2007 Annual Report

HERE.

Cepheid®
Bring answers to life.

This annual report contains forward-looking statements that are not purely historical regarding Cepheid's or its management's intentions, beliefs, expectations and strategies for the future, including those relating to: future products; development activities; future regulatory approvals; product performance; and business prospects. Because such statements deal with future events, they are subject to various risks and uncertainties, and actual results could differ materially from Cepheid's current expectations. Factors that could cause actual results to differ materially include risks and uncertainties such as those relating to: unforeseen research, development and manufacturing problems, which could delay the introduction of new products; unforeseen manufacturing costs; the need for additional licenses for new tests and other products and the terms of such licenses; our ability to successfully obtain regulatory approvals, including the success of any required clinical testing, and introduce new products in the clinical market; the performance and market acceptance of new products; our reliance on distributors to market and sell our products; the fact that our collaborative relationships may not result in successful introduction of new products or result in material revenues, including for many of the reasons noted above; the impact of competitive products and pricing; and underlying market conditions worldwide. Readers should also refer to the section entitled "Risk Factors" in Cepheid's Annual Report on Form 10-K for 2007 as filed with the Securities and Exchange Commission. All forward-looking statements and reasons why results might differ are made as of the date of this report, based on information currently available to Cepheid, and Cepheid assumes no obligation to update any such forward-looking statement or reasons why results might differ.

HERE.

Is where we imagined a molecular diagnostic revolution that could alter healthcare forever.

After more than a decade Cepheid stands alone upon the on-demand molecular diagnostic landscape — holding fast to its original vision of medical innovation that combines molecular diagnostics with treatment-altering test results. Years ago, that broad and sweeping vision included plans for a paradigm-shifting platform that could not only simplify molecular testing for the lab, but bring the power of molecular testing closer to the patient. That platform needed to sync with the way patients are admitted and treated in healthcare institutions, with the flexibility to immediately test one or many — 24 hours a day, 7 days a week. That vision became the GeneXpert® System, and it is here.

HERE.

Is where we saw a world connected by the common need for rapid answers.

A common thread that binds us all is the continual need for answers. Nowhere is that need more critical than in today's healthcare setting. Whether it's expectant parents, a patient being prepped for surgery, or a concerned mother with a sick child, the question we all want answered is, "Will everything be OK?" During 2007, Cepheid's vision for rapid answers that can aid physicians in making critical patient management decisions was expanded with the FDA clearance of both Xpert™ EV and Xpert MRSA. But this is just the beginning, as a full pipeline of important tests is scheduled to unfold within the next five years. In addition to expanding our healthcare associated infection portfolio, the pipeline includes key products in the areas of women's health, critical infectious disease, immuno-compromised, genetic disease and oncology. The age of on-demand answers, of rapid molecular diagnostics, is here.

HERE.

Is where we envisioned a diverse landscape changed by a single solution.

Nearly 500 GeneXpert® Systems, comprised of more than 2,500 modules, were placed worldwide during 2007 — and the demand continues to grow. With the expected GeneXpert Infinity Systems and CLIA waived testing on the horizon, Cepheid's GeneXpert System is becoming even more flexible. With the capability for large patient population testing in a hospital core lab, or single patient testing in a small nursing home, the GeneXpert System is expected to standardize on-demand molecular testing across all settings. By expanding the reach of the lab and moving testing closer to the patient, the future of molecular testing is here.

HERE.

Is where we are rewarded by a vision that is changing the lives of many.

More important than the successes we achieved during 2007 are how those successes will affect each and every one of us. Cepheid's achievements will continue to have monumental impact upon the way our healthcare system connects us to the answers we need. Answers that will help us live longer, healthier and more rewarding lives. That time is here.

HERE.

Is where we see answers being brought to life.

Today, we are witnessing a paradigm shift in the way patients are tested and treated. Cepheid's products are accelerating time-to-result, empowering healthcare professionals with the answers to more effectively manage an individual's well being. This is your time. This is our time. Together we are changing the world of molecular diagnostics.

HERE.

Is where we are.

Cepheid Product Sales
($ millions)

Dear Fellow Shareholders,

2007 was a breakout year for Cepheid as we fully crossed over from a company predominately driven by Biothreat product sales to a company driven by Clinical product sales. 52% of our product sales in 2007 were from the Clinical market as compared to 24% in 2006. Biothreat sales were 35% of total product sales in 2007 versus 58% in 2006 and Industrial sales were 13% of the total product sales in 2007 versus 18% in 2006. Our annual revenues grew to $129.5 million in 2007. Top line sales growth for 2007 was driven by the developing market for MRSA surveillance and the introduction of our Xpert™ MRSA test in the U.S. last April. The transition to the Clinical market offers a substantially larger, higher-growth and higher-margin opportunity compared to the Industrial and Biothreat market segments.

As of December 31, 2007, we had installed 2,569 GeneXpert® diagnostic modules in 483 GeneXpert Systems in the U.S. and Europe. This is an increase of 1,583 modules and 231 systems compared to the end of the second quarter of 2007 when our Xpert MRSA test was approved for the U.S. market.

The Veterans Administration (VA) required that hospitals within its network implement MRSA screening procedures during 2007 to aid in the reduction of infection rates. Even though our Xpert MRSA product wasn't FDA cleared for market launch until April of 2007, we were still able to secure 4 out of 5 accounts desiring to do molecular testing within the VA network. This is a testament to the added value our customers recognize in the GeneXpert System.

While the early success of our MRSA business was driven by the VA market opportunity, general hospital adoption outside of the VA hospital system drove our MRSA business at the end of 2007 and into 2008. As of the end of the fourth quarter, general hospital accounts comprised 52% of our MRSA accounts.

Looking ahead in 2008, our success will be measured on three fronts. First, through commercial operations with the continued market adoption of the GeneXpert System, and increased test cartridge utilization. Second, through R&D with the expansion of our clinical test menu in the Healthcare Associated Infection (HAI) market, along with the expected release of our first genetic market test for the evaluation of coagulation Factor II and Factor V. We also expect to expand the scope of our GeneXpert System offering with the initiation of shipment of our high throughput GeneXpert Infinity-48 System. Third, we expect to realize an increase in the percentage of gross profit margin earned on product sales.

Growth of the HAI market continues to be driven in part by state and national legislation including mandatory reporting of hospital rates of infection and mandated MRSA surveillance testing. Four states have already enacted legislation mandating active MRSA surveillance of all high-risk patients entering hospitals and there is similar legislation at various stages of development in an additional seven states and the District of Columbia. Legislation was introduced on a national level this past December that included provisions for near-term implementation of mandated surveillance in all acute care hospitals for high risk patients and surveillance of all acute care hospital admissions by 2012.

We plan to offer the most robust platform and menu of tests for HAI in the industry. We plan to release our *Clostridium difficile* and Vancomycin resistant enterococci (VRE) tests in Europe as CE marked products at the end of 2008 and in the U.S. following FDA clearance in 2009. These two infections pose an additional substantial threat to our healthcare system, and in some parts of the world *C. difficile* infections have already surpassed MRSA as a serious health issue.

We expect to further expand our MRSA testing portfolio. In 2008, we expect FDA clearance of our MRSA/SA/*mecA* combination products for blood culture bottles as well as for skin and soft tissue infections for the diagnosis of symptomatic patients. We have also expanded our development plans to include a nasal specimen application of our MRSA/SA/*mecA* test for pre-surgical testing. This product is also expected to be released in Europe as a CE marked product by the end of 2008 and in the U.S. following FDA clearance in 2009.

Work is also continuing on the potential 2009 release of a CLIA waived product for MRSA surveillance, which will extend the market to U.S. nursing home testing. As an additional note, we will also be improving our existing MRSA surveillance product, which is currently on the market in the U.S. and Europe, reducing the time-to-result to approximately 50 minutes from the current time-to-result of approximately 70 minutes. This improvement is expected to be implemented before the end of 2008.

> "We plan to offer the most robust platform and menu of tests for healthcare associated infections in the industry."

The scalability of the GeneXpert System is proving to be a significant benefit as it allows accounts to easily configure the system to meet their current high volume or low volume needs — as well as having the ability to further increase the capacity of their system at their discretion. Presently, accounts can configure their GeneXpert Systems with anywhere from one to 16 modules per system. With the introduction of our new GeneXpert Infinity Systems, accounts will have the ability to configure systems with up to 72 modules. In addition to its high throughput capability, the GeneXpert Infinity Systems will have true random access capability enabling the user to run up to 48 or 72 different tests simultaneously, depending on system configuration.

We expect 2008 to be another significant year of achievement for Cepheid. Based on the strong market adoption we are seeing in our GeneXpert Systems and associated Xpert tests, we expect continued revenue growth in 2008 driving us to profitability, excluding stock option expenses.

I thank you, our shareholders, for your commitment to our endeavors to improve the efficiency of clinical molecular lab testing and to place molecular diagnostics in the hands of the healthcare professionals, closer to the patient, to make rapid on-demand treatment decisions. This undertaking is just beginning to unfold, and we are looking ahead to expanding our reach to additional clinical care settings.

Thank you for your continued support.

John L. Bishop
Chief Executive Officer

March 2008

SELECTED FINANCIAL DATA

YEAR ENDED DECEMBER 31,

Consolidated Statements of Operations (in thousands, except per share data)	2007	2006	2005
Revenues			
Product sales	$ 116,532	$ 82,403	$ 80,440
Other revenue	12,941	4,949	4,570
Total revenues	129,473	87,352	85,010
Cost and operating expenses:			
Cost of product sales	69,174	48,800	46,232
Collaboration profit sharing	12,256	14,974	14,483
Research and development	31,449	23,886	18,961
In-process research and development	—	139	—
Selling, general and administrative	41,081	26,470	18,901
Expense for patent related matter	—	3,350	—
Total costs and operating expenses	153,960	117,619	98,577
Loss from operations	(24,487)	(30,267)	(13,567)
Other income (expense), net	3,277	4,282	(27)
Net loss before provision for income taxes	(21,210)	(25,985)	(13,594)
Provision for income taxes	(213)	—	—
Net loss	$ (21,423)	$ (25,985)	$ (13,594)
Basic and diluted net loss per share	$ (0.39)	$ (0.50)	$ (0.32)
Shares used in computing basic and diluted net loss per share	55,263	52,325	42,494

AS OF DECEMBER 31,

Balance Sheet Information (in thousands)	2007	2006	2005
Cash, cash equivalents and marketable securities	$ 44,026	$ 94,936	$ 37,222
Working capital	56,109	90,362	19,561
Total assets	165,245	167,661	103,188
Long-term obligations	2	44	2,439
Accumulated deficit	(154,909)	(133,486)	(107,501)
Total shareholders' equity	126,935	132,706	55,403

FORM 10-K IS HERE.

TODAY.

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

Form 10-K

(Mark One)

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

For the fiscal year ended December 31, 2007

or

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

For the transition period from to

Commission file number 000-0030755

CEPHEID
(Exact name of Registrant as Specified in its Charter)

California *(State or Other Jurisdiction of Incorporation or Organization)*	**77-0441625** *(I.R.S. Employer Identification Number)*
904 Caribbean Drive, Sunnyvale, California *(Address of Principal Executive Office)*	**94089-1189** *(Zip Code)*

(408) 541-4191
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, no par value and the associated Stock Purchase Rights
(Title of Class)

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer ☑ Accelerated Filer ☐ Non-accelerated Filer ☐ Smaller Reporting Company ☐
(Do not check if a Smaller Reporting Company)

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

As of June 29, 2007, the last business day of the Registrant's most recently completed second fiscal quarter, the aggregate market value of the common stock held by non-affiliates of the registrant was approximately $787,152,853 based on the closing sale price for the registrant's common stock on the NASDAQ Global Market on that date of $14.60 per share. For purposes of determining this number, all executive officers and directors of the registrant are considered to be affiliates of the registrant, as well as individual shareholders holding more than 10% of the registrant's outstanding common stock. This number is provided only for the purpose of this report on Form 10-K and does not represent an admission by either the registrant or any such person as to the status of such person.

As of February 15, 2008 there were 55,855,136 shares of the registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Document Description	10-K Part
Portions of the Proxy Statement for the Annual Meeting of Stockholders (the "Proxy Statement") to be held on April 24, 2008, and to be filed pursuant to Regulation 14A within 120 days after registrant's fiscal year ended December 31, 2007 are incorporated by reference into Part III of this Report.	III

2007 ANNUAL REPORT ON FORM 10-K

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FORWARD-LOOKING STATEMENTS

The following discussion of our business, and other parts of this report, contain forward-looking statements that are based upon current expectations. These statements are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. In some cases, you can identify forward-looking statements by terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "intend", "potential" or "continue" or the negative of these terms or other comparable terminology. Forward-looking statements involve risks and uncertainties. Our actual results and the timing of events could differ materially from those anticipated in our forward-looking statements as a result of many factors, including, but not limited to, the following: unforeseen development and manufacturing problems; the need for additional licenses for new tests and other products and the terms of such licenses; lengthy sales cycles in certain markets; the performance and market acceptance of our new products; our ability to obtain regulatory approvals and introduce new products into the Clinical Molecular Diagnostic market; our ability to successfully sell products in the Clinical Molecular Diagnostic market; our reliance on distributors to market, sell and support our products; the occurrence of unforeseen expenditures, acquisitions or other transactions; our ability to integrate the businesses, technologies, operations and personnel of acquired companies; the scope and timing of actual United States Postal Service ("USPS") funding of the Biohazard Detection System ("BDS"); the rate of environmental testing using the BDS conducted by the USPS, which will affect the amount of consumable products sold; our success in increasing our direct sales; the impact of competitive products and pricing; our ability to manage geographically-dispersed operations; underlying market conditions worldwide and the other risks set forth under "Risk Factors" and elsewhere in this report, and we can not guarantee future results, levels of activity, performance or achievements. We assume no obligation to update any of the forward-looking statements after the date of this report or to conform these forward-looking statements to actual results.

PART I

ITEM 1. BUSINESS

OVERVIEW

We are a broad based molecular diagnostics company that develops, manufactures, and markets fully-integrated systems for genetic testing in the Clinical Molecular Diagnostic, Industrial and Biothreat markets. Our systems enable rapid, sophisticated molecular testing for organisms and genetic-based diseases by automating otherwise complex manual laboratory procedures. Molecular testing involves a number of complicated and time-intensive steps, including sample preparation, DNA amplification and detection. Our easy-to-use systems integrate these steps and analyze complex biological samples in our proprietary test cartridges. We are currently the only company to have obtained Clinical Laboratory Improvement Amendments moderate complexity categorization for an amplified molecular test system and an associated specific infectious disease test on the market in the United States. Our efforts are currently focused on those applications where rapid molecular testing is particularly important, such as identifying infectious diseases and cancer in the Clinical Molecular Diagnostic market; food, agricultural and environmental testing in the Industrial market; and identifying bio-terrorism agents in the Biothreat market.

Our two principal system platforms are the SmartCycler and GeneXpert systems. The SmartCycler system integrates DNA amplification and detection to allow rapid analysis of a sample. The GeneXpert system integrates sample preparation in addition to DNA amplification and detection. The GeneXpert system is designed for a broad range of user types ranging from reference laboratories and hospital central laboratories to satellite testing locations, such as emergency departments and intensive care units within hospitals, and doctors' offices.

The GeneXpert system represents a paradigm shift in the automation of molecular analysis, producing accurate results in a timely manner with minimal risk of contamination. Our GeneXpert system can provide rapid results with superior test specificity and sensitivity over comparable systems on the market today that are integrated but have open architectures.

We currently have available a relatively broad menu of tests and reagents for use on our respective systems. Our reagents and tests are marketed along with our systems on a worldwide basis.

Sales for products within our specific markets are conducted through both direct sales and distribution channels worldwide. Clinical Molecular Diagnostic market sales in the United States are handled primarily on a direct basis, while sales in all markets for Europe and our markets in the rest of the world are handled on both a direct and distributor basis. Our marketing programs are managed on a direct basis.

OUR STRATEGY

Our strategy is to become the leading supplier of integrated systems and tests for genetic assessment in a variety of environments. Key elements of our strategy to achieve this objective include:

- *Provide a fully-integrated molecular testing solution to the Clinical Molecular Diagnostic market.* We believe our GeneXpert system will enable us to significantly expand our presence in the Clinical Molecular Diagnostic market, because we believe this system is currently the only closed, self-contained, fully-integrated and automated system for molecular testing commercially available. The GeneXpert system will allow healthcare providers to obtain timely, accurate results from a raw biological sample, with minimal risk of contamination. The system is currently available in a variety of configurations ranging from 1 to 16 individual test modules. To our knowledge, the system is also the only currently available system to offer true random access and on demand test capability. Additional configurations of the system are under development for high volume test requirements.

- *Obtain additional target rights.* We expect to continue to expand our collaborations with academic institutions to develop and obtain target rights to various infectious disease and cancer targets. In addition, we will be focusing key business development activities on identifying infectious disease and cancer targets held by academic institutions or commercial operations for potential license or acquisition.

- *Continue to develop and market new tests.* We plan to capitalize on our strengths in nucleic acid chemistry and molecular biology to internally develop new tests for our GeneXpert and SmartCycler systems. In addition, in order to more rapidly expand our test pipeline, we are working and expect to continue to expand collaborations with strategic partners and major academic medical centers to co-develop and validate additional tests

- *Enhance international platform.* Internationally we are currently primarily focused on developing the European Clinical Molecular Diagnostic market. However, we also have and are developing programs for the markets in Japan and the rest of the world. We conduct our European sales and marketing operations through our French subsidiary, Cepheid SA, which has a facility, sales and customer support personnel and an established European distribution network. We will continue to expand our distribution capability in Europe on both a direct and distributor basis. In addition, we intend to expand in other international markets.

- *Continue to maintain applications in the Industrial and Biothreat markets.* We currently sell products into the Industrial and Biothreat markets and expect to continue our offerings in these markets.

PRODUCTS

Our product portfolio consists of tests, reagents and instrument systems for the Clinical Molecular Diagnostic, Industrial, and Biothreat markets. Our two main systems are the SmartCycler, which is a system that integrates DNA amplification and detection for rapid batch or random access analysis in "real-time", and a GeneXpert system, which incorporates sample preparation, nucleic acid extraction and purification, DNA amplification, and detection into a small self-contained single cartridge providing rapid "on-demand" molecular testing 24/7, offering medically relevant results when and where they are needed most.

In the Clinical Molecular Diagnostic market, we market tests for both the GeneXpert and the SmartCycler systems in the areas of healthcare associated infections, critical infectious disease, immuno-compromised transplantation, women's health, and oncology. These tests include United States Food and Drug Administration ("FDA") cleared products, such as in *vitro medical devices* ("IVDs"), CE Marked ("CE IVD"), Analyte Specific Reagents ("ASRs"), and Research Use Only tests. We continue to develop tests for both systems.

Our February 2007 acquisition of Sangtec Molecular Diagnostics AB ("Sangtec") in Bromma, Sweden brought a relatively complete line of products for potential use in managing infections of immuno-compromised patients. We have integrated the Sangtec affigene family of real-time PCR molecular diagnostic products targeted at the immuno-compromised market into our existing European and U.S. portfolio of in vitro diagnostic products. The expanded line includes affigene assay kits for cytomegalovirus ("CMV"), Epstein-Barr Virus ("EBV"), Herpes Simplex Virus 1 and 2 ("HSV"), Hepatitis B Virus ("HBV"), Varicella Zoster Virus ("VZV"), BK Virus ("BKV"), and Aspergillus.

In March 2007, we received FDA clearance to market our Xpert EV test, which runs on the GeneXpert system, for the presumptive qualitative detection of Enterovirus ("EV") RNA in cerebrospinal fluid ("CSF") as an aid in the laboratory diagnosis of EV infection in patients with a clinical suspicion of meningitis. The Xpert EV test, designed to detect EV RNA in CSF by reverse-transcription real-time polymerase chain reaction ("RT-PCR"), is the first test of its type to receive FDA clearance. Xpert EV is the

first and only RT-PCR test that delivers EV results in less than two and a half hours compared to up to three and six days for standard culture testing.

In April 2007, we received FDA clearance to market our Xpert MRSA test, which runs on the GeneXpert system, for the rapid detection of MRSA. Xpert MRSA results are delivered in just over one hour, identifying carriers of the potential pathogen and enabling healthcare organizations to promptly implement the proper infection control measures, leading to lower healthcare associated infection rates while improving patient care. This was our fourth clinical in vitro diagnostic test.

In December 2007 we released Xpert MRSA/SA-BC (Blood Cultures) and Xpert MRSA/SA-S STI (Skin and Soft Tissue Infection) tests in Europe as CE IVD Mark products under the European Directive on In Vitro Diagnostic Medical Devices. The tests are designed to enable simultaneous rapid detection of two leading causes of hospital and community acquired infections, MRSA and, *Staphylococcus aureus*, directly from blood cultures and soft tissue infection samples respectively. We expect to complete our clinical trials and submit the product to the FDA during 2008.

During 2008, we expect to continue development programs for use with Clostridium difficile ("C. difficile"), vancomycin resistant enterococcus ("VRE"), drug resistant tuberculosis, sepsis, and a test for genetic polymorphisms in clotting factors II and V that are widely used to predict risk of thrombosis (blood clots).

In the Industrial market, we sell our SmartCycler system along with general use PCR reagents and reaction tubes.

In the Biothreat market, the GeneXpert system is the main platform. GeneXpert modules have been integrated into the Biohazard Detection Systems ("BDS"), purchased by the United States Postal Service ("USPS"). We have tests currently available for anthrax, pestis, and tullarensis.

RESEARCH AND DEVELOPMENT

The objective of our research and development programs is to develop high value test applications for the GeneXpert and/or SmartCycler systems for the Clinical Molecular Diagnostic, Biothreat, and Industrial testing market. We focus efforts on four main areas: a) systems engineering efforts to extend the multiplexing capabilities of our systems and to develop new low and high throughput systems, b) chemistry research in our Bothell, Washington facility to develop innovative and proprietary methods to design and synthesize oligonucleotide primers, probes, and dyes to optimize the speed, performance and ease-of-use of our assays, c) assay development efforts to design, optimize, and produce specific tests that leverage the systems and chemistry we have developed, and d) target discovery research to identify novel micro RNA targets to be used in the development of future assays.

SALES

We sell our products in the Clinical Molecular Diagnostic, Industrial and Biothreat markets on both a direct and distributed product basis.

Distribution and collaboration arrangements

bioMerieux, Inc. In December 2003, we entered into an agreement for a strategic commercial relationship with bioMerieux, Inc. ("bioMerieux") for bioMerieux to develop DNA testing products using its proprietary Nucleic Acid Sequence-Based Amplification ("NASBA") technology to be run on systems employing our SmartCycler and GeneXpert systems. To date, bioMerieux has not commercialized a product based on our technology.

bioMerieux SA. In January 2007, we entered into a program with bioMerieux SA for the development, production and marketing of a line of sepsis products, based upon our real-time PCR technologies. To date, no commercialized product has been jointly developed.

Infectio Diagnostic, Inc./GeneOhm Sciences, Inc. In November 2003, we entered into a series of agreements with Infectio Diagnostics, Inc. ("IDI"). IDI merged with GeneOhm Sciences, Inc. in 2004. GeneOhm Sciences, Inc. was acquired by Becton, Dickson and Company ("BDC") in February 2006. Under these agreements, we received non-exclusive worldwide, excluding Canada, distribution rights to IDI tests for GBS, MRSA and VRE that have been configured for use with the SmartCycler system. The distribution rights relating to tests for MRSA were terminated in November 2006, and the distribution rights relating to GBS terminated in April 2007. In the event that BDC introduces a VRE product for the SmartCycler system, our distribution rights relating to VRE tests will terminate two years from the date of such introduction. IDI received non-exclusive worldwide rights to distribute our SmartCycler system for use with IDI tests. Such IDI distribution rights, now owned by BDC, have an initial term that expires in November 2008.

Applied Biosystems Group. In October 2002, we entered into a collaboration agreement with Applied Biosystems Group ("ABI") to develop reagents for use in the USPS BDS program, which was developed by the consortium led by Northrop Grumman Corporation. Under the agreement, reagents are manufactured by ABI for packaging by us into our GeneXpert test cartridges and sold by us for use in the BDS. This agreement calls for the computed gross margin on sales of anthrax cartridges for the USPS BDS program to be equally shared between the two parties.

USPS Program. In 2003, a Northrop Grumman-led consortium that includes Cepheid and other subcontractors developed the BDS for the USPS. This consortium was awarded a production contract, and installations were completed at the end of 2005. In August 2007, we entered into a five-year master purchase order with Northrop Grumman for the purchase of up to $200 million in anthrax test cartridges and associated materials used in BDS. The agreement covers the USPS fiscal years of 2007 through 2011. Under the terms of the agreement, the purchase quantity of anthrax tests will be determined on an annual basis, based on the USPS fiscal year of October 1 through September 30. We have received notice that expected test purchases for fiscal 2008 will be approximately two million cartridges.

Foundation for Innovative New Diagnostics. In May 2006, we entered into an agreement with the Foundation for Innovative New Diagnostics ("FIND") to develop a simple, rapid test that can detect mycobactrium tuberculosis and associated rifampin resistance from human sputum samples. Under the agreement, we are responsible for the development of a 6-color GeneXpert system to accomplish such test and the development of an enhanced manufacturing line for the manufacture of test cartridges used in the test. FIND will reimburse us at agreed upon amounts. The term of the development portion of the agreement is for 30 months. The supply term of the agreement is for twelve years, unless terminated by either party in accordance with relevant provisions of the agreement.

Centers for Disease Control and Prevention. In December 2006, we entered into a contract with the Centers for Disease Control and Prevention ("CDC") for the first two phases of a five phase program for the development of a new Point-of-Care in vitro diagnostic product that tests for influenza viruses A and B, and H5N1, providing general clinical utility for seasonal flu diagnosis in addition to its application in the case of an avian flu pandemic. Under the first two phases of the program, we were responsible to develop a pre-clinical development plan, a clinical development and a regulatory plan. In September 2007, the contract was terminated.

MANUFACTURING

Our facilities and manufacturing processes are designed to comply with the quality standard set by the International Organization for Standardization and the FDA's Quality System Regulations, enabling us to market our systems in the Clinical Molecular Diagnostic, Industrial and Biothreat testing markets worldwide. In our manufacturing facilities, we assemble our instrument systems and produce reagents and tests for use on our GeneXpert and SmartCycler systems. We assemble our disposable reaction tubes on a custom, automated assembly line that is designed with an expandable capacity. We depend on suppliers for various components used in the manufacture of the SmartCycler and GeneXpert systems, disposable reaction tubes, and cartridges, some of which are our sole source for such components.

We received ISO 13485:1996 certification in February 2003. In 2006 we received ISO 13485:2003 certification that includes CADMAS for European and Canadian product distribution. Our facility was inspected by the FDA during 2007 and found to be in compliance with Quality System Regulations.

COMPETITION

We face intense competition from an increasing number of companies that offer products in our targeted application areas. These competitors include:

- companies developing and marketing sequence detection systems for industrial research products;
- healthcare companies that manufacture laboratory-based tests and analyzers;
- diagnostic and pharmaceutical companies;
- companies developing drug discovery technologies; and
- companies developing or offering biothreat detection technologies.

Several companies provide instruments and reagents for DNA amplification or detection. ABI and F. Hoffman-La Roche Ltd ("Roche") sell systems integrating DNA amplification and detection (sequence detection systems) to the commercial market. Roche,

Abbott Laboratories, Becton, Dickinson and Company, Qiagen, Celera and GenProbe sell sequence detection systems, some with separate robotic batch DNA purification systems and sell reagents to the Clinical Molecular Diagnostic market. Other companies, including Siemens, Third Wave Technologies and bioMerieux, offer molecular tests.

We also face competition from both established and development-stage companies that are entering these markets. Several companies are currently making or developing products that may or will compete with our products. Our competitors may succeed in developing, obtaining FDA approval for, or marketing technologies or products that are more effective or commercially attractive than our potential products or that render our technologies and potential products obsolete. As these companies develop their technologies, they may develop proprietary positions that prevent us from successfully commercializing our products.

In order to compete effectively, we will need to demonstrate the advantages of our products over alternative well-established technologies and products. We will also need to demonstrate the potential economic value of our products relative to these technologies and products.

In many instances, particularly in the clinical genetics assessment area, our competitors have substantially greater financial, technical, research and other resources, and larger, more established marketing, sales, distribution and service organizations than we have. Moreover, these competitors may offer broader product lines and tactical discounts and have greater name recognition. If we fail to compete effectively against these and other competitors, we could lose sales, and our business will be harmed.

We believe that the principal competitive factors affecting sales of genetic and DNA analysis systems include the speed, integrated functionality and portability of the equipment, ease of use, the quality of the test results, price, market acceptance of the technology, regulatory approvals, particularly in the Clinical Molecular Diagnostic market, and possession of the necessary intellectual property licenses for specific markets, collaborations and distributor relationships for specific markets and tests, and the selection of tests available for the system. We believe our products better integrate the various processes associated with DNA and RNA analysis than other currently available equipment, and that the speed, portability, flexibility, reliability and ease of use of our products are competitive.

GOVERNMENT REGULATION

In the Clinical Molecular Diagnostic market, our products are generally regulated as medical device products by the FDA and comparable agencies of other countries. In particular, FDA regulations govern activities such as product development, product testing, product labeling, product storage, premarket clearance or approval, manufacturing, advertising, promotion, product sales, reporting of certain product failures and distribution. Some of our products, depending on their intended use, will require either premarket approval ("PMA") or 510(k) clearance from the FDA prior to marketing. The 510(k) clearance pathway usually takes from three to four months from submission but can take longer.

To date, we have received FDA clearance on Smart GBS, Xpert GBS, Xpert EV and Xpert MRSA. In addition, we have CE IVD-marked products for sale in Europe for Xpert BCR/ABL, Xpert GBS, Xpert EV, Xpert MRSA Xpert MRSA/SA-BC and Xpert MRSA/SA-SSTI on the GeneXpert system. We also have CE IVD-marked products for Smart GBS, EBV, CMV and VZV on the SmartCycler system. We have CE IVD marked the SmartCycler system and GeneXpert system for IVD use in EU countries.

For the Industrial and Biothreat markets, some of our products may not need FDA or other regulatory approval; however, all of our products will be produced under ISO 13485 and Quality System Regulations.

INTELLECTUAL PROPERTY

We integrate capabilities in systems design, development, production and DNA amplification technologies, along with design, development and manufacture of primers, probes, dyes, quenchers and other individual reagent components. We have and are continuing to develop our own proprietary intellectual property along with licensing specific third-party technologies. We currently have, either through assignment or exclusive license, 41 issued and allowed US patents along with 36 pending US patent applications. These do not include international counterparts.

Our competitive success will be affected in part by our continued ability to obtain and maintain patent protection for our inventions, technologies and discoveries, including intellectual property that includes technologies that we license. We have patents covering technologies of our own and have licensed technologies from others. Our pending patent applications may lack priority over applications submitted by third parties or may not result in the issuance of patents. Even if issued, our patents may not be sufficiently broad to provide protection against competitors with similar technologies and may be challenged, invalidated or circumvented.

In addition to patents, we rely on a combination of trade secrets, copyright and trademark laws, nondisclosure agreements, licenses and other contractual provisions and technical measures to maintain and develop our competitive position with respect to intellectual property. Nevertheless, these measures may not be adequate to safeguard the technology underlying our products. For example, employees, consultants and others who participate in the development of our products may breach their agreements with us regarding our intellectual property, and we may not have adequate remedies for the breach. We also may not be able to effectively protect our intellectual property rights in some foreign countries, as many countries do not offer the same level of legal protection for intellectual property as the United States. Furthermore, for a variety of reasons, we may decide not to file for patent, copyright or trademark protection outside of the United States. Our trade secrets could become known through other unforeseen means. Notwithstanding our efforts to protect our intellectual property, our competitors may independently develop similar or alternative technologies or products that are equal or superior to our technology. Our competitors may also develop similar products without infringing on any of our intellectual property rights or design around our proprietary technologies. Furthermore, any efforts to enforce our proprietary rights could result in disputes and legal proceedings that could be costly and divert attention from our business. We could also be subject to third-party claims that we require additional licenses for our products, and such claims could interfere with our business. From time to time, third parties have contacted us regarding their intellectual property, whether to license intellectual property, or in some instances, alleging potential infringement. If our products infringe on the intellectual property rights of others, we could face costly litigation, which could cause us to pay substantial damages and limit our ability to sell some or all of our products. Even if our products were determined not to infringe on the intellectual property rights of others, we could incur substantial costs in defending any such claims.

We hold an exclusive license to key technologies from Lawrence Livermore National Laboratory ("LLNL") related to thermal cycling with integrated optical detection. This license is limited to the fields of nucleic acid analysis and ligand binding tests and contains diligence and U.S. preference provisions. These technologies have resulted in three issued U.S. patents and two pending international counterpart patent applications. The LLNL technologies are the basis of our I-CORE module and encompass the key I-CORE features.

In April 2004, we entered into a patent license agreement with Applera for a non-exclusive worldwide license to make, use, and sell our products incorporating technology covered by Applera patents. In June 2006, the patent license agreement was expanded to include additional products.

In July 2004, we entered into an agreement with Roche that provides us with rights under a broad range of Roche patents, which include patents relating to the PCR process, reverse transcription-based methods, nucleic acid quantification methods, real-time PCR detection process and composition, and patents relating to methods for detection of viral and cancer targets.

In September 2005, we entered into a license agreement with Abaxis, Inc. ("Abaxis"), pursuant to which Abaxis granted us a non-exclusive, worldwide, royalty-bearing license to certain Abaxis patents relating to lyophilization technology in accordance with the provisions specified in the agreement. In exchange for the license rights, we (i) made an upfront license payment, (ii) agreed to pay royalties during the term of the agreement and (iii) agreed to pay a yearly license maintenance fee during the term of the agreement, which fee will be creditable against any royalties due during such calendar year.

In November 2005, we entered into a license agreement with DxS Limited ("DxS"), a private United Kingdom based company, pursuant to which DxS granted us a non-exclusive, worldwide, royalty-bearing license to the DxS Scorpions patents and other intellectual property rights relating to its Scorpions technology for the real-time PCR detection of nucleic acid amplification. Under the amended agreement, and subject to certain limitations set forth therein, we will be able to use the licensed rights to develop and sell test products incorporating the licensed technology in the human *in vitro* diagnostics field, in addition to the environmental, veterinarian, forensics identity relationship testing and agricultural fields.

In September 2006, we entered in a sublicense agreement with Abbott Laboratories ("Abbott"), pursuant to which Abbott granted us a non-exclusive, world-wide, non-transferable right to Abbott's exclusive license to certain patents from the Baylor College of Medicine. Under the sublicense agreement, we will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as multiple genomic DNA amplification for deletion detection. In September 2006, we also entered into a license agreement with Abbott, pursuant to which Abbott granted us a non-exclusive, world-wide, non-transferable right to a certain Abbott patent. Under the license agreement, we will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as detection of cervical chlamydia trachomatis infection.

In January 2007, we entered into a sublicense agreement with bioMerieux SA, pursuant to which bioMerieux SA granted us a non-exclusive, worldwide, irrevocable sublicense to certain patents that relate to the diagnosis of MRSA. The patents are owned by Kainos Laboratories Inc. and Professor Keiichi Hiramatsu and have been exclusively licensed to bioMerieux SA with the right for bioMerieux SA to sub-license. Under the sublicense agreement, and subject to certain limitations set forth therein, we will be able to use the licensed rights to develop and sell products for use with our GeneXpert and SmartCycler systems.

We intend to actively pursue acquisitions of additional molecular markers and/or complementary products, technologies or companies in the fields of oncology, infectious diseases and other fields appropriate for molecular diagnostics. Under this program, we made our first significant technology acquisition during 2006 in the emerging field of micro RNA technology. Based on this acquisition, we currently have over 600 micro RNA targets under evaluation, and an additional 1,400 candidates are under investigation. These targets are expected to lead to specific potential test opportunities in the cancer and infectious disease areas.

EMPLOYEES

As of December 31, 2007, we had 473 full-time equivalent and contract employees worldwide. At December 31, 2007 none of our employees were represented by a labor union. Many of our employees in Sweden are under a collective bargaining agreement. We consider our employee relations to be good.

EXECUTIVE OFFICERS OF THE REGISTRANT

The names of our executive officers and their ages, titles and biographies as of February 15, 2008 appear below: Our former Senior Vice President and Chief Financial Officer, John R. Sluis, retired on December 31, 2007. We entered into a separation and consulting agreement with Mr. Sluis, pursuant to which he will provide us with consulting services on a part-time basis until December 31, 2008. On February 6, 2008, we entered into an employment agreement with our new Senior Vice President, Finance and Chief Financial Officer, Andrew D. Miller, who we expect to begin employment with us on or about April 14, 2008.

The following table and discussion set forth certain information with regard to our current executive officers.

Name	Age	Position
John L. Bishop	63	Chief Executive Officer and Director
Peter J. Dailey, Ph.D.	54	Senior Vice President, Research and Development
Russel K. Enns, Ph.D.	59	Senior Vice President, Regulatory and Clinical Affairs, Quality System and Reimbursement
Robert J. Koska	50	Senior Vice President, Worldwide Commercial Operations
David H. Persing, M.D., Ph.D.	52	Executive Vice President and Chief Medical and Technology Officer and Director
Humberto Reyes	62	Executive Vice President, Operations
Joseph H. Smith	63	Senior Vice President, General Counsel and Secretary

John L. Bishop. Mr. Bishop joined us as Chief Executive Officer and as a director in April 2002. Mr. Bishop served as President and a director of Vysis, a genomic disease management company, from 1993 to 2002 and as Chief Executive Officer from 1996 to March 2002. From 1991 until November 1993, Mr. Bishop was Chairman and Chief Executive Officer of MicroProbe Corporation, a biotechnology company, and, from 1987 until 1991, of Source Scientific Systems, a biomedical instrument manufacturing company. From 1984 to 1986, Mr. Bishop was President and Chief Operating Officer of Gen-Probe, Inc. From 1968 to 1984, Mr. Bishop held various management positions with American Hospital Supply Company and its affiliates, including a three-year assignment in Japan as an Executive Vice President and Chief Executive Officer of International Reagents Corp., a joint venture between American Hospital Supply Company and Green Cross Corporation.

Peter J. Dailey, Ph.D. Dr. Dailey joined us as Vice President, Research and Development in June 2006 and now serves as our Senior Vice President, Research and Development. Most recently, Dr. Dailey was the Senior Director of the Department of Infectious Disease in Discovery Research at Roche Molecular Systems, Inc. He is a microbiologist and virologist by training and has worked in the field of diagnostic microbiology for the last 25 years. Dr. Dailey worked as a Public Health Microbiologist at the California State Dept. of Health's Viral & Rickettsial Disease Laboratory in Berkeley, California in the 1980s on the development of diagnostic assays for HIV and HTLV. He also worked many years as a Clinical Laboratory microbiologist in medical centers, hospitals, and reference laboratories. Beginning in 1990, he was employed at Chiron Diagnostics (now Bayer Diagnostics) working on the research, development, and application of nucleic acid probe assays, in particular viral load assays for HCV, HIV, and SIV. He has served as a subcommittee member on the National Committee for Clinical Laboratory Standards committee revising Guidelines for Molecular Diagnostic Methods for Infectious Diseases and has authored or co-authored more than 35 peer-reviewed papers as well as several book chapters and reviews on infectious disease nucleic acid diagnostic assays.

Russel K. Enns, Ph.D. Dr. Enns joined us as Senior Vice President, Regulatory Affairs, Quality System, Clinical Affairs and Medical Reimbursement in June 2003. Prior to joining Cepheid, Dr. Enns was Divisional Vice President for Regulatory and Clinical Affairs, Quality Systems, and Medical Reimbursement at Vysis, Inc., a genomic disease management company that was acquired by Abbott Laboratories, from 1995 to April 2003. Before joining Vysis, he was Vice President, Technical Affairs of MicroProbe

Corporation, a biotechnology company, from 1992 to 1995. Before joining MicroProbe Corporation, he was Director of Product Development Clinical Programs and Technical Affairs at GenProbe, Inc., a biotechnology diagnostic company, from 1984 to 1992. From 1979 to 1984, Dr. Enns was the Director of Cell Biology at Alpha Therapeutics Corporation, and from 1975 to 1979 he was a Senior Biochemist at Monsanto Corporation. He received his Ph.D. in Biochemistry from University of California at Davis in 1976. Dr. Enns is a charter member and past chair of the CLSI (formerly NCCLS) Area Committee on Molecular Methods, and he is currently a member of the CLSI Board of Directors.

Robert J. Koska. Mr. Koska joined us in February 2005 and since September 2007 has served as our Senior Vice President, Worldwide Commercial Operations. Prior to joining Cepheid, Mr. Koska held various positions with Vysis, Inc. and subsequently Abbott Laboratories since 1996. Mr. Koska's work experience includes Divisional Vice President, Vysis U.S. and Canadian Sales at Abbott Molecular Diagnostics, and Senior Vice President Worldwide Sales & Marketing, Vysis prior to the Abbott acquisition. Mr. Koska further previously held progressive positions of increased responsibility in sales and marketing at DIFCO Laboratories, Inc., Bristol Myers Genetic Systems Corporation, and Johnson and Johnson's Ortho Diagnostic Systems, Inc. Mr. Koska has an MBA, Marketing Emphasis, from the University of Michigan, Ann Arbor, MI, and a BS degree in Medical Technology from Wayne State University, Detroit, MI.

David H. Persing, M.D., Ph.D. Dr. Persing first joined us as a director in May 2004, and became our Executive Vice President and Chief Medical and Technology Officer in August 2005. Dr. Persing was previously Senior Vice President and Chief Scientific Officer at Corixa Corporation, a Seattle-based biotechnology company, until their acquisition by GlaxoSmithkline from 1999 to July 2005. From 1990 to 1999 he was a member of the Clinical and Research Faculty of the Mayo Clinic in Rochester, Minnesota where he researched programs on hepatitis viruses and tick-borne infections. In 1992 he founded and directed the Molecular Microbiology Laboratory at Mayo Clinic. He has authored over 240 peer-reviewed articles and served as Editor in Chief for three textbooks on Molecular Diagnostics, the most recent of which was published by ASM press in December 2004. Dr. Persing currently serves as a director of Monogram Biosciences, Inc.

Humberto Reyes. Mr. Reyes joined us as Senior Vice President of Operations in November 2004 and became our Executive Vice President of Operations in November 2006. Prior to joining Cepheid, Mr. Reyes was an Operations Consultant with Brownsboro Group, LLC. from September 2003 to November 2004. Prior to joining Brownsboro, Mr. Reyes was a Senior Operations Consultant for EXPERTech Associates, consulting in medical devices and biotech industries from November 2001 to June 2003. Prior to that, he was Head of Operations for OXIS Health Products Inc., which developed, manufactured and marketed products for oxidative research and wellness programs from August 1997 to September 2001. He is an experienced operations executive with more than 25 years of progressive management experience in the diagnostic and related industries. Mr. Reyes' work experience also includes Vice President, Operations, Dade Diagnostics at Baxter; Vice President/General Manager, Chromatography Division, Varian and Associates; and Sr. Vice President, Operations, Microgenics Corporation.

Joseph H. Smith. Mr. Smith joined us in June 2003 and now serves as Senior Vice President and General Counsel. He has been Secretary of the Corporation since March 2004. From 1989 to April 2002, Mr. Smith was Vice President of Intellectual Property at Applied Biosystems Group and its predecessors, a biotechnology research equipment company, and during 2002-2003 was its Senior Vice President for Business Development. Prior to Applied Biosystems, Mr. Smith was a partner in the law firm of Wiseman, Jones, and Smith; and prior to that he was also a member of the Technical Legal Department of Hewlett-Packard.

AVAILABLE INFORMATION

We are subject to the informational requirements of the Securities Exchange Act of 1934. Therefore, we file periodic reports, proxy statements and other information with the Securities and Exchange Commission ("SEC"). Such reports, proxy statements and other information may be obtained by visiting the Public Reference Room of the SEC at 100 F Street N.E., Washington, D.C. 20549 or by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet site (http://www.sec.gov) that contains reports, proxy and information statements and other information regarding issuers that file electronically.

You can also access financial and other information at our Investor Relations website. Our website is located at www.cepheid.com. We make available free of charge on our web site our Annual Reports on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after we electronically file them with or furnish them to the SEC. Information contained on our web site is not part of this Annual Report on Form 10-K or our other filings with the SEC.

The charters of our Audit Committee, our Compensation Committee and our Nominating/Governance Committee, are available on the Investor Relations section of our website under "Corporate Governance". Also available on that section of our website is our Code of Business Conduct and Ethics, which we expect every employee, officer, director, staffing agency worker and consultant to read,

understand and abide by. This information is also available by writing to us at the address on the cover of this Annual Report on Form 10-K.

ITEM 1A. RISK FACTORS

You should carefully consider the risks and uncertainties described below, together with all of the other information included in this Report, in considering our business and prospects. The risks and uncertainties described below are not the only ones facing Cepheid. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations. The occurrence of any of the following risks could harm our business, financial condition or results of operations.

We may not achieve profitability.

We have incurred operating losses in each period since our inception. We experienced net losses of approximately $13.6 million in 2005, $26.0 million in 2006 and $21.4 million in 2007. As of December 31, 2007, we had an accumulated deficit of approximately $154.9 million. Our ability to become profitable will depend on our ability to continue to increase our revenues, which is subject to a number of factors including our ability to successfully penetrate the Clinical Molecular Diagnostic market, our ability to successfully market the GeneXpert system and develop effective GeneXpert tests, the extent of our participation in the USPS BDS program and the operating parameters of the USPS BDS program, which will affect the rate of our consumable products sold, the success of our other collaborative programs, our ability to compete effectively against current and future competitors, global economic and political conditions and the impact of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment". Our ability to become profitable also depends on our expense levels and product gross margin, which are also influenced by a number of factors, including the resources we devote to developing and supporting our products, the continued progress of our research and development of potential products, the ability to gain FDA clearance for our products, our ability to improve manufacturing efficiencies, license fees or royalties we may be required to pay, our ability to integrate acquired businesses and technologies, acquisition-related costs and expenses and the potential need to acquire licenses to new technology or to use our technology in new markets, which could require us to pay unanticipated license fees and royalties in connection with these licenses. Our expansion efforts may prove more expensive than we currently anticipate, and we may not succeed in increasing our revenues to offset higher expenses. These expenses, among other things, may cause our net income and working capital to decrease. If we fail to grow our revenue and manage our expenses and improve our product gross margin, we may never achieve profitability. If we fail to do so, the market price of our common stock will likely decline.

If we cannot successfully commercialize our products, our business could be harmed.

If our tests for use on the SmartCycler and GeneXpert systems do not gain continued market acceptance, we will be unable to generate significant sales, which will prevent us from achieving profitability. While we have received FDA clearance for our Xpert GBS, Xpert EV and Xpert MRSA tests, these products may not continue to achieve commercial success. Many factors may affect the market acceptance and commercial success of our products, including:

- timely development of a menu of tests and reagents;
- the results of clinical trials needed to support any regulatory approvals of our tests;
- our ability to obtain requisite FDA or other regulatory clearances or approvals for our tests under development on a timely basis;
- demand for the tests and reagents we are able to introduce;
- the timing of market entry for various tests for the GeneXpert and the SmartCycler systems;
- our ability to convince our potential customers of the advantages and economic value of our systems and tests over competing technologies and products;
- the breadth of our test menu relative to competitors;
- the extent and success of our marketing and sales efforts; and
- publicity concerning our systems and tests.

In particular, we believe that the success of our business will depend in large part on our ability to introduce additional tests for the Clinical Molecular Diagnostic market. We believe that successfully building our business in the Clinical Molecular Diagnostic market is critical to our long-term goals and success. We have limited ability to forecast future demand for our products in this market. In addition, we have committed substantial funds to licenses that are required for us to enter the Clinical Molecular Diagnostic market. If we cannot successfully penetrate the Clinical Molecular Diagnostic market to exploit these licenses, these investments may not yield significant returns, which could harm our business.

The regulatory approval process is expensive, time-consuming, and uncertain and may prevent us from obtaining required approvals for the commercialization of some of our products.

In the Clinical Molecular Diagnostic market, our products are regulated as medical device products by the FDA and comparable agencies of other countries. In particular, FDA regulations govern activities such as product development, product testing, product labeling, product storage, premarket clearance or approval, manufacturing, advertising, promotion, product sales, reporting of certain product failures and distribution. Some of our products, depending on their intended use, will require premarket approval ("PMA") or 510(k) clearance from the FDA prior to marketing. The 510(k) clearance process usually takes from three to four months from submission but can take longer. The PMA process is much more costly, lengthy, and uncertain and generally takes from six months to one year or longer from submission. Clinical trials are generally required to support both PMA and 510(k) submissions. Certain of our products for use on our SmartCycler and GeneXpert systems, when used for clinical purposes, may require PMA, and all such tests will most likely, at a minimum, require 510(k) clearance. We are planning clinical trials for other proposed products. Clinical trials are expensive and time-consuming. In addition, the commencement or completion of any clinical trials may be delayed or halted for any number of reasons, including product performance, changes in intended use, changes in medical practice and issues with evaluator Institutional Review Boards.

Failure to comply with the applicable requirements can result in, among other things, warning letters, administrative or judicially imposed sanctions such as injunctions, civil penalties, recall or seizure of products, total or partial suspension of production, refusal to grant premarket clearance or PMA for devices, withdrawal of marketing clearances or approvals, or criminal prosecution. With regard to future products for which we seek 510(k) clearance or PMA from the FDA, any failure or material delay to obtain such clearance or approval could harm our business. If the FDA were to disagree with our regulatory assessment and conclude that approval or clearance is necessary to market the products, we could be forced to cease marketing the products and seek approval or clearance. With regard to those future products for which we will seek 510(k) clearance or PMA from the FDA, any failure or material delay to obtain such clearance or approval could harm our business. In addition, it is possible that the current regulatory framework could change or additional regulations could arise at any stage during our product development or marketing, which may adversely affect our ability to obtain or maintain approval of our products and could harm our business.

Our manufacturing facilities located in Sunnyvale, California, Bothell, Washington and Bromma, Sweden, where we assemble and produce the SmartCycler and GeneXpert systems, cartridges and other molecular diagnostic kits and reagents, are subject to periodic regulatory inspections by the FDA and other federal and state regulatory agencies. For example, these facilities are subject to Quality System Regulations ("QSR") of the FDA and are subject to annual inspection and licensing by the State of California and European regulatory agencies. If we fail to maintain these facilities in accordance with the QSR requirements, international quality standards or other regulatory requirements, our manufacturing process could be suspended or terminated, which would prevent us from being able to provide products to our customers in a timely fashion and therefore harm our business.

The U.S. Food and Drug Administration has issued a final interpretation of the regulations governing the sale of Analyte Specific Reagent products which could prevent or delay our sales of these products and harm our business.

In September 2006, the FDA published "Draft Guidance for Industry and FDA Staff: Commercially Distributed Analyte Specific Reagents ("ASRs"): Frequently Asked Questions" clarifying the FDA's interpretation of the regulations governing the sale of ASR products. On September 14, 2007, the FDA published its final guidance that becomes effectively enforced on September 15, 2008. ASRs are a class of products that do not require regulatory clearance or approval but do require compliance with the FDA's Good Manufacturing Practice Regulations. The final guidance contains changes in interpretation of the ASR regulations with regard to which products may be characterized as ASRs that represent a departure from what we believe had been the previous FDA practice and policy, in particular, the final guidance excludes reagent mixtures used to detect multiple targets from the definition of ASRs. The changes in the final ASR guidance may require modifications of some of our ASR products for us to continue selling them, or may require us to seek FDA clearance in order to sell them. In addition, the final guidance may curtail our interest in developing any new products that would qualify as ASRs.

We rely on licenses of key technology from third parties and may require additional licenses for many of our new product candidates.

We rely on third-party licenses to be able to sell many of our products, and we could lose these third-party licenses for a number of reasons, including, for example, early terminations of such agreements due to breaches or alleged breaches by either party to the agreement. If we are unable to enter into a new agreement for licensed technologies, either on terms that are acceptable to us or at all, we may be unable to sell some of our products or access some geographic or industry markets. We also need to introduce new products and product features in order to market our products to a broader customer base and grow our revenues, and many new products and product features could require us to obtain additional licenses and pay additional license fees and royalties. Furthermore, for some markets, we intend to manufacture reagents and tests for use on our instruments. We believe that manufacturing reagents and developing tests for our instruments is important to our business and growth prospects but may require additional licenses, which may not be available on commercially reasonable terms or at all. Our ability to develop, manufacture and sell products, and our strategic plans and growth, could be impaired if we are unable to obtain these licenses or if these licenses are terminated or expire and cannot be renewed. We may not be able to obtain or renew licenses for a given product or product feature or for some reagents on commercially reasonable terms, if at all. Furthermore, some of our competitors have rights to technologies and reagents that we do not have which may put us at a competitive disadvantage in certain circumstances and could adversely affect our performance.

We enter into collaborations with third parties that may not result in the development of commercially viable products or the generation of significant future revenues.

In the ordinary course of our business, we enter into collaborative arrangements to develop new products or to pursue new markets. These collaborations may not result in the development of products that achieve commercial success, and these collaborations could be terminated prior to developing any products. Accordingly, we cannot assure you that any of our collaborations will result in the successful development of a commercially viable product or result in significant additional future revenues in the future.

Our participation in the USPS BDS program may not result in predictable contracts or revenues in the future.

Our participation in the USPS BDS program involves significant uncertainties related to governmental decision-making and timing of deployment, and is highly sensitive to changes in national and international priorities and budgets. Budgetary pressures may result in reduced allocations to government agencies such as the USPS, sometimes without advanced notice. We cannot be certain that actual funding and operating parameters, or product purchases, will occur at currently expected levels or in the currently expected timeframe.

We may face risks associated with acquisitions of companies, products and technologies, and our business could be harmed if we are unable to address these risks.

If we are presented with appropriate opportunities, we intend to acquire or make other investments in complementary companies, products or technologies. We may not realize the anticipated benefit of any acquisition or investment. We will likely face risks, uncertainties and disruptions associated with the integration process, including difficulties in the integration of the operations and services of an acquired company, integration of acquired technology with our products, diversion of our management's attention from other business concerns, the potential loss of key employees or customers of the acquired businesses and impairment charges if future acquisitions are not as successful as we originally anticipate. If we fail to successfully integrate other companies, products or technologies that we acquire, our business could be harmed. Furthermore, we may have to incur debt or issue equity securities to pay for any additional future acquisitions or investments, the issuance of which could be dilutive to our existing shareholders. In addition, our operating results may suffer because of acquisition-related costs or amortization expenses or charges relating to acquired intangible assets.

We expect that our operating results will fluctuate significantly, and any failure to meet financial expectations may result in a decline in our stock price.

We expect that our quarterly operating results will fluctuate in the future as a result of many factors, such as those described elsewhere in this section, many of which are beyond our control. Because our revenue and operating results are difficult to predict, we believe that period-to-period comparisons of our results of operations are not a good indicator of our future performance. Our operating results may be affected by the inability of some of our customers to consummate anticipated purchases of our products, whether due to changes in internal priorities or, in the case of governmental customers, problems with the appropriations process and variability and timing of orders, or manufacturing inefficiencies. If revenue declines in a quarter, whether due to a delay in recognizing expected revenue, unexpected costs or otherwise, our results of operations will be harmed because many of our expenses are relatively fixed. In particular, research and development and selling, general and administrative expenses are not significantly affected by variations in revenue. If our quarterly operating results fail to meet or exceed the expectations of securities analysts or investors, our stock price could drop suddenly and significantly.

If we are unable to manufacture our products in sufficient quantities and in a timely manner, our operating results will be harmed and our ability to generate revenue could be diminished.

Our revenues and other operating results will depend in large part on our ability to manufacture and assemble our products in sufficient quantities and in a timely manner. Any interruptions we experience in the manufacturing or shipping of our products could delay our ability to recognize revenues in a particular quarter. We have limited experience in manufacturing large volumes of products, and manufacturing problems can and do arise or we may be unable to adequately scale-up manufacturing in a timely manner or on a commercially reasonable basis if we experience increased demand. In the past, we have experienced problems and delays in production that have impacted our product yield and caused delays in our ability to ship finished products, and we may experience such delays in the future. We may not be able to react quickly enough to ship products and recognize anticipated revenues for a given period if we experience significant delays in the manufacturing process. If we are unable to manufacture our products consistently and on a timely basis, our revenues from product sales, gross margins and our other operating results will be materially and adversely affected.

If certain single source suppliers fail to deliver key product components in a timely manner, our manufacturing ability would be impaired and our product sales could suffer.

We depend on certain single source suppliers that supply some of the components used in the manufacture of our instruments and our disposable reaction tubes and cartridges. If we need alternative sources for key component parts for any reason, these component parts may not be immediately available to us. If alternative suppliers are not immediately available, we will have to identify and qualify alternative suppliers, and production of these components may be delayed. We may not be able to find an adequate alternative supplier in a reasonable time period or on commercially acceptable terms, if at all. Shipments of affected products have been limited or delayed as a result of such problems in the past, and similar problems could occur in the future. Our inability to obtain our key source supplies for the manufacture of our products may require us to delay shipments of products, harm customer relationships or force us to curtail or cease operations.

If certain of our products fail to obtain an adequate level of reimbursement from third-party payers, our ability to sell products in the Clinical Molecular Diagnostic market would be harmed.

Our ability to sell our products in the Clinical Molecular Diagnostic market will depend in part on the extent to which reimbursement for tests using our products will be available from:

- government health administration authorities;
- private health coverage insurers;
- managed care organizations; and
- other organizations.

There are efforts by governmental and third-party payers to contain or reduce the costs of health care through various means. Additionally, third-party payers are increasingly challenging the price of medical products and services. If purchasers or users of our products are not able to obtain adequate reimbursement for the cost of using our products, they may forego or reduce their use. Significant uncertainty exists as to the reimbursement status of newly approved health care products and whether adequate third-party coverage will be available.

If our competitors and potential competitors develop superior products and technologies, our competitive position and results of operations would suffer.

We face intense competition from a number of companies that offer products in our target markets. These competitors include:

- healthcare companies that manufacture laboratory-based tests and analyzers;
- companies developing and marketing sequence detection systems for industrial research products;
- diagnostic and pharmaceutical companies;
- companies developing drug discovery technologies; and
- companies developing or offering biothreat detection technologies.

Several companies provide instruments and reagents for DNA amplification or detection. ABI and Roche sell systems integrating DNA amplification and detection (sequence detection systems) to the commercial market. Roche, Abbott Laboratories, Becton, Dickinson and Company, Qiagen, Celera and GenProbe sell sequence detection systems, some with separate robotic batch DNA purification systems and sell reagents to the Clinical Molecular Diagnostic market. Other companies, including Siemens, Third Wave Technologies and bioMerieux, offer molecular tests.

If our products do not perform as expected or the reliability of the technology on which our products are based is questioned, we could experience lost revenue, delayed or reduced market acceptance of our products, increased costs and damage to our reputation.

Our success depends on the market's confidence that we can provide reliable, high-quality molecular test systems. We believe that customers in our target markets are likely to be particularly sensitive to product defects and errors. Our reputation and the public image of our products or technologies may be impaired if our products fail to perform as expected or our products are perceived as difficult to use. Despite testing, defects or errors could occur in our products or technologies. Furthermore, with respect to the BDS program, our products are incorporated into larger systems that are built and delivered by others; we cannot control many aspects of the final system.

In the future, if our products experience a material defect or error, this could result in loss or delay of revenues, delayed market acceptance, damaged reputation, diversion of development resources, legal claims, increased insurance costs or increased service and warranty costs, any of which could harm our business. Any failure in the overall BDS, even if it is unrelated to our products, could harm our business. Even after any underlying concerns or problems are resolved, any widespread concerns regarding our technology or any manufacturing defects or performance errors in our products could result in lost revenue, delayed market acceptance, damaged reputation, increased service and warranty costs, and claims against us.

If product liability lawsuits are successfully brought against us, we may face reduced demand for our product and incur significant liabilities.

We face an inherent risk of exposure to product liability claims if our technologies or systems are alleged to have caused harm or do not perform in accordance with specifications, in part because our products are used for sensitive applications. We cannot be certain that we would be able to successfully defend any product liability lawsuit brought against us. Regardless of merit or eventual outcome, product liability claims may result in:

- decreased demand for our products;
- injury to our reputation;
- costs of related litigation; and
- substantial monetary awards to plaintiffs.

If we become the subject of a successful product liability lawsuit, we could incur substantial liabilities, which could harm our business.

We rely on relationships with collaborative partners and other third parties for development, supply and marketing of certain products and potential products, and such collaborative partners or other third parties could fail to perform sufficiently.

We believe that our success in penetrating our target markets depends in part on our ability to develop and maintain collaborative relationships with other companies. Relying on collaborative relationships is risky to our future success for these products because, among other things:

- our collaborative partners may not devote sufficient resources to the success of our collaboration;
- our collaborative partners may not obtain regulatory approvals necessary to continue the collaborations in a timely manner;
- our collaborative partners may be acquired by another company and decide to terminate our collaborative partnership or become insolvent;
- our collaborative partners may develop technologies or components competitive with our products;
- components developed by collaborators could fail to meet specifications, possibly causing us to lose potential projects and subjecting us to liability;

- disagreements with collaborators could result in the termination of the relationship or litigation;
- collaborators may not have sufficient capital resources;
- collaborators may pursue tests or other products that will not generate significant volume for us, but may consume significant research and development and manufacturing resources; and
- we may not be able to negotiate future collaborative arrangements, or renewals of existing collaborative agreements, on acceptable terms.

Because these and other factors may be beyond our control, the development or commercialization of these products may be delayed or otherwise adversely affected.

If we or any of our collaborative partners terminate a collaborative arrangement, we may be required to devote additional resources to product development and commercialization or we may need to cancel some development programs, which could adversely affect our product pipeline and business.

If our direct selling efforts for our products fail, our business expansion plans could suffer, and our ability to generate revenue will be diminished.

We have a relatively small sales force compared to our competitors. If our direct sales force is not successful, or new additions to our sales team fail to gain traction among our customers, we may not be able to increase market awareness and sales of our products. If we fail to establish our systems in the marketplace, it could have a negative effect on our ability to sell subsequent systems and hinder the planned expansion of our business.

If our distributor relationships are not successful, our ability to market and sell our products would be harmed and our financial performance will be adversely affected.

We depend on relationships with distributors for the marketing and sales of our products in the Industrial and Clinical Molecular Diagnostic markets in various geographic regions, and we have a limited ability to influence their efforts. We expect to continue to rely substantially on our distributor relationships for sales into other markets or geographic regions, which is key to our long-term growth potential. Relying on distributors for our sales and marketing could harm our business for various reasons, including:

- agreements with distributors may terminate prematurely due to disagreements or may result in litigation between the partners;
- we may not be able to renew existing distributor agreements on acceptable terms;
- our distributors may not devote sufficient resources to the sale of products;
- our distributors may be unsuccessful in marketing our products;
- our existing relationships with distributors may preclude us from entering into additional future arrangements with other distributors; and
- we may not be able to negotiate future distributor agreements on acceptable terms.

We may be subject to third-party claims that require additional licenses for our products and we could face costly litigation, which could cause us to pay substantial damages and limit our ability to sell some or all of our products.

Our industry is characterized by a large number of patents, claims of which appear to overlap in many cases. As a result, there is a significant amount of uncertainty regarding the extent of patent protection and infringement. Companies may have pending patent applications, which are typically confidential for the first eighteen months following filing, that cover technologies we incorporate in our products. Accordingly, we may be subjected to substantial damages for past infringement or be required to modify our products or stop selling them if it is ultimately determined that our products infringe a third party's proprietary rights. Moreover, from time to time, we receive correspondence and other communications from companies that ask us to evaluate the need for a license of patents they hold, and indicating or suggesting that we need a license to their patents in order to offer our products and services or to conduct our business operations. Even if we are successful in defending against claims, we could incur substantial costs in doing so. Any litigation related to claims of patent infringement could consume our resources and lead to significant damages, royalty payments or an injunction on the sale of certain products. Any additional licenses to patented technology could obligate us to pay substantial additional royalties, which could adversely impact our product costs and harm our business.

If we fail to maintain and protect our intellectual property rights, our competitors could use our technology to develop competing products and our business will suffer.

Our competitive success will be affected in part by our continued ability to obtain and maintain patent protection for our inventions, technologies and discoveries, including our intellectual property that includes technologies that we license. Our ability to do so will depend on, among other things, complex legal and factual questions. We have patents related to some of our technology and have licensed some of our technology under patents of others. We cannot assure you that our patents and licenses will successfully preclude others from using our technology. Our pending patent applications may lack priority over applications submitted by third parties or may not result in the issuance of patents. Even if issued, our patents may not be sufficiently broad to provide protection against competitors with similar technologies and may be challenged, invalidated or circumvented.

In addition to patents, we rely on a combination of trade secrets, copyright and trademark laws, nondisclosure agreements, licenses and other contractual provisions and technical measures to maintain and develop our competitive position with respect to intellectual property. Nevertheless, these measures may not be adequate to safeguard the technology underlying our products. For example, employees, consultants and others who participate in the development of our products may breach their agreements with us regarding our intellectual property, and we may not have adequate remedies for the breach. We also may not be able to effectively protect our intellectual property rights in some foreign countries, as many countries do not offer the same level of legal protection for intellectual property as the United States. Furthermore, for a variety of reasons, we may decide not to file for patent, copyright or trademark protection outside of the United States. Our trade secrets could become known through other unforeseen means. Notwithstanding our efforts to protect our intellectual property, our competitors may independently develop similar or alternative technologies or products that are equal or superior to our technology. Our competitors may also develop similar products without infringing on any of our intellectual property rights or design around our proprietary technologies. Furthermore, any efforts to enforce our proprietary rights could result in disputes and legal proceedings that could be costly and divert attention from our business.

The United States Government has certain rights to use and disclose some of the intellectual property that we license and could exclusively license it to a third party if we fail to achieve practical application of the intellectual property.

Aspects of the technology licensed by us under agreements with third party licensors may be subject to certain government rights. Government rights in inventions conceived or reduced to practice under a government-funded program may include a non-exclusive, royalty-free worldwide license to practice or have practiced such inventions for any governmental purpose. In addition, the U.S. government has the right to require us or our licensors (as applicable) to giant licenses which shall be exclusive under any of such inventions to a third party if they determine that: (i) adequate steps have not been taken to commercialize such inventions in a particular field of use; (ii) such action is necessary to meet public health or safety needs; or (iii) such action is necessary to meet requirements for public use under federal regulations. Further, the government rights include the right to use and disclose, without limitation, technical data relating to licensed technology that was developed in whole or in part at government expense. At least one of our technology license agreements contains a provision recognizing these government rights.

We may need to initiate lawsuits to protect or enforce our patents, which would be expensive and, if we lose, may cause us to lose some, if not all, of our intellectual property rights, and thereby impair our ability to compete.

We rely on patents to protect a large part of our intellectual property. To protect or enforce our patent rights, we may initiate patent litigation against third parties, such as infringement suits or interference proceedings. These lawsuits could be expensive, take significant time and divert management's attention from other business concerns. They would also put our patents at risk of being invalidated or interpreted narrowly, and our patent applications at risk of not issuing. We may also provoke these third parties to assert claims against us. Patent law relating to the scope of claims in the technology fields in which we operate is still evolving and, consequently, patent positions in our industry are generally uncertain. We cannot assure you that we would prevail in any of these suits or that the damages or other remedies awarded, if any, would be commercially valuable. During the course of these suits, there may be public announcements of the results of hearings, motions and other interim proceedings or developments in the litigation. Any public announcements related to these suits could cause our stock price to decline.

Our sales cycle can be lengthy, which can cause variability and unpredictability in our operating results.

The sales cycles for our systems products can be lengthy, which makes it more difficult for us to accurately forecast revenues in a given period, and may cause revenues and operating results to vary significantly from period to period. Sales of our products to the Industrial market often involve purchasing decisions by large public and private institutions, and any purchases can require many levels of pre-approval. In addition, many of these sales depend on these institutions receiving research grants from various federal agencies, which grants vary considerably from year to year in both amount and timing due to the political process. As a result, we may

expend considerable resources on unsuccessful sales efforts or we may not be able to complete transactions on the schedule anticipated.

Our international operations subject us to additional risks and costs.

Our international operations have expanded recently. These operations are subject to a number of difficulties and special costs, including:

- compliance with multiple, conflicting and changing governmental laws and regulations;
- laws and business practices favoring local competitors;
- potential for exchange and currency risks;
- potential difficulty in collecting accounts receivable;
- import and export restrictions and tariffs;
- difficulties staffing and managing foreign operations;
- difficulties and expense in enforcing intellectual property rights;
- business risks, including fluctuations in demand for our products and the cost and effort to conduct international operations and travel abroad to promote international distribution, and global economic conditions;
- multiple conflicting tax laws and regulations; and
- political and economic instability.

We intend to expand our international sales and marketing activities, including through our subsidiary in France, and enter into relationships with additional international distribution partners. We may not be able to attract international distribution partners that will be able to market our products effectively.

Our international operations could also increase our exposure to international laws and regulations. If we cannot comply with foreign laws and regulations, which are often complex and subject to variation and unexpected changes, we could incur unexpected costs and potential litigation. For example, the governments of foreign countries might attempt to regulate our products and services or levy sales or other taxes relating to our activities. In addition, foreign countries may impose tariffs, duties, price controls or other restrictions on foreign currencies or trade barriers, any of which could make it more difficult for us to conduct our business.

The nature of some of our products may also subject us to export control regulation by the US Department of State and the Department of Commerce. Violations of these regulations can result in monetary penalties and denial of export privileges.

Our SmartCycler and GeneXpert products are marketed in Europe under the CE IVD mark, and we intend to introduce additional products under the CE IVD mark as we pursue our expansion plans. Our use of the CE IVD mark is based on self declarations of conformity with stated directives and standards of the European Parliament and Council and is subject to review by competent authorities in Europe. Our recently acquired subsidiary, Cepheid AB, successfully introduced CE IVD-marked products that require independent third party review recognized by competent authorities, for example, a CMV test for use on our SmartCycler instrument. Any finding of non-conformity under such a review could prevent or otherwise adversely affect our ability to market products in Europe and result in other consequences, including both criminal sanctions, such as the imposition of fines or penalties, and civil claims for damages from persons suffering damage as a result of the non-conformity.

If we fail to retain key members of our staff, our ability to conduct and expand our business would be impaired.

We are highly dependent on the principal members of our management and scientific staff. The loss of services of any of these persons could seriously harm our product development and commercialization efforts. In addition, we require skilled personnel in areas such as microbiology, clinical and sales, marketing and finance. Attracting, retaining and training personnel with the requisite skills remains challenging, and, as general economic conditions improve, is becoming increasingly competitive, particularly in the Silicon Valley area of California where our main office is located. If at any point we are unable to hire, train and retain a sufficient number of qualified employees to match our growth, our ability to conduct and expand our business could be seriously reduced.

If we become subject to claims relating to improper handling, storage or disposal of hazardous materials, we could incur significant cost and time to comply.

Our research and development processes involve the controlled storage, use and disposal of hazardous materials, including biological hazardous materials. We are subject to foreign, federal, state and local regulations governing the use, manufacture, storage, handling and disposal of materials and waste products. We may incur significant costs complying with both existing and future environmental laws and regulations. In particular, we are subject to regulation by the Occupational Safety and Health Administration ("OSHA") and the Environmental Protection Agency ("EPA"), and to regulation under the Toxic Substances Control Act and the Resource Conservation and Recovery Act in the United States. OSHA or the EPA may adopt regulations that may affect our research and development programs. We are unable to predict whether any agency will adopt any regulations that would have a material adverse effect on our operations.

The risk of accidental contamination or injury from hazardous materials cannot be eliminated completely. In the event of an accident, we could be held liable for any damages that result, and any liability could exceed the limits or fall outside the coverage of our workers' compensation insurance. We may not be able to maintain insurance on acceptable terms, if at all.

If a catastrophe strikes our manufacturing facilities, we may be unable to manufacture our products for a substantial amount of time and we would experience lost revenue.

Our manufacturing facilities are located in Sunnyvale, California, Bromma, Sweden, and Bothell, Washington. Although we have business interruption insurance, our facilities and some pieces of manufacturing equipment are difficult to replace and could require substantial replacement lead-time. Various types of disasters, including earthquakes, fires, floods and acts of terrorism, may affect our manufacturing facilities. Earthquakes are of particular significance since our primary manufacturing facilities in California are located in an earthquake-prone area. In the event our existing manufacturing facilities or equipment is affected by man-made or natural disasters, we may be unable to manufacture products for sale or meet customer demands or sales projections. If our manufacturing operations were curtailed or ceased, it would seriously harm our business.

We might require additional capital to support business growth, and such capital might not be available.

We may need to engage in additional equity or debt financing to support business growth and respond to business challenges, which include the need to develop new products or enhance existing products, conduct clinical trials, enhance our operating infrastructure and acquire complementary businesses and technologies. Equity and debt financing, however, might not be available when needed or, if available, might not be available on terms satisfactory to us. In addition, to the extent that additional capital is raised through the sale of equity or convertible debt securities, the issuance of these securities could result in dilution to our shareholders. In addition, these securities may be sold at a discount from the market price of our common stock and may include rights, preferences or privileges senior to those of our common stock. If we are unable to obtain adequate financing or financing on terms satisfactory to us, our ability to continue to support our business growth and to respond to business challenges could be significantly limited.

Compliance with regulations governing public company corporate governance and reporting is complex and expensive.

Many laws and regulations, notably those adopted in connection with the Sarbanes-Oxley Act of 2002 by the SEC and the NASDAQ Global Market, impose obligations on public companies, such as ours, which have increased the scope, complexity, and cost of corporate governance, reporting, and disclosure practices. Our implementation of these reforms and enhanced new disclosures has required and will continue to require substantial management time and oversight and requires us to incur significant additional accounting and legal costs.

Our business could be harmed by adverse economic conditions in our target markets or reduced spending in our industry.

Our business depends on the overall demand in our industry. The markets we serve are emerging and the purchase of our products can be discretionary. Weak economic conditions in our target markets, or a reduction in spending in our industry even if economic conditions improve, would likely adversely impact our business, operating results and financial condition in a number of ways, including lower prices for our products and reduced unit sales.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

In Sunnyvale, California, the base for our manufacturing, product support and research and development efforts, we lease approximately 76,000 square feet of office and laboratory space pursuant to a lease that expires in March 2012, sublease approximately 25,100 square feet of office and manufacturing space pursuant to a sublease that expires in September 2009. We also sublease 21,750 square feet to support warehousing and distribution efforts pursuant to a sublease that expires in September 2010. In Bothell, Washington we sublease approximately 16,000 square feet of laboratory space for advanced chemistry research and development pursuant to a sublease that expires in August 2011. Outside of Toulouse, France we own an 18,800 square-foot building and lease approximately 2,300 square feet of office space pursuant to a lease that expires in December 2008. In Bromma, Sweden we lease approximately 45,200 square feet of office and manufacturing space pursuant to a lease that expires in December 2009 and lease approximately 1,800 square feet of office space that expires in September 2011. We believe we will be able to obtain additional facilities space on commercially-reasonable terms, if and when they are required.

ITEM 3. LEGAL PROCEEDINGS

We are not currently a party to any material legal proceedings.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders in the last quarter of 2007.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF THE EQUITY SECURITIES

PRICE RANGE OF COMMON STOCK

Our common stock has been traded on the NASDAQ Global Market since our initial public offering on June 21, 2000 under the symbol CPHD. The high and low sale prices for our common stock for each quarter of our two most recent fiscal years, as reported on the NASDAQ Global Market, were as follows:

	High	Low
Fiscal year ended December 31, 2007		
First Quarter	$ 12.27	$ 7.40
Second Quarter	14.92	10.66
Third Quarter	23.41	14.05
Fourth Quarter	27.91	19.13
Fiscal year ended December 31, 2006		
First Quarter	$ 10.70	$ 8.25
Second Quarter	10.20	8.39
Third Quarter	9.82	6.50
Fourth Quarter	10.00	6.65

On February 15, 2008, the last reported sale price of our common stock on the NASDAQ Global Market was $31.33 per share. On February 15, 2008, there were approximately 170 holders of record of our common stock. The actual number of shareholders is greater than the number of record holders, and includes shareholders who are beneficial owners, but whose shares are held in street name by brokers and other nominees. The number of holders of record also does not include shareholders whose shares may be held in trust by other entities.

We have never declared or paid any cash dividends on our capital stock. We currently intend to retain future earnings, if any, for development of our business and, therefore, do not anticipate that we will declare or pay cash dividends on our capital stock in the foreseeable future.

EQUITY COMPENSATION PLAN INFORMATION

The following table summarizes information about our equity compensation plans as of December 31, 2007. All outstanding awards relate to our common stock.

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuances under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders (1)(2)(3)	8,904,662	$8.48	1,643,568
Equity compensation plans not approved by security holders	—	—	—
Total	8,904,662	$8.48	1,643,568

(1) The number of securities remaining available for future issuance in column (c) includes 155,489 shares of common stock authorized and available for issuance under our Employee Stock Purchase Plan ("ESPP"). The number of shares authorized for issuance under the ESPP is subject to an annual increase equal to the lesser of 200,000 shares, 0.75% of the outstanding shares on the date of the annual increase or a lesser amount determined by the Board of Directors. The number of securities to be issued to participants in column (a) does not include shares of common stock to be issued to participants in consideration of aggregate participant contributions under the ESPP as of December 31, 2007.

(2) We issue securities under our 2006 Equity Incentive Plan ("2006 Plan") in forms other than options, warrants or rights. We may issue stock awards, including but not limited to restricted stock awards, restricted stock units, stock bonus awards, stock appreciation rights and performance share awards. Under the 2006 Plan, non-employee directors are automatically granted options to purchase 25,000 shares of common stock upon initial election or appointment to the Board. On the date of the first Board meeting following each annual shareholder meeting each non-employee director then in office for longer than six months will automatically be granted options to purchase 12,500 shares of common stock. The Board may also make discretionary grants to purchase common stock to any non-employee director. Under the terms of our 2006 Plan, each award other than a stock option or stock appreciation right will reduce the number of shares remaining available for future issuance in column (c) by 1.6 shares for each share subject to such award.

(3) We have made awards of restricted stock under our 2006 Plan in forms which do not require a payment by the recipient to us at the time of exercise or vesting. Accordingly, the weighted average exercise price in column (b) does not take these awards into consideration.

STOCK PRICE PERFORMANCE GRAPH

The following graph is furnished to, but not filed with, the Securities and Exchange Commission and shows the total shareholder return of an investment of $100 in cash on December 31, 2002, through December 31, 2007, the last date of trading of fiscal 2007 for (1) Cepheid's common stock, (2) the NASDAQ Biotechnology Index and the NASDAQ Composite Index. All values assume reinvestment of the full amount of all dividends. No cash dividends have been declared on shares of Cepheid's common stock. Shareholder returns over the indicated period are based on historical data and are not necessarily indicative of future shareholder returns.

Total Return Analysis	12/31/2002	12/31/2003	12/31/2004	12/31/2005	12/31/20065	12/31/2007
Cepheid	$100.00	$187.92	$194.98	172.22	$166.73	$516.87
Nasdaq Biotechnology	$100.00	$145.75	154.68	$159.06	$160.69	$168.05
Nasdaq Composite	$100.00	$150.01	$162.89	$165.13	$180.85	$198.60

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data have been derived from our audited consolidated financial statements. The information below is not necessarily indicative of the results of future operations, and should be read in conjunction with Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Form 10-K and the consolidated financial statements and related notes thereto included in Item 8 of this Form 10-K in order to fully understand factors that may affect the comparability of the information presented below.

	Years Ended December 31,				
	2007	2006	2005	2004	2003
	(In thousands, except per share data)				
Consolidated Statements of Operations Data:					
Revenues:					
Product sales	$116,532	$ 82,403	$ 80,440	$ 49,967	$ 15,817
Contract revenues	8,554	3,913	3,062	2,967	638
Grants and government sponsored research revenue	4,387	1,036	1,508	34	2,079
Total revenues	129,473	87,352	85,010	52,968	18,534
Costs and operating expenses:					
Cost of product sales (1)	69,174	48,800	46,232	27,541	8,628
Collaboration profit sharing	12,256	14,974	14,483	6,096	262
Research and development (1)	31,449	23,886	18,961	15,903	15,330
In-process research and development	—	139	—	—	—
Selling, general and administrative (1)	41,081	26,470	18,901	16,134	11,872
Expense for patent related matter	—	3,350	—	1,264	—
Total costs and operating expenses	153,960	117,619	98,577	66,938	36,092
Loss from operations	(24,487)	(30,267)	(13,567)	(13,970)	(17,558)
Other income (expenses):					
Interest income	2,731	4,402	1,413	675	60
Interest expense	(22)	(367)	(1,082)	(693)	(179)
Foreign currency exchange gain (loss) and other	568	247	(358)	188	146
Other income (expense), net	3,277	4,282	(27)	170	27
Net loss, before income tax expense	(21,210)	(25,985)	(13,594)	(13,800)	(17,531)
Income tax expense	(213)	—	—	—	—
Net loss	$ (21,423)	$ (25,985)	$ (13,594)	$ (13,800)	$ (17,531)
Basic and diluted net loss per common share	$ (0.39)	$ (0.50)	$ (0.32)	$ (0.34)	$ (0.53)
Shares used in computing basic and diluted net loss per share	55,263	52,325	42,494	41,083	33,367
(1) Amounts reported include stock-based compensation cost as follows:					
Cost of product sales	$ 794	$ 584	$ —	$ —	$ —
Research and development	4,294	2,839	—	16	68
Selling, general and administrative	6,032	3,907	—	—	31
	$ 11,120	$ 7,330	$ —	$ 16	$ 99

In February 2007, we acquired Sangtec Molecular Diagnostics AB ("Sangtec"). The consolidated statements of operations data above and the following consolidated balance sheet data include the balance sheet of Sangtec as of December 31, 2007 and the results of its operations subsequent to the February 14, 2007 acquisition date. See Note 7—Acquisitions to the consolidated financial statements appearing in Item 15 to this annual report.

	December 31,				
	2007	2006	2005	2004	2003
			(In thousands)		
Consolidated Balance Sheet Data:					
Cash and cash equivalents and marketable securities	$ 44,026	$ 94,936	$ 37,222	$ 57,439	$ 18,510
Restricted cash	661	661	661	688	688
Working capital	56,109	90,362	19,561	45,217	21,839
Total assets	165,245	167,661	103,188	120,315	41,558
Long-term obligations	2	44	2,439	14,165	1,978
Accumulated deficit	(154,909)	(133,486)	(107,501)	(93,907)	(80,107)
Total shareholders' equity	126,935	132,706	55,403	65,609	20,075

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 that relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "intend", "potential" or "continue" or the negative of these terms or other comparable terminology. Forward-looking statements are based upon current expectations that involve risks and uncertainties. Our actual results and the timing of events could differ materially from those anticipated in our forward-looking statements as a result of many factors, including, but not limited to, the following: development and manufacturing problems; the need for additional licenses for new tests and other products and the terms of such licenses; our ability to successfully sell products in the Clinical Molecular Diagnostic market; lengthy sales cycles in certain markets; the performance and market acceptance of our new products; our ability to obtain regulatory approvals and introduce new products into the Clinical Molecular Diagnostic market; our reliance on distributors to market, sell and support our products; the occurrence of unforeseen expenditures, asset impairments, acquisitions or other transactions; our ability to integrate the businesses, technologies, operations and personnel of acquired companies; the scope and timing of actual United States Postal Service ("USPS") funding of the Biohazard Detection System ("BDS") in its current configuration; the rate of environmental testing using the BDS conducted by the USPS, which will affect the amount of consumable products sold; our success in increasing our direct sales; the impact of competitive products and pricing; our ability to manage geographically-dispersed operations; underlying market conditions worldwide; and the other risks set forth under "Risk Factors" and elsewhere in this report. We assume no obligation to update any of the forward-looking statements after the date of this report or to conform these forward-looking statements to actual results.

OVERVIEW

We are a molecular diagnostics company that develops, manufactures, and markets fully-integrated systems for genetic analysis in the Clinical Molecular Diagnostic, Industrial and Biothreat markets. Our systems enable rapid, sophisticated molecular testing for organisms and genetic-based diseases by automating otherwise complex manual laboratory procedures. We are focusing our efforts on those applications where rapid molecular testing is particularly important, such as identifying infectious disease and cancer in the Clinical Molecular Diagnostic market; food, agricultural and environmental testing in the Industrial market; and identifying bio-terrorism agents in the Biothreat market.

Our two principal instrument platforms are our SmartCycler and GeneXpert systems. The SmartCycler system, integrates DNA amplification and detection to allow rapid analysis of a sample. The GeneXpert system integrates automated sample preparation with our SmartCycler DNA amplification and detection technology and is a closed, self-contained, fully-integrated and automated system.

Licenses and Strategic Relationships

In December 2003, we entered into an agreement for a strategic commercial relationship with bioMerieux in which bioMerieux is to develop DNA testing products using their proprietary Nucleic Acid Sequence-Based Amplification technology to be run on systems employing our GeneXpert systems. Under the agreement, bioMerieux has paid us a $10.0 million license fee, and an additional $5.0 million payment will become due when and if bioMerieux commercializes its first product based on our technology. We may also receive potential product purchases and royalty payments on end-user GeneXpert test cartridge sales if any such products are introduced under the agreement. The $10.0 million license fee received from bioMerieux was deferred and is being amortized over the period of approximately five years.

In April 2004, we entered into a patent license agreement with Applera, through its ABI and its Celera Diagnostics joint venture, and, effective July 1, 2004, we entered into a patent license agreement with F. Hoffmann-La Roche Ltd. ("Roche"), each of which provides for non-exclusive worldwide licenses to make, use, and sell our products incorporating technologies covered by Applera's and Roche's respective patents. Under the license agreements, we agreed to pay aggregate license fees of $32.2 million, which was fully paid as of December 31, 2006. We also agreed to pay Applera and Roche ongoing royalties on sales of products incorporating their licensed patents. In connection with the license agreements, we recorded intangible assets of $31.1 million, representing the present value of license fee obligations net of imputed interest of $1.1 million. In June 2006, the Applera patent license agreement was expanded to include additional products, for which we paid an additional $0.5 million. The intangible assets related to the Applera and Roche licenses are being amortized on a straight-line basis over their useful lives of approximately 10 and 15 years, respectively, with the amortization recorded as part of the cost of product sales.

In September 2005, we entered into a license agreement with Abaxis, effective as of September 30, 2005, pursuant to which Abaxis granted us a non-exclusive, worldwide, royalty-bearing license to certain Abaxis patents relating to lyophilization technology. In exchange for the license rights, we agreed to (i) make an upfront license payment, (ii) pay royalties during the term of the agreement and (iii) pay a yearly license maintenance fee during the term of the agreement, which fee will be creditable against any royalties due during such calendar year.

In November 2005, we entered into a license agreement with DxS Limited ("DxS"), a private United Kingdom based company, pursuant to which DxS granted us a non-exclusive, worldwide, royalty-bearing license to the DxS scorpions patents and other intellectual property rights relating to its Scorpions technology for the real-time PCR detection of nucleic acid amplification, including, the human in vitro diagnostics field.

In September 2006, we entered into a sublicense agreement with Abbott Laboratories ("Abbott"), pursuant to which Abbott granted us a non-exclusive, world-wide, non-transferable right to Abbott's exclusive license to certain patents from the Baylor College of Medicine. Under the sublicense agreement, we will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as multiple genomic DNA amplification for deletion detection. In September 2006, Cepheid also entered into a license agreement with Abbott, pursuant to which Abbott granted us a non-exclusive, world-wide, non-transferable right to a certain Abbott patent. Under the license agreement, we will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as detection of cervical chlamydia trachomatis infection. License payments for these agreements totaled $2.0 million.

In December 2006, we entered into a contract with the Centers for Disease Control and Prevention ("CDC") for the first two phases of a five phase program for the development of a new Point-of-Care *in vitro* diagnostic product that tests for influenza viruses A and B, and H5N1, providing general clinical utility for seasonal flu diagnosis in addition to its application in the case of an avian flu pandemic. Under the first two phases of the program, we were responsible for developing a pre-clinical development plan, a clinical development and a regulatory plan. In September 2007, the contract was terminated.

In January 2007, we entered into two agreements with bioMerieux SA a sublicense agreement and a collaboration agreement. Pursuant to the sublicense agreement, bioMerieux SA granted us a non-exclusive, worldwide, irrevocable sublicense to certain patents that relate to the diagnosis of methicillin resistant staphylococcus aureus ("MRSA"). We will be able to use the licensed rights to develop and sell products for use in connection with our GeneXpert and SmartCycler platforms. In exchange for such rights, we agreed to pay an initial license fee of approximately $4.0 million and quarterly royalties based on net product sales during the term of the sublicense agreement. The collaboration agreement is for the development, production and marketing of a line of sepsis and hospital acquired pneumonia products, based upon our real-time PCR technologies. Both companies will jointly develop the products. We will exclusively manufacture these Cepheid products at an agreed upon price for bioMerieux SA, who will market and distribute the products on an exclusive worldwide basis.

In August 2007, we entered into a five-year master purchase order with Northrop Grumman for the purchase of up to $200 million in anthrax test cartridges and associated materials. The anthrax test is currently used in BDS units installed at USPS mail processing centers nationwide. The agreement covers the USPS fiscal years of 2007 through 2011. Under the terms of the agreement, the purchase quantity of anthrax tests will be determined on an annual basis, based on the USPS fiscal year of October 1 through September 30. We have received notice that expected test purchases for fiscal 2008 will be approximately two million cartridges.

In September 2007, we entered into two Veterans Affairs Federal Supply Service Schedule ("VA/FSS") contracts for our GeneXpert system and the Xpert MRSA test for the rapid detection of Methicillin-resistant Staphylococcus aureus. The two contracts, VA/FSS 65 VII and GSA 66, respectively, cover the purchase of Xpert MRSA tests and GeneXpert systems. These two contracts are expected to streamline the acquisition process and ensure that VA hospitals and other federal agencies can purchase GeneXpert systems and Xpert MRSA test kits without individual negotiations as they await funding for the next fiscal year.

In November 2007, we signed a group purchasing contract with Broadlane, Inc., a leading supply chain services company serving more than 20,000 acute care hospitals, ambulatory care facilities, physicians' practices and other healthcare providers throughout the United States. Under the terms of the contract, Broadlane, Inc. customers can take advantage of our molecular diagnostic instruments, reagents and services for our GeneXpert system and Xpert line of tests, including Xpert MRSA.

Acquisitions

In August 2006, we, through our wholly owned French subsidiary, Cepheid SA, purchased 100% of the stock of Actigenics SA ("Actigenics"), a French micro RNA research and services company. The acquisition was accounted for as a purchase transaction in accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations" ("SFAS 141"); accordingly, the results of Actigenics operations have been included in our consolidated results of operations from the date of acquisition. The purchase amount paid was $1.2 million in cash, of which 10% was retained for a period of one year from the purchase date as security for the seller's indemnification obligations. In addition, Cepheid assumed approximately $0.7 million of liabilities, offset by approximately $0.2 million of assets. The marker technology and discovery and validation technology acquired in this acquisition will be amortized on a straight-line basis over ten and six year periods, respectively. Immediately subsequent to the acquisition date, in accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 4, "Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method—an interpretation of FASB Statement No. 2", $0.1 million of in-process research and development intangible assets with no alternative future uses were written off.

In February 2007, we completed the purchase of 100% of the outstanding stock of Sangtec Molecular Diagnostics AB ("Sangtec"), a company located in Bromma, Sweden, from Nycomed-owned Altana Technology Projects GmbH. Sangtec is a PCR molecular diagnostics company that develops and manufactures products for standardized nucleic acid testing of infectious diseases. The acquisition will allow us to provide a line of products for potential use in managing infections of immuno-compromised patients, a research and development operation to develop and expand our clinical test products, and a reagent manufacturing base in Europe. Subsequent to the acquisition, Sangtec's name was changed to Cepheid AB. The acquisition was accounted for as a purchase transaction in accordance with SFAS 141; accordingly, the results of Cepheid AB operations have been included in our consolidated results of operations from the date of acquisition. The purchase price of the acquisition was approximately $27.5 million, including $26.7 million cash (net of cash acquired) and $0.8 million direct acquisition costs.

Sales Channels

We sell our products both direct and through other distribution channels. In the United States, we sell through our direct sales force in the Clinical Molecular Diagnostic and Industrial markets, as well as through non-exclusive distributors in the Industrial market. Additional sales occur through our arrangements with BD-GeneOhm and Veridex. In Europe, our products are sold direct and through distributors. In Japan and other parts of the world, we sell solely through distributors. Through our French subsidiary, Cepheid SA, additional distributors have been established in Europe, the Middle East, Western Asia and Africa. We expect to continue expanding our sales efforts into other territories throughout the world.

Research and Development

Since our inception, we have devoted significant resources to research and development, particularly in developing the technologies for our SmartCycler and GeneXpert systems and, more recently, developing tests and ASRs for use on those systems. Research and development expenses were approximately $19.0 million in 2005, $23.9 million in 2006 and $31.4 million in 2007. We expect that our research and development expenses in 2008 will increase in line with our contract and collaborator revenues and as we complete clinical trials for our MRSA/SA products, Factors II and V, C. difficile and VRE tests and continue research on other tests.

Revenues

Currently, we derive our revenues primarily from the sales of our two instrument systems and associated reagents and disposables in the Clinical Molecular Diagnostic, Industrial, and Biothreat markets, and to a lesser extent from contract and government sponsored research.

CRITICAL ACCOUNTING POLICIES, ESTIMATES AND ASSUMPTIONS

We consider our accounting policies related to revenue recognition, impairment of intangible assets and goodwill, inventory valuation, warranty accrual and stock based compensation to be critical accounting policies. A number of significant estimates, assumptions, and judgments are inherent in our determination of when to recognize revenue, how to evaluate our intangible assets and goodwill, and the calculation of our inventory valuation adjustments, warranty accrual, and stock-based compensation expense. These estimates, assumptions and judgments include deciding whether the elements required to recognize revenue from a particular

arrangement are present, estimating the fair value of an intangible asset, which represents the future undiscounted cash flows to be derived from the intangible asset, estimating the amount of inventory obsolescence and warranty costs associated with shipped products and estimating the useful life and volatility of stock awards granted. We base our estimates and judgments on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ materially from these estimates.

Revenue Recognition

We recognize revenue from the sale of our products and contract arrangements. Our revenue arrangements with multiple elements are divided into separate units of accounting if certain criteria are met, including whether the delivered element has stand-alone value to the customer and whether there is objective and reliable evidence of the fair value of the undelivered items. The consideration we receive is allocated among the separate units based on their respective fair values, and the applicable revenue recognition criteria are applied to each of the separate units. Advance payments received in excess of amounts earned are classified as deferred revenue until earned.

Determining whether the criteria for recognizing revenue have been met, including, for example, determining whether there is sufficient evidence that an arrangement exists, the collectibility of billings are reasonably assured and whether contractual performance obligations and milestones have been satisfied, requires us to make estimates, assumptions and judgments that affect our operating results. For example, our determination of the probability of collection is based upon assessment of the customer's financial condition through review of their current financial statements or publicly-available credit reports, as well as approvals from government agencies and availability of budgets. For sales to existing customers, prior payment history is also considered in assessing probability of collection. We are required to exercise significant judgment in deciding whether collectibility is reasonably assured, and such judgments may materially affect the timing of our revenues and our results of operations.

Product sales. We recognize revenue from product sales when goods are shipped, there is persuasive evidence that an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is reasonably assured. No right of return exists for our products except in the case of damaged goods. We have not experienced any significant returns of our products.

Contract revenues. Contract revenues consist of fees earned under technology license arrangements, services rendered under research and development arrangements, grants and government sponsored research agreements, and milestone payments and royalties received under license and collaboration agreements. Deferred revenue is recorded when funds are received in advance of technologies to be delivered or services to be performed.

License revenue is generally recognized only after both the license period has commenced and the technology has been delivered. However, in multiple-element revenue arrangements, if the delivered technology does not have stand-alone value or if we do not have objective and reliable evidence of the fair value of the undelivered products or services, the amount of revenue allocable to the delivered technology is deferred and amortized over the related involvement period in which the remaining products or services are provided to the customer.

Research and development and government sponsored research contract revenues are recognized as the related services are performed based on the performance requirements of the relevant contract. Under the agreements, we are required to perform specific research and development activities and are compensated either based on the costs or costs plus a mark-up associated with each specific contract over the term of the agreement.

Incentive milestone payments are recognized as revenue upon the achievement of the specified milestone, assuming there are no continuing performance obligations related to that milestone. Incentive milestone payments are substantially at risk at the inception of the arrangement and are normally triggered by events external to Cepheid.

Royalties are typically based on licensees' net sales of products that utilize our technology and are recognized as earned in accordance with the contract terms when royalties from licensees can be reliably measured and collectibility is reasonably assured, such as upon the receipt of a royalty statement from the customer.

Service revenue is recognized when the services have been provided.

Impairment of Intangible Assets and Goodwill

Our intangible assets consist primarily of rights to certain patented technologies that we purchased. Intangible assets are recorded at cost, less accumulated amortization. Intangible assets are amortized over their estimated useful lives, ranging from 5 to 20 years, on

a straight-line basis except for intangible assets acquired in the acquisition of Sangtec, which are amortized on the basis of economic useful life. Amortization of intangible assets is primarily included in cost of product sales in the consolidated statements of operations.

We review our intangible assets for impairment under SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". We conduct an impairment review when events or circumstances indicate the carrying value of a long-lived asset may be impaired, by estimating the future undiscounted cash flows to be derived from an asset to assess whether or not a potential impairment exists. If the carrying value exceeds our estimate of future undiscounted cash flows, we then calculate the impairment as the excess of the carrying value of the asset over our estimate of its fair market value. Events or circumstances which could trigger an impairment review include a significant adverse change in business climate, an adverse action or assessment by a regulator, unanticipated competition, significant changes in the manner of our use of acquired assets, the strategy for our overall business, or significant negative industry or economic trends. There is significant judgment in estimating future cash flows and fair value. There were no impairment charges recorded in the three year period ended December 31, 2007.

We annually review our goodwill for impairment under SFAS No. 142, "Goodwill and Other Intangible Assets". If our fair value exceeds our net book value including goodwill, then goodwill is not considered impaired. The initial step is to compare our fair value as determined by our market capitalization to our net book value. If the market capitalization exceeds the net book value, goodwill is presumed to be unimpaired. Otherwise, we would estimate expected future cash flows of our business, which operates in a number of markets and geographical regions. We would then determine the carrying value of our business and compare the carrying value including goodwill and other intangibles to the discounted future cash flows. If the total of future cash flows is less than the carrying amount of the assets, we would recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets. Estimates of the future cash flows associated with the assets are critical to these assessments. Changes in these estimates based on changed economic conditions or business strategies could result in material impairment charges in future periods. At December 31, 2007, we compared our market value to our net book value and determined that goodwill was not impaired as the fair value exceeded the net book value.

Inventory and Warranty Provisions

We maintain provisions for inventory obsolescence and warranty costs that we believe are reasonable and that are based on our historical experience and current expectations for future performance. The inventory provision is established using management's estimate of the potential future obsolescence or excess inventory. A substantial decrease in demand for our products or the introduction of new products could lead to excess inventories and could require us to increase our provision for inventory obsolescence. Our current estimates and assumptions are consistent with prior periods. In the past, there have not been significant adjustments of the actual results to our estimates.

We warrant our instrument products to be free from defects for a period of 12 to 15 months from the date of sale and its disposable products to be free from defects, when handled according to product specifications, for the stated life of such products. Accordingly, a provision for the estimated cost of warranty repair or replacement is recorded at the time revenue is recognized. Our warranty provision is established using management's estimate of future failure rates and of the future costs of repairing any instrument failures during the warranty period or replacing any disposable products with defects. Significant increases in the failure rates of our products could lead to increased warranty costs and require us to increase our warranty provision. As of December 31, 2007 and 2006, the accrued warranty liability was $0.5 million and $0.3 million, respectively.

Stock Based Compensation

Effective January 1, 2006, we adopted the fair value recognition provisions of SFAS No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123(R)") using the modified prospective transition method. Under the modified prospective transition method, prior periods are not restated for the effect of SFAS 123(R). Commencing with the first quarter of 2006, compensation cost includes all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), and compensation for all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). We recognize the fair value of our stock option awards as compensation expense over the requisite service period of each award, which is generally four years. Compensation expense related to stock options granted prior to January 1, 2006 is accounted for under the recognition and measurement provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), and related interpretations, as permitted by SFAS 123.

Prior to the adoption of SFAS 123(R), we applied SFAS 123, amended by SFAS No. 148, "Accounting for Stock-Based Compensation — Transition and Disclosure" ("SFAS 148"), which allowed companies to apply the existing accounting rules under APB 25 and related interpretations. In general, as the exercise price of options granted under our plans was equal to the market price

of the underlying common stock on the grant date, no stock-based employee compensation cost was recognized in the consolidated financial statements for periods prior to the adoption of SFAS 123(R).

In determining fair value, we use the Black–Scholes model and a single option award approach, which requires the input of subjective assumptions. These assumptions include: estimating the length of time employees will retain their vested stock options before exercising them (expected term); the estimated volatility of our common stock price over the expected term (volatility), risk-free interest rate and the number of options that will ultimately not complete their vesting requirements (forfeitures). Changes in the following assumptions can materially affect the estimate of fair value of stock–based compensation.

- Expected term is determined based on historical experience, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior as influenced by changes to the terms of its stock-based awards.
- Expected volatility is based on the historical volatility for the past 5 years, which matches the expected term of the option grant.
- Risk-free interest rate is based on the implied yield currently available on U.S. Treasury zero-coupon issues with a remaining term equivalent to the expected term of a stock award.
- Estimated forfeitures are based on voluntary termination behavior as well as analysis of actual option forfeitures.

Recent Accounting Pronouncements

For recent accounting pronouncements, see Note 1—Organization and Summary of Significant Accounting Policies to the consolidated financial statements appearing in Item 15 to this annual report, which are incorporated by reference into this Item 7.

Results of Operations

Comparison of Years Ended December 31, 2007 and 2006

Revenues

	Years Ended December 31,		
	2007	2006	% Change
	(Amounts in thousands)		
Revenues:			
Instrument sales	$ 47,739	$ 22,737	110 %
Reagent and disposable sales	68,793	59,666	15 %
Total product sales	116,532	82,403	41 %
Contract revenues	8,554	3,913	119 %
Grant and government sponsored research revenue	4,387	1,036	323 %
Total Revenues	$129,473	$ 87,352	48 %

Product Sales

We operate in three market areas: Clinical Molecular Diagnostic, Industrial and Biothreat markets. The following table illustrates product sales in the three market areas as a percentage of total product sales:

	Years Ended December 31,	
	2007	2006
	(As a % of total product sales)	
Product sales by market:		
Clinical Molecular Diagnostic	52 %	24 %
Biothreat	35 %	58 %
Industrial	13 %	18 %
Total Product Sales	100 %	100 %

Total product sales increased 41% to $116.5 million in 2007 from $82.4 million in 2006. The increase in instrument sales was primarily due to an increase of $18.6 million of GeneXpert systems sales and $5.3 million Smart Cycler system sales. Instrument sales in Europe increased $5.9 million. The increase in reagent and disposable sales was primarily due to sales of $10.6 million of FDA-

approved GeneXpert disposable tests and from $7.1 million sales by Cepheid AB. Such increases were partially offset by reduced anthrax test cartridge sales of $7.5 million to Northrop Grumman/USPS in the Biothreat market. Product sales to Northrop Grumman/USPS represented 36% and 59% of our total product sales in 2007 and 2006, respectively. The following table provides a breakdown of our product sales by geographic regions:

	Years Ended December 31,	
	2007	2006
	(As a % of total product sales)	
Product Sales by Geographic Regions:		
North America	80 %	88 %
Europe	19 %	10 %
Japan and other	1 %	2 %
Total Product Sales	100 %	100 %

The change in product sales by geographic regions in 2007 compared to 2006 was primarily due to increases in both instrument and reagent and disposable sales in the European Clinical Molecular Diagnostic market.

No single country outside of the United States represented more than 10% of our total revenues in any period presented.

Contract Revenues

Contract revenues were $8.6 million in 2007 and $3.9 million in 2006 and include $1.9 million related to the amortization of license fees in conjunction with our collaboration agreement with bioMerieux, Inc., which are being recognized ratably over the period of approximately five years, which represents the estimated period of our continuing involvement under this agreement. The increase in revenues was primarily due to collaboration agreements which began in the second half of 2006.

Grants and Government Sponsored Research Revenue

Grants and government sponsored research revenue increased to $4.4 million in 2007 from $1.0 million in 2006. The revenue in 2007 was derived from programs with the Centers for Disease Control and Prevention ("CDC") and National Institutes of Health, revenues from which started in the first quarter of 2007. Such revenue increase was partially offset by decreased revenue from the completion of the National Cancer Institute program in 2006. Revenue derived from the program with the CDC, which terminated in September 2007, was $2.9 million in 2007 and $0.1 million in 2006.

Costs and Operating Expenses

	Years Ended December 31,		
	2007	2006	% Change
	(Amounts in thousands)		
Costs and operating expenses:			
Cost of product sales	$ 69,174	$ 48,800	42 %
Collaboration profit sharing	12,256	14,974	(18)%
Research and development	31,449	23,886	32 %
In-process research and development	—	139	(100)%
Selling, general and administrative	41,081	26,470	55 %
Expense for patent related matter	—	3,350	(100)%
Total costs and operating expenses	$153,960	$117,619	31 %

Cost of Product Sales

Cost of product sales consists of raw materials, direct labor and stock-based compensation expense, manufacturing overhead, facility costs and warranty costs. Cost of product sales also includes royalties on product sales and amortization of intangible assets related to technology licenses and intangibles acquired in the purchase of Sangtec and Actigenics. As a result of the increased product sales discussed above, cost of product sales increased 42% to $69.2 million in 2007 compared to $48.8 million in 2006. Our product gross margin was 41% in 2007 and 2006. The manufacturing efficiencies achieved in 2007 were offset primarily by increased expense related to amortization of intangible assets associated with the acquisition of Sangtec in 2007 and by stock-based compensation expense.

Collaboration Profit Sharing

Collaboration profit sharing represents the amount that we pay to ABI under our collaboration agreement to develop reagents for use in the USPS BDS. Under the agreement, computed gross margin on anthrax cartridge sales are shared equally between the two parties. The collaboration profit sharing was $12.3 million and $15.0 million in 2007 and 2006, respectively. The decrease in collaboration profit sharing was the result of decreased anthrax cartridge sales under the USPS BDS program, and this expense will remain proportional to the sales of anthrax cartridges under the USPS BDS program.

Research and Development Expenses

Research and development expenses consist of salaries and employee-related expenses, which include stock-based compensation, clinical trials, research and development materials, facility costs and depreciation. Research and development expenses increased 32% to $31.4 million in 2007 from $23.9 million in 2006. The increase in research and development expenses of $7.6 million was primarily due to a $4.5 million increase in salaries and employee-related expenses, including an increase of $1.3 million in stock-based compensation, resulting from our operational expansion in Europe and the United States, a $1.3 million increase in facility related costs and depreciation expense, a $0.6 million in direct material related costs, a $0.3 million increase in consulting costs, and a $0.3 million increase in travel related expenses. The increase in 2007 also reflects expansion in our contract, grants and government sponsored research activities and the impact of the Sangtec acquisition in 2007.

In-process Research and Development

In-process research and development of $0.1 million in 2006 represents the write-off of research and development intangible assets acquired in the acquisition of Actigenics in August 2006 that had no alternative future uses. No related expense was incurred in 2007.

Selling, General and Administrative Expenses

Selling, general and administrative expenses consist primarily of salaries and employee-related expenses, including stock-based compensation, travel, facility, legal, accounting and other professional fees. Selling, general and administrative expenses increased 55% to $41.1 million in 2007 from $26.5 million in 2006. The increase of $13.4 million was primarily due to a $9.0 million increase in salaries and employee-related expenses. Such increase reflects a 40% increase in headcount, partially from the acquisition of Sangtec, an increase in sales commissions of $2.6 million due to greater commission-based sales, and an increase of $2.0 million in stock-based compensation. Other increases included $2.4 million in legal, accounting, and other professional consulting expenses, $0.7 million in travel related expenses, and $0.9 million in facility related costs and depreciation expense. In December 2007, we entered into a separation and consulting agreement with our former Chief Financial Officer, pursuant to which he will provide us with consulting services on a part-time basis until December 31, 2008, and will receive compensation equal to his 2007 base salary and continue to vest in outstanding options to purchase common stock. As a result of this agreement, in 2007 we recorded salary and employee related expenses of $0.3 million and stock-based compensation of $0.8 million, both of which are included in the explanation of 2007 increases.

Expense for Patent-related Matter

On January 2, 2007, we entered into a Settlement and Cross-License Agreement (the "Settlement Agreement") with Idaho Technology regarding certain Cepheid and Idaho Technology intellectual property (the "Intellectual Property"). The Settlement Agreement provides each of the parties with a non-exclusive, worldwide, fully paid, non-terminable, irrevocable license to certain of the other's patents for use in their respective product lines and contains certain covenants by each of the parties not to sue the other. Pursuant to the Settlement Agreement, we made a payment of $3.35 million to Idaho Technology in January 2007. As of December 31, 2006, the settlement amount was accrued and recorded as an expense in the consolidated statement of operations. Although we believed we would not be held liable for infringement had the issue ultimately gone to litigation, we came to the conclusion to settle the litigation. We made the Settlement Agreement and payment to avoid incurring significant legal costs to defend our case. Our belief that we did not infringe Idaho Technology's patents was based on our detailed legal analysis by outside counsel that the patents referenced in the litigation were either not being infringed and/or that the patents referenced were potentially invalid, due to prior art not specified or referenced in the patents. Due to the fact that we did not believe there to be any validity to the patent infringement case, we did not ascribe any value to future product sales and recorded the whole amount as fiscal 2006 expense.

Other Income (Expense), Net

	Years Ended December 31,		
	2007	2006	% Change
	(Amounts in thousands)		
Other income (expenses), net:			
Interest income	$ 2,731	$ 4,402	(38)%
Interest expense	(22)	(367)	(94)%
Foreign currency gain and other	568	247	130 %
Total other income (expenses), net	$ 3,277	$ 4,282	(23)%

Interest income decreased to $2.7 million in 2007 from $4.4 million in 2006. The decrease was primarily due to the redemption of marketable securities in the first quarter of 2007, the proceeds from which were used to acquire Sangtec. The decrease in interest expense of $0.3 million was primarily due to repayment of the line of credit during the first quarter of 2006. Foreign currency gain and other increased by $0.3 million primarily as a result of the weakening of the U.S. Dollar during 2007.

Income Taxes

We have recorded no U.S. federal or state income tax provision for any period as we have incurred operating losses in all periods. Income tax expense of $0.2 million in 2007 represents current foreign income taxes related to our French subsidiary. As of December 31, 2007 and 2006, we had deferred tax assets of approximately $63.2 million and $60.0 million, respectively, which were offset by a valuation allowance of $59.9 million and $60.0 million, respectively. We also had a deferred tax liability of $3.3 million as of December 31, 2007. As of December 31, 2007, we had net operating loss carryforwards for federal income tax purposes of approximately $124.8 million, which expire in the years 2011 through 2027, and federal research and development tax credits of approximately $4.1 million, which expire in the years 2012 through 2026. As of December 31, 2007, we had net operating loss carryforwards for state income tax purposes of approximately $47.2 million, which expire in the years 2011 through 2017, and state research and development tax credits of approximately $2.9 million, which have no expiration date.

Utilization of our net operating loss may be subject to a substantial annual limitation due to ownership change limitations provided by the Internal Revenue Code and similar state provisions. Such annual limitation may result in the expiration of net operating loss before utilization.

Undistributed earnings of our foreign subsidiaries of approximately $1.4 million and $0.5 million at December 31, 2007 and 2006, respectively, are considered to be indefinitely reinvested, and, accordingly, no provisions for federal and state income taxes have been provided thereon. Upon distribution of those earnings in the form of dividends or otherwise, we would be subject to both federal income taxes, subject to an adjustment for foreign income tax credit, and withholding taxes payable to various foreign countries. The distribution of such foreign earnings to the U.S. parent would have no U.S. tax impact as the net operating loss carryforwards exceed the undistributed earnings.

Comparison of Years Ended December 31, 2006 and 2005

Revenues

	Years Ended December 31,		
	2006	2005	% Change
	(Amounts in thousands)		
Revenues:			
Instrument sales	$ 22,737	$ 28,263	(20)%
Reagent and disposable sales	59,666	52,177	14 %
Total product sales	82,403	80,440	2 %
Contract revenues	3,913	3,062	28 %
Grants and government sponsored research revenue	1,036	1,508	(31)%
Total Revenues	$ 87,352	$ 85,010	3 %

Product Sales

We operate in three market areas: Clinical Molecular Diagnostic, Industrial and Biothreat markets. The following table illustrates product sales in the three market areas as a percentage of total product sales:

	Years Ended December 31,	
	2006	2005
	(As a % of total product sales)	
Product sales by market:		
Clinical Molecular Diagnostic	24 %	11 %
Biothreat	58 %	72 %
Industrial	18 %	17 %
Total Product Sales	100 %	100 %

Total product sales increased 2% to $82.4 million in 2006 from $80.4 million in 2005. The increase in product sales was the result of a change in product mix due to an increase in Clinical Molecular Diagnostic and Industrial product sales offset by an anticipated decrease in GeneXpert module sales to the USPS. The change in product mix is attributed primarily to expanded efforts in the Clinical Molecular Diagnostic market. In 2006, product sales to Northrop Grumman represented 59% of our total product sales. In 2005, product sales to Northrop Grumman and Smiths Detection represented 61% and 12% of our total product sales, respectively. The following table provides a breakdown of our product sales by geographic regions:

	Years Ended December 31,	
	2006	2005
	(As a % of total product sales)	
Product Sales by Geographic Regions:		
North America	88 %	92 %
Europe	10 %	5 %
Japan and other	2 %	3 %
Total Product Sales	100 %	100 %

No single country outside of the United States represented more than 10% of our total revenues in any period presented.

Contract Revenues

Contract revenues were $3.9 million in 2006 and $3.1 million in 2005. In 2006, Contract revenues were derived primarily from the amortization of license fees in conjunction with our collaboration agreement with bioMerieux, Inc., which are being recognized ratably over the term of the agreement, our collaboration agreement with Foundation for Innovative New Diagnostics ("FIND"), and our contract with Amplimedical. The increase in contract revenues in 2006 as compared to 2005 is due to the revenues from FIND, which began in 2006, and from increased revenues from Amplimedical.

Grants and Government Sponsored Research Revenue

Grants and government sponsored research revenue decreased to $1.0 million in 2006 from $1.5 million in 2005. The 2006 revenue was derived principally from programs with the National Cancer Institute and National Institutes of Health. The decrease in revenue in 2006 as compared to 2005 is primarily due to reductions from Northrop Grumman which has a contract with the Homeland Security Advanced Research Project Agency and from the National Cancer Institute.

Costs and Operating Expenses

	Years Ended December 31,		
	2006	2005	% Change
	(Amounts in thousands)		
Costs and operating expenses:			
Cost of product sales	$ 48,800	$ 46,232	6 %
Collaboration profit sharing	14,974	14,483	3 %
Research and development	23,886	18,961	26 %
In-process research and development	139	—	N/A
Selling, general and administrative	26,470	18,901	40 %
Expense for patent related matter	3,350	—	N/A
Total costs and operating expenses	$117,619	$ 98,577	19 %

Cost of Product Sales

As a result of the increased product sales discussed above, cost of product sales increased 6% to $48.8 million in 2006 compared to $46.2 million in 2005. Our product gross margin percentage declined to 41% in 2006 from 43% in 2005. The cost of product sales in 2006 included $0.6 million of stock-based compensation expense, whereas there was no such expense for 2005. This had the effect of a 1 percentage point decrease in our product gross margin percentage in 2006. The remaining 1 percentage point decline is due to a less favorable product mix.

Collaboration Profit Sharing

The collaboration profit sharing was $15.0 million and $14.5 million in 2006 and 2005, respectively. The increase in collaboration profit sharing was the result of increased anthrax cartridge sales under the USPS BDS program, and this expense will remain proportional to the sales of anthrax cartridges under the USPS BDS program.

Research and Development Expenses

Research and development expenses increased 26% to $23.9 million in 2006 from $19.0 million in 2005. Research and development expenses in 2006 included $2.8 million of stock-based compensation expense, whereas there was no such expense for 2005. The increase in research and development expenses resulted primarily from a $3.7 million increase in salaries and employee-related expenses, including stock compensation expense, a $0.1 million increase in outside engineering and other consulting services, a $0.6 million increase in clinical trial costs, and a $0.5 million increase in occupancy costs and supplies. The increase in clinical trial costs is associated with our GBS, EV, MRSA and BCR/ABL products.

In-process Research and Development

In-process research and development of $0.1 million in 2006 represents the write-off of research and development intangible assets acquired in the acquisition of Actigenics in August 2006 that had no alternative future uses.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased 40% to $26.5 million in 2006 from $18.9 million in 2005. The increase included a $5.3 million increase in salaries and employee-related expenses, including stock-based compensation of $3.9 million, a $1.5 million increase in legal, accounting, and other professional expenses, and a $0.8 million increase in insurance and other administrative expenses. Selling, general and administrative expenses in 2006 included $3.9 million of stock-based compensation expense, whereas there was no such expense for 2005.

Expense for Patent-related Matter

As discussed above in the comparison of the years ended December 31, 2007 and 2006, we recorded an expense of $3.35 million for patent-related matters in 2006. There was no related expense in 2005.

Other Income (Expense), Net

	Years Ended December 31,		
	2006	2005	% Change
	(Amounts in thousands)		
Other income (expenses), net:			
Interest income	$ 4,402	$ 1,413	212 %
Interest expense	(367)	(1,082)	(66)%
Foreign currency exchange gain (loss)	195	(358)	(154)%
Other income (expenses), net	52	—	N/A
Total other income (expenses), net	$ 4,282	$ (27)	(15,959)%

Interest income increased to $4.4 million in 2006 from $1.4 million in 2005. The increase was primarily due to additional cash balances resulting from proceeds of our public offering of common stock in March 2006. Interest expense decreased to $0.4 million in 2006 from $1.1 million in 2005. The decrease was primarily due to repayment of the lines of credit during the first quarter of 2006. Foreign exchange income increased as the U.S. dollar has strengthened against the Euro in 2006 compared to 2005.

LIQUIDITY AND CAPITAL RESOURCES

Cash and Cash Flow

As of December 31, 2007, we had $44.0 million in cash and cash equivalents and marketable securities. Our total cash and marketable securities used in the year ended December 31, 2007 was $50.9 million, which consisted primarily of $14.7 million used for operating activities, $27.6 million for the acquisition of Sangtec and Actigenics, $7.1 million used for capital expenditures and $4.9 million for purchases of technology licenses and intangible assets, offset by $3.3 million provided by financing activities. We maintain our portfolio of cash equivalents and marketable securities in short-term commercial paper, auction rate securities and money market funds in order to minimize market risk and preserve principal. In February 2008, we had $25.0 million invested in auction rate securities, of which $20.5 million in principal amount failed to settle at auction in February 2008. We continue to earn interest on the investments that failed to settle at auction at the maximum contractual rate. The next auctions for these securities are scheduled to occur in March 2008. As of December 31, 2007, the carrying value of these investments was equal to the fair value based on successful auctions preceding and subsequent to year end. All of our auction rate securities continue to carry at least a AAA rating by one of the rating agencies. Approximately $20.7 million of principal amount of auction rate securities owned by us are either backed by federal student loans, which are guaranteed by the Federal Family Educational Loan Program ("FFELP"), or are insured.

Net cash used in operating activities was $14.7 million, $11.7 million and $5.7 million in 2007, 2006 and 2005, respectively. In 2007, net cash used in operating activities primarily consisted of a $21.4 million net loss, which was partially offset by $9.8 million of depreciation expense and amortization of intangible assets and $11.1 million of stock based compensation. In addition, the decrease of $14.4 million attributable to changes in operating assets and liabilities consisted primarily of increases in receivables of $4.6 million, inventory of $11.3 million, prepaid expenses of $0.9 million, payments of $3.4 million for patent-related matters and $0.8 million of deferred revenue, which were partially offset by increases $6.1 million in accounts payable, other current liabilities and accrued compensation, $0.2 million in income taxes payable and $0.2 million in other non-current assets. In 2006, net cash used in operating activities primarily consisted of $26.0 million net loss, which was partially offset by $7.6 million of depreciation expense and amortization of intangible assets and $7.3 million of stock based compensation. In addition, the decrease in operating assets and liabilities of $1.1 million consisted primarily of $3.4 million for accrued expense for patent-related matter, which was offset by $4.4 million principally related to inventory, accounts receivable, deferred revenue and accounts payable and other accrued liabilities. In 2005, net cash used in operating activities primarily consisted of $13.6 million net loss, which was partially offset by $6.0 million of depreciation expense and amortization of intangible assets. In addition, the increase in operating assets and liabilities of $1.2 million consisted primarily of $4.5 million for accounts payable and other accrued liabilities, which were offset by $3.3 million principally related to inventory and deferred revenue.

Net cash provided by (used in) investing activities was $10.5 million, ($74.9) million and ($5.6) million in 2007, 2006 and 2005, respectively. In 2007, net cash provided by investing activities consisted of $50.2 million net marketable securities sold, which was partially offset by $27.6 million used to acquire Sangtec and Actigenics, $4.9 million used for technology licenses and $7.1 million in capital expenditures. In 2006, net cash used in investing activities consisted of $56.6 million net purchases of marketable securities, $1.0 million to acquire Actigenics, and $5.9 million in capital expenditures and $11.3 million for technology licenses. In 2005, net cash used in investing activities consisted of $6.7 million in capital expenditures, $12.0 million for technology licenses offset by $13.1 million in net marketable securities activities.

Net cash provided by financing activities was $3.3 million, $87.7 million and $4.1 million in 2007, 2006 and 2005, respectively. In 2007, cash provided by financing activities consisted of $3.7 million in net proceeds from the sale of common stock under our employee equity incentive plans that was partially offset by repayments of $0.4 million on our equipment and other loans. In 2006, cash provided by financing activities consisted of $95.8 million in net proceeds from the sale of common stock. This was partially offset by repayments of $8.1 million on our equipment loans and line of credit. In 2005, cash provided by financing activities was $3.2 million from sales of common stock, $3.0 million in borrowings under our equipment financing arrangements offset by payments of $2.1 million under our equipment financing arrangements.

Contractual Obligations

As of December 31, 2007, our contractual obligations for the next five years, and thereafter, were as follows (in thousands):

	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Operating Leases	$ 10,304	$ 2,963	$ 5,043	$ 2,298	—
Notes payable	4	2	2	—	—
Purchase Obligations	11,559	4,135	7,424	—	—
Minimum Royalties	9,885	891	1,821	1,876	5,297
	$ 31,752	$ 7,991	$ 14,290	$ 4,174	$ 5,297

Purchase obligations include purchase orders or contracts for the purchase of raw materials and other goods and services. We do not have significant agreements for the purchase of raw materials or other goods specifying minimum quantities or set prices that exceed our expected requirements. Minimum royalty payments represent licensed royalties we are obligated to pay under our license agreements.

The expected timing of payment of the obligations discussed above is estimated based on current information. Timing of payments and actual amounts paid could vary in some circumstances depending on the time of receipt of goods or services or changes to agreed-upon amounts for some obligations.

Off-Balance-Sheet Arrangements

As of December 31, 2007, we did not have any off-balance-sheet arrangements, as defined in Item 303(a)(4)(ii) we did not have any off-balance-sheet arrangements, as defined in Item 303(a) (4) (ii) of Regulation S-K promulgated under the Securities Act of 1933.

Financial Condition Outlook

We plan to continue to make expenditures to expand our manufacturing capacity, to support our activities in sales and marketing and research and development, and to support our working capital needs. We expect to spend approximately $16 million for capital equipment in 2008. We expect to have positive cash flow from operations for the year 2008.

In the future, we may seek additional funds to support our strategic business needs and may seek to raise such additional funds through private or public sales of equity, debt or convertible securities, strategic relationships, bank debt, lease financing arrangements, or other available means. If additional funds are raised through the issuance of equity or equity-related securities, stockholders may experience additional dilution, or such equity securities may have rights, preferences, or privileges senior to those of the holders of our common stock. If adequate funds are not available or are not available on acceptable terms to meet our business needs, our business may be harmed.

ITEM 7A. *QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS*

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. Our investments in interest-bearing assets are subject to interest rate risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk, we maintain our interest-bearing portfolio,

which consists of cash and cash equivalents, in taxable auction variable rate notes and money market funds. Due to the short-term nature of the investments, we believe we currently have no material exposure to interest rate risk arising from our investments. Therefore we have not included quantitative tabular disclosure in this Form 10-K. As described above, we had $25.0 million invested in auction rate securities, of which $20.5 million in principal amount failed to settle at auction in February 2008. All of our auction rate securities continue to carry at lease a AAA rating by one of the rating agencies. Approximately $20.7 million of principal amount of auction rate securities owned by us are either backed by federal student loans, which are guaranteed by the Federal Family Educational Loan Program ("FFELP"), or are insured.

We do not enter into financial investments for speculation or trading purposes and are not a party to financial or commodity derivatives.

We operate primarily in the United States and a majority of our revenue, cost, expense and capital purchasing activities for 2007 were transacted in U.S. Dollars. As a corporation with international as well as domestic operations, we are exposed to changes in foreign exchange rates. These exposures may change over time and could have a material adverse impact on our financial results. During the fiscal years ended December 31, 2007 and 2006, we did not utilize foreign currency forward contracts to manage the risk of exchange rate fluctuations. We did not have material exposure to foreign currency rate fluctuations. We do not anticipate any material effect on our consolidated financial position utilizing our current hedging strategy but will continue to monitor and evaluate our internal processes relating to foreign exchange.

ITEM 8. ***CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA***

The following consolidated financial statements and the related notes thereto, of Cepheid and the Reports of Independent Registered Public Accounting Firm, Ernst and Young LLP, are filed as a part of this Form 10-K.

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MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Under the supervision and with the participation of management, including the principal executive officer and acting principal financial officer, management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Cepheid AB, which was acquired on February 14, 2007 and at the date of acquisition was named Sangtec Molecular Diagnostics AB, which is included in the Company's 2007 consolidated financial statements and constituted 0.3% and 0.6% of total and net assets, respectively, as of December 31, 2007 and 5.6% and 4.0% of revenue and net loss, respectively, for the year then ended.

Based on management's evaluation under the framework in *Internal Control – Integrated Framework,* management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2007. Ernst & Young LLP, an independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report on Form 10-K and, as part of its audit, has issued an attestation report, included herein, on the effectiveness of the Company's internal control over financial reporting.

February 29, 2008

/s/ John L. Bishop
John L. Bishop
Chief Executive Officer

/s/ Michael T. Myhre
Michael T. Myhre
Vice President and Corporate Controller

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Cepheid

We have audited Cepheid's internal control over financial reporting as of December 31, 2007 based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the "COSO criteria"). Cepheid's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Report on Management's Assessment of Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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

As indicated in the accompanying Management's Report on Internal Control over Financial Reporting, management's assessment of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Cepheid AB, which was acquired on February 14, 2007 and at the date of acquisition was named Sangtec Molecular Diagnostics AB, which is included in the 2007 consolidated financial statements of Cepheid and constituted 0.3% and 0.6% of total and net assets, respectively, as of December 31, 2007 and 5.6% and 4.0% of revenue and net loss, respectively, for the year then ended. Our audit of internal control over financial reporting of Cepheid also did not include an evaluation of the internal control over financial reporting of Cepheid AB.

In our opinion, Cepheid maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Cepheid as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2007 and our report dated February 29, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

San Jose, California
February 29, 2008

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Cepheid

We have audited the accompanying consolidated balance sheets of Cepheid as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2007. Our audits also included the financial statement schedule listed in the index at Item 15(b). These financial statements and schedule are the responsibility of Cepheid's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Cepheid at December 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects, the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, Cepheid changed its method of accounting for stock-based compensation as of January 1, 2006 and its method of accounting for uncertain tax positions as of January 1, 2007.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Cepheid's internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 29, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

San Jose, California
February 29, 2008

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CONSOLIDATED BALANCE SHEETS

	December 31, 2007	December 31, 2006
	(In thousands, except share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 16,476	$ 17,186
Marketable securities	27,550	77,750
Accounts receivable, less allowance for doubtful accounts of $37 and $87 as of December 31, 2007 and 2006, respectively	21,263	15,246
Inventory	23,821	10,240
Prepaid expenses and other current assets	2,565	1,390
Total current assets	91,675	121,812
Property and equipment, net	17,174	14,097
Restricted cash	661	661
Other non-current assets	262	666
Intangible assets, net	40,629	30,425
Goodwill	14,844	—
Total assets	$165,245	$167,661
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 10,587	$ 8,977
Accrued compensation	8,573	3,319
Accrued royalties	6,913	3,516
Accrued collaboration profit sharing	522	3,497
Accrued other liabilities	4,740	4,107
Income tax payable	213	—
Accrued expense for patent-related matter	—	3,350
Current portion of deferred revenue	4,016	3,913
Current portion of license fees payable	—	447
Current portion of equipment financing	—	313
Current portion of note payable	2	11
Total current liabilities	35,566	31,450
Long-term portion of deferred revenue	2,054	2,663
Long-term portion of equipment financing	—	3
Long-term portion of note payable	2	41
Deferred rent	688	798
Total liabilities	38,310	34,955
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, no par value; 5,000,000 shares authorized, none issued or outstanding	—	—
Common stock, no par value; 100,000,000 shares authorized, 55,611,398 and 54,950,284 shares issued and outstanding at December 31, 2007 and 2006, respectively	254,807	251,132
Additional paid-in capital	26,697	15,065
Accumulated other comprehensive income (loss)	340	(5)
Accumulated deficit	(154,909)	(133,486)
Total shareholders' equity	126,935	132,706
Total liabilities and shareholders' equity	$165,245	$167,661

See accompanying notes.

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CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	2007	2006	2005
	(In thousands, except per share data)		
Revenues:			
Instrument sales	$ 47,739	$ 22,737	$ 28,263
Reagent and disposable sales	68,793	59,666	52,177
Total product sales	116,532	82,403	80,440
Contract revenues	8,554	3,913	3,062
Grants and government sponsored research revenue	4,387	1,036	1,508
Total revenues	129,473	87,352	85,010
Costs and operating expenses:			
Cost of product sales	69,174	48,800	46,232
Collaboration profit sharing	12,256	14,974	14,483
Research and development	31,449	23,886	18,961
In-process research and development	—	139	—
Selling, general and administrative	41,081	26,470	18,901
Expense for patent related matter	—	3,350	—
Total costs and operating expenses	153,960	117,619	98,577
Loss from operations	(24,487)	(30,267)	(13,567)
Other income (expense):			
Interest income	2,731	4,402	1,413
Interest expense	(22)	(367)	(1,082)
Foreign currency exchange gain (loss) and other	568	247	(358)
Other income (expense), net	3,277	4,282	(27)
Net loss before provision for income taxes	(21,210)	(25,985)	(13,594)
Provision for income taxes	(213)	—	—
Net loss	$ (21,423)	$ (25,985)	$ (13,594)
Basic and diluted net loss per share	$ (0.39)	$ (0.50)	$ (0.32)
Shares used in computing basic and diluted net loss per share	55,263	52,325	42,494

See accompanying notes.

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In thousands)	Common Stock Shares	Amount	Additional Paid-In	Accumu-lated Other Compre-	Accumu-lated Deficit	Total Share-holders' Equity
Balance at December 31, 2004	42,048	$ 152,136	$ 7,517	$ (137)	$ (93,907)	$ 65,609
Components of comprehensive loss:						
Net loss	—	—	—	—	(13,594)	(13,594)
Foreign currency translation adjustment	—	—	—	179	—	179
Net unrealized loss on available-for-sale securities	—	—	—	(3)	—	(3)
Total comprehensive loss						(13,418)
Issuance of shares of common stock under employee and director option plans	438	2,099	—	—	—	2,099
Stock-based compensation related to stock options issued to consultants	—	—	1	—	—	1
Issuance of shares of common stock under employee stock purchase plan	269	1,112	—	—	—	1,112
Balance at December 31, 2005	42,755	155,347	7,518	39	(107,501)	55,403
Components of comprehensive loss:						
Net loss	—	—	—	—	(25,985)	(25,985)
Foreign currency translation adjustment	—	—	—	(49)	—	(49)
Net unrealized gain on available-for-sale securities	—	—	—	5	—	5
Total comprehensive loss						(26,029)
Issuance of common shares under a follow on offering (net of issuance costs of $6,312)	11,420	91,899	—	—	—	91,899
Issuance of shares of common stock under employee and director option plans	652	2,993	—	—	—	2,993
Stock-based compensation related to stock options and awards and employee stock purchase plan	—	—	7,547	—	—	7,547
Issuance of shares of common stock under employee stock purchase plan	123	893	—	—	—	893
Balance at December 31, 2006	54,950	251,132	15,065	(5)	(133,486)	132,706
Components of comprehensive loss:						
Net loss	—	—	—	—	(21,423)	(21,423)
Foreign currency translation adjustment	—	—	—	345	—	345
Total comprehensive loss						(21,078)
Issuance of shares of common stock under employee and director option plans	512	2,620	—	—	—	2,620
Stock-based compensation related to stock options and awards and employee stock purchase plan	—	—	11,632	—	—	11,632
Issuance of shares of common stock under employee stock purchase plan	149	1,055	—	—	—	1,055
Balance at December 31, 2007	55,611	$ 254,807	$ 26,697	$ 340	$ (154,909)	$ 126,935

See accompanying notes

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CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2007	2006	2005
		(In thousands)	
Cash flows from operating activities:			
Net loss	$ (21,423)	$ (25,985)	$ (13,594)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	5,506	4,824	3,485
Amortization of intangible assets	4,263	2,746	2,544
Amortization of imputed interest	—	222	501
In-process technology expense	—	139	—
Amortization of prepaid compensation	302	105	—
Stock-based compensation related to employees and consulting services rendered	11,120	7,330	1
Deferred rent	(110)	63	136
Changes in operating assets and liabilities:			
Accounts receivable	(4,555)	(1,237)	608
Inventory	(11,279)	(2,034)	(1,445)
Prepaid expenses and other current assets	(880)	(439)	(181)
Other non-current assets	169	(284)	—
Accounts payable and other current liabilities	2,100	555	4,516
Income tax payable	213	—	—
Accrued expense for patent-related matter	(3,350)	3,350	—
Accrued compensation	3,967	86	355
Deferred revenue	(748)	(1,082)	(2,672)
Net cash used in operating activities	(14,705)	(11,641)	(5,746)
Cash flows from investing activities:			
Capital expenditures	(7,098)	(5,917)	(6,729)
Payments for technology licenses	(4,945)	(11,325)	(12,013)
Cost of acquisitions, net	(27,637)	(1,037)	—
Proceeds from the sale of fixed assets	23	—	—
Proceeds from maturities of marketable securities	55,000	47,850	32,380
Purchases of marketable securities	(4,800)	(104,450)	(19,280)
Restricted cash	—	—	27
Net cash provided by (used in) investing activities	10,543	(74,879)	(5,615)
Cash flows from financing activities:			
Net proceeds from the sale of common shares and exercise of stock options and awards	3,675	95,785	3,211
Principal payment of line of credit	—	(4,000)	—
Proceeds from equipment financing	—	—	3,000
Principal payments under equipment financing	(316)	(4,044)	(2,143)
Principal payments of note payable	(48)	(63)	—
Net cash provided by financing activities	3,311	87,678	4,068
Effect of exchange rate change on cash	141	(44)	176
Net increase (decrease) in cash and cash equivalents	(710)	1,114	(7,117)
Cash and cash equivalents at beginning of year	17,186	16,072	23,189
Cash and cash equivalents at end of year	$ 16,476	$ 17,186	$ 16,072
Supplemental Cash Flow Information:			
Cash paid for interest	$ 22	$ 367	$ 1,082

See accompanying notes.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2007

1. Organization and Summary of Significant Accounting Policies

Organization and Business

Cepheid (the "Company") was incorporated in the State of California on March 4, 1996. The Company is a molecular diagnostics company that develops, manufactures, and markets fully-integrated systems for genetic analysis in the Clinical Molecular Diagnostic, Industrial and Biothreat markets. The Company's systems enable rapid, sophisticated genetic testing for organisms and genetic-based diseases by automating otherwise complex manual laboratory procedures.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries after elimination of intercompany transactions and balances. In August 2006, the Company's French subsidiary acquired Actigenics SA ("Actigenics"), which was subsequently merged into the French subsidiary. In February 2007, the Company acquired Sangtec Molecular Diagnostics AB ("Sangtec"). The consolidated financial statements include the results of operations of Actigenics and Sangtec subsequent to their respective acquisition dates of August 8, 2006 and February 14, 2007, respectively. The functional currency of the French subsidiary is the Euro, and the functional currency of the Swedish subsidiary is the Swedish Krona; accordingly, all gains and losses arising from foreign currency transactions in currencies other than the functional currency are included in the consolidated statements of operations. Adjustments resulting from translating the financial statements of foreign subsidiaries into U.S. Dollars are reported as a separate component of accumulated other comprehensive income in shareholders' equity.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from these estimates.

Financial Instruments

The carrying amounts of financial instruments, including cash and cash equivalents, marketable securities, accounts receivable, accounts payable, short-term debt and long-term debt, approximated fair value as of December 31, 2007 and 2006, due to their short-term nature.

Cash, Cash Equivalents and Marketable Securities

Cash and cash equivalents consist of cash on deposit with banks, money market instruments, commercial paper and debt securities with maturities from the date of purchase of 90 days or less. Interest income includes interest, dividends, amortization of purchase premiums and discounts and realized gains and losses on sales of securities.

The Company's marketable securities are designated as available-for-sale and recorded at fair value, and realized and unrealized gains and losses on investments are determined on the specific identification method. Unrealized holding gains or losses are reported as a component of accumulated other comprehensive income (loss). Marketable securities with maturities greater than 90 days and less than one year are classified as short-term; otherwise they are classified as long-term.

The following is a summary of the Company's cash, cash equivalents and marketable securities (in thousands):

	December 31,	
	2007	2006
Cash and cash equivalents:		
Cash	$ 12,207	$ 13,753
Money market funds	4,269	3,433
	16,476	17,186
Marketable securities:		
Taxabale auction variable rate notes	27,550	77,750
	$ 44,026	$ 94,936

As of December 31, 2007, the average auction rate securities portfolio duration was less than 30 days, and the securities had contractual maturities greater than twenty years.

An impairment charge is recognized when the decline in the fair value of a security below the amortized cost basis is determined to be other-than-temporary. The Company considers various factors in determining whether to recognize an impairment charge, including the duration of time and the severity to which the fair value has been less than our amortized cost basis, any adverse changes in the investees' financial condition and the Company's intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value. To date, the Company has not recorded any impairment charges on investments related to other-than-temporary declines in market value.

In February 2008, the Company had $25.0 million invested in auction rate securities of which $20.5 million in principal amount failed to settle at auction in February 2008. The Company continues to earn interest on the investments that failed to settle at auction, at the maximum contractual rate. As of December 31, 2007 the carrying value of these investments was equal to the fair value based on successful auctions preceding and subsequent to year end. All of the auction rate securities held by the Company continue to carry a high credit rating. Approximately $20.7 million of principal amount of auction rate securities owned by the Company are either backed by federal student loans, which are guaranteed by the Federal Family Educational Loan Program ("FFELP"), or are insured.

Restricted Cash

Restricted cash consists of a certificate of deposit and bank term deposits all with maturities of greater than 90 days, and is collateral for a standby letter of credit issued in connection with a facility lease obligation.

Inventory

Inventory is stated at the lower of standard cost (which approximates actual cost) or market, with cost determined on the first-in-first-out method. Accordingly, allocation of fixed production overheads to conversion costs is based on normal capacity of the production. Abnormal amounts of idle facility expense, freight, handling costs and spoilage are expensed as incurred and not included in overhead.

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

	December 31,	
	2007	2006
Raw Materials	$ 9,956	$ 4,910
Work in Process	7,550	2,587
Finished Goods	6,315	2,743
	$ 23,821	$ 10,240

Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated using the straight-line method, and the cost is amortized over the estimated useful lives of the assets, which range from 3 to 10 years. Leasehold improvements are amortized using the straight-line method over the estimated useful lives of the assets or the term of the lease, whichever is shorter.

Property and equipment consisted of the following (in thousands):

	December 31,	
	2007	2006
Land	$ 21	$ 21
Building	1,312	486
Scientific equipment	11,897	8,868
Manufacturing equipment	11,768	9,933
Office furniture, computers and equipment	7,920	5,139
Leasehold improvements	7,461	5,215
	40,379	29,662
Less accumulated depreciation and amortization	(23,205)	(15,565)
	$ 17,174	$ 14,097

Intangible Assets and Goodwill

As of December 31, 2007, intangible assets consisted primarily of rights to certain patented technologies licensed from F. Hoffmann-La Roche Ltd. ("Roche") and Applera Corporation ("Applera'), (see Note 3, "Patent License Agreements and Note 5, "Collaborative Agreements and Contracts") and intangible assets acquired in the acquisition of Sangtec (see Note 7, "Acquisitions").

Intangible assets related to licenses are recorded at cost, less accumulated amortization. Intangible assets related to technology acquired in acquisitions and other intangible assets are recorded at fair value at the date of acquisition, less accumulated amortization. Intangible assets are amortized over their estimated useful lives, ranging from 3 to 20 years, on a straight-line basis, except for intangible assets acquired in the acquisition of Sangtec, which are amortized on the basis of economic useful life. Amortization of intangible assets is included in cost of product sales in the accompanying consolidated statements of operations.

The Company reviews its intangible assets for impairment under Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". The Company conducts the impairment review when events or circumstances indicate the carrying value of a long-lived asset may be impaired by estimating the future undiscounted cash flows to be

derived from an asset to assess whether or not a potential impairment exists. If the carrying value exceeds the Company's estimate of future undiscounted cash flows, an impairment value is calculated as the excess of the carrying value of the asset over the Company's estimate of its fair market value. Events or circumstances which could trigger an impairment review include a significant adverse change in the business climate, an adverse action or assessment by a regulator, unanticipated competition, significant changes in the Company's use of acquired assets, the Company's overall business strategy, or significant negative industry or economic trends. There were no impairment charges recorded in any of the periods presented.

The recorded value and accumulated amortization of major classes of intangible assets were as follows (in thousands):

	Recorded Value	Accumulated Amortization	Net Book Value
Balance, December 31, 2007			
Licenses	$ 40,885	$ 10,159	$ 30,726
Technology acquired in acquisitions	8,613	306	8,307
Other	2,170	574	1,596
	$ 51,668	$ 11,039	$ 40,629
Balance, December 31, 2006			
Licenses	$ 36,388	$ 6,737	$ 29,651
Technology acquired in acquisitions	813	39	774
	$ 37,201	$ 6,776	$ 30,425

Included in licenses was $19.9 million in connection with a patent license agreement with F. Hoffman-La Roche Ltd., effective July 1, 2004. The net book value of this license was $15.5 million and $16.7 million at December 31, 2007 and 2006, respectively.

Amortization expense of intangible assets was $4.3 million, $2.8 million and $2.5 million for the years ended December 31, 2007, 2006 and 2005, respectively. The expected future annual amortization expense of intangible assets recorded on the Company's consolidated balance sheet as of December 31, 2007 is as follows, assuming no impairment charges (in thousands):

For the Years Ending December 31,	Amortization Expense
2008	$ 4,621
2009	4,927
2010	4,886
2011	4,792
2012	4,686
Thereafter	16,717
Total expected future annual amortization	$ 40,629

The Company annually reviews its goodwill for impairment under SFAS No. 142, "Goodwill and Other Intangible Assets". If the fair value of the Company exceeds its net book value including goodwill, then goodwill is not considered impaired. The initial step is to compare Company's fair value as determined by its market capitalization to its net book value. If the market capitalization exceeds the net book value, goodwill is presumed to be unimpaired. Otherwise, the Company would estimate expected future cash flows of its business, which operates in a number of markets and geographical regions. The Company would then determine the carrying value of its business and compare its carrying value including goodwill and other intangibles to the discounted future cash flows. If the total of future cash flows is less than the carrying amount of the assets, the Company would recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets. At December 31, 2007, the Company compared its market capitalization to its net book value and determined that goodwill was not impaired.

Warranty Reserve

The Company warrants its instrument products to be free from defects for a period of 12 to 15 months from the date of sale and its disposable products to be free from defects, when handled according to product specifications, for the stated life of such products. Accordingly, a provision for the estimated cost of warranty repair or replacement is recorded at the time revenue is recognized. The Company's warranty provision is established using management's estimate of future failure rates and of the future costs of repairing any instrument failures during the warranty period or replacing any disposable products with defects. The activities in the warranty provision for each of the three years ended December 31, 2007 consisted of the following (in thousands):

	2007	2006	2005
Balance at beginning of year	$ 256	$ 470	$ 379
Costs incurred and charged against reserve	(210)	(451)	(767)
Accrual related to current year product sales	546	651	1,165
Adjustment to pre-existing warranties	(43)	(414)	(307)
Balance at end of year	$ 549	$ 256	$ 470

Revenue Recognition

In accordance with Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition", the Company recognizes revenue from product sales when there is persuasive evidence that an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is reasonably assured. No right of return exists for the Company's products except in the case of damaged goods. The Company has not experienced any significant returns of its products. Contract revenues include fees for technology licenses and research and development services, royalties under license and collaboration agreements. Contract revenue related to technology licenses is generally fully recognized only after the license period has commenced, the technology has been delivered and no further involvement of the Company is required. When the Company has continuing involvement related to a technology license, revenue is recognized over the license term. Royalties are typically based on licensees' net sales of products that utilize the Company's technology, and royalty revenues are recognized as earned in accordance with the contract terms when the royalties can be reliably measured and their collectibility is reasonably assured, such as upon the receipt of a royalty statement from the customer. Service revenue is recognized when the services have been provided. Shipping and handling costs are expensed as incurred and included in cost of product sales. In those cases where the Company bills shipping and handling costs to customers, the amounts billed are classified as revenue.

The Company recognizes revenue from product sales and contract arrangements. From time to time, the Company enters into revenue arrangements with multiple deliverables. Multiple element revenue agreements are evaluated under Emerging Issues Task Force ("EITF") Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables" ("EITF 00-21"), to determine whether the delivered item has value to the customer on a stand-alone basis and whether objective and reliable evidence of the fair value of the undelivered item exists. Deliverables in an arrangement that do not meet the separation criteria in EITF 00-21 must be treated as one unit of accounting for purposes of revenue recognition. Advance payments received in excess of amounts earned, such as funds received in advance of products to be delivered or services to be performed, are classified as deferred revenue until earned.

Grants and government sponsored research revenue and contract revenue related to research and development services are recognized as the related services are performed based on the performance requirements of the relevant contract. Under such agreements, the Company is required to perform specific research and development activities and is compensated either based on the costs or costs plus a mark-up associated with each specific contract over the term of the agreement or when certain milestones are achieved and recoverability is reasonably assured.

Research and Development

Research and development expenses consist of costs incurred for company-sponsored and collaborative research and development activities. These costs include direct and research-related overhead expenses. The Company expenses research and development costs, including the expenses for research under collaborative agreements, as such costs are incurred.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123(R)"), using the modified prospective transition method. Under the modified prospective transition method, prior periods are not restated for the effect of SFAS 123(R). Commencing with the first quarter of 2006, compensation cost includes all share-based awards granted to employees and directors, including employee stock option awards, restricted stock and employee stock purchases made under our Employee Stock Purchase Plan ("ESPP"), prior to but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123") , and compensation for all share-based awards granted to employees and directors subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). The Company recognizes the fair value of its stock option awards as compensation expense on a straight-line basis over the requisite service period of each award, which is generally four years. Compensation expense related to stock options granted to employees and directors prior to January 1, 2006 is accounted for under the recognition and measurement provisions of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), and related interpretations, as permitted by SFAS No. 123. Stock-based compensation to other than employees was not impacted by the adoption of SFAS 123(R) and is determined in

accordance with SFAS 123 and EITF Issue No. 96-18, "Accounting for Equity Instruments That Are Issued to Other than Employees for Acquiring, or in Conjunction with Selling, Goods, or Services".

Determining Fair Value Under SFAS 123(R):

Valuation and amortization method — The Company estimates the fair value of other than restricted stock awards granted using the Black-Scholes option-pricing formula and a single option award approach. The fair value of restricted stock awards is measured at the market price of non-restricted stock at the date of grant. This fair value is then amortized on a straight-line basis over the requisite service periods of the awards, which is generally the vesting period.

Expected Term—The expected term of the award represents the period that the Company's stock-based awards are expected to be outstanding and was determined based on historical experience, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior as influenced by changes to the terms of its stock-based awards.

Expected Volatility— Volatility is a measure of the amounts by which a financial variable such as stock price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. The Company uses the historical volatility for the past 5 years to estimate expected volatility, which matches the expected term of the option grant.

Risk-Free Interest Rate—The Company bases the risk-free interest rate used in the Black-Scholes valuation method on the implied yield currently available on U.S. Treasury zero-coupon issues with a remaining term equivalent to the expected term of a stock award.

Estimated Forfeitures — When estimating forfeitures, the Company considers voluntary termination behavior as well as analysis of actual option forfeitures.

The adoption of SFAS 123(R) also requires additional accounting related to income taxes. Due to the full valuation allowance provided on its net deferred tax assets, the Company has not recorded any tax benefit attributable to stock-based compensation expense.

Pro Forma Information for Periods Prior to the Adoption of SFAS 123(R)

Prior to the adoption of SFAS 123(R), the Company applied SFAS 123, amended by SFAS No. 148, "Accounting for Stock-Based Compensation — Transition and Disclosure" ("SFAS 148"), which allowed companies to apply the former accounting rules under APB 25 and related interpretations. In general, as the exercise price of options granted under the Company's plans was equal to the market price of the underlying common stock on the grant date, no stock-based employee compensation cost was recognized in the Company's consolidated statement of operations for periods prior to the adoption of SFAS 123(R). As required by SFAS 148 prior to the adoption of SFAS 123(R), the Company provided pro forma net loss and pro forma net loss per common share disclosures for stock-based awards, as if the fair-value-based method defined in SFAS 123 had been applied.

The following table illustrates the effect on net loss and net loss per share if the Company had applied the fair value recognition provision of SFAS 123 to options granted under the Company's stock-based compensation plans for the year ended December 31, 2005. For purposes of this pro-forma disclosure, the value of the options was estimated using a Black-Scholes option pricing formula and amortized on a straight-line basis over the respective vesting periods of the awards (in thousands, except per share data).

Net loss as reported	$ (13,594)
Deduct: total pro forma stock-based compensation determined under the fair value method of all employee related stock-based awards, net of related tax effects	(8,710)
Pro forma net loss	$ (22,304)
Basic and diluted net loss per share:	
As reported	$ (0.32)
Pro forma	$ (0.52)

The fair value of these options was estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

Risk-free interest rate	3.84%
Dividend yield	0.00%
Volatility factors of the expected market price of the Company's common stock	0.9
Weighted average expected life of option (years)	4.01

The same assumptions were applied in the determination of the option values related to stock options granted to non-employees, except the option life, for which the term of the consulting contracts was used.

Comprehensive Income (Loss)

Comprehensive loss includes net loss as well as other comprehensive income or loss. The Company's other comprehensive income or loss consists of foreign currency translation adjustments and unrealized gains and losses on available-for-sale securities. Total accumulated comprehensive income (loss) in the accompanying consolidated statements of shareholders' equity at December 31, 2007 and 2006 consisted entirely of cumulative translation adjustments.

Net Loss Per Share

Basic net loss per share has been calculated based on the weighted average number of common shares outstanding during the period. Shares used in diluted net loss per share calculations exclude anti-dilutive common stock equivalent shares, consisting of stock options and restricted awards. These anti-dilutive common stock equivalent shares totaled 8,905,000, 7,402,000 and 6,644,000, at December 31, 2007, 2006 and 2005, respectively.

Income Taxes

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. As a result of the implementation of FIN 48 on January 1, 2007, the Company recognized no material adjustment in the liability for unrecognized income tax benefits.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. For the year ended December 31, 2007, the Company did not recognize any interest or penalties related to uncertain tax positions in the consolidated statements of operations, and at December 31, 2007, the Company had no accrued interest or penalties.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, rather, it applies under existing accounting pronouncements that require or permit fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company will adopt SFAS 157 as required. The Company is currently evaluating the impact of SFAS 157 on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115" ("SFAS 159"). The fair value option established by SFAS 159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity will report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date. The fair value option: (a) may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method; (b) is irrevocable (unless a new election date occurs); and (c) is applied only to entire instruments and not to portions of instruments. SFAS 159 is effective as of the beginning of fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS 159 on its consolidated financial statements.

In December 2007, the FASB issued SFAS No, 141(revised 2007), "Business Combinations" ("SFAS 141(R)"). SFAS 141(R) will significantly change the accounting for business combinations in a number of areas including the treatment of contingent

consideration, contingencies, acquisition costs, in-process research and development and restructuring costs. In addition, under SFAS 141(R), changes in deferred tax asset valuation allowances and acquired income tax uncertainties in a business combination after the measurement period will impact income tax expense. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008, and earlier application is prohibited. Accordingly, any business combinations the Company engages in will be recorded and disclosed following existing generally accepted accounting principles until January 1, 2009, when the Company will adopt this standard. The Company expects SFAS 141(R) will have an impact on accounting for business combinations once adopted, but the effect is dependent upon acquisitions at that time.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" ("SFAS 160"). SFAS 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. This new consolidation method will significantly change the accounting for transactions with minority interest holders. SFAS 160 is effective for fiscal years beginning after December 15, 2008, and, as such, the Company will adopt this standard in fiscal 2009. The effect of adopting this standard is dependent upon the extent, if any, of noncontrolling financial interests at that time.

2. Segment and Significant Concentrations

The Company and its wholly owned subsidiaries operate in one business segment.

The Company currently sells its products through its direct sales force and through third-party distributors. For the years ended December 31, 2007 and 2006, there was one customer that accounted for 36% and 58% of total products sales, respectively. For the year ended December 31, 2005, there were two direct customers that represented 61% and 12% of total product sales. The Company has distribution agreements with several companies to distribute products in the U.S. and has several regional distribution arrangements throughout Europe, Japan, South Korea, China, Mexico and other parts of the world. The following table provides a breakdown of product sales by geographic region for the three years ended December 31, 2007, 2006 and 2005:

	Years Ended December 31,		
	2007	2006	2005
Product Sales Geographic information:			
North America	80 %	88 %	92 %
Europe	19 %	10 %	5 %
Japan and other	1 %	2 %	3 %
Total product sales	100 %	100 %	100 %

No single country outside of the United States represented more than 10% of the Company's total revenues, total net assets or total net property, plant and equipment in any period presented.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of bank deposits and accounts receivable. The Company maintains its portfolio of cash equivalents in short-term commercial paper, auction rate securities and money market funds. The Company's accounts receivable are derived primarily from sales to customers. The Company performs ongoing credit evaluations of its customers and limits the amount of credit extended when deemed necessary, but generally requires no collateral. In addition, the Company maintains an allowance for potential doubtful accounts.

There was one customer whose accounts receivable balance represented 22% of total receivables as of December 31, 2007 and 35% of total receivables as of December 31, 2006. The Company relies on several companies as its sole source for various materials used in its manufacturing process. Any extended interruption in the supply of these materials could result in the failure to meet customer demand.

3. Patent License Agreements

In April 2004, the Company entered into a patent license agreement with Applera, through its Applied Biosystems Group ("ABI") and its Celera Diagnostics joint venture, for a non-exclusive worldwide license to make, use, and sell the Company's products incorporating technology covered by Applera patents. The Company also entered into a patent license agreement with Roche, effective July 1, 2004, for a non-exclusive worldwide license to make, use, and sell the Company's products incorporating technology covered by Roche patents. Under the license agreements, the Company agreed to pay aggregate license fees of $32.2 million, of which $23.5 million was paid as of December 31, 2005 and $8.7 million was paid in 2006. In connection with the license agreements, the Company recorded intangible assets of $31.1 million, representing the present value of license fee obligations which is net of imputed interest of $1.1 million. The effective interest rate used to calculate the present value of the discounted payments was 4.0% for both

the Roche and Applera licenses. In June 2006, the Applera patent license agreement was expanded to include additional Company products, for which the Company paid an additional $0.5 million. The intangible assets related to the Applera and Roche licenses are amortized on a straight-line basis over their useful lives of approximately 10 and 15 years, respectively, with the amortization recorded as part of the cost of product sales. The Company also paid approximately $1.2 million in back royalties related to the Applera license, which was expensed during the quarter ended March 31, 2004.

The Company also agreed to pay Applera and Roche ongoing royalties on sales of any products incorporating the licensed patents. Resulting product royalties are recorded as part of the cost of product sales when the related product sales are recognized.

In September 2005, the Company entered into a license agreement with Abaxis, Inc. ("Abaxis"), pursuant to which Abaxis granted the Company a non-exclusive, worldwide, royalty-bearing license to certain Abaxis patents relating to lyophilization technology in accordance with the provisions specified in the agreement. Under the agreement, the Company will be able to make, distribute and sell products for nucleic acid based amplification assays. In exchange for the license rights, the Company agreed to (i) make an upfront license payment of $0.5 million, (ii) pay royalties during the term of the agreement and (iii) pay a yearly license maintenance fee during the term of the agreement, which fee will be creditable against any royalties due during such calendar year.

In November 2005, Cepheid entered into a license agreement with DxS Limited ("DxS"), a private United Kingdom based company, pursuant to which DxS granted Cepheid a non-exclusive, worldwide, royalty-bearing license to the DxS Scorpions patents and other intellectual property rights relating to its Scorpions technology for the real-time PCR detection of nucleic acid amplification. This amends a December 2004 agreement, which provided for license rights to develop and commercialize license technology in the environmental, veterinarian, forensics identity relationship testing, and agricultural fields. Under the Agreement, and subject to certain limitations set forth therein, Cepheid will be able to use the licensed rights to develop and sell assay products incorporating the licensed technology in the human in vitro diagnostics field.

In September 2006, Cepheid entered into a sublicense agreement with Abbott Laboratories ("Abbott"), pursuant to which Abbott granted Cepheid a non-exclusive, world-wide, non-transferable right to Abbott's exclusive license to certain patents from the Baylor College of Medicine. Under this sublicense agreement, the Company will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as multiple genomic DNA amplification for deletion detection. In September 2006, Cepheid also entered into a license agreement with Abbott, pursuant to which Abbott granted Cepheid a non-exclusive, world-wide, non-transferable right to a certain Abbott patent. Under this license agreement, the Company will be able to make, use, distribute and sell products incorporating the patented technology generally characterized as detection of cervical chlamydia trachomatis infection. License payments for these agreements totaled $2.0 million. The intangible assets related to these sublicenses are amortized on a straight-line basis over their useful lives of approximately 7 and 9 years, respectively, with the amortization recorded as part of the cost of product sales.

In January 2007, Cepheid entered into a sublicense agreement with bioMerieux SA, pursuant to which bioMerieux SA granted Cepheid a non-exclusive, worldwide, irrevocable sublicense to certain patents that relate to the diagnosis of methicillin resistant staphylococcus aureus. The patents are owned by Kainos Laboratories Inc. and Professor Keiichi Hiramatsu and have been exclusively licensed to bioMerieux SA with the right for bioMerieux SA to sub-license. Under the sublicense agreement, and subject to certain limitations set forth therein, Cepheid is able to use the licensed rights to develop and sell products for use in connection with its GeneXpert and SmartCycler platforms. In exchange for such rights, Cepheid agreed to pay an initial license fee of approximately $4.0 million and quarterly royalties based on net product sales during the term of the sublicense agreement, which expires when the last of the patents licensed under the agreement expires. The license fee was paid in the first quarter of 2007 and is being amortized on a straight-line basis over the useful life of approximately 9 years, with the amortization recorded as part of the cost of product sales.

4. Collaboration Profit Sharing

Collaboration profit sharing represents the amount that the Company pays to ABI under our collaboration agreement to develop reagents for use in the Biohazard Detection System ("BDS") developed for the United States Postal Service ("USPS"). Under the agreement, computed gross margin on anthrax cartridge sales are shared equally between the two parties. As of December 31, 2007 and 2006, the accrued profit sharing liability was $0.5 million and $3.5 million, respectively. Collaboration profit sharing expense was $12.3 million, $15.0 million and $14.5 million for the years ended December 31, 2007, 2006 and 2005. The total revenues and cost of sales related to these cartridge sales are included in the respective balances in the consolidated statement of operations.

5. Collaborative Agreements and Contracts

bioMerieux, Inc.

In December 2003, the Company entered into an agreement with bioMerieux, Inc. for bioMerieux to develop DNA testing products using its proprietary nucleic acid sequence-based amplification technology to be run on systems employing the Company's GeneXpert systems. Under the agreement, bioMerieux has paid the Company a $10.0 million license fee, and an additional $5.0 million payment will become due when and if bioMerieux commercializes its first product based on our technology. The Company may also receive potential product purchases and royalty payments on end-user GeneXpert test cartridge sales under the agreement. The $10.0 million license fee received from bioMerieux was deferred and is being amortized over the period of approximately five years, which represents the estimated period of our continuing involvement under this agreement.

Infectio Diagnostic, Inc./GeneOhm Sciences, Inc.

In November 2003, the Company entered into a series of agreements with Infectio Diagnostics, Inc. ("IDI"). IDI merged with GeneOhm Sciences, Inc. in 2004. GeneOhm Sciences, Inc. was acquired by Becton, Dickson and Company ("BDC") in February 2006. Under these agreements, the Company received non-exclusive worldwide, excluding Canada, distribution rights to IDI tests for GBS, MRSA and vancomycin resistant enterococcus ("VRE") that have been configured for use with the SmartCycler system. The distribution rights relating to tests for MRSA were terminated in November 2006, and the distribution rights relating to GBS terminated in April 2007. In the event that BDC introduces a VRE product for the SmartCycler system, our distribution rights relating to VRE tests will terminate two years from the date of such introduction. IDI received non-exclusive worldwide rights to distribute the Company's SmartCycler system for use with IDI tests. Such IDI distribution rights, now owned by BDC, have an initial term that expires in November 2008.

ABI and Northrop Grumman Corporation

In October 2002, the Company entered into a collaboration agreement with ABI to develop reagents for use in the USPS BDS program, which was developed by the consortium led by Northrop Grumman Corporation. Under the agreement, reagents will be manufactured by ABI for packaging by the Company into its GeneXpert test cartridges and sold by the Company for use in the BDS. This agreement calls for the computed gross margin on sales of anthrax cartridges for the USPS BDS program to be equally shared between the two parties.

In August 2007, the Company entered into a five-year master purchase order with Northrop Grumman for the purchase of up to $200 million in anthrax test cartridges and associated materials. The agreement covers the USPS fiscal years of 2007 through 2011. Under the terms of the agreement, the purchase quantity of anthrax tests will be determined on an annual basis, based on the USPS fiscal year of October 1 through September 30.

Lawrence Livermore National Laboratory

The Company has a worldwide exclusive license with Lawrence Livermore National Laboratory ("LLNL") to use or sublicense certain patent rights and to make, have made, import, and use certain licensed products relating to the patent rights for the use of rapid thermal cycling technology with real time optical detection for nucleic acid amplification. The Company paid LLNL an issuance fee of $0.2 million for this technology in 1997. In addition, upon commercialization of any product containing the licensed technology, including the SmartCycler system, the Company is required to pay royalties to LLNL based on net sales.

Foundation for Innovative New Diagnostics

In May 2006, Cepheid entered into an agreement with the Foundation for Innovative New Diagnostics ("FIND") to develop a simple, rapid test that can detect mycobactrium tuberculosis and associated rifampin resistance from human sputum samples. Under the agreement, Cepheid is responsible for the development of a 6-color GeneXpert system to accomplish such test and the development of an enhanced manufacturing line for the manufacture of test cartridges used in the test. FIND will reimburse Cepheid at agreed upon amounts. The term of the development portion of the agreement is for 30 months. The supply term of the agreement is for twelve years, unless terminated by either party in accordance with relevant provisions of the agreement.

Centers for Disease Control and Prevention

In December 2006, Cepheid entered into a contract with the Centers for Disease Control and Prevention ("CDC") for the first two phases of a five phase program for the development of a new Point-of-Care *in vitro* diagnostic product that tests for influenza viruses A and B, and H5N1, providing general clinical utility for seasonal flu diagnosis in addition to its application in the case of an avian flu pandemic. Under the first two phases of the program, Cepheid was responsible to develop a pre-clinical development plan, a clinical

development and a regulatory plan. In September 2007, the contract was terminated. Under the contract, Cepheid recorded revenue of $2.9 million in 2007 and $0.1 million in 2006.

bioMerieux SA

In January 2007, the Company entered into a collaboration agreement with bioMerieux SA for the development, production and marketing of a line of sepsis products, based upon the Company's real-time polymerase chain reaction ("PCR") technologies. Both companies will jointly develop the products, with the initial development program relating to sepsis products for bacterial and fungal identification assays, as well a series of genetic markers for antibiotic resistance. Cepheid will exclusively manufacture these Cepheid products. bioMerieux SA will market and distribute these test products on an exclusive worldwide basis. Each party will bear its own costs of joint development. Cepheid will sell the products to bioMerieux SA at an agreed upon price. The term of the collaboration agreement is 15 years following the latest date that a sepsis product or HAP product is successfully launched and may be terminated earlier under certain circumstances.

6. Equipment Financing and Line of Credit

In November 2004, the Company entered into an agreement with a financial lending institution for a revolving line of credit totaling $4.0 million of which up to $2.0 million could be used for letters of credit. The agreement was subsequently amended in May 2005 to increase the existing line of credit to $4.3 million and to add an equipment financing line of $3.0 million. The equipment line of credit and revolving line of credit were collateralized by the Company's accounts receivable, certain equipment, tenant improvements, or other personal property of the Company financed pursuant to the agreement, and bore an annual interest rate, at the Company's option, equal to the lender's prime rate or LIBOR plus 2.5% per annum. After being extended in November 2006, the agreement matured in February 2007. As of December 31, 2006 and 2007, the Company had no balance outstanding under the revolving or equipment line of credit.

The Company also financed a portion of its equipment purchases under an equipment financing agreement with another financial lending institution. The equipment loans under this financing arrangement were to be repaid over 36 to 48 months at interest rates ranging from 7.4% to 9.9% and were secured by the related equipment. As of December 31, 2007 and 2006, the balance outstanding totaled $0 and $0.3 million, respectively.

7. Acquisitions

Sangtec

On February 14, 2007, Cepheid completed the purchase of 100% of the outstanding stock of Sangtec, a company located in Bromma, Sweden, from Nycomed-owned Altana Technology Projects GmbH. Sangtec was a broad-based PCR molecular diagnostics company that developed and manufactured products for standardized nucleic acid testing of infectious diseases. The acquisition brought Cepheid the ability to provide a line of products for potential use in managing infections of immuno-compromised patients, a research and development operation to develop and expand its clinical test products, and a reagent manufacturing base in Europe. Subsequent to the acquisition, Sangtec's name was changed to Cepheid AB.

The acquisition was accounted for as a purchase transaction in accordance with SFAS No. 141, "Business Combinations", and accordingly, the tangible and intangible assets acquired and liabilities assumed were recorded at their estimated fair value at the date of the acquisition. The aggregate purchase price of the acquisition was approximately $27.5 million, including $26.7 million cash (net of $0.6 million cash acquired) and $0.8 million direct acquisition costs. The following table summarizes the preliminary allocation of the purchase price based on the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands).

Current assets	$ 3,571
Property, plant and equipment	1,337
Intangible assets	9,970
Current liabilities	(2,197)
Goodwill	14,844
	$ 27,525

In performing the purchase price allocation, the Company considered, among other factors, its intention for future use of the acquired assets, analyses of historical financial performance and estimates of future performance of Sangtec's products. The fair value of intangible assets was based in part on a valuation completed by a third-party valuation firm using a discounted cash flow and

income approaches and other valuation techniques, as well as estimates and assumptions provided by he Company. The acquired intangible assets consisted of the following:

	Fair Value (in thousands)	Useful Life (in years)
Existing technology	$ 7,800	9
Contract manufacturing agreement	1,700	5
Distributor relationships	400	9
Trademark	70	3
	$ 9,970	

Existing technology is comprised of a proprietary diagnostic product line, affigene, The affigene product is a CE-labeled, standardized assay designed to provide diagnostic guidance in the infectious disease and oncology fields. Existing technology also includes a combination of processes and patents related to the design and development of Sangtec's products. The contract manufacturing agreement relates to the revenue generated from two contracts which expire in 2010 and 2011 and have minimum commitments.

The amortization expense related to the existing technology and contract manufacturing was recorded as cost of product sales, and the amortization expense related to distributor relationships and trademark was recorded as selling, general and administrative expense. Total amortization expense recorded for the year ended December 31, 2007 was $0.7 million.

The following table provides pro forma financial information assuming the acquisition of Sangtec had occurred at the beginning of each period presented (in thousands, except per share data):

	Years Ended December 31,	
	2007	2006
Total revenues	$ 130,671	$ 95,829
Net loss	(22,026)	(29,037)
Basic and diluted net loss per share	(0.40)	(0.55)

Actigenics

In August 2006, the Company, through its wholly owned French subsidiary, Cepheid SA, purchased 100% of the stock of Actigenics, a French micro RNA research and services company. The acquisition gave Cepheid direct access to micro RNA markers used in diagnostic and therapeutic products and the related discovery, validation and development processes. Cepheid paid $1.2 million in cash. In addition, Cepheid assumed approximately $0.7 million of liabilities, and acquired $0.2 million of tangible assets.

Of the $1.2 million paid, $0.7 million represented deferred prepaid compensation expense to be recognized over a service period of three years from the August 2006 acquisition date. This deferred compensation expense is being amortized on a straight line basis.

The acquisition was accounted for as a purchase transaction in accordance with SFAS 141, and accordingly, the tangible and intangible assets acquired and liabilities assumed were recorded at their estimated fair value at the date of the acquisition. The results of Actigenics operations have been included in the Company's consolidated results of operations from the acquisition date. Pro forma results of operations have not been presented because the effect of the acquisition was not material.

The purchase price was allocated as follows (in thousands):

Deferred compensation expense	$ 730
Marker technology	591
Discovery and validation technology	197
In-process research and development	139
Liabilities assumed, net of assets acquired	(505)
Total allocation of purchase price	$ 1,152

The marker technology and discovery and validation technology will be amortized on a straight-line basis over ten and six year periods, respectively. Immediately subsequent to the acquisition date, in accordance with FASB Interpretation No. 4, "Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method—an interpretation of FASB Statement No. 2", $0.1 million of in-process research and development intangible assets with no alternative future use was written off.

8. Commitments, Contingencies and Legal Matters

Facility Leases

The Company leases its Sunnyvale, California headquarters under two operating leases. The primary lease expires in March 2012 and provides for a three percent annual base rent increase. In connection with this lease agreement, the Company obtained an irrevocable standby letter of credit collateralized by a certificate of deposit, which has been classified as restricted cash on the consolidated balance sheet. In April 2007, the Company entered into a sublease of additional office and manufacturing space that expires in September 2009. In December 2005, the Company also entered into a lease for additional warehouse space that expires in September 2010. In May 2005, the Company entered into a facility lease for a research and development center in Bothell, Washington that expires in August 2011. In Bromma, Sweden, the Company leases office and manufacturing space pursuant to a lease that expires in December 2009. Minimum annual rental commitments under facility operating leases at December 31, 2007 are as follows (in thousands):

Years Ending December 31,	
2008	$ 2,963
2009	2,982
2010	2,061
2011	1,916
2012	382
Total minimum payments	$ 10,304

Rent expense for the years ended December 31, 2007, 2006 and 2005 was $2.6 million, $1.9 million and $1.7 million, respectively.

Contingencies

The Company responds to claims arising in the ordinary course of business. In certain cases, management has accrued estimates of the amounts it expects to pay upon resolution of such matters, and such amounts are included in other accrued liabilities. Should the Company not be able to secure the terms it expects, these estimates may change and will be recognized in the period in which they are identified. Although the ultimate outcome of such claims is not presently determinable, management believes that the resolution of these matters will not have a material adverse effect on the Company's financial position, results of operations and cash flows.

Legal Matters

A complaint filed on December 22, 2005, in the United States District Court for the District of Utah by Idaho Technology, Inc. ("Idaho Technology") and University of Utah Research Foundation was served on the Company in March 2006. The complaint alleged that the Company infringed certain patents licensed by the University of Utah Research Foundation to Idaho Technology.

On January 2, 2007, the Company entered into a Settlement and Cross-License Agreement (the "Settlement Agreement") with Idaho Technology regarding certain Company and Idaho Technology intellectual property (the "Intellectual Property"). The Settlement Agreement provided that the parties dismiss with prejudice litigation related to the Intellectual Property. In addition, the Settlement Agreement provides each of the parties with a non-exclusive, worldwide, fully paid, non-terminable, irrevocable license to certain of the other's patents for use in their respective lines of products and contains certain covenants by each of the parties not to sue the other. Pursuant to the Settlement Agreement, the Company made a payment of $3.35 million to Idaho Technology in January 2007. As of December 31, 2006, the settlement amount was accrued and recorded as an expense in the consolidated statement of operations. Although the Company believed it would not be held liable for infringement had the issue ultimately gone to litigation, it came to the conclusion to settle the litigation. The Company made the Settlement Agreement and payment to avoid incurring significant legal costs to defend its case. The Company's belief that it did not infringe Idaho Technology's patents was based on the Company's detailed legal analysis by outside counsel that the patents referenced in the litigation were either not being infringed and/or that the patents referenced were potentially invalid, due to prior art not specified or referenced in the patents. Due to the fact that the Company did not believe there to be any validity to the patent infringement case, it did not ascribe any value to future product sales and recorded the whole amount as a fiscal 2006 expense.

9. Shareholders' Equity

Common Stock

On March 13, 2006, the Company completed an underwritten public offering of 10,000,000 shares of common stock at a price of $8.60 per share and received proceeds of approximately $80.6 million, net of $5.4 million expenses. On April 5, 2006, the underwriters exercised their over allotment option and purchased an additional 1,419,910 shares of common stock at a price of $8.60 per share, and the Company received additional proceeds of $11.3 million, net of $0.9 million expenses.

Stock Option Plans

On April 16, 1997, the Board of Directors approved a Stock Option Plan ("1997 Plan"). The 1997 Plan provided for annual increases in the number of shares available for issuance on the first business day of each year, beginning January 1, 2001, equal to the lesser of 1,000,000 shares, 3.0% of the outstanding shares on the date of the annual increase or such amount as may be determined by the Board, and were 1,000,000 in 2006 and 2005. In May 2003, the shareholders approved an amendment to terminate the 2000 Non-Employee Directors' Stock Option Plan ("Directors' Plan") and reserve for issuance under the 1997 Plan the shares previously available for issuance under the Directors' Plan.

Under the 1997 Plan, as amended, incentive stock options may be granted to employees, and nonstatutory stock options may be granted to employees, directors and consultants. Options are granted at an exercise price of no less than the fair market value per share of the common stock on the date of grant and expire not later than ten years from the date of grant. Options under the 1997 Plan generally vest 25% one year after the date of grant and then on a pro rata basis over the following 36 months. All options contain provisions restricting their transferability and limiting their exercise in the event of termination of employment or the disability or death of the optionee.

On April 27, 2006, the Company's shareholders approved the 2006 Equity Incentive Plan ("2006 Plan"), which was approved by the Board in February 2006. On April 27, 2006, the Board also terminated the 1997 Plan. No new grants will be made under the 1997 Plan, and options granted or shares issued under the 1997 Plan that were outstanding on the date the 1997 Plan was terminated will remain subject to the terms of the 1997 Plan. Shares of common stock reserved for issuance under the 2006 Plan include (i) an initial authorization of 3,800,000 shares of common stock, (ii) shares reserved but unissued under the 1997 Plan as of the date the 1997 Plan was terminated and (iii) shares subject to awards granted under the 1997 Plan that are cancelled, forfeited or repurchased by the Company or expire after the 1997 Plan termination.

Under the 2006 Plan, the Company may grant incentive stock options ("ISOs") and non-qualified stock options ("NQSOs"), restricted stock awards ("RSAs"), stock bonus awards ("SBAs"), stock appreciation rights ("SARs"), restricted stock units ("RSUs") and performance share awards ("PSAs"). ISOs may be granted only to employees and directors of the Board, and all other awards may be granted to Company employees and directors and to consultants, independent contractors and advisors of the Company for services rendered. Any award, other than a stock option or a SAR, shall reduce the number of shares available for issuance by 1.6 shares for each share subject to such award (for a stock option or a SAR this ratio shall remain 1:1). The 2006 Plan is administered by the Compensation Committee of the Board ("Committee"). The following provides a general description of each type of award under the 2006 Plan.

Stock options may be granted at no less than the fair market value per share of common stock on the date of the grant (at 110% of fair market value for ISOs granted to 10% shareholders), expire not later than 7 years from the date of grant (5 years from the date of grant for ISOs granted to 10% shareholders) and generally vest 25% one year after the date of grant and then on a pro rata basis over the following 36 months.

RSAs may be granted at a purchase price that is less than fair market value on the date of grant, and the restrictions are determined by the Committee and may be based on years of service with the Company or completion of performance goals during a period. The Committee will determine the extent that the RSA is earned prior to the payment for the shares awarded.

SBAs may be granted for past or future services and may contain restrictions based on years of service with the Company or completion of performance goals during a period. No payment will be required for shares awarded under an SBA. Payments to recipients of an SBA may be in the form of cash, shares of common stock, or a combination thereof, based on the fair market value of shares earned under the SBA. The Committee will determine the number of shares to be awarded under the SBA and the extent that the SBA is earned prior to the payment for the shares awarded.

SARs are awards for past or future services that may be settled in cash or shares of common stock, including restricted stock, having a value equal to the number of shares subject to the SAR multiplied by the difference between the fair market value on the date of grant and the exercise price. The Committee determines the terms of each SAR, including the number of shares of common stock subject to the SAR, the exercise price and the times during which the SAR may be settled, consideration to be made on settlement, and effect of the participant's termination. If SARs are awarded based on performance goals, the Committee will determine the extent that the SAR is earned. SARs may be granted at an exercise price that may be less than fair market value per share of common stock on the date of grant, may be exercisable at one time or from time to time, and have a term not to exceed seven years.

RSUs are awards for past or future services that may be settled in cash or shares of common stock, including restricted stock. The Committee determines the terms of each RSU, including the number of shares of common stock subject to the RSU, the times during which the RSU may be settled, consideration to be made on settlement, and effect of the participant's termination. If RSUs are awarded based on performance goals, the Committee will determine the extent that the RSU is earned. The number of shares subject to the RSU may be fixed or may vary depending on in accordance with performance goals as determined by the Committee. While the RSU shall be paid currently, under certain circumstances the Committee may permit the participant to defer settlement of the RSU.

PSAs are awards denominated in shares of common stock that may be settled in cash or issuance of such shares (which may consist of restricted stock). The Committee will determine the terms of each PSA, including the number of shares of common stock subject to the PSA, the performance factors and period that shall determine the time and extent to which each PSA shall be settled, consideration to be made on settlement, and effect of the participant's termination. The Committee will determine the extent that the PSA is earned. The number of shares subject to the PSA may be fixed or may vary depending on in accordance with performance goals as determined by the Committee.

Pursuant to the Change of Control Retention and Severance Agreements between the Company and its executives, in the event of an executive's termination upon a change of control, all of the executive's outstanding stock options granted by the Company to the executive prior to the change of control shall become fully vested and exercisable immediately prior to the effective date of the termination upon a change of control. Approximately 1.0 million shares of the executive options outstanding were remeasured at various dates in 2003 and 2002, the dates of the modification, for the change in control provision. Such remeasured shares, if outstanding at the time of a change in control, would result in additional stock-based compensation recorded at that time. The amount of such additional stock-based compensation would not be significant.

A summary of option activity under all plans is as follows:

	Shares	Weighted Average Exercise Price
Balance, December 31, 2004	5,597,564	$ 5.53
Granted	1,972,280	$ 8.98
Exercised	(438,414)	$ 4.79
Forfeited	(487,531)	$ 6.71
Balance, December 31, 2005	6,643,899	$ 6.53
Granted	2,127,575	$ 8.68
Exercised	(641,920)	$ 4.59
Forfeited	(737,548)	$ 8.62
Balance, December 31, 2006	7,392,006	$ 7.12
Granted	2,091,867	$ 12.36
Exercised	(410,644)	$ 6.38
Forfeited	(168,567)	$ 9.66
Balance, December 31, 2007	8,904,662	$ 8.48

The following table summarizes information about options outstanding at December 31, 2007:

	Options Outstanding				Options Exercisable			
Exercise Price	Number of Shares (in 000s)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in 000s)	Number of Shares (in 000s)	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Aggregate Intrinsic Value (in 000s)
$1.50 to $3.61	1,255	$ 3.18	4.07	$ 29,080	1,255	4.07	$ 3.18	$ 29,079
$3.69 to $5.25	977	$ 4.37	4.97	21,481	977	4.97	$ 4.37	21,481
$5.26 to $7.38	999	$ 7.22	6.45	19,104	769	6.32	$ 7.18	14,739
$7.39 to $8.88	1,366	$ 8.47	6.75	24,418	602	6.65	$ 8.48	10,767
$8.93 to $9.11	1,174	$ 9.06	5.89	20,302	459	6.23	$ 9.05	7,935
$9.13 to $10.74	1,076	$ 9.65	6.55	17,973	699	6.58	$ 9.68	11,643
$10.79 to $11.88	440	$ 11.35	6.96	6,596	124	6.56	$ 10.82	1,930
$11.94 to $11.94	1,075	$ 11.94	6.32	15,486	—	—	$ —	—
$12.04 to $25.09	543	$ 17.65	6.11	4,727	70	2.82	$ 14.32	845
	8,905	$ 8.48	5.93	$ 159,167	4,955	5.51	$ 6.49	$ 98,419

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on the Company's closing stock price of $26.35 at December 31, 2007 (the last quoted market price in 2007), which would have been received by award holders had all award holders exercised their awards that were in-the-money as of that date. The aggregate intrinsic value of options exercised during 2007, 2006 and 2005 was $4.6 million, $2.7 million and $2.1 million, respectively.

A summary of the status of the nonvested shares as of December 31, 2007, and changes during the year ended December 31, 2007, is as follows:

	Shares (in 000s)	Weighted Average Grant Date Fair Value
Non-vested at beginning of year	3,500	$ 6.46
Granted	2,092	$ 6.75
Vested	(148)	$ 6.50
Forfeited	(1,494)	$ 6.41
Non-vested at end of year	3,950	$ 6.63

A summary of all award activity, which consists of RSAs, is as follows:

	Shares	Weighted Average Grant Date Fair Value
Balance, December 31, 2005	—	$ —
Granted	20,000	$ 8.00
Vested	—	$ —
Balance, December 31, 2006	20,000	$ 8.00
Granted	96,000	$ 14.73
Vested	(25,250)	$ 13.64
Balance, December 31, 2007	90,750	$ 13.55

In accordance with the 2006 Plan, RSAs granted in 2007 and 2006 reduced the number of shares available for future grant by a factor of 1.6 for each share subject to such award, or 153,600 and 32,000 shares, respectively.

Employee Stock Purchase Plan

The 2000 Employee Stock Purchase Plan ("ESPP") was adopted in April 2000 and amended in June 2003. The ESPP permits eligible employees of the Company and its participating subsidiaries to purchase common stock at a discount up to a maximum of 15% of compensation through payroll deductions during defined offering periods. The price at which stock is purchased under the ESPP is equal to 85% of the fair market value of the common stock on the first or last day of the offering period, whichever is lower. The number of shares available for future issuance increase annually equal to the lesser of 200,000 shares, 0.75% of the outstanding shares on the date of the annual increase or a lesser amount determined by the Board.

Non-Employee Director Stock Options

In March 2000, the Company adopted the Directors' Plan and reserved a total of 200,000 shares of common stock for issuance thereunder. Each non-employee director who becomes a director of the Company will be automatically granted a NQSO to purchase 15,000 shares of common stock on the date on which such person first becomes a director. At the first board meeting following each annual shareholders meeting, beginning with the first board meeting after the first annual shareholders' meeting, each non-employee director then in office for over six months will automatically be granted a NQSO to purchase 5,000 shares of common stock. The exercise price of options under the Directors' Plan will be equal to the fair market value of the common stock on the date of the grant. The term of these options is 10 years.

In May 2003, the Directors' Plan was terminated pursuant to amendments to the 1997 Plan approved by the Board and the shareholders. Upon the termination of the Directors' Plan, no further options were granted under the Directors' Plan, and all shares then reserved for issuance under the Directors' Plan that were not subject to outstanding options granted under the Directors' Plan became reserved and available for issuance under the 1997 Plan. Options and shares granted or issued under the Directors' Plan that were outstanding on the date the Directors' Plan was terminated will remain subject to the terms of the Directors' Plan. After the Directors' Plan was terminated, any shares subject to options issued under the Directors' Plan that cease to be subject to the options for any reason other than option exercise, and any shares issued under the Directors' Plan that are repurchased by the Company or forfeited, become available for grant under the 1997 Plan. Under the 1997 Plan, as amended, new non-employee directors will receive nondiscretionary, automatic grants of options to purchase 15,000 shares of the common stock upon joining the Board, and the continuing non-employee directors will receive nondiscretionary, automatic grants of options to purchase 7,500 shares of common stock each year after the annual meeting of shareholders.

On April 27, 2006, the 1997 Plan was terminated and replaced by the 2006 Plan. Under the 2006 Plan, non-employee directors will automatically be granted NQSOs to purchase 25,000 shares of common stock upon initial election or appointment to the Board, which vest and become exercisable in equal amounts on each of three annual anniversary dates of the grant date as long as the director remains on the Board. On the date of the first Board meeting following each annual shareholder meeting each non-employee director then in office for longer than six months will automatically be granted NQSOs to purchase 12,500 shares of common stock, which vest and become exercisable on the one-year anniversary from the grant date as long as the director remains on the Board. The Board may also make discretionary grants to purchase common stock to any non-employee director that vest and become exercisable as determined by the Board. On April 27, 2006, the Board granted an option under the 2006 Plan to purchase 10,000 shares of common stock at $9.18 per share to a non-employee director who became a member of the Board in February 2006. Such option vests and becomes exercisable in equal amounts on each of three annual anniversary dates of the grant date as long as the director remains on the Board. The exercise price of non-employee director options will be equal to the fair market value of the common stock on the date of the grant.

Reserved Shares

As of December 31, 2007, the Company has reserved shares of common stock for future issuance as follows (in thousands):

Stock Options:	
Options and awards outstanding for all plans	8,905
Reserved for future grants	1,488
ESPP	155
	10,548

Stock-Based Compensation

Fair Value—The fair value of the Company's stock options granted to employees and shares purchased by employees under the ESPP for the years ended December 31, 2007 and 2006 was estimated using the following assumptions:

	Years Ended December 31,	
	2007	2006
OPTION SHARES:		
Expected Term (in years)	5.00	5.00
Volatility	0.56	0.96
Expected Dividends	0.00%	0.00%
Risk Free Interest Rates	4.49%	4.87%
Estimated Forfeitures	10.60%	13.45%
Weighted Average Fair Value	$ 6.76	$ 6.65
ESPP SHARES:		
Expected Term (in years)	1.25	1.25
Volatility	0.47	0.49
Expected Dividends	0.00%	0.00%
Risk Free Interest Rates	4.95%	5.01%
Estimated Forfeitures	10.60%	13.45%
Weighted Average Fair Value	$ 3.94	$ 3.42

Stock Based Compensation Cost—Prior to the adoption of SFAS 123(R), the Company recorded stock-based compensation in accordance with APB 25 when the option price was less than the fair market value. As of December 31, 2003, all deferred compensation previously recognized had been amortized to expense. The following table is a summary of the major categories of stock compensation expense recognized in accordance with SFAS 123(R) for the year ended December 31, 2007 and 2006 (in thousands).

	Years Ended December 31,	
	2007	2006
Cost of product sales	$ 794	$ 584
Research and development	4,294	2,839
Selling, general and administrative	6,032	3,907
Total stock-based compensation cost	$ 11,120	$ 7,330

The impact on 2007 and 2006 basic and diluted net loss per share resulting from the adoption of SFAS 123(R) was $0.20 and $0.14, respectively.

The above stock-based compensation cost includes $1.5 million and $1.1 million related to ESPP for 2007 and 2006, respectively. In addition, stock-based compensation cost of approximately $0.5 million and $0.2 million was included in inventory as of December 31, 2007 and 2006, respectively.

In December 2007, the Company entered into a separation and consulting agreement with John R. Sluis, the Company's former Senior Vice President and Chief Financial Officer. Under the terms of the agreement, during the twelve months following December 31, 2007, Mr. Sluis is to provide consulting services to the Company up to a predetermined number of hours. During the twelve-month period ending December 31, 2008, unvested options previously granted to Mr. Sluis will continue to vest according to the schedules set forth in each such option. At the conclusion of the consulting period, provided Mr. Sluis has completed his duties to the satisfaction of the Company's Chief Executive Officer, an additional 24,000 then-unvested shares that are subject to such options will become vested and exercisable. As a result of the modification of Mr. Sluis' existing options, the Company recorded additional stock-based compensation of $0.8 million in 2007. In addition, Mr. Sluis will continue to receive his existing salary on the effective date of his retirement of $0.3 million for his consulting services, which was accrued and recorded as an expense in 2007.

As of December 31, 2007, the total compensation cost related to unvested stock-based grants awarded under the Company's 1997 Plan and 2006 Plan but not yet recognized was approximately $20.7 million, which is net of estimated forfeitures of $3.9 million. This cost will be amortized on a straight line basis over a weighted average period of approximately 2.73 years and will be adjusted for subsequent changes in estimated forfeitures.

At December 31, 2007, the total compensation cost related to options to purchase the Company's common shares under the ESPP but not yet recognized was approximately $0.9 million. The cost will be amortized on a straight-line basis over the two year offering period, as such term is defined in the ESPP.

10. Employee Benefit Plan

Effective January 1, 1998, the Company adopted a 401(k) plan that allows eligible employees to contribute a percentage of their qualified compensation subject to IRS limits. The Company has the discretion to make matching contributions each year. Contributions made by the Company for the years ended December 31, 2007, 2006 and 2005 were $0.2 million, $0, and $0, respectively.

11. Income Taxes

The Company has no U.S. federal or state income tax provision for any period as it has incurred operating losses in all periods. Income tax expense of $0.2 million in 2007 represents current foreign income taxes related to our French subsidiary, and no foreign income taxes were recorded in 2006 or 2005.

The Company has substantially concluded all U.S. federal income tax matters for years through December 31, 2002. For federal income tax purposes, the open years are from 1996 through 2007 due to net operating loss carryforwards relating to these years. Substantially all material state, local and foreign income tax matters have been concluded for years through December 31, 2001. For California state income tax purposes, the open years are from 1997 through 2007 due to either research credit carryovers or net operating loss carryforwards.

The Company anticipates that the total unrecognized tax benefits will not significantly change due to the settlement of audits and the expiration of statute of limitations prior to December 31, 2008.

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets are as follows (in thousands):

	December 31,	
	2007	2006
Net operating loss carryforwards	$ 45,272	$ 43,811
Capitalized research and development costs	1,384	1,855
Research and other credit carryforwards	7,105	8,489
Accruals and reserves	414	335
Stock option compensation	5,031	2,074
Other	3,951	3,401
Total deferred tax assets	63,157	59,965
Valuation allowance for deferred tax assets	(59,893)	(59,965)
Deferred tax liability	(3,264)	—
Net deferred tax assets	$ —	$ —

Realization of deferred tax assets is dependent upon future earnings, if any, the timing and amount of which are uncertain. Accordingly, the net deferred tax assets have been fully offset by a valuation allowance. The valuation allowance decreased by approximately $0.1 million and increased by $17.6 million and $5.5 million during the years ended December 31, 2007, 2006 and 2005, respectively.

As of December 31, 2007, the Company had net operating loss carryforwards for federal income tax purposes of approximately $124.8 million, which expire in the years 2011 through 2027, and federal research and development tax credits of approximately $4.1 million, which expire in the years 2012 through 2026. As of December 31, 2007, the Company had net operating loss carryforwards for state income tax purposes of approximately $47.2 million, which expire in the years 2011 through 2017, and state research and development tax credits of approximately $2.9 million, which have no expiration date.

Utilization of the Company's net operating loss may be subject to a substantial annual limitation due to ownership change limitations provided by the Internal Revenue Code and similar state provisions. Such annual limitation may result in the expiration of net operating loss before utilization.

Undistributed earnings of the Company's foreign subsidiaries of approximately $1.4 million and $0.5 million at December 31, 2007 and 2006, respectively, are considered to be indefinitely reinvested, and, accordingly, no provisions for federal and state income taxes have been provided thereon. Upon distribution of those earnings in the form of dividends or otherwise, the Company would be subject to both federal income taxes, subject to an adjustment for foreign income tax credit, and withholding taxes payable to various foreign countries. The distribution of such foreign earnings to the U.S. parent would have no U.S. tax impact as the net operating loss carryforwards exceed the undistributed earnings.

The following table summarizes the activity related to our unrecognized tax benefits (in thousands):

Balance at January 1, 2007	$	200
Increase related to current year tax positions		673
Increase for tax positions of prior years		2,802
Balance at December 31., 2007	$	3,675

All of the unrecognized tax benefits would affect our effective tax rate if recognized, before consideration of certain valuation allowances.

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SUPPLEMENTARY DATA
QUARTERLY FINANCIAL INFORMATION

	Quarters Ended			
	Mar 31	June 30	Sep 30	Dec 31
	(Unaudited) (In thousands, except per share data)			
2007				
Total revenues	$ 25,544	$ 27,173	$ 36,329	$ 40,427
Costs and operating expenses:				
Cost of product sales	13,877	13,879	19,966	21,452
Collaboration profit sharing	3,497	2,731	2,729	3,299
Research and development	6,922	7,439	8,371	8,717
Selling, general and administrative	8,428	9,105	10,856	12,692
Total costs and operating expenses	32,724	33,154	41,922	46,160
Loss from operations	(7,180)	(5,981)	(5,593)	(5,733)
Other income (expenses), net	1,027	740	852	658
Net loss, before income tax expense	(6,153)	(5,241)	(4,741)	(5,075)
Income tax expense	—	—	—	(213)
Net loss	$ (6,153)	$ (5,241)	$ (4,741)	$ (5,288)
Basic and diluted net loss per share	$ (0.11)	$ (0.10)	$ (0.09)	$ (0.10)
Weighted average shares used in computing basic and diluted net loss per share	55,012	55,149	55,356	55,529
2006				
Total revenues	$ 20,161	$ 19,847	$ 23,762	$ 23,582
Costs and operating expenses:				
Cost of product sales	11,393	11,683	13,281	12,443
Collaboration profit sharing	3,811	3,843	3,813	3,507
Research and development	5,829	5,807	5,568	6,682
In-process research and development	—	—	139	—
Selling, general and administrative	6,146	6,921	6,146	7,257
Expense for patent related matter	—	—	—	3,350
Total costs and operating expenses	27,179	28,254	28,947	33,239
Loss from operations	(7,018)	(8,407)	(5,185)	(9,657)
Other income (expenses), net	346	1,365	1,215	1,356
Net loss	$ (6,672)	$ (7,042)	$ (3,970)	$ (8,301)
Basic and diluted net loss per share	$ (0.15)	$ (0.13)	$ (0.07)	$ (0.15)
Weighted average shares used in computing basic and diluted net loss per share	44,946	54,518	54,771	54,930

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

Not applicable.

ITEM 9A. *CONTROLS AND PROCEDURES*

Evaluation of Disclosure Controls and Procedures

As of December 31, 2007, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Acting Principal Financial Officer of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(a) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended). Based on the evaluation, we concluded that our disclosure controls and procedures are effective.

Management's Annual Report on Internal Control over Financial Reporting

The report of management required under this Item 9A is contained in Item 8 of Part II of this Annual Report on Form 10-K under the heading "Management's Report on Internal Control Over Financial Reporting."

Attestation Report of Independent Registered Public Accounting Firm

The attestation report required under this Item 9A is contained in Item 8 of Part II of this Annual Report on Form 10-K under the heading "Report of Independent Registered Public Accounting Firm".

Changes in Internal Control over Financial Reporting

There were no significant changes in our internal control over financial reporting during the fourth quarter of 2007.

ITEM 9B. *OTHER INFORMATION*

In November 2007, most of our executives entered into trading plans pursuant to Rule 10b5-1 under the Securities Exchange Act of 1934 that provide for periodic sales of shares of our common stock on the basis of parameters described in such trading plans. Trading commenced as early as February 28, 2008, under such plans.

In February 2008, our Board of Directors approved our entry into an amendment of the Rights Agreement, dated as of September 26, 2002, between Cepheid and Computershare Trust Company, for the purpose of increasing the purchase price for each one one-hundredth of a Preferred Share (as defined in the Rights Agreement) pursuant to an exercise of a Right (as defined in the Rights Agreement) from $40.00 to $180.00.

PART III

ITEM 10. *DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE*

Information in response to this item is incorporated herein by reference to our definitive proxy statement for our 2008 annual meeting of stockholders to be held on April 24, 2008. Information related to our executive officers also appears under the caption "Executive Officers of the Registrant" in Item 1 to this report.

ITEM 11. *EXECUTIVE COMPENSATION*

Information in response to this item is incorporated herein by reference to our definitive proxy statement for our 2008 annual meeting of stockholders to be held on April 24, 2008.

ITEM 12. *SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS*

Information in response to this item is incorporated herein by reference to our definitive proxy statement for our 2008 annual meeting of stockholders to be held on April 24, 2008.

ITEM 13. *CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE*

Information in response to this item is incorporated herein by reference to our definitive proxy statement for our 2008 annual meeting of stockholders to be held on April 24, 2008.

ITEM 14. *PRINCIPAL ACCOUNTANT FEES AND SERVICES*

Information in response to this item is incorporated herein by reference to our definitive proxy statement for our 2008 annual meeting of stockholders to be held on April 24, 2008.

PART IV

ITEM 15. *EXHIBITS AND FINANCIAL STATEMENT SCHEDULES*

The following documents are being filed as part of this report on Form 10-K:

(a) Financial Statements

The following financial statements are filed as part of this report under Item 8 — "Financial Statements and Supplementary Data."

Consolidated Balance Sheets

Consolidated Statements of Operations

Consolidated Statements of Shareholders' Equity

Consolidated Statements of Cash Flows

Notes to Consolidated Financial Statements

Supplementary Data: Quarterly Financial Information

(b) Schedule II — Valuation and Qualifying Accounts for the years ended December 31, 2007, 2006 and 2005.

All other schedules are omitted as the required information is inapplicable or the information is presented in the Consolidated Financial Statements and notes thereto in Item 8 above.

(c) Exhibits

The exhibit list in the Index to Exhibits is incorporated herein by reference as the list of exhibits required as part of this report.

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SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS

Description	Balance at Beginning of Year	Costs and Expenses	Deductions	Balance at End of Year
		(In thousands)		
Allowance for doubtful accounts:				
Year ended December 31, 2005	14	—	(3)	11
Year ended December 31, 2006	11	78	(2)	87
Year ended December 31, 2007	87	97	(147)	37

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the city of Sunnyvale, State of California, on the 29th day of February, 2008.

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By: /s/ JOHN L. BISHOP
John L. Bishop
Chief Executive Officer and Director

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints John L. Bishop and Michael T. Myhre or either of them, his true and lawful attorneys-in-fact and agents, with full power of substitution and re-substitution, for him and in his name, place and stead, in any and all capacities to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto the attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that the attorneys-in-fact and agents, or either of them, or their, his substitutes or substitute, may lawfully do or cause to be done by virtue hereof.

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

Signature	Title	Date
/s/ JOHN L. BISHOP John L. Bishop	Chief Executive Officer and Director (Principal Executive Officer)	February 29, 2008
/s/ MICHAEL T. MYHRE Michael T. Myhre	Vice President and Corporate Controller (Acting Principal Financial and Accounting Officer)	February 29, 2008
/s/ THOMAS D. BROWN Thomas D. Brown	Director	February 29, 2008
/s/ THOMAS L. GUTSHALL Thomas L. Gutshall	Director and Chairman of the Board	February 29, 2008
/s/ CRISTINA H. KEPNER Cristina H. Kepner	Director	February 29, 2008
/s/ ROBERT EASTON Robert Easton	Director	February 29, 2008
/s/ DEAN O. MORTON Dean O. Morton	Director	February 29, 2008
/s/ MITCHELL D. MROZ Mitchell D. Mroz	Director	February 29, 2008
/s/ DAVID H. PERSING, M.D., PH.D. David H. Persing	Director	February 29, 2008
/s/ HOLLINGS C. RENTON Hollings C. Renton	Director	February 29, 2008

Exhibit Number	Description of Exhibit	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Articles of Incorporation	S-1	333-34340	3.1	4/7/2000	
3.2	Amended and Restated Bylaws	10-Q		3.01	7/31/2002	
3.3	Certificate of Determination specifying the terms of the Series A Junior Participating Preferred Stock of registrant, as filed with the Secretary of State to the State of California on October 2, 2002	8-A		3.02	10/4/2002	
4.1	Reference is made to Exhibits 3.1 and 3.2					
4.2	Specimen Common Stock Certificate	10-Q		4.01	7/31/2002	
4.3	Rights Agreement dated September 26, 2002 between Cepheid and Computershare Trust Company as Rights Agent, which includes as Exhibit A the form of Certificate of Determination of Series A Junior Participating Preferred Stock, as Exhibit B the Summary of Stock Purchase Rights and as Exhibit C the Form of Rights Certificate	8-A		3.02	10/4/2002	
10.1*	1997 Stock Option Plan, as amended	S-8	333-106181	4.2	6/17/2003	
10.2*	2000 Employee Stock Purchase Plan, as amended	S-8	333-106181	4.1	6/17/2003	
10.3*	2000 Non-Employee Directors' Stock Option Plan	S-8	333-41682	99.3	7/18/2000	
10.4*	2006 Equity Incentive Plan and related forms of agreement for stock options, restricted stock, stock bonuses, stock appreciation rights, restricted stock units and other awards	8-K		99.1	5/2/2006	
10.5*	Form of Indemnification Agreement between Cepheid and its officers and directors	S-1	333-34340	10.6	4/7/2000	
10.6†	License Agreement, dated January 16, 1996, between Cepheid and The Regents of the University of California, Lawrence Livermore National Laboratory	S-1	333-34340	10.9	6/7/2000	
10.7†	Thermal Cycler Supplier Agreement, dated April 15, 2000, between Cepheid and PE Biosystems, a division of PE Corporation	S-1	333-34340	10.16	5/18/2000	
10.8†	Distribution Agreement dated July 11, 2000 between Cepheid and Takara Shuzo Co., Ltd.	10-Q		10.1	11/14/2000	
10.9	Lease Agreement dated October 18, 2001, between Cepheid and Aetna Life Insurance Company	10-K		10.17	3/22/2002	
10.10†	Letter Agreement between Takara Biomedical Co, Ltd. and Cepheid dated January 25, 2002	10-Q		10.2	5/15/2002	
10.11†	Modification of Distribution Agreement dated July 11, 2000 between Cepheid and Takara Biomedical Co., Ltd. dated February 11, 2002	10-Q		10.4	5/15/2002	
10.12†	Collaboration Agreement between Applied Biosystems and Cepheid dated October 11, 2002	10-K		10.28	3/25/2003	
10.13	Change of Control Retention and Severance Agreement between Joseph H. Smith and Cepheid dated June 2, 2003	10-Q		10.3	8/14/2003	
10.14†	Letter Agreement between Aridia Corp. and Cepheid and Infectio Diagnostic Inc. dated November 4, 2003	10-K		10.23	3/12/2004	
10.15†	License Agreement between Cepheid and Infectio Diagnostic	10-K		10.24	3/12/2004	

Exhibit Number	Description of Exhibit	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
	Inc. dated November 4, 2003					
10.16†	Distribution Agreement between Cepheid and Infectio Diagnostic Inc. dated November 4, 2003	10-K		10.25	3/12/2004	
10.17†	Distribution Agreement between Cepheid and Infectio Diagnostic Inc. dated November 4, 2003	10-K		10.26	3/12/2004	
10.18†	License, Development and Supply Agreement between bioMerieux, Inc. and Cepheid dated December 31, 2003	10-K		10.27	3/12/2004	
10.19†	IVD Products Patent License Agreement between Cepheid and F. Hoffmann-La Roche Ltd, effective July 1, 2004	10-Q		10.28	8/9/2004	
10.20†	Real-Time Instrument Patent License Agreement between Applera Corporation and Cepheid, dated April 5, 2004	10-Q		10.29	8/9/2004	
10.21*	Amended and Restated Change of Control Retention and Severance Agreement, dated May 18, 2004, between Cepheid and Joseph Smith	10-Q		10.32	8/9/2004	
10.22*	Amended and Restated Change of Control Retention and Severance Agreement, dated May 18, 2004, between Cepheid and Russel Enns	10-Q		10.33	8/9/2004	
10.23*	Offer letter to Mr. Humberto Reyes from Cepheid dated November 4, 2004	10-K		10.35	2/28/2005	
10.24	Facility lease agreement between Cepheid and Teachers Insurance & Annuity Association of America, Inc. dated May 13, 2005	8-K		99.01	5/18/2005	
10.25*	Employment offer letter between Cepheid and David H. Persing dated July 21, 2005	8-K		99.01	7/26/2005	
10.26	Change of Control Retention and Severance Agreement dated July 21, 2005, by and between Cepheid and David H. Persing	8-K		99.02	7/26/2005	
10.27†	First amendment to the Distribution Agreement between Cepheid and Infectio Diagnostic ("I.D.I.") Inc. of November 4, 2003 by and between Cepheid and GeneOhm Sciences, Inc. dated April 6, 2005	10-Q		10.2	8/4/2005	
10.28*	Form of Stock Option Grant Agreement with certain executive officers of Cepheid approved by Cepheid's Compensation Committee of the Board of Directors on April 27, 2005	10-Q		10.3	8/4/2005	
10.29†	Advanced Authorization Letter Agreement between Cepheid and Northrop Grumman Security Systems dated July 20, 2005	10-Q		10.1	11/3/2005	
10.30†	First amendment to the Distribution Agreement between Cepheid and Infectio Diagnostic ("I.D.I.") Inc. of November 4, 2003 by and between Cepheid and GeneOhm Sciences Canada, Inc. dated September 30, 2005	10-Q		10.4	11/3/2005	
10.31†	License Agreement between Cepheid and Abaxis, Inc. dated September 30, 2005	10-Q		10.5	11/3/2005	
10.32†	License Agreement between Cepheid and DxS Limited dated November 28, 2005	10-K		10.45	2/22/2006	
10.33*	Amended and Restated Change of Control Retention and Severance Agreement dated October 31, 2006 by and between Cepheid and Humberto Reyes	8-K		10.01	11/6/2006	

Exhibit Number	Description of Exhibit	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
10.34*	Employment Agreement dated January 24, 2007, by and between Cepheid and John L. Bishop	8-K		10.1	1/29/2007	
10.35*	Share Purchase Agreement dated February 14, 2007, by and between Cepheid, Altana Technology Projects GmbH, and Altana Pharma AG	8-K		2.1	2/20/2007	
10.36	Settlement and Cross-License Agreement between Cepheid and Idaho Technology, Inc. dated January 2, 2007	10-Q		10.1	5/10/2007	
10.37	Sublicense agreement between Cepheid and bioMerieux S.A. dated January 16, 2007	10-Q		10.2	5/10/2007	
10.38††	Master Purchase Order between Northrop Grumman Security Systems and Cepheid dated August 15, 2007	10-Q		10.1	11/5/2007	
10.39*	Separation Agreement dated December 31, 2007, by and between Cepheid and John R. Sluis					X**X
10.40*	Amended and Restated Change of Control Retention and Severance Agreement dated February 1, 2008, by and between Cepheid and Peter Dailey					X**
10.41*	Employment Agreement dated February 6, 2008, by and between Cepheid and Andrew D. Miller	8-K		10.01	2/11/2008	
10.42*	Change of Control Retention and Severance Agreement dated April 14, 2008, by and between Cepheid and Andrew D. Miller			10.02	2/11/2008	
10.43	Amended and Restated Form of Change of Control Retention and Severance Agreement	8-K		99.01	2/21/2008	
21.1	List of Subsidiaries					X**
23.1	Consent of Independent Registered Public Accounting Firm					X**
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X**
31.2	Certification of Acting Principal Financial Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X**
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X**
32.2	Certification of Acting Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X**

* Management contract or compensatory plan or arrangement.

† Confidential treatment has been granted with respect to portions of the exhibit. A complete copy of the agreement, including the redacted terms, has been separately filed with the Securities and Exchange Commission.

†† Confidential treatment has been requested with regard to portions of this exhibit. Such portions were filed separately with the Securities and Exchange Commission.

** **Copy of exhibit filed with the 2007 Annual Report on Form 10-K is available free of charge by accessing our website located at www.cepheid.com under the heading "Investors – Financial Information – SEC Filings".**

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We are. Here.

NORTH AMERICA
United States
Canada
Mexico

CENTRAL & SOUTH AMERICA
Argentina

EUROPE
Austria
Belgium
Bulgaria
Croatia
Czech Republic
Denmark
Estonia
Finland
France
Germany
Greece
Hungary
Iceland
Ireland
Italy
Latvia
Lithuania
Luxembourg
Macedonia
Netherlands
Norway
Poland
Portugal
Romania
Russia
Serbia
Slovakia
Slovenia
Spain
Sweden
Switzerland
Turkey
United Kingdom

MIDDLE EAST & AFRICA
Bahrain
Egypt
Iraq
Israel
Jordan
Kuwait
Lebanon
Morocco
Qatar
Saudi Arabia
South Africa
Tunisia
U.A.E.

ASIA & OCEANIA
Australia
Azerbaijan
Cambodia
China
Georgia
India
Japan
Kazakhstan
Kirghizistan
Korea
Laos
Malaysia
Myanmar
New Zealand
Pakistan
Singapore
Taiwan
Thailand
Vietnam

BOARD OF DIRECTORS

THOMAS L. GUTSHALL
Chairman of the Board

JOHN L. BISHOP
Chief Executive Officer

THOMAS D. BROWN
Senior Vice President & President Diagnostics Division (retired)
Abbott Laboratories

ROBERT J. EASTON
Chairman,
Easton Strategy LLC

CRISTINA H. KEPNER
Executive Vice President and Corporate Finance Director (retired)
Invemed Associates LLC

DEAN O. MORTON
Executive Vice President & Chief Operating Officer (retired)
Hewlett Packard

MITCHELL D. MROZ
Vice President & General Manager (retired)
Northrop Grumman

DAVID H. PERSING, M.D., Ph.D.
Executive Vice President, Chief Medical and Technology Officer

HOLLINGS C. RENTON
President & Chief Executive Officer (retired)
Onyx Pharmaceuticals Inc.

EXECUTIVE OFFICERS

JOHN L. BISHOP
Chief Executive Officer

DAVID H. PERSING, M.D., Ph.D.
Executive Vice President, Chief Medical and Technology Officer

HUMBERTO REYES
Executive Vice President, Operations

PETER J. DAILEY, Ph.D.
Senior Vice President, Research and Development

RUSSEL K. ENNS, Ph.D.
Sr. Vice President, Regulatory , Clinical & Government Affairs & Quality Systems

ROBERT J. KOSKA
Sr. Vice President, Worldwide Commercial Operations

ANDREW D. MILLER
Sr. Vice President, Chief Financial Officer

JOSEPH H. SMITH
Sr. Vice President, Business Development and General Counsel

PAUL STEUPERAERT
President, Cepheid SA

ANNUAL MEETING OF SHAREHOLDERS

The Company's annual meeting will be held at 1:00 P.M. Pacific Daylight Time on Thursday, April 24, 2008 at the Company's principal office in Sunnyvale, California.

REGISTRAR AND STOCK TRANSFER AGENT

COMPUTERSHARE INVESTOR SERVICES, LLC
Chicago, Illinois

INVESTOR RELATIONS

PORTER NOVELLI LIFE SCIENCES
San Diego, California

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

ERNST & YOUNG LLP
San Jose, California

CORPORATE COUNSEL

FENWICK & WEST LLP
San Francisco, California

U.S. OPERATIONS

CORPORATE HEADQUARTERS,
R&D AND MANUFACTURING FACILITY
904 Caribbean Drive
Sunnyvale, California 94089, USA

OLIGO CHEMISTRY,
R&D AND MANUFACTURING
1631-220th Street, SE
Bothell, Washington 98021

EUROPEAN OPERATIONS

EUROPEAN HEADQUARTERS
81470 Maurens-Scopont, France

R&D AND MANUFACTURING
Bällstavägen 34-36,
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