

ZEBRA TECHNOLOGIES CORP

Form 10-Q

November 05, 2010

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D. C. 20549

**FORM 10-Q**

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

For the quarterly period ended October 2, 2010

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: 000-19406

**Zebra Technologies Corporation**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**36-2675536**  
(I.R.S. Employer  
Identification No.)

**475 Half Day Road, Suite 500, Lincolnshire, IL 60069**

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(847) 634-6700**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or

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for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if smaller reporting company) Smaller reporting company

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

As of October 29, 2010, there were 56,528,911 shares of Class A Common Stock, \$.01 par value, outstanding.

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**ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES**

**QUARTER ENDED OCTOBER 2, 2010**

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**Table of Contents****PART I - FINANCIAL INFORMATION****Item 1. Consolidated Financial Statements****ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

(Amounts in thousands)

|  | October 2,<br>2010<br>(Unaudited) | December 31,<br>2009 |
|--|-----------------------------------|----------------------|
| <b>ASSETS</b>  |                                   |                      |
| Current assets:  |                                   |                      |
| Cash and cash equivalents  | \$ 47,447                         | \$ 38,943            |
| Restricted cash  | 1,615                             | 1,725                |
| Investments and marketable securities  | 123,058                           | 114,064              |
| Accounts receivable, net   | 165,423                           | 150,992              |
| Inventories, net   | 95,842                            | 79,926               |
| Deferred income taxes  | 11,282                            | 10,792               |
| Income taxes receivable  |                                   | 4,724                |
| Prepaid expenses and other current assets                                      | 11,043                            | 9,771                |
| <b>Total current assets</b>  | <b>455,710</b>                    | <b>410,937</b>       |
| Property and equipment at cost, less accumulated depreciation and amortization | 84,809                            | 77,589               |
| Long-term deferred income taxes  | 32,234                            | 35,842               |
| Goodwill   | 152,418                           | 153,225              |
| Other intangibles, net   | 51,592                            | 55,982               |
| Long-term investments and marketable securities                                | 90,076                            | 91,989               |
| Other assets   | 4,806                             | 4,915                |
| <b>Total assets</b>  | <b>\$ 871,645</b>                 | <b>\$ 830,479</b>    |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>                                     |                                   |                      |
| Current liabilities:   |                                   |                      |
| Accounts payable   | \$ 33,908                         | \$ 28,137            |
| Accrued liabilities  | 66,486                            | 52,591               |
| Deferred revenue   | 22,292                            | 24,082               |
| Income taxes payable   | 5,752                             |                      |
| <b>Total current liabilities</b>   | <b>128,438</b>                    | <b>104,810</b>       |
| Deferred rent  | 2,853                             | 4,108                |
| Other long-term liabilities  | 9,647                             | 9,432                |
| <b>Total liabilities</b>   | <b>140,938</b>                    | <b>118,350</b>       |
| Stockholders equity:   |                                   |                      |

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|  |                   |                   |
|--|-------------------|-------------------|
| Preferred Stock                                  |                   |                   |
| Class A Common Stock                             | 722               | 722               |
| Additional paid-in capital                       | 128,068           | 136,104           |
| Treasury stock                                   | (430,515)         | (385,831)         |
| Retained earnings                                | 1,042,756         | 969,195           |
| Accumulated other comprehensive loss             | (10,324)          | (8,061)           |
| <b>Total stockholders equity</b>                 | <b>730,707</b>    | <b>712,129</b>    |
| <b>Total liabilities and stockholders equity</b> | <b>\$ 871,645</b> | <b>\$ 830,479</b> |

See accompanying notes to consolidated financial statements.

**Table of Contents****ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF EARNINGS**

(Amounts in thousands, except per share data)

(Unaudited)

|   | <b>Three Months Ended</b>  |                            | <b>Nine Months Ended</b>   |                            |
|---|----------------------------|----------------------------|----------------------------|----------------------------|
|   | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> |
| <b>Net sales:</b>                         |                            |                            |                            |                            |
| Net sales of tangible products            | \$ 221,795                 | \$ 175,334                 | \$ 632,198                 | \$ 503,947                 |
| Revenue from services and software        | 24,712                     | 25,444                     | 76,475                     | 77,116                     |
| <b>Total net sales</b>                    | <b>246,507</b>             | <b>200,778</b>             | <b>708,673</b>             | <b>581,063</b>             |
| <b>Cost of sales:</b>                     |                            |                            |                            |                            |
| Cost of sales of tangible products        | 117,502                    | 98,682                     | 341,815                    | 291,117                    |
| Cost of services and software             | 10,291                     | 10,398                     | 29,630                     | 30,703                     |
| <b>Total cost of sales</b>                | <b>127,793</b>             | <b>109,080</b>             | <b>371,445</b>             | <b>321,820</b>             |
| <b>Gross profit</b>                       | <b>118,714</b>             | <b>91,698</b>              | <b>337,228</b>             | <b>259,243</b>             |
| <b>Operating expenses:</b>                |                            |                            |                            |                            |
| Selling and marketing                     | 30,365                     | 26,395                     | 88,193                     | 73,992                     |
| Research and development                  | 26,746                     | 21,454                     | 75,189                     | 64,552                     |
| General and administrative                | 20,302                     | 22,447                     | 60,889                     | 61,881                     |
| Amortization of intangible assets         | 2,444                      | 2,649                      | 7,147                      | 7,857                      |
| Exit, restructuring and integration costs |                            | 3,515                      | 2,392                      | 9,455                      |
| Asset impairment charges                  |                            |                            |                            | (1,058)                    |
| <b>Total operating expenses</b>           | <b>79,857</b>              | <b>76,460</b>              | <b>233,810</b>             | <b>216,679</b>             |
| <b>Operating income</b>                   | <b>38,857</b>              | <b>15,238</b>              | <b>103,418</b>             | <b>42,564</b>              |
| <b>Other income (expense):</b>            |                            |                            |                            |                            |
| Investment income                         | 635                        | 813                        | 2,111                      | 2,238                      |
| Foreign exchange gain (loss)              | (325)                      | 575                        | 235                        | (840)                      |
| Other, net                                | (216)                      | (286)                      | (1,052)                    | (622)                      |
| <b>Total other income (expense)</b>       | <b>94</b>                  | <b>1,102</b>               | <b>1,294</b>               | <b>776</b>                 |
| <b>Income before income taxes</b>         | <b>38,951</b>              | <b>16,340</b>              | <b>104,712</b>             | <b>43,340</b>              |
| <b>Income taxes</b>                       | <b>12,800</b>              | <b>5,229</b>               | <b>31,151</b>              | <b>13,866</b>              |

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|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
| Net income   | \$ 26,151 | \$ 11,111 | \$ 73,561 | \$ 29,474 |
| Basic earnings per share                                     | \$ 0.46   | \$ 0.19   | \$ 1.28   | \$ 0.49   |
| Diluted earnings per share                                   | \$ 0.46   | \$ 0.19   | \$ 1.28   | \$ 0.49   |
| Basic weighted average shares outstanding                    | 56,739    | 58,954    | 57,405    | 59,548    |
| Diluted weighted average and equivalent shares outstanding   | 56,998    | 59,083    | 57,657    | 59,643    |
| See accompanying notes to consolidated financial statements. |           |           |           |           |

**Table of Contents****ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Amounts in thousands)

(Unaudited)

|  | <b>Nine Months Ended</b>   |                            |
|--|----------------------------|----------------------------|
|  | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> |
| <b>Cash flows from operating activities:</b>   |                            |                            |
| Net income   | \$ 73,561                  | \$ 29,474                  |
| <b>Adjustments to reconcile net income to net cash provided by (used in) operating activities:</b> |                            |                            |
| Depreciation and amortization  | 23,698                     | 24,409                     |
| Equity-based compensation  | 8,155                      | 8,687                      |
| Excess tax benefit from equity-based compensation  | (83)                       | (11)                       |
| Loss (Gain) on sale of assets  | (58)                       | 357                        |
| Asset impairment charges   |                            | (1,058)                    |
| Deferred income taxes  | 3,208                      | 4,259                      |
| <b>Changes in assets and liabilities:</b>  |                            |                            |
| Accounts receivable, net   | (14,463)                   | 13,797                     |
| Inventories, net   | (15,972)                   | 22,632                     |
| Other assets   | (1,192)                    | 178                        |
| Accounts payable   | 6,747                      | (21,216)                   |
| Accrued liabilities  | 13,861                     | (19,389)                   |
| Deferred revenue   | (1,530)                    | 2,674                      |
| Income taxes   | 9,197                      | (2,394)                    |
| Other operating activities   | (3,391)                    | 584                        |
| <b>Net cash provided by operating activities</b>   | <b>101,738</b>             | <b>62,983</b>              |
| <b>Cash flows from investing activities:</b>   |                            |                            |
| Purchases of property and equipment  | (23,752)                   | (19,499)                   |
| Payments for patents and licensing arrangements  | (2,882)                    | (425)                      |
| Purchases of investments and marketable securities   | (312,201)                  | (236,520)                  |
| Maturities of investments and marketable securities  | 230,715                    | 194,939                    |
| Sales of investments and marketable securities   | 74,371                     | 49,899                     |
| <b>Net cash used in investing activities</b>   | <b>(33,749)</b>            | <b>(11,606)</b>            |
| <b>Cash flows from financing activities:</b>   |                            |                            |
| Purchase of treasury stock   | (67,384)                   | (49,609)                   |
| Proceeds from exercise of stock options and stock purchase plan purchases                          | 7,772                      | 3,250                      |
| Excess tax benefit from equity-based compensation  | 83                         | 11                         |
| <b>Net cash used in financing activities</b>   | <b>(59,529)</b>            | <b>(46,348)</b>            |
| Effect of exchange rate changes on cash  | 44                         | 752                        |



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|  |           |           |
|--|-----------|-----------|
| Net increase in cash and cash equivalents                    | 8,504     | 5,781     |
| Cash and cash equivalents at beginning of period             | 38,943    | 33,267    |
| Cash and cash equivalents at end of period                   | \$ 47,447 | \$ 39,048 |
| Supplemental disclosures of cash flow information:           |           |           |
| Income taxes paid  | \$ 17,162 | \$ 9,764  |
| See accompanying notes to consolidated financial statements. |           |           |

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**ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited)

**Note 1 Basis of Presentation**

Management prepared these unaudited interim consolidated financial statements for Zebra Technologies Corporation and subsidiaries ( Zebra ) according to the rules and regulations of the Securities and Exchange Commission ( SEC ) for interim financial information. Accordingly, they do not include all of the information and footnotes required by United States generally accepted accounting principles ( GAAP ) for complete financial statements. Therefore, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in Zebra s Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

The consolidated balance sheet as of December 31, 2009 in this Form 10-Q is taken from the audited consolidated balance sheet in our Form 10-K. These interim financial statements include all adjustments (of a normal, recurring nature) necessary to present fairly Zebra s consolidated financial position as of October 2, 2010, the consolidated statement of earnings for the three and nine months ended October 2, 2010 and October 3, 2009, and consolidated statement of cash flows for the nine months ended October 2, 2010 and October 3, 2009. These results, however, are not necessarily indicative of results for the full year.

*Reclassifications.* Certain amounts in the prior years financial statements have been reclassified to conform to the current year s presentation. For the three and nine months ended October 3, 2009, general and administrative expenses of \$602,000 and \$1,799,000 were reclassified to selling and marketing expenses. For the three and nine months ended October 3, 2009, general and administrative expenses of \$299,000 and \$979,000 were reclassified to research and development expenses. These reclassifications were made to better reflect costs as they relate to their functional areas. In addition, write-offs of an equity investment in an international technology company in the amount of \$88,000 and \$855,000 for the three and nine months ended October 3, 2009 that were previously presented netted against asset impairment charges were reclassified to investment income in order to be consistent with the 2009 year end presentation. Prior period amounts will differ in the above categories from amounts previously reported.

**Note 2 Fair Value Measurements**

Financial assets and liabilities are to be measured using inputs from three levels of the fair value hierarchy. Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Zebra uses a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as consider counterparty credit risk in the assessment of fair value.

Included in our investment portfolio are three auction rate security instruments. These instruments are classified as available-for-sale securities and are reflected at fair value. Due to events in credit markets, however, the auction events for the instruments held by Zebra as of October 2, 2010, are failed. Therefore, the fair values of these securities are estimated utilizing broker quotations, discounted cash flow analysis or other types of valuation adjustment methodologies at October 2, 2010. These analyses consider, among other items, the collateral underlying the security instruments, the creditworthiness of the counterparty, the timing of expected future cash flows, estimates of the next time the security is expected to have a successful auction, and Zebra s intent and ability to hold such securities until credit markets improve.



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These securities were also compared, when possible, to other securities with similar characteristics. In June 2010, one of the four auction rate securities held at the end of the first quarter of 2010 was called by the issuer and redeemed at par value. Zebra received proceeds in the amount of \$1,650,000 and adjusted other comprehensive income by \$200,000. See Level 3 table below for more details.

Of the three auction rate security instruments still held, Zebra deemed one to be other than temporarily impaired and recorded the market value decline in 2008. The decline in the market value of the other securities is considered temporary and has been recorded in accumulated other comprehensive income (loss) on Zebra's balance sheet. Since Zebra has the intent and ability to hold these securities until they are sold at auction, redeemed at carrying value or reach maturity, we have classified them as long-term investments on the balance sheet.

Financial assets and liabilities carried at fair value as of October 2, 2010, are classified below (in thousands):

|  | Level 1           | Level 2       | Level 3         | Total             |
|--|-------------------|---------------|-----------------|-------------------|
| <b>Assets:</b>   |                   |               |                 |                   |
| U.S. government and agency securities                              | \$ 19,231         | \$            | \$              | \$ 19,231         |
| Obligations of government-sponsored enterprises (1)                | 7,999             |               |                 | 7,999             |
| State and municipal bonds  | 140,782           |               | 2,683           | 143,465           |
| Corporate securities   | 39,489            |               | 2,914           | 42,403            |
| Other investments  | 36                |               |                 | 36                |
| Investments subtotal   | 207,537           |               | 5,597           | 213,134           |
| Money market investments related to the deferred compensation plan | 3,196             |               |                 | 3,196             |
| <b>Total assets at fair value</b>                                  | <b>\$ 210,733</b> |               | <b>\$ 5,597</b> | <b>\$ 216,330</b> |
| <b>Liabilities:</b>  |                   |               |                 |                   |
| Forward contracts (2)  | \$ 5,295          | 578           |                 | \$ 5,873          |
| Liabilities related to the deferred compensation plan              | 3,185             | \$            | \$              | 3,185             |
| <b>Total liabilities at fair value</b>                             | <b>\$ 8,480</b>   | <b>\$ 578</b> | <b>\$</b>       | <b>\$ 9,058</b>   |

Financial assets and liabilities carried at fair value as of December 31, 2009, are classified below (in thousands):

|  | Level 1           | Level 2   | Level 3         | Total             |
|--|-------------------|-----------|-----------------|-------------------|
| <b>Assets:</b>   |                   |           |                 |                   |
| U.S. government and agency securities                              | \$ 12,811         | \$        | \$              | \$ 12,811         |
| Obligations of government-sponsored enterprises (1)                | 10,666            |           |                 | 10,666            |
| State and municipal bonds  | 161,839           |           | 4,133           | 165,972           |
| Corporate securities   | 13,654            |           | 2,914           | 16,568            |
| Other investments  | 36                |           |                 | 36                |
| Investments subtotal   | 199,006           |           | 7,047           | 206,053           |
| Forward contracts (2)  | 851               |           |                 | 851               |
| Money market investments related to the deferred compensation plan | 3,155             |           |                 | 3,155             |
| <b>Total assets at fair value</b>                                  | <b>\$ 203,012</b> | <b>\$</b> | <b>\$ 7,047</b> | <b>\$ 210,059</b> |
| <b>Liabilities:</b>  |                   |           |                 |                   |
| Liabilities related to the deferred compensation plan              | \$ 3,155          | \$        | \$              | \$ 3,155          |
| <b>Total liabilities at fair value</b>                             | <b>\$ 3,155</b>   | <b>\$</b> | <b>\$</b>       | <b>\$ 3,155</b>   |

- (1) Includes investments in notes issued by the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association and the Federal Home Loan Bank.

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(2) The fair value of forward contracts are calculated as follows:

- a. Fair value of forward collar contract associated with forecasted sales hedges are calculated using the midpoint of ask and bid rates for similar contracts.
- b. Fair value of regular forward contracts associated with forecasted sales hedges are calculated using the period-end exchange rate adjusted for the discount rate (3 month LIBOR rate).
- c. Fair value of balance sheet hedges are calculated at the period end exchange rate adjusted for current forward points unless the hedge has been traded but not settled at period end. If this is the case, the fair value is calculated at the rate at which the hedge is being settled.

The following table presents Zebra's activity for assets measured at fair value on a recurring basis using significant unobservable inputs, Level 3, for the three month periods (in thousands):

|   | Nine Months Ended |                 |
|---|-------------------|-----------------|
|   | October 2, 2010   | October 3, 2009 |
| Balance at beginning of the year  | \$ 7,047          | \$ 7,047        |
| Transfers to Level 3  |                   |                 |
| Total losses (realized or unrealized):  |                   |                 |
| Included in earnings  |                   |                 |
| Included in other comprehensive income (loss)   | 200               |                 |
| Purchases and settlements (net)   | (1,650)           |                 |
| <br>  |                   |                 |
| Balance at end of period  | \$ 5,597          | \$ 7,047        |
| <br>  |                   |                 |
| Total gains and (losses) for the period included in earnings attributable to the change in unrealized losses relating to assets still held at end of period | \$                | \$              |

The following is a summary of short-term and long-term investments at October 2, 2010 and December 31, 2009 (in thousands):

|   | As of October 2, 2010   |                        |                         | Estimated Fair Value |
|---|-------------------------|------------------------|-------------------------|----------------------|
|   | Amortized Cost          | Gross Unrealized Gains | Gross Unrealized Losses |                      |
| U.S. government and agency securities           | \$ 19,084               | \$ 153                 | \$ (6)                  | \$ 19,231            |
| Obligations of government-sponsored enterprises | 7,877                   | 122                    |                         | 7,999                |
| State and municipal bonds                       | 143,225                 | 638                    | (398)                   | 143,465              |
| Corporate securities                            | 42,516                  | 303                    | (416)                   | 42,403               |
| Other investments                               | 36                      |                        |                         | 36                   |
| <br>  |                         |                        |                         |                      |
| Total investments                               | \$ 212,738              | \$ 1,216               | \$ (820)                | \$ 213,134           |
| <br>  |                         |                        |                         |                      |
|   | As of December 31, 2009 |                        |                         | Estimated Fair Value |
|   | Amortized Cost          | Gross Unrealized Gains | Gross Unrealized Losses |                      |
| U.S. government and agency securities           | \$ 12,931               | \$ 45                  | \$ (165)                | \$ 12,811            |
| Obligations of government-sponsored enterprises | 10,589                  | 82                     | (5)                     | 10,666               |
| State and municipal bonds                       | 165,366                 | 1,177                  | (571)                   | 165,972              |
| Corporate securities                            | 16,680                  | 306                    | (418)                   | 16,568               |
| Other investments                               | 36                      |                        |                         | 36                   |

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|                   |            |          |            |            |
|-------------------|------------|----------|------------|------------|
| Total investments | \$ 205,602 | \$ 1,610 | \$ (1,159) | \$ 206,053 |
|-------------------|------------|----------|------------|------------|

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The maturity dates of investments are as follows (in thousands):

|                  | As of October 2, 2010 |                            |
|------------------|-----------------------|----------------------------|
|                  | Amortized<br>Cost     | Estimated<br>Fair<br>Value |
| Less than 1 year | \$ 122,785            | \$ 123,058                 |
| 1 to 5 years     | 88,892                | 88,995                     |
| 6 to 10 years    | 1,061                 | 1,081                      |
| Thereafter       |                       |                            |
| <b>Total</b>     | <b>\$ 212,738</b>     | <b>\$ 213,134</b>          |

The carrying value for Zebra's financial instruments classified as current assets (other than short-term investments) and current liabilities approximate fair value due to short maturities.

**Note 3 Investments and Marketable Securities**

We classify our investments in marketable debt securities as available-for-sale. As of October 2, 2010, all of our investments in marketable debt securities with maturities greater than one year are classified as long-term investments on the balance sheet due to our ability and intent to hold them until maturity.

Changes in the market value of available-for-sale securities are reflected in the accumulated other comprehensive income caption of stockholders' equity in the balance sheet, until we dispose of the securities. Once these securities are disposed of, either by sale or maturity, the accumulated changes in market value are transferred to investment income. On the statement of cash flows, changes in the balances of *available-for-sale* securities are shown as purchases, sales and maturities of investments and marketable securities under investing activities.

Changes in market value of *trading* securities would be recorded in investment income as they occur, and the related statement of cash flows would include changes in the balances of trading securities as operating cash flows.

Change in unrealized gains and losses on available-for-sale securities are included in these financial statements as follows (in thousands):

|   | Three Months Ended |                    | Nine Months Ended  |                    |
|---|--------------------|--------------------|--------------------|--------------------|
|   | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
| Changes in unrealized gains and losses on available-for-sale securities, net of tax, recorded in accumulated other comprehensive income | \$ 8               | \$ 289             | \$ (34)            | \$ 814             |

**Note 4 Inventories**

The components of inventories are as follows (in thousands):

|              | As of              |                      |
|--------------|--------------------|----------------------|
|              | October 2,<br>2010 | December 31,<br>2009 |
| Raw material | \$ 30,916          | \$ 27,953            |



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|                                       |                  |                  |
|---------------------------------------|------------------|------------------|
| Work in process                       | 614              | 162              |
| Deferred costs of long-term contracts | 427              | 1,937            |
| Finished goods                        | 73,060           | 58,928           |
| <b>Total inventories, gross</b>       | <b>105,017</b>   | <b>88,980</b>    |
| Inventory reserves                    | (9,175)          | (9,054)          |
| <b>Total inventories, net</b>         | <b>\$ 95,842</b> | <b>\$ 79,926</b> |

**Table of Contents****Note 5 Goodwill and Other Intangible Assets**

Intangible asset data are as follows (in thousands):

|                             | As of October 2, 2010 |                          |                  |
|-----------------------------|-----------------------|--------------------------|------------------|
|                             | Gross Amount          | Accumulated Amortization | Net Amount       |
| Amortized intangible assets |                       |                          |                  |
| Current technology          | \$ 31,918             | \$ (19,887)              | \$ 12,031        |
| Patent and patent rights    | 16,545                | (8,618)                  | 7,927            |
| Customer relationships      | 44,727                | (13,093)                 | 31,634           |
| <b>Total</b>                | <b>\$ 93,190</b>      | <b>\$ (41,598)</b>       | <b>\$ 51,592</b> |

Amortization expense for the nine months ended October 2, 2010

\$ 7,147

|                             | As of December 31, 2009 |                          |                  |
|-----------------------------|-------------------------|--------------------------|------------------|
|                             | Gross Amount            | Accumulated Amortization | Net Amount       |
| Amortized intangible assets |                         |                          |                  |
| Current technology          | \$ 32,038               | \$ (17,071)              | \$ 14,967        |
| Patent and patent rights    | 13,663                  | (6,774)                  | 6,889            |
| Customer relationships      | 44,822                  | (10,696)                 | 34,126           |
| <b>Total</b>                | <b>\$ 90,523</b>        | <b>\$ (34,541)</b>       | <b>\$ 55,982</b> |

Amortization expense for the year ended December 31, 2009

\$ 10,466

| <b>Goodwill</b>         | As of                  |                          |
|-------------------------|------------------------|--------------------------|
|                         | <b>October 2, 2010</b> | <b>December 31, 2009</b> |
| Goodwill at gross cost  | \$ 265,799             | \$ 265,799               |
| Impairment charges      | (112,184)              | (112,184)                |
| Foreign exchange impact | (1,197)                | (390)                    |
| <b>Goodwill</b>         | <b>\$ 152,418</b>      | <b>\$ 153,225</b>        |

During the second quarter of 2010, Zebra entered into an agreement with an international technology provider to acquire patents and patent rights related to card printer solutions technology. The agreement requires total consideration in the amount of 2,400,000. Zebra has paid 1,950,000 or \$2,399,000 in accordance with the agreement through the end of September 2010, and has an obligation to pay an additional 450,000 in the fourth quarter upon completion of the agreement. This agreement provides Zebra with a new distribution partner and enhanced technology solutions and software.

Certain of our intangible assets including goodwill are denominated in foreign currency and, as such, include the effects of foreign currency translation.

We test goodwill for impairment on an annual basis or more frequently if we believe indicators of impairment exist.

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Factors considered that may trigger an impairment review consist of:

Significant underperformance relative to historical or projected future operating results,

Significant changes in the manner of use of the acquired assets or the strategy for the overall business,

Significant negative industry or economic trends,

Significant decline in Zebra's stock price for a sustained period, and

Significant decline in market capitalization relative to net book value.

If we believe that one or more of the above indicators of impairment have occurred, we perform an impairment test. The performance of the test involves a two-step process. The first step of the impairment test involves comparing the fair values of the applicable reporting units with their aggregate carrying values, including goodwill. We generally determine the fair value of our reporting units using three valuation methods: Income Approach, Discounted Cash Flow Analysis, Market Approach, Guideline Public Company Method and Market Approach, Comparative Transactions Method. If

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the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test to determine the amount of impairment loss. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill.

We performed our annual impairment test in June 2010 and determined that our goodwill was not impaired as of the end of May 2010.

**Note 6 Costs Associated with Exit or Disposal Activities**

In 2008, we announced plans to establish regional distribution and configuration centers, consolidate our supplier base, and transfer final assembly of thermal printers to Jabil Circuit, Inc., a global third-party electronics manufacturer. These actions are intended to optimize our global printer product supply chain by improving responsiveness to customer needs and increasing Zebra's flexibility to meet emerging business opportunities. As a result, substantially all printer manufacturing in our Vernon Hills, Illinois, and Camarillo, California, facilities has been transferred to Jabil's facility in Guangzhou, China, and there are no further related exit costs that are expected to be incurred.

As of October 2, 2010, we have incurred the following exit costs (in thousands):

| Type of Cost   | Cost incurred through December 31, 2009 | Costs incurred for the nine months ended October 2, 2010 | Total costs incurred as of October 2, 2010 |
|--|---|--|--|
| Severance, stay bonuses, and other employee-related expenses | \$ 7,633                                | \$ 103   | \$ 7,736                                   |
| Professional services  | 5,915                                   | 115  | 6,030                                      |
| Relocation and transition costs                              | 8,802                                   | 1,959  | 10,761                                     |
| Other exit costs   | 30                                      | 215  | 245  |
| <b>Total</b>   | <b>\$ 22,380</b>                        | <b>\$ 2,392</b>  | <b>\$ 24,772</b>                           |

For the nine months ended October 2, 2010, we have incurred the following exit costs by segment (in thousands):

| Type of Cost   | Specialty Printing Group (SPG) costs | Zebra Enterprise Solutions (ZES) costs | Total costs incurred for the nine months ended October 2, 2010 |
|--|--------------------------------------|--|--|
| Severance, stay bonuses, and other employee-related expenses | \$ 94                                | \$ 9                                   | \$ 103   |
| Professional services  | 110                                  | 5                                      | 115  |
| Relocation and transition costs                              | 1,959                                | 0                                      | 1,959  |
| Other exit costs   | 0                                    | 215                                    | 215  |
| <b>Total</b>   | <b>\$ 2,163</b>                      | <b>\$ 229</b>                          | <b>\$ 2,392</b>  |

For the nine months ended October 3, 2009, we incurred the following exit, restructuring and integration costs by segment (in thousands):

| Type of Cost | Specialty Printing Group (SPG) costs | Zebra Enterprise Solutions (ZES) costs | Total costs incurred for the nine months ended October |
|--------------|--------------------------------------|--|--|
|--------------|--------------------------------------|--|--|

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|  |              |              | 3,<br>2009   |
|--|--------------|--------------|--------------|
| Severance, stay bonuses, and other employee-related expenses | \$ 1,530     | \$ 969       | \$ 2,499     |
| Professional services  | 54           | 1            | 55           |
| Relocation and transition costs                              | 4,526        | 0            | 4,526        |
| Other exit costs   | 0            | 10           | 10           |
| Integration costs  | 0            | 2,365        | 2,365        |
| <br>Total  | <br>\$ 6,110 | <br>\$ 3,345 | <br>\$ 9,455 |

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Liabilities and expenses related to exit activities were as follows (in thousands):

|                                | Nine Months Ended |                 |
|--------------------------------|-------------------|-----------------|
|                                | October 2, 2010   | October 3, 2009 |
| Balance at beginning of period | \$ 3,038          | \$ 6,378        |
| Charged to earnings            | 2,392             | 7,090           |
| Cash paid                      | (4,159)           | (9,991)         |
| Balance at the end of period   | \$ 1,271          | \$ 3,477        |

Liabilities related to exit activities are included in the accrued liabilities line item on the balance sheet. All current exit costs are included in operating expenses under the line item exit, restructuring and integration costs.

**Note 7 Derivative Instruments**

In the normal course of business, portions of our operations are subject to fluctuations in currency values. We manage these risks using derivative financial instruments. We conduct business on a multinational basis in a wide variety of foreign currencies. Our exposure to market risk for changes in foreign currency exchange rates arises from international financing activities between subsidiaries, foreign currency denominated monetary assets and liabilities and transactions arising from international trade. Our objective is to preserve the economic value of non-functional currency denominated cash flows. We attempt to hedge transaction exposures with natural offsets to the fullest extent possible and, once these opportunities have been exhausted, through foreign exchange forward and option contracts with third parties.

*Credit and market risk*

Financial instruments, including derivatives, expose us to counter party credit risk for nonperformance and to market risk related to interest and currency exchange rates. We manage our exposure to counterparty credit risk through specific minimum credit standards, diversification of counterparties, and procedures to monitor concentrations of credit risk. Our counterparties in derivative transactions are commercial banks with significant experience using derivative instruments. We monitor the impact of market risk on the fair value and cash flows of our derivative and other financial instruments considering reasonably possible changes in interest rates and currency exchange rates and restrict the use of derivative financial instruments to hedging activities.

We continually monitor the creditworthiness of our customers to which we grant credit terms in the normal course of business. The terms and conditions of our credit sales are designed to mitigate or eliminate concentrations of credit risk with any single customer. Our sales are not materially dependent on a single customer or a small group of customers.

*Fair Value of Derivative Instruments*

Zebra has determined that derivative instruments for hedges that have traded but have not settled are considered Level 1 in the fair value hierarchy, and hedges that have not traded are considered Level 2 in the fair value hierarchy. Derivative instruments are used to manage risk and are not used for trading or other speculative purposes, nor do we use leveraged derivative financial instruments. Our foreign currency exchange contracts are valued using broker quotations or market transactions, in either the listed or over-the-counter markets.

*Hedging of Net Assets*

We use forward contracts and options to manage exposure related to our pound and euro-denominated net assets. Forward contracts typically mature within three months after execution of the contracts. We record gains and losses on these contracts and options in income each quarter along with the transaction gains and losses related to our net asset positions, which would ordinarily offset each other. Summary financial information related to these activities included in our consolidated statement of earnings as other income (expense) is as follows (in thousands):

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|  | Three Months Ended |                    | Nine Months Ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
| Change in gains (losses) from foreign exchange derivatives | \$ (6,446)         | \$ (2,149)         | \$ 2,626           | \$ (1,348)         |
| Gain (loss) on net foreign currency assets                 | 6,121              | 2,724              | (2,391)            | 508                |
| Foreign exchange gain (loss)                               | \$ (325)           | \$ 575             | \$ 235             | \$ (840)           |

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|  | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|--|--------------------|-------------------------------|
| Notional balance of outstanding contracts: |                    |                               |
| Pound/US dollar                            | £ 8,419            | £ 7,500                       |
| Euro/US dollar                             | 42,905             | 37,000                        |
| Net fair value of outstanding contracts    | \$ (212)           | \$ (6)                        |

Summary financial information related to the cash flow hedges is as follows (in thousands):

|   | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|---|--------------------|-------------------------------|
| Net unrealized gains (losses) deferred in other comprehensive income: |                    |                               |
| Gross   | \$ (3,297)         | \$ 31                         |
| Income tax benefit  | (1,241)            | 12                            |
| Net   | \$ (2,056)         | \$ 19                         |

*Hedging of Anticipated Sales*

We can manage the exchange rate risk of anticipated euro-denominated sales using purchased options, forward contracts, participating forwards and option collars. We designate these contracts as cash flow hedges which mature within twelve months after the execution of the contracts. Gains and losses on these contracts are deferred in other comprehensive income until the contracts are settled and the hedged sales are realized, the deferred gains or losses will then be reported as an increase or decrease to sales.

Summary financial information related to the cash flow hedges of future revenues follows (in thousands, except percentages):

|   | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|---|--------------------|-------------------------------|
| Notional balance of outstanding contracts versus the dollar | 62,450             |                               |
| Hedge effectiveness   | 100%               |                               |

|  | Three Months Ended |                    | Nine Months Ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
| Net gains and (losses) included in revenue | \$                 | \$ (629)           | \$                 | \$ 724             |

*Forward contracts*

We record our forward contracts at fair value on our consolidated balance sheet as either other assets or other liabilities depending upon the fair value calculation as detailed in Note 2 of Zebra's financial statements. The amounts recorded on our consolidated balance sheet are as follows (in thousands):

|         | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|---------|--------------------|-------------------------------|
| Assets: |                    |                               |



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|                          |                 |           |            |
|--------------------------|-----------------|-----------|------------|
| Other assets             | \$              | \$        | 851        |
| <b>Total</b>             | <b>\$</b>       | <b>\$</b> | <b>851</b> |
| Liabilities:             |                 |           |            |
| <b>Other liabilities</b> | <b>\$ 5,873</b> | <b>\$</b> |            |
| <b>Total</b>             | <b>\$ 5,873</b> | <b>\$</b> |            |

**Table of Contents****Note 8 Warranty**

In general, Zebra provides warranty coverage of one year on SPG printers against defects in material and workmanship. SPG printheads are warranted for nine months and batteries are warranted for twelve months. Warranty coverage for most ZES hardware products is similar, with coverage periods ranging from 90 days to one year depending on the nature of the product. Battery based products, such as location tags, are covered by a 30 day warranty. For ZES software products, the warranty period is generally 90 days and provides coverage against defects in material and workmanship as well as performance materially in compliance with the accompanying documentation. A provision for warranty expense is recorded at the time of shipment and adjusted quarterly based on historical warranty experience.

The following table is a summary of Zebra's accrued warranty obligation (in thousands):

|                                      | Nine Months Ended |                 |
|--------------------------------------|-------------------|-----------------|
|                                      | October 2, 2010   | October 3, 2009 |
| Balance at the beginning of the year | \$ 3,813          | \$ 2,814        |
| Warranty expense                     | 4,490             | 3,477           |
| Warranty payments                    | (4,101)           | (3,033)         |
| Balance at the end of the period     | \$ 4,202          | \$ 3,258        |

In the European Union, we have an obligation to recycle printers. We reserve for this obligation based on the number of new printers sold after August 13, 2005, and printers sold prior to that date that are returned to us upon our sale of a new printer to a customer. The following is a summary of Zebra's accrued recycling obligation (in thousands):

|                                      | Nine Months Ended |                 |
|--------------------------------------|-------------------|-----------------|
|                                      | October 2, 2010   | October 3, 2009 |
| Balance at the beginning of the year | \$ 1,001          | \$ 1,207        |
| Recycling expense                    | 83                | 250             |
| Reserve adjustment                   |                   | (640)           |
| Recycling payments                   |                   |                 |
| Other adjustments                    | 2                 | 138             |
| Balance at the end of the period     | \$ 1,086          | \$ 955          |

**Note 9 Contingencies**

We are subject to a variety of investigations, claims, suits and other legal proceedings that arise from time to time in the ordinary course of business, including but not limited to, intellectual property, employment, tort and breach of contract matters. We currently believe that the outcomes of such proceedings, individually and in the aggregate, will not have a material adverse impact on our business, cash flows, financial position, or results of operations. Any legal proceedings are subject to inherent uncertainties, and management's view of these matters and their potential effects may change in the future.

**Note 10 Changes to Benefit Programs**

Zebra has a Retirement Savings and Investment Plan (401(k) Plan), which is intended to qualify under Section 401(k) of the Internal Revenue Code. During the first quarter of 2009, Zebra announced changes to its 401(k) Plan, profit sharing plan and stock purchase plan. Qualified employees may participate in Zebra's 401(k) Plan by contributing up to 15% of their gross earnings to the plan subject to certain Internal Revenue Service restrictions. Effective March 1, 2009, Zebra reduced the company match to each participant's contribution from 6% of gross eligible earnings at the rate of 50%, to 3% of gross eligible earnings at the rate of 50%. Effective January 1, 2010, Zebra increased the company match to each participant's contribution to 4% of gross eligible earnings. Zebra will match 100% of the first 2% of gross eligible earnings, and

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also match the next 4% of gross eligible earnings at the rate of 50%. Zebra may contribute additional amounts to its 401(k) Plan at the discretion of the Board of Directors, subject to certain legal limits.

Zebra also has a discretionary profit-sharing plan for qualified employees, to which it contributes a percentage of eligible payroll each year. Zebra announced that it will suspend any contributions to the profit sharing plan for the 2009 plan year and plan years going forward. Participants are not permitted to make contributions under the discretionary profit-sharing plan.

**Table of Contents****Note 11 Stockholders Equity**

Share count and par value data related to stockholders equity are as follows:

|                             | October 2, 2010 | December 31, 2009 |
|-----------------------------|-----------------|-------------------|
| <b>Preferred Stock</b>      |                 |                   |
| Par value per share         | \$ 0.01         | \$ 0.01           |
| Shares authorized           | 10,000,000      | 10,000,000        |
| Shares outstanding          |                 |                   |
| <b>Common Stock Class A</b> |                 |                   |
| Par value per share         | \$ 0.01         | \$ 0.01           |
| Shares authorized           | 150,000,000     | 150,000,000       |
| Shares issued               | 72,151,857      | 72,151,857        |
| Shares outstanding          | 56,519,663      | 58,318,983        |
| Treasury stock              |                 |                   |
| Shares held                 | 15,632,194      | 13,832,874        |

During the nine-month period ended October 2, 2010, Zebra purchased 2,449,286 shares of common stock for \$67,384,000 under board authorized share repurchase plans compared to the nine-month period ended October 3, 2009, in which Zebra purchased 2,579,630 shares of common stock for \$49,609,000.

A roll forward of Class A common shares outstanding is as follows:

|                                      | Nine Months Ended |                 |
|--------------------------------------|-------------------|-----------------|
|                                      | October 2, 2010   | October 3, 2009 |
| Balance at the beginning of the year | 58,318,983        | 60,861,592      |
| Repurchases                          | (2,449,286)       | (2,579,630)     |
| Stock option and ESPP issuances      | 296,512           | 202,009         |
| Restricted share issuances           | 375,279           | 406,242         |
| Restricted share forfeitures         | (14,627)          | (48,679)        |
| Shares withheld for tax obligations  | (7,198)           | (8,914)         |
| Balance at the end of the period     | 56,519,663        | 58,832,620      |

**Note 12 Earnings Per Share**

Earnings per share were computed as follows (in thousands, except per share amounts):

|  | Three Months Ended |                 | Nine Months Ended |                 |
|--|--------------------|-----------------|-------------------|-----------------|
|  | October 2, 2010    | October 3, 2009 | October 2, 2010   | October 3, 2009 |
| <b>Basic earnings per share:</b>           |                    |                 |                   |                 |
| Net income                                 | \$ 26,151          | \$ 11,111       | \$ 73,561         | \$ 29,474       |
| Weighted average common shares outstanding | 56,739             | 58,954          | 57,405            | 59,548          |
| Per share amount                           | \$ 0.46            | \$ 0.19         | \$ 1.28           | \$ 0.49         |
| <b>Diluted earnings per share:</b>         |                    |                 |                   |                 |

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|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
| Net income   | \$ 26,151 | \$ 11,111 | \$ 73,561 | \$ 29,474 |
| Weighted average common shares outstanding                 | 56,739    | 58,954    | 57,405    | 59,548    |
| Add: Effect of dilutive securities stock options           | 259       | 129       | 252       | 95        |
| Diluted weighted average and equivalent shares outstanding | 56,998    | 59,083    | 57,657    | 59,643    |
| Per share amount   | \$ 0.46   | \$ 0.19   | \$ 1.28   | \$ 0.49   |

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Potentially dilutive securities that were excluded from the earnings per share calculation consist of options with an exercise price greater than the average market closing price of the Class A common stock during the respective three and nine month periods. These options were as follows:

|                             | Three Months Ended |                 | Nine Months Ended |                 |
|-----------------------------|--------------------|-----------------|-------------------|-----------------|
|                             | October 2, 2010    | October 3, 2009 | October 2, 2010   | October 3, 2009 |
| Potentially dilutive shares | 1,887,000          | 2,421,000       | 1,893,000         | 2,708,000       |

**Note 13 Equity-Based Compensation**

Zebra has an equity-based compensation plan and a stock purchase plan available for future grants. Zebra recognizes compensation costs using the straight-line method over the vesting period of 1 month to 5 years.

The compensation expense and the related tax benefit for equity-based payments were included in the Consolidated Statement of Earnings as follows (in thousands):

|                            | Three Months Ended |                 | Nine Months Ended |                 |
|----------------------------|--------------------|-----------------|-------------------|-----------------|
|                            | October 2, 2010    | October 3, 2009 | October 2, 2010   | October 3, 2009 |
| Cost of sales              | \$ 285             | \$ 321          | \$ 856            | \$ 907          |
| Selling and marketing      | 551                | 605             | 1,401             | 1,384           |
| Research and development   | 401                | 494             | 1,207             | 1,317           |
| General and administrative | 1,763              | 1,681           | 4,691             | 5,079           |
| <b>Total compensation</b>  | <b>3,000</b>       | <b>3,101</b>    | <b>8,155</b>      | <b>8,687</b>    |
| Income tax benefit         | \$ 1,035           | \$ 992          | \$ 2,813          | \$ 2,780        |

Cash flows resulting from the tax benefits from tax deductions in excess of the compensation cost recognized (excess tax benefits) are classified as financing cash flows in the statement of cash flows. The tax benefits classified as financing cash flows for the nine months ended October 2, 2010 was \$83,000 and for the nine months ended October 3, 2009, was \$11,000.

The fair value of equity-based compensation is estimated on the date of grant using a binomial model. Volatility is based on an average of the implied volatility in the open market and the annualized volatility of Zebra stock prices over our entire stock history. Stock option grants in the table below include both stock options, all of which were non-qualified, and stock appreciation rights (SAR) that will be settled in Zebra stock. The following table shows the weighted-average assumptions used for grants of stock options and SARs as well as the fair value of the grants based on those assumptions:

|  | Nine Months Ended |                 |
|--|-------------------|-----------------|
|  | October 2, 2010   | October 3, 2009 |
| Expected dividend yield                | 0%                | 0%              |
| Forfeiture rate                        | 9.78%             | 9.92%           |
| Volatility                             | 39.50%            | 43.08%          |
| Risk free interest rate                | 2.26%             | 2.23%           |
| Range of interest rates                | 0.06% - 3.41%     | 0.15% - 3.29%   |
| Expected weighted-average life         | 5.36 years        | 5.23 years      |
| Fair value of options and SARs granted | \$ 6,527,000      | \$ 5,970,000    |

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|  |    |       |    |      |
|--|----|-------|----|------|
| Weighted-average grant date fair value of options and SARs granted | \$ | 10.65 | \$ | 8.04 |
|--|----|-------|----|------|

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SAR activity was as follows:

| SARs                              | Nine Months Ended October 2, 2010 |                                 |
|-----------------------------------|-----------------------------------|---------------------------------|
|                                   | Shares                            | Weighted-Average Exercise Price |
| Outstanding at beginning of year  | 684,058                           | \$ 19.97                        |
| Granted                           | 612,681                           | 27.82                           |
| Exercised                         | (25,442)                          | 19.56                           |
| Forfeited                         | (30,678)                          | 22.14                           |
| Expired                           | (273)                             | 19.56                           |
| Outstanding at end of period      | 1,240,346                         | \$ 23.80                        |
| Exercisable at end of period      | 154,627                           | \$ 20.15                        |
| Intrinsic value of exercised SARs | \$ 252,000                        |                                 |

There were no equity grants of SARs during the three months ended October 2, 2010.

The terms of the SARs are established under the 2006 Zebra Technologies Corporation Incentive Compensation Plan (the 2006 Plan) and the applicable SAR agreement. Once vested, a SAR entitles the holder to receive a payment equal to the difference between the per-share base price of the SAR and the fair market value of a share of Zebra stock on the date the SAR is exercised, multiplied by the number of SARs exercised. Exercised SARs are settled in whole shares of Zebra stock, and any fraction of a share is settled in cash. The SARs granted during the first nine months of 2010 vest annually in four equal amounts on each of the first four anniversaries of the grant date and expire 10 years after the grant date.

The following table summarizes information about SARs outstanding at October 2, 2010:

| Range of Exercise Prices | Outstanding      |   | Weighted-Average Exercise Price | Exercisable      |                                 |
|--------------------------|------------------|---|---------------------------------|------------------|---------------------------------|
|                          | Number of Shares | Weighted-Average Remaining Contractual Life |                                 | Number of Shares | Weighted-Average Exercise Price |
| \$ 19.56-\$19.56         | 578,598          | 8.59 years                                  | \$ 19.56                        | 127,463          | \$ 19.56                        |
| \$ 19.57-\$27.50         | 75,686           | 9.05 years                                  | 24.84                           | 27,164           | 22.95                           |
| \$ 27.51-\$27.82         | 568,938          | 9.59 years                                  | 27.82                           | 0                | 0.00                            |
| \$ 27.83-\$29.06         | 11,647           | 9.47 years                                  | 28.57                           | 0                | 0.00                            |
| \$ 29.07-\$30.08         | 5,477            | 9.45 years                                  | 30.08                           | 0                | 0.00                            |
|                          | 1,240,346        |   |                                 | 154,627          |                                 |

|   |             |               |             |              |
|---|-------------|---------------|-------------|--------------|
| Aggregate intrinsic value                   | Outstanding | \$ 12,438,000 | Exercisable | \$ 2,114,000 |
| Weighted-average remaining contractual term |             | 9.1 years     |             | 8.6 years    |

Stock option activity was as follows:



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| Options                              | Nine Months Ended October 2, 2010 |                                 |
|--------------------------------------|-----------------------------------|---------------------------------|
|                                      | Shares                            | Weighted-Average Exercise Price |
| Outstanding at beginning of year     | 2,767,887                         | \$ 35.98                        |
| Granted                              | 0                                 | 0.00                            |
| Exercised                            | (206,507)                         | 23.81                           |
| Forfeited                            | (55,523)                          | 35.23                           |
| Expired                              | (67,941)                          | 35.54                           |
| Outstanding at end of period         | 2,437,916                         | \$ 37.01                        |
| Exercisable at end of period         | 1,969,919                         | \$ 37.14                        |
| Intrinsic value of exercised options | \$ 1,207,000                      |                                 |

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The following table summarizes information about stock options outstanding at October 2, 2010:

| Range of Exercise Prices | Outstanding      |   |                                 | Exercisable      |                                 |
|--------------------------|------------------|---|---------------------------------|------------------|---------------------------------|
|                          | Number of Shares | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number of Shares | Weighted-Average Exercise Price |
| \$ 1.29-\$25.23          | 541,675          | 2.76 years                                  | \$ 21.17                        | 497,744          | \$ 21.28                        |
| \$ 25.24-\$36.49         | 585,099          | 6.60 years                                  | 35.60                           | 337,950          | 35.34                           |
| \$ 36.50-\$42.28         | 518,941          | 6.49 years                                  | 40.31                           | 394,618          | 40.31                           |
| \$ 42.29-\$46.18         | 463,998          | 4.91 years                                  | 44.91                           | 411,404          | 45.03                           |
| \$ 46.19-\$53.92         | 328,203          | 3.75 years                                  | 49.33                           | 328,203          | 49.33                           |
|                          | 2,437,916        |   |                                 | 1,969,919        |                                 |

|   | Outstanding  | Exercisable  |
|---|--------------|--------------|
| Aggregate intrinsic value                   | \$ 6,983,000 | \$ 6,354,000 |
| Weighted-average remaining contractual term | 5.0 years    | 4.5 years    |

Restricted stock award activity, granted under the 2006 Plan, was as follows:

| Restricted Stock Awards          | Nine Months Ended October 2, 2010 |  |
|----------------------------------|-----------------------------------|--|
|                                  | Shares                            | Weighted-Average Grant Date Fair Value |
| Outstanding at beginning of year | 507,984                           | \$ 23.90                               |
| Granted                          | 375,279                           | 27.84                                  |
| Released                         | (22,325)                          | 29.11                                  |
| Forfeited                        | (14,627)                          | 25.88                                  |
| Outstanding at end of period     | 846,311                           | \$ 25.48                               |

There were no equity grants of restricted stock awards during the three months ended October 2, 2010.

As of October 2, 2010, there was \$20,576,000 of unearned compensation cost related to awards granted under Zebra's equity-based compensation plans, which is expected to be recognized over a weighted-average period of 2.6 years.

The fair value of the purchase rights of all Zebra employees issued under the stock purchase plan is estimated using the following weighted-average assumptions for purchase rights granted. Expected lives of three months to one year have been used along with these assumptions.

|                         | Nine Months Ended |                 |
|-------------------------|-------------------|-----------------|
|                         | October 2, 2010   | October 3, 2009 |
| Fair market value       | \$ 26.34          | \$ 20.60        |
| Option price            | \$ 25.02          | \$ 18.62        |
| Expected dividend yield | 0%                | 0%              |
| Expected volatility     | 27%               | 38%             |
| Risk free interest rate | 0.13%             | 0.16%           |

**Note 14 Income Taxes**

Zebra has identified, evaluated, and measured the amount of income tax benefits to be recognized for all of our income tax positions. Included in deferred tax assets are amounts related to federal and state net operating losses that resulted from our acquisition of WhereNet Corp. Zebra's intention is to utilize these net operating loss carryforwards to offset future income taxes owed.

Zebra has concluded all U.S. federal income tax audits for years through 2006. The tax years 2006 through 2009 remain open to examination by multiple state taxing jurisdictions. Tax authorities in the United Kingdom have completed income tax audits for tax years through 2006.

Zebra's continuing practice is to recognize interest and/or penalties related to income tax matters as part of income tax expense. For the three and nine month periods ended October 2, 2010 and October 3, 2009, we did not accrue any interest or penalties into income tax expense.

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The effective income tax rate for the third quarter of 2010 was 32.9% compared with 32.0% for the third quarter of 2009. The effective income tax rate for the first nine months of 2010 was 29.7% compared to 32.0% for the first nine months of 2009. Zebra's effective tax rate for the first quarter of 2010 included a \$2,764,000 reduction of federal taxes related to prior years' adjustments for intercompany profit in ending inventory which reduced our effective rate for the first nine months of 2010 by 2.6%.

**Note 15 Other Comprehensive Income**

Stockholders' equity includes certain items classified as accumulated other comprehensive income, including:

**Foreign currency translation adjustment** relates to our non-U.S. subsidiary companies that have designated a functional currency other than the U.S. dollar. We are required to translate the subsidiary functional currency financial statements to dollars using a combination of historical, period-end, and average foreign exchange rates. This combination of rates creates the foreign currency translation adjustment component of other comprehensive income.

**Unrealized gains (losses) on foreign currency hedging activities** relate to derivative instruments used to hedge the currency exchange rates for forecasted euro sales. These hedges are designated as cash flow hedges, and we have deferred income statement recognition of gains and losses until the hedged transaction occurs. See Note 7 for more details.

**Unrealized gains (losses) on investments classified as available-for-sale** are deferred from income statement recognition until the gains or losses are realized. See Note 3 for more details.

The Consolidated Statements of Comprehensive Income are as follows (in thousands):

|  | Three Months Ended |                    | Nine Months Ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
| Net income   | \$ 26,151          | \$ 11,111          | \$ 73,561          | \$ 29,474          |
| Other comprehensive income (loss):                                       |                    |                    |                    |                    |
| Foreign currency translation adjustment                                  | 1,237              | (660)              | (173)              | 4,137              |
| Changes in unrealized gains (losses) on hedging transactions, net of tax | (2,185)            | 352                | (2,056)            | (57)               |
| Changes in unrealized gains (losses) on investments, net of tax          | 8                  | 289                | (34)               | 814                |
| Comprehensive income   | \$ 25,211          | \$ 11,092          | \$ 71,298          | \$ 34,368          |

The components of other comprehensive income gross and net of income tax are as follows (in thousands):

|  | Three Months Ended |                    | Nine Months Ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
| Changes in unrealized gains and losses on foreign currency hedging activities: |                    |                    |                    |                    |
| Gross  | \$ (3,504)         | \$ 565             | \$ (3,297)         | \$ (91)            |
| Income tax (benefit)   | (1,319)            | 213                | (1,241)            | (34)               |

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|   |            |        |            |          |
|---|------------|--------|------------|----------|
| Net   | \$ (2,185) | \$ 352 | \$ (2,056) | \$ (57)  |
| Changes in unrealized gains and losses on investments classified as available-for-sale: |            |        |            |          |
| Gross   | \$ 13      | \$ 463 | \$ (55)    | \$ 1,305 |
| Income tax (benefit)  | 5          | 174    | (21)       | 491      |
| Net   | \$ 8       | \$ 289 | \$ (34)    | \$ 814   |

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The components of accumulated other comprehensive income (loss) included in the Consolidated Balance Sheets are as follows (in thousands):

|  | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|--|--------------------|-------------------------------|
| Foreign currency translation adjustments                                       | \$ (8,515)         | \$ (8,342)                    |
| Unrealized gains and (losses) on hedging transactions:                         |                    |                               |
| Gross  | \$ (3,298)         | \$ (1)                        |
| Income tax (benefit)   | (1,241)            |                               |
| Net  | \$ (2,057)         | \$ (1)                        |
| Unrealized gains and (losses) on investments classified as available-for-sale: |                    |                               |
| Gross  | \$ 397             | \$ 452                        |
| Income tax (benefit)   | 149                | 170                           |
| Net  | \$ 248             | \$ 282                        |

**Note 16 Segment Information**

Zebra has two reportable segments: Specialty Printing Group (SPG) and Zebra Enterprise Solutions (ZES).

SPG includes direct thermal and thermal transfer label and receipt printers, passive radio frequency identification (RFID) printer/encoders and dye sublimation card printers. Also included in this group is a comprehensive range of specialty supplies consisting of self-adhesive labels, thermal transfer ribbons, thermal printheads, batteries and other accessories, including software for label design and printer network management.

ZES has evolved since the beginning of 2007 with the acquisitions of WhereNet Corp., proveo AG, Navis Holdings, LLC and Multispectral Solutions, Inc. The solutions that these companies provide are generally sold on a contract basis and are typically installed over several quarters. These contracts cover a range of services, including design, installation and ongoing maintenance services.

Segment information is as follows (in thousands):

|                             | October 2,<br>2010 | As of<br>December 31,<br>2009 |
|-----------------------------|--------------------|-------------------------------|
| <b>Identifiable assets:</b> |                    |                               |
| SPG                         | \$ 378,380         | \$ 336,428                    |
| ZES                         | 184,037            | 185,495                       |
| Corporate and other         | 309,228            | 308,556                       |
| Total                       | \$ 871,645         | \$ 830,479                    |

| Three Months Ended |                    | Nine Months Ended  |                    |
|--------------------|--------------------|--------------------|--------------------|
| October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |

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|                                 |            |            |            |            |
|---------------------------------|------------|------------|------------|------------|
| <b>Net sales:</b>               |            |            |            |            |
| SPG Tangible products           | \$ 213,406 | \$ 171,977 | \$ 616,493 | \$ 493,491 |
| SPG Service & software          | 9,413      | 8,780      | 27,380     | 25,943     |
| SPG Net Sales                   | 222,819    | 180,757    | 643,873    | 519,434    |
| ZES Tangible products           | 8,389      | 3,357      | 15,705     | 10,456     |
| ZES Service & software          | 15,299     | 16,664     | 49,095     | 51,173     |
| ZES Net Sales                   | 23,688     | 20,021     | 64,800     | 61,629     |
| Total                           | \$ 246,507 | \$ 200,778 | \$ 708,673 | \$ 581,063 |
| <b>Operating profit (loss):</b> |            |            |            |            |
| SPG                             | \$ 60,084  | \$ 36,682  | \$ 167,457 | \$ 100,769 |
| ZES                             | (4,928)    | (2,912)    | (14,191)   | (9,839)    |
| Corporate and other             | (16,299)   | (18,532)   | (49,848)   | (48,366)   |
| Total                           | \$ 38,857  | \$ 15,238  | \$ 103,418 | \$ 42,564  |

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Zebra records its federal and state deferred tax assets and liabilities in corporate and other as reflected above. Intersegment sales are not significant. Corporate and other includes corporate administration costs or assets that support both reporting segments.

**Note 17 New Accounting Pronouncements**

In October 2009, the FASB issued update 2009-13, ASC 605, Revenue Recognition: Multiple Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force. The revised guidance provides for two significant changes to existing multiple element arrangement guidance. The first relates to the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting. This change is significant as it may result in the requirement to separate more deliverables within an arrangement, ultimately leading to less revenue deferral. The second change modifies the manner in which the transaction consideration is allocated across the separately identifiable deliverables. These changes may result in earlier recognition of revenue for multiple-element arrangements than under previous guidance. This standard is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. We have not yet determined the effect of this standard upon our consolidated financial statements.

In October 2009, the FASB issued update 2009-14, ASC 985, Software: Certain Revenue Arrangements That Include Software Elements a consensus of the FASB Emerging Issues Task Force. This updated guidance is expected to significantly affect how entities account for revenue arrangements that contain both hardware and software elements. This standard is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. We have not yet determined the effect of this standard upon our consolidated financial statements.

In January 2010, the FASB issued update 2010-06, ASC 820, Fair Value Measurements and Disclosures: Improving Disclosures about Fair Value Measurements. This updated guidance requires new disclosures related to transfers in and out of Levels 1 and 2. The standard also provides guidance on the disclosures related to Level 3 activities. In addition, existing disclosures related to disaggregation levels and disclosures about inputs and valuation techniques are clarified. This standard is effective for interim and annual periods beginning after December 15, 2009. This standard did not have a material effect upon our consolidated financial statements.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Results of Operations: Third Quarter of 2010 versus Third Quarter of 2009***Consolidated Results of Operations*

(Amounts in thousands, except percentages):

|                                   | Three Months Ended |                  | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|-----------------------------------|--------------------|------------------|----------------|-----------------------------|-----------------------------|
|                                   | October 2, 2010    | October 3, 2009  |                |                             |                             |
| <b>Net Sales</b>                  |                    |                  |                |                             |                             |
| Tangible products                 | \$ 221,795         | \$ 175,334       | 26.5           | 90.0                        | 87.3                        |
| Service & software                | 24,712             | 25,444           | (2.9)          | 10.0                        | 12.7                        |
| <b>Total net sales</b>            | <b>246,507</b>     | <b>200,778</b>   | <b>22.8</b>    | <b>100.0</b>                | <b>100.0</b>                |
| <b>Cost of Sales</b>              |                    |                  |                |                             |                             |
| Tangible products                 | 117,502            | 98,682           | 19.1           | 47.7                        | 49.1                        |
| Service & software                | 10,291             | 10,398           | (1.0)          | 4.1                         | 5.2                         |
| <b>Total cost of sales</b>        | <b>127,793</b>     | <b>109,080</b>   | <b>17.2</b>    | <b>51.8</b>                 | <b>54.3</b>                 |
| <b>Gross profit</b>               | <b>118,714</b>     | <b>91,698</b>    | <b>29.5</b>    | <b>48.2</b>                 | <b>45.7</b>                 |
| <b>Operating expenses</b>         | <b>79,857</b>      | <b>76,460</b>    | <b>4.4</b>     | <b>32.4</b>                 | <b>38.1</b>                 |
| <b>Operating income</b>           | <b>38,857</b>      | <b>15,238</b>    | <b>155.0</b>   | <b>15.8</b>                 | <b>7.6</b>                  |
| <b>Other income (expense)</b>     | <b>94</b>          | <b>1,102</b>     | <b>(91.5)</b>  |                             | <b>0.5</b>                  |
| <b>Income before income taxes</b> | <b>38,951</b>      | <b>16,340</b>    | <b>138.4</b>   | <b>15.8</b>                 | <b>8.1</b>                  |
| <b>Income taxes</b>               | <b>12,800</b>      | <b>5,229</b>     | <b>144.8</b>   | <b>5.2</b>                  | <b>2.6</b>                  |
| <b>Net income</b>                 | <b>\$ 26,151</b>   | <b>\$ 11,111</b> | <b>135.4</b>   | <b>10.6</b>                 | <b>5.5</b>                  |
| <b>Diluted earnings per share</b> | <b>\$ 0.46</b>     | <b>\$ 0.19</b>   |                |                             |                             |

*Consolidated Results of Operations - Third quarter**Sales*

Net sales for the third quarter of 2010 compared with the 2009 quarter increased 22.8% due to a broad-based increase in demand for Zebra products, driven by global economic recovery. This was the third consecutive quarter of strong year-over-year growth. The increase in sales was largely attributable to 36.8% growth in hardware sales (including all printer categories and aftermarket parts). Printer unit volume increased 32.0% for the third quarter of 2010 compared to levels in 2009.

Sales by product category were as follows (amounts in thousands, except percentages):

| Product Category | Three Months Ended |                 | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|------------------|--------------------|-----------------|----------------|-----------------------------|-----------------------------|
|                  | October 2, 2010    | October 3, 2009 |                |                             |                             |

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|                        |                   |                   |             |              |              |
|------------------------|-------------------|-------------------|-------------|--------------|--------------|
| Hardware               | \$ 178,991        | \$ 130,856        | 36.8        | 72.6         | 65.2         |
| Supplies               | 41,644            | 43,229            | (3.7)       | 16.9         | 21.5         |
| Service and software   | 24,712            | 25,443            | (2.9)       | 10.0         | 12.7         |
| Shipping and handling  | 1,160             | 1,250             | (7.2)       | 0.5          | 0.6          |
| <b>Total net sales</b> | <b>\$ 246,507</b> | <b>\$ 200,778</b> | <b>22.8</b> | <b>100.0</b> | <b>100.0</b> |

Sales increased in all geographic territories due primarily to the global economic recovery. The sales growth on a percentage basis was greatest in Latin America and Asia Pacific because of higher rates of economic growth in those regions and as a result of greater investment in sales and marketing. Movements in foreign exchange rates decreased sales by \$6,633,000 in the Europe, Middle East and Africa regions for the quarter due principally to a stronger euro against the dollar.

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Sales to customers by geographic region were as follows (in thousands, except percentages):

| Geographic Region              | Three Months Ended |                 | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|--------------------------------|--------------------|-----------------|----------------|-----------------------------|-----------------------------|
|                                | October 2, 2010    | October 3, 2009 |                |                             |                             |
| Europe, Middle East and Africa | \$ 82,456          | \$ 67,591       | 22.0           | 33.4                        | 33.7                        |
| Latin America                  | 22,338             | 17,452          | 28.0           | 9.1                         | 8.7                         |
| Asia-Pacific                   | 35,453             | 20,889          | 69.7           | 14.4                        | 10.4                        |
| Total International            | 140,247            | 105,932         | 32.4           | 56.9                        | 52.8                        |
| North America                  | 106,260            | 94,846          | 12.0           | 43.1                        | 47.2                        |
| Total net sales                | \$ 246,507         | \$ 200,778      | 22.8           | 100.0                       | 100.0                       |

*Gross Profit*

Gross profit increased 29.5% due to higher volumes and an improved product mix, with increased sales primarily in mobile, high-performance and mid-range table top printers, partially offset by \$3,653,000 in higher freight costs in 2010. Gross profit was affected by unfavorable foreign currency movements which decreased third quarter gross profit by \$5,809,000. As a percentage of sales, gross margin improved from 45.7% to 48.2%. The benefit of outsourcing printer production to a third party, higher volumes, improved product mix and continued cost control contributed to the increase in gross margin.

*Operating Expenses*

Operating expenses for the quarter increased 4.4% due mainly to greater selling and marketing expenses and research and development expenses. Several categories accounted for these increases, including compensation costs which include salaries, benefits, bonuses and commissions. Business development, outside professional services, project expenses, and travel and entertainment expenses all increased over 2009 levels. Exit, restructuring and integration costs decreased \$3,515,000 in the third quarter of 2010 as compared to 2009. Zebra's program for outsourcing its manufacturing operations is complete and the related restructuring costs for this program ended in the second quarter of 2010. Integration costs associated with the Zebra Enterprise Solutions (ZES) businesses were completed in 2009.

Operating expenses are summarized below (in thousands, except percentages):

| Operating Expenses                        | Three Months Ended |                 | Percent Change | Percent of Net Sales 2010 | Percent of Net Sales 2009 |
|---|--------------------|-----------------|----------------|---------------------------|---------------------------|
|   | October 2, 2010    | October 3, 2009 |                |                           |                           |
| Selling and marketing                     | \$ 30,365          | \$ 26,395       | 15.0           | 12.2                      | 13.1                      |
| Research and development                  | 26,746             | 21,454          | 24.7           | 10.7                      | 10.7                      |
| General and administrative                | 20,302             | 22,447          | (9.6)          | 8.1                       | 11.2                      |
| Amortization of intangible assets         | 2,444              | 2,649           | (7.7)          | 1.0                       | 1.3                       |
| Exit, restructuring and integration costs |                    | 3,515           | (100.0)        | 0.0                       | 1.8                       |
| Asset impairment charges                  |                    |                 |                |                           |                           |
| Total operating expenses                  | \$ 79,857          | \$ 76,460       | 4.4            | 32.0                      | 38.1                      |

*Other Income*

Investment income declined from lower short-term interest rates in the third quarter of 2010 compared with 2009. Zebra recorded a foreign exchange gain in the third quarter of 2009 as the U.S. dollar strengthened against the euro.

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Zebra's non-operating income and expense items are summarized in the following table (in thousands):

|                              | Three Months Ended |                 |
|------------------------------|--------------------|-----------------|
|                              | October 2, 2010    | October 3, 2009 |
| Investment income            | \$ 635             | \$ 813          |
| Foreign exchange gain (loss) | (325)              | 575             |
| Other, net                   | (216)              | (286)           |
| Total other income           | \$ 94              | \$ 1,102        |

**Table of Contents***Operating Income*

The operating income increase for the third quarter of 2010 was the result of increased sales and gross profit as noted above.

*Income Taxes*

The effective income tax rate for the third quarter of 2010 was 32.9% compared with 32.0% for the third quarter of 2009.

*Business Groups**Specialty Printing Group*

(Amounts in thousands, except percentages):

|                      | <b>Three Months Ended</b>  |                            |                           |  |  |
|----------------------|----------------------------|----------------------------|---------------------------|--|--|
|                      | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> | <b>Percent<br/>Change</b> | <b>Percent of<br/>Net Sales - 2010</b> | <b>Percent of<br/>Net Sales - 2009</b> |
| <b>Net Sales</b>     |                            |                            |                           |  |  |
| Tangible products    | \$ 213,406                 | \$ 171,977                 | 24.1                      | 95.8                                   | 95.1                                   |
| Service & software   | 9,413                      | 8,780                      | 7.2                       | 4.2                                    | 4.9                                    |
| Total net sales      | 222,819                    | 180,757                    | 23.3                      | 100.0                                  | 100.0                                  |
| <b>Cost of Sales</b> |                            |                            |                           |  |  |
| Tangible products    | 110,789                    | 96,918                     | 14.3                      | 49.8                                   | 53.6                                   |
| Service & software   | 4,785                      | 5,008                      | (4.5)                     | 2.1                                    | 2.8                                    |
| Total cost of sales  | 115,574                    | 101,926                    | 13.4                      | 51.9                                   | 56.4                                   |
| Gross profit         | 107,245                    | 78,831                     | 36.0                      | 48.1                                   | 43.6                                   |
| Operating expenses   | 47,161                     | 42,149                     | 11.9                      | 21.2                                   | 23.3                                   |
| Operating income     | \$ 60,084                  | \$ 36,682                  | 63.8                      | 26.9                                   | 20.3                                   |

*Specialty Printing Group Third quarter*

Net sales in our Specialty Printing Group (SPG) increased 23.3% with the highest percentage growth in sales occurring in Latin America and Asia Pacific, and the highest dollar growth occurring in Asia-Pacific, North America and the Europe, Middle East and Africa region.

The increase in sales was largely attributable to increased hardware sales, with notable increases in sales of high-performance and mid-range tabletop, desktop, mobile printers and aftermarket parts.

Gross profit increased due to higher volumes and an improved product mix, with increased sales primarily in mobile, high-performance and mid-range table top printers, partially offset by \$3,653,000 in higher freight costs in 2010. Gross profit for SPG was affected by unfavorable foreign currency movements which decreased third quarter gross profit by \$5,809,000. As a percentage of sales, gross margin increased. The benefit of outsourcing printer production to a third party, higher volumes, improved product mix and continued cost control contributed to the increase in gross margin.

Printer unit volumes and average selling price information is summarized below:

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|   | Three Months Ended |                    |                   |
|---|--------------------|--------------------|-------------------|
|   | October 2,<br>2010 | October 3,<br>2009 | Percent<br>Change |
| Total printers shipped                    | 265,962            | 201,713            | 31.9              |
| Average selling price of printers shipped | \$ 545             | \$ 530             | 2.8               |

For the third quarter of 2010, unit volumes increased in nearly all printer product lines compared to the same period of 2009, with notable volume increases in high-performance tabletop, desktop and mobile printers.

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Operating expense related changes for SPG are as follows (in thousands):

|                                 | <b>Three Months Ended</b>  |                            |                                  |
|---------------------------------|----------------------------|----------------------------|----------------------------------|
|                                 | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> | <b>Increase /<br/>(Decrease)</b> |
| Payroll and benefit costs       | \$ 28,969                  | \$ 24,125                  | \$ 4,844                         |
| Business development            | 4,344                      | 3,687                      | 657                              |
| Outside professional services   | 2,981                      | 2,277                      | 704                              |
| Project expenses                | 1,598                      | 927                        | 671                              |
| Travel and entertainment        | 1,940                      | 1,330                      | 610                              |
| Exit and restructuring costs    |                            | 2,375                      | (2,375)                          |
| Other expenses                  | 7,329                      | 7,428                      | (99)                             |
| <b>Total operating expenses</b> | <b>\$ 47,161</b>           | <b>\$ 42,149</b>           | <b>\$ 5,012</b>                  |

Operating expenses for SPG increased primarily to greater selling and marketing expenses from the higher level of business activity and expansion into new geographic markets. Operating expenses are higher due to increases in payroll and benefit costs, advertising and marketing costs, compliance costs, project expenses and travel and entertainment expenses. Exit, restructuring and integration costs were completed in second quarter.

**Zebra Enterprise Solutions**

(Amounts in thousands, except percentages):

|                    | <b>Three Months Ended</b>  |                            |                           |  |  |
|--------------------|----------------------------|----------------------------|---------------------------|--|--|
|                    | <b>October 2,<br/>2010</b> | <b>October 3,<br/>2009</b> | <b>Percent<br/>Change</b> | <b>Percent of<br/>Net Sales - 2010</b> | <b>Percent of<br/>Net Sales - 2009</b> |
| Net Sales          |                            |                            |                           |  |  |
| Tangible products  | \$ 8,389                   | \$ 3,357                   | 149.9                     | 35.4                                   | 16.8                                   |
| Service & software | 15,299                     | 16,664                     | (8.2)                     | 64.6                                   | 83.2                                   |
| Net sales          | 23,688                     | 20,021                     | 18.3                      | 100.0                                  | 100.0                                  |
| Cost of Sales      |                            |                            |                           |  |  |
| Tangible products  | 6,713                      | 1,764                      | 280.6                     | 28.3                                   | 8.8                                    |
| Service & software | 5,506                      | 5,390                      | 2.2                       | 23.3                                   | 26.9                                   |
| Cost of sales      | 12,219                     | 7,154                      | 70.8                      | 51.6                                   | 35.7                                   |
| Gross profit       | 11,469                     | 12,867                     | (10.9)                    | 48.4                                   | 64.3                                   |
| Operating expenses | 16,397                     | 15,779                     | 3.9                       | 69.2                                   | 78.8                                   |
| Operating loss     | \$ (4,928)                 | \$ (2,912)                 | 69.2                      | (20.8)                                 | (14.5)                                 |

**Zebra Enterprise Solutions Third quarter**

ZES sales increased 18.3% for the third quarter of 2010 compared to 2009 primarily due to increased hardware revenue. This was offset by a reduction to installation services revenue associated with customer project implementations delays. Gross margin decline for the third quarter of 2010 compared to 2009 was primarily driven by revenue mix change and license revenue being delayed due to customer project implementation delays.

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Operating expense changes for ZES are due to the following (in thousands):

|   | Three Months Ended |                    |                         |
|---|--------------------|--------------------|-------------------------|
|   | October 2,<br>2010 | October 3,<br>2009 | Increase/<br>(Decrease) |
| Payroll and benefit costs                 | \$ 9,832           | \$ 8,960           | \$ 872                  |
| Business development                      | 582                | 178                | 404                     |
| Outside professional services             | 630                | 482                | 148                     |
| Travel and entertainment                  | 974                | 601                | 373                     |
| Exit, restructuring and integration costs |                    | 1,020              | (1,020)                 |
| Other expenses                            | 4,379              | 4,538              | (159)                   |
| <b>Total operating expenses</b>           | <b>\$ 16,397</b>   | <b>\$ 15,779</b>   | <b>\$ 618</b>           |

ZES operating expenses for the third quarter of 2010 are higher than 2009 due to increases in payroll and benefit costs, selling and marketing, consulting, project expenses and travel and entertainment costs. These increases were offset by reductions to exit, restructuring and integration costs which were completed during the second quarter, and lower amortization expense due to an intangible asset being fully amortized at the end of 2009.



**Table of Contents****Results of Operations: Nine months ended October 2, 2010 versus nine months ended October 3, 2009****Consolidated Results of Operations**

(Amounts in thousands, except percentages):

|                                   | Nine Months Ended |                  | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|-----------------------------------|-------------------|------------------|----------------|-----------------------------|-----------------------------|
|                                   | October 2, 2010   | October 3, 2009  |                |                             |                             |
| <b>Net Sales</b>                  |                   |                  |                |                             |                             |
| Tangible products                 | \$ 632,198        | \$ 503,947       | 25.4           | 89.2                        | 86.7                        |
| Service & software                | 76,475            | 77,116           | (0.8)          | 10.8                        | 13.3                        |
| <b>Total net sales</b>            | <b>708,673</b>    | <b>581,063</b>   | <b>22.0</b>    | <b>100.0</b>                | <b>100.0</b>                |
| <b>Cost of Sales</b>              |                   |                  |                |                             |                             |
| Tangible products                 | 341,815           | 291,117          | 17.4           | 48.2                        | 50.1                        |
| Service & software                | 29,630            | 30,703           | (3.5)          | 4.2                         | 5.3                         |
| <b>Total cost of sales</b>        | <b>371,445</b>    | <b>321,820</b>   | <b>15.4</b>    | <b>52.4</b>                 | <b>55.4</b>                 |
| <b>Gross profit</b>               | <b>337,228</b>    | <b>259,243</b>   | <b>30.1</b>    | <b>47.6</b>                 | <b>44.6</b>                 |
| Operating expenses                | 233,810           | 216,679          | 7.9            | 33.0                        | 37.3                        |
| <b>Operating income</b>           | <b>103,418</b>    | <b>42,564</b>    | <b>143.0</b>   | <b>14.6</b>                 | <b>7.3</b>                  |
| Other income (expense)            | 1,294             | 776              | 66.8           | 0.2                         | 0.2                         |
| <b>Income before income taxes</b> | <b>104,712</b>    | <b>43,340</b>    | <b>141.6</b>   | <b>14.8</b>                 | <b>7.5</b>                  |
| Income taxes                      | 31,151            | 13,866           | 124.7          | 4.4                         | 2.4                         |
| <b>Net income</b>                 | <b>\$ 73,561</b>  | <b>\$ 29,474</b> | <b>149.6</b>   | <b>10.4</b>                 | <b>5.1</b>                  |
| Diluted earnings per share        | \$ 1.28           | \$ 0.49          |                |                             |                             |

**Consolidated Results of Operations Year to date****Sales**

Net sales for the first nine months of 2010 compared with the same 2009 period increased 22.0% due to a broad-based increase in demand for Zebra products and global economic recovery. The increase in sales was largely attributable to increased hardware sales with notable volume increases in high-performance tabletop, desktop, mobile printers and aftermarket parts. Supplies sales increased from greater shipments of labels and thermal ribbons. Printer unit volume increased 28.9% for the first nine months of 2010 compared to levels in 2009.

Sales by product category were as follows (amounts in thousands, except percentages):

| Product Category | Nine Months Ended |                 | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|------------------|-------------------|-----------------|----------------|-----------------------------|-----------------------------|
|                  | October 2, 2010   | October 3, 2009 |                |                             |                             |

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|                        |                   |                   |             |              |              |
|------------------------|-------------------|-------------------|-------------|--------------|--------------|
| Hardware               | \$ 502,500        | \$ 383,228        | 31.1        | 70.9         | 65.9         |
| Supplies               | 125,914           | 116,836           | 7.8         | 17.8         | 20.1         |
| Service and software   | 76,475            | 77,116            | (0.8)       | 10.8         | 13.3         |
| Shipping and handling  | 3,784             | 3,883             | (2.5)       | 0.5          | 0.7          |
| <b>Total net sales</b> | <b>\$ 708,673</b> | <b>\$ 581,063</b> | <b>22.0</b> | <b>100.0</b> | <b>100.0</b> |

Sales increased in all geographic territories due primarily to the global economic recovery. The sales growth on a percentage basis was greatest in Latin America and Asia Pacific because of higher rates of economic growth in those regions and as a result of greater investment in sales and marketing. Movements in foreign exchange rates decreased sales by \$7,369,000 in the Europe, Middle East and Africa regions principally due to a stronger euro against the dollar.

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Sales to customers by geographic region were as follows (in thousands, except percentages):

| Geographic Region              | Nine Months Ended |                 | Percent Change | Percent of Net Sales - 2010 | Percent of Net Sales - 2009 |
|--------------------------------|-------------------|-----------------|----------------|-----------------------------|-----------------------------|
|                                | October 2, 2010   | October 3, 2009 |                |                             |                             |
| Europe, Middle East and Africa | \$ 246,773        | \$ 211,919      | 16.4           | 34.9                        | 36.5                        |
| Latin America                  | 64,063            | 44,864          | 42.8           | 9.0                         | 7.7                         |
| Asia-Pacific                   | 89,338            | 60,136          | 48.6           | 12.6                        | 10.3                        |
| Total International            | 400,174           | 316,919         | 26.3           | 56.5                        | 54.5                        |
| North America                  | 308,499           | 264,144         | 16.8           | 43.5                        | 45.5                        |
| Total net sales                | \$ 708,673        | \$ 581,063      | 22.0           | 100.0                       | 100.0                       |

*Gross Profit*

Gross profit increased 30.1% due to higher volumes and an improved product mix, with increased sales primarily in mobile, high-performance and mid-range table top printers, partially offset by \$14,776,000 in higher freight costs in 2010. Gross profit was affected by unfavorable foreign currency movements which decreased gross profit by \$6,544,000. As a percentage of sales, gross margin improved from 44.6% to 47.6%. The benefit of outsourcing printer production to a third party, higher volumes, improved product mix and continued cost control contributed to the increase in gross margin.

*Operating Expenses*

Operating expenses for the nine-month period increased 7.9% due to greater selling and marketing expenses and research and development expenses. Several categories accounted for these increases, including compensation costs, business development, project expenses, outside professional services, travel and entertainment, and offsite meeting expenses. Amortization of intangibles decreased \$710,000 and exit costs decreased \$7,063,000 in the first nine months of 2010 as compared to 2009. Amortization decreases were due to an intangible asset being fully amortized at the end of 2009. Zebra's program for outsourcing its manufacturing operations is complete and the related restructuring costs for this program ended. In addition, integration costs associated with integrating the Zebra Enterprise Solutions (ZES) businesses were completed in 2009.

Operating expenses are summarized below (in thousands, except percentages):

| Operating Expenses                        | Nine Months Ended |                 | Percent Change | Percent of Net Sales 2010 | Percent of Net Sales 2009 |
|---|-------------------|-----------------|----------------|---------------------------|---------------------------|
|   | October 2, 2010   | October 3, 2009 |                |                           |                           |
| Selling and marketing                     | \$ 88,193         | \$ 73,992       | 19.2           | 12.4                      | 12.7                      |
| Research and development                  | 75,189            | 64,552          | 16.5           | 10.6                      | 11.1                      |
| General and administrative                | 60,889            | 61,881          | (1.6)          | 8.6                       | 10.6                      |
| Amortization of intangible assets         | 7,147             | 7,857           | (9.0)          | 1.0                       | 1.4                       |
| Exit, restructuring and integration costs | 2,392             | 9,455           | (74.7)         | 0.2                       | 1.6                       |
| Asset impairment charges                  |                   | (1,058)         | (100.0)        |                           | (.2)                      |
| Total operating expenses                  | \$ 233,810        | \$ 216,679      | 7.9            | 32.8                      | 37.3                      |

*Other Income*

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Investment income for 2009 was reduced by the write-off of an investment in an international technology company in the amount of \$855,000. Considering this item, investment income in 2010 actually declined primarily from lower short-term interest rates in the third quarter of 2010 compared with 2009.

Zebra's non-operating income and expense items are summarized in the following table (in thousands):

|                              | Nine Months Ended  |                    |
|------------------------------|--------------------|--------------------|
|                              | October 2,<br>2010 | October 3,<br>2009 |
| Investment income            | \$ 2,111           | \$ 2,238           |
| Foreign exchange gain (loss) | 235                | (840)              |
| Other, net                   | (1,052)            | (622)              |
| Total other income (loss)    | \$ 1,294           | \$ 776             |

**Table of Contents***Operating Income (Loss)*

The operating income increase for the first nine months of 2010 was the result of increased sales and gross profit as noted above.

*Income Taxes*

The effective income tax rate for the first nine months of 2010 was 29.7% compared with an income tax rate of 32.0% for the first nine months of 2009. Zebra's effective tax rate for the first nine months ended October 2, 2010 included a \$2,764,000 reduction of federal taxes related to prior years' adjustments for intercompany profit in ending inventory which reduced our effective rate by 2.6%.

**Business Groups****Specialty Printing Group**

(Amounts in thousands, except percentages):

|                     | Nine Months Ended  |                    | Percent<br>Change | Percent of<br>Net Sales - 2010 | Percent of<br>Net Sales - 2009 |
|---------------------|--------------------|--------------------|-------------------|--------------------------------|--------------------------------|
|                     | October 2,<br>2010 | October 3,<br>2009 |                   |                                |                                |
| Net Sales           |                    |                    |                   |                                |                                |
| Tangible products   | \$ 616,493         | \$ 493,491         | 24.9              | 95.7                           | 95.0                           |
| Service & software  | 27,380             | 25,943             | 5.5               | 4.3                            | 5.0                            |
| Total net sales     | 643,873            | 519,434            | 24.0              | 100.0                          | 100.0                          |
| Cost of Sales       |                    |                    |                   |                                |                                |
| Tangible products   | 328,788            | 283,777            | 15.9              | 51.1                           | 54.6                           |
| Service & software  | 13,304             | 13,281             | 0.2               | 2.0                            | 2.6                            |
| Total cost of sales | 342,092            | 297,058            | 15.2              | 53.1                           | 57.2                           |
| Gross profit        | 301,781            | 222,376            | 35.7              | 46.9                           | 42.8                           |
| Operating expenses  | 134,324            | 121,607            | 10.5              | 20.9                           | 23.4                           |
| Operating income    | \$ 167,457         | \$ 100,769         | 66.2              | 26.0                           | 19.4                           |

**Specialty Printing Group Year to date**

Net sales in our Specialty Printing Group (SPG) increased 24.0% with the highest percentage growth in sales occurring in Latin America and Asia Pacific, and the highest dollar growth occurring in North America and the Europe, Middle East and Africa region.

The increase in sales was largely attributable to increased hardware sales, with notable increases in sales of high-performance and mid-range tabletop, desktop, mobile printers and aftermarket parts. Supplies sales increased from higher shipments of labels and thermal ribbons.

Gross profit for SPG increased due to higher volumes and an improved product mix, with increased sales primarily in mobile, high-performance and mid-range table top printers, partially offset by \$14,776,000 in higher freight costs in 2010. Gross profit was affected by unfavorable foreign currency movements which decreased gross profit by \$6,544,000. As a percentage of sales, gross margin increased. The benefit of outsourcing printer production to a third party, higher volumes, improved product mix and continued cost control contributed to the increase in gross margin.

Printer unit volumes and average selling price information is summarized below:

|   | Nine Months Ended  |                    |                   |
|---|--------------------|--------------------|-------------------|
|   | October 2,<br>2010 | October 3,<br>2009 | Percent<br>Change |
| Total printers shipped                    | 781,147            | 606,130            | 28.9              |
| Average selling price of printers shipped | \$ 532             | \$ 518             | 2.6               |

For the first nine months of 2010, unit volumes increased in nearly all printer product lines compared to the same period of 2009, with notable volume increases in high-performance tabletop, desktop and mobile printers. These increases were offset by a reduction in photo printers as this line was discontinued in 2009.

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Operating expense related changes for SPG are as follows (in thousands):

|   | Nine Months Ended  |                    | Increase /<br>(Decrease) |
|---|--------------------|--------------------|--------------------------|
|   | October 2,<br>2010 | October 3,<br>2009 |                          |
| Payroll and benefit costs                 | \$ 81,859          | \$ 72,151          | \$ 9,708                 |
| Business development                      | 13,153             | 11,437             | 1,716                    |
| Outside professional services             | 7,362              | 5,215              | 2,147                    |
| Project expenses                          | 4,344              | 3,248              | 1,096                    |
| Travel and entertainment                  | 5,047              | 3,717              | 1,330                    |
| Exit, restructuring and integration costs | 2,124              | 6,002              | (3,878)                  |
| Other expenses                            | 20,435             | 19,837             | 598                      |
| Total operating expenses                  | \$ 134,324         | \$ 121,607         | \$ 12,717                |

Operating expenses for SPG increased primarily due to greater selling and marketing expenses from the higher level of business activity and expansion into new markets. Operating expenses are higher due to increases in payroll and benefit costs, advertising and marketing costs, consulting fees, compliance costs, and travel and entertainment expenses. Exit, restructuring and integration costs are being reduced as the outsourcing project was completed in 2010.

**Zebra Enterprise Solutions**

(Amounts in thousands, except percentages):

|                    | Nine Months Ended  |                    | Percent<br>Change | Percent of<br>Net Sales - 2010 | Percent of<br>Net Sales -2009 |
|--------------------|--------------------|--------------------|-------------------|--------------------------------|-------------------------------|
|                    | October 2,<br>2010 | October 3,<br>2009 |                   |                                |                               |
| Net Sales          |                    |                    |                   |                                |                               |
| Tangible products  | \$ 15,705          | \$ 10,456          | 50.2              | 24.2                           | 17.0                          |
| Service & software | 49,095             | 51,173             | (4.1)             | 75.8                           | 83.0                          |
| Net sales          | 64,800             | 61,629             | 5.1               | 100.0                          | 100.0                         |
| Cost of Sales      |                    |                    |                   |                                |                               |
| Tangible products  | 13,027             | 7,340              | 77.5              | 20.1                           | 11.9                          |
| Service & software | 16,326             | 17,422             | (6.3)             | 25.2                           | 28.3                          |
| Cost of sales      | 29,353             | 24,762             | 18.5              | 45.3                           | 40.2                          |
| Gross profit       | 35,447             | 36,867             | (3.9)             | 54.7                           | 59.8                          |
| Operating expenses | 49,638             | 46,706             | 6.3               | 76.6                           | 75.8                          |
| Operating loss     | \$ (14,191)        | \$ (9,839)         | 44.2              | (21.9)                         | (16.0)                        |

**Zebra Enterprise Solutions Year to date**

ZES sales increased 5.1% for the first nine months of 2010 compared to 2009 primarily due to higher sales of hardware related to bookings and steady license revenue. Services remained steady in a difficult economy. Margins declined as a result of the change in sales mix.

Operating expense changes for ZES are due to the following (in thousands):

|   | Nine Months Ended  |                    | Increase /<br>(Decrease) |
|---|--------------------|--------------------|--------------------------|
|   | October 2,<br>2010 | October 3,<br>2009 |                          |
| Payroll and benefit costs                 | \$ 29,816          | \$ 27,121          | \$ 2,695                 |
| Business development                      | 1,583              | 832                | 751                      |
| Outside professional services             | 1,946              | 1,247              | 699                      |
| Project expenses                          | 836                | 336                | 500                      |
| Travel and entertainment                  | 2,735              | 1,748              | 987                      |
| Exit, restructuring and integration costs | 229                | 3,344              | (3,115)                  |
| Asset impairment charge                   |                    | (1,058)            | 1,058                    |
| Amortization expense                      | 4,980              | 5,795              | (815)                    |
| Other expenses                            | 7,513              | 7,341              | 172                      |
| Total operating expenses                  | \$ 49,638          | \$ 46,706          | \$ 2,932                 |



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ZES operating expenses for the first nine months of 2010 are higher than the 2009 period due to increases in payroll and benefit costs, consulting, project expenses and travel and entertainment costs. These increases were offset due to the collection of receivables that had been previously considered uncollectible, reduced integration costs, and lower amortization expense due to an intangible asset being fully amortized at the end of 2009.

**Liquidity and Capital Resources**

(Amounts in thousands, except percentages):

|   | Nine Months Ended  |                    |
|---|--------------------|--------------------|
|   | October 2,<br>2010 | October 3,<br>2009 |
| <b>Rate of Return Analysis:</b>                 |                    |                    |
| Average cash and marketable securities balances | \$ 254,458         | \$ 224,079         |
| Annualized rate of return                       | 1.1%               | 1.3%               |

Average cash and marketable securities balances for the first nine months of 2010 increased compared to 2009 as a result of increased cash provided by operations and a lesser amount spent on stock repurchases throughout 2009 compared to 2008.

As of October 2, 2010, Zebra had \$262,196,000 in cash, restricted cash, investments and marketable securities, compared with \$246,721,000 at December 31, 2009. Factors affecting cash and investment balances during the first nine months of 2010 include the following (changes below include the impact of foreign currency):

Operations provided cash in the amount of \$101,738,000, primarily from net income.

Accounts receivable increased \$14,463,000 due to increased sales.

Inventories increased \$15,972,000 due to increases in raw materials and finished goods.

Accounts payable increased \$6,747,000 due to the timing of payments at period end.

Accrued liabilities increased \$13,861,000, due to increased benefit accruals.

Taxes payable increased \$9,197,000 due to the timing of tax payments.

Purchases of property and equipment totaled \$23,752,000.

Net sales of investments totaled \$74,371,000.

Purchases of treasury shares totaled \$67,384,000.

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Stock option exercises and purchases under the stock purchase plan contributed \$7,772,000.

Management believes that existing capital resources and funds generated from operations are sufficient to finance anticipated capital requirements.

### **Critical Accounting Policies and Estimates**

Management prepared the consolidated financial statements of Zebra under accounting principles generally accepted in the United States of America. These principles require the use of estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions we used are reasonable, based upon the information available.

Our estimates and assumptions affect the reported amounts in our financial statements. The following accounting policies comprise those that we believe are the most critical in understanding and evaluating Zebra's reported financial results.

#### *Revenue Recognition*

Product revenue is recognized once four criteria are met: (1) we have persuasive evidence that an arrangement exists; (2) delivery has occurred and title has passed to the customer, which happens at the point of shipment provided that no significant obligations remain; (3) the price is fixed and determinable; and (4) collectability is reasonably assured. Other items that affect our revenue recognition include:

#### Customer Returns

Customers have the right to return products that do not function properly within a limited time after delivery. We monitor and track product returns and record a provision for the estimated future returns based on historical experience and any notification received of pending returns. Returns have historically been within expectations and the provisions established, but Zebra cannot guarantee that it will continue to experience return rates consistent with historical patterns. Historically, our product returns have not been significant. However, if a significant issue should arise, it could have a material impact on our financial statements.

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### Growth Rebates

Some of our channel program partners are offered incentive rebates based on the attainment of specific growth targets related to products they purchase from us over a quarter or year. These rebates are recorded as a reduction to revenue. Each quarter, we estimate the amount of outstanding growth rebates and establish a reserve for them based on shipment history. Historically, actual growth rebates have been in line with our estimates.

### Pass Through Rebate Program

Some of our distributors are offered monthly rebates based on distribution of products to our program partners. These rebates are recorded as a reduction to revenue. Each month we estimate the amount of rebate earned and establish a reserve for them based on recent trends of actual activity. The actual distributor rebates paid have historically been in line with our estimates.

### Price Protection

Some of our customers are offered price protection by Zebra as an incentive to carry inventory of our product. These price protection plans provide that if we lower prices, we will credit them for the price decrease on inventory they hold. We estimate future payments under price protection programs quarterly and establish a reserve, which is charged against revenue. Our customers typically carry limited amounts of inventory, and Zebra infrequently lowers prices on current products. As a result, the amounts paid under these plans have been minimal.

### Software Revenue

We sell four types of software and record revenue as follows:

ZES has *fixed fee software implementation projects*, for which we use the percentage of completion method for revenue recognition. Under this method of accounting, we recognize revenue based on the ratio of costs incurred to total estimated costs. If increases in projected costs-to-complete are sufficient to create a loss contract, the entire estimated loss is charged to operations in the period the loss first becomes known.

Our printers contain *embedded firmware*, which is part of the hardware purchase. We consider the sale of this firmware to be incidental to the sale of the printer and do not attribute any revenue to it.

We sell a limited amount of *prepackaged, or off-the-shelf, software* for the creation of bar code labels using our printers. There is no customization required to use this software, and we have no post-shipment obligations on the software. Revenue is recognized at the time this prepackaged software is shipped.

We sometimes provide *custom software* as part of a printer installation project. We bill custom software development services separate from the related hardware. Revenue related to custom software is recognized once the custom software development services have been completed and accepted by the customer.

We recognize license revenue when (1) a signed contract is obtained; (2) delivery of the product has occurred; (3) the license fee is fixed or determinable; and (4) collection is probable.

### Maintenance and Support Agreements

We enter into post-contract maintenance and support agreements. Revenues are recognized ratably over the service period and the cost of providing these services is expensed as incurred.

### Shipping and Handling

We charge our customers for shipping and handling services based upon our internal price list for these items. The amounts billed to customers are recorded as revenue when the product ships. Any costs incurred related to these services are included in cost of sales.

Zebra enters into sales transactions that include more than one product type. This bundle of products might include printers, current or future supplies, and services. When this type of transaction occurs, we allocate the purchase price to each product type based on the fair value of the individual products determined by vendor specific objective evidence. The revenue for each individual product is then recognized when the

recognition criteria for that product is fully met.

**Table of Contents***Investments and Marketable Securities*

Investments and marketable securities at October 2, 2010, consisted of the following:

|   |       |
|---|-------|
| U.S. government and agency securities               | 9.0%  |
| Obligations of government sponsored enterprises (1) | 3.8%  |
| State and municipal bonds                           | 67.3% |
| Corporate securities                                | 19.9% |

(1) Includes investments in notes issued by the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association and the Federal Home Loan Bank.

We classify our debt and marketable equity securities in one of three categories: trading, available-for-sale or held-to-maturity. Trading securities are bought and held principally for the purpose of selling them in the near term. Held-to-maturity securities are those debt securities that Zebra has the ability and intent to hold until maturity. All investments in marketable securities are classified as available-for-sale securities.

Trading and available-for-sale securities are recorded at fair value. Held-to-maturity securities are recorded at amortized cost, adjusted for the amortization or accretion of discounts or premiums. Unrealized holding gains and losses on trading securities are included in earnings. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a separate component of stockholders' equity until realized. As of October 2, 2010, Zebra's investments in marketable debt securities are classified as available-for-sale. In addition, as of October 2, 2010, all of our investments in marketable debt securities with maturities greater than one year are classified as long-term in the consolidated balance sheet due to our ability and intent to hold them until maturity.

*Accounts Receivable*

We have standardized credit granting and review policies and procedures for all customer accounts, including:

Credit reviews of all new customer accounts,

Ongoing credit evaluations of current customers,

Credit limits and payment terms based on available credit information,

Adjustments to credit limits based upon payment history and the customer's current creditworthiness,

An active collection effort by regional credit functions, reporting directly to the corporate financial officers, and

Limited credit insurance on the majority of our international receivables.

We reserve for estimated credit losses based upon historical experience and specific customer collection issues. Over the last three years, accounts receivable reserves varied from 1.3% to 3.8% of total accounts receivable. Accounts receivable reserves as of October 2, 2010, were \$2,183,000, or 1.3% of the balance due. Accounts receivable reserves as of December 31, 2009, were \$2,186,000, or 1.4% of the balance due. The decrease is driven primarily by the collection of previously reserved accounts. We believe our reserve level is appropriate considering the

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quality of the portfolio as of October 2, 2010. While credit losses have historically been within expectations and the provisions established, we cannot guarantee that our credit loss experience will continue to be consistent with historical experience.

### *Inventories*

We value our inventories at the lower of the actual cost to purchase or manufacture using the first-in, first-out (FIFO) method, or the current estimated market value. We review inventory quantities on hand and record a provision for excess and obsolete inventory based on forecasts of product demand and production requirements for the subsequent twelve months.

Over the last three years, our reserves for excess and obsolete inventories have ranged from 6.8% to 11.0% of gross inventory. As of October 2, 2010, inventory reserves were \$9,175,000, or 8.7% of gross inventory compared to inventory reserves of \$9,054,000, or 10.2% of gross inventory as of December 31, 2009. We believe our reserve level is appropriate considering the quantities and quality of the inventories as of October 2, 2010.

### *Valuation of Goodwill*

We test the impairment of goodwill each year at the end of May or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We completed our annual assessment during June 2010 and determined that our goodwill was not impaired as of the end of May 2010.

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Goodwill of a reporting unit is tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Examples of such events or circumstances include:

Significant adverse change in legal factors or in the business climate,

Adverse action or assessment by a regulator,

Unanticipated competition,

Loss of key personnel,

More-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of,

Testing for recoverability under ASC 360 (formerly SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*) of a significant asset group within a reporting unit,

Recognition of a goodwill impairment loss in the financial statement of a subsidiary that is a component of a reporting unit, or

Allocation of a portion of goodwill to a business to be disposed of.

If we believe that one or more of the above indicators of impairment have occurred, we perform an impairment test. The performance of the test involves a two-step process. The first step of the impairment test involves comparing the fair values of the applicable reporting units with their aggregate carrying values, including goodwill. We generally determine the fair value of our reporting units using three valuation methods: Income Approach Discounted Cash Flow Analysis, Market Approach Guideline Public Company Method and Market Approach Comparative Transactions Method.

Under the Income Approach Discounted Cash Flow Analysis the key assumptions consider sales, cost of sales and operating expenses projected through the year 2016. These assumptions were determined by management utilizing our internal operating plan and assuming growth rates for revenues and operating expenses, and margin assumptions. The fourth key assumption under this approach is the discount rate which is determined by looking at current risk-free rates of capital, current market interest rates and the evaluation of risk premia relevant to the business segment. If our assumptions relative to growth rates were to change or were incorrect, our fair value calculation may change which could result in impairment.

Under the Market Approach Guideline Company Method we identified 12 publicly traded companies, including Zebra, which we believe have significant relevant similarities. For these 12 companies we calculated the mean ratio of invested capital to revenues and invested capital to EBITDA. Similar to the Income approach discussed above, sales, cost of sales, operating expenses and their respective growth rates were the key assumptions utilized. The market prices of Zebra and other guideline company shares are key assumptions. If these market prices increase, the estimated market value would increase. If the market prices decrease, the estimated market value would decrease.

Under the Market Approach Comparative Transactions Method we looked at 22 market based transactions for companies that have similarities to our business segment, including similarities to one or more of the business lines, markets, growth prospects, margins and size. We calculated mean revenue and EBITDA multiples for the selected transactions. These multiples were applied to forecasted Zebra results for that segment to estimate market value. The key assumptions and impact to changes to those assumptions would be similar to those assumptions under the

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Income Approach Discounted Cash Flow Analysis and the Market Approach Guideline Company Method .

The results of these three methods are weighted based upon management's determination with more weighing upon the Income approach because it considers anticipated future financial performance. The Market approaches are based upon historical and current economic conditions which might not reflect the long term prospects or opportunities for our business segment being evaluated.

If the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test to determine the amount of impairment loss. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill.



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*Valuation of Long-Lived and Other Intangible Assets*

We evaluate the impairment of identifiable intangibles and other long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors considered that may trigger an impairment review consist of:

Significant underperformance relative to expected historical or projected future operating results,

Significant changes in the manner of use of the acquired assets or the strategy for the overall business,

Significant negative industry or economic trends,

Significant decline in Zebra's stock price for a sustained period, and

Significant decline in market capitalization relative to net book value.

If we believe that one or more of the above indicators of impairment have occurred and the undiscounted cash flow test has failed in the case of amortizable assets, we measure impairment based on projected discounted cash flows using a discount rate that incorporates the risk inherent in the cash flows.

Net intangible assets, long-lived assets and goodwill amounted to \$288,819,000 as of October 2, 2010.

*Income Taxes*

Zebra has identified, evaluated, and measured the amount of income tax benefits to be recognized for all of our income tax positions. Included in deferred tax assets are amounts related to federal and state net operating losses that resulted from our acquisition of WhereNet Corp. Zebra's intention is to utilize these net operating loss carryforwards to offset future income taxes owed.

Zebra has concluded all U.S. federal income tax audits for years through 2006. The tax years 2006 through 2009 remain open to examination by multiple state taxing jurisdictions. Tax authorities in the United Kingdom have completed income tax audits for tax years through 2006.

Zebra's continuing practice is to recognize interest and/or penalties related to income tax matters as part of income tax expense. For the three and nine month periods ended October 2, 2010 and October 3, 2009, we did not accrue any interest or penalties into income tax expense.

The effective income tax rate for the first nine months of 2010 was 29.7% compared with an income tax rate of 32.0% for the first nine months of 2009. Zebra's effective tax rate for the nine months ended October 2, 2010 included a \$2,764,000 reduction of federal taxes related to prior years' adjustments for intercompany profit in ending inventory which reduced our effective rate by 2.6%.

**Significant Customer**

ScanSource, Inc. is our most significant customer. Our net sales to ScanSource, Inc., an international distributor of Zebra products, as a percentage of total net sales, were as follows:

**Three Months Ended**

**Nine Months Ended**

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|                               | October 2,<br>2010 | October 3,<br>2009 | October 2,<br>2010 | October 3,<br>2009 |
|-------------------------------|--------------------|--------------------|--------------------|--------------------|
| Net Sales to ScanSource, Inc. | 17.1%              | 16.8%              | 17.5%              | 14.9%              |

No other customer accounted for 10% or more of total net sales during these periods.

### Safe Harbor

Forward-looking statements contained in this filing are subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995 and are highly dependent upon a variety of important factors which could cause actual results to differ materially from those reflected or implied in such forward looking statements. These factors include:

Market acceptance of Zebra's printer and software products and competitors' product offerings and the potential effects of technological changes,

The effect of market conditions in North America and other geographic regions,

Our ability to control manufacturing and operating costs, including the success of migrating final printer product assembly offshore to a third-party manufacturer,

Success of acquisitions and their integration,

Interest rate and financial market conditions because of our large investment portfolio,

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Foreign exchange rates due to the large percentage of our international sales and operations, and

The outcome of litigation in which Zebra is involved, particularly litigation or claims related to infringement of third-party intellectual property rights.

When used in this document and documents referenced, the words anticipate, believe, estimate, will and expect and similar expressions as they relate to Zebra or its management are intended to identify such forward-looking statements. We encourage readers of this report to review Item 1A, Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2009, for a further discussion of issues that could affect Zebra's future results. Zebra undertakes no obligation, other than as may be required by law, to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changed circumstances or any other reason after the date of this report.

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

There were no material changes in Zebra's market risk during the quarter ended October 2, 2010. For additional information on market risk, refer to the "Quantitative and Qualitative Disclosures About Market Risk" section of our Form 10-K for the year ended December 31, 2009. See Note 3 to the Consolidated Financial Statements included in this report for further discussion of investments and marketable securities.

In the normal course of business, portions of Zebra's operations are subject to fluctuations in currency values. We manage these risks using derivative financial instruments. See Note 7 to the Consolidated Financial Statements included in this report for further discussion of derivative instruments.

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### **Item 4. Controls and Procedures Evaluation of Disclosure Controls and Procedures**

We conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)) as of the end of the period covered by this Form 10-Q. The evaluation was conducted under the supervision of our Disclosure Committee, and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective to provide reasonable assurance that (i) the information required to be disclosed by us in this report on Form 10-Q was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (ii) information required to be disclosed by us in our reports that we file or furnish under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

### **Changes in Internal Control over Financial Reporting**

In January 2008, Zebra began a program to update substantially all of its key financial systems over a three year period. As pieces of these systems are completed, they will be subject to the requirements related to internal control over financial reporting. The requirements for internal control over financial reporting will be a fundamental element of the design and implementation of these systems.

As of January 1, 2010, we changed the functional currency of our UK subsidiary from the pound to the U. S. dollar. As a result we modified and enhanced our reconciliation and management review controls over this subsidiary. The modified controls have been in effect since the conversion date.

During the first nine months of 2010, we made additional changes to our controls and procedures as part of our ongoing monitoring of our controls. None of these changes has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. In addition, there were no other changes that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **Inherent Limitations on the Effectiveness of Controls**

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Zebra have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

**Table of Contents****PART II - OTHER INFORMATION****Item 1. Legal Proceedings**

See Note 9 to the Consolidated Financial Statements included in this report.

**Item 1A. Risk Factors**

In addition to the other information included in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2009, and the factors identified under Safe Harbor at the end of Item 2 of Part I of this Quarterly Report on Form 10-Q, which could materially affect our business, financial condition, cash flows or results of operations. The risks described in our Annual Report on Form 10-K are not the only risks facing Zebra. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition, cash flows and/or results of operations.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds  
Treasury Shares**

During the third quarter of 2010, Zebra purchased 764,749 shares of Zebra's Class A Common Stock at a weighted average share price of \$26.96 per share, as follows:

**ISSUER PURCHASES OF EQUITY SECURITIES**

| <b>Period</b>                          | <b>Total number of shares purchased</b> | <b>Average price paid per share</b> | <b>Total number of shares purchased as part of publicly announced programs</b> | <b>Maximum number of shares that may yet be purchased under the program</b> |
|--|---|-------------------------------------|--|---|
| July 2010 (July 4 - July 31)           | 514,749                                 | \$ 25.93                            | 514,749  | 0   |
| August 2010 (August 1 - August 28)     | 139,215                                 | \$ 28.34                            | 139,215  | 2,860,785   |
| September 2010 (August 29 - October 2) | 110,785                                 | \$ 30.01                            | 110,785  | 2,750,000   |

- (1) In July 2010 the remaining shares yet to be purchased under the program were depleted. On August 3, 2010, Zebra's Board authorized the purchase of up to an additional 3,000,000 shares under the same terms as previous authorizations. The August 2010 authorization does not have an expiration date.
- (2) During the third quarter, Zebra acquired 2,069 shares of Zebra Class A Common Stock through the withholding of shares necessary to satisfy tax withholding obligations upon the vesting of restricted stock awards. These shares were acquired at an average price of \$33.30 per share.

**Item 5. Other Information**

In lieu of filing under Form 8-K, Zebra is making this filing under Item 5 of Form 10-Q.

**Amendment to Employment Agreements**

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On November 1, 2010, the Compensation Committee of the Board of Directors of Zebra approved a form of amendment to the employment agreement of each of the executive officers of Zebra other than Anders Gustafsson, the Chief Executive Officer, and recommended to the Board for its approval an identical amendment to Mr. Gustafsson's Amended and Restated Employment Agreement with Zebra (the Amendment). On November 2, 2010, the Board approved the Amendment to Mr. Gustafsson's employment agreement. The Amendment was approved as a result of guidance from the Internal Revenue Service clarifying when severance payments may commence following an employee's execution of a waiver and release. The Amendment is intended to establish the 60th day after an executive's termination of employment as the date by which severance payments, if any, payable under an employment agreement would commence.

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**Item 6. Exhibits**

|      |   |   |
|------|---|---|
| 10.1 | + | Form of Amendment to Employment Agreement between Zebra Technologies Corporation and executive officers   |
| 31.1 |   | Rule 13a-14(a)/15d-14(a) Certification  |
| 31.2 |   | Rule 13a-14(a)/15d-14(a) Certification  |
| 32.1 |   | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 32.2 |   | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 101  |   | The following financial information from Zebra Technologies Corporation Quarterly Report on Form 10-Q for the quarter ended October 2, 2010, filed with the SEC on November 5, 2010, formatted in XBRL (Extensible Business Reporting Language): (i) the consolidated balance sheets; (ii) the consolidated statements of earnings; (iii) the consolidated statements of cash flows; and (iv) notes to consolidated financial statements. |
|      | + | Management contract or compensatory plan or arrangement required to be filed as an exhibit to this Report   |



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**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.

Date: November 5, 2010

**ZEBRA TECHNOLOGIES CORPORATION**

By: /s/ Anders Gustafsson  
Anders Gustafsson  
Chief Executive Officer

Date: November 5, 2010

By: /s/ Michael C. Smiley  
Michael C. Smiley  
Chief Financial Officer

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