SIERRA WIRELESS INC
Form 6-K
November 14, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

Report of Foreign issuer

Pursuant to Rule 13a-16 or 15d-16 of the Securities Exchange Act of 1934

For the Month of November 2005

(Commission File. No 0-30718).

SIERRA WIRELESS, INC., A CANADA CORPORATION

(Translation of registrant s name in English)

13811 Wireless Way

Richmond, British Columbia, Canada V6V 3A4

(Address of principal executive offices and zip code)

Registrant s Telephone Number, including area code: **604-231-1100**

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F:

Form 20-F o 40-F ý

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934:

Yes: o No: ý

SIGNATURES

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

Sierra Wireless, Inc.

By:	/s/ David G. McLennan David G. McLennan, Chief Financial Officer and Secretary

Date: November 9, 2005

SIERRA WIRELESS, INC.

THIRD QUARTER REPORT

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2005

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SIERRA WIRELESS, INC.

CHAIRMAIN S REPORT TO SHAREHOLDERS

On October 27th, Sierra Wireless announced a changing of the guard with the appointment of Jason W. Cohenour as President and Chief Executive Officer of Sierra Wireless.

Jason s appointment came after a comprehensive search, both internally and externally, to identify the candidate best able to lead Sierra Wireless to the next level. After reviewing a broad field of highly qualified candidates, it became very apparent that Jason is the right person to take on this role.

Jason joined Sierra Wireless in 1996, built the company s carrier, reseller and OEM distribution channels, was promoted to Senior Vice President, Worldwide Sales in 2000, and has served as the company s Chief Operating Officer since August 2004. He has cross-functional experience in sales, service, marketing, product management, manufacturing operations, mergers & acquisitions, corporate governance and corporate strategy.

Jason succeeds David Sutcliffe, who has served as the company s CEO since 1995. Under David s leadership, Sierra Wireless rapidly evolved into a leading global supplier of wireless data products. The company s products are now in the hands of millions of customers and on dozens of wireless networks in countries all around the world. At the request of the Board, David will continue to serve the company in a non-management capacity as a member of the Board.

On behalf of the Board, I want to thank David for his leadership and his energetic service and dedication to Sierra Wireless these past ten years. We congratulate Jason on his well earned promotion. Sierra Wireless is moving forward in strong and capable hands.

/s/ Peter Ciceri
Peter Ciceri,
Chairman of the Board of Directors

PRESIDENT S REPORT TO SHAREHOLDERS

TO OUR SHAREHOLDERS AND EMPLOYEES

It is my pleasure to report to you for the first time as the President and CEO of Sierra Wireless, and to tell you about recent improvements and developments in our business.

During the third quarter, we completed the business restructuring initiated at the end of the second quarter, and began to see improvements in the key metrics of our business. Our sales increased, gross margins were higher, and we reduced our operating expenses compared to the previous quarter. These results contributed to a lower net loss and reduced cash utilization. The third quarter also brought considerable progress in new product development in both our core PC card and embedded module businesses, and promising business developments related to these products.

A highlight of the quarter was the announcement by several leading laptop manufacturers of their intention to embed high speed wireless wide area network capability inside their products. This represents an exciting and potentially high-volume opportunity, and we believe Sierra Wireless is very well positioned to capture a strong position in this emerging market.

Q3 2005 results compared to Q3 2004

Results for the third quarter of 2005, compared to the third quarter of 2004, were as follows:

For the three months ended September 30, 2005, our revenue was $27.5 million, compared to $59.1 million in the third quarter of 2004. The change in revenue primarily reflects the decline in sales of our PC cards and embedded modules.

Gross margin decreased to $9.6 million (34.9% of revenue), from $23.0 million (39.0% of revenue) in the third quarter of 2004. Third quarter operating expenses were $14.0 million, compared to $15.1 million for the same period in 2004. We reported a net loss of $3.1 million (loss per share of $0.12), compared to net earnings of $7.1 million (diluted earnings per share of $0.27) in the third quarter of 2004.

Q3 2005 Results Compared to Guidance

Results for the third quarter of 2005, relative to company guidance provided on July 20, 2005, were as follows:

Revenue of $27.5 million was better than our guidance of $24.0 million. Gross margin of 34.9% was higher than our guidance of 31%. Operating expenses were $14.0 million, slightly higher than our guidance range of $13.7-$13.9 million. Our net loss of $3.1 million (loss per share of $0.12) was better than our guidance of a loss of approximately $5.7 million (loss per share of $0.22). Our cash flow from operations was negative $0.9 million, consistent with our guidance of negative cash flow.

Business Developments

During the third quarter we achieved a number of product and business development milestones with both existing and new products:

<u>Progress on Products using CDMA Technology</u>

Earlier in the year, we announced design wins with two major laptop OEMs for our MC5720 PCI express Mini Card modules (minicard) for EVDO networks. During the third quarter, we commenced commercial shipments of this product to Lenovo, which announced that two of its notebook models featuring our EVDO minicard will be available starting in October.

North American commercial shipments of our EM5625 EVDO module commenced to some of our long-time mobile computing OEM customers. We also announced that one of these OEM customers, Panasonic, has integrated our EM5625 module into three of its notebook platforms.

Together with iPass, we announced the certification and availability of the AirCard 580 wireless PC card for use with the iPass Mobile Data Service. We have also become an iPass Alliance Technology Partner. Our two companies will continue to work together to provide enterprise customers the latest technology for accessing the iPass 3G/EV-DO network via the iPassConnect universal client.

<u>Progress on Products Using GSM or UMTS Technology</u>

We have successfully completed development of our HSDPA PC Card and obtained a supply agreement with Cingular to deliver the AirCard 860 for use on its HSDPA network. We expect to commence commercial shipments to Cingular during the fourth quarter of 2005. Business development for this product with other carriers is also progressing well.

The MC8755/MC8765 PCI Express Mini Card modules for HSDPA networks are now available to OEM customers for testing and integration, with commercial shipments expected to begin in early 2006. Earlier in the year, we announced a design win with a major laptop OEM for our minicard for HSDPA networks.

We joined forces with NetMotion Wireless to provide mobile workers in the city of Aurora, the third largest city in Colorado, with secure, persistent connectivity using two distinct networks a cellular-based EDGE/GPRS system and Wi-Fi (802.11). NetMotion combined its Mobility XE mobile VPN solution with our AirCard 775 wireless wide area network cards and MP 775 rugged wireless modems to provide police officers and fire fighters with real-time access to mission critical information on its network.

Our mobile products were selected as part of the Royal Canadian Mounted Police s (RCMP s) standing offer for complete mobile workstation systems. The system, which includes technology from Nisha Technologies Inc. and Itronix Canada Ltd., features a combination of MP 775 GPS (for EDGE and GSM/GPRS networks) and MP 555 GPS (for CDMA 1X networks) rugged vehicle-mounted wireless modems.

The Missouri State Highway Patrol chose to upgrade to the Sierra Wireless MP 775 GPS modem from its existing solution with the MP 200 modem for CDPD.

Outlook

We believe that the emerging market for laptop computers with embedded high speed wireless capabilities represents a significant opportunity for Sierra Wireless, one that leverages our core competencies and extensive experience with OEM customers. We are investing for a leadership position in this market and recently launched the industry s first EVDO embedded minicard enabling our customers to be first to market. We are also the first to launch a fully functional HSDPA PC card, providing us with a leadership position in North America and a strong product offering to re-energize sales in Europe.

Going forward, we will continue to focus the company on the substantial opportunities in our core business, while working to achieve growth, profitability and industry leadership.

/s/ Jason W. Cohenour
Jason W. Cohenour
President and Chief Executive Officer

This report contains forward-looking statements that are not promises or guarantees but are only predictions that relate to future events or our future performance or state other forward-looking information and are subject to substantial risks and uncertainties that could cause our actual results, performance or achievements to differ materially from those expressed, anticipated or implied by the forward-looking statements. These forward-looking statements relate to, among other things, our revenue, earnings, plans, objectives and timing for the introduction or enhancement of our services and products, statements concerning strategies, developments, statements about future market conditions, supply conditions, channel and end customer demand conditions, projected or future revenues, gross margins, operating expenses, profits and other statements of expectations, intentions, objectives and plans that are not statements of historical facts. When used in this report, the words may , plan , expect , believe , intends , anticipates , estimates , predicts and similar expressions generally identify forward-looking statements. Forward-looking statements reflect our current expectations. The risks and uncertainties that may affect our actual results, performance or achievements are many and include, among others, our ability to develop, manufacture, supply and market new products that we do not produce today and that may not gain commercial acceptance, our reliance on the deployment of next generation networks by major wireless operators, and increased competition. These risk factors and others are discussed in our Annual Information Form which may be found on SEDAR at www.sedar.com and in our other regulatory filings with the Securities and Exchange Commission in the United States and the Provincial Securities Commissions in Canada. These factors should be reviewed carefully and you should not place undue reliance on any forward-looking statements. Unless otherwise required by applicable securities laws, Sierra Wireless disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our consolidated financial condition and results of operations, as of November 9, 2005, has been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and, except where otherwise specifically indicated, all amounts are expressed in United States dollars.

Additional information related to Sierra Wireless, Inc., including our Annual Information Form, may be found on SEDAR at www.sedar.com.

Overview

We provide innovative wireless modem solutions worldwide. We develop and market a range of products that include wireless data modems for portable computers, embedded modules for original equipment manufacturers, or OEMs, and rugged vehicle-mounted modems. Our products permit users to access wireless data and voice networks using notebook computers, personal digital assistants, or PDAs, and vehicle-based systems.

Wireless data communications is an expanding market positioned at the convergence of wireless communications, mobile computing and the Internet, each of which we believe represents a growing market. Our products are based on open standards, including the Internet protocol, and operate on the networks of major wireless operators around the world.

Our products are primarily used by businesses and government organizations to enable their employees to access a wide range of applications, including the Internet, e-mail, messaging, corporate intranet, remote database inquiry and computer aided dispatch. We sell our products through indirect channels, including wireless operators, resellers and OEMs.

During the latter part of 2003 and throughout 2004, we experienced stronger than expected demand primarily, as a result of our strong market position in CDMA EVDO Release 0 PC cards and our CDMA 1X embedded module sales to palmOne. Customer concentration increased in our revenue base. Following our considerable revenue and earnings growth in 2004, we experienced a significant reduction in our business in the first three quarters of 2005 relative to 2004 as a result of:

The reduction in our embedded module business volumes as a result of the completion of CDMA 1X module shipments to palmOne for its Treo 600 Smartphone at the end of 2004;

Reported channel inventory at some of our channel partners that was already sufficient to meet near-term customer demand during the first quarter of 2005; and

The near-term impact of increased competition in CDMA EVDO and EDGE PC cards, including a loss of market share at Verizon Wireless.

In June 2005, we announced our decision to exit our Voq professional phone initiative. We also decided to shift some Voq resources to our core PC card and embedded modules business, where we already have well established market positions and believe there are significant growth opportunities. In addition to the exit of the Voq initiative, we made some non-Voq related reductions to our operating expenses and assets and we recorded a provision for future legal costs associated with litigation matters.

Our revenue decreased 53.5% to $27.5 million in the third quarter of 2005, compared to $59.1 million in the same period of 2004. In the third quarter of 2005, our net loss was $3.1 million, or loss per share of $0.12, compared to net earnings of $7.1 million, or diluted earnings per share of $0.27, in the same period of 2004.

Our balance sheet remains strong, with $102.2 million of cash, cash equivalents and short- and long-term investments, compared to $105.7 million at June 30, 2005. During the third quarter of 2005, we used $0.9 million in cash from operations, compared to cash generated from operations of $8.0 million in the third quarter of 2004.

We continue to believe that the long-term prospects in the wireless communications industry remain strong, driven by advances in wireless network technologies such as the deployment of next generation 3G networks by carriers worldwide. We believe the deployment of these networks will be a catalyst to increasing the demand for wireless communications products such as those sold by us.

Key factors that we expect will affect our revenue in the near term are the timing of deployment of 3G high speed wireless data networks by carriers, the rate of adoption by end user customers, the timely launch of our new products currently under development and our ability to compete effectively with our competitors. We expect that competition from other wireless communications device manufacturers will continue to increase as more companies focus on opportunities in this market.

Having restructured the Company around PC cards and embedded modules, we are very focused on executing our product development and business development strategies in these areas. Specific initiatives include:

PC Cards: We have successfully completed the development of our UMTS/HSDPA PC card and obtained a supply agreement with Cingular to deliver the AirCard 860 for use on their HSDPA network. We expect to commence commercial shipments to Cingular during the fourth quarter of 2005. We believe business development for this product with other carriers is progressing well. We have also commenced the development of the next generation EVDO PC card (EVDO Rev A) and expect this to be commercially available in the second half of 2006; and

Embedded Modules: With the announcement by several of the leading laptop manufacturers of their plans to embed high speed wireless wide area network capability inside laptops, the opportunity for sales of embedded modules has potentially increased significantly. We believe we are well positioned to supply embedded modules to this market as a result of our extensive experience in the embedded module market. Earlier in the year, we announced we had design wins with two major laptop OEMs for PCI express Mini Card modules (minicard). One of these design wins is for both EVDO and HSDPA minicards, the other is for EVDO. We have begun shipment of our EVDO minicard to one of our partners, Lenovo, which announced that two of its notebook models would be available with our EVDO minicard commencing in October. We expect commercial shipments of our HSDPA minicard to commence in early 2006. During the third quarter, we also commenced shipment in North America of our EM5625 EVDO module to some of our long-time mobile computing OEM customers. One of these OEM customers, Panasonic, has subsequently integrated our EM5625 module into three of its notebook platforms.

We believe these new product developments provide us with a strong, up-to-date 3G product portfolio in both principal wireless technologies and in both the PC card and embedded module markets.

Results of Operations

The following table sets forth our operating results for the three and nine months ended September 30, 2005, expressed as a percentage of revenue:

	Three months ended September 30, 2005	2004	Nine months ended September 30, 2005	2004
Revenue	100.0%	100.0%	100.0%	100.0%
Cost of goods sold	65.1	61.0	84.5	60.1
Gross margin	34.9	39.0	15.5	39.9
Expenses				
Sales and marketing	10.8	9.5	16.6	9.3
Research and development, net	28.6	11.1	32.4	11.3
Administration	8.9	4.0	13.3	4.6
Restructuring and other charges	0.0	0.0	7.1	0.0
Amortization	2.6	1.0	3.0	1.2
	50.9	25.6	72.4	26.4
Earnings (loss) from operations	(16.0)	13.4	(56.9)	13.5
Other income	2.4	0.7	2.0	0.3
Earnings (loss) before income taxes	(13.6)	14.1	(54.9)	13.8
Income tax expense (recovery)	(2.4)	2.1	(1.2)	2.2
Net earnings (loss)	(11.2)%	12.0%	(53.7)%	11.6%

Our revenue by product, by distribution channel and by geographical region is as follows:

	Three months ended September 30, 2005	2004	Nine months ended September 30, 2005	2004
Revenue by product				
PC card	71%	67%	70%	58%
Embedded modules	11	30	10	34
Mobile	12	1	15	5
Other	6	2	5	3
	100%	100%	100%	100%
Revenue by distribution channel				
Wireless carriers	52%	23%	45%	27%
OEM	13	30	10	35
Resellers	34	47	43	38
Direct and other	1		2	
	100%	100%	100%	100%
Revenue by geographical region				
Americas	75%	91%	67%	92%
Europe	6	5	10	5
Asia-Pacific	19	4	23	3

	100%	100%	100%	100%

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Restructuring and Other Charges

In June 2005, we announced our decision to exit our Voq professional phone initiative. We also decided to shift some Voq resources to our core PC card and embedded modules business, where we already have well established market positions and believe there are significant growth opportunities. As announced we incurred restructuring and other charges associated with the exit of the program. In addition to the exit of the Voq initiative, we implemented some non-Voq related reductions to our operating expenses and assets as a result of the reduction in our business in the first half of 2005 and we recorded a provision for future legal costs associated with litigation matters.

In the second quarter of 2005, we recorded restructuring and other charges of $18.2 million that included inventory writedowns, severance costs, impairment of fixed, intangible and deferred tax assets, provisions for facilities restructuring, commitments and other costs related to the restructuring. Restructuring charges related to Voq were approximately $13.5 million of the total $18.2 million. Approximately $5.9 million represented cash disbursements, of which $4.5 million were paid during the third quarter of 2005.

As part of the restructuring, we reduced our workforce by 51 employees, of which 32 were terminated during the second quarter of 2005. For the remaining 19 employees who were on working notice, $0.4 million was expensed as part of our operating expenses during the third quarter of 2005 and at the end of the third quarter one employee remained on working notice.

In the second quarter of 2005, we also recorded a provision for legal costs of $1.0 million. This is related to the class action complaints filed in the U.S. District Court for the Southern District of New York and the U.S. District Court for the Southern District of California (which actions, effective August 24, 2005 were transferred to the Southern District of New York) for alleged violations of federal securities laws.

Results of Operations   Three Months Ended September 30, 2005 Compared to Three Months Ended September 30, 2004

Revenue

Revenue amounted to $27.5 million for the three months ended September 30, 2005, compared to $59.1 million in the same period of 2004, a decrease of 53.5%. The decrease in revenue was due primarily to a decrease in sales of PC cards and embedded modules. PC card revenue decreased primarily due to the impact of increased competition in CDMA EVDO PC cards, including a loss of market share at Verizon Wireless, and lower sales of legacy 2.5G products. Embedded module revenue decreased primarily due to the completion of shipments of embedded modules to palmOne for the Treo 600 at the end of 2004. During the third quarter of 2005, revenue from the sale of previously written down Voq product was $0.6 million.

Key factors that we expect will affect our revenue in the near term are the timing of deployment of 3G high speed wireless data networks by carriers, the rate of adoption by end user customers, the timely launch of our new products currently under development and our ability to compete effectively with our competitors. We expect that competition from other wireless communications device manufacturers will continue to increase as more companies focus on opportunities in this market.

Our revenue from customers in the Americas, Europe and the Asia-Pacific region comprised 75%, 6% and 19%, respectively, of our total revenue in the third quarter of 2005 and 91%, 5% and 4%, respectively, in the same period of 2004. Our North American business has decreased significantly compared to the prior year as a result of a decline in sales of our PC card and embedded module products to certain North American customers. As has been the case in the past several years, our business continues to be driven predominantly by short lead time purchase orders from channels and end customers rather than by long-term, large volume commitments from wireless operators. In Europe, the deployment of UMTS networks continues to negatively affect our sales in that region, as we currently do not have a UMTS product. Following the launch of our UMTS/HSDPA PC card and embedded minicard, we expect our sales to improve in Europe. Our business in the Asia-Pacific region has increased as a result of strong sales of CDMA EVDO and EDGE PC cards.

In the third quarter of 2005, two customers individually accounted for more than 10% of our revenue and, in aggregate, these two customers represented 40% of our revenue. This compared favorably with the same period last year in which three customers individually accounted for more than 10% of our revenue and these three customers represented approximately 69% of our revenue.

Gross margin

Gross margin amounted to $9.6 million in the third quarter of 2005, or 34.9% of revenue, compared to $23.0 million, or 39.0% of revenue, in the third quarter of 2004. The decline in gross margin percentage resulted primarily from lower selling prices of our PC card products and the impact of lower volumes overall, offset slightly by the positive impact of a favorable product mix between higher margin PC cards and mobiles versus lower margin embedded modules. During the third quarter of 2005, gross margin on the sale of previously written down Voq product was $0.2 million, or 36.1%.

We expect our gross margin percentage to continue to fluctuate from quarter to quarter as a result of changes in product mix, competition, changes in geographical mix and changes in product cost.

Sales and marketing

Sales and marketing expenses decreased significantly to $3.0 million in the third quarter of 2005, compared to $5.6 million in the same period of 2004. This decline reflects the impact of our business restructuring and continued cost containment. Sales and marketing expenses as a percentage of revenue increased to 10.8% in 2005, compared to 9.5% in 2004, due primarily to the decrease in revenue for the third quarter of 2005, which was partially offset by the decline in sales and marketing expenses. While managing sales and marketing expenses in relation to top-line revenue, we will continue to make selected investments in sales and marketing as we market existing products, introduce new products, expand our distribution channels in the Americas and the Asia-Pacific region and focus on core customers in Europe.

Research and development, net

Research and development expenses, net of conditionally repayable government research and development funding, amounted to $7.9 million in the third quarter of 2005, compared to $6.6 million in the third quarter of 2004, an increase of 19.8%.

Gross research and development expenses, before government research and development funding, were $7.9 million or 28.6% of revenue in the third quarter of 2005, compared to $7.0 million, or 11.7% of revenue, in the third quarter of 2004. Repayment of TPC funding of $0.1 million is included in our gross research and development expenses in the third quarter of 2005, compared to $0.5 million in 2004. Gross research and development expenses increased due to the development of new PC cards and embedded modules. As previously disclosed, our decision in June 2005 to exit the Voq professional phone initiative will reduce gross research and development expenditures in the future and TPC funding associated with the initiative will cease unless the TPC agreement is otherwise renegotiated. However, we expect our gross research and development expenses to continue to increase in our core business as we invest in next generation technology and develop new products.

Administration

Administration expenses equaled $2.4 million in each of the three months ended September 30 for both 2005 and 2004. Administration expenses as a percentage of revenue increased to 8.9% in 2005, compared to 4.0% in 2004, due primarily to the decrease in revenue for the third quarter of 2005.

Other income

Other income increased to $0.7 million in the third quarter of 2005, compared to $0.4 million in the same period of 2004. Other income includes interest income, interest expense and foreign exchange gains and losses.

Income tax expense (recovery)

Income tax recovery was $0.7 million in the third quarter of 2005, compared to $1.3 million of income tax expense in the third quarter of 2004. The income tax recovery is a result of the utilization of loss carrybacks to recover income taxes previously paid in 2004.

Net earnings (loss)

Our net loss amounted to $3.1 million, or loss per share of $0.12, in the three months ended September 30, 2005, compared to net earnings of $7.1 million, or diluted earnings per share of $0.27, in the same period of 2004.

The weighted average diluted number of shares outstanding decreased to 25.4 million in the third quarter of 2005, compared to 26.1 million in the same period of 2004.

Results of Operations Nine Months Ended September 30, 2005 Compared to Nine Months Ended September 30, 2004

Revenue

Revenue amounted to $69.6 million for the nine months ended September 30, 2005, compared to $152.4 million in the same period of 2004, a decrease of 54.3%. The decrease in revenue was due primarily to a decrease in sales of PC cards and embedded modules. PC card revenue decreased primarily due to reported channel inventory at some of our channel partners that was sufficient to meet near term customer demand and the near term impact of increased competition in CDMA EVDO PC cards, including a loss of market share at Verizon Wireless. Embedded module revenue decreased primarily due to the completion of shipments of embedded modules to palmOne for the Treo 600 at the end of 2004. In the second quarter of this year we announced our plan to exit the Voq professional phone initiative. During the three quarters ended September 30, 2005, revenue from the sale of previously written down Voq product was $0.6 million.

Key factors that we expect will affect our revenue in the near term are the timing of deployment of 3G high speed wireless data networks by carriers, the rate of adoption by end user customers and the timely launch of our new products currently under development. In addition, we expect that competition from other wireless communications device manufacturers will continue to increase as more companies focus on opportunities in this market.

Our revenue from customers in the Americas, Europe and the Asia-Pacific region comprised 67%, 10% and 23%, respectively, of our total revenue for the first three quarters of 2005 and 92%, 5% and 3%, respectively, in the same period of 2004. Our North American business has decreased significantly compared to the prior year as a result of a decline in sales of our PC card and embedded module products to certain North American customers. As has been the case in the past several years, our business continues to be driven predominantly by short lead time purchase orders from channels and end customers rather than by long-term, large volume commitments from wireless operators. In Europe, the deployment of UMTS networks continues to negatively affect our GSM/GPRS sales in that region as we currently do not have a UMTS product. This negative impact is partially offset by sales of our EDGE product. Following the launch of our UMTS/HSDPA PC card and embedded minicard, we expect our sales to improve in Europe. Our business in the Asia-Pacific region has increased as a result of strong sales of CDMA EVDO and EDGE PC cards.

In the first three quarters of 2005, two customers individually accounted for more than 10% of our revenue and, in the aggregate, these two customers represented approximately 32% of our revenue. This compared favorably with the same period last year in which two customers individually accounted for more than 10% of our revenue and these two customers represented approximately 51% of our revenue.

Gross margin

Gross margin amounted to $10.8 million in the first three quarters of 2005. Of the total $18.2 million restructuring charge that was recorded in the second quarter of this year, $12.8 million is recorded in gross margin. Excluding this amount, gross margin amounted to $23.6 million, or 33.9% of revenue, in the nine months ended September 30, 2005, compared to $60.8 million, or 39.9% of revenue, in the same period in 2004. The decline in gross margin percentage resulted primarily from lower selling prices of our PC card products and the impact of lower volumes overall, offset slightly by the positive impact of a favorable product mix between higher margin PC cards and mobiles versus lower margin embedded modules. During the first three quarters of 2005, gross margin on the sale of previously written down Voq product was $0.2 million, or 36.1%.

We expect our gross margin percentage to continue to fluctuate from quarter to quarter as a result of changes in product mix, competition, changes in geographical mix and changes in product cost.

Sales and marketing

Sales and marketing expenses declined to $11.6 million in the nine months ended September 30, 2005, compared to $14.2 for the comparable period in 2004. This decline reflects the impact of our business restructuring and continued cost containment. Sales and marketing expenses as a percentage of revenue increased to 16.6% in 2005, compared to 9.3% in 2004, due primarily to the decrease in revenue for the first three quarters of 2005. While managing sales and marketing expenses in relation to top-line revenue, we will continue to make selected investments in sales and marketing as we market existing products, introduce new products, expand our distribution channels in the Americas and the Asia-Pacific region and focus on core customers in Europe.

Research and development, net

Research and development expenses, net of conditionally repayable government research and development funding, amounted to $22.5 million in the nine months ended September 30, 2005, compared to $17.3 million in the same period of 2004, an increase of 30.2%.

Gross research and development expenses, before government research and development funding, were $23.3 million or 33.5% of revenue in the first nine months of 2005, compared to $19.5 million, or 12.8% of revenue, in the same period of 2004. Repayment of TPC funding of $0.5 million is included in our gross research and development expenses in the first three quarters of 2005, compared to $1.4 million in 2004. Gross research and development expenses increased due to the development of new PC cards, embedded modules and, for the first half of 2005, the next generation of the Voq professional phone. Our decision to exit the Voq professional phone initiative will reduce gross research and development expenditures in the future and TPC funding associated with the initiative will cease. However, we expect our gross research and development expenses to continue to increase in our core business as we invest in next generation technology and develop new products.

During the first quarter of 2004, we signed a second agreement with the Government of Canada s Technology Partnerships Canada (TPC) program under which we are eligible to receive conditionally repayable research and development funding up to Cdn. $9.5 million to support the development of Voq. The agreement is effective for development work commencing April 2003. For the three quarter ended September 30, 2005 funding of $0.8 million was recognized. Funding of $2.2 million was recognized during the first nine months of 2004, of which $1.1 million relates to the period from April 1, 2003 to December 31, 2003. Our TPC funding is based on research and development work completed in each quarter. Unless the second agreement is otherwise renegotiated, with the termination of the Voq professional phone initiative no further TPC funding is anticipated

Administration

Administration expenses amounted to $9.3 million, or 13.3% of revenue, in the nine months ended September 30, 2005, compared to $7.0 million, or 4.6% of revenue, in the same period of 2004. The increase of $2.3 million is primarily due to the provision of $1.0 million for future legal costs related to litigation matters and an increase in professional fees.

Restructuring and other charges

During the second quarter of 2005, we decided to exit the Voq Professional Phone initiative and to implement some non-Voq related reductions to our operating expenses and assets. As a result, in the first three quarters of 2005, we recorded restructuring and other charges of $18.2 million, consisting of inventory writedowns, severance costs, impairment of fixed, intangible and deferred tax assets, provisions for facilities restructuring, commitments and other costs related to the restructuring. Of this amount, $4.9 million was charged to restructuring and other charges, $12.8 million to cost of goods sold and $0.5 million to income tax expense.

Other income

Other income increased to $1.4 million in the first nine months of 2005, compared to $0.4 million in the same period of 2004. Other income includes interest income, interest expense and foreign exchange gains and losses. This increase is due primarily to an increase in interest income from rising interest rates that was partially offset by foreign exchange losses.

Income tax expense (recovery)

Income tax recovery was $0.8 million in the nine months ended September 30, 2005, compared to $3.4 million of income tax expense in the same period of 2004. Income tax recovery, excluding the increase in our deferred tax asset valuation allowance of $0.5 million, was $1.3 million. The income tax recovery is a result of the utilization of loss carrybacks to recover income taxes previously paid in 2004.

Net earnings (loss)

Our net loss amounted to $37.4 million, or loss per share of $1.47, in the nine months ended September 30, 2005. Our net loss, excluding restructuring and other charges of $18.2 million and the provision for future legal costs of $1.0 million, was $18.2 million, or loss per share of $0.72, in the three quarters ended September 30, 2005, compared to net earnings of $17.7 million, or diluted earnings per share of $0.68, in the same period of 2004.

The weighted average diluted number of shares outstanding decreased to 25.4 million in the first nine months of 2005, compared to 26.1 million in the same period of 2004.

Management Change

In April 2005, David Sutcliffe, who has served as our CEO and director for ten years, announced that he planned to retire as President and CEO. Since then the Board of Directors has conducted a comprehensive search process, considering a strong field of both external and internal candidates. Subsequent to the end of the third quarter we announced that, effective October 28, 2005, Mr. Jason Cohenour would become our new President and Chief Executive Officer. Mr. Cohenour joined Sierra Wireless in 1996, built the Company s carrier, reseller and OEM distribution channels, was promoted to Senior Vice President, Worldwide Sales in 2000 and has served as the Company s Chief Operating Officer since August 2004. Mr. Sutcliffe will, at the request of the Board of Directors, continue to serve the Company in a non-management capacity as a member of the Board.

Stock-Based Compensation

Subsequent to the end of the third quarter of 2005 the Board of Directors approved the accelerated vesting of certain stock options previously granted under the Company s stock option plan to participants other than board members and executive officers of the Company. The accelerated vesting of these options will have the positive effect of rewarding those eligible participants during a challenging year as well as reducing the future expense associated with those options as a result of a change in United States GAAP. Effective January 1, 2006 for the Company, United States GAAP will require the expensing in the Company s financial statements of the fair value of all stock-based compensation arrangements, including employee stock options. The expensing of the cost of employee stock options in the financial statements is in contrast to the current practice of providing supplemental pro forma disclosure in the footnotes to the financial statements of our income (loss) after giving effect to the employee stock-based compensation charge.

In aggregate, the vesting of a total of 368,091 stock options with an exercise price of US$14.25 (CAD$16.82) per share or higher, being 25% above the trading price at the time of the Board of Directors approval of this initiative, was accelerated and these options are now fully exercisable. These options would otherwise have vested over time periods ranging up to December, 2008.

By taking this accelerated vesting initiative now, a value of approximately $2.8 million will be recorded as a charge in the calculation of our supplemental footnote disclosure of our pro forma income (loss) in the fourth quarter of 2005. This will result in a reduction of our otherwise calculated stock-based compensation expense by approximately $1.3 million in 2006, $1.3 million in 2007 and $0.2 million in 2008.

Contingent Liabilities

Sierra Wireless America, Inc., as successor to AirPrime, Inc., along with other defendants, has been served with the complaint of Joshua Cohen and David Beardsley on behalf of themselves and others similarly situated, filed in the U.S. District Court for the Central District of California for alleged violations of federal and state securities laws allegedly occurring prior to the time AirPrime, Inc. was acquired by the Company. The plaintiffs filed the third amended complaint on July 7, 2005 and all defendants, including the Company, filed motions to dismiss the plaintiffs third amended complaint on August 22, 2005. We expect s decision from the Court regarding the motions to dismiss in November 2005. We have given notice to our liability insurance carrier which has agreed to pay our costs of defense that exceed the policy s retention amount, subject to a reservation of rights in the event it is determined that the carrier has no liability for this litigation and without conceding any liability for payment of loss. We have also submitted an escrow claim notice under the escrow agreement dated August 12, 2003 relating to the acquisition of AirPrime and the escrow shareholders are disputing their obligations with respect to this complaint. Although there can be no assurance that an unfavourable outcome of the dispute would not have a material adverse effect on our operating results, liquidity or financial position, we believe the claims are without merit and will vigorously defend them. The Company has determined that it is not possible to establish a reasonable estimate of the possible loss, or range of possible loss, if any.

The Company and certain of our officers are named as defendants in several class action complaints filed in the U.S. District Court for the Southern District of New York and the U.S. District Court for the Southern District of California (which actions, effective August 24, 2005, were transferred to the Southern District of New York) for alleged violations of federal securities laws. We are assessing the complaints and have not yet been required to file our response. We have given notice to our liability insurance carrier, which has agreed to pay our costs of defense that exceed the policy s retention amount, subject to a reservation of rights in the event that it is determined that the carrier has no liability for this litigation. Although there can be no assurance that an unfavourable outcome would not have a material adverse effect on our operating results, liquidity or financial position, we believe the claims are without merit and will vigorously defend the lawsuits. The Company has determined that it is not possible to establish a reasonable estimate of the possible loss, or range of possible loss, if any. However, the Company believes that it is probable that the legal costs related to these complaints may exceed our policy retention amount of $1.0 million. Accordingly, we accrued nil and $1.0 million in our results of operations for the three and nine months ended September 30, 2005, respectively.

On February 8, 2005, Sierra Wireless, Inc. was served with the first amended complaint of MLR, LLC filed in the U.S. District Court for the Northern District of Illinois Eastern Division for alleged patent infringement relating to our line of professional phones. We were added as a defendant in existing civil action no. 04 C 7044 MLR, LLC v. Kyocera Wireless Corporation and Novatel Wireless, Inc. Since that date, we have reached an agreement with MLR, under which we received non-royalty bearing licenses to use all of MLR s present and future patents for all of our products and MLR released us from all claims related to their patent portfolio. MLR has dismissed all claims against us in the lawsuit.

We are engaged in other legal actions in the ordinary course of business and believe that the ultimate outcome of these actions will not have a material adverse effect on our operating results, liquidity or financial position.

Critical Accounting Estimates

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States, and we make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and the related disclosure of contingent liabilities. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, adequacy of allowance for doubtful accounts, adequacy of inventory reserve, income taxes and adequacy of warranty reserve. We base our estimates on historical experience and anticipated results and trends and on various other assumptions that we believe are reasonable under the circumstances. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results may differ from our estimates. Senior management has discussed with our audit committee the development, selection, and disclosure of accounting estimates used in the preparation of our consolidated financial statements.

During the nine months ended September 30, 2005, we did not adopt any new accounting policies that have a material impact on our consolidated financial statements or make changes to existing accounting policies.

The following critical accounting policies affect our more significant estimates and assumptions used in preparing our consolidated financial statements:

We recognize revenue from sales of products and services upon the later of transfer of title or upon shipment of the product to the customer or rendering of the service, so long as collectibility is reasonably assured. Customers include resellers, original equipment manufacturers, wireless service providers and end-users. We record deferred revenue when we receive cash in advance of the revenue recognition criteria being met.

A significant portion of our revenue is generated from sales to resellers. We recognize revenue on the portion of sales to certain resellers that are subject to provisions allowing various rights of return and stock rotation when the rights have expired or the products have been reported as sold by the resellers.

Funding from research and development agreements, other than government research and development arrangements, is recognized as revenue when certain criteria stipulated under the terms of those funding agreements have been met, and when there is reasonable assurance the funding will be received. Certain research and development funding will be repayable only on the occurrence of specified future events. If such events do not occur, no repayment would be required. We will recognize the liability to repay research and development funding in the period in which conditions arise that would cause research and development funding to be repayable.

Revenues from contracts with multiple-element arrangements, such as those including technical support services, are recognized as each element is earned based on the relative fair value of each element and only when there are no undelivered elements that are essential to the functionality of the delivered elements.

Revenue from licensed software is recognized at the inception of the license term and in accordance with Statement of Position 97-2, Software Revenue Recognition . Revenue from software maintenance, unspecified upgrades and technical support contracts is recognized over the period such items are delivered or services are provided. Technical support contracts extending beyond the current period are recorded as deferred revenue.

We maintain an allowance for doubtful accounts for estimated losses that may arise if any of our customers are unable to make required payments. We consider the following factors when determining if collection is reasonably assured: customer credit-worthiness, past transaction history with the customer, current economic industry trends and changes in customer payment terms. If we have no previous experience with the customer, we typically obtain reports from credit organizations to ensure that the customer has a history of paying its creditors. We may also request financial information, including financial statements, to ensure that the customer has the means of making payment. If these factors indicate collection is not reasonably assured, revenue is deferred until collection becomes reasonably assured, which is generally upon receipt of cash. If the financial condition of any of our customers deteriorates, we may increase our allowance.

We value our inventory at the lower of cost, determined on a first-in-first-out basis, and estimated net realizable value. We assess the need for an inventory writedown or an accrual for estimated losses on inventory purchase commitments based on our assessment of estimated market value using assumptions about future demand and market conditions. Our reserve requirements generally increase as our projected demand requirements decrease, due to market conditions, technological and product life cycle changes and longer than previously expected usage periods. If market conditions are worse than our projections, we may further writedown the value of our inventory or increase the accrual for estimated losses on inventory purchase commitments.

We currently have intangible assets of $11.5 million and goodwill of $19.2 million generated from our acquisition of AirPrime in August 2003. Goodwill is tested for impairment annually, or more often, if an event or circumstance indicates that an impairment loss has been incurred.

The initial goodwill impairment test was completed during the fourth quarter of 2003, which resulted in no impairment loss. We assessed the realizability of goodwill related to our reporting unit during the fourth quarter of 2004 and determined that the fair value amount exceeded the carrying amount of the reporting unit by a substantial margin. Therefore, the second step of the impairment test that measures an impairment loss by comparing the implied fair market value of the reporting unit goodwill with the carrying amount of the goodwill was not required.

We evaluate our deferred income tax assets to assess whether their realization is more likely than not. If their realization is not considered more likely than not, we provide for a valuation allowance. The ultimate realization of our deferred tax assets is dependent upon the generation of future taxable income during the periods in which temporary differences become deductible. We consider projected future taxable income and tax planning strategies in making our assessment. If our assessment of our ability to realize our deferred tax assets changes, we may make an adjustment to our deferred tax assets that would be charged to income.

We accrue product warranty costs in accrued liabilities to provide for the repair or replacement of defective products. Our accrual is based on an assessment of historical experience and management s estimates. If we suffer a decrease in the quality of our products, we may increase our accrual.

Under license agreements, we are committed to royalty payments based on the sales of products using certain technologies. We recognize royalty obligations as determinable in accordance with agreement terms. Where agreements are not finalized, we have recognized our current best estimate of the obligation in accrued liabilities.

When the agreements are finalized, the estimate will be revised accordingly.

We recorded a lease provision during 2002 and the second quarter of 2005 as a result of our restructuring program by estimating the net present value of the future cash outflows over the remaining lease period. The estimate was based on various assumptions, including the obtainable sublease rates and the time it will take to find a suitable tenant. These assumptions are influenced by market conditions and the availability of similar space nearby. If market conditions change, we will adjust our provision.

We are engaged in certain legal actions. We estimate the range of liability related to pending litigation where the amount and range of loss can be reasonably estimated. We record our best estimate of a loss when the loss is considered probable. As additional information becomes available, we assess the potential liability relating to our pending litigation and revise our estimates.

Liquidity and Capital Resources

Operating Activities

Cash used by operating activities amounted to $20.6 million for the first nine months of 2005, compared to cash provided by operating activities of $21.5 million in the same period of 2004. The use of cash in operating activities in the first nine months of 2005 primarily resulted from the loss from operations of $37.4 million adjusted for non-cash items, inventory levels and changes in other operating assets and liabilities of $16.8 million. Our working capital has decreased from December 31, 2004 as a result of the significant decline in our business and the cash costs of the business restructuring. During the third quarter of 2005, inventory decreased by $6.2 million.

Investing Activities

Cash used by investing activities was $67.1 million for the nine months ended September 30, 2005, compared to cash provided by investing activities of $31.0 million in the same period of 2004. The use of cash in investing activities during 2005 was due primarily to the purchase, net of proceeds on maturity, of short-term investments of $44.3 million and the purchase of long-term investments of $14.8 million. Expenditures on intangible assets were $1.8 million and on fixed assets were $6.3 million for the nine months ended September 30, 2005, compared to $1.7 million and $5.5 million, respectively, in the same period of 2004. Expenditures on intangible assets were primarily for license fees and patents while capital expenditures were primarily for tooling, research and development equipment, computer equipment and software.

We do not have any trading activities that involve any type of commodity contracts that are accounted for at fair value but for which a lack of market price quotations necessitate the use of fair value estimation techniques.

Financing Activities

Cash used by financing activities was $0.9 million in the first three quarters of 2005, compared to cash provided by financing activities of $3.1 million during the same period in 2004. The use of cash by financing activities in the nine months ended September 30, 2005 was primarily for repayment of long-term liabilities. The source of cash in 2004 was primarily from the issuance of common shares upon the exercise of stock options, offset slightly by repayments of our long-term obligations.

As of September 30, 2005, we did not have any off-balance sheet finance or special purpose entities.

Cash Requirements

Our near-term cash requirements are primarily related to funding our operations, the cash costs of the business restructuring, capital expenditures and other obligations discussed below. In the near term, we expect that our cash flow from operations will be negative. The cash costs of the business restructuring total approximately $5.9 million, of which $4.5 million were paid during the third quarter of 2005. We believe our cash, cash equivalents and short- and long-term investments of $102.2 million and cash generated from operations will be sufficient to fund our expected working and other capital requirements for at least the next twelve months based on current business plans. Our capital expenditures during the fourth quarter of 2005 are expected to be primarily for research and development equipment, tooling, licenses and patents. However, we cannot provide assurance that our actual cash requirements will not be greater than we currently expect.

The following table quantifies our future contractual obligations as of September 30, 2005:

In 000s of US $ **Payments due in fiscal**	**Operating Leases**	**Obligations under Capital Leases**	**Total**
2005	$ 705	$ 161	$ 866
2006	2,856	302	3,158
2007	2,933		2,933
2008	2,918		2,918
2009	2,239		2,239
2010	2,230		2,230
Thereafter	1,350		1,350
Total	$ 15,231	$ 463	$ 15,694

We have entered into purchase commitments totaling approximately $27.0 million with certain contract manufacturers under which we have committed to buy a minimum amount of designated products. In certain of these agreements, we may be required to acquire and pay for such products up to the prescribed minimum or forecasted purchases.

Sources and Uses of Cash

During 2004, we had an operating line of credit of $10.0 million, which bore interest at prime plus 1.25% per annum. This line of credit was secured by a general security agreement providing a first charge against all assets. On December 31, 2004, we renegotiated our line of credit and now have an unsecured revolving demand facility for $10.0 million that bears interest at prime per annum. The balance at September 30, 2005 was nil (2004   nil).

In the past, our revenue was dependent on us fulfilling our commitments in accordance with agreements with major customers. We have completed volume shipments on those contracts. We now rely on purchase orders with these customers and these customers, like our other customers, are under no contractual obligation to purchase our products. If they do not make such purchases, our future operating cash flow will be negatively impacted. We have a risk of impairment to our liquidity should there be any interruption to our business operations.