

ASTRONICS CORP  
Form 10-Q  
November 14, 2006

Table of Contents

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**Form 10-Q**

☒ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
**For the quarterly period ended September 30, 2006 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 0-7087**

**ASTRONICS CORPORATION**

(Exact name of registrant as specified in its charter)

**New York**

(State or other jurisdiction of  
incorporation or organization)

**16-0959303**

(IRS Employer Identification Number)

**130 Commerce Way East Aurora, New York**

(Address of principal executive offices)

**14052**

(Zip code)

**(716) 805-1599**

(Registrant's telephone number, including area code)

**NOT APPLICABLE**

(Former name, former address and former fiscal year, if changed since last report)

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

**\$.01 par value Common Stock, \$.01 par value Class B Stock**

(Title of Class)

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

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.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒

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 September 30, 2006 8,020,482 shares of common stock were outstanding consisting of 6,620,012 shares of common stock (\$.01 par value) and 1,400,470 shares of Class B common stock (\$.01 par value).

## TABLE OF CONTENTS

### PART I FINANCIAL INFORMATION

Item 1. Financial Statements

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Item 4. Controls and Procedures

### PART II OTHER INFORMATION

Item 1. Legal Proceedings

Item 1a. Risk Factors

Item 2. Unregistered sales of equity securities and use of proceeds

Item 3. Defaults Upon Senior Securities

Item 4. Submission of Matters to a Vote of Securities Holders

Item 5. Other Information

Item 6 Exhibits and Reports on Form 8-K

### SIGNATURES

EX-31.1 302 Certification for CEO

EX-31.2 302 Certification for CFO

EX-32 906 Certification for CEO and CFO

EX-31.1

EX-31.2

EX-32

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements**

## ASTRONICS CORPORATION

**Consolidated Balance Sheet**

September 30, 2006

with Comparative Figures for December 31, 2005

(dollars in thousands except per share amounts)

	September 30, 2006 (Unaudited)	December 31, 2005
Current Assets:		
Cash and Cash Equivalents	\$ 645	\$ 4,473
Accounts Receivable, net of allowance for doubtful accounts of \$279 in 2006 and \$365 in 2005	18,065	12,635
Inventories	26,584	19,013
Prepaid Expenses	1,227	626
Deferred Taxes	739	775
Total Current Assets	47,260	37,522
Property, Plant and Equipment, at cost	33,999	31,665
Less Accumulated Depreciation and Amortization	12,778	11,204
Net Property, Plant and Equipment	21,221	20,461
Intangible Assets, net of accumulated amortization of \$559 in 2006 and \$329 in 2005	3,170	3,400
Goodwill	2,780	2,686
Other Assets	1,741	1,788
Total Assets	\$ 76,172	\$ 65,857

See notes to consolidated financial statements.

**Table of Contents**

## ASTRONICS CORPORATION

**Consolidated Balance Sheet**

September 30, 2006

with Comparative Figures for December 31, 2005

(dollars in thousands except per share amounts)

	September 30, 2006 (Unaudited)	December 31, 2005
Current Liabilities:		
Current Maturities of Long-term Debt	\$ 921	\$ 914
Note Payable	7,900	7,000
Accounts Payable	9,878	5,421
Accrued Payroll and Employee Benefits	3,885	3,861
Customer Advance Payments	3,582	4,404
Other Accrued Expenses	1,498	1,156
Income Taxes Payable		171
Contract Loss Reserve		830
Total Current Liabilities	27,664	23,757
Long-term Debt	9,837	10,304
Supplemental Retirement Plan and Other Benefits	4,622	4,494
Other Liabilities	1,365	1,317
Deferred Income Taxes	192	151
Shareholders' Equity:		
Common Stock, \$.01 par value		
Authorized 20,000,000 shares, issued 7,298,450 in 2006, 7,082,100 in 2005	72	71
Class B Stock, \$.01 par value		
Authorized 5,000,000 shares, issued 1,506,282 in 2006, 1,603,323 in 2005	15	16
Additional Paid-in Capital	5,289	3,808
Accumulated Other Comprehensive Income	838	799
Retained Earnings	29,997	24,859
	36,211	29,553
Less Treasury Stock: 784,250 shares in 2006 and 2005	3,719	3,719
Total Shareholders' Equity	32,492	25,834
Total Liabilities and Shareholders' Equity	\$ 76,172	\$ 65,857

See notes to consolidated financial statements.

Table of Contents

**ASTRONICS CORPORATION**  
**Consolidated Statement of Income and Retained Earnings**  
 Three and Nine Months Ended September 30, 2006  
 with Comparative Figures for 2005  
 (Unaudited)  
 (dollars in thousands except per share data)

	Nine Months Ended		Three Months Ended	
	September	October 1,	September	October 1,
	30,	2005	30,	2005
	2006	2005	2006	2005
Sales	\$ 82,505	\$ 54,916	\$ 28,540	\$ 20,421
Costs and Expenses:				
Cost of products sold	63,891	43,654	22,019	15,947
Selling, general and administrative expenses	9,931	7,679	3,469	2,890
Interest expense, net of interest income	650	519	232	202
Other income	(39)		(5)	
Total costs and expenses	74,433	51,852	25,715	19,039
Income Before Income Taxes	8,072	3,064	2,825	1,382
Provision for Income Taxes	2,934	1,468	912	592
Net Income	\$ 5,138	\$ 1,596	\$ 1,913	\$ 790
Retained Earnings:				
Beginning of period	24,859	22,206		
End of period	\$ 29,997	\$ 23,802		
Earnings per share:				
Basic	\$ .65	\$ .20	\$ .24	\$ .10
Diluted	\$ .63	\$ .20	\$ .23	\$ .10

See notes to consolidated financial statements.

**Table of Contents**

ASTRONICS CORPORATION  
**Consolidated Statement of Cash Flows**  
 Nine Months Ended September 30, 2006  
 With Comparative Figures for 2005  
 (Unaudited)  
 (dollars in thousands)

	September 30, 2006	October 1, 2005
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 5,138	\$ 1,596
Adjustments to reconcile net income to cash (used in) provided by operating activities:		
Depreciation and Amortization	1,960	2,042
Deferred Taxes	102	505
Other		(195)
Provision for non-cash losses on inventories and receivables	(125)	498
Stock Compensation Expense	493	
Cash flows from changes in operating assets and liabilities, excluding effects of acquisition:		
Accounts Receivable	(5,303)	(2,330)
Inventories	(7,404)	(4,593)
Prepaid Expenses	(347)	(165)
Accounts Payable	4,422	1,639
Accrued Expenses	408	1,072
Customer Advanced Payments	(822)	
Contract Loss Reserves	(830)	
Income Taxes	(410)	1,339
Supplemental Retirement and Other Liabilities	64	
Cash (used in) provided by Operating Activities	(2,654)	1,408
<b>Cash Flows from Investing Activities:</b>		
Business Acquisition		(13,366)
Proceeds from sale of short-term investments		1,000
Capital Expenditures	(2,300)	(1,765)
Other	(74)	(162)
Cash used in Investing Activities	(2,374)	(14,293)
<b>Cash Flows from Financing Activities:</b>		
Principal Payments on Long-term Debt and Capital Lease Obligations	(529)	(506)
Proceeds from Note Payable	3,200	7,000
Payment on Note Payable	(2,300)	
Proceeds from exercise of stock options	916	162
Income tax benefit from exercise of stock options	72	

Other	(83)	
Cash provided by Financing Activities	1,276	6,656
Effect of Exchange Rates on Cash	(76)	(14)
Cash used in Continuing Operations	(3,828)	(6,243)
Cash used in Discontinued Operations operating activities		(447)
Net decrease in Cash and Cash Equivalents	(3,828)	(6,690)
Cash at Beginning of Period	4,473	8,476
Cash at End of Period	\$ 645	\$ 1,786

See notes to consolidated financial statements.



**Table of Contents**

ASTRONICS CORPORATION  
**Notes to Consolidated Financial Statements**  
September 30, 2006  
(Unaudited)

**1) Basis of Presentation**

The accompanying unaudited statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of results for the full year. Operating results for the nine month period ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

The balance sheet at December 31, 2005 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

For further information, refer to the financial statements and footnotes thereto included in Astronics Corporation's (the Company) 2005 annual report on Form 10-K.

**Reclassifications** Certain amounts in the prior year financial statements have been reclassified to conform with the current year presentation.

**2) Stock Based Compensation**

The Company has stock option plans that authorize the issuance of options for shares of Common Stock to directors, officers and key employees. Stock option grants are designed to reward long-term contributions to the Company and provide incentives for recipients to remain with the Company. The exercise price, determined by a committee of the Board of Directors, may not be less than the fair market value of the Common Stock on the grant date. Options become exercisable over periods not exceeding ten years. The Company's practice has been to issue new shares upon the exercise of the options.

During the first quarter of 2006, the Company adopted SFAS 123(R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the statement of earnings based on the grant date fair value of the award. Under the modified prospective method, the Company is required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The Company uses a straight-line method of attributing the value of stock-based compensation expense, subject to minimum levels of expense, based on vesting. Stock compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Vesting requirements vary for directors, officers and key employees. In general, options granted to outside directors vest six months from the date of grant and options granted to officers and key employees straight line vest over a five-year period from the date of grant.

The fair value of stock options granted was estimated on the date of grant using the Black-Scholes option-pricing model. The weighted average fair value of the options was \$6.05 for options granted during the nine months ended September 30, 2006 and was \$3.32 for options granted during the nine months ended October 1, 2005. The following table provides the range of assumptions used to value stock options granted during the nine months ended September 30, 2006 and October 1, 2005.

	Nine Months Ended	
	September 30, 2006	October 1, 2005
Expected volatility	0.34	0.33
Risk-free rate	4.70%	5.34%

Edgar Filing: ASTRONICS CORP - Form 10-Q

Expected dividends		0.00%	0.00%
Expected term (in years)	7	7 Years	7 10 Years

---

**Table of Contents**

To determine expected volatility, the Company uses historical volatility based on weekly closing prices of its Common Stock and considers currently available information to determine if future volatility is expected to differ over the expected terms of the options granted. The risk-free rate is based on the United States Treasury yield curve at the time of grant for the appropriate term of the options granted. Expected dividends are based on the Company's history and expectation of dividend payouts. The expected term of stock options is based on vesting schedules, expected exercise patterns and contractual terms.

The table below reflects net earnings and net earnings per share for the three and nine months ended September 30, 2006 compared with the pro forma information for the three and nine months ended October 1, 2005 as follows:

	Nine Months Ended		Three Months Ended	
	September	October	September	October
	30,	1,	30,	1,
(in thousands, except per share data)	2006	2005	2006	2005
Net earnings, as reported for the prior period (1)	\$ N/A	\$ 1,596	\$ N/A	\$ 790
Stock compensation expense	493	242	164	81
Tax benefit	(79)	(42)	(28)	(14)
Stock compensation expense, net of tax (2)	414	200	136	67
Net earnings, including the effect of stock compensation expense (3)	\$ 5,138	\$ 1,396	\$ 1,913	\$ 723
Net earnings per share:				
Basic, as reported for the prior period (1)	\$ N/A	\$ 0.20	\$ N/A	\$ 0.10
Basic, including the effect of stock compensation expense (3)	\$ 0.65	\$ 0.18	\$ 0.24	\$ 0.09
Diluted, as reported for the prior period (1)	\$ N/A	\$ 0.20	\$ N/A	\$ 0.10
Diluted, including the effect of stock compensation expense (3)	\$ 0.63	\$ 0.17	\$ 0.23	\$ 0.09

(1) Net earnings and earnings per share prior to 2006 did not include stock compensation expense for stock options.

(2) Stock compensation expense prior to 2006 is calculated based on the pro forma application of SFAS No. 123.

- (3) Net earnings and earnings per share prior to 2006 represents pro forma information based on SFAS No. 123.

A summary of the Company's stock option activity and related information for the nine months ended September 30, 2006 is as follows:

	Number of Options	2006 Weighted Average Exercise Price per option	Aggregate Intrinsic Value
(dollars in thousands, except per option data)			
Outstanding at December 31, 2005	801,583	\$ 6.49	\$ 7,423
Options Granted	25,000	13.41	59
Options Exercised	(57,001)	7.31	(481)
Outstanding at September 30, 2006	769,582	6.65	7,003
Exercisable at September 30, 2006	489,837	\$ 6.53	\$ 4,516

The aggregate intrinsic value in the preceding table represents the total pretax option holder's intrinsic value, based on the Company's closing stock price of Common Stock of \$15.75 as of September 30, 2006, which would have been received by the option holders had all option holders exercised their options as of that date.

The fair value of options vested since December 31, 2005 is \$0.3 million. At September 30, 2006, total compensation costs related to non-vested awards not yet recognized amounts to \$0.7 million and will be recognized over a weighted average period of 2.2 years.

**Table of Contents**

The following is a summary of weighted average exercise prices and contractual lives for outstanding and exercisable stock options as of September 30, 2006:

Exercise Price Range		Shares	Outstanding Weighted Average Remaining Life in Years	Weighted Average Exercise Price	Shares	Exercisable Weighted Average Remaining Life in Years	Weighted Average Exercise Price
\$3.39	\$4.59	54,497	0.9	\$ 4.01	54,497	0.9	\$ 4.01
\$5.09	\$7.65	543,180	6.7	5.63	345,840	6.1	5.63
\$9.83	\$13.49	171,905	7.1	10.73	89,500	5.3	11.55
		769,582	6.4	6.65	489,837	5.3	6.53

**3) Acquisition**

On February 3, 2005, the Company acquired substantially all of the assets of the General Dynamics - Airborne Electronic Systems (AES) business unit from a subsidiary of General Dynamics. Astronics AES produces a wide range of products related to electrical power generation, in-flight control, and distribution on military, commercial, and business aircraft. On the acquisition date, the Company paid \$13.0 million in cash and incurred approximately \$0.4 million in acquisition costs. The Company borrowed \$7.0 million on its credit facility and used \$6.4 million of cash on hand to finance the purchase and acquisition costs. Results of operations include the results of Astronics AES since February 3, 2005, the date of the acquisition.

The following table summarizes the gross carrying amount and accumulated amortization for major categories of acquired intangible assets:

(in thousands)	Weighted Average Life	Gross Carrying Amount Sept 30, 2006	Accumulated Amortization Sept 30, 2006	Gross Carrying Amount Dec. 31, 2005	Accumulated Amortization Dec 31, 2005
Patents	12 Years	\$ 1,271	\$ 165	\$ 1,271	\$ 91
Trade Names	N/A	553		553	
Completed and unpatented technology	10 Years	487	81	487	45
Government contracts	6 Years	347	96	347	53
Backlog	4 Years	314	217	314	140
Total Intangible assets		\$ 2,972	\$ 559	\$ 2,972	\$ 329

Amortization expense for each of the next five years is expected to amount to \$0.3 million for the year ended December 31, 2006 and \$0.2 million for each of the years ended December 31, 2007, 2008, 2009 and 2010. The following summary, prepared on a pro forma basis, combines the consolidated results of operations of the Company with those of the acquired business as if the acquisition took place on January 1, 2005. The pro forma consolidated results include the impact of adjustments, including depreciation, amortization of intangibles, increased

interest expense on acquisition debt and related income tax effects.

Unaudited	Nine Months Ended		Three Months Ended	
	October 1, 2005	October 1, 2005	October 1, 2005	October 1, 2005
	As Reported	Pro Forma	As Reported	Pro Forma
(in thousands, except for per share data)				
Sales	\$ 54,916	\$ 56,615	\$ 20,421	\$ 20,421
Net income	\$ 1,596	\$ 1,388	\$ 790	\$ 790
Basic earnings per share	\$ 0.20	\$ 0.18	\$ 0.10	\$ 0.10
Diluted earnings per share	\$ 0.20	\$ 0.17	\$ 0.10	\$ 0.10

The pro forma results are not necessarily indicative of what would have actually occurred if the acquisition had taken place on January 1, 2005. In addition, they are not intended to be a projection of future results.

**Table of Contents****4) Discontinued Operations**

In December of 2002 the Company announced the discontinuance of the Electroluminescent Lamp Business Group, whose business has involved sales of microencapsulated electroluminescent lamps to customers in the consumer electronics industry. The liabilities of discontinued operations at October 1, 2005 consisted of lease payments for equipment that was used in this business, the remaining payments under these leases were made during 2005. As of December 31, 2005 there were no remaining assets or liabilities of discontinued operations.

**5) Inventories**

Inventories are stated at the lower of cost or market, cost being determined in accordance with the first-in, first-out method. Inventories are as follows:

(in thousands)	September 30, 2006	December 31, 2005
Finished Goods	\$ 3,295	\$ 2,658
Work in Progress	10,235	7,805
Raw Material	13,054	8,550
	\$ 26,584	\$ 19,013

**6) Comprehensive Income and Accumulated Other Comprehensive Income**

The components of comprehensive income are as follows:

(in thousands)	Nine Months Ended September 30, 2006		Three Months Ended September 30, 2006	
	October 1, 2005		October 1, 2005	
Net income	\$ 5,138	\$ 1,596	\$ 1,913	\$ 790
Other comprehensive income:				
Foreign currency translation adjustments	89	95	18	174
(Loss) gain on derivatives, net of tax	(50)	49	(55)	12
Comprehensive income	\$ 5,177	\$ 1,740	\$ 1,876	\$ 976

The components of accumulated other comprehensive income is as follows:

(in thousands)	September 30, 2006	December 31, 2005
Cumulative foreign currency adjustments	\$ 888	\$ 799
Accumulated loss on derivatives, net of tax of \$25 thousand for 2006 and \$ for 2005	(50)	
Accumulated other comprehensive income	\$ 838	\$ 799

**Table of Contents****7) Earnings Per Share**

The following table sets forth the computation of earnings per share:

	Nine Months Ended		Three Months Ended	
	September	October	September	October
	30,	1,	30,	1,
(in thousands, except per share data)	2006	2005	2006	2005
Net Income	\$ 5,138	\$ 1,596	\$ 1,913	\$ 790
Basic earnings per share weighted average shares	7,933	7,843	7,951	7,858
Net effect of dilutive stock options	277	163	313	236
Diluted earnings per share weighted average shares	8,210	8,006	8,264	8,094
Basic earnings per share	\$ .65	\$ .20	\$ .24	\$ .10
Diluted earnings per share	\$ .63	\$ .20	\$ .23	\$ .10

**8) Supplemental Retirement Plan and Related Post Retirement Benefits**

The Company has a non-qualified supplemental retirement defined benefit plan for certain executives. The following table sets forth information regarding the net periodic pension cost for the plan.

	Nine Months Ended		Three Months Ended	
	September	October	September	October
	30,	1,	30,	1,
(in thousands)	2006	2005	2006	2005
Service cost	\$ 27	\$ 18	\$ 9	\$ 6
Interest cost	231	231	77	77
Amortization of prior service cost	81	81	27	27
Amortization of net actuarial losses	3		1	
Net periodic cost	\$ 342	\$ 330	\$ 114	\$ 110

Participants in the non-qualified supplemental retirement plan are entitled to paid medical, dental and long-term care insurance benefits upon retirement under the plan. The following table sets forth information regarding the net periodic cost recognized for those benefits:

	Nine Months Ended		Three Months Ended	
	September	October	September	October
	30,	1,	30,	1,
(in thousands)	2006	2005	2006	2005
Service cost	\$ 6	\$ 3	\$ 2	\$ 1
Interest cost	33	30	11	10
Amortization of prior service cost	24	24	8	8
Amortization of net actuarial losses	9	3	3	1
Net periodic cost	\$ 72	\$ 60	\$ 24	\$ 20





**Table of Contents**

**9) New Accounting Pronouncements**

In June 2006, the FASB issued Interpretation ( FIN ) No. 48, Accounting for Uncertainty in Income Taxes an Interpretation for SFAS No. 109. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with for SFAS No. 109, Accounting for Income Taxes. The pronouncement prescribes a recognition threshold and measurement attributable to financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. The Company is in the process of determining the effect, if any; the adoption of FIN 48 will have on our financial statements.

In September 2006, the FASB issued FASB Statement No. 157, Fair Value Measurements . This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Where applicable, this Statement simplifies and codifies related guidance within generally accepted accounting principles. The Company is in the process of determining the effect, if any; the adoption of Statement No. 157 will have on our financial statements.

In September 2006, the FASB issued FASB Statement No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (an amendment of FASB Statements No. 87, 88, 106, and 132R). The Statement requires employers to fully recognize the obligations associated with single-employer defined benefit pension, retiree healthcare and other postretirement plans in their financial statements. Statement 158 also requires companies to measure a plan s assets and its obligations that determine its funded status as of the end of the employer s fiscal year (with limited exceptions) instead of permitting companies to use a lag of up to three-months permitted by FASB Statement No. 87, Employers Accounting for Pensions , and FASB Statement No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions . The Company is in the process of determining the effect, if any; the adoption of Statement No. 158 will have on our financial statements.

**10) Income Taxes**

On April 12, 2005, New York State enacted tax legislation resulting in a change to the New York State apportionment methodology. Beginning in 2006, a single sales factor apportionment method will be phased in, with a single sales factor solely used in 2008. It is expected that this enacted legislation will result in a lower apportionment of the Company s taxable income to New York State, resulting in lower New York state income taxes. Accordingly, the Company s ability to use or realize New York State tax credits has been reduced. In 2005, the Company has assessed the impact of the new tax legislation and recorded a valuation allowance reducing the Company s \$490 thousand deferred tax asset relating to New York State tax credits to \$40 thousand. As a result of this valuation allowance the Company recorded a non-cash charge to income tax expense of \$300 thousand or \$0.04 per diluted share during the third quarter of 2005. The charge to income tax expense is net of the affect of federal income taxes. The effective tax rate in 2006 returned to a more normal rate of 36.4%

**11) Sales To Major Customers**

The Company has a significant concentration of business with two customers. Sales to the U.S. Government were approximately 10.9% and 12.9% of revenue during the 3<sup>rd</sup> quarter and year to date 2006, respectively. Sales to one other customer amounted to approximately 27.3% and 21.6% of its sales during the 3<sup>rd</sup> quarter and year to date 2006, respectively.

**Table of Contents****Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*(The following should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's Form 10-K for the year ended December 31, 2005.)*

The following table sets forth income statement data as a percent of net sales:

(in thousands)	Nine Months Ended		Three Months Ended	
	September 30, 2006	October 1, 2005	September 30, 2006	October 1, 2005
Sales	100.0%	100.0%	100.0%	100.0%
Cost of products sold	77.4	79.5	77.2	78.1
Selling, general and administrative and other expense	12.0	14.0	12.1	14.2
Interest expense	0.8	0.9	0.8	1.0
Total cost and expenses	90.2	94.4	90.1	93.3
Income before taxes	9.8%	5.6%	9.9%	6.7%

**ACQUISITION**

On February 3, 2005, the Company acquired the assets of the Airborne Electronic Systems (AES) business unit from a subsidiary of General Dynamics, for \$13.0 million. The Company used \$6.0 million of cash and borrowed \$7.0 million against its line of credit to finance the acquisition. No goodwill was recognized as a result of this acquisition. Operating results for this acquisition are included in the consolidated statement of income from the acquisition date.

**SALES**

Sales for the third quarter of 2006 increased 39.8% to \$28.5 million compared with \$20.4 million for the same period last year. Sales to the commercial transport market were \$15.8 million, as compared to \$7.9 million for the same period of 2005, an increase of \$7.9 million or 100.0 %. The sales increase to the commercial transport market was a result of increased volume of cabin electronics products. This volume increase was driven by increased installations of in-seat power and in-flight entertainment systems utilizing our products. Sales to the business jet market were \$6.3 million, up \$2.5 million, or 66.3%, compared with sales of \$3.8 million for the same period in 2005. The increase of sales to the business jet market was due primarily to an increase in volume as production of new business jets by the airframe manufacturers increased over last year. Sales to the military market were \$6.1 million as compared to \$8.3 million last year, a decrease of \$2.2 million or 26.3%. The decrease was primarily caused by a \$2.2 million decrease in deliveries for F-16 night vision kits for the Korean air force as the Korean program was concluded in 2005.

2006 year to date sales increased 50.2 % to \$82.5 million compared with \$54.9 million for the same period last year. Sales to the commercial transport market increased \$22.6 million, or 100.2% to \$45.1 million compared with \$22.5 million in the same period last year. This volume increase was driven by increased installations of in-seat power and in-flight entertainment systems utilizing our products. Sales to the business jet market were \$16.7 million, up \$4.8 million, or 39.9%, compared with \$11.9 million for the same period in 2005. The increase of sales to the business jet market was due primarily to an increase in volume as production of new business jets by the airframe manufacturers increased over last year. Sales to the military market were \$19.7 million, up from \$19.5 million in the same period of 2005. Shipments for the Tactical Tomahawk and Taurus Missile programs were primarily responsible for a \$1.9 million increase of sales for airframe power products to the military markets. This was offset by a \$3.0 million decrease in deliveries for F-16 night vision kits for the Korean air force as the Korean program was concluded in 2005. The balance of the change for military sales was a result of a general increase in volume.

A portion of the 2006 year to date sales increase is due to the timing of the Astronics Advanced Electronic Systems acquisition. The acquisition date was February 3, 2005, as such the first nine months of 2005 contained only thirty four weeks of sales for Astronics Advanced Electronic Systems as compared with thirty nine weeks in the first nine months of 2006.

**Table of Contents**

***EXPENSES AND MARGINS***

Cost of products sold as a percentage of sales remained basically flat at 77.2% for the third quarter of 2006 as compared to 78.1% for the same period last year. That slight decrease was primarily a result of the leverage provided by sales volume increases offset by a \$0.6 million increase in engineering and development costs.

Year to date costs of products sold decreased by 2.1 percentage points to 77.4 % as compared to 79.5% for the same period last year. That decrease was also a result of the leverage provided by sales volume increases without a corresponding increase to our fixed manufacturing costs. That leverage was partially offset by a \$1.0 million increase in engineering and development costs over the same period last year.

Selling, general and administrative and other (SG&A) expenses were \$3.5 million in the third quarter of 2006, up from \$2.9 million in the same period last year. But as a percent of sales, SG&A expenses was 12.1% for the third quarter of 2006 as compared to 14.2% for the same period in 2005 as sales grew at a faster pace than SG&A spending. The increase in total dollars was primarily due to increased wages and benefits due to increased staffing and compensation related costs and increased costs for audit and other professional services related to Sarbanes-Oxley 404 implementation.

For the first nine months of 2006 SG&A as a percentage of sales was 12.0% compared to 14.0% for the same period of 2005 as sales grew at a faster pace than SG&A spending. In terms of dollars SG&A costs increased \$2.2 million to \$9.9 million for the first nine months of 2006 from \$7.7 million in the first nine months of 2005. The increase was due to increased wages and benefits due to increased staffing and compensation related costs and increased costs for audit and other professional services related to Sarbanes-Oxley 404 implementation. Also, a portion of the 2006 year to date SG&A increase is due to the timing of the Astronics Advanced Electronic Systems acquisition. The acquisition date was February 3, 2005, as such the first nine months of 2005 contained only thirty four weeks of expenses for Astronics Advanced Electronic Systems as compared with thirty nine weeks in the first nine months of 2006.

Net interest expense for the third quarter of 2006 and 2005 was \$0.2 million. Net interest expense for the first nine months of 2006 increased by \$0.1 million from \$0.5 million in 2005 to \$0.6 million due to an increase in interest rates.

***TAXES***

The effective income tax rate for the third quarter of 2006 was 32.3 % compared to 42.8% last year. The 2006 year to date effective income tax rate was 36.4% compared to 47.9% last year. The 2005 tax rate was greater than the Company's historical rates due primarily to the Company's assessment of the impact of the new tax legislation in 2005 and the recording of a valuation allowance reducing the Company's \$0.5 million deferred tax asset relating to New York State tax credits to \$40 thousand. As a result of this valuation allowance the Company recorded a non-cash charge to income tax expense of \$0.3 million or \$.04 per share during the second quarter of 2005.

***NET INCOME AND EARNINGS PER SHARE***

Net income for the third quarter of 2006 was \$1.9 million or \$0.23 per diluted share, an increase of \$1.1 million from \$0.8 million, or \$0.10 per diluted share in the third quarter of 2005. The earnings per share increase was due to increased net income and was not significantly impacted by a change in shares outstanding.

***LIQUIDITY***

Cash used by operating activities totaled \$2.7 million during the first nine months of 2006, as compared with \$1.4 million of cash provided by operations during the first nine months of 2005. The change was due primarily to net income being offset by increased investment in net working capital components, primarily inventory and receivables associated with our increasing sales.

Cash used in investing activities decreased to \$2.4 million in the first nine months of 2006, from \$14.3 million used in the first nine months of 2005. This was due primarily to last year's \$13.4 million acquisition of Astronics

**Table of Contents**

Advanced Electronic Systems, offset partially by proceeds from the sale of short-term investments of \$1.0 million in 2005. Capital expenditures increased by \$0.5 million to \$2.3 million in 2006 compared to \$1.8 million in 2005. In the first nine months of 2006 cash provided by financing activities totaled \$1.3 million. The Company borrowed \$0.9 million using its revolving credit facility and had proceeds from the issuance of stock relating to the exercise of stock options totaling \$0.9 million. This was partially offset by principal payments against the long term debt of \$0.5 million.

The Company has a \$15 million demand line of credit facility. Interest on outstanding borrowings bears interest at either LIBOR plus an applicable margin, currently 150 basis points or prime interest rate, at the Company's option. At September 30, 2006 the Company had \$7.9 million outstanding on the line of credit. The line is subject to annual review and is payable on demand. The line of credit, among other requirements, imposes certain financial performance covenants measured on an annual basis with which the Company anticipates it will be compliant. During the third quarter the Company committed to proceed with an expansion to its East Aurora, NY operation. The facility is expected to be completed in the first half of 2007 and will add 57,000 square feet of production capacity. The cost for the expansion, including the initial acquisition of machinery and equipment is expected to be approximately \$7.5 million. The project has received an Industrial Revenue Bond inducement from the Erie County Industrial Development Agency and expects to finance the project through the issuance of long term Industrial Revenue Bonds.

The Company believes that cash flow from operations and its available credit facility will be adequate to meet the Company's operational and capital expenditure requirements for 2006.

***BACKLOG***

The Company's backlog at September 30, 2006 was \$86.4 million compared with \$77.6 million at October 1, 2005.

***CONTRACTUAL OBLIGATIONS AND COMMITMENTS***

The Company's contractual obligations and commercial commitments have not changed materially from disclosures in the Company's Form 10-K for the year ended December 31, 2005 except for those related to the 57,000 square foot building expansion project in East Aurora, NY. As of September 30, 2006, the Company estimates that obligations related to that project range between \$0.7 and \$1.0 million.

***MARKET RISK***

Risk due to fluctuation in interest rates is a function of the Company's floating rate debt obligations, which total approximately \$9.8 million at September 30, 2006. To partially offset this exposure, the Company entered into an interest rate swap in February 2006, on its New York Industrial Revenue Bond which effectively fixes the rate at 3.99% on this \$4.3 million obligation through January 2016. As a result, a change of 1% in interest rates would impact annual net income by less than \$0.1 million.

There have been no material changes in the current year regarding the market risk information for its exposure to currency exchange rates. The Company has limited exposure to fluctuation in Canadian currency exchange rates to the U.S. dollar.

Refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 for a complete discussion of the Company's market risk.

***CRITICAL ACCOUNTING POLICIES***

Refer to the Company's annual report on Form 10-K for the year ended December 31, 2005 for a complete discussion of the Company's critical accounting policies. Other than the adoption of SFAS 123(R), Share-Based Payments, (see Note 2 of the Notes to Consolidated Financial Statements) there have been no significant changes in the current year regarding critical accounting policies.

**Table of Contents**

***RECENT ACCOUNTING PRONOUNCEMENTS***

During the first quarter of 2006, we adopted SFAS 123(R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the statement of earnings based on the grant date fair value of the award. Under the modified prospective method, we are required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. We use a straight-line method of attributing the value of stock-based compensation expense, based on vesting. Stock compensation expense was \$0.1 million in the third quarter of 2006 and \$0.4 million year to date, after taxes. No stock compensation expense was recognized prior to 2006.

In June 2006, the FASB issued Interpretation ( FIN ) No. 48, Accounting for Uncertainty in Income Taxes an Interpretation for SFAS No. 109. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with for SFAS No. 109, Accounting for Income Taxes. The pronouncement prescribes a recognition threshold and measurement attributable to financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. The Company is in the process of determining the effect, if any; the adoption of FIN 48 will have on our financial statements.

In September 2006, the FASB issued FASB Statement No. 157, Fair Value Measurements . This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Where applicable, this Statement simplifies and codifies related guidance within generally accepted accounting principles. The Company is in the process of determining the effect, if any; the adoption of Statement No. 157 will have on our financial statements.

In September 2006, the FASB issued FASB Statement No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (an amendment of FASB Statements No. 87, 88, 106, and 132R). The Statement requires employers to fully recognize the obligations associated with single-employer defined benefit pension, retiree healthcare and other postretirement plans in their financial statements. Statement 158 also requires companies to measure a plan s assets and its obligations that determine its funded status as of the end of the employer s fiscal year (with limited exceptions) instead of permitting companies to use a lag of up to three-months permitted by FASB Statement No. 87, Employers Accounting for Pensions , and FASB Statement No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions . The Company is in the process of determining the effect, if any; the adoption of Statement No. 158 will have on our financial statements.

***FORWARD-LOOKING STATEMENTS***

This Quarterly Report contains certain forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involves uncertainties and risks. These statements are identified by the use of the words believes, expects, intends, anticipates, may, will, estimate, potential and words of similar import cautioned not to place undue reliance on these forward looking statements as various uncertainties and risks could cause actual results to differ materially from those anticipated in these statements. These uncertainties and risks include the success of the Company with effectively executing its plans; the timeliness of product deliveries by vendors and other vendor performance issues; changes in demand for our products from the U.S. government and other customers; the acceptance by the market of new products developed; our success in cross-selling products to different customers and markets; changes in government contracts; the state of the commercial and business jet aerospace market; the Company s success at increasing the content on current and new aircraft platforms; the level of aircraft build rates; as well as other general economic conditions and other factors.

**Table of Contents**

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

See Market Risk in Item 2, above.

**Item 4. Controls and Procedures**

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of September 30, 2006. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2006. There were no material changes in the Company's internal control over financial reporting during the third quarter of 2006.



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

None.

**Item 1a Risk Factors.**

In addition to other information set forth in this report, you should carefully consider the factors discussed in Part 1, Item 1A. Risk Factors, in our Annual Report on Form 10-K for the year ended December 31, 2005, which could materially affect our business, financial condition or results of operations. The risks described in our Annual Report of Form 10-K are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or results of operations.

**Item 2. Unregistered sales of equity securities and use of proceeds.**

(c) The following table summarizes the Company's purchases of its common stock for the quarter ended September 30, 2006:

Period	(a) Total number of shares Purchased	(b) Average Price Paid per Share	(c) Total number of shares Purchased as part of Publicly Announced Plans or Programs	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
July 2 July 29, 2006				432,956
July 30 August 26, 2006				432,956
August 27 September 30, 2006				432,956
Total				432,956

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Submission of Matters to a Vote of Securities Holders.**

None.

**Item 5. Other Information.**

None.

**Item 6 Exhibits and Reports on Form 8-K****(a) Exhibits**

Exhibit 31.1 Section 302 Certification Chief Executive Officer

Exhibit 31.2 Section 302 Certification Chief Financial Officer

Exhibit 32. Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

**(b) Reports on Form 8-K**

On August 7, 2006, Astronics Corporation issued a news release in Form 8-K announcing its financial results for the second quarter of 2006.

**Table of Contents**

**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.

**ASTRONICS CORPORATION**

(Registrant)

Date: November 14,  
2006

By: /s/ David C. Burney

David C. Burney  
Vice President-Finance and  
Treasurer  
(Principal Financial Officer)

19