U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

☒ **QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended September 30, 2001

☐ **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 0-21221

MICROVISION, INC.

(Exact Name of Registrant as Specified in Its Charter)

Washington	**91-1600822**
(State or Other Jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

19910 North Creek Parkway, Bothell, Washington 98011-3008
(Address of Principal Executive Offices)

Issuer's telephone number, including area code: **(425) 415-6847**

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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

As of October 31, 2001, 12,995,000 shares of the Company's common stock, no par value, were outstanding.

PART I
FINANCIAL INFORMATION

Microvision, Inc.

Consolidated Balance Sheet
(In thousands)

	September 30, 2001 (Unaudited)	December 31, 2000

Assets				
Current Assets				
Cash and cash equivalents	$	11,991	$	7,307
Investment securities, available-for-sale		21,883		33,410
Accounts receivable, net of allowances of $109 and $93		884		1,033
Costs and estimated earnings in excess of billings on uncompleted contracts		1,271		2,116
Current restricted investments		-		1,125
Other current assets		2,729		976
Total current assets		38,758		45,967
Long-term investment, at cost		624		624
Property and equipment, net		8,949		7,516
Restricted investments		903		951
Receivables from related parties		2,277		1,000
Other assets		1,585		114
Total assets	$	53,096	$	56,172
Liabilities, Minority Interest and Shareholders' Equity				
Current Liabilities				
Accounts payable	$	1,616	$	1,974
Accrued liabilities		4,980		2,359
Allowance for estimated contract losses		155		295
Billings in excess of costs and estimated earnings on uncompleted contracts		60		419
Current portion of capital lease obligations		198		317
Current portion of long-term debt		56		52
Total current liabilities		7,065		5,416
Capital lease obligations, net of current portion		100		182
Long-term debt, net of current portion		247		290
Deferred rent, net of current portion		255		242
Total liabilities		7,667		6,130
Commitments and Contingencies		-		-
Minority Interest		15,952		-
Shareholders' Equity				
Common stock and paid-in capital, no par value, 31,250 shares authorized; 12,023 and 11,884 shares issued and outstanding		125,378		120,506
Deferred compensation		(3,014)		(4,378)
Subscriptions receivable from related parties		(323)		(403)
Accumulated other comprehensive income		557		454
Accumulated deficit		(93,121)		(66,137)
Total shareholders' equity		29,477		50,042
Total liabilities, minority interest and shareholders' equity	$	53,096	$	56,172

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

Microvision, Inc.

Consolidated Statement of Operations
(In thousands, except earnings per share data)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2001	**2000**	**2001**	**2000**
Revenue	$ 2,402	$ 1,971	$ 6,511	$ 5,256
Cost of revenue	1,338	1,717	3,981	4,068
Gross margin	1,064	254	2,530	1,188
Research and development expense (exclusive of non-cash compensation expense of $257 and $2 for the three months and $608 and $7 for the nine months ended September 30, 2001 and 2000, respectively)	8,479	5,732	24,489	13,851
Marketing, general and administrative expense (exclusive of non-cash compensation expense of $294 and $479 for the three months and $1,261 and $1,144 for the nine months ended September 30, 2001and 2000, respectively)	3,816	2,672	10,820	8,010
Non-cash compensation expense	551	481	1,869	1,151
Total operating expenses	12,846	8,885	37,178	23,012
Loss from operations	(11,782)	(8,631)	(34,648)	(21,824)
Interest income	553	973	1,982	2,269
Interest expense	(25)	(25)	(70)	(133)

	Three months 2001	Three months 2000	Nine months 2001	Nine months 2000
Realized gain on sale of investment securities	295	-	295	-
Loss before minority interests	(10,959)	(7,683)	(32,441)	(19,688)
Minority interests in loss of consolidated subsidiary	2,761	-	5,457	-
Net loss	$ (8,198)	$ (7,683)	$ (26,984)	$ (19,688)
Net loss per share - basic and diluted	$ (0.68)	$ (0.65)	$ (2.25)	$ (1.75)
Weighted-average shares outstanding - basic and diluted	12,010	11,828	11,967	11,276

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

Microvision, Inc.

Consolidated Statement of Comprehensive Loss
(In thousands)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2001	**2000**	**2001**	**2000**
Net loss	$ (8,198)	$ (7,683)	$ (26,984)	$ (19,688)
Other comprehensive income loss - Unrealized gain (loss) on investment securities available-for-sale:				
Unrealized holding gains arising during period	164	215	398	245
Less: reclassification adjustment for gains realized in net loss	(295)	-	(295)	-
Net unrealized gain (loss)	(131)	215	103	245
Comprehensive loss	$ (8,329)	$ (7,468)	$ (26,881)	$ (19,443)

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

Microvision, Inc.

Consolidated Statement of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30,	
	2001	**2000**
Cash flows from operating activities		
Net loss	$ (26,984)	$ (19,688)
Adjustments to reconcile net loss to net cash used in operations		
Depreciation	1,707	841
Non-cash expenses related to issuance of stock, warrants, options and amortization of deferred compensation	2,840	1,151
Minority interests in loss of consolidated subsidiary	(5,457)	-
Non-cash deferred rent	13	23
Allowance for estimated contract losses	(140)	437
Change in		
Accounts receivable	149	515
Costs and estimated earnings in excess of billings on uncompleted contracts	845	266
Other current assets	(750)	20
Receivables from related parties	(1,277)	(400)
Other assets	(58)	49
Accounts payable	(358)	(57)
Accrued liabilities	2,621	2,163
Billings in excess of costs and estimated earnings on uncompleted contracts	(359)	(7)
Net cash used in operating activities	(27,208)	(14,687)
Cash flows from investing activities		
Sales of investment securities	17,069	77,185
Purchases of investment securities	(5,439)	(80,649)
Sales of restricted investment securities	1,173	149
Purchases of restricted investment securities	-	(1,600)
Purchases of property and equipment	(3,084)	(3,725)
Net cash provided by (used in) investing activities	9,719	(8,640)

Cash flows from financing activities		
Principal payments under capital leases	(257)	(202)
Principal payments under long-term debt	(39)	(35)
Payments received on subscriptions receivable	80	173
Net proceeds from issuance of common stock	1,147	36,654
Net proceeds from sale of subsidiary's equity to minority interests	21,242	-
Net cash provided by financing activities	22,173	36,590
Net increase in cash and cash equivalents	4,684	13,263
Cash and cash equivalents at beginning of period	7,307	2,798
Cash and cash equivalents at end of period	$ 11,991	$ 16,061

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

Microvision, Inc.

Consolidated Statement of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30,	
	2001	**2000**
Supplemental disclosure of cash flow information		
Cash paid for interest	$ 70	$ 133
Supplemental schedule of non-cash investing and financing activities		
Property and equipment acquired under capital leases	$ 56	$ 348
Conversion of preferred stock to common stock	$ -	$ 1,536
Payments for exclusive license agreements by issuance of common stock	$ 971	$ 377
Issuance of subsidiary common stock under sponsored research agreement	$ 3,001	$ -
Issuance of subsidiary stock options for services rendered	$ 137	$ -
Exercise of stock options for subscriptions receivable	$ -	$ 397
Deferred compensation - warrants, options and stock grants	$ (247)	$ 8,345
Unrealized gain on investment securities, available-for-sale	$ 398	$ 245

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

MICROVISION, INC.
Notes to Consolidated Financial Statements
September 30, 2001

Management's Statement

The Consolidated Balance Sheet as of September 30, 2001, the Consolidated Statements of Operations, Cash Flows and Comprehensive Loss for the three and nine months ended September 30, 2001, and September 30, 2000 have been prepared by Microvision, Inc. (the "Company") and have not been audited. In the opinion of management, all adjustments necessary to present fairly the financial position, results of operations and cash flows at September 30, 2001 and all periods presented, have been made. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. You should read these condensed financial statements in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000. The results of operations for the three and nine months ended September 30, 2001 are not necessarily indicative of the operating results that may be attained for the entire fiscal year.

Principles of Consolidation

The consolidated financial statements of the Company include the accounts of its majority owned subsidiary Lumera Corporation ("Lumera"). All material intercompany accounts and transactions have been eliminated in consolidation.

As of September 30, 2001 Microvision owns 76% and 11% of the Common Stock and Preferred Stock, respectively of Lumera. In consolidation, Lumera's net losses were first allocated to its common shareholders until such losses exceeded its common equity and then to its preferred shareholders in proportion to their ownership interest.

Net Loss Per Share

Basic net loss per share is calculated on the basis of the weighted-average number of common shares outstanding during the reporting periods. Diluted net loss per share is calculated on the basis of the weighted-average number of common shares outstanding and taking into account the dilutive effect of all potential common stock equivalents outstanding. Diluted net loss per share for the periods ended September 30, 2001 and September 30, 2000 is equal to basic net loss per share because the effect of potential common stock equivalents outstanding during the periods, including options and warrants, is anti-dilutive.

The components of basic and diluted earnings per share were as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2001	2000	2001	2000
Numerator:				
Net loss	$ (8,198)	$ (7,683)	$ (26,984)	$ (19,688)
Denominator:				
Basic and diluted weighted-average common shares outstanding	12,010	11,828	11,967	11,276
Basic and diluted net loss per share	$ (.68)	$ (.65)	$ (2.25)	$ (1.75)

As of September 30, 2001 and 2000, the Company had outstanding options and warrants to purchase 4,157,000 and 3,430,300 shares of common stock, respectively. As of September 30, 2001 and 2000, Lumera had outstanding options and warrants to purchase 775,300 and 125,000 shares of common stock, respectively.

Equity

In March 2001, Lumera raised $21,360,000, before issuance costs, from the sale of 2,136,000 shares of mandatorily redeemable convertible preferred stock ("Preferred Stock"). In addition, Lumera issued 264,000 shares of Preferred Stock to Microvision to retire $2,640,000 of intercompany debt. The Preferred Stock is convertible to an equal number of shares of Lumera Class A Common Stock.

In February 2001, the Company issued 37,000 shares of common stock and paid $100,000 to the University of Washington as final payment for a fully paid exclusive license for the HALO technology. The total value of the payment of $1.1 million was recorded as an expense.

In January 2001, Lumera issued 802,414 shares of Lumera Class A Common Stock, valued at $3,009,000, to the University of Washington as partial consideration for a three year sponsored research agreement. The value of the shares will be amortized over the three year term of the sponsored research agreement.

Segment Information

The Company is organized into two major segments - Microvision, which is engaged in the development and manufacture of retinal scanning displays and related technologies, and Lumera, which is engaged in developing optical systems components technology. The segments were determined based on how management views and evaluates the Company's operations.

A significant portion of the segments' expenses arise from shared services that Microvision provides to the segments to realize economies of scale and to efficiently use resources. These services include centralized management, legal, accounting, human resources, real estate, management information systems, treasury and other corporate services. Expenses related to these services are allocated to the segments on a basis that the Company considers to be a reasonable reflection of the utilization of services provided to or benefits received by the segments.

The following tables reflect the results of the Company's reportable segments for the three months and nine months ended September 30, 2001. The performance of each segment is measured based on appropriate metrics. These results are used, in part, by management in evaluating the performance of, and in the allocation of resources to, each of the segments.

	Three months ended September 30, 2001			
	Microvision	Lumera	Elimination	Total
Revenues	$ 2,101	$ 301	$ -	$ 2,402
Interest income	483	111	(41)	553
Interest expense	25	41	(41)	25
Depreciation	386	244	-	630
Segment loss	7,857	3,102	(2,761)	8,198
Segment assets	42,097	17,504	(6,505)	53,096
Expenditures for capital assets	332	149	-	481

	Nine months ended September 30, 2001			
	Microvision	Lumera	Elimination	Total
Revenues	$ 6,171	$ 340	$ -	$ 6,511
Interest income	2,119	297	(434)	1,982
Interest expense	70	434	(434)	70
Depreciation	1,106	601	-	1,707
Segment loss	24,080	8,361	(5,457)	26,984
Segment assets	42,097	17,504	(6,505)	53,096
Expenditures for capital assets	1,348	1,792	-	3,140

As of September 30, 2000, there was no significant activity in the Lumera segment.

New Accounting Pronouncements

The Company adopted SFAS No. 133 "Accounting for Derivatives and Hedging Activities" in the quarter ended March 31, 2001. The adoption of this standard did not have a material impact on the Company's financial position, results of operations or cash flows.

In July 2001, the FASB issued SFAS No. 141, Business Combinations. This statement provides accounting and reporting standards for business combinations initiated subsequent to June 30, 2001. All business combinations in the scope of this statement are to be accounted for under one method, the purchase method.

In July 2001, the FASB issued SFAS No. 142, Goodwill and Other Intangible Assets. This statement provides accounting and reporting standards for intangible assets acquired individually, with a group of other assets, or as part of a business combination. This statement addresses how acquired goodwill and other intangible assets are recorded upon their acquisition as well as how they are to be accounted for after they have been initially recognized in the financial statements. Under this statement, goodwill and other intangibles with indefinite useful lives, on a prospective basis, will no longer be amortized, however will be tested for impairment at least annually, based on a fair value comparison. Intangibles which have finite useful lives will continue to be amortized over their respective useful lives. This statement also requires expanded disclosure for goodwill and other intangible assets. Microvision will be required to adopt this statement no later than January 1, 2002. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

In July 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. This statement provides accounting and reporting standards for costs associated with the retirement of long-lived assets. This statement requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the entity capitalizes a cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Adoption of this statement is required no later than January 1, 2003. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

In October 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This statement replaces SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of. FAS 144 retains the fundamental provisions of SFAS No. 121 for recognition and measurement of the impairment of long-lived assets to be held and used and for measurement of long-lived assets to be disposed of by sale. This statement applies to all long-lived assets, including discontinued operations, and replaces the provisions of APB Opinion No. 30, Reporting Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, for the disposal of segments of a business. This statement requires that those long-lived assets be measured at the lower of carrying amount of fair value less cost to sell, whether reported in continuing operations or in discontinued operations. Microvision will be required to adopt this statement no later than January 1, 2002. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

Subsequent Event

In October 2001 the Company raised $11.0 million, before issuance costs, from the sale of 971,496 shares of Microvision common stock and warrants to purchase 145,723 shares of Microvision common stock. The warrants have an exercise price of $14.62 per share and a four year term.

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

Forward-Looking Statements

The information set forth in this report in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," and Item 3, "Quantitative and Qualitative Disclosure about Market Risk," includes "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and is subject to the safe harbor created by that section. Such statements may include, but are not limited to, projections of revenues, income or loss, capital expenditures, plans for product development and cooperative arrangements, future operations, financing needs or plans of the Company, as well as assumptions relating to the foregoing. The words "believe," "expect," "anticipate," "estimate," "project," and similar expressions identify forward-looking statements, which speak only as of the date the statement was made. Certain factors that realistically could cause results to differ materially from those projected in the forward-looking statements are set forth below under the caption "Considerations Relating to the Company's Business. "

Overview

Microvision, Inc. ("Microvision" or the "Company") develops information display and related technologies that allow electronically generated images and information to be projected directly onto a viewer's retina. The Company has defined three distinct business platforms relating to the delivery of images and information:

- Retinal Scanning Displays - Utilizing the retinal scanning display technology to display information on the viewer's retina.
- Imaging Solutions – Utilizing proprietary scanning technology and the retinal scanning display technology to capture images and information.
- Optical Materials – Utilizing a new class of organic non-linear chromophore materials ("Optical Materials") technology to transmit information using light.

Retinal Scanning Displays

The Company has developed prototype retinal scanning display technology devices, including portable color and monochrome versions and full color table-top versions, and is currently refining and developing its retinal scanning display technology for potential defense, medical, industrial and consumer applications. The Company expects to commercialize its technology through the development of products and as a supplier of personal display technology to original equipment manufacturers. The Company believes the retinal scanning display technology will be useful in a variety of applications, including portable communications and visual simulations that include applications requiring the superimposing of images onto the user's field of vision. The Company expects that its retinal scanning display technology will allow for the production of highly miniaturized, lightweight, battery-operated displays that can be held or worn comfortably.

The Company's retinal scanning display technology includes proprietary technology developed by the Company, technology licensed from other companies and the Virtual Retinal Display ™ technology licensed from the University of Washington.

Imaging Solutions

The Imaging Solutions group develops products, such as bar code readers and miniature high resolution cameras, that capture images using the retinal scanning display technology and other proprietary technology. The Company believes that the basic components of the retinal scanning display system can be used to develop bar code readers and miniature high resolution cameras that have higher performance and lower cost than those currently available. The Company has developed proprietary scanner technology that it has used to build a prototype handheld bar code scanner. During 2001, the Company plans to continue to refine the design of the hand held scanner and plans to introduce a commercial version of the device in 2002.

Optical Materials

The Company formed Lumera Corporation ("Lumera") to develop and commercialize the Optical Materials technology and devices that utilize the properties of these proprietary materials. Lumera expects that the Optical Materials and devices made from Optical Materials will improve the performance and reduce the cost of electro-optic components used for fiber-optic telecommunications and data communications systems, phased-array antennas, optical computing and other photonics applications. Lumera plans to introduce its first product, an electro-optic modulator, in late 2002.

Plan of Operation

The Company plans to introduce a production version of a retinal scanning display in late 2001. To support the product introduction, the Company has produced engineering prototypes of the commercial product. These prototypes are being used by the Company's sales and marketing groups to demonstrate the technology to potential customers and to obtain customer feedback on market requirements (see "Considerations Relating to the Company's Business").

The Company intends to continue entering into strategic relationships with systems integrators and equipment manufacturers to pursue the development of commercial products incorporating the retinal scanning display technology.

In addition, the Company plans to continue to pursue, obtain and perform on development contracts. The Company expects that such contracts will further the development of the retinal scanning display technology and lead to additional commercial products. The Company also plans to invest funds for ongoing innovation and improvements to the retinal scanning display technology. These innovations and improvements include developing component technology, building additional prototypes and designing components and products for commercial production. The Company intends to continue hiring qualified sales, marketing, technical and other personnel, and to continue investing in laboratory and production facilities and equipment to achieve development and production objectives.

Lumera plans to develop optical components that offer increased speed, reduced size and cost, greater reliability, and more efficient operation than existing electro-optic component technologies. Moreover, Lumera believes that its Optical Materials technology is well suited to the manufacture of highly complex, highly integrated optical systems. The first product planned for introduction is a high-speed electro-optical ("EO") modulator that will provide a direct replacement for currently available lithium niobate modulators. The function of an EO modulator is to encode data into laser beams that carry and deliver data through optical fiber. Lumera believes its Optical Materials will overcome the fundamental limitations of materials currently used in EO modulators. A distinct market advantage of Lumera's approach is that the Optical Materials can be chemically designed to optimize performance for a specific application. Lumera believes the Optical Materials technology has potential applications in a broad range of optical networking components.

Lumera's Optical Materials technology may ultimately be sold in a variety of forms, including coated wafers, non-packaged discrete devices, non-packaged integrated devices, packaged discrete components, packaged integrated components, and intellectual property in the form of licenses, integrated cells, and other forms. Lumera's target customers include strategic technology partners, sub-system manufacturers, private label component vendors, component distributors and systems manufacturers in the telecommunications industry.

Results of Operations

THREE MONTHS ENDED SEPTEMBER 30, 2001 COMPARED TO
THREE MONTHS ENDED SEPTEMBER 30, 2000

Contract Revenue. The Company earns revenue from performance on development contracts and sales of engineering prototypes. Revenue in the three months ended September 30, 2001 increased by $400,000, or 22%, to $2.4 million from $2.0 million in the same period in 2000. For the three months ended September 30, 2001, all revenue was derived from performance on development contracts. The Company's customers include both the United States government and commercial enterprises.

The backlog of development contracts and product sales at September 30, 2001 was $7.3 million, all of which is scheduled for completion during the next twelve months.

In August 2001, Lumera entered into a $1.6 million contract with the United States government to design new Electro-optic polymer materials appropriate for the fabrication of a wideband optical modulator demonstration system.

Cost of Revenue. Cost of revenue includes both the direct and allocated indirect costs of performing on development contracts. Indirect costs include staff and related support costs associated with building the Company's technical capabilities and capacity to perform on development contracts that the Company expects to enter into in the future.

Cost of revenue for the three months ended September 30, 2001 decreased by $400,000, or 22%, to $1.3 million from $1.7 million in the same period in 2000. The decrease is attributable to lower overhead cost allocation to cost of revenue in the three months ended September 30, 2001 than in the same period in 2000. Research and development overhead is allocated to cost of revenue and research and development expense based on the relative direct labor cost incurred in cost of revenue and research and development, respectively. In addition, during the three month period ended September 30, 2000 the Company recorded a $400,000 reserve for estimated losses on uncompleted development contracts to cost of revenue.

Cost of revenue for Lumera was $100,000 for the three months ended September 30, 2001. For the three months ended September 30, 2000 there was no significant activity in the Lumera segment.

The Company expects that the cost of revenue will increase in the future. This increase will likely result from additional development contract work that the Company expects to perform and the cost of future product sales. As a percentage of revenue, the Company expects the cost of revenue to decline over time as the Company realizes economies of scale associated with higher levels of development contract business and expected future commercial product sales.

Research and Development Expense. Research and development expense consists of:

- Compensation related costs of employees and contractors engaged in internal research and development activities,
- Laboratory operations, outsourced development and processing work,
- Fees and expenses related to license acquisition, patent applications, prosecution and protection, and
- Related operating expenses.

Included in research and development expense are costs incurred in acquiring and maintaining licenses of technology from other companies. The Company has charged all costs associated with product development activity not allocable to cost of revenue to research and development expense.

Research and development expense in the three months ended September 30, 2001 increased by $2.8 million, or 48%, to $8.5 million from $5.7 million in the same period in 2000. The increase reflects continued implementation of the Company's operating plan, which calls for building technical staff and supporting activities, establishing and equipping in-house laboratories, and developing and maintaining intellectual property.

During the three months ended September 30, 2001, Lumera recognized $750,000 of expense for quarterly cash payments under the sponsored research agreement with the University of Washington. Additional equal quarterly payments are required over the three-year term of the sponsored research agreement. Research and development expense for Lumera during the three months ended September 30, 2001 was $1.8 million. During the three month period ended September 30, 2000 there was no significant activity in the Lumera segment.

The Company believes that a substantial level of continuing research and development expense will be required to develop commercial products using the retinal scanning display technology and the Optical Materials technology. Accordingly, the Company anticipates that a high level of research and development spending will continue. These expenses will be incurred as a result of:

- Hiring additional technical and support personnel,
- Expanding and equipping in-house laboratories,
- Acquiring rights to additional technologies,
- Subcontracting work to development partners, and
- Incurring related operating expenses.

The Company expects that the amount of spending on research and development will continue to grow, compared to prior years, in future periods as the Company:

- Continues development of its retinal scanning display technology,
- Develops and commercializes the Optical Materials technology,
- Prepares for the planned introduction of the Company's first commercial product in late 2001, and a second product in 2002,
- Accelerates development of microdisplays to meet emerging market opportunities,
- Incurs additional cost to develop new bar code reader technology, and
- Pursues other potential business opportunities.

Marketing, General and Administrative Expense. Marketing, general and administrative expenses include compensation and support costs for sales, marketing, management and administrative staff, and for other general and administrative costs, including legal and accounting, consultants and other operating expenses.

Marketing, general and administrative expenses in the three months ended September 30, 2001 increased by $1.1 million, or 43%, to $3.8 million from $2.7 million in the same period in 2000. The change includes increases in compensation expenses and support costs for employees and contractors. Marketing, general and administrative expense for Lumera for the three months ended September 30, 2001 was $1.2 million. During the three month period ended September 30, 2000 there was no significant activity in the Lumera segment. A significant portion of Lumera's marketing, general and administrative expenses, for the three months ended September 30, 2001, are for shared services that Microvision provides to Lumera. The Company expects marketing, general and administrative expenses to increase substantially in future periods as the Company:

- Adds to its sales and marketing staff,
- Incurs additional cost in sales and marketing activities, and
- Increases the level of corporate and administrative activity.

Non-Cash Compensation Expense. Non-cash compensation expense in the three months ended September 30, 2001 increased by $100,000 or 15% to 600,000 from $500,000 in the same period in 2000. Non-cash compensation expense includes:

- The amortization of the value of stock warrants granted to individuals who are not employees or directors of the Company,
- The amortization of the excess of fair market value over the exercise price for options issued to employees and the Board of Directors,
- The amortization of the value of stock granted to the Board of Directors, and
- The amortization of shares of Lumera common stock issued to the University of Washington under the sponsored research agreement.

Non-cash compensation expense in 2001 includes the amortization of the value of warrants issued in connection with two five-year consulting agreements that the Company entered into with two independent consultants in August 2000 to provide strategic business and financial consulting services to Microvision. Non-cash compensation expense of approximately $45,000 related to these agreements was recorded in the three months ended September 30, 2001, compared to $186,000 during the same period in 2000.

During the three months ended September 30, 2001, Lumera recognized $250,000 of expense relating to the issuance of $3.0 million of Lumera Class A Common Stock to the University of Washington pursuant to a sponsored research agreement.

Interest Income and Expense. Interest income in the three months ended September 30, 2001 decreased by $400,000, or 43%, to $600,000 from $1.0 million in the same period in 2000. This decrease resulted primarily from lower average cash and investment securities balances in the three months ended September 30, 2001 than the average cash and investment securities balances in the same period of the prior year.

Interest expense in the three months ended September 30, 2001 was consistent with the same period in 2000.

NINE MONTHS ENDED SEPTEMBER 30, 2001 COMPARED TO
NINE MONTHS ENDED SEPTEMBER 30, 2000

Contract Revenue. Revenue in the nine months ended September 30, 2001 increased by $1.2, or 24%, to $6.5 million from $5.3 million in the same period in 2000. For the nine months ended September 30, 2001, all revenue was derived from performance on development contracts.

In April 2001, the Company entered into a $4.6 million modification of its Aircrew Integrated Helmet System contract. In April 2001, the Company also entered into a $2.9 million modification of its Virtual Cockpit Optimization Program contract. The modifications fund continued improvements in helmet mounted displays being developed under the respective programs.

Cost of Revenue. Cost of revenue for the nine months ended September 30, 2001 decreased by $100,000, or 2%, to $4.0 million from $4.1 million in the same period in 2000. The decrease is attributable to lower overhead cost allocation to cost of revenue in the nine months ended September 30, 2001 than in the same period in 2000. Research and development overhead is allocated to cost of revenue and research and development expense based on the relative direct labor cost incurred in cost of revenue and research and development, respectively. In addition during the nine month period ended September 30, 2000 the Company recorded a $400,000 reserve for estimated losses on uncompleted development contracts to cost of revenue. Revenue in both the nine months ended September 30, 2001 and September 30, 2000, includes revenue for which precontract costs were recognized in the prior quarters.

Cost of Revenue for Lumera was $138,000 during the nine month period ending September 30, 2001. During the period from inception to September 30, 2000 there was no significant activity in the Lumera segment.

Research and Development Expense. Research and development expense in the nine months ended September 30, 2001 increased by $10.6 million, or 77%, to $24.5 million from $13.9 million in the same period in 2000. The increase reflects continued implementation of the Company's operating plan, which calls for building technical staff and supporting activities, establishing and equipping in-house laboratories, and developing and maintaining intellectual property.

In February 2001, the Company made the final payment on a fully paid exclusive license for the "HALO" technology from the University of Washington. This technology involves the projection of data and images onto the inside of a dome that is placed over the viewer's head. The Company issued 37,000 shares of Common Stock valued at $1.0 million and paid $100,000 to the University of Washington for the license. The total value of the final payment of $1.1 million was recorded as an expense.

In March 2001, Lumera paid $200,000 to the University of Washington for an exclusive royalty-bearing license relating to the Optical Materials technology. The payment was recorded as an expense. In addition, during the nine months ended September 30, 2001, Lumera has made three $750,000 payments to the University of Washington as quarterly payments under the sponsored research agreement. Continued quarterly payments of $750,000 are required over the remaining term of the three-year research agreement. Lumera amortized $1.8 million to expense for the cash portion of the payments under the sponsored research agreement during the nine months ended September 30, 2001. The remaining $500,000 paid to the University of Washington is recorded as a current asset at September 30, 2001.

Research and development expense for Lumera during the nine months ended September 30, 2001, including the payments under the research agreement was $5.2 million.

During the period from inception to September 30, 2000 there was no significant activity in the Lumera segment.

Marketing, General and Administrative Expense. Marketing, general and administrative expenses in the nine months ended September 30, 2001 increased by $2.8 million, or 35%, to $10.8 million from $8.0 million in the same period in 2000. The increase includes increases in compensation expenses and support costs for employees and contractors. Marketing, general and administrative expenses for Lumera during the nine months ended September 30, 2001 were $2.6 million. During the period from inception to September 30, 2000 there was no significant activity in the Lumera segment.

Non-Cash Compensation Expense. Non-cash compensation expense in the nine months ended September 30, 2001 increased by $700,000 or 62% to $1.9 million from $1.2 million in the same period in 2000.

Non-cash compensation expense in 2001 includes the amortization of the value of warrants issued in connection with two five-year consulting agreements that the Company entered into with two independent consultants in August 2000 to provide strategic business and financial consulting services. Non-cash compensation expense of approximately $600,000 related to these agreements was recorded in the nine months ended September 30, 2001 compared to $186,000 during the same period in 2000.

Lumera issued 802,414 shares of its Class A Common Stock to the University of Washington pursuant to a sponsored research agreement. The total value of the stock of $3.0 million is being amortized over the three year life of the sponsored research agreement. The total amortization expense relating to the research agreement during the nine months ended September 30, 2001 was $600,000.

Interest Income and Interest expense in the nine months ended September 30, 2001 were consistent with the same period in 2000.

Liquidity and Capital Resources

The Company has funded operations to date primarily through the sale of common stock, convertible preferred stock and, to a lesser extent, contract revenue. At September 30, 2001, the Company had $33.9 million in cash, cash equivalents and investment securities.

Cash used in operating activities totaled $27.2 million during the nine months ended September 30, 2001 compared to $14.7 million during the same period in 2000. Cash used in operating activities for each period resulted primarily from the net loss for the period.

Cash provided by investing activities totaled $9.7 million during the nine months ended September 30, 2001, compared to cash used in investing activities of $8.6 million during the same period of 2000. During the nine months ended September 30, 2001, the Company had net sales of investment securities of $11.6 million compared to net purchases of $3.5 million during the same period in 2000. The proceeds from the sales of investment securities were used to fund the Company's operations.

The Company used $3.1 million for capital expenditures during the nine months ended September 30, 2001 compared to $3.7 million during the same period in 2000. Historically, capital expenditures have been used to make leasehold improvements to leased office space and to acquire laboratory equipment, computer hardware and software, and furniture and fixtures to support growth. The Company expects capital expenditures to continue to increase substantially as the Company continues to expand operations.

Cash provided by financing activities totaled $22.2 million during the nine months ended September 30, 2001, compared to $36.6 million during the same period in 2000. During the nine months ended September 30, 2001, Lumera raised $21.4 million, before issuance costs, from the issuance of 2,136,000 shares of mandatorily redeemable convertible preferred stock.

Future operating expenditures and capital requirements will depend on numerous factors, including the following:

- The progress of research and development programs,
- The progress in commercialization activities and arrangements,
- The cost of filing, prosecuting, defending and enforcing any patent claims and other intellectual property rights,
- Competing technological and market developments, and
- The Company's ability to establish cooperative development, joint venture and licensing arrangements.

In order to maintain exclusive rights under its license agreements with the University of Washington, the Company is obligated to make royalty payments to the University of Washington. If the Company is successful in establishing OEM co-development and joint venture arrangements, the Company expects that its partners will fund a portion of non-recurring engineering costs for product development. Nevertheless, the Company expects cash requirements to increase significantly each year as the Company expands its activities and operations to commercialize its technologies.

Lumera is required to make payments of $750,000 per quarter to the University of Washington until March 2003 under the sponsored research agreement.

The Company believes that its cash, cash equivalents and investment securities balances at September 30, 2001 and the $11.0 million raised by the Company in October 2001 will satisfy its budgeted cash requirements for at least the next 12 months. Actual expenses, however, may be higher than estimated and the Company may require additional capital earlier than anticipated to:

- Accelerate the development of retinal scanning display technology and the Optical Materials technology,
- Respond to competitive pressures, or
- Meet unanticipated development difficulties.

The Company's operating plan calls for the addition of technical and business staff and the purchase of additional computer and laboratory equipment and leasehold improvements. The operating plan also provides for the development of strategic relationships with systems and equipment manufacturers. There can be no assurance that additional financing will be available to the Company or that, if available, it will be available on acceptable terms on a timely basis. If adequate funds are not available to satisfy either short-term or long-term capital requirements, the Company may be required to substantially reduce operations. The Company's capital requirements will depend on many factors, including, but not limited to, the rate at which the Company can, directly or through arrangements with OEMs, introduce products incorporating the retinal scanning display technology and the Optical Materials technology and the market acceptance and competitive position of such products.

Subsequent Event

In October 2001, the Company raised $11.0 million, before issuance costs, through the sale of 971,496 shares of Microvision common stock and warrants to purchase 145,723 shares of Microvision common stock. The warrants have an exercise price of $14.62 per share and a four year life.

New Accounting Pronouncements

In July 2001, the FASB issued SFAS No. 141, Business Combinations. This statement provides accounting and reporting standards for business combinations initiated subsequent to June 30, 2001. All business combinations in the scope of this statement are to be accounted for under one method, the purchase method.

In July 2001, the FASB issued SFAS No. 142, Goodwill and Other Intangible Assets. This statement provides accounting and reporting standards for intangible assets acquired individually, with a group of other assets, or as part of a business combination. This statement addresses how acquired goodwill and other intangible assets are recorded upon their acquisition as well as how they are to be accounted for after they have been initially recognized in the financial statements. Under this statement, goodwill and other intangibles with indefinite useful lives, on a prospective basis, will no longer be amortized, however will be tested for impairment at least annually, based on a fair value comparison. Intangibles which have finite useful lives will continue to be amortized over their respective useful lives. This statement also requires expanded disclosure for goodwill and other intangible assets. Microvision will be required to adopt this statement no later than January 1, 2002. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

In July 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. This statement provides accounting and reporting standards for costs associated with the retirement of long-lived assets. This statement requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the entity capitalizes a cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Adoption of this statement is required no later than January 1, 2003. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

In October 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This statement replaces SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of. FAS 144 retains the fundamental provisions of SFAS No. 121 for recognition and measurement of the impairment of long-lived assets to be held and used and for measurement of long-lived assets to be disposed of by sale. This statement applies to all long-lived assets, including discontinued operations, and replaces the provisions of APB Opinion No. 30, Reporting Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, for the disposal of segments of a business. This statement requires that those long-lived assets be measured at the lower of carrying amount of fair value less cost to sell, whether reported in continuing operations or in discontinued operations. Microvision will be required to adopt this statement no later than January 1, 2002. Microvision is currently assessing the impact of this statement on its results of operations, financial position and cash flows.

Considerations Relating to the Company's Business

We cannot be certain that the retinal scanning display technology or products incorporating this technology will achieve market acceptance. If the retinal scanning display technology does not achieve market acceptance, our revenues may not grow.

Our success will depend in part on the commercial acceptance of the retinal scanning display technology. The retinal scanning display technology may not be accepted by manufacturers who use display technologies in their products or by consumers of these products. To be accepted, the retinal scanning display technology must meet the expectations of our potential customers in the defense, medical, industrial and consumer markets. If our technology fails to achieve market acceptance, we may not be able to continue to develop the retinal scanning display technology.

Our lack of the financial and technical resources relative to our competitors may reduce our revenues, potential profits and overall market share.

The retinal scanning display and products that may incorporate this technology will compete with established manufacturers of miniaturized cathode ray tube and flat panel display devices, many of which have substantially greater financial, technical and other resources than us and many of which are also developing miniature displays. Because of their greater resources, our competitors may develop products or technologies that are superior to our own. The introduction of superior competing products or technologies could result in reduced revenues, lower margins or loss of market share, any of which could reduce the value of our business.

We may not be able to keep up with rapid technological change and our financial results may suffer.

The electronic information display industry and the optical switching industries have been characterized by rapidly changing technology, accelerated product obsolescence and continuously evolving industry standards. Our success will depend upon our ability to further develop the retinal scanning display technology, the Optical Materials technology and to introduce new products and features on a cost effective basis in a timely manner to meet evolving customer requirements and compete effectively with competitors' product advances. We may not succeed in these efforts because of:

- delays in product development,
- lack of market acceptance for our products, or
- lack of funds to invest in development.

The occurrence of any of the above factors could result in decreased revenues and market share.

Our products may be subject to future health and safety regulations that could increase our development and production costs.

Products incorporating retinal scanning display technology could become subject to new health and safety regulations that would reduce our ability to commercialize the retinal scanning display technology. Compliance with any such new regulations would likely increase our cost to develop and produce products using the retinal scanning display technology and adversely affect our financial results.

If we experience delays or failures in developing and producing commercially viable products, we may have lower revenues.

Although we have developed prototype products incorporating the retinal scanning display technology and prototype devices have been built using the Optical Materials technology, we must undertake additional research, development and testing before we are able to produce products for commercial sale. In addition, product development delays or the inability to enter into relationships with potential product development partners may delay or prevent us from introducing commercial products.

If we are unable to adequately protect our patents and other proprietary technology, we may be unable to compete with other companies.

Our success will depend in part on our ability and the ability of the University of Washington and our other licensors to maintain the proprietary nature of the retinal scanning display and related technologies. We also rely on proprietary Optical Materials technology licensed from the University of Washington. Although our licensors have patented various aspects of the retinal scanning display technology and applied for patents on various aspects of Optical Materials technology and, although we continue to file our own patent applications covering retinal scanning display features, Optical Materials technology and related technologies, we cannot be certain as to the degree of protection offered by these patents or as to the likelihood that patents will be issued from the pending patent applications. Moreover, these patents may have limited commercial value or may lack sufficient breadth to protect adequately the aspects of our technology to which the patents relate. We cannot be certain that our competitors, many of whom have substantially greater resources than us and have made substantial investments in competing technologies, will not apply for and obtain patents that will prevent, limit or interfere with our ability to make and sell our products.

We also rely on unpatented proprietary technology. Third parties could develop the same or similar technology or otherwise obtain access to our proprietary technology. We cannot be certain that we will be able to adequately protect our trade secrets, know–how or other proprietary information or prevent the unauthorized use, misappropriation or disclosure of such trade secrets, know–how or other proprietary information.

We could face lawsuits related to our use of the retinal scanning display technology. These suits could be costly, time consuming and reduce our revenues.

We are aware of several patents held by third parties that relate to certain aspects of retinal scanning displays. These patents could be used as a basis to challenge the validity of the University of Washington's patents, to limit the scope of the University of Washington's patent rights or to limit the University of Washington's ability to obtain additional or broader patent rights. A successful challenge to the validity of the University of Washington's patents could limit our ability to commercialize the retinal scanning display technology and, consequently, materially reduce our revenues. Moreover, we cannot be certain that patent holders or other third parties will not claim infringement by us or by the University of Washington with respect to current and future technology. Because U.S. patent applications are held and examined in secrecy, it is also possible that presently pending U.S. applications will eventually be issued with claims that will be infringed by our products or the retinal scanning display technology. The defense and prosecution of a patent suit would be costly and time–consuming, even if the outcome were ultimately favorable to us. An adverse outcome in the defense of a patent suit could subject us to significant cost, require others and us to cease selling products that incorporate retinal scanning display technology, or to cease licensing the retinal scanning display technology, or to require disputed rights to be licensed from third parties. Such licenses would increase our cost or may not be available at all. Moreover, if claims of infringement are asserted against our future co–development partners or customers, those partners or customers may seek indemnification from us for damages or expenses they incur.

Our revenues are highly sensitive to developments in the defense and aerospace industries.

Our revenues to date have been derived principally from product development research relating to defense applications of the retinal scanning display technology. We believe that development programs and sales of potential products in this market will represent a significant portion of our future revenues. Developments that adversely affect the defense sector, including delays in government funding and a general economic downturn, could cause our revenues to decline substantially.

If we cannot supply products in commercial quantities, we will not achieve commercial success.

We currently lack the capability to manufacture products in commercial quantities. Our success depends in part on our ability to provide our components and future products in commercial quantities at competitive prices. Accordingly, we will be required to obtain access, through business partners or contract manufacturers, to manufacturing capacity and processes for the commercial production of our expected future products. We cannot be certain that we will successfully obtain access to sufficient manufacturing resources. Future manufacturing limitations of our suppliers could result in a limitation on the number of products incorporating our technology that we are able to produce.

If we cannot manufacture products at competitive prices, our financial results will be adversely affected.

To date, we have produced only prototype products for research, development and demonstration purposes. The cost per unit for these prototypes currently exceeds the level at which we could expect to profitably sell commercial versions of these products to customers. If we cannot lower our cost of production, we may face increased demands on our financial resources, possibly requiring additional equity and/or debt financing to sustain our business operations.

If we lose the exclusive use of the Virtual Retinal Display technology or the Optical Materials technology, our business operations and prospects would be adversely affected.

We acquired the exclusive rights to the Virtual Retinal Display technology and the Optical Materials technology under exclusive license agreements with the University of Washington. If the University of Washington were to violate the terms of the license agreements by providing the technology to another company, our business, operations and prospects would be adversely affected. In addition, we could lose the exclusivity under the license agreement if we fail to challenge, within the designated time limits, claims that other companies are using the Virtual Retinal Display technology in violation of our license agreements.

We need to collaborate with third parties to be able to successfully develop products for commercial sale.

Our strategy for developing, testing, manufacturing and commercializing the retinal scanning display technology and products incorporating the retinal scanning display technology includes entering into cooperative development, sales and marketing arrangements with corporate partners, OEMs and other third parties. We cannot be certain that we will be able to negotiate arrangements on acceptable terms, if at all, or that these arrangements will be successful in yielding commercially viable products. If we cannot establish these arrangements, we would require additional capital to undertake such activities on our own and would require extensive manufacturing, sales and marketing expertise that we do not currently possess and that may be difficult to obtain. In addition, we could encounter significant delays in introducing the retinal scanning display technology or find that the development, manufacture or sale of products incorporating the retinal scanning display technology would not be feasible. To the extent that we enter into cooperative development, sales and marketing or other joint venture arrangements, our revenues will depend upon the efforts of third parties. We cannot be certain that any such arrangements will be successful.

We may require additional capital to continue implementing our business plan. This may lessen the value of current stockholders' shares.

We may need additional funds in order to, among other requirements,

- Further develop retinal scanning display technology and Optical Materials technology,
- Add manufacturing capacity,
- Add to our sales and marketing staff,
- Develop and protect our intellectual property rights, or
- Fund long-term business development opportunities.

We cannot be certain that we will be able to obtain financing when needed or that we will be able to obtain financing on satisfactory terms, if at all. If additional funds are raised through the issuance of equity, convertible debt or similar securities, current shareholders will experience dilution and the securities issued to the new investors may have rights or preferences senior to those of the shareholders of common stock. Moreover, if adequate funds were not available to satisfy our short–term or long–term financial needs, we would be required to limit our operations significantly.

Loss of any of our key personnel could have a negative effect on the operation of our business.

Our success depends on our officers and other key personnel and on the ability to attract and retain qualified new personnel. Achievement of our business objectives will require substantial additional expertise in the areas of sales and marketing, research and development, and manufacturing. Competition for qualified personnel in these fields is intense, and the inability to attract and retain additional highly skilled personnel, or the loss of key personnel, could reduce our revenues and adversely affect our business.

We have a history of operating losses and expect to incur significant losses in the future.

We have had substantial losses since our inception and our operating losses may increase in the future. Accordingly, we cannot assure you that we will ever become or remain profitable.

- As of September 30, 2001, we had an accumulated deficit of $93.1 million
- We incurred net losses of $22.8 million from inception through 1998, $16.7 million in 1999, $26.6 million in 2000, and $27.0 million during the nine months ended September 30, 2001.

Our revenues to date have been generated from development contracts and sales of engineering prototype units. We do not expect to generate significant revenues from product sales in 2001, and possibly thereafter. The likelihood of our success must be considered in light of the expenses, difficulties and delays frequently encountered by companies formed to develop and market new technologies. In particular, our operations to date have focused primarily on research and development of the retinal scanning display technology and development of prototypes. We are unable to accurately estimate future revenues and operating expenses based upon historical performance.

We cannot be certain that we will succeed in obtaining additional development contracts or that we will be able to obtain customer orders for products incorporating the retinal scanning display technology. In light of these factors, we expect to continue to incur substantial losses and negative cash flow at least through 2002 and likely thereafter. We cannot be certain that we will become profitable or achieve positive cash flow at any time in the future.

A substantial number of our shares may be sold into the market in the near future, which could cause the market price of our common stock to drop significantly.

As of October 31, 2001, we had outstanding:

- Options to purchase an aggregate of 5,044,000 shares of Microvision common stock, and
- Warrants to purchase 615,000 shares of Microvision common stock.

Sales in the public market of common stock issuable upon exercises of stock options or warrants could depress prevailing market prices for our common stock. Even the perception that such sales could occur may adversely impact the market price for our stock. A decrease in market price would decrease the value of an investment in our common stock.

Our quarterly performance may vary substantially and this variance may decrease our stock price.

Our revenues to date have been generated from a limited number of development contracts with U.S. government entities and commercial partners. Our quarterly operating results may vary significantly based on:

- Reductions or delays in funding of development programs involving new information display technologies by the U.S. government or our current or prospective commercial partners, or
- The status of particular development programs and the timing of performance under specific development agreements.

In one or more future quarters, our results of operations may fall below the expectations of securities analysts and investors and the trading price of our common stock may decline as a consequence.

If we fail to manage expansion effectively, our revenue and expenses could be adversely affected.

Our ability to successfully offer products and implement our business plan in a rapidly evolving market requires an effective planning and management process. We have significantly expanded the scope of our operations. In addition, we plan to continue to hire a significant number of employees during the next twelve months. The growth in business, head count and relationships with customers and other third parties has placed and will continue to place a significant strain on our management systems and resources. We will need to continue to improve our financial and managerial controls, reporting systems and procedures and will need to continue to expand, train and manage our work force.

It may be difficult for a third party to acquire the Company and this could depress our stock price.

Certain provisions of Washington law and our amended and restated articles of incorporation and bylaws contain provisions that create burdens and delays when someone attempts to purchase our Company. As a result, these provisions could limit the price that investors are willing to pay for our stock. These provisions:

- Authorize our board of directors, without further shareholder approval, to issue preferred stock that has rights superior to those of the common stock. Potential purchasers may pay less for our Company because the preferred stockholders may use their rights to take value from the Company, and
- Provide that written demand of at least 30% of the outstanding capital shares is required to call a special meeting of the shareholders, which may be needed to approve the sale of the Company. The delay that this creates could deter a potential purchaser.

Additional risks associated with the Lumera business.

We cannot be certain that our Optical Materials will achieve market acceptance.

Lumera's success will depend in part on the commercial acceptance of the Optical Materials. The optical switching industry is currently fragmented with many competitors developing different technologies. We expect that only a few of these technologies ultimately will gain market acceptance. The Optical Materials may not be accepted by OEMs and systems integrators of optical switching networks. To be accepted, the Optical Material must meet the technical and performance requirements of our potential customers in the telecommunications industry. If our Optical Materials technology fails to achieve market acceptance, we may not be able to continue to develop the technology.

Our lack of the financial and technical resources relative to our competitors may affect our ability to commercialize the Optical Materials.

The optical switching market is a highly competitive market. Many companies, with substantially greater financial, technical and other resources than us, are working on competing technologies. Because of their greater resources, our competitors may develop products or technologies that are superior to our own. The introduction of superior competing products or technology could cause our Optical Materials technology not to become commercially viable, which could reduce the value of our business.

Lumera's revenues are highly sensitive to developments in the telecommunications industry.

Lumera's expected revenues will be derived from product sales to OEMs and system integrators in the telecommunications industry. We believe that sales of potential products in the telecommunications market could represent a significant portion of our future revenues. Developments that adversely affect the telecommunications sector, including delays or reductions in infrastructure investments, delays in traffic growth, government regulation or a general economic downturn, could slow or halt our revenue growth.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Substantially all of the Company's cash equivalents and investment securities are at fixed interest rates and, as such, the fair value of these instruments is affected by changes in market interest rates. Due to the generally short-term maturities of these investment securities, the Company believes that the market risk arising from its holdings of these financial instruments is not material. A one hundred basis point change in market interest rates would have approximately a $200,000 impact on the fair value of the investment securities.

Presently, all of the Company's development contract payments are made in U.S. dollars and, consequently, the Company believes it has no foreign currency exchange rate risk. However, in the future the Company may enter into development contracts or product sales contracts in foreign currencies, which may subject the Company to foreign exchange rate risk. The Company does not have any derivative instruments and does not presently engage in hedging transactions.

The maturities of cash equivalents and investment securities, available-for-sale, as of September 30, 2001, are as follows.

	Amount (in thousands)	Percent
Cash	$ 1,617	4.8 %
Less than one year	18,766	55.4 %
One to two years	10,482	30.9 %
Two to three years	3,009	8.9 %
	$ 33,874	100.0 %

Part II
OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

On August 8, 2001, the Company issued 3,000 shares of common stock to a warrant holder upon an exercise of a warrant. The Company received cash consideration of $37,500 in connection with the transaction. This transaction was exempt from registration under the Securities Act pursuant to Section 4(2) thereof as a transaction not involving a public offering.

ITEM 6. Exhibits

(a.) Exhibits

4.1 Form of Indenture (1)

(1) Incorporated by reference to the Registration Statement on Form S-3, Reg. No. 333-69652.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MICROVISION, INC.

Date: November 9, 2001

/s/ Richard F. Rutkowski
Richard F. Rutkowski
President, Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2001

/s/ Jeff Wilson
Jeff Wilson
Controller
(Principal Accounting Officer)

EXHIBIT INDEX

The following documents are filed herewith or have been included as exhibits to previous filings with the Securities and Exchange Commission and are incorporated by reference as indicated below.

Exhibit Number	Description