SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 1998

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

For the transition period from _________ to __________

Commission File Number: 0-23081

FARO TECHNOLOGIES, INC.
(Exact name of Registrant as specified in its charter)

FLORIDA	59-3157093
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
125 TECHNOLOGY PARK DRIVE, LAKE MARY, FLORIDA	32746
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, including area code: 407-333-9911

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

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

Class: Voting Common Stock, $.001 Par Value Outstanding at November 12, 1998:
11,341,470

FARO Technologies Inc.
Index to Form 10-Q

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(Unaudited)
ASSETS

	DECEMBER 31, 1997	SEPTEMBER 30, 1998
CURRENT ASSETS:		
Cash and cash equivalents	$ 28,815,069	$ 20,492,804
Accounts receivable, net of allowance	6,159,173	8,082,129
Inventories	4,275,376	5,843,376
Deferred taxes	126,572	526,572
Prepaid expenses	109,649	264,887
Total current assets	39,485,839	35,209,768
PROPERTY AND EQUIPMENT, at cost:		
Machinery and equipment	1,014,309	1,745,944
Furniture and fixtures	605,913	897,091
Total	1,620,222	2,643,035
Less accumulated depreciation	(792,442)	(1,134,065)
Property and equipment, net	827,780	1,508,970
INTANGIBLE ASSETS, net of accumulated amortization of $321,261 and $721,133, respectively	747,979	2,330,595
DEFERRED INCOME TAXES	130,735	1,269,910
TOTAL ASSETS	$ 41,192,333	$ 40,319,243

LIABILITIES AND SHAREHOLDERS' EQUITY

	DECEMBER 31, 1997	SEPTEMBER 30, 1998
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	$ 1,196,967	$ 2,002,764
Income taxes payable	413,167	--
Customer deposits	121,358	161,001
Current portion unearned service revenues	476,802	216,600
Total current liabilities	2,208,294	2,380,365
UNEARNED SERVICE REVENUES, less current portion	44,628	135,774
TOTAL LIABILITIES	2,252,922	2,516,139
SHAREHOLDERS' EQUITY:		
Class A preferred stock - par value $.001, 10,000,000 shares authorized, no shares issued and outstanding		
Common stock - par value $.001, 50,000,000 shares authorized, 9,919,000 and 11,008,138 issued and outstanding, respectively	9,919	11,045
Additional paid-in-capital	36,502,004	47,523,065
Treasury stock	--	(150,625)
Retained earnings (deficit)	3,018,265	(8,810,785)
Unearned compensation	(464,480)	(335,357)
Accumulated other comprehensive income:		
Cumulative translation adjustments	(126,297)	(434,239)
Total shareholders' equity	38,939,411	37,803,104
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 41,192,333	$ 40,319,243

See accompanying notes to consolidated financial statements.

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Unaudited)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1998	1997	1998
Sales	$5,909,306	$ 4,972,182	$6,227,841	$ 19,376,191
Cost of sales	2,379,114	2,460,143	6,567,395	7,921,748
Gross profit	3,530,192	2,512,039	9,660,446	11,454,443
Operating expenses:				
Selling	1,432,265	2,870,373	3,955,236	6,665,432
General and administrative	310,082	851,532	916,517	1,967,250
Depreciation and amortization	79,023	399,935	204,998	772,814
Research and development	326,918	737,732	721,757	1,559,710
Employee stock options	813	43,041	364,959	129,123
Purchased in-process research and development costs	--	--	--	14,374,000
Total operating expenses	2,149,101	4,902,613	6,163,467	25,468,329
Income (loss) from operations	1,381,091	(2,390,574)	3,496,979	(14,013,886)
Interest income	33,010	215,766	38,841	838,545
Other income	31,941	19,391	68,754	22,145
Interest expense	(43,809)	(3,234)	(109,660)	(11,099)
Income (loss) before income taxes	1,402,233	(2,158,651)	3,494,914	(13,164,295)
Income tax expense (benefit)	573,118	(882,347)	1,410,191	(1,335,245)
Net income (loss)	829,115	(1,276,304)	2,084,723	(11,829,050)
Other comprehensive expense				
Foreign currency translation adjustments	(59,970)	(103,488)	(103,955)	(307,942)
Other comprehensive expense	(59,970)	(103,488)	(103,955)	(307,942)
Comprehensive income (loss)	$ 769,145	$(1,379,792)	$1,980,768	$(12,136,992)
NET INCOME (LOSS) PER COMMON SHARE - BASIC	$ 0.11	$ (0.12)	$ 0.29	$ (1.13)
NET INCOME (LOSS) PER COMMON SHARE - ASSUMING DILUTION	$ 0.11	$ (0.11)	$ 0.28	$ (1.10)

See accompanying notes to consolidated financial statements.

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(Unaudited)

	Common Stock Shares	Common Stock Amounts	Additional Paid-in Capital	Unearned Compensation
BALANCE, DECEMBER 31, 1997	9,919,000	$ 9,919	$36,502,004	$ (464,480)
Common stock issued in connection with acquisition of business, net of issuance costs	916,668	917	10,260,692	
Exercise of stock options	209,470	209	77,095	
Acquisition of treasury stock	(40,000)			
Amortization of unearned compensation	129,123			129,123
Tax benefit from exercise of stock options			683,274	
Currency translation adjustment				
Net loss for period				
BALANCE, SEPTEMBER 30, 1998	11,005,138	$ 11,045	$47,523,065	$ (335,357)

	Cumulative Translation Adjustment	Treasury Stock	Retained Earnings (Deficit)	Total
BALANCE, DECEMBER 31, 1997	$(126,297)	$ --	$ 3,018,265	$38,939,411
Common stock issued in connection with acquisition of business, net of issuance costs				10,261,609
Exercise of stock options				77,304
Acquisition of treasury stock		(150,625)		(150,625)
Amortization of unearned compensation				129,123
Tax benefit from exercise of stock options				683,274
Currency translation adjustment	(307,942)			(307,942)
Net loss for period			(11,829,050)	(11,829,050)
BALANCE, SEPTEMBER 30, 1998	$434,239)	$(150,625)	$(8,810,785)	$37,803,104

See accompanying notes to consolidated financial statements.

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30, 1997	1998
OPERATING ACTIVITIES:		
Net income (loss)	$ 2,084,723	$(11,829,050)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation, amortization and other	204,998	883,399
In-process research and development		14,374,000
Employee stock options	364,959	129,123
Deferred income taxes	(276,302)	(1,391,422)
Change in operating assets and liabilities:		
Decrease (increase) in:		
Accounts receivable	(2,458,006)	(575,203)
Inventories	(448,739)	(1,537,663)
Prepaid expenses	(31,652)	(42,878)
Increase (decrease) in:		
Accounts payable and accrued liabilities	(639,054)	(992,933)
Income taxes payable	(68,294)	(413,167)
Customer deposits	(70,345)	39,643
Unearned service revenues	486,239	(169,056)
Net cash used in operating activities	(851,473)	(1,525,207)
INVESTING ACTIVITIES:		
Purchases of property and equipment	(350,849)	(852,906)
Payments of patent costs	(157,728)	(65,587)
Payments of product design costs	--	(485,120)
Acquisition of business, net of cash acquired	--	(5,306,057)
Net cash used in investing activities	(508,577)	(6,709,670)
FINANCING ACTIVITIES:		
Payments on debt	(604,806)	--
Proceeds from issuance of common stock, net	32,265,217	96,105
Acquisition of treasury stock		(150,625)
Net cash provided by (used in) financing activities	31,660,411	(54,520)
EFFECT OF FOREIGN CURRENCY FLUCTUATIONS	--	(32,868)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	30,300,361	(8,322,265)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	263,342	28,815,069
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 30,563,703	$ 20,492,804
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	$ 27,181	$ 11,099
Cash paid for income taxes	$ --	$ 492,749
Translation adjustment effect on accounts receivable	$ (103,955)	$ --
Noncash financing activities:		
Payables recorded in connection with initial public offering	$ 419,811	$ --
Net decrease in deferred tax assets and current tax liability due to exercise of employee stock options	$ --	$ 683,274

See accompanying notes to consolidated financial statements.

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 1997 AND 1998

NOTE A - DESCRIPTION OF ORGANIZATION AND BUSINESS

FARO Technologies Inc. and Subsidiaries (the "Company") develops, manufactures, markets and supports portable, software-driven, 3-D measurement systems that are used in a broad range of manufacturing and industrial applications.

On May 15, 1998 the Company acquired all the stock of privately held CATS computer aided technologies, Computeranwendungen in der Fertigungssteurung, GmbH ("CATS") of Karlsruhe, Germany for $5 million in cash, 916,668 shares of common stock of the Company, plus the right to receive up to an additional 333,332 shares of Company common stock if CATS meets certain performance goals. In addition, the Company assumed certain of CATS outstanding liabilities. CATS develops, markets and supports 3-D measurement retrofit and statistical process control software used in both main frame and PC based CAD environments. CATS is a wholly owned subsidiary of the Company and operates as a separate entity under the name of "CATS." The acquisition was treated as a purchase for accounting purposes. See Note F.

The Company has two other wholly-owned subsidiaries, FARO Worldwide, Inc. and FARO France, s.a.s., which distribute the Company's 3-D measurement equipment throughout Europe through three primary offices located in France, Germany and the United Kingdom.

NOTE B - BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all the information and footnote disclosure required by generally accepted accounting principles for complete consolidated financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of the consolidated financial position and operating results for the interim periods have been included. The consolidated results of operations for the three and nine months ended September 30, 1998 are not necessarily indicative of results that may be expected for the year ending December 31, 1998. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements of the Company as of December 31, 1996 and 1997, and for each of the three years in the period ended December 31, 1997 included in the Company's Annual Report to Stockholders included by reference within the Company's Annual Report on Form 10-K and in conjunction with the Form S-1, as amended, dated August 7, 1998.

Effective January 1, 1998 the Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS No. 130). SFAS No. 130 requires that all items that are required to be recognized under accounting standards as components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements. Prior year financial statements have been restated for comparative purposes to conform with this new standard.

NOTE C - Earnings Per Share

A reconciliation of the number of common shares used in the calculation of basic and diluted earnings per share ("EPS") is presented below:

Three months ended September 30,	1997		1998	
	Shares	Per-Share Amount	Shares	Per-Share Amount
Basic EPS				
Weighted-Average Shares	7,384,923	$ .11	11,028,890	($.12)
Effect of Dilutive Securities				
Stock Options	365,139		102,787	
Diluted EPS				
Weighted-Average Shares and Assumed Conversions	7,750,062	$ .11	11,131,677	($.11)

Nine months ended September 30,	1997		1998	
	Shares	Per-Share Amount	Shares	Per-Share Amount
Basic EPS				
Weighted-Average Shares	7,129,733	$ .29	10,506,189	($1.13)
Effect of Dilutive Securities				
Stock Options	350,529		213,102	
Diluted EPS				
Weighted-Average Shares and Assumed Conversions	7,480,262	$ .28	10,719,291	($1.10)

NOTE D - Inventory

Inventories consist of the following:

	DECEMBER 31, 1997	SEPTEMBER 30, 1998
Raw materials	$2,432,194	$3,182,831
Finished goods	804,827	965,134
Sales demonstration	1,038,355	1,664,702
	$4,275,376	$5,812,667

NOTE E - INTANGIBLE ASSETS

Intangible assets include patents, product design costs, and the value assigned to the work force in place in connection with the acquisition of CATS (Note A). Patents are amortized on a straight-line basis over the lives of the patents (17 years). Costs incurred in the development of products after technological feasibility is attained are capitalized and amortized using the straight-line method over the estimated economic lives of the related products, not to exceed three years. The value assigned to the work force in place in connection with the acquisition of CATS is being amortized over five years. Management evaluates the recoverability of these assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

NOTE F - PURCHASED IN-PROCESS RESEARCH AND DEVELOPMENT COSTS

In connection with the purchase of CATS (Note A), the Company obtained a valuation study from a third-party valuation/financial advisory service to assist the Company in appropriately allocating the purchase price. As a result, the Company expensed approximately $14.4 million related to in-process research and development costs in the second quarter. In-process research and development relates to technology that has not yet established technological feasibility and at present has no alternative future uses. In-process research and development was valued by discounting forecasted cash flow directly related to the products expecting to result from the research and development. Due to the development efforts required to make these products technologically feasible, management anticipates that these projects will be released over the next six months to two years at an additional cost to the Company of approximately $1.8 million.

PART I. FINANCIAL INFORMATION

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following information should be read in conjunction with the Consolidated Financial Statements of the Company, including the notes thereto, included elsewhere in this Form 10-Q, and the Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Quarterly Report on Form 10-Q dated August 12, 1998.

RESULTS OF OPERATIONS

THREE MONTHS ENDED SEPTEMBER 30, 1998 COMPARED TO THREE MONTHS ENDED SEPTEMBER 30, 1997

Sales. Sales decreased $0.9 million, or 15.3% from $5.9 million for the three months ended September 30, 1997 to $5.0 million for three months ended September 30, 1998. The decrease was primarily due to a 35.5% reduction in average sale price of the Company's traditional products from $46,000 in the third quarter of 1997 to $30,000 in the third quarter of 1998, which offset a 15.8% increase in unit sales of these products, from 114 units in the third quarter of 1997 to 132 units in the third quarter of 1998, and the addition of sales from CATS GmbH, which the company acquired on May 15,1998. The Company's price reduction was related to disposal of inventory of its traditional product line as part of a transition to a new generation product line.

Gross profit. Gross profit decreased $1.0 million, or 28.8% from $3.5 million for the three months ended September 30, 1997 to $2.5 million for the three months ended September 30, 1998. Gross margin decreased to 50.5% for the three months ended September 30, 1998, from 59.7% for the three months ended September 30, 1997. The decrease in gross profit percentage was primarily related to the unit price reduction on the Company's traditional product line as it began transition to its new generation products.

Selling expenses. Selling expenses increased $1.4 million, or 100.4%, from $1.4 million for the three months ended September 30, 1997 to $2.9 million for the three months ended September 30, 1998. This increase was a result of the Company's expansion of sales and marketing staff in the United States and Europe, the addition of the selling expenses ($428,000) from CATS, and increased promotion related to the Company's introduction of its new generation of products. Excluding CATS, the number of sales and marketing employees increased from 40 at September 30, 1997 to 60 at September 30, 1998.

General and administrative expenses. General and administrative expenses increased $541,000, or 174.6%, from $310,000 for the three months ended September 30, 1997 to $852,000 for the three months ended September 30, 1998. This increase was due to salaries for additional administration and accounting employees to support the increased sales effort, the addition of general and administrative expenses ($81,000) from CATS, and increased professional and legal expenses related to investor relations and public company reporting requirements. Excluding CATS, the number of administrative and accounting employees has increased from 13 at September 30, 1997 to 25 at September 30, 1998. Five of these new employees are in network systems, and two new employees were added to each of the accounting, total quality, and human resources departments.

Depreciation and amortization expenses. Depreciation and amortization expenses increased $321,000, or 406.1% from $79,000 for the three months ended September 30, 1997 to $400,000 for the three months ended September 30, 1998. This increase was due primarily to the amortization of the value assigned to work force in place in connection with the Company's acquisition of CATS on May 15, 1998. The value assigned to work force in place is being amortized over five years.

Research and development expenses. Research and development expenses increased $411,000, or 125.7%, from $327,000 for the three months ended September 30, 1997 to $738,000 for the three months ended September 30, 1998. This increase was a result of the Company's continued activities associated with the development of technologies related to new products, and research and development costs ($260,000) from CATS.

Interest Income. Interest income is attributable to interest on the remaining cash proceeds (approximately $20 million at September 30) from the Company's initial public offering in 1997.

Interest expense. Interest expense decreased $41,000, or 92.6% from $44,000 for the three months ended September 30, 1997 to $3,000 for the three months ended September 30, 1998. This reduction was attributable to the repayment of the Company's debt in September 1997 from use of proceeds from the Company's initial public offering, and the addition of interest expense ($3,000) from CATS.

Income Tax Expense. Income tax expense decreased $1.5 million from an expense of $573,000 for the three months ended September 30, 1997 to a benefit of $882,000 for the three months ended September 30, 1998 as a result of the net loss from operations. The provision for income taxes as a percentage of income before income tax was 40.9% for the three months ended September 30, 1998 representing estimated statutory tax rates.

Net Income. Net income decreased $2,105,000 from $829,000 for the three months ended September 30, 1997 to a loss of $1,276,000 for the three months ended September 30, 1998. The decrease was primarily due to a loss from operations in the three months ended September 30, 1998 of $2.4 million. The loss from operations is due primarily to lower gross margin resulting from a decrease in average sales price of the Company's traditional products.

NINE MONTHS ENDED SEPTEMBER 30, 1998 COMPARED TO NINE MONTHS ENDED SEPTEMBER 30, 1997

Sales. Sales increased $3.1 million, or 19.4% from $16.2 million for the first nine months of 1997 to $19.4 million for the first nine months of 1998. The increase was the result of increased product sales due to an expanded sales effort that included the addition of sales personnel at existing offices, the opening of sales offices, and the acquisition of CATS.

Gross profit. Gross profit increased $1.8 million, or 18.6%, from $9.7 million for the first nine months of 1997 to $11.5 million for the first nine months of 1998. Gross margin decreased from 59.5% for the first nine months of 1997 to 59.1% for the first nine months of 1998. Gross margin decreased as a result of sales of traditional Faro products at reduced selling prices in the third quarter, offset by higher margin software sales in the second and third quarters.

Selling expenses. Selling expenses increased $2.7 million, or 68.5%, from $4.0 million for the first nine months of 1997 to $6.7 million for the first nine months of 1998. This increase was a result of the Company's increased sales and promotion activities related to its expansion of sales and marketing staff in the United States and in Europe, including CATS. Selling expenses as a percentage of sales increased from 24.4% for the first nine months of 1997 to 34.4% for the first nine months of 1998.

General and administrative expenses. General and administrative expenses increased $1.1 million or 114.6% from $917,000 for the first nine months of 1997 to $1,967,000 for the first nine months of 1998. This increase resulted primarily from the hiring of additional administrative personnel to support staff increases in sales and marketing and increased transactional volume resulting from increased sales and increases in professional and legal expenses associated with investor relations and public reporting requirements. General and administrative expenses as a percentage of sales increased from 5.6% for the first nine months of 1997 to 10.2% for the first nine months of 1998.

Depreciation and amortization expenses. Depreciation and amortization expenses increased $568,000, or 277.0% from $205,000 for the nine months ended September 30, 1997 to $773,000 for the nine months ended September 30, 1998. This increase was due primarily to amortization of the value assigned to work force in place in connection with the Company's acquisition of CATS on May 15, 1998. The value assigned to work force in place is being amortized over five years.

Research and development expenses. Research and development expenses increased $838,000, or 116.1%, from $722,000 for the first nine months of 1997 to $1,560,000 for the first nine months of 1998. This increase was a result of the Company's continued activities associated with the development of technologies related to new products, and the addition of CATS research and development expenses ($371,000). Research and development expenses as a percentage of sales increased from 4.4% for the first nine months of 1997 to 8.0% for the first nine months of 1998.

In-process research and development resulting from acquisition. In-process research and development resulting from the acquisition of CATS represents the allocation of purchase price to products under development by CATS which had not achieved technological feasibility.

Employee stock options expenses. Employee stock options expenses decreased $236,000 or 64.6% from $365,000 for the first nine months of 1997 to $129,000 for the first nine months of 1998. The higher expense in 1997 was primarily attributable to the grant of 52,733 options in May 1997, which was made at an exercise price below the fair market value of the Common Stock on the date of the grant.

Interest Income. Interest income increased $800,000 to $839,000 for the nine months ended September 30 1998, compared to $39,000 in the nine months ended September 30 1997. The increase was attributable to interest on the remaining cash proceeds (approximately $20 million at September 30, 1998) from the Company's initial public offering in 1997.

Interest expense. Interest expense decreased $99,000, or 89.9%, from $110,000 for the first nine months of 1997 to $11,000 for the first nine months of 1998. This reduction was primarily attributable to the elimination of the Company's debt in September, 1997 from use of proceeds from the Company's initial public offering, offset by $11,000 in interest expense paid by CATS in the period since the acquisition.

Income tax expense. Income tax expense decreased $2,745,000, or 194.7%, from $1,335,000 for the first nine months of 1997 to a benefit of $1,410,000 for the first nine months of 1998. The income tax reduction was primarily a result of a tax benefit of $1.6 million resulting from the $14,374,000 charge for in-process research and development associated with the Company's acquisition of CATS on May 15, 1998, and a tax benefit of $882,000 from a $2.4 million loss from operations in the three months ended September 30, 1998.

Net Income. Net income decreased $13.9 million, from $2.1 million for the first nine months of 1997 to a loss of $11.8 million for the first nine months of 1998. The decrease was primarily due to the $14,374,000 charge for in-process research and development associated with the Company's acquisition of CATS on May 15, 1998. Exclusive of the in-process research and development charge, net income decreased $1,140,000, or 54.7%, from $2,085,000 for the nine months ended September 30, 1997 to $945,000.

LIQUIDITY AND CAPITAL RESOURCES

In September 1997, the Company completed an initial public offering of stock which provided net cash after offering expenses, of $31.8 million.

For the nine months ended September 30, 1998, net cash used in operating activities was $1,525,000 compared to $851,000 for the same period of 1997. Net cash used in this period increased as a result of decreases in net income of $13,914,000, accounts receivable of $1,882,000, unearned service revenues of $655,000, accounts payable of $354,000 and income taxes payable of $345,000 offset by increases in in-process research and development expense of $14,374,000, deferred income taxes of $1,115,000 and inventories of $1,089,000.

Net cash used in investing activities was $6,710,000 for the nine months ended September 30, 1998 compared to $509,000 for the nine months ended September 30, 1997. Net cash used in investing activities increased for the first nine months of 1998 primarily due to the acquisition of CATS for $5,306,000.

Net cash used in financing activities for the nine months ended September 30, 1998 was $55,000 compared to net cash provided by financing activities of $31.7 million for the nine months ended September 30, 1997, as a result of the initial public offering.

The Company has a loan agreement (the "Agreement") in the form of a term note and a line of credit. The Agreement combines the equivalent of three successive one-year term loans, each equal to that portion of the loan that will be fully amortized in the ensuing year, with a line of credit equal to that portion of the loan that will not be fully amortized in the ensuing year. The Company had available borrowings under the Agreement totaling approximately $2 million as of September 30, 1998. Interest accrues at the 30-day commercial paper rate plus 2.7% and is paid monthly. Borrowings under the Agreement are collateralized by the Company's accounts and notes receivable, inventory, property and equipment, intangible assets, and deposits. The Agreement contains restrictive covenants, including the maintenance of certain amounts of working capital and tangible net worth and limits on loans to related parties, and prohibits the Company from declaring dividends. There were no outstanding borrowings under this loan agreement at September 30, 1998.

In April 1997, the Company obtained a one-year secured $1.0 million line of credit which bears interest at the 30-day commercial paper rate plus 2.65% per annum. The line of credit was extended in 1998 and expires on March 31, 1999. There were no outstanding borrowings under this line of credit agreement at September 30, 1998.

The Company's principal commitments at September 30, 1998 were leases on its headquarters and regional offices, and there were no material commitments for capital expenditures at that date. The Company believes that its cash, investments, cash flows from operations and funds available from its credit facilities will be sufficient to satisfy its working capital and capital expenditure needs at least through 1998.

NEW PRODUCT LINES

On September 1, 1998, the Company announced plans to introduce a new, completely redesigned generation of its FAROArm products featuring higher accuracy and reliability at lower cost than the previous generation. The Company expected to replace the previous Bronze and Silver Series product lines with two new product lines: the Sterling Series and the Gold Series. Based on customer demand since the new product announcement, the Company has elected to retain the Silver Series product line, and position it between the lower priced Sterling Series and higher priced Gold Series lines.

To clear the way for the new product lines, the Company has sold for the quarter ended September 30, and will continue to sell for the fourth quarter its Bronze Series products at discount to reduce inventory. The Company will also continue to sell the Silver Series product line at discount to traditional price levels, to fit between the new Sterling and Gold Product lines. The Company plans to offset Silver Series product gross margin reductions from lower selling price by applying cost saving features of the new product lines to the Silver Series. This is expected to be complete for Silver Series products shipped in the second quarter of 1999.

The Company expects certain delays in shipments of Sterling and Gold Series products to customers, as a result of converting its production to the new product lines, and until it has completely supplied models of these new products to its sales force for demonstration. This is expected to be complete by December 31, 1998.

The Company expects the transition from the previous product lines to the new product lines to have material negative impact on the Company's results of operations until the third quarter of 1999.

FOREIGN EXCHANGE EXPOSURE

Sales outside the United States represent a significant portion of the Company's total revenues. Currently, the majority of the Company's revenues and expenses are invoiced and paid in U.S. dollars. In the future, the Company expects a greater portion of its revenues to be denominated in foreign currencies. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on the Company's business, results of operation and financial condition, particularly its operating margins, and could also result in exchange losses. The impact of future exchange rate fluctuations on the results of the Company's operations cannot be accurately predicted. Historically, the Company has not managed the risks associated with fluctuations in exchange rates but intends to undertake transactions to manage such risks in the future. To the extent that the percentage of the Company's non-U.S. dollar revenues derived from international sales increases in the future, the risks associated with fluctuations in foreign exchange rates will increase. The Company may use forward foreign exchange contracts with foreign currency options to hedge these risks.

IMPACT OF YEAR 2000

The Company has invested significant resources in the latest information technologies over the past five years and therefore has minimized the effect of Year 2000 issues. Management initiated a program to evaluate all computer systems and applications and determined the adjustments necessary to become Year 2000 compliant. Management is confident that existing internal resources are sufficient to correct any internal systems deficiencies that may be determined. The Company is currently making inquiries of its major suppliers and other third-party entities with which it has business relations to obtain assurances of their Year 2000 compliance. However, there can be no assurance that the systems of other companies on which the Company relies will be timely corrected, or that any failure by another company to correct such systems would not have a material adverse effect on the Company. Contingency plans are currently being developed to be implemented in the event any information technology system, non-information technology system, third party or supplier is not Year 2000 compliant in a timely manner.

The total cost to the Company of these Year 2000 Compliance activities has not been and is not anticipated to be material to its financial position or results of operations in a given year. These costs are based on Management's best estimates, which were derived utilizing numerous assumptions of future events including the continued availability of certain resources, third party modification plans, and other factors. However, there can be no guarantee that these estimates will be achieved and actual results could differ from those plans.

PART II. OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

The effective date of the Company's registration statement filed under the Securities Act in connection with its initial public offering was September 17, 1997.

From the effective date of such registration statement to September 30, 1998 none of the net proceeds from the Company's initial public offering were used for construction of plant, building and facilities; purchase and installation of machinery and equipment or the purchase of real estate. The Company used $5 million of such net proceeds to acquire CATS and $3 million as working capital.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

a) Exhibits

Exhibit No.	Description
27.1.1	Financial Data Schedule (for SEC use only)

b) Reports on Form 8-K

None

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 13, 1998

FARO TECHNOLOGIES, INC.
(Registrant)

By: /s/Gregory A. Fraser

Gregory A. Fraser
Executive Vice President and Chief Financial Officer
(Duly Authorized Officer and Principal Financial Officer)

9-MOS
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JAN-01-1998
SEP-30-1998
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