company's international operations. A significant amount of the Company's sales and marketing costs are denominated in currencies other than the U.S. Dollar, primarily the Euro Dollar and Japanese Yen. During 2004, the Euro Dollar and Japanese Yen strengthened versus the U.S. Dollar, resulting in a higher level of expenses when these amounts were translated into U.S. Dollars. The increase in SISD expenses was primarily due to higher personnel-related costs, as well as the accrual of company bonuses for 2004. The increase in corporate expenses was principally due to the accrual of company bonuses for 2004, as well as higher professional fees related to services required to ensure the Company's compliance with the Sarbanes-Oxley Act of 2002.

NONOPERATING INCOME

Investment and other income for the year ended December 31, 2004 decreased 14% to $4,670,000 from $5,450,000 for the year ended December 31, 2003. This decrease was due principally to lower average interest rates on the Company's portfolio of debt securities.

The foreign currency gain for the year ended December 31, 2004 was $1,641,000 compared to a loss of $1,712,000 for the year ended December 31, 2003. The loss in 2003 was primarily due to the revaluation and settlement of the Company's Irish subsidiary's accounts receivable denominated in U.S. Dollars and Japanese Yen. During 2003, the Euro Dollar strengthened versus the U.S. Dollar and Japanese Yen, resulting in foreign currency losses on the Irish subsidiary's books when these receivables were revalued and collected. Although the Company experienced similar losses in 2004, they were offset by gains on the revaluation and settlement of intercompany balances and gains on forward contracts.

INCOME TAXES

The Company's effective tax rate for 2004 was 29% compared to 31% for 2003. The decrease in the effective tax rate was primarily due to more of the Company's profits being earned and taxed in lower tax jurisdictions.

YEAR ENDED DECEMBER 31, 2003 COMPARED TO YEAR ENDED DECEMBER 31, 2002

REVENUE

Revenue for the year ended December 31, 2003 increased 32% to $150,092,000 from $114,107,000 for the year ended December 31, 2002. During the year, the Company experienced an increase in demand as its business rebounded from a slowdown in capital spending by manufacturers worldwide. Sales to OEM customers, most of whom make capital equipment used in the semiconductor and electronics industries, increased $19,076,000, or 51%, from the prior year. Sales to end-user customers increased from the prior year by $16,909,000, or 22%, due to higher demand from customers across a variety of industries. Sales to end-user customers continued to comprise the majority of the Company's revenue despite the rebound in the OEM business, representing 62% of total revenue in 2003 compared to 67% in 2002. Geographically, revenue increased from the prior year in all of the Company's major regions, but most significantly in Japan, where many of the Company's OEM customers are located.

Product revenue for the year ended December 31, 2003 increased 36% to $130,670,000 from $96,202,000 for the year ended December 31, 2002. The increase in product revenue was due to a higher volume of machine vision systems sold to customers in the semiconductor, electronics, automotive, paper, metals, and other industries. Service revenue, which is derived from the sale of maintenance and support, education, consulting, and installation services, increased 8% to $19,422,000 from $17,905,000. Many of the Company's products that were sold during 2003 included bundled maintenance and support programs for which a portion of the revenue will be recognized in future quarters over the program period. As a result, service revenue did not increase as dramatically as product revenue, and it decreased as a percentage of total revenue from 16% in 2002 to 13% in 2003.

MVSD revenue for the year ended December 31, 2003 increased 34% to $121,016,000 from $90,358,000 for the year ended December 31, 2002. The increase in MVSD revenue was due to a higher volume of modular vision systems sold to customers in the semiconductor, electronics, automotive, and other industries. SISD revenue for the year ended December 31, 2003 increased 22% to $29,076,000 from $23,749,000 for the year ended December 31, 2002. The increase in SISD revenue was due principally to a higher volume of SmartView, systems sold to customers in the paper and metals industries. The markets served by SISD had not been as severely impacted by the worldwide slowdown in capital spending. As a result, SISD revenue did not increase as dramatically as MVSD revenue, and it decreased as a percentage of total revenue to 19% in 2003 compared to 21% in 2002.

GROSS MARGIN

Gross margin as a percentage of revenue was 67% for 2003 compared to 65% for 2002. The increase in gross margin was primarily due to the impact of the higher sales volume with relatively flat manufacturing overhead costs, as well as a greater percentage of revenue from the sale of modular vision systems, which have higher margins than the sale of services and surface inspection systems. This increase was partially offset by a lower amount of benefits recorded to "Cost of product revenue" in 2003 from the sale of previously reserved inventory and the favorable resolution of inventory purchase commitments, both of which had been reserved in 2001. These benefits amounted to $1,290,000 in 2003 compared to $2,684,000 in 2002.

Product gross margin as a percentage of revenue was 71% for 2003 compared to 70% for 2002. The increase in product margin was primarily due to the increased sales volume, as well as the shift in product mix to higher-margin modular vision systems. This increase was partially offset by the decreased benefit from the sale of previously reserved inventory. Service gross margin as a percentage of revenue remained consistent with the prior year at 37%.

MVSD gross margin as a percentage of revenue was 71% for 2003 compared to 70% for 2002. The increase in MVSD margin was primarily due to the impact of the higher sales volume, as well as a greater percentage of revenue from the sale of products, which carry higher margins than the service business. This increase was partially offset by the decreased benefit from the sale of previously reserved inventory. SISD gross margin as a percentage of revenue was 48% for 2003 compared to 45% for 2002. The increase in SISD margin was due principally to the increased sales volume.

OPERATING EXPENSES

Research, development, and engineering (R,D&E) expenses for the year ended December 31, 2003 decreased 4% to $24,719,000 from $25,630,000 for the year ended December 31, 2002. MVSD R,D&E expenses decreased $1,245,000, or 5%, from the prior year primarily due to a headcount reduction in the third quarter of 2002. SISD R,D&E expenses increased $334,000, or 15%, from the prior year due principally to an increase in spending on software translation services and other activities related to the SmartView product line.

Selling, general, and administrative (S,G&A) expenses for the year ended December 31, 2003 decreased 5% to $55,724,000 from $58,376,000 for the year ended December 31, 2002. MVSD S,G&A expenses increased $1,674,000, or 4%, from the prior year, while SISD S,G&A expenses increased $587,000, or 8%, from 2002. Corporate expenses that are not allocated to a division decreased $4,913,000, or 46%, from the prior year. The increase in MVSD and SISD expenses was primarily due to higher spending in sales and marketing undertaken to increase sales opportunities, as well as the unfavorable impact of foreign exchange rate changes on the Company's international operations. A significant amount of the Company's sales and marketing costs are denominated in currencies other than the U.S. Dollar, primarily the Euro Dollar and Japanese Yen. During 2003, the Euro Dollar and Japanese Yen strengthened versus the U.S. Dollar, resulting in a higher level of expenses when these amounts were translated into U.S. Dollars. The decrease in corporate expenses was due principally to lower legal expenses associated with patent infringement lawsuits initiated by the Company to protect its intellectual property.

NONOPERATING INCOME

Investment and other income for the year ended December 31, 2003 decreased 40% to $5,450,000 from $9,156,000 for the year ended December 31, 2002. This decrease was due principally to lower average interest rates on the Company's portfolio of debt securities. In addition, during 2003, the Company reduced the carrying value of its investment in a limited partnership by $1,031,000 compared to $680,000 during 2002, representing realized investment losses and fund expenses that were not offset by realized investment gains.

During the fourth quarter of 2002, based upon the estimated fair value of the Company's investment in a limited partnership, the Company determined that it may be unable to recover its full carrying value. As a result, the Company recorded a charge of $1,768,000, representing an other-than-temporary impairment in the carrying value of this investment. In addition, during 2002, the Company recorded losses from the sale of equity securities totaling $6,184,000.

The foreign currency loss for the year ended December 31, 2003 was $1,712,000 compared to a gain of $350,000 for the year ended December 31, 2002. The loss in 2003 was primarily due to the revaluation and settlement of the Company's Irish subsidiary's accounts receivable denominated in U.S. Dollars and Japanese Yen. During 2003, the Euro Dollar strengthened versus the U.S. Dollar and Japanese Yen, resulting in foreign currency losses on the Irish subsidiary's books when these receivables were revalued and collected. Although the Company experienced similar losses in 2002, they were offset by gains on the revaluation of intercompany balances that were not fully hedged. In addition, a smaller percentage of the Company's Irish subsidiary's accounts receivable were denominated in currencies other than the Euro Dollar in 2002.

INCOME TAXES

The Company's effective tax rate for 2003 was a provision of 31% compared to a benefit of 27% for 2002. The change in the effective tax rate was primarily due to lower tax-exempt investment income generated from the Company's municipal bond portfolio.

LIQUIDITY AND CAPITAL RESOURCES

The Company has historically been able to generate positive cash flow from operations, which has funded the Company's operating activities and other cash requirements and has resulted in an accumulated cash, cash equivalent, and investment balance of $391,076,000 at December 31, 2004, representing 85% of shareholders' equity. The Company has established guidelines relative to credit ratings, diversification, and maturities of its investments that maintain liquidity.

The Company's cash requirements during the year ended December 31, 2004 were met with positive cash flow from operations and the proceeds from the issuance of common stock under stock option and stock purchase plans. Cash requirements primarily consisted of operating activities, capital expenditures, and the payment of dividends. Capital expenditures in 2004 totaled $3,120,000 and consisted primarily of expenditures for computer hardware and software.

The Company believes that its existing cash, cash equivalent, and investment balance, together with continued positive cash flow from operations, will be sufficient to meet its operating, investing, and financing activities in 2005 and the foreseeable future.

The following table summarizes the Company's material contractual obligations, both fixed and contingent (in thousands):

Year Ended December 31,	Limited Partnership Interest	Acquisitions	Leases	Total
2005	$ 6,625	$ 2,577	$ 3,878	$ 13,080
2006	-	-	977	977
2007	-	-	349	349
2008	-	-	192	192
2009	-	-	190	190
Thereafter	-	-	445	445
	$ 6,625	$ 2,577	$ 6,031	$ 15,233

LIMITED PARTNERSHIP INTEREST

On June 30, 2000, Cognex Corporation became a Limited Partner in Venrock Associates III L.P. (Venrock), a venture capital fund. A director of the Company is a Managing General Partner of Venrock Associates. In the original agreement with Venrock, the Company committed to a total investment in the limited partnership of up to $25,000,000, with the commitment period expiring on January 1, 2005. In January 2005, the Company signed an amendment to the original agreement with Venrock, which reduces its commitment to $22,500,000 and extends the commitment period through December 31, 2010. The Company does not have the right to withdraw from the partnership prior to December 31, 2010. As of December 31, 2004, the Company had contributed $15,875,000 to the partnership, including $2,250,000 during 2004. The remaining commitment of $6,625,000 can be called by Venrock in any period through 2010.

ACQUISITIONS

On March 31, 2003, the Company acquired the wafer identification business of Siemens Dematic AG for 7,000,000 Euros in cash (or approximately $7,630,000) paid at closing, with the potential for an additional cash payment in 2005 of up to 1,700,000 Euros (or approximately $2,306,000) depending upon the achievement of certain performance criteria.

On December 1, 2003, the Company acquired the machine vision business of Gavitec AG for 3,777,000 Euros in cash (or approximately$4,516,000), including 3,477,000 Euros paid at closing, 100,000 Euros (or approximately $123,000) paid on December 1, 2004, and 200,000 Euros (or approximately $271,000) to be paid on December 1, 2005. There was the potential for two additional cash payments of up to 250,000 Euros (or approximately $339,000) each in the third quarter of 2004 and the first quarter of 2005 depending upon the achievement of certain performance criteria. These criteria were not met, and therefore, these contingent payments were not made.

In addition to the obligations described above, the following items may also result in future material uses of cash:

DERIVATIVE INSTRUMENTS

In certain instances, the Company enters into forward contracts and currency swaps to hedge against foreign currency fluctuations. Because the terms of the derivative instrument and underlying exposure are generally matched at inception, changes in foreign currency exchange rates should not expose the Company to significant net cash outflows.

STANDBY LETTERS OF CREDIT

On March 25, 2004, the Company provided standby letters of credit totaling 3,146,280,000 Yen (or approximately $30,722,000) to taxing authorities in Japan that are collateralized by investments on the Consolidated Balance Sheet. The Tokyo Regional Taxation Bureau (TRTB) has asserted that Cognex Corporation has a permanent establishment in Japan that would require certain income, previously reported on U.S. tax returns for the years ended December 31, 1997 through December 31, 2001, to be subject instead to taxation in Japan. The Company disagrees with this position and is contesting the TRTB's assertion. Until this matter is resolved, the Company is required to provide collateral for these tax assessments. Should the TRTB prevail in its assertion, the income in question would be taxable in Japan and the Company would be required to pay approximately $30,722,000 in taxes, interest, and penalties to Japanese taxing authorities. The Company would then be entitled to recoup the majority of this amount from taxing authorities in the U.S.

STOCK REPURCHASE PROGRAM

On December 12, 2000, the Company's Board of Directors authorized the repurchase of up to $100,000,000 of the Company's common stock. During 2002, a total of 1,768,452 shares were repurchased at a cost of $26,425,000. There have been no other shares repurchased under this program. The Company may repurchase additional shares under this program in future periods depending upon a variety of factors, including the market value of the Company's common stock and the average return on the Company's invested balances.

DIVIDENDS

Beginning in the third quarter of 2003, the Company's Board of Directors has declared and paid a cash dividend in each quarter, including the first quarter of 2005. During the third quarter of 2004, the Company's Board of Directors voted to increase the quarterly cash dividend from $0.06 per share to $0.08 per share. Dividend payments amounted to $12,756,000 during 2004 and $3,698,000 in the first quarter of 2005. Future dividends will be declared at the discretion of the Board of Directors and will depend upon such factors as the Board of Directors deems relevant. The Board of Directors may modify the Company's dividend policy from time to time.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and various other assumptions believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates under different assumptions or circumstances resulting in charges that could be material in future reporting periods. The Company believes the following critical accounting policies require the use of significant estimates and judgments in the preparation of its consolidated financial statements.

REVENUE RECOGNITION

The Company recognizes revenue from product sales upon delivery if a signed customer contract or purchase order has been received, the fee is fixed or determinable, and collection of the resulting receivable is probable. If the arrangement contains customer-specified acceptance criteria, then revenue is deferred until the Company can demonstrate that the customer's criteria have been met. The Company maintains reserves against revenue for potential product returns. Revenue from maintenance and support programs is deferred and recognized ratably over the program period. Revenue from education and consulting services is recognized over the period the services are provided. Revenue from installation services is recognized when the customer has signed off that the installation is complete.

While the Company applies the guidance of Statement of Position (SOP) No. 97-2, "Software Revenue Recognition," as amended by SOP No. 98-9, "Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions," management exercises judgment in connection with the determination of the amount of revenue to be recognized each period. Such judgments include, but are not limited to, assessing the probability of collecting the receivable, assessing whether the fee is fixed or determinable, and assessing whether customer-specified acceptance criteria are substantive in nature.

INVESTMENTS

At December 31, 2004, the Company's investment balance totaled $336,806,000, of which $325,094,000 consisted of municipal bonds. Investments in municipal bonds are reported at fair value, with unrealized gains and losses, net of tax, recorded in shareholders' equity as other comprehensive income (loss). The remaining investment balance of $11,712,000 represents a limited partnership interest in Venrock

Associates III, L.P., a venture capital fund. A director of the Company is a Managing General Partner of Venrock Associates. The Company's limited partnership interest is accounted for using the cost method because the Company's investment is less than 5% of the partnership and the Company has no influence over the partnership's operating and financial policies.

The fair value of the Company's limited partnership interest is based upon valuations of the partnership's investments as determined by the General Partner. The Company understands that the General Partner adjusts the investment valuations at least quarterly to reflect both realized and unrealized gains and losses on partnership investments. Securities of public companies are valued at market, subject to appropriate discounts to reflect limitations on liquidity. Securities of private companies are valued at an estimated fair value, which initially is at cost, adjusted for subsequent transactions that indicate a higher or lower value is warranted. The value of private securities may be discounted when, in the General Partner's judgment, the carrying value of such private securities has been impaired by specific events.

The Company monitors the carrying value of its investment compared to its fair value to determine whether an other-than-temporary impairment in its interest in the limited partnership has occurred. In considering whether a decline in fair value is other than temporary, the Company considers many factors, both qualitative and quantitative in nature. Some of these factors include the duration and extent of the fair value decline, the length of the Company's contractual commitment to the partnership, general economic and stock market trends, and specific communications from the General Partner.

In 2002, the Company determined that it may be unable to recover the full carrying value of this investment, and as a result, recorded an other-than-temporary impairment charge of $1,768,000 to reduce the carrying value of this investment to its then estimated fair value. Given the nature of the partnership's portfolio and the difficulty inherent in valuing these investments, there is a great deal of uncertainty surrounding the future value of the Company's interest in the limited partnership and future impairment charges may be required.

ACCOUNTS RECEIVABLE

The Company maintains reserves against its accounts receivable for potential credit losses. Ongoing credit evaluations of customers are performed and the Company has historically not experienced significant losses related to the collection of its accounts receivable. Allowances for uncollectible accounts are estimated by management taking into account the length of time receivables have been outstanding, specific accounts determined to be at risk for collection, the risks associated with selling to smaller customers, and the economic conditions of the primary regions and industries sold to, as well as general economic conditions. An adverse change in any of these factors may result in the need for additional bad debt provisions.

INVENTORIES

Inventories are stated at the lower of cost or market. The Company estimates excess and obsolescence exposures based upon assumptions about future demand, product transitions, and market conditions and records reserves to reduce the carrying value of inventories to their net realizable value. The failure to accurately forecast demand, in terms of both volume and configuration, and adjust material requirement plans in a timely manner may lead to additional excess and obsolete inventory and future charges.

In 2001, the Company recorded a $16,300,000 charge for excess inventories and purchase commitments resulting from an extended slowdown in the semiconductor and electronics industries, as well as the expected transition to newer Cognex hardware platforms by the Company's OEM customers. The Company has been able to subsequently sell $3,885,000 of this inventory to customers as a result of actual demand being higher than the demand that was forecasted at the time of the charge. In addition, the Company has negotiated the favorable resolution of $894,000 of the inventory purchase commitments. The Company did not record significant excess and obsolete inventory provisions in 2002, 2003, or 2004.

LONG-LIVED ASSETS

The Company has long-lived assets including property, plant, and equipment, as well as acquired goodwill and other intangible assets. These assets are susceptible to shortened estimated useful lives and changes in fair value due to changes in their use, market or economic changes, or other events or circumstances. In addition, the fair value of goodwill is susceptible to changes in the fair value of the reporting units in which the goodwill resides, which are also reportable segments. The Company evaluates the potential impairment of its long-lived assets annually, as required, or whenever events or circumstances indicate their carrying value may not be recoverable. If events or circumstances occur which would require a significant reduction in the estimated useful lives of these assets or a significant decrease in fair value below their carrying value, an adjustment to the lives or carrying values would result in a charge to income in the period of determination.

WARRANTY OBLIGATIONS

The Company records the estimated cost of fulfilling product warranties at the time of sale based upon historical costs to fulfill warranty obligations. Provisions may also be recorded subsequent to the time of sale whenever specific events or circumstances impacting product quality become known that would not have been taken into account using historical data. While the Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its component suppliers and third-party contract manufacturers, the Company's warranty obligation is affected by product failure rates, material usage, and service delivery costs incurred in correcting a product failure. An adverse change in any of these factors may result in the need for additional warranty provisions.

CONTINGENCIES

Estimated losses from contingencies are accrued by management based upon the likelihood of a loss and the ability to reasonably estimate the amount of the loss. Estimating potential losses, or even a range of losses, is difficult and involves a great deal of judgment. The Company relies primarily on assessments made by its internal and external legal counsel to make its determination as to whether a loss contingency arising from litigation should be recorded or disclosed. Should the resolution of a contingency result in a loss that the Company did not accrue because management did not believe that the loss was probable or capable of being reasonably estimated, then this loss would result in a charge to income in the period the contingency was resolved.

INCOME TAXES

As part of the process of preparing consolidated financial statements, management is required to estimate income taxes in each of the jurisdictions in which the Company operates. This process involves estimating the current tax liability, as well as assessing temporary differences arising from the different treatment of items for financial statement and tax purposes. These differences result in deferred tax assets and liabilities, which are recorded on the Consolidated Balance Sheet.

At December 31, 2004, the Company had net deferred tax assets of $31,020,000, primarily resulting from temporary differences between the financial statement and tax bases of assets and liabilities. Management has evaluated the realizability of these deferred tax assets and has determined that it is more likely than not that these assets will be realized. In reaching this conclusion, management has evaluated relevant criteria, including the Company's historical profitability, current projections of future profitability, and the lives of tax credits, net operating and capital losses, and other carryforwards, certain of which have indefinite lives. Should the Company fail to generate sufficient pre-tax profits in future periods, the Company may be required to record material adjustments to these deferred tax assets, resulting in a charge to income in the period of determination.

Significant judgment is required in determining worldwide income tax expense based upon tax laws in the various jurisdictions in which the Company operates. The Company is subject to audits by various tax authorities, which may result in future charges or credits.

DERIVATIVE INSTRUMENTS

In certain instances, the Company enters into forward contracts and currency swaps to hedge against foreign currency fluctuations. These contracts are used to reduce the Company's risk associated with foreign currency exchange rate changes, as the gains or losses on these contracts are intended to offset the losses or gains on the underlying exposures. The Company does not engage in foreign currency speculation.

The Company recorded foreign currency gains of $1,641,000 in 2004, foreign currency losses of $1,712,000 in 2003, and foreign currency gains of $350,000 in 2002. The Company's exposure to foreign currency gains and losses has increased in recent years as a greater portion of its revenues, expenses, assets, and liabilities are denominated in currencies other than the functional currencies of the Company or its subsidiaries. In addition, foreign exchange rates have fluctuated more significantly in the past few years.

Administering the Company's foreign currency risk management program requires the use of estimates and the application of judgment, including compiling forecasts of transaction activity denominated in various currencies. The failure to identify foreign currency exposures and construct effective hedges may result in material foreign currency gains or losses.

NEW PRONOUNCEMENTS

On December 16, 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard (SFAS) No. 123R, "Share-Based Payment," which is a revision of SFAS No. 123, "Accounting for Stock-Based Compensation." SFAS No. 123R requires companies to recognize compensation cost for all share-based payments to employees (including stock option and employee stock purchase plans) at fair value. SFAS 123R will be effective for public companies for interim or annual periods beginning after June 15 , 2005. The Company will adopt SFAS No. 123R beginning in the third quarter of 2005 using the modified prospective method in which compensation cost is recognized beginning on the effective date.

The Company currently recognizes compensation costs using the intrinsic value based method and, as such, generally recognizes no compensation cost. Accordingly, the adoption of SFAS No. 123R's fair value based method will have a significant impact on the Company's results of operations, although it will have no impact on its overall financial position. The impact of adoption of SFAS No. 123R cannot be predicted at this time because it will depend upon levels of share-based payments granted in the future. However, had the Company adopted SFAS No. 123R in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as described in the disclosure of pro forma net income (loss) and net income (loss) per share in Note 1 to the Company's consolidated financial statements.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

FOREIGN CURRENCY RISK

The Company faces exposure to adverse movements in foreign currency exchange rates as a significant portion of its revenues, expenses, assets, and liabilities are denominated in currencies other than the functional currencies of the Company or its subsidiaries. These exposures may change over time as business practices evolve. The Company evaluates its foreign currency exposures on an ongoing basis and makes adjustments to its foreign currency risk management program as circumstances change.

In certain instances, the Company enters into forward contracts and currency swaps to hedge against foreign currency fluctuations. Currency swaps are used to hedge long-term transactions between the Company and its subsidiaries. Forward contracts are used to provide an economic hedge against transactions denominated in currencies other than the functional currencies of the Company or its subsidiaries.

These forward contracts and currency swaps are used to reduce the Company's risk associated with foreign currency exchange rate changes, as the gains or losses on these contracts are intended to offset the losses or gains on the underlying exposures. The Company does not engage in foreign currency speculation.

The success of the Company's foreign currency risk management program depends upon forecasts of transaction activity denominated in various currencies. To the extent that these forecasts are overstated or understated during periods of currency volatility, the Company could experience unanticipated foreign currency gains or losses that could have a material impact on the Company's results of operations. In addition, the failure to identify new exposures and hedge them in a timely manner may result in material foreign currency gains or losses.

The Company enters into currency swaps to hedge the foreign currency exposure of its long-term intercompany loans between the parent and certain of its European subsidiaries. Currency swaps to exchange a total of 48,340,000 Euro Dollars for U.S. Dollars at a weighted-average settlement price of 1.02 USD/Euro, with original terms of two to five years, were outstanding at December 31, 2004. These instruments had a fair value of $68,565,000 at December 31, 2004. The Company also enters into forward contracts to hedge the foreign currency exposure of a portion of its intercompany transactions between its subsidiaries. In addition, the Company enters into forward contracts to hedge the foreign currency exposure of its Irish subsidiary's accounts receivable denominated in U.S. dollars and Japanese Yen. Forward contracts to exchange 1,421,000,000 Japanese Yen for Euro Dollars at a weighted-average settlement price of 135.55 Yen/Euro and contracts to exchange 2,945,000 U.S. dollars for Euro Dollars at a weighted-average settlement price of 1.34 USD/Euro, both with terms of one to four months, were outstanding at December 31, 2004. These instruments had a fair value of $17,112,000 at December 31, 2004.

While the contract amounts of derivative instruments provide one measure of the volume of these transactions, they do not represent the amount of the Company's exposure to changes in foreign currency exchange rates. Because the terms of the derivative instrument and underlying exposure are generally matched at inception, changes in foreign currency exchange rates should not expose the Company to significant losses in earnings or net cash outflows when exposures are properly hedged.

INTEREST RATE RISK

The Company's investment portfolio includes municipal bonds. Debt securities with original maturities greater than three months are designated as available-for-sale and are reported at fair value. At December 31, 2004, the fair value of the Company's bond portfolio amounted to $325,094,000, with principal amounts totaling $321,120,000, maturities that do not exceed three years, and a yield to maturity of 1.77%. Differences between the fair value and principal amounts of the Company's bond portfolio are primarily attributable to discounts and premiums arising at the acquisition date, as well as unrealized gains and losses at the balance sheet date.

Given the relatively short maturities and investment-grade quality of the Company's bond portfolio at December 31, 2004, a sharp rise in interest rates should not have a material adverse effect on the fair value of these instruments. As a result, the Company does not currently hedge these interest rate exposures.

The following table presents hypothetical changes in the fair value of the Company's bond portfolio at December 31, 2004 arising from selected potential changes in interest rates (in thousands):

Type of security	Valuation of securities given an interest rate decrease		No change in interest rates	Valuation of securities given an interest rate increase	
	(100 BP)	(50 BP)		50 BP	100 BP
Municipal bonds	$ 327,363	$ 326,185	$ 325,094	$ 324,041	$ 323,014

A 50 basis point (BP) movement in the Federal Funds Rate has occurred in 15 of the last 56 quarters. There has not been a 100 BP movement in the Federal Funds Rate in any of the last 56 quarters.

OTHER MARKET RISKS

The Company's investment portfolio also includes a limited partnership interest in Venrock Associates III, L.P., a venture capital fund with an investment focus on Information Technology and Health Care and Life Sciences. The majority of the partnership's portfolio consists of investments in early stage, private companies characterized by a high degree of risk, volatility, and illiquidity. A director of the Company is a Managing General Partner of Venrock Associates.

The fair value of the Company's limited partnership interest is based upon valuations of the partnership's investments as determined by the General Partner. The Company understands that the General Partner adjusts the investment valuations at least quarterly to reflect both realized and unrealized gains and losses on partnership investments. Securities of public companies are valued at market, subject to appropriate discounts to reflect limitations on liquidity. Securities of private companies are valued at an estimated fair value, which initially is at cost, adjusted for subsequent transactions that indicate a higher or lower value is warranted. The value of private securities may be discounted when, in the General Partner's judgment, the carrying value of such private securities has been impaired by specific events.

Given the nature of the partnership's portfolio and the difficulty inherent in valuing these investments, there is a great deal of uncertainty surrounding the future value of the Company's interest in the limited partnership and future impairment charges may be required.

(in thousands, except per share amounts)

Year Ended December 31,	2004	2003	2002
Revenue			
Product	$ 176,569	$ 130,670	$ 96,202
Service	25,388	19,422	17,905
	201,957	150,092	114,107
Cost of revenue			
Product	42,788	37,870	28,499
Service	14,583	12,269	11,360
	57,371	50,139	39,859
Gross margin			
Product	133,781	92,800	67,703
Service	10,805	7,153	6,545
	144,586	99,953	74,248
Research, development, and engineering expenses	27,063	24,719	25,630
Selling, general, and administrative expenses	70,674	55,724	58,376
Operating income (loss)	46,849	19,510	(9,758)
Investment and other income	4,670	5,450	9,156
Loss on sale of equity securities and impairment of investment in limited partnership	-	-	(7,952)
Foreign currency gain (loss)	1,641	(1,712)	350
Income (loss) before taxes	53,160	23,248	(8,204)
Income tax provision (benefit)	15,416	7,297	(2,177)
Net income (loss)	$ 37,744	$ 15,951	$ (6,027)
Net income (loss) per common and common equivalent share:			
Basic	$ 0.83	$ 0.37	$ (0.14)
Diluted	$ 0.80	$ 0.36	$ (0.14)
Weighted-average common and common equivalent shares outstanding:			
Basic	45,480	43,173	43,503
Diluted	47,358	44,466	43,503
Cash dividends per common share	$ 0.28	$ 0.12	$ -

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

COGNEX CORPORATION: CONSOLIDATED BALANCE SHEETS 43
(in thousands)

December 31,	2004	2003
ASSETS		
Current assets:		
Cash and cash equivalents	$ 54,270	$ 49,980
Short-term investments	180,409	82,653
Accounts receivable, less reserves of $2,596 and $2,613 in 2004 and 2003, respectively	33,816	26,697
Inventories, net	20,091	15,519
Deferred income taxes	9,504	8,223
Prepaid expenses and other current assets	14,871	14,526
Total current assets	312,961	197,598
Long-term investments	156,397	170,869
Property, plant, and equipment, net	23,995	24,980
Deferred income taxes	21,516	19,428
Intangible assets, net	7,506	8,582
Goodwill	7,033	7,222
Other assets	3,900	3,854
	$ 533,308	$ 432,533
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 5,563	$ 5,555
Accrued expenses	55,779	32,098
Customer deposits	3,445	3,932
Deferred revenue	5,714	5,702
Total current liabilities	70,501	47,287
Other liabilities	-	252
Commitments (Notes 4, 9, 10, 11, 12, and 18)		
Shareholders' equity:		
Common stock, $.002 par value - Authorized: 140,000 shares, issued: 46,155 and 48,186 shares in 2004 and 2003, respectively	92	96
Additional paid-in capital	192,860	209,679
Treasury stock, at cost, 0 and 4,253 shares in 2004 and 2003, respectively	-	(72,445)
Retained earnings	283,712	258,724
Accumulated other comprehensive loss	(13,857)	(11,060)
Total shareholders' equity	462,807	384,994
	$ 533,308	$ 432,533

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

 COGNEX CORPORATION: CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(in thousands)

	Common Stock Shares	Common Stock Par Value	Additional Paid-in Capital
Balance at December 31, 2001	46,289	$ 93	$ 173,675
Issuance of common stock under stock option, stock purchase, and other plans	588	1	7,470
Tax benefit from exercise of stock options	-	-	3,450
Repurchase of common stock	-	-	-
Common stock received for payment of stock option exercises	-	-	-
Comprehensive loss:			
Net loss	-	-	-
Recognition of accumulated gains on equity securities in current operations, net of tax of $2,506	-	-	-
Losses on currency swaps, net of gains on long-term intercompany loans, net of tax of $21	-	-	-
Foreign currency translation adjustment	-	-	-
Comprehensive loss			
Balance at December 31, 2002	46,877	$ 94	$ 184,595
Issuance of common stock under stock option, stock purchase, and other plans	1,309	2	20,782
Tax benefit from exercise of stock options	-	-	4,302
Payment of dividends	-	-	-
Common stock received for payment of stock option exercises	-	-	-
Comprehensive income:			
Net income	-	-	-
Losses on currency swaps, net of gains on long-term intercompany loans, net of tax of $367	-	-	-
Net unrealized gain on available-for-sale investments, net of tax of $299	-	-	-
Foreign currency translation adjustment	-	-	-
Comprehensive income			
Balance at December 31, 2003	48,186	$ 96	$ 209,679
Issuance of common stock under stock option, stock purchase, and other plans	2,232	4	44,213
Tax benefit from exercise of stock options	-	-	11,722
Payment of dividends	-	-	-
Common stock received for payment of stock option exercises	-	-	-
Retirement of treasury stock	(4,263)	(8)	(72,754)
Comprehensive income:			
Net income	-	-	-
Losses on currency swaps, net of gains on long-term intercompany loans, net of tax of $1,016	-	-	-
Net unrealized loss on available-for-sale investments, net of tax of $696	-	-	-
Foreign currency translation adjustment	-	-	-
Comprehensive income			
Balance at December 31, 2004	46,155	$ 92	$ 192,860

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

Treasury Stock					
Shares	Cost	Retained Earnings	Accumulated Other Comprehensive Loss	Comprehensive Income(Loss)	Total Shareholders' Equity
2,390	$ (43,419)	$ 254,037	$ (6,342)		$ 378,044
-	-	-	-	-	7,471
-	-	-	-	-	3,450
1,768	(26,425)	-	-	-	(26,425)
91	(2,467)	-	-	-	(2,467)
-	-	(6,027)	-	(6,027)	(6,027)
-	-	-	4,269	4,269	4,269
-	-	-	(35)	(35)	(35)
-	-	-	(3,760)	(3,760)	(3,760)
4,249	$ (72,311)	$ 248,010	$ (5,868)	$ (5,553)	$ 354,520
-	-	-	-	-	20,784
-	-	-	-	-	4,302
-	-	(5,237)	-	-	(5,237)
4	(134)	-	-	-	(134)
-	-	15,951	-	15,951	15,951
-	-	-	(625)	(625)	(625)
-	-	-	509	509	509
-	-	-	(5,076)	(5,076)	(5,076)
4,253	$ (72,445)	$ 258,724	$ (11,060)	$ 10,759	$ 384,994
-	-	-	-	-	44,217
-	-	-	-	-	11,722
-	-	(12,756)	-	-	(12,756)
10	(317)	-	-	-	(317)
(4,263)	72,762	-	-	-	-
-	-	37,744	-	37,744	37,744
-	-	-	(1,730)	(1,730)	(1,730)
-	-	-	(1,185)	(1,185)	(1,185)
-	-	-	118	118	118
-	$ -	$ 283,712	$ (13,857)	$ 34,947	$ 462,807

(in thousands)

Year Ended December 31,	2004	2003	2002
Cash flows from operating activities:			
Net income (loss)	$ 37,744	$ 15,951	$ (6,027)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation of property, plant, and equipment	4,548	5,422	6,534
Amortization of intangible assets	1,526	1,012	543
Amortization of investments	3,896	3,728	2,447
Tax benefit from exercise of stock options	11,722	4,302	3,450
Deferred income tax benefit	(2,568)	(432)	(2,196)
Net loss (gain) on investment in limited partnership	(154)	1,031	680
Impairment on investment in limited partnership	-	-	1,768
Loss on sale of equity securities	-	-	6,184
Changes in current assets and current liabilities:			
Accounts receivable	(5,417)	(4,775)	(348)
Inventories	(3,642)	5,833	5,010
Accounts payable	(290)	1,482	(2,569)
Accrued expenses	15,785	148	(1,411)
Other current assets and current liabilities	(49)	(2,783)	1,979
Other operating activities	75	45	402
Net cash provided by operating activities	63,176	30,964	16,446
Cash flows from investing activities:			
Purchase of investments	(805,621)	(316,481)	(137,922)
Maturity and sale of investments	716,714	276,529	184,453
Purchase of property, plant, and equipment	(3,120)	(2,462)	(2,227)
Cash paid for business acquisitions	(123)	(11,787)	(349)
Net cash provided by (used in) investing activities	(92,150)	(54,201)	43,955
Cash flows from financing activities:			
Issuance of common stock under stock option, stock purchase, and other plans	43,900	20,650	5,004
Repurchase of common stock	-	-	(26,425)
Payment of dividends	(12,756)	(5,237)	-
Net cash provided by (used in) financing activities	31,144	15,413	(21,421)
Effect of exchange rate changes on cash	2,120	(660)	(4,875)
Net increase (decrease) in cash and cash equivalents	4,290	(8,484)	34,105
Cash and cash equivalents at beginning of year	49,980	58,464	24,359
Cash and cash equivalents at end of year	$ 54,270	$ 49,980	$ 58,464

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

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying consolidated financial statements reflect the application of the significant accounting policies described below.

NATURE OF OPERATIONS

Cognex Corporation (the "Company") designs, develops, manufactures, and markets machine vision systems, or computers that can "see." The Company's products are used to automate a wide range of manufacturing processes where vision is required.

USE OF ESTIMATES IN THE PREPARATION OF FINANCIAL STATEMENTS

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the balance sheet date and the reported amounts of revenue and expenses during the year. Actual results could differ from those estimates.

BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of Cognex Corporation and its subsidiaries, all of which are wholly-owned. All intercompany accounts and transactions have been eliminated. Certain amounts reported in prior years have been reclassified to be consistent with the current year presentation.

FOREIGN CURRENCY

The financial statements of the Company's foreign subsidiaries, where the local currency is the functional currency, are translated using exchange rates in effect at the end of the year for assets and liabilities and average exchange rates during the year for results of operations. The resulting foreign currency translation adjustment is recorded in shareholders' equity as other comprehensive income (loss).

CASH, CASH EQUIVALENTS, AND INVESTMENTS

Debt securities purchased with original maturities of three months or less are classified as cash equivalents and are stated at amortized cost. Debt securities with original maturities greater than three months and remaining maturities of one year or less, as well as auction rate securities for which interest rates reset in less than 90 days but for which the maturity date is greater than 90 days, are classified as short-term investments. Despite the long-term nature of their contractual maturities, the Company has the ability to quickly liquidate auction rate securities. Debt securities with remaining maturities greater than one year, as well as a limited partnership interest, are classified as long-term investments. It is the Company's policy to invest in debt securities with contractual maturities that do not exceed three years.

Debt securities with original maturities greater than three months are designated as available-for-sale and are reported at fair value, with unrealized gains and losses, net of tax, recorded in shareholders' equity as other comprehensive income (loss). Realized gains and losses are included in current operations, along with the amortization of the discount or premium arising at acquisition and are calculated using the specific identification method.

The Company's limited partnership interest is accounted for using the cost method because the Company's investment is less than 5% of the partnership and the Company has no influence over the partnership's operating and financial policies. The Company monitors the carrying value of its investment compared to its fair value to determine whether an other-than-temporary impairment in its interest in the limited partnership has occurred. If the decline in fair value is determined to be other-than-temporary, an impairment charge is recorded in current operations.

ACCOUNTS RECEIVABLE

The Company establishes reserves against its accounts receivable for potential credit losses when it determines receivables are at risk for collection based upon the length of time receivables have been outstanding, as well as various other factors. Receivables are written off against these reserves in the period they are determined to be uncollectible.

INVENTORIES

Inventories are stated at the lower of cost or market. Cost is determined using standard costs, which approximate the first in, first out (FIFO) method. The Company estimates excess and obsolescence exposures based upon assumptions about future demand, product transitions, and market conditions and records reserves to reduce the carrying value of inventories to their net realizable value.

The Company generally disposes of obsolete inventory upon determination of obsolescence. The Company does not dispose of excess inventory immediately, due to the possibility that some of this inventory could be sold to customers as a result of differences between actual and forecasted demand.

When inventory has been written down below cost, such reduced amount is considered the new cost basis for subsequent accounting purposes. As a result, the Company would recognize a higher than normal gross margin if the reserved inventory were subsequently sold.

PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment are stated at cost and depreciated using the straight-line method over the assets' estimated useful lives. Buildings' useful lives are 39 years, building improvements' useful lives are 10 years, and the useful lives of computer hardware, computer software, and furniture and fixtures range from two to five years. Leasehold improvements are depreciated over the shorter of the estimated useful lives or the remaining terms of the leases. Maintenance and repairs are expensed when incurred; additions and improvements are capitalized. Upon retirement or disposition, the cost and related accumulated depreciation of the assets disposed of are removed from the accounts, with any resulting gain or loss included in current operations.

INTANGIBLE ASSETS

Intangible assets are stated at cost and amortized using the straight-line method over the assets' estimated useful lives, which range from two to ten years. The Company evaluates the possible impairment of long-lived assets, including intangible assets, whenever events or circumstances indicate the carrying value of the assets may not be recoverable. At the occurrence of a certain event or change in circumstances, the

Company evaluates the potential impairment of an asset based upon the estimated future undiscounted cash flows. If an impairment exists, the Company determines the amount of such impairment based upon the present value of the estimated future cash flows using a discount rate commensurate with the risks involved.

GOODWILL

Goodwill is stated at cost. The Company evaluates the possible impairment of goodwill annually each fourth quarter, and whenever events or circumstances indicate the carrying value of the goodwill may not be recoverable. The Company evaluates the potential impairment of goodwill by comparing the fair value of the reporting unit to its carrying value, including goodwill. If the fair value is less than the carrying value, the Company determines the amount of such impairment by comparing the implied fair value of the goodwill to its carrying value.

WARRANTY OBLIGATIONS

The Company warrants its hardware products to be free from defects in material and workmanship for periods ranging from six months to two years from the time of sale based upon the product being purchased and the terms of the customer arrangement. Warranty obligations are accounted for in accordance with Statement of Financial Accounting Standards No. 5, "Accounting for Contingencies," since it is probable that customers will make claims under warranties related to products that have been sold and the amount of these claims can be reasonably estimated based upon experience. Estimated warranty obligations are evaluated and recorded at the time of sale based upon historical costs to fulfill warranty obligations. Provisions may also be recorded subsequent to the time of sale whenever specific events or circumstances impacting product quality become known that would not have been taken into account using historical data.

REVENUE RECOGNITION

The Company recognizes revenue in accordance with Statement of Position (SOP) No. 97-2, "Software Revenue Recognition," as amended by SOP No. 98-9, "Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions," since the software is not incidental to the arrangement and the services in the arrangement do not involve significant production, modification, or customization of the software. The Company recognizes revenue from product sales upon delivery if a signed customer contract or purchase order has been received, the fee is fixed or determinable, and collection of the resulting receivable is probable. If the arrangement contains customer-specified acceptance criteria, then revenue is deferred until the Company can demonstrate that the customer's criteria have been met.

Certain of the Company's products are sold with multiple elements, such as maintenance and support programs, education services, and installation services. The Company accounts for each element separately. The amount allocated to each undelivered element is the price charged when the item is sold separately, with the residual value from the arrangement allocated to the delivered element. In addition, the Company also provides consulting services. Revenue from maintenance and support programs is deferred and recognized ratably over the program period.

Revenue from education and consulting services are recognized over the period the services are provided. Revenue from installation services is recognized when the customer has signed off that the installation is complete.

The Company's products are sold directly to end users, as well as to resellers including original equipment manufacturers (OEMs), system integrators, and distributors. Revenue is recognized upon delivery of the product to the reseller, assuming all other revenue recognition criteria have been met. The Company establishes reserves against revenue for potential product returns in accordance with Statement of Financial Accounting Standards No. 48, "Revenue Recognition When Right of Return Exists," since the amount of future returns can be reasonably estimated based upon experience.

Amounts billed to customers related to shipping and handling, as well as reimbursements received from customers for out-of-pocket expenses, are classified as revenue, with the associated costs included in cost of revenue.

RESEARCH AND DEVELOPMENT

Research and development costs for internally-developed products are expensed when incurred until technological feasibility has been established for the product. Thereafter, all software costs are capitalized until the product is available for general release to customers. The Company determines technological feasibility at the time the product reaches beta in its stage of development. Historically, the time incurred between beta and general release to customers has been short, and therefore, the costs have been insignificant. As a result, the Company has not capitalized software costs associated with internally-developed products.

The cost of acquired software for products determined to have reached technological feasibility is capitalized; otherwise the cost is expensed. Capitalized software costs are amortized using the straight-line method over the economic life of the product, which is typically two to five years.

INCOME TAXES

The Company accounts for income taxes under the liability method. Under this method, a deferred tax asset or liability is determined based upon the differences between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Tax credits are recorded as a reduction in income taxes. Valuation allowances are provided if, based upon the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

NET INCOME (LOSS) PER SHARE

Basic net income (loss) per share is computed by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted net income (loss) per share is computed by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding for the period plus potential dilutive common shares. All potential dilutive common shares are excluded from the computation of net loss per share because they are antidilutive. Dilutive common equivalent shares consist of stock options and are calculated using the treasury stock method.

COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) is defined as the change in equity of a company during a period from transactions and other events and circumstances, excluding transactions resulting from investments by owners and distributions to owners. Other comprehensive income (loss) consists of foreign currency translation adjustments, unrealized gains and losses on available-for-sale investments, net of tax, and gains and losses on long-term intercompany loans and their associated currency swaps, net of tax.

CONCENTRATIONS OF RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents, investments, and trade receivables. The Company primarily invests in municipal obligations of state and local government entities. The Company has established guidelines relative to credit ratings, diversification, and maturities of its debt securities that maintain safety and liquidity. The Company has not experienced any significant realized losses on its debt securities.

A significant portion of the Company's sales and receivables are from customers who are either in or who serve the semiconductor and electronics industries. The Company performs ongoing credit evaluations of its customers and maintains allowances for potential credit losses. The Company has not experienced any significant losses related to the collection of its accounts receivable.

A significant portion of the Company's MVSD inventory is manufactured by a third-party contractor. The Company is dependent upon this contractor to provide quality product and meet delivery schedules. The Company engages in extensive product quality programs and processes, including actively monitoring the performance of its third-party manufacturers.

DERIVATIVE INSTRUMENTS

The Company has adopted the accounting and disclosure requirements of Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 requires that all derivative instruments be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in current operations or in shareholders' equity as other comprehensive income (loss), depending upon whether the derivative is designated as part of a hedge transaction and, if it is, the type of hedge transaction. Hedges of underlying exposures are designated and documented at the inception of the hedge and are evaluated for effectiveness at least quarterly. As the terms of the derivative are generally matched at inception with the underlying exposure, hedging effectiveness is calculated by comparing the change in fair value of the derivative to the change in fair value of the underlying exposure.

In certain instances, the Company enters into forward contracts and currency swaps to hedge against foreign currency fluctuations. Currency swaps are used to hedge long-term transactions between the Company and its subsidiaries. Forward contracts are used to provide an economic hedge against transactions denominated in currencies other than the functional currencies of the Company or its subsidiaries.

These forward contracts and currency swaps are used to reduce the Company's risk associated with exchange rate changes, as the gains or losses on these contracts are intended to offset the losses or gains on the underlying exposures. The Company does not engage in foreign currency speculation.

STOCK-BASED COMPENSATION PLANS

The Company has adopted the disclosure requirements of Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation," and SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123." The Company continues to recognize compensation costs using the intrinsic value based method described in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." No compensation costs were recognized in 2004, 2003, or 2002.

Net income (loss) and net income (loss) per share as reported in these consolidated financial statements and on a pro forma basis, as if the fair value based method described in SFAS No. 123 had been adopted, are as follows (in thousands, except per share amounts):

Year Ended December 31,	2004	2003	2002
Net income (loss), as reported	$ 37,744	$ 15,951	$ (6,027)
Less: Total stock-based compensation costs determined under fair value based method, net of tax	(13,183)	(14,092)	(17,235)
Net income (loss), pro forma	$ 24,561	$ 1,859	$ (23,262)
Basic net income (loss) per share, as reported	$ 0.83	$ 0.37	$ (0.14)
Basic net income (loss) per share, pro forma	$ 0.54	$ 0.04	$ (0.53)
Diluted net income (loss) per share, as reported	$ 0.80	$ 0.36	$ (0.14)
Diluted net income (loss) per share, pro forma	$ 0.49	$ 0.04	$ (0.53)

For the purpose of providing pro forma disclosures, the fair values of stock options granted were estimated using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants:

Year Ended December 31,	2004	2003	2002
Risk-free interest rate	2.5%	2.1%	3.5%
Expected life (in years)	3.1	2.9	2.9
Expected volatility	45%	58%	57%
Expected annualized dividend yield	.73%	.85%	-

TREASURY STOCK

Effective July 1, 2004, the Massachusetts Business Corporation Act (the "Act") eliminated the concept of treasury shares. Under the Act, shares previously classified as treasury shares are to be treated as authorized but unissued shares of common stock. As a result of this change, the Company reclassified its treasury shares to authorized but unissued shares of common stock on the Consolidated Balance Sheet.

NOTE 2: NEW PRONOUNCEMENTS

On December 16, 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard (SFAS) No. 123R, "Share-Based Payment," which is a revision of SFAS No. 123, "Accounting for Stock-Based Compensation." SFAS No. 123R requires companies to recognize compensation cost for all share-based payments to employees (including stock option and employee stock purchase plans) at fair value. SFAS 123R will be effective for public companies for interim or annual periods beginning after June 15 , 2005. The Company will adopt SFAS No. 123R beginning in the third quarter of 2005 using the modified prospective method in which compensation cost is recognized beginning on the effective date.

The Company currently recognizes compensation costs using the intrinsic value based method and, as such, generally recognizes no compensation cost. Accordingly, the adoption of SFAS No. 123R's fair value based method will have a significant impact on the Company's results of operations, although it will have no impact on its overall financial position. The impact of adoption of SFAS No. 123R cannot be predicted at this time because it will depend upon levels of share-based payments granted in the future. However, had the Company adopted SFAS No. 123R in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as described in the disclosure of pro forma net income (loss) and net income (loss) per share in Note 1 to the Company's consolidated financial statements.

NOTE 3: FOREIGN CURRENCY RISK MANAGEMENT

The Company enters into currency swaps to hedge the foreign currency exposure of its long-term intercompany loans between the parent and certain of its European subsidiaries. These contracts, which relate to the Euro Dollar, have original terms of two to five years. These hedges have been designated for hedge accounting. They are classified as net investment hedges, with the gains or losses on the currency swaps, along with the associated losses or gains on the intercompany loans, net of tax, recorded in shareholders' equity as other comprehensive income (loss) to the extent they are effective as a hedge. The Company recorded net foreign currency losses of $1,730,000, $625,000, and $35,000 in other comprehensive income (loss) on the intercompany loans and associated currency swaps in 2004, 2003, and 2002, respectively.

The Company enters into forward contracts to hedge the foreign currency exposure of a portion of its intercompany transactions between its subsidiaries and to hedge the foreign currency exposure of its Irish subsidiary's accounts receivable denominated in U.S. Dollars and Japanese Yen. These contracts, which relate to the Euro Dollar and Japanese Yen, generally have terms of one to four months. These hedges have been deemed economic hedges and have not been designated for hedge accounting. They are classified as fair value hedges, with the gains or losses on the forward contracts, along with the associated losses or gains on the revaluation and settlement of the intercompany balances and accounts receivable, recorded in current operations. In addition to the transactions described above that are included in the Company's hedging program, the Company enters into other transactions denominated in foreign currencies for which the exchange rate gains or losses are included in current operations. The Company recorded net foreign currency gains of $1,641,000 in 2004, net foreign currency losses of $1,712,000 in 2003, and net foreign currency gains of $350,000 in 2002, representing the total net exchange rate gains or losses that are recognized in current operations.

NOTE 4: CASH, CASH EQUIVALENTS, AND INVESTMENTS

Cash, cash equivalents, and investments consist of the following (in thousands):

December 31,	2004	2003
Cash	$ 54,270	$ 49,980
Total cash and cash equivalents	54,270	49,980
Municipal bonds	180,409	82,653
Total short-term investments	180,409	82,653
Municipal bonds	144,685	156,511
Corporate bonds	-	4,212
Limited partnership interest	11,712	10,146
Total long-term investments	156,397	170,869
	$ 391,076	$ 303,502

In connection with the preparation of the accompanying consolidated financial statements, the Company concluded that it was appropriate to classify its auction rate securities as short-term investments. Previously, such securities were classified as cash and cash equivalents. Accordingly, the Company revised the classification to exclude from cash and cash equivalents $26,247,000 at December 31, 2003 and to include such amounts in short-term investments on the Consolidated Balance Sheets. This revised classification was also reflected in the Consolidated Statements of Cash Flows for all periods presented to reflect gross purchases and sales of these investments, which had the impact of increasing net cash used in investing activities by $23,847,000 in 2003 and increasing net cash provided by investing activities by $4,901,000 in 2002. This change in classification did not affect previously reported cash flows from operations or financing activities, or the results of operations and statements of shareholders' equity for the periods presented.

The following is a summary of the Company's available-for-sale investments at December 31, 2004 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term municipal bonds	$ 180,627	$ 14	$ (232)	$ 180,409
Long-term municipal bonds	145,540	5	(860)	144,685
	$ 326,167	$ 19	$ (1,092)	$ 325,094

The Company recorded gross realized gains on the sale of debt securities totaling $392,000 in 2004, $1,222,000 in 2003, and $1,112,000 in 2002. The Company recorded gross realized losses on the sale of debt securities totaling $90,000 in 2004, $24,000 in 2003, and $25,000 in 2002.

On June 30, 2000, Cognex Corporation became a Limited Partner in Venrock Associates III, L.P. (Venrock), a venture capital fund. A director of the Company is a Managing General Partner of Venrock Associates. In the original agreement with Venrock, the Company committed to a total investment in the limited partnership of up to $25,000,000 with an expiration date of January 1, 2005. In January 2005, the Company signed an amendment to the original agreement with Venrock, which reduces its total commitment to $22,500,000 and extends the commitment period through December 31, 2010. The Company does not have the right to withdraw from the partnership prior to December 31, 2010. As of December 31, 2004, the Company had contributed $15,875,000 to the partnership, including $2,250,000 during 2004. Venrock returned $838,000 to the Company during 2004 representing realized gains on the sale of certain investments in the portfolio.

At December 31, 2004, the carrying value of this investment was $11,712,000 compared to an estimated fair value, as determined by the General Partner, of $10,730,000. The unrealized loss of $982,000 was determined to be temporary.

NOTE 5: INVENTORIES

Inventories consist of the following (in thousands):

December 31,	2004	2003
Raw materials	$ 6,311	$ 7,831
Work-in-process	6,285	3,323
Finished goods	7,495	4,365
	$20,091	$ 15,519

In the fourth quarter of 2001, the Company recorded a $16,300,000 charge in "Cost of product revenue" on the Consolidated Statement of Operations for excess inventories and purchase commitments resulting from an extended slowdown in the semiconductor and electronics industries, as well as the expected transition to newer Cognex hardware platforms by the Company's OEM customers. A total of $12,500,000 of this charge represented reserves against existing inventories and was accordingly included in "Inventories" on the Consolidated Balance Sheet at December 31, 2001. The remaining $3,800,000 of the charge represented commitments to purchase excess components and systems from various suppliers and accordingly was included in "Accrued Expenses" on the Consolidated Balance Sheet at December 31, 2001.

The following table summarizes the change in the inventory-related reserve established in the fourth quarter of 2001 (in thousands):

	Balance Sheet		Statement of Operations
	Inventories	Accrued Expenses	Benefits
Initial charge in the fourth quarter of 2001	$ 12,500	$ 3,800	-
Inventory sold to customers	(1,790)	-	$ 1,790
Settlement of purchase commitments	1,506	(2,400)	894
Reserve balance at December 31, 2002	$ 12,216	$ 1,400	
Benefits to cost of product revenue recorded in 2002			$ 2,684
Inventory sold to customers	(1,290)	-	1,290
Inventory sold to brokers	(667)	-	-
Write-off and scrap of inventory	(876)	-	-
Reserve balance at December 31, 2003	$ 9,383	$ 1,400	
Benefits to cost of product revenue recorded in 2003			$ 1,290
Inventory sold to customers	(805)	-	805
Inventory sold to brokers	(387)	-	-
Write-off and scrap of inventory	(743)	-	-
Reserve balance at December 31, 2004	$ 7,448	$ 1,400	
Benefits to cost of product revenue recorded in 2004			$ 805

A favorable settlement of the remaining purchase commitments may result in a recovery of a portion of the remaining $1,400,000 accrued at December 31, 2004.

NOTE 6: PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment consist of the following (in thousands):

December 31,	2004	2003
Land	$ 3,051	$ 3,051
Buildings	17,571	17,571
Building improvements	4,622	4,156
Computer hardware and software	33,826	32,100
Furniture and fixtures	4,183	3,919
Leasehold improvements	2,197	2,308
	65,450	63,105
Less: accumulated depreciation	(41,45)	(38,125)
	$ 23,995	$ 24,980

Buildings include property held for lease with a cost $4,950,000 at December 31, 2004 and 2003 and accumulated depreciation of $1,206,000 and $1,079,000 at December 31, 2004 and 2003, respectively.

NOTE 7: INTANGIBLE ASSETS

Intangible assets consist of the following (in thousands):

	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
December 31, 2004			
Customer contracts and relationships	$ 8,349	$ 1,522	$ 6,827
Complete technology	5,440	4,864	576
Patents	122	42	80
Noncompete agreements	54	31	23
	$ 13,965	$ 6,459	$ 7,506
December 31, 2003			
Customer contracts and relationships	$ 7,832	$ 492	$ 7,340
Complete technology	5,388	4,280	1,108
Patents	113	17	96
Noncompete agreements	50	12	38
	$ 13,383	$ 4,801	$ 8,582

Aggregate amortization expense was $1,526,000 in 2004, $1,012,000 in 2003, and $543,000 in 2002. Estimated amortization expense for each of the five succeeding fiscal years and thereafter is as follows (in thousands):

Year ended December 31,	Amount
2005	$ 1,315
2006	1,195
2007	1,136
2008	1,035
2009	1,001
Thereafter	1,824
	$ 7,506

NOTE 8: GOODWILL

The Company has two reporting units with goodwill, the Modular Vision Systems Division (MVSD) and the Surface Inspection Systems Division (SISD), which are also reportable segments.

The changes in the carrying value of goodwill are as follows (in thousands):

	MVSD	SISD	Consolidated
Balance at December 31, 2002	$ 1,488	$ 2,254	$ 3,742
Business acquisitions (Note 18)	2,753	-	2,753
Foreign exchange rate changes	281	446	727
Balance at December 31, 2003	$ 4,522	$ 2,700	$ 7,222
Purchase price adjustment (Note 18)	(514)	-	(514)
Foreign exchange rate changes	113	212	325
Balance at December 31, 2004	$ 4,121	$ 2,912	$ 7,033

NOTE 9: ACCRUED EXPENSES

Accrued expenses consist of the following (in thousands):

December 31,	2004	2003
Forward contracts and currency swaps	$ 19,527	$12,971
Income taxes	9,165	3,017
Company bonuses	5,979	423
Consumption taxes	4,900	2,368
Salaries, commissions, and payroll taxes	3,452	2,340
Vacation	2,775	2,348
Warranty obligations	1,758	2,119
Professional fees	1,698	1,780
Purchase commitments	1,400	1,400
Other	5,125	3,332
	$ 55,779	$32,098

The changes in the warranty obligation are as follows (in thousands):

Balance at December 31, 2002	$ 1,523
Provisions for warranties issued during the period	1,591
Provisions related to pre-existing warranties	550
Fulfillment of warranty obligations	(1,771)
Foreign exchange rate changes	226
Balance at December 31, 2003	$ 2,119
Provisions for warranties	797
Fulfillment of warranty obligations	(1,298)
Foreign exchange rate changes	140
Balance at December 31, 2004	$ 1,758

NOTE 10: COMMITMENTS

At December 31, 2004, the Company had purchase orders totaling $4,960,000 to purchase inventory from various vendors. These purchase commitments relate to expected sales in 2005.

The Company conducts certain of its operations in leased facilities. These lease agreements expire at various dates through 2014 and are accounted for as operating leases. Annual rental expense totaled $4,662,000 in 2004, $4,427,000 in 2003, and $4,536,000 in 2002. Future minimum rental payments under these agreements are as follows (in thousands):

Year ended December 31,	Amount
2005	$ 3,878
2006	977
2007	349
2008	192
2009	190
Thereafter	445
	$ 6,031

The Company owns an 83,000 square-foot office building adjacent to its corporate headquarters. The building is currently occupied with tenants who have lease agreements that expire at various dates through 2007. Annual rental income totaled $818,000 in 2004, $1,137,000 in 2003, and $1,224,000 in 2002. Rental income and related expenses are included in "Investment and other income" on the Consolidated Statement of Operations. Future minimum rental receipts under non-cancelable lease agreements are $891,000 in 2005 and 2006, $294,000 in 2007, $95,000 in 2008, and $40,000 in 2009.

NOTE 11: INDEMNIFICATION PROVISIONS

Except as limited by Massachusetts law, the by-laws of the Company require it to indemnify certain current or former directors, officers, and employees of the Company against expenses incurred by them in connection with each proceeding in which he or she is involved as a result of serving or having served in certain capacities. Indemnification is not available with respect to a proceeding as to which it has been adjudicated that the person did not act in good faith in the reasonable belief that the action was in the best interests of the Company. The maximum potential amount of future payments the Company could be required to make under these provisions is unlimited. The Company has never incurred significant costs related to these indemnification provisions. As a result, the Company believes the estimated fair value of these provisions is minimal.

The Company accepts standard limited indemnification provisions in the ordinary course of business, whereby it indemnifies its customers for certain direct damages incurred in connection with third-party patent or other intellectual property infringement claims with respect to the use of the Company's products. The term of these indemnification provisions generally coincides with the customer's use of the Company's products. The maximum potential amount of future payments the Company could be required to make under these provisions is always subject to fixed monetary limits. The Company has never incurred significant costs to defend lawsuits or settle claims related to these indemnification provisions. As a result, the Company believes the estimated fair value of these provisions is minimal.

The Company also accepts limited indemnification provisions from time to time, whereby it indemnifies customers for certain direct damages incurred in connection with bodily injury and property damage arising from the installation of the Company's products. The term of these indemnification provisions generally coincides with the period of installation. The maximum potential amount of future payments the Company could be required to make under these provisions is limited and is likely recoverable under the Company's insurance policies. As a result of this coverage, and the fact that the Company has never incurred significant costs to defend lawsuits or settle claims related to these indemnification provisions, the Company believes the estimated fair value of these provisions is minimal.

NOTE 12: STANDBY LETTERS OF CREDIT

On March 25, 2004, the Company provided standby letters of credit totaling 3,146,280,000 Yen (or approximately $30,722,000) to taxing authorities in Japan that are collateralized by investments on the Consolidated Balance Sheet. The Tokyo Regional Taxation Bureau (TRTB) has asserted that Cognex Corporation has a permanent establishment in Japan that would require certain income, previously reported on U.S. tax returns for the years ended December 31, 1997 through December 31, 2001, to be subject instead to taxation in Japan. The Company disagrees with this position and believes that this assertion is inconsistent with principles under the U.S. - Japan income tax treaty. The Company has filed a notice of objection and request for deferral of tax payment and intends to contest this assessment vigorously, although no assurances can be made that the Company will prevail in this matter. In September 2003, the Company also filed a request with the Internal Revenue Service Tax Treaty Division for competent authority assistance. Until this matter is resolved, the Company is required to provide collateral for these tax assessments. These letters of credit expire in approximately one year. Should the TRTB prevail in its assertion, the income in question would be taxable in Japan and the Company would be required to pay approximately $30,722,000 in taxes, interest, and penalties to Japanese taxing authorities. The Company would then be entitled to recoup the majority of this amount from taxing authorities in the U.S.

NOTE 13: SHAREHOLDERS' EQUITY

PREFERRED STOCK

The Company has 400,000 shares of authorized but unissued $.01 par value preferred stock.

STOCK REPURCHASE PROGRAM

On December 12, 2000, the Company's Board of Directors authorized the repurchase of up to $100,000,000 of the Company's common stock. During 2002, a total of 1,768,452 shares were repurchased at a cost of $26,425,000. There have been no other shares repurchased under this program.

STOCK OPTION PLANS

At December 31, 2004, the Company had 9,311,319 shares available for grant under the following stock option plans: the 1998 Director Plan, 4,000; the 1998 Stock Incentive Plan, 1,807,319; no shares under the 2001 Interim General Stock Incentive Plan; and the 2001 General Stock Option Plan, 7,500,000.

The 2001 General Stock Option Plan was adopted by the Board of Directors on December 11, 2001 without shareholder approval. This plan provides for the granting of nonqualified stock options to any employee who is actively employed by the Company and is not an officer or director of the Company. The maximum number of shares of common stock available for grant under the plan is 7,500,000 shares. All option grants must have an exercise price per share that is no less than the fair market value per share of the Company's common stock on the grant date and must have a term that is no longer than fifteen years from the grant date. No stock options have been granted under the 2001 General Stock Option Plan.

The 2001 Interim General Stock Incentive Plan was adopted by the Board of Directors on July 17, 2001 without shareholder approval. This plan provides for the granting of nonqualified stock options to any employee who is actively employed by the Company and is not an officer or director of the Company. The maximum number of shares of common stock available for grant under the plan is 400,000 shares. All option grants have an exercise price per share that is no less than the fair market value per share of the Company's common stock on the grant date and must have a term that is no longer than fifteen years from the grant date. All 400,000 stock options have been granted under the 2001 Interim General Stock Incentive Plan.

On April 21, 1998, the shareholders approved the 1998 Stock Incentive Plan, under which the Company initially was able to grant stock options and stock awards to purchase up to 1,700,000 shares of common stock. Effective January 1, 1999 and each January 1st thereafter during the term of the 1998 Stock Incentive Plan, the number of shares of common stock available for grants of stock options and stock awards is increased automatically by an amount equal to 4.5% of the total number of issued shares of common stock as of the close of business on December 31st of the preceding year.

Stock options generally vest over four years and generally expire no later than ten years from the date of grant.

The following table summarizes the status of the Company's stock option plans at December 31, 2004, 2003, and 2002, and changes during the years then ended (shares in thousands):

	2004		2003		2002	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	10,986	$ 22.85	10,381	$ 22.40	9,529	$ 22.31
Granted at fair market value	2,253	29.31	2,402	21.54	2,211	21.38
Exercised	(2,210)	19.78	(1,279)	15.84	(550)	12.56
Forfeited	(409)	26.06	(518)	25.75	(809)	25.26
Outstanding at end of year	10,620	24.74	10,986	22.85	10,381	22.40
Options exercisable at year-end	5,074	24.52	5,182	22.37	4,156	19.01
Weighted-average grant-date fair value of options granted during the year at fair market value	$ 9.22		$ 8.32		$ 8.39	

No stock options were granted above fair market value in 2004, 2003, or 2002.

The following table summarizes information about stock options outstanding at December 31, 2004 (shares in thousands):

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$ 1.00 - 18.13	1,981	5.2	$ 14.00	1,461	$ 12.79
18.19 - 21.73	1,847	8.3	21.05	353	20.62
21.74 - 24.45	1,568	6.8	22.34	864	22.45
24.49 - 28.51	1,165	7.3	25.67	700	25.53
28.67 - 28.90	1,913	8.8	28.69	316	28.77
28.95 - 59.69	2,146	7.6	35.56	1,380	37.76
	10,620	7.3	24.74	5,074	24.52

EMPLOYEE STOCK PURCHASE PLAN

Under the Company's Employee Stock Purchase Plan (ESPP), employees who have completed six months of continuous employment with the Company may purchase common stock semi-annually at the lower of 85% of the fair market value of the stock at the beginning or end of the six-month payment period through accumulation of payroll deductions. Employees are required to hold common stock purchased under the ESPP for a period of one year from the date of purchase. The maximum number of shares of common stock available for issuance under the ESPP is 250,000 shares. Effective January 1, 2001 and each January 1st thereafter during the term of the ESPP, 250,000 shares of common stock will always be available for issuance. Shares purchased under the ESPP totaled 21,031 in 2004, 31,667 in 2003, and 38,105 in 2002. The weighted-average fair value of shares purchased under the ESPP was $10.61 in 2004, $9.89 in 2003, and $5.73 in 2002.

For the purpose of providing pro forma disclosures, the fair values of shares purchased were estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions:

Year Ended December 31,	2004	2003	2002
Risk-free interest rate	2.3%	2.0%	1.5%
Expected life (in months)	12	12	6
Expected volatility	39%	58%	57%
Expected annualized dividend yield	1.00%	.85%	-

NOTE 14: EMPLOYEE SAVINGS PLAN

Under the Company's Employee Savings Plan, a defined contribution plan, employees who have attained age 21 may contribute up to 25% of their salary on a pre-tax basis subject to the annual dollar limitations established by the Internal Revenue Service. The Company contributes fifty cents for each dollar an employee contributes, with a maximum contribution of 3% of an employee's pre-tax salary. Company contributions vest 20%, 40%, 60%, and 100% after two, three, four, and five years of continuous employment with the Company, respectively. Company contributions totaled $967,000 in 2004, $917,000 in 2003, and $869,000 in 2002. Cognex stock is not an investment alternative, nor are Company contributions made in the form of Cognex stock.

NOTE 15: INCOME TAXES

Domestic income before taxes was $22,507,000, $24,852,000, and $3,422,000 and foreign income (loss) before taxes was $30,653,000, $(1,604,000), and $(11,626,000) in 2004, 2003, and 2002, respectively.

The provision (benefit) for income taxes consists of the following (in thousands):

Year Ended December 31,	2004	2003	2002
Current:			
Federal	$ 9,662	$ 6,330	$ (1,930)
State	758	431	48
Foreign	983	2,181	1,040
	11,403	8,942	(842)
Deferred:			
Federal	(177)	(616)	524
State	306	48	(51)
Foreign	3,884	(1,077)	(1,808)
	4,013	(1,645)	(1,335)
	$ 15,416	$ 7,297	$ (2,177)

A reconciliation of the United States federal statutory corporate tax to the Company's effective tax is as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Income tax provision (benefit) at federal statutory rate	$ 18,606	$ 8,137	$ (2,871)
State income taxes, net of federal benefit	1,070	325	67
Tax-exempt investment income	(1,463)	(1,901)	(2,992)
Foreign tax rate differential	(3,138)	1,023	2,934
Goodwill amortization and impairment charges	-	-	846
Other	341	(287)	(161)
Provision (benefit) for income taxes	$ 15,416	$ 7,297	$ (2,177)

Deferred tax assets consist of the following (in thousands):

December 31,	2004	2003
Current deferred tax assets:		
Inventory and revenue related	$ 6,321	$ 6,494
Bonus, commission, and other compensation	937	500
Other	2,246	1,229
Total net current deferred tax asset	$ 9,504	$ 8,223
Noncurrent deferred tax assets (liabilities):		
Federal and state tax credit carryforwards	$ 8,138	$ 6,638
Net operating loss carryforwards	3,989	5,519
Acquired complete technology and other intangibles	3,180	3,353
Federal and state capital loss carryforwards	1,640	1,694
Unrealized investment gains (losses)	1,573	(462)
Depreciation	1,339	1,308
Acquired in-process technology	972	1,021
Other	685	357
Total net noncurrent deferred tax asset	$ 21,516	$ 19,428

At December 31, 2004, the Company had federal research and experimentation tax credit carryforwards of approximately $4,424,000, which may be available to offset future federal income tax liabilities and will begin to expire in 2015. The Company also had approximately $2,290,000 of alternative minimum tax credits and approximately $991,000 of foreign tax credits, which may be available to offset future regular income tax liabilities. The alternative minimum tax credits have an unlimited life and the foreign tax credits will begin to expire in 2007. In addition, the Company had approximately $433,000 of state research and experimentation tax credit carryforwards, which will begin to expire in 2015.

At December 31, 2004, the Company's subsidiaries had net operating loss carryforwards of approximately $15,688,000, of which $9,011,000, representing a tax benefit of $3,154,000, will expire in 2009. The remaining balance of $6,677,000, representing a tax benefit of $835,000, has an unlimited life.

The Company did not establish valuation allowances against its deferred tax assets at December 31, 2004 and 2003. While these assets are not assured of realization, the Company has evaluated the realizability of these deferred tax assets and has determined that it is more likely than not that these assets will be realized. In reaching this conclusion, the Company has evaluated certain relevant criteria including the Company's historical profitability, current projections of future profitability, and the lives of tax credits, net operating and capital losses, and other carryforwards. Should the Company fail to generate sufficient pre-tax profits in future periods, the Company may be required to establish valuation allowances against these deferred tax assets, resulting in a charge to income in the period of determination.

The Company files income tax returns in all jurisdictions in which it operates. The Company has established reserves to provide for additional income taxes that may be due in future years as these previously filed tax returns are audited. These reserves have been established based upon management's assessment as to the potential exposure attributable to permanent differences and interest applicable to both permanent and temporary differences. All tax reserves are analyzed periodically and adjustments are made as events occur that warrant modification.

The Company does not provide U.S. taxes on its foreign subsidiaries' undistributed earnings, as they are deemed to be permanently reinvested outside the U.S. Non-U.S. income taxes are, however, provided on those foreign subsidiaries' undistributed earnings. Upon repatriation, the Company would provide the appropriate U.S. income taxes on these earnings.

On October 22, 2004, the American Jobs Creation Act of 2004 (the "Act") was signed into law. The Act creates a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the U.S. at an effective tax rate of 5.25%. On November 15, 2004, the Financial Accounting Standards Board issued proposed Statement of Financial Accounting Standard (SFAS) No. 109-2, "Accounting and Disclosure for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004." SFAS No. 109-2 would allow companies additional time to evaluate the effect of the law on whether unrepatriated foreign earnings continue to qualify for SFAS No. 109's exception to recognizing deferred tax liabilities and would require explanatory disclosures from those companies who need the additional time. Through December 31, 2004, the Company had not provided deferred taxes on foreign earnings because such earnings were intended to be indefinitely reinvested outside the U.S. Whether the Company will ultimately take advantage of this provision depends upon a number of factors, including reviewing future Congressional guidance, before a decision can be made. Until that time, the Company will not change its current intention to indefinitely reinvest accumulated earnings of its foreign subsidiaries.

NOTE 16: NET INCOME (LOSS) PER SHARE

Net income (loss) per share is calculated as follows (in thousands, except per share amounts):

Year Ended December 31,	2004	2003	2002
Net income (loss)	$ 37,744	$ 15,951	$ (6,027)
Basic:			
Weighted-average common shares outstanding	45,480	43,173	43,503
Net income (loss) per common share	$ 0.83	$ 0.37	$ (0.14)
Diluted:			
Weighted-average common shares outstanding	45,480	43,173	43,503
Effect of dilutive stock options	1,878	1,293	-
Weighted-average common and common equivalent shares outstanding	47,358	44,466	43,503
Net income (loss) per common and common equivalent share	$ 0.80	$ 0.36	$ (0.14)

Stock options to purchase 1,656,927, 2,934,936, and 6,347,233 shares of common stock were outstanding in 2004, 2003, and 2002, respectively, but were not included in the calculation of diluted net income (loss) per share because the options' exercise prices were greater than the average market price of the Company's common stock during those years. Additionally, stock options to purchase 939,961 shares of common stock were not included in the calculation of diluted net loss per share in 2002 because they were antidilutive.

NOTE 17: SEGMENT AND GEOGRAPHIC INFORMATION

The Company has two reportable segments: the Modular Vision Systems Division (MVSD) and the Surface Inspections Systems Division (SISD). MVSD designs, develops, manufactures, and markets modular vision systems that are used to control the manufacturing of discrete items by locating, identifying, inspecting, and measuring them during the manufacturing process. SISD designs, develops, manufactures, and markets surface inspection vision systems that are used to inspect surfaces of materials that are processed in a continuous fashion to ensure there are no flaws or defects in the surfaces. Segments are determined based upon the way that management organizes its business for making operating decisions and assessing performance. The Company evaluates segment performance based upon income or loss from operations, excluding unusual items.

The following table summarizes information about the Company's segments (in thousands):

	MVSD	SISD	Reconciling Items	Consolidated
YEAR ENDED DECEMBER 31, 2004				
Product revenue	$ 155,966	$ 20,603	-	$ 176,569
Service revenue	17,923	7,465	-	25,388
Depreciation and amortization	5,526	341	$ 207	6,074
Operating income (loss)	53,572	1,336	(8,059)	46,849
Year Ended December 31, 2003				
Product revenue	$ 108,170	$ 22,500	-	$ 130,670
Service revenue	12,846	6,576	-	19,422
Depreciation and amortization	5,863	392	$ 179	6,434
Operating income (loss)	21,397	3,830	(5,717)	19,510
Year Ended December 31, 2002				
Product revenue	$ 78,270	$ 17,932	-	$ 96,202
Service revenue	12,088	5,817	-	17,905
Depreciation and amortization	6,487	388	$ 202	7,077
Operating income (loss)	(497)	1,369	(10,630)	(9,758)

Reconciling items consist of unallocated corporate expenses, which primarily include corporate headquarters costs, professional fees, and patent infringement litigation. Asset information by segment is not produced internally for use by the chief operating decision maker, and therefore, is not presented. Asset information is not provided because the cash and investments are commingled and the divisions share assets and resources in a number of locations around the world.

No customer accounted for greater than 10% of revenue in 2004, 2003, or 2002.

The following table summarizes information about geographic areas (in thousands):

	United States	Japan	Ireland	Other	Consolidated
YEAR ENDED DECEMBER 31, 2004					
Product revenue	$ 50,548	-	$ 126,021	-	$ 176,569
Service revenue	16,254	-	9,134	-	25,388
Long-lived assets	26,217	$ 2,396	12,797	$ 1,024	42,434
Year Ended December 31, 2003					
Product revenue	$ 43,001	-	$ 87,669	-	$ 130,670
Service revenue	12,792	-	6,630	-	19,422
Long-lived assets	27,921	$ 2,434	13,358	$ 925	44,638
Year Ended December 31, 2002					
Product revenue	$ 44,292	$ 14,355	$ 37,555	-	$ 96,202
Service revenue	13,263	2,119	2,523	-	17,905
Long-lived assets	28,891	3,077	2,744	$ 1,040	35,752

Revenue is presented geographically based upon the country in which the sale is recorded. The "Other" column represents all long-lived assets in other countries, none of which were individually significant.

NOTE 18: ACQUISITIONS

ACQUISITION OF SIEMENS DEMATIC AG WAFER IDENTIFICATION BUSINESS

On March 31, 2003, the Company acquired the wafer identification business of Siemens Dematic AG, a subsidiary of Siemens AG. Siemens Dematic is a leading supplier of logistics and factory automation equipment and has been a leading supplier of wafer identification systems to semiconductor manufacturers in Europe. Under the terms of the agreement, the Company acquired the rights to all of Siemens' patented and unpatented wafer identification technology, as well as substantially all of the assets related to its wafer identification business. This acquisition enhances the Company's position as a leading provider of wafer identification systems worldwide. The results of operations of the acquired business have been included in the Company's consolidated results of operations since the date of the acquisition. The historical results of operations of the acquired business were not material compared to the consolidated results of operations, and therefore, pro forma results are not presented.

The original purchase price consisted of 7,000,000 Euros in cash (or approximately $7,630,000) paid on March 31, 2003, with the potential for an additional cash payment in 2005 of up to 1,700,000 Euros (or approximately $2,306,000) depending upon the achievement of certain performance criteria. Any contingent consideration will be recorded as purchase price when paid and will be allocated to goodwill. The March 31, 2003 cash payment of 7,000,000 Euros was based upon an estimated balance sheet for the wafer identification business as of March 31, 2003. After receipt of a final March 31, 2003 balance sheet and resolution of certain items in dispute, Siemens reimbursed Cognex 796,000 Euros (or $868,000), of which $354,000 was allocated to receivables and $514,000 was allocated to goodwill.

The final purchase price of 6,204,000 Euros (or approximately $6,762,000) was allocated as follows: $616,000 to inventories; $274,000 to receivables; $25,000 to accrued expenses; $4,469,000 to customer contracts and relationships, to be amortized over eight years; $447,000 to complete technology, to be amortized over five years; $98,000 to patents, to be amortized over five years; $44,000 to non-compete agreements, to be amortized over three years; and $839,000 to goodwill, which is assigned to the MVSD segment and is not deductible for tax purposes.

ACQUISITION OF GAVITEC AG MACHINE VISION BUSINESS

On December 1, 2003, the Company acquired the machine vision business of Gavitec AG. Gavitec produces machine vision products for direct part mark identification (or Industrial ID), which can read markings on the surfaces of manufactured items to collect data about product components during the manufacturing process and trace the manufacturing history of the components during the product's lifetime. Under the terms of the agreement, the Company acquired all of the tangible and intangible assets and assumed certain liabilities associated with Gavitec's machine vision business. This acquisition strengthens the Company's overall market position in Germany and combines Gavitec's experience in the design of easy-to-use Industrial ID products with Cognex's global sales force and engineering support to enable the Company to provide additional products for the growing Industrial ID market. The results of operations of the acquired business have been included in the Company's consolidated results of operations since the date of the acquisition. The historical results of operations of the acquired business were not material compared to the consolidated results of operations, and therefore, pro forma results are not presented.

The net purchase price consisted of 3,777,000 Euros in cash (or approximately $4,516,000), including 3,477,000 Euros paid at closing, 100,000 Euros (or approximately $123,000) paid on December 1, 2004, and 200,000 Euros (or approximately $271,000) to be paid on December 1, 2005. There was the potential for two additional cash payments of up to 250,000 Euros (or approximately $339,000) each in the third quarter of 2004 and first quarter of 2005 depending upon the achievement of certain performance criteria. These criteria were not met, and therefore, these contingent payments were not made.

The purchase price was allocated as follows: $213,000 to inventories; $76,000 to receivables; $60,000 to fixed assets; $114,000 to accrued expenses; $2,726,000 to customer contracts and relationships, to be amortized over nine years; $155,000 to complete technology, to be amortized over three years; and $1,400,000 to goodwill, which is assigned to the MVSD segment and is not deductible for tax purposes.

NOTE 19: DIVIDENDS

Beginning in the third quarter of 2003, the Company's Board of Directors has declared and paid a cash dividend in each quarter. During the third quarter of 2004, the Company's Board of Directors voted to increase the quarterly cash dividend from $0.06 per share to $0.08 per share. Dividend payments amounted to $12,756,000 in 2004 and $5,237,000 in 2003.

NOTE 20: SUBSEQUENT EVENTS

On January 28, 2005, the Company's Board of Directors declared a cash dividend of $0.08 per share. The dividend was paid on February 25, 2005 to all shareholders of record at the close of business on February 11, 2005 and amounted to $3,698,000.

On January 19, 2005, the Company signed an amendment to its agreement with Venrock Associates III L.P., a venture capital fund in which the Company is a limited partner. The amendment reduced the Company's commitment to $22,500,000 from $25,000,000 and extended the commitment period through December 31, 2010.

NOTE 21: SUPPLEMENTAL DISCLOSURES

Cash paid for income taxes totaled $2,327,000 in 2004, $4,169,000 in 2003, and $1,180,000 in 2002.

Common stock received as payment for stock option exercises totaled $317,000 in 2004, $134,000 in 2003 and $2,467,000 in 2002.

The Company retired certain fully depreciated property, plant, and equipment totaling $1,824,000 in 2004, $2,497,000 in 2003, and $5,407,000 in 2002.

Advertising costs are expensed as incurred and totaled $2,000,000 in 2004, $1,684,000 in 2003, and $1,753,000 in 2002.

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF COGNEX CORPORATION:

We have audited the accompanying consolidated balance sheets of Cognex Corporation and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Cognex Corporation and subsidiaries at December 31, 2004 and 2003, and the consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Cognex Corporation and subsidiaries internal control over financial reporting as of December 31 2004, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 4, 2005 expressed an unqualified opinion thereon.

Boston, Massachusetts ERNST & YOUNG LLP March 4, 2005

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF COGNEX CORPORATION:

In our opinion, the accompanying consolidated statements of operations, of shareholders' equity and cash flows for the year ended December 31, 2002 present fairly, in all material respects, the results of operations and cash flows of Cognex Corporation and its subsidiaries for the year ended December 31, 2002, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Boston, Massachusetts PRICEWATERHOUSECOOPERS LLP January 24, 2003

(in thousands, except per share amounts)

STATEMENT OF OPERATIONS DATA:

Year Ended December 31,	2004	2003	2002	2001	2000
Revenue	$ 201,957	$ 150,092	$ 114,107	$ 140,729	$ 250,726
Cost of revenue	57,371	50,139	39,859	62,345	63,820
Gross margin	144,586	99,953	74,248	78,384	186,906
Research, development, and engineering expenses	27,063	24,719	25,630	30,094	33,341
Selling, general, and administrative expenses	70,674	55,724	58,376	61,262	62,015
Amortization of goodwill	-	-	-	3,108	1,964
Charge for intangible asset impairment	-	-	-	10,932	-
Operating income (loss)	46,849	19,510	(9,758)	(27,012)	89,586
Nonoperating income	6,311	3,738	1,554	11,341	10,632
Income (loss) before taxes	53,160	23,248	(8,204)	(15,671)	100,218
Income tax provision (benefit)	15,416	7,297	(2,177)	(4,544)	32,070
Net income (loss)	$ 37,744	$ 15,951	$ (6,027)	$ (11,127)	$ 68,148
Basic net income (loss) per share	$ 0.83	$ 0.37	$ (0.14)	$ (0.25)	$ 1.58
Diluted net income (loss) per share	$ 0.80	$ 0.36	$ (0.14)	$ (0.25)	$ 1.49
Basic weighted-average common shares outstanding	45,480	43,173	43,503	43,639	43,043
Diluted weighted-average common shares outstanding	47,358	44,466	43,503	43,639	45,698
Cash dividends per common share	$ 0.28	$ 0.12	$ -	$ -	$ -

BALANCE SHEET DATA:

December 31,	2004	2003	2002	2001	2000
Working capital	$ 242,460	$ 150,311	$ 162,808	$ 143,712	$ 167,913
Total assets	533,308	432,533	385,934	406,904	436,141
Long-term debt	-	-	-	-	-
Shareholders' equity	462,807	384,994	354,520	378,044	383,949

COGNEX CORPORATION: SELECTED QUARTERLY FINANCIAL (UNAUDITED) 73

(in thousands, except per share amounts and stock prices)

2004 Quarter Ended	April 4	July 4	October 3	December 31
Revenue	$ 48,169	$ 54,467	$ 55,412	$ 43,909
Gross margin	33,380	38,562	40,526	32,118
Operating income	10,168	14,339	15,875	6,467
Net income	8,567	10,878	11,655	6,644
Basic net income per share	0.19	0.24	0.26	0.15
Diluted net income per share	0.18	0.23	0.25	0.14
Cash dividends per common share	0.06	0.06	0.08	0.08
Common stock prices:				
High	35.05	38.48	37.06	29.90
Low	28.24	30.09	23.50	23.14

2003 Quarter Ended	March 30	June 29	September 28	December 31
Revenue	$ 32,888	$ 36,622	$ 38,704	$ 41,878
Gross margin	21,172	24,623	25,514	28,644
Operating income	1,945	4,411	5,507	7,647
Net income	1,793	3,306	5,138	5,714
Basic net income per share	0.04	0.08	0.12	0.13
Diluted net income per share	0.04	0.08	0.11	0.13
Cash dividends per common share	-	-	0.06	0.06
Common stock prices:				
High	24.40	24.00	31.79	31.11
Low	18.17	17.91	20.55	25.00

TRANSFER AGENT
National City Bank
Corporate Trust Operations
3rd Floor, North Annex
4100 West 150th Street
Cleveland, OH 44135-1385
Telephone: (216) 257-8663
Toll free: (800) 622-6757

GENERAL COUNSEL
Goodwin Procter LLP
Boston, Massachusetts

INDEPENDENT AUDITORS
Ernst & Young LLP
Boston, Massachusetts

FORM 10-K
A copy of the Annual Report on Form 10-K filed with the Securities and Exchange Commission is available to shareholders, without charge, upon request to:

Department of Investor Relations
Cognex Corporation
One Vision Drive
Natick, MA 01760

Additional copies of this annual report are also available, without charge, upon request to the above address, or on-line at http://www.cognex.com

The Company's report on internal controls over financial reporting and the report of the Company's independent registered accounting firm is included in Item 9A of the Annual Report on Form 10-K.

The Company's common stock is traded on the NASDAQ Stock Market, under the symbol CGNX. As of February 11, 2005, there were approximately 600 shareholders of record of the Company's common stock. The Company believes the number of beneficial owners of the Company's common stock on that date was substantially greater.

The Company declared and paid a cash dividend of $0.06 per share in the first and second quarters of 2004, and a cash dividend of $0.08 per share in the third and fourth quarters of 2004. Any future declaration and payment of cash divi- dends will be subject to the discretion of the Board of Directors and will depend upon such factors as the Board of Directors deems relevant. The Board of Directors may modify the Company's dividend policy from time to time.

BOARD OF DIRECTORS

Robert J. Shillman
Chairman and Chief Executive Officer
Cognex Corporation

Patrick A. Alias
Executive Vice President
Cognex Corporation

Jerald G. Fishman
President and Chief Executive Officer
Analog Devices, Inc.

William A. Krivsky
Chairman and CEO
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Anthony Sun
Managing General Partner
Venrock Associates

Reuben Wasserman
Business Consultant

OFFICERS

Robert J. Shillman
Chairman and Chief Executive Officer

James F. Hoffmaster
President and Chief Operating Officer

Patrick A. Alias
Executive Vice President

Richard A. Morin
Senior Vice President of Finance and
Administration, Chief Financial Officer, and Treasurer

John McGarry
Senior Vice President,
In-Sight Products

William Silver
Senior Vice President and
Chief Technology Officer, MVSD

This annual report, including the letter to shareholders, contains "forward-looking statements" within the meaning of the Securities Act of 1933 and the Securities Exchange Act of 1934. Please see the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Forward-looking Statements" in this report for a discussion regarding risks associated with these statements.

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76 COGNEX CORPORATION: OFFICES

UNITED STATES
Corporate Headquarters
One Vision Drive
Natick, MA 01760
Telephone: (508) 650-3000
Fax: (508) 650-3333

2060 Challenger Drive
Alameda, CA 94501
Telephone: (510) 749-4000
Fax: (510) 865-9927

1001 Rengstorff Avenue
Mountain View, CA 94043
Telephone: (650) 969-4812
Fax: (650) 969-4818

800 East Diehl Road, Suite 125
Naperville, IL 60563
Telephone: (630) 649-6312
Fax: (630) 955-0661

46850 Magellan Drive, Suite 150
Novi, MI 48377
Telephone: (248) 668-5100
Fax: (248) 624-2964

15865 SW 74th Street, Suite 105
Portland, OR 97224
Telephone: (503) 620-6601
Fax: (503) 620-6093

318 Seaboard Lane
Suite 314
Franklin, TN 37067
Telephone: (615) 844-6158
Fax: (615) 844-6159

10150 West National Avenue, Suite 202
West Allis, WI 53227
Telephone: (414) 604-7000
Fax: (414) 604-2342

FINLAND
Cognex Finland, Oy
Kellonkierto 7
70460 Kuopio, Finland
Telephone: +358-17-3893 200
Fax: +358-17-3893 232

FRANCE
Cognex International Inc., France
104 Avenue Albert 1er
F-92563 Rueil Malmaison cedex, France
Telephone: +33-1-47-77-15-50
Fax: +33-1-47-77-15-55

GERMANY
Cognex Germany, Inc.
Emmy Noether Strasse 11
D-76131 Karlsruhe, Germany
Telephone: + 49-721-6639-0
Fax: + 49-721-6639-599

IRELAND
Cognex Ltd,
1, South Mall,
Cork, Ireland
Telephone: +353 (0)21 230 0271
Fax: +353 (0)21 230 0133

ITALY
Cognex International Inc., Italy
Via Gasparotto, 1
I-20124 Milano, Italy
Telephone: + 39-02-67471200
Fax: +39-02-67471300

NETHERLANDS
Cognex Benelux
Fellenoord, 130
NL-5611 ZB Eindhoven, Netherlands
Telephone: +31-402668565
Fax: +31-402668567

SWEDEN
Cognex International Inc.
Skrapan 1830
Kopparbergsvagen 10
S-722 10 Vasteras, Sweden
Telephone: +46-21-145588
Fax: +46-21-144080

UNITED KINGDOM
Cognex UK, Ltd.
Sunningdale House
43 Caldecotte Lake Drive
Caldecotte Lake Business Park
Milton Keynes MK7 8LF, UK
Telephone: +44-1908-206000
Fax: +44-1908-392463

Cognex UK, Ltd., Epsom Branch
Units 7-9, First Quarter
Blenheim Road, Epsom
Surrey, KT19 9QN, UK
Telephone: +44-1372-754 100
Fax: +44-1372-754 150

JAPAN
Cognex KK-Headquarters
23F Bunkyo Green Court
2-28-8 Honkomagome,
Bunkyo-ku
Tokyo 113-6591, Japan
Telephone: +81-3-5977-5400
Fax: +81-3-5977-5401

Cognex KK-Osaka
3F Central Shin-Osaka Building
4-5-36 Miyahara,
Yodogawa-ku
Osaka-shi, Osaka 532-0003 Japan
Telephone: +81-6-4807-8201
Fax: +81-6-4807-8202

Cognex KK-Fukuoka
5F, Dai 5 Hakata Kaisei Building
1-18-25 Hakataeki-Higashi,
Hakata-ku
Fukuoka-shi, Fukuoka-ken
812-0013, Japan
Telephone: +81-92-432-7741
Fax: +81-92-412-3590

Cognex KK-Nagoya
4F, IT Meieki Building
3-11-22 Meieki
Nakamura-ku, Nagoya-shi
Aichi-ken
450-0002 Japan
Telephone: + 81-52-569-5900
Fax: +81-52-581-7760

Cognex KK-Sendai
10F, Sendai-Hashimoto Building
27-21 Tachimachi
Aoba-ku, Sendai-shi, Miyagi-ken

980-0822, Japan
Telephone: +81-22-711-1971
Fax: +81-22-711-1982

SINGAPORE
10 Anson Road
#26-06A International Plaza
Singapore 079903
Telephone: +65-632-55-700
Fax: +65-632-55-703

TAIWAN
10F-1, No. 25
Puding Road
Hsin-Chu City
300 Taiwan, R.O.C.
Telephone: +886-3-5780060
Fax: +886-3-5781520

KOREA
8Fl., Dongkyung Bldg. 824-19
Yuksam-dong, Kangnam-Ku
Seoul, 135-080, Korea
Telephone: +82-2-539-9047
Fax: +82-2-569-9823

CHINA
Cognex China
CIIC Business Center
Unit B, 22/F Jian Hui Building,
922 Heng Shan Road
Shanghai 200030 PRC

Telephone: +86 21 6407-5835

EXHIBIT 14

COGNEX CORPORATION
CODE OF BUSINESS CONDUCT AND ETHICS

INTRODUCTION

PURPOSE AND SCOPE

The Board of Directors of Cognex Corporation (together with its subsidiaries, branches and affiliates, "Cognex") has adopted this Code of Business Conduct and Ethics to aid Cognex's directors, officers and employees in making ethical and legal decisions when conducting Cognex's business and performing their day-to-day duties.

Cognex's Board of Directors or a committee of the Board is responsible for administering the Code. The Board of Directors has delegated day-to-day responsibility for administering and interpreting the Code to a Compliance Officer. The highest ranking employee in the Cognex Human Resources Department (currently, the Vice President, Corporate Employee Services) has been appointed Cognex's Compliance Officer under this Code.

Cognex expects its directors, officers and employees to exercise reasonable judgment when conducting Cognex's business. Cognex encourages its directors, officers and employees to refer to this Code frequently to ensure that they are acting within both the letter and the spirit of this Code. Cognex also understands that this Code will not specifically address every situation you may encounter or every concern you may have about conducting Cognex's business ethically and legally. In these situations, or if you otherwise have questions or concerns about this Code, Cognex encourages each director, officer and employee to speak with his or her supervisor (if applicable) or, if you are uncomfortable doing that, with our Compliance Officer.

CONTENTS OF THIS CODE

This Code has two sections which follow this Introduction. The first section, "Standards of Conduct," contains the actual guidelines that our directors, officers and employees are expected to adhere to in the conduct of Cognex's business. The second section, "Compliance Procedures," contains specific information about how this Code functions, including who administers the Code, who can provide guidance under the Code and how violations may be reported, investigated and enforced. This section also contains a discussion about waivers of and amendments to this Code.

A NOTE ABOUT OTHER OBLIGATIONS

Cognex's directors, officers and employees generally have other legal and contractual obligations to Cognex, including without limitation Cognex's Invention, Non-Disclosure and Non-Competition Agreement and/or other employee agreements that may be applicable. This Code is not intended to reduce or limit the other obligations that you may have to Cognex. Instead, the standards in this Code should be viewed as the minimum standards that Cognex expects from its directors, officers and employees in the conduct of Cognex's business.

STANDARDS OF CONDUCT

CONFLICTS OF INTEREST

Cognex recognizes and respects the right of its directors, officers and employees to engage in outside activities which they may deem proper and desirable, provided that these activities do not impair or interfere with the performance of their duties to the Company or their ability to act in Cognex's best interests. In most, if not all cases, this will mean that our directors, officers and employees must avoid situations that present a potential or actual conflict between their personal interests and Cognex's interests.

A "conflict of interest" occurs when a director's, officer's or employee's personal interest interferes with Cognex's interests. Conflicts of interest may arise in many situations. Each individual's situation is different and, in evaluating his or her own situation, a director, officer or employee will have to consider many factors. By way of example, to avoid even the appearance of impropriety:

- No director, officer or employee may take an action or have an outside interest, responsibility or obligation that would have a high likelihood of affecting his/her ability to perform the responsibilities of his or her position objectively and/or effectively in Cognex's best interests.

- Employees may only accept personal favors, loans, meals, entertainment, transportation or services worth a nominal value from Cognex's customers, contractors, suppliers, vendors or anyone else doing business with Cognex. Such payments likely to improperly influence decisions to the non-Cognex party's benefit are considered improper, whether or not that purpose was intended. Similarly, under no circumstances are personal, intimate, romantic or sexual relationships between any Cognex employee and any Cognex customer, contractor, supplier, vendor or anyone else doing business with Cognex (whether actual or potential) allowed to influence a decision pertaining to that outside party. If there is any reason to believe a gift, entertainment, or other item of value offered to, or received from, a customer, purchasing agent, supplier, provider of services, or other person, creates the appearance of impropriety, the employee considering making/receiving the gift or providing the entertainment or other item, should discuss the proposal/item with his/her manager or the highest ranking employee in the Human Resources Department.

- Employees are not permitted to become employed by, or retained as a consultant by, or otherwise provide services to any customer, contractor, supplier, vendor or competitor of Cognex. Before accepting any consulting or freelance work, employees should discuss the work with Cognex's Human Resources Department to ensure that it does not conflict with Cognex's interests.

Any transaction or relationship that reasonably could be expected to give rise to a conflict of interest should be reported promptly to the Compliance Officer. The Compliance Officer may notify the Board of Directors or a committee thereof as he or she deems appropriate. Actual or potential conflicts of interest involving a director or executive officer should be disclosed directly to the Chairman of the Board of Directors.

COMPLIANCE WITH LAWS, RULES AND REGULATIONS

Cognex seeks to conduct its business in compliance with both the letter and the spirit of applicable laws, rules and regulations. No director, officer or employee shall engage in any unlawful activity in conducting Cognex's business or in performing his or her day-to-day company duties, nor shall any director, officer or employee instruct others to do so.

PROTECTION AND PROPER USE OF COGNEX'S ASSETS

Loss, theft and misuse of Cognex's assets has a direct impact on Cognex's business and its profitability. Employees, officers and directors are expected to protect Cognex's assets that are entrusted to them and to protect Cognex's assets in general. Employees, officers and directors are also expected to take steps to ensure that Cognex's assets are used only for legitimate business purposes.

CORPORATE OPPORTUNITIES

Employees, officers and directors owe a duty to Cognex to advance its legitimate business interests when the opportunity to do so arises. Each employee, officer and director is prohibited from:

- diverting to himself or herself or to others any opportunities that are discovered through the use of Cognex's property or information or as a result of his or her position with Cognex,

- using Cognex's property or information or his or her position for improper personal gain, or

- competing with the Company.

CONFIDENTIALITY

Confidential Information (see below) generated and gathered in Cognex's business plays a vital role in Cognex's business, prospects and ability to compete. Directors, officers and employees shall use Confidential Information solely for legitimate company purposes. Directors, officers and employees may not disclose or distribute Cognex's Confidential Information, except when disclosure is authorized by Cognex or required by applicable law, rule or regulation or pursuant to an applicable legal proceeding. If any Cognex director, officer or employee believes he or she has a need, duty or obligation to divulge a Cognex trade secret or other confidential or proprietary information to a third party, that employee must first contact the Legal Department to discuss the matter, which may result in the need to execute a non-disclosure agreement with said third party. Directors, officers and employees must return all of Cognex's Confidential Information in their possession to Cognex when they cease to be employed by or to otherwise serve Cognex.

"Confidential Information" includes all non-public information that might be of use to competitors or harmful to the Company or its customers if disclosed. Examples of Cognex trade secrets include, but are not limited to:
software algorithms, software source code, designs of Cognex boards and chips, vision technology, "how" Cognex vision software tools work, new product developments, customer identification and lists, customer contract prices, sales data, business strategies, marketing plans and studies, cost reports and bookkeeping methods.

Further, Cognex considers the components of each employee's compensation package as Confidential Information. Any employee found to be discussing, with anyone other than his/her manager or Human Resources Representative, his or her salary, stock option agreements, performance bonuses, commission plans, and/or profit-sharing contributions - or that of any other employee other than for an official company purpose - may be subject to disciplinary action, up to and including termination of employment.

Employees should also refer to their Employee Invention, Non-Disclosure and Non-Competition Agreement regarding the protection of Cognex's Confidential Information.

FAIR DEALING

Competing vigorously, yet lawfully, with competitors and establishing advantageous, but fair, business relationships with customers and suppliers is a part of the foundation for long-term success. However, unlawful and unethical conduct, which may lead to short-term gains, may damage a company's reputation and long-term business prospects. Accordingly, it is Cognex's policy that directors, officers and employees must endeavor to deal ethically and lawfully with Cognex's customers, suppliers, competitors and employees in all business dealings on Cognex's behalf. No director, officer or employee should take unfair advantage of another person in business dealings on Cognex's behalf through the abuse of privileged or confidential information or through improper manipulation, concealment or misrepresentation of material facts.

ACCURACY OF RECORDS

The integrity, reliability and accuracy in all material respects of Cognex's books, records and financial statements is fundamental to Cognex's continued and future business success. No director, officer or employee may cause Cognex to enter into a transaction with the intent to document or record it in a deceptive or unlawful manner. In addition, no director, officer or employee may create any false or artificial documentation or book entry for any transaction entered into by Cognex. Similarly, officers and employees who have responsibility for accounting and financial reporting matters have a responsibility to accurately record all funds, assets and transactions on Cognex's books and records.

QUALITY OF PUBLIC DISCLOSURES

Cognex is committed to providing its shareholders with complete and accurate information about its financial condition and results of operations in accordance with the securities laws of the United States. It is Cognex's policy that the reports and documents it files with or submits to the Securities and Exchange Commission, and its earnings releases and similar public communications made by Cognex, include fair, timely and understandable disclosures. Officers and employees who are responsible for these filings and disclosures, including Cognex's principal executive, financial and accounting officers, must use reasonable judgment and perform their responsibilities honestly, ethically and objectively in order to ensure that this disclosure policy is fulfilled.

COMPLIANCE PROCEDURES

COMMUNICATION OF CODE

All directors and employees will be supplied with a copy of the Code upon beginning service at Cognex. Updates of the Code will be provided from time to time. A copy of the Code is also available to all directors and employees by requesting one from the Human Resources Department, and may be accessed by all employees and the general public by accessing the company's website at www.cognex.com.

MONITORING COMPLIANCE AND DISCIPLINARY ACTION

Cognex's management, under the supervision of its Board of Directors or a committee thereof or, in the case of accounting, internal accounting controls or auditing matters, the Audit Committee, shall take reasonable steps from time to time to (i) monitor compliance with the Code, and (ii) when appropriate, impose and enforce appropriate disciplinary measures for violations of the Code.

Disciplinary measures for violations of the Code may include, but are not limited to, counseling, oral or written reprimands, warnings, probation or suspension with or without pay, demotions, reductions in salary, termination of employment or service and restitution.

Cognex's management shall periodically report to the Board of Directors or a committee thereof on these compliance efforts including, without limitation, periodic reporting of alleged violations of the Code and the actions taken with respect to any such violation.

REPORTING CONCERNS/RECEIVING ADVICE

COMMUNICATION CHANNELS

Be Proactive. Every employee is required to act proactively by asking questions, seeking guidance and reporting suspected violations of the Code and other policies and procedures of Cognex, as well as any violation or suspected violation of applicable law, rule or regulation arising in the conduct of Cognex's business or occurring on Cognex's property. IF ANY EMPLOYEE BELIEVES THAT ACTIONS HAVE TAKEN PLACE, MAY BE TAKING PLACE, OR MAY BE ABOUT TO TAKE PLACE THAT VIOLATE OR WOULD VIOLATE THE CODE, HE OR SHE IS OBLIGATED TO BRING THE MATTER TO COGNEX'S ATTENTION.

Seeking Guidance. The best starting point for an employee seeking advice on ethics-related issues or reporting potential violations of the Code will usually be his or her manager. However, if the conduct in question involves his or her manager, if the employee has reported the conduct in question to his or her manager and does not believe that he or she has dealt with it properly, or if the employee does not feel that he or she can discuss the matter with his or her manager, the employee may raise the matter with the Compliance Officer.

Communication Alternatives. Any employee may communicate with the Compliance Officer by any of the following methods:

a) In writing (which may be done anonymously as set forth below under "Reporting; Anonymity; Retaliation"), addressed to the Compliance Officer, by U.S. mail to P.O. Box 2232, Natick, MA 01760;

b) By e-mail to feedback@cognex.com; or

c) Through Cognex's intranet site; or

d) By leaving a voice mail message at (508) 652-3777. This voice mailbox will only be accessible by the Compliance Officer and the Chair of the Audit Committee.

Please note that anonymity may not be completely maintained through options b, c and d.

Reporting Accounting and Similar Concerns. Any concerns or questions regarding potential violations of the Code, any other company policy or procedure or applicable law, rules or regulations involving accounting, internal accounting controls or auditing matters should be directed to the Audit Committee or the Compliance Officer. Such communication may be made by any of the methods listed above, or by writing directly to the Chair of the Audit Committee.

Misuse of Reporting Channels. Employees should only use these reporting channels for complaints that he/she reasonably believes, in good faith, may be valid. Any use by an employee of these reporting channels in bad faith or in a false or frivolous manner, will be considered a material breach of his/her employment and such employee would be subject to disciplinary action, including termination.

REPORTING; ANONYMITY; RETALIATION

When reporting suspected violations of the Code, Cognex prefers that employees identify themselves in order to facilitate Cognex's ability to take appropriate steps to address the report, including conducting any appropriate investigation. However, Cognex also recognizes that some people may feel more comfortable reporting a suspected violation anonymously.

If an employee wishes to remain anonymous, he or she may do so, and Cognex will use reasonable efforts to protect the confidentiality of the reporting person subject to applicable law, rule or regulation or to any applicable legal proceedings. In the event the report is made anonymously, however, Cognex may not have sufficient information to look into or otherwise investigate or evaluate the allegations. Accordingly, persons who make reports anonymously should provide as much detail as is reasonably necessary to permit Cognex to evaluate the matter(s) set forth in the anonymous report and, if appropriate, commence and conduct an appropriate investigation.

NO RETALIATION

Cognex expressly forbids any retaliation against any employee who, acting in good faith, reports suspected misconduct. Any person who participates in any such retaliation is subject to disciplinary action, including termination.

WAIVERS AND AMENDMENTS

No waiver of any provisions of the Code for the benefit of a director or an executive officer (which includes without limitation, for purposes of this Code, Cognex's principal executive, financial and accounting officers) shall be effective unless (i) approved by the Board of Directors or, if permitted, a committee thereof, and (ii) if applicable, such waiver is promptly disclosed to Cognex's shareholders in accordance with applicable United States securities laws and/or the rules and regulations of the exchange or system on which the Company's shares are traded or quoted, as the case may be.

Any waivers of the Code for other employees may be made by the Compliance Officer, the Board of Directors or, if permitted, a committee thereof.

All amendments to the Code must be approved by the Board of Directors or a committee thereof and, if applicable, must be promptly disclosed to Cognex's shareholders in accordance with applicable United States securities laws and/or the rules and regulations of the exchange or system on which the Company's shares are traded or quoted, as the case may be.

EXHIBIT 21

COGNEX CORPORATION
SUBSIDIARIES OF THE REGISTRANT

At December 31, 2004, the registrant had the following subsidiaries, the financial statements of which are all included in the consolidated financial statements of the registrant:

NAME OF SUBSIDIARY	STATE/COUNTRY OF INCORPORATION	PERCENT OWNERSHIP
Cognex Technology and Investment Corporation	California	100%
Cognex Canada Technology, Inc.	California	100%
Cognex Foreign Sales Corporation	Barbados	100%
Vision Drive, Inc.	Delaware	100%
Cognex Canada, Inc.	Delaware	100%
Cognex K.K.	Japan	100%
Cognex International, Inc.	Delaware	100%
Cognex Europe, Inc.	Delaware	100%
Cognex Europe, b.v.	Netherlands	100%
Cognex Germany, Inc.	Massachusetts	100%
Cognex, Ltd.	Ireland	100%
Cognex UK Ltd.	United Kingdom	100%
Cognex Finland Oy	Finland	100%
Cognex Singapore, Inc.	Delaware	100%
Cognex Korea, Inc.	Delaware	100%
Cognex Taiwan, Inc.	Delaware	100%
Cognex Asia, Inc. (formerly Cognex China, Inc.)	Delaware	100%

EXHIBIT 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in this Annual Report (Form 10-K) of Cognex Corporation of our report dated March 4, 2005, included in the 2004 Annual Report to Shareholders of Cognex Corporation.

We consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 33-81150, 333-04621, 333-02151, 333-60807, 33-32815, 333-44824, 333-68158, 333-96961, and 333-100709) of Cognex Corporation of our report dated March 4, 2005, with respect to the consolidated financial statements of Cognex Corporation incorporated by reference in this Annual Report (Form 10-K) for the years ended December 31, 2004 and 2003, our report dated March 4, 2005 with respect to Cognex Corporation management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of internal control over financial reporting included in this Annual Report (Form 10-K), and our report dated March 4, 2005 with respect to the financial statement schedule of Cognex Corporation and subsidiaries for the years ended December 31, 2004 and 2003 included in this Annual Report (Form 10-K).

/s/ Ernst & Young LLP

Boston, Massachusetts
March 4, 2005

EXHIBIT 23.2

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 33-81150, 333-04621, 333-02151, 333-60807, 33-32815, 333-44824, 333-68158, 333-96961, and 333-100709) of Cognex Corporation of our report dated January 24, 2003 relating to the financial statements, which appears in the Annual Report to Shareholders, which is incorporated in this Annual Report on Form 10-K. We also consent to the incorporation by reference of our report dated January 24, 2003 relating to the financial statement schedule, which appears in this Form 10-K.

/s/ PricewaterhouseCoopers LLP

Boston, Massachusetts
March 4, 2005

CERTIFICATION

EXHIBIT 31.1

I, Robert J. Shillman, Chief Executive Officer and Chairman of the Board of Directors of Cognex Corporation, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cognex Corporation;

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(s) 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(s) 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: March 11, 2005

/s/ Robert J. Shillman

Robert J. Shillman
Chief Executive Officer and
Chairman of the Board of Directors

CERTIFICATION

EXHIBIT 31.2

I, Richard A. Morin, Senior Vice President of Finance, Chief Financial Officer, and Treasurer of Cognex Corporation, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cognex Corporation;

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(s) 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(s) 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: March 11, 2005

/s/ Richard A. Morin

Richard A. Morin
Senior Vice President of Finance,
Chief Financial Officer, and Treasurer

EXHIBIT 32.1*

CERTIFICATION PURSUANT TO
18 U.S.C. 1350,
AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

The undersigned officer of Cognex Corporation (the "Company") hereby certifies that the Company's Annual Report on Form 10-K for the year ended December 31, 2004 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, as amended, and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 11, 2005

/s/ Robert J. Shillman

Robert J. Shillman
Chief Executive Officer and
Chairman of the Board of Directors
(principal executive officer)

* This certification shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, nor shall it be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.

EXHIBIT 32.2*

CERTIFICATION PURSUANT TO
18 U.S.C. 1350,
AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

The undersigned officer of Cognex Corporation (the "Company") hereby certifies that the Company's Annual Report on Form 10-K for the year ended December 31, 2004 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, as amended, and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 11, 2005

/s/ Richard A. Morin

Richard A. Morin
Senior Vice President of Finance,
Chief Financial Officer, and Treasurer
(principal financial officer)

* This certification shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, nor shall it be deemed to be incorporated by reference into any

filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.