

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

FORM 10-Q

(Mark One)

/X/ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended: September 30, 1995

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 0-9992

KLA INSTRUMENTS CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE  
(STATE OR OTHER JURISDICTION OF  
INCORPORATION OR ORGANIZATION)

04-2564110  
(I.R.S. EMPLOYER  
IDENTIFICATION NO.)

160 Rio Robles  
San Jose, California  
(Address of principal executive offices)

95134  
(Zip Code)

Registrant's telephone number, including area code: (408) 468-4200

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 Act of 1934 during  
the preceding 12 months (or for such shorter period that the registrant was  
required to file such reports), and (2) has been subject to such filing  
requirements for the past 90 days.

Yes X No  
--- ---

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:  
Common Stock, \$0.001 par value  
Common Stock Purchase Rights

Common shares outstanding at September 30, 1995: 50,421,000

This report, including all exhibits and attachments, contains 13 pages.

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KLA INSTRUMENTS CORPORATION

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<CAPTION>

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KLA INSTRUMENTS CORPORATION

PART I FINANCIAL INFORMATION

Item 1 Financial Statements

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
THREE MONTHS ENDED SEPTEMBER 30,  
(In thousands except per share amounts)  
(Unaudited)

<TABLE>  
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	1994 ----	1995 ----
<S>	<C>	<C>
Net sales	\$ 83,179 -----	\$ 149,076 -----
Costs and expenses:		
Cost of sales	40,602	66,672
Engineering, research and development	8,182	15,621
Selling, general and administrative	16,450	27,855
	-----	-----
	65,234	110,148
	-----	-----
Income from operations	17,945	38,928
Interest income and other, net	1,497	4,187
Interest expense	(474)	(418)
	-----	-----
Income before income taxes	18,968	42,697
Provision for income taxes	6,070	15,371
	-----	-----
Net income	\$ 12,898 =====	\$ 27,326 =====
Net income per share	\$ 0.27 =====	\$ 0.52 =====
Shares used in computing net income per share	47,760	52,408

</TABLE>

See accompanying notes to unaudited condensed consolidated financial statements.

KLA INSTRUMENTS CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS  
(In thousands)  
(Unaudited)

<TABLE>  
<CAPTION>

June 30, 1995 -----	September 30, 1995 -----
---------------------------	--------------------------------

<u>&lt;S&gt;</u>	<u>&lt;C&gt;</u>	<u>&lt;C&gt;</u>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 92,059	\$ 65,820
Short-term investments	26,681	38,529
Accounts receivable, net of allowances of \$2,196 and \$2,645	129,274	148,355
Inventories	79,759	92,584
Deferred income taxes	18,155	18,155
Other current assets	14,949	8,262
	-----	-----
Total current assets	360,877	371,705
Land, property and equipment, net	49,004	53,716
Marketable securities	126,013	137,227
Other assets	10,402	7,828
	-----	-----
Total assets	\$ 546,296	\$ 570,476
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Notes payable	\$ 4,458	\$ 2,440
Current portion of long-term debt	20,000	--
Accounts payable	19,376	20,742
Income taxes payable	22,797	29,742
Other current liabilities	66,220	76,859
	-----	-----
Total current liabilities	132,851	129,783
	-----	-----
Deferred income taxes	9,476	9,476
	-----	-----
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value, 1,000 shares authorized, none issued and outstanding	--	--
Common stock, \$0.0005 par value, 150,000 shares authorized, 50,160 and 50,421 shares issued and outstanding	25	25
Capital in excess of par value	263,016	263,804
Retained earnings	138,893	166,219
Treasury stock	(581)	(581)
Net unrealized gain on investments	1,241	1,074
Cumulative translation adjustment	1,375	676
	-----	-----
Total stockholders' equity	403,969	431,217
	-----	-----
Total liabilities and stockholders' equity	\$ 546,296	\$ 570,476
	=====	=====

</TABLE>

See accompanying notes to condensed consolidated financial statements.

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KLA INSTRUMENTS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
THREE MONTHS ENDED SEPTEMBER 30,  
(In thousands)  
(Unaudited)

<TABLE>  
<CAPTION>

	1994	1995
<u>&lt;S&gt;</u>	<u>&lt;C&gt;</u>	<u>&lt;C&gt;</u>
Cash flows from operating activities:		
Net income	\$ 12,898	\$ 27,326
Adjustments required to reconcile net income to cash provided by operations:		
Depreciation and amortization	2,105	3,385
Changes in assets and liabilities:		
Accounts receivable	(9,780)	(19,081)
Inventories	(6,690)	(12,825)
Other assets	(1,147)	9,261
Accounts payable	1,897	1,366
Income taxes payable	2,867	6,945
Other current liabilities	6,188	10,639

Cash provided by operating activities	8,338	27,016
Cash flows from investing activities:		
Capital expenditures	(2,590)	(8,097)
Purchases of short and long-term available for sale securities	--	(137,685)
Sales and maturities of short and long-term available for sale securities	--	114,456
Cash used for investing activities	(2,590)	(31,326)
Cash flows from financing activities:		
Short-term borrowings, net	(2,480)	(2,018)
Payment of current portion of long-term debt	--	(20,000)
Sales of common stock/tax benefit of options exercised	1,543	788
Cash used for financing activities	(937)	(21,230)
Effect of exchange rate changes	136	(699)
Increase (decrease) in cash and cash equivalents	4,947	(26,239)
Cash and cash equivalents at beginning of period	139,126	92,059
Cash and cash equivalents at end of period	\$ 144,073	\$ 65,820

Supplemental disclosure of cash flow information

CASH PAID DURING THE PERIOD FOR:

INTEREST	\$ 470	\$ 405
INCOME TAXES	2,955	8,552

See accompanying notes to condensed consolidated financial statements.

KLA INSTRUMENTS CORPORATION  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1) This information is unaudited but, in the opinion of Registrant's management, all adjustments (consisting only of adjustments that are of a normal recurring nature) necessary for a fair statement of results have been included. The results for the quarter ended September 30, 1995, are not necessarily indicative of results to be expected for the entire year. This financial information should be read in conjunction with the Registrant's Annual Report on Form 10-K (including items incorporated by reference therein) for the year ended June 30, 1995.

2) Details of certain balance sheet components:

<TABLE>  
<CAPTION>

	June 30, 1995	September 30, 1995
	-----	-----
		(In thousands)
<S>	<C>	<C>
Inventories:		
Systems raw materials	\$ 18,944	\$ 25,875
Customer service spares	13,050	12,524
Work-In-Process	26,863	33,491
Demonstration Equipment	20,902	20,694
	-----	-----
	\$ 79,759	\$ 92,584
	=====	=====

</TABLE>

3) In August of 1995, the Company repaid the \$20.0 million mortgage on its principal facility.

4) Net Income per share is computed using the weighted average number of common and common equivalent shares outstanding during the respective periods, including the assumed net shares issuable upon exercise of

stock options, when dilutive.

A two-for-one stock split was declared by the Board of Directors on July 24, 1995. The stock split was in the form of a 100% stock dividend. The dividend was paid on September 29, 1995, to stockholders of record on August 31, 1995. Earnings per share was calculated on a post-split basis.

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KLA INSTRUMENTS CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF  
OPERATIONS AND FINANCIAL CONDITION

Results of Operations

First Quarter of Fiscal 1996 Compared with First Quarter of Fiscal 1995

Net Sales

Net sales increased \$65.9 million or 79.2% for the three month period ended September 30, 1995 as compared to the prior fiscal year. The WISARD business unit was predominately responsible for the increase in sales. The Company attributes the continuing increase in WISARD's sales primarily to the accelerating acceptance of the Company's in-line wafer monitoring equipment that allows semiconductor manufacturers to optimize device yields and also to the continued strength of capital spending by the industry. Significant increases in sales were also achieved by the Metrology and Automated Test business units. Net sales of the Optical Metrology business increased almost 100% compared to the prior fiscal year's first quarter.

Gross Margin

Gross margins were 55.3% for the three month period ended September 30, 1995 compared to 51.2% for the prior fiscal year. Most of the improvement in the gross margin percentage was due to a favorable product mix as the WISARD business unit's share of total revenues rose substantially. The WISARD business unit's gross margin also benefited from continued learning curve effects, volume efficiencies as well as from the yen's strengthening in late fiscal 1995.

Engineering, Research and Development

Engineering, research and development expenses were 10.5% of net sales for the three month period ended September 30, 1995 compared to 9.8% in the first quarter of the prior fiscal year. Net engineering expenditures rose \$7.4 million during the first quarter of fiscal 1996 compared to the first quarter of fiscal 1995. The Company is concentrating on the broad opportunities in yield management, including the networking of all measurement tools in a fab, the development of new measurement tools and the related software for using those tools. The WISARD business unit accounted for approximately one-third of the increase in dollar spending. The next largest dollar increases were recorded in the Optical Metrology business unit and the E-Beam Metrology business unit. Smaller increases in dollar spending were also recorded in the RAPID, PRISM and SEMSpec divisions.

Selling, General and Administrative

Selling, general and administrative expenses were 18.7% of net sales for the three month period ended September 30, 1995 compared to 19.8% in the first quarter of the prior fiscal year. Sales and administration expenses increased at a rate somewhat slower than sales while representative commissions increased slightly faster than sales due to an increase in shipments to Japan.

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Interest Income and Other, net

Interest income and other, net increased \$2.7 million for the three month period ended September 30, 1995 compared to the prior fiscal year. This increase is due both to higher average cash balances, as a result primarily of the Company's \$91 million secondary stock offering in May 1995, and also to higher yields on the Company's investment portfolio, the management of which the Company outsourced starting in December 1994.

Provision for Income Taxes

The Company's effective tax rate increased to 36% for the three months ended September 30, 1995. The Company's tax rate was 34% for the year ended June 30, 1995. The increase from 34% to 36% is due primarily to the lower impact of the realization of previously reserved deferred tax assets and the expiration of the federal research and development tax credit on June 30, 1995.

The IRS is currently auditing the Company's federal income tax returns for fiscal years 1985 to 1992. The Company has not yet received a notice of proposed tax deficiency. However, it anticipates a notice will be received in fiscal 1996. Management believes sufficient taxes have been provided in prior years and that the ultimate outcome of the IRS audit will not have a material adverse impact on the Company's financial position or results of operations.

Future Operating Results

The Company's future results will depend on its ability to continuously introduce new products and enhancements to its customers as demands for higher performance yield management and process control systems change or increase. Due to the risks inherent in transitioning to new products, the Company must accurately forecast demand in both volume and configuration and also manage the transition from older products. The Company's results could be affected by the ability of competitors to introduce new products which have technological and/or pricing advantages. The Company's results also will be affected by strategic decisions made by management regarding whether to continue particular product lines, and by volume, mix and timing of orders received during a period, fluctuations in foreign exchange rates, and changing conditions in both the semiconductor industry and key semiconductor markets around the world. As a result, the Company's operating results may fluctuate, especially when measured on a quarterly basis.

Liquidity and Capital Resources

Cash, cash equivalents and marketable securities balances remained relatively flat at \$241.6 million for the three months ended September 30, 1995. Cash generated by operations was \$27.0 million. This was offset by the repayment in full of the \$20.0 million mortgage on the Company's principal facility, and by \$8.0 million of capital expenditures. The Company's capital expenditures were primarily in facility improvements, new computers to accommodate the planned introduction of new enterprise business systems, and engineering computers and equipment to support the Company's rapidly expanding research and development efforts. The Company believes that its current level of liquid assets, credit facilities and expected cash generated from operations are sufficient to fund growth through the next fiscal year.

KLA INSTRUMENTS CORPORATION

FORM 10-Q

PART II: OTHER INFORMATION

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	Item 1	- Legal Proceedings	Not Applicable
	Item 2	- Changes in Securities	Not Applicable
	Item 3	- Defaults Upon Senior Securities	Not Applicable
	Item 4	- Submission of Matters to a Vote of Security Holders	Not Applicable
	Item 5	- Other Events	Not Applicable
	Item 6	- Exhibits and Reports on Form 8-K	Page 11 - 12

SIGNATURES

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

KLA INSTRUMENTS CORPORATION

October 25, 1995  
[Date]

ROBERT J. BOEHLKE  
-----  
Robert J. Boehlke  
V.P. Finance and Administration  
Chief Financial Officer

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INDEX TO EXHIBITS

(i) EXHIBITS INCORPORATED BY REFERENCE:

- 3.1 Certificate of Incorporation as amended(7)
- 3.2 Bylaws, as amended(7)
- 4.1 Amended and Restated Rights Agreement dated as of August 30, 1995, between the Company and First National Bank of Boston, as Rights Agent. The Rights Agreement includes as Exhibit A, the form of Right Certificate.(1)
- 10.15 Statement of Partnership to Triangle Partners dated April 12, 1983(2)
- 10.16 Lease Agreement and Addendum thereto dated January 10, 1983, between BB&K Partnership and the Company(2)
- 10.18 Purchase and Sale Agreement dated January 10, 1983, between BB&K Partnership, Triangle Partners and the Company(2)
- 10.35 Research and Development Agreement, Cross License and Technology Transfer Agreement and Agreement for Option to License and Purchase Resulting Technology, all dated October 1, 1986, by and between KLA Development No. 4, Ltd., and the Company(3)
- 10.45 Distribution Agreement dated July 1990, by and between Tokyo Electron Limited, a Japanese Corporation, and the Company(4)
- 10.46 Principal facility Purchase Agreement dated July 1990, including all exhibits and amendments; Lease Agreement, Termination of Lease, Lot line adjustment, rights of first refusal, Deeds of Trust(4)
- 10.47 Joint Venture Agreement between the Company and Nippon Mining Company, Limited, dated September 18, 1990(5)
- 10.49 Exercise of Option to Purchase Technology made effective as of January 1, 1990, by and between KLA Development No. 4, and the Company(5)
- 10.54 Micrion Corporation Series E Preferred Stock Purchase Agreement, dated September 13, 1991(6)
- 10.67 Amendment of Credit Agreement between Bank of America NT & SA and the Company, dated March 31, 1994(9)
- 10.68 Credit Agreement between Bank of America NT & SA and the Company, dated April 30, 1994(9)
- 10.71 1990 Outside Directors Stock Option Plan(8)
- 10.73 Amendment of Credit Agreement between Bank of America NT & SA and the Company dated December 31, 1994(10)
- 10.74 1981 Employee Stock Purchase Plan, as amended by the Board of Directors on October 7, 1994(10)
- 10.75 1982 Stock Option Plan, as amended by the Board of Directors on October 7, 1994(10)
- 10.76 Amendment of Credit Agreement between Bank of America NT & SA and the Company dated February 15, 1995(10)
- 10.77 Lease Agreement, Ground Lease Agreement and Purchase Agreement dated June 5, 1995, between BNP Leasing Corporation and the Company(10)
- 10.78 Lease Agreement and Purchase Agreement dated August 10, 1995, between BNP Leasing Corporation and the Company(10)

(ii) EXHIBITS INCLUDED HEREWITH:

- 27 Financial Data Schedule

- 
- (1) Filed as exhibit number 1 to Form 8-A/A, filed effective September 25, 1995
  - (2) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1983
  - (3) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1987
  - (4) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1990
  - (5) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1991
  - (6) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1992

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- (7) Filed as the same exhibit number to Registrant's registration statement no.33-51819 on Form S-3, dated February 2, 1994
- (8) Filed as exhibit number 4.6 as set forth herein to Registrant's Form 10-K for the year ended June 30, 1991
- (9) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1994
- (10) Filed as the same exhibit number as set forth herein to Registrant's Form 10-K for the year ended June 30, 1995

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONSOLIDATED STATEMENT OF OPERATIONS, THE CONSOLIDATED BALANCE SHEET AND THE ACCOMPANYING NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, AND IS QUALIFIED IN IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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