

ASTRONICS CORP  
Form 10-K  
March 12, 2008

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

**þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the Fiscal Year Ended December 31, 2007**

**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**  
*(I.R.S. Employer Identification No.)*

**130 Commerce Way, East Aurora, N.Y. 14052**  
*(Address of principal executive office)*

**Registrant's telephone number, including area code**  
**(716) 805-1599**

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

**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 if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

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

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

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

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

|   |   |  |   |
|---|---|--|---|
| Large accelerated filer <input type="radio"/> | Accelerated filer <input checked="" type="checkbox"/> | Non-accelerated filer <input type="radio"/><br>(Do not check if a smaller reporting company) | Smaller reporting company <input type="radio"/> |
|---|---|--|---|

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

As of February 29, 2008, 8,176,848 shares were outstanding, consisting of 6,870,735 shares of Common Stock \$.01 Par Value and 1,306,113 shares of Class B Stock \$.01 Par Value. The aggregate market value, as of the last business day of the Company's most recently completed second fiscal quarter, of the shares of Common Stock and Class B Stock of Astronics Corporation held by non-affiliates was approximately \$218 million (assuming conversion of all of the outstanding Class B Stock into Common Stock and assuming the affiliates of the Registrant to be its directors, executive officers and persons known to the Registrant to beneficially own more than 10% of the outstanding capital stock of the Corporation).

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Company's Proxy Statement for the 2008 Annual Meeting of Shareholders to be held May 6, 2008 are incorporated by reference into Part III of this Report.

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## **FORWARD LOOKING STATEMENTS**

This Annual 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 may, will, should, believes, expects, expected, intends, plans, projects, estimates, predicts, anticipates, presume and assume, and words of similar import. Readers are 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. Certain of these factors, risks and uncertainties are discussed in the sections of this report entitled "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

## PART I

### ITEM 1. BUSINESS

Astronics is a leading supplier of advanced, high-performance lighting, electronics and power distribution systems for the global aerospace industry. We sell our products to airframe manufacturers (OEM s) in the commercial transport, business jet, military markets, OEM suppliers, and aircraft operators around the world. The Company provides its products through its wholly owned subsidiaries Luminescent Systems, Inc., Luminescent Systems Canada, Inc., and Astronics Advanced Electronic Systems Corp. (AES).

#### Strategy

Astronics strategy for growth is to continue to develop or acquire the necessary technology to evolve into a leading aircraft lighting, electronics and power generation and distribution systems integrator, increasing the value and content we provide on a growing base of aircraft and missile platforms.

#### Products and Customers

Astronics products are sold worldwide to manufacturers of business jets, military aircraft, missiles, and commercial transports, as well as airlines and suppliers to the OEM s. During 2007 the Company s sales were divided 63.5% to the commercial transport market, 16.0% to the military market, 19.7% to the business jet market, and the balance of 0.8% to other markets. Most of the Company s sales are a result of contracts or purchase orders received from customers, placed on a day-to-day basis or for single year procurements rather than long-term multi-year contract commitments. On occasion the Company does receive contractual commitments or blanket purchase orders from our customers covering multiple year deliveries of hardware to our customers. Sales by Geographic Region, Major Customer and Canadian Operations are provided in Note 8 of Item 8, Financial Statements and Supplementary Data in this report.

The Company has a significant concentration of business with one major customer and the U.S. Government. Sales to Panasonic Avionics accounted for 27.7% of sales in 2007, 21.2% of sales in 2006 and 2.1% of sales in 2005. Accounts receivable from this customer at December 31, 2007 and 2006 were \$4.0 million and \$1.9 million, respectively. Sales to the U.S. Government accounted for 4.0% of sales in 2007, 6.5% of sales in 2006 and 10.8% of sales in 2005. Accounts receivable from the U.S. Government at December 31, 2007 and 2006 were \$0.6 million and \$0.6 million, respectively.

#### Practices as to Maintaining Working Capital

Liquidity is discussed in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, in the Liquidity section in this report.

#### Competitive Conditions

Astronics experiences considerable competition in the Aerospace market sectors we serve, principally with respect to product performance and price, from various competitors, many of which are substantially larger and have greater resources. Success in the Aerospace markets we serve depends upon product innovation, customer support, responsiveness, and cost management. Astronics continues to invest in developing the technologies and engineering support critical to competing in our Aerospace markets.

#### Government Contracts

All U.S. Government contracts, including subcontracts where the U.S. Government is the ultimate customer, may be subject to termination at the election of the government.

### **Raw Materials**

Materials, supplies and components are purchased from numerous sources. We believe that the loss of any one source, although potentially disruptive in the short-term, would not materially affect our operations in the long-term.

### **Seasonality**

Our business is typically not seasonal.

### **Backlog**

At December 31, 2007, the Company's backlog was \$92.4 million. At December 31, 2006, the Company's backlog was \$99.5 million.

### **Patents**

The Company has a number of patents. While the aggregate protection of these patents is of value, the Company's only material business that is dependent upon the protection afforded by these patents is its cabin power distribution product. The Company's patents and patent applications relate to electroluminescence, instrument panels, keyboard technology and a broad patent covering the cabin power distribution technology. The Company regards its expertise and techniques as proprietary and relies upon trade secret laws and contractual arrangements to protect its rights. We have trademark protection in major markets.

### **Research, Development and Engineering Activities**

The Company is engaged in a variety of engineering and design activities as well as basic research and development activities directed to the substantial improvement or new application of the Company's existing technologies. These costs are expensed when incurred and included in cost of sales. Research and development and engineering costs amounted to approximately \$14.8 million in 2007, \$10.9 million in 2006 and \$8.9 million in 2005.

### **Employees**

The Company's continuing operations employed 967 employees as of December 31, 2007. The Company considers its relations with its employees to be good. None of our employees are subject to collective bargaining agreements.

### **Available information**

The Company files its financial information and other materials as electronically required by the SEC with the SEC. These materials can be accessed electronically via the Internet at [www.sec.gov](http://www.sec.gov). Such materials and other information about the Company are also available through the Company's website at [www.astronics.com](http://www.astronics.com).

## **ITEM 1A. RISK FACTORS**

**The markets we serve are cyclical and sensitive to domestic and foreign economic conditions and events, which may cause our operating results to fluctuate.** Demand by the business jet markets for our products is dependent upon several factors, including capital investment, product innovations, economic growth, and technology upgrades. In addition, the commercial airline industry is highly cyclical and sensitive to fuel price increases, labor disputes and economic conditions. A change in any of these factors could result in a reduction in the amount of air travel. A reduction in air travel would reduce orders for new aircraft and reductions in cabin upgrades by airlines for which we

supply products and for the sales of spare parts, thus reducing our sales and profits. A reduction in air travel may also result in our commercial airline customers being unable to pay our invoices on a timely basis or not at all.



We are a supplier on various new aircraft programs just entering or expected to begin production in the near future. As with any new program there is risk as to whether the aircraft or program will be successful and accepted by the market. As is customary for our business we purchase inventory and invest in specific capital equipment to support our production requirements generally based on delivery schedules provided by our customer. If a program or aircraft is not successful we may have to write off all or a part of the inventory, accounts receivable and capital equipment related to the program. A write off of these assets could result in a significant reduction of earnings and cause covenant violations relating to our debt agreements. This could result in our being unable to borrow additional funds under our bank credit facility or being obliged to refinance or renegotiate the terms of our bond debt.

**Our products are sold in highly competitive markets.** Some of our competitors are larger, more diversified corporations and have greater financial, marketing, production and research and development resources. As a result, they may be better able to withstand the effects of periodic economic downturns. Our operations and financial performance will be negatively impacted if our competitors:

Develop products that are superior to our products;

Develop products that are more competitively priced than our products;

Develop methods of more efficiently and effectively providing products and services or

Adapt more quickly than we do to new technologies or evolving customer requirements.

We believe that the principal points of competition in our markets are product quality, price, design and engineering capabilities, product development, conformity to customer specifications, quality of support after the sale, timeliness of delivery and effectiveness of the distribution organization. Maintaining and improving our competitive position will require continued investment in manufacturing, engineering, quality standards, marketing, customer service and support and our distribution networks. If we do not maintain sufficient resources to make these investments, or are not successful in maintaining our competitive position, our operations and financial performance will suffer.

**The loss of a major customer or a significant reduction in sales to a major customer would reduce our sales and earnings.** In 2007 we had a concentration of sales to a major customer representing 27.7% of our sales. The loss of this customer or a significant reduction in sales to this customer would significantly reduce our sales and earnings.

**Our future success depends to a significant degree upon the continued contributions of our management team and technical personnel.** The loss of members of our management team could have a material and adverse effect on our business. In addition, competition for qualified technical personnel in our industries is intense, and we believe that our future growth and success will depend on our ability to attract, train and retain such personnel.

**Future terror attacks, war, or other civil disturbances could negatively impact our business.** Continued terror attacks, war or other disturbances could lead to further economic instability and decreases in demand for our products, which could negatively impact our business, financial condition and results of operations. Terrorist attacks world-wide have caused instability from time to time in global financial markets and the aviation industry. The long-term effects of terrorist attacks on us are unknown. These attacks and the U.S. Government's continued efforts against terrorist organizations may lead to additional armed hostilities or to further acts of terrorism and civil disturbance in the United States or elsewhere, which may further contribute to economic instability.

**If we are unable to adapt to technological change, demand for our products may be reduced.** The technologies related to our products have undergone, and in the future may undergo, significant changes. To succeed in the future, we will need to continue to design, develop, manufacture, assemble, test, market and support new products and

enhancements on a timely and cost-effective basis. Our competitors may develop technologies and products that are more effective than those we develop or that render our technology and products obsolete or uncompetitive. Furthermore, our products could become unmarketable if new industry

standards emerge. We may have to modify our products significantly in the future to remain competitive, and new products we introduce may not be accepted by our customers.

**Our new product development efforts may not be successful, which would result in a reduction in our sales and earnings.** We may experience difficulties that could delay or prevent the successful development of new products or product enhancements, and new products or product enhancements may not be accepted by our customers. In addition, the development expenses we incur may exceed our cost estimates, and new products we develop may not generate sales sufficient to offset our costs. If any of these events occur, our sales and profits could be adversely affected.

**If our subcontractors or suppliers fail to perform their contractual obligations, our prime contract performance and our ability to obtain future business could be materially and adversely impacted.** Many of our contracts involve subcontracts with other companies upon which we rely to perform a portion of the services we must provide to our customers. There is a risk that we may have disputes with our subcontractors, including disputes regarding the quality and timeliness of work performed by the subcontractor or customer concerns about the subcontractor. Failure by our subcontractors to satisfactorily provide on a timely basis the agreed-upon supplies or perform the agreed-upon services may materially and adversely impact our ability to perform our obligations with our customer. Subcontractor performance deficiencies could result in a customer terminating our contract for default. A default termination could expose us to liability and substantially impair our ability to compete for future contracts and orders. In addition, a delay in our ability to obtain components and equipment parts from our suppliers may affect our ability to meet our customers' needs and may have an adverse effect upon our profitability.

**Our results of operations are affected by our fixed-price contracts, which could subject us to losses in the event that we have cost overruns.** For the year ended December 31, 2007, fixed-price contracts represented 100% of our sales. On fixed-price contracts, we agree to perform the scope of work specified in the contract for a predetermined price. Depending on the fixed price negotiated, these contracts may provide us with an opportunity to achieve higher profits based on the relationship between our costs and the contract's fixed price. However, we bear the risk that increased or unexpected costs may reduce our profit.

**Some of our contracts contain late delivery penalties.** Failure to deliver in a timely manner due to supplier problems, development schedule slides, manufacturing difficulties, or similar schedule related events could have a material adverse effect on our business.

**The failure of our products may damage our reputation, necessitate a product recall or result in claims against us that exceed our insurance coverage, thereby requiring us to pay significant damages.** Defects in the design and manufacture of our products may necessitate a product recall. We include complex system design and components in our products that could contain errors or defects, particularly when we incorporate new technology into our products. If any of our products are defective, we could be required to redesign or recall those products or pay substantial damages or warranty claims. Such an event could result in significant expenses, disrupt sales and affect our reputation and that of our products. We are also exposed to product liability claims. We carry aircraft and non-aircraft product liability insurance consistent with industry norms. However, this insurance coverage may not be sufficient to fully cover the payment of any potential claim. A product recall or a product liability claim not covered by insurance could have a material adverse effect on our business, financial condition and results of operations.

**Our facilities could be damaged by catastrophes which could reduce our production capacity and result in a loss of customers.** We conduct our operations in facilities located in the United States and Canada. Any of these facilities could be damaged by fire, floods, earthquakes, power loss, telecommunication and information systems failure or similar events. Although we carry property insurance, including business interruption insurance, our inability to meet customers' schedules as a result of catastrophe may result in a loss of customers or significant additional costs such as penalty claims under customer contracts.

**Contracting in the defense industry is subject to significant regulation, including rules related to bidding, billing and accounting kickbacks and false claims, and any non-compliance could subject us to fines and penalties or possible debarment.** Like all government contractors, we are subject to risks

associated with this contracting. These risks include the potential for substantial civil and criminal fines and penalties. These fines and penalties could be imposed for failing to follow procurement integrity and bidding rules, employing improper billing practices or otherwise failing to follow cost accounting standards, receiving or paying kickbacks or filing false claims. We have been, and expect to continue to be, subjected to audits and investigations by government agencies. The failure to comply with the terms of our government contracts could harm our business reputation. It could also result in suspension or debarment from future government contracts.

**We depend on government contracts and subcontracts with defense prime contractors and sub contractors that may not be fully funded or may be terminated, and the failure to receive funding or the termination of one or more of these contracts could reduce our sales.** Sales to the U.S. Government and its prime contractors and subcontractors represent a significant portion of our business. The funding of these programs is generally subject to annual congressional appropriations, and congressional priorities are subject to change. In addition, government expenditures for defense programs may decline or these defense programs may be terminated. A decline in governmental expenditures may result in a reduction in the volume of contracts awarded to us.

**If we fail to meet expectations of securities analysts or investors due to fluctuations in our revenue or operating results, our stock price could decline significantly.** Our revenue and earnings may fluctuate from quarter to quarter due to a number of factors, including delays or cancellations of programs. It is likely that in some future quarters our operating results may fall below the expectations of securities analysts or investors. In this event, the trading price of our common stock could decline significantly.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None

**ITEM 2. PROPERTIES**

The Company owns manufacturing and office facilities of approximately 125,000 square feet in the Buffalo, New York area. The Company owns manufacturing and office facilities of approximately 80,000 square feet in Lebanon, New Hampshire. Astronics AES leases approximately 100,000 square feet of space, located in Redmond, Washington. The lease expires in March of 2008 with one option to renew to 2013. The Montreal, Quebec, Canada operations are in leased facilities of approximately 16,000 square feet. The lease expires in 2009. Upon expiration of its current leases, the Company believes that it will be able to secure renewal terms or enter into a lease for alternative locations.

We believe that our properties have been adequately maintained and are generally in good condition.

**ITEM 3. LEGAL PROCEEDINGS**

We are not party to any pending legal proceedings that management believes will result in material adverse effect on our financial condition or results of operations.

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

Not applicable

**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

The table below sets forth the range of prices for the Company's Common Stock, traded on the NASDAQ National Market System, for each quarterly period during the last two years. The approximate number of shareholders of record as of February 29, 2008, was 756 for Common Stock and 651 for Class B Stock.

| <b>2007</b>  | <b>High</b> | <b>Low</b> |
|--------------|-------------|------------|
| (In dollars) |             |            |
| First        | \$ 21.09    | \$ 16.92   |
| Second       | 32.63       | 16.31      |
| Third        | 43.57       | 29.25      |
| Fourth       | 53.88       | 38.30      |
| <b>2006</b>  | <b>High</b> | <b>Low</b> |
| First        | \$ 13.67    | \$ 10.15   |
| Second       | 15.04       | 11.61      |
| Third        | 16.55       | 12.66      |
| Fourth       | 17.50       | 14.42      |

The Company has not paid any cash dividends in the three-year period ended December 31, 2007. It has no plans to pay cash dividends as it plans to retain all cash from operations as a source of capital to finance growth in the business. There are no restrictions, however on the Company's ability to pay dividends.

With respect to information regarding our securities authorized for issuance under equity incentive plans, the information contained in the section entitled "Equity Compensation Plan Information" of our definitive Proxy Statement for the 2008 Annual Meeting of Shareholders is incorporated herein by reference.

We did not repurchase any shares of our common stock in 2007.

The following graph charts the annual percentage change in return on the Company's common stock compared to the S&P 500 Index Total Return and the NASDAQ US and Foreign Securities:

**Comparison of 5 Year Cumulative Total Return  
Assumes Initial Investment of \$100  
December 2007**

**COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***

Among Astronics Corporation, The S&P 500 Index  
And The NASDAQ US & Foreign Index

\* \$100 invested on 12/31/02 in stock or index-including reinvestment of dividends.  
Fiscal year ending December 31.

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[www.researchdatagroup.com/S&P.htm](http://www.researchdatagroup.com/S&P.htm)

|                                  | <b>2002</b>   | <b>2003</b>   | <b>2004</b>   | <b>2005</b>   | <b>2006</b>   | <b>2007</b>    |
|----------------------------------|---------------|---------------|---------------|---------------|---------------|----------------|
| ASTRONICS CORP                   | <b>100.00</b> | <b>138.68</b> | <b>142.30</b> | <b>299.95</b> | <b>477.97</b> | <b>1185.86</b> |
| S&P 500 Index Total Return       | <b>100.00</b> | <b>128.68</b> | <b>142.69</b> | <b>149.70</b> | <b>173.34</b> | <b>182.87</b>  |
| NASDAQ US and Foreign Securities | <b>100.00</b> | <b>149.34</b> | <b>161.86</b> | <b>166.64</b> | <b>186.18</b> | <b>205.48</b>  |

**ITEM 6. SELECTED FINANCIAL DATA****Five-Year Performance Highlights**

|  | 2007(1)    | 2006(1)    | 2005(1)   | 2004      | 2003      |
|--|------------|------------|-----------|-----------|-----------|
| (Dollars in thousand, except for per share data)         |            |            |           |           |           |
| PERFORMANCE (continuing operations)                      |            |            |           |           |           |
| Sales  | \$ 158,240 | \$ 110,767 | \$ 74,354 | \$ 34,696 | \$ 33,182 |
| Income (Loss) from Continuing Operations                 | \$ 15,391  | \$ 5,736   | \$ 2,237  | \$ (734)  | \$ 782    |
| Net Margin   | 9.7%       | 5.2%       | 3.0%      | (2.1)%    | 2.4%      |
| Diluted Earnings (Loss) per Share, Continuing Operations | \$ 1.80    | \$ 0.69    | \$ 0.28   | \$ (0.09) | \$ 0.10   |
| Weighted Average Shares Outstanding Diluted              | 8,569      | 8,269      | 8,038     | 7,766     | 7,815     |
| Return on Average Assets                                 | 16.5%      | 7.7%       | 4.0%      | (1.6)%    | 1.7%      |
| Return on Average Equity                                 | 38.2%      | 20.2%      | 9.3%      | (3.2)%    | 3.4%      |

**YEAR-END FINANCIAL POSITION**

(continuing operations)

|                      |            |           |           |           |           |
|----------------------|------------|-----------|-----------|-----------|-----------|
| Working Capital      | \$ 32,100  | \$ 17,437 | \$ 13,349 | \$ 18,104 | \$ 18,767 |
| Total Assets         | \$ 104,121 | \$ 82,538 | \$ 66,439 | \$ 45,236 | \$ 45,474 |
| Indebtedness         | \$ 22,935  | \$ 18,449 | \$ 18,218 | \$ 12,062 | \$ 13,378 |
| Shareholders Equity  | \$ 49,232  | \$ 31,348 | \$ 25,418 | \$ 22,660 | \$ 22,940 |
| Book Value Per Share | \$ 6.04    | \$ 3.91   | \$ 3.22   | \$ 2.91   | \$ 2.96   |

**OTHER YEAR-END DATA**

(continuing operations)

|                               |          |          |          |          |          |
|-------------------------------|----------|----------|----------|----------|----------|
| Depreciation and Amortization | \$ 3,440 | \$ 2,929 | \$ 2,373 | \$ 1,273 | \$ 1,212 |
| Capital Expenditures          | \$ 9,592 | \$ 5,400 | \$ 2,498 | \$ 1,136 | \$ 420   |
| Shares Outstanding            | 8,149    | 8,026    | 7,901    | 7,800    | 7,742    |
| Number of Employees           | 967      | 787      | 702      | 424      | 369      |

(1) Information includes the effects of the acquisition of AES on February 3, 2005.

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

Astronics Corporation, through its subsidiaries Astronics Advanced Electronic Systems Corp., Luminescent Systems Inc. and Luminescent Systems Canada Inc. designs and manufactures electrical power generation, control and



distribution systems and lighting systems and components, for the aerospace industry. We operate four principal facilities located in New York State, New Hampshire, Washington State and Quebec, Canada. We serve the three primary aircraft markets which are the military, commercial transport and the business jet markets. In 2007, the break down of sales to the commercial transport market, the military market and the business jet market were 63.5%, 16.0% and 19.7%, respectively, miscellaneous sales to non-aerospace markets accounted for 0.8% of sales. Astronics strives to offer comprehensive lighting and electrical systems for aircraft which we believe make the Company unique in our ability to serve our customers.

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 acquired the business for \$13.0 million in cash. The Company financed the acquisition and related costs by borrowing \$7.0 million on its revolving line of credit and used \$6.4 million of cash on hand.

During the fourth quarter of 2006 we broke ground on a 57,000 square foot expansion to our East Aurora, New York facility. The cost of the building was approximately \$4.3 million exclusive of manufacturing

equipment which is being acquired as needed. We financed the project and equipment purchases relating to the expansion with a \$6.0 million tax exempt bond offering during the first half of 2007. This expansion provides additional production capacity allowing for continued growth. The bond will be repaid over 18 years beginning in 2010. We began utilizing the space during the third quarter of 2007.

Key factors affecting Astronics' growth are our ability to have our products designed into the plans for new aircraft, the rate at which new aircraft are produced, government funding of military programs, and the rates at which aircraft owners, including commercial airlines, refurbish or install upgrades to their aircraft. Once designed into a new aircraft, the spare parts business is frequently retained by the Company. Astronics' strategy is to increase the amount of content on aircraft platforms, evolving the Company from our historic role of a components supplier to a turn-key provider of complete systems.

We provide cabin electronics and cabin lighting to the commercial transport market, this is our largest market. The February 2005 acquisition of Astronics AES increased our footprint in the commercial transport market to the point where sales to this market represent approximately 63.5% of our total revenue in 2007 compared with 19.1% prior to the acquisition. From 2005 to 2007 we saw our revenue from the commercial transport market increase from \$30.2 million to \$100.5 million a 82.4% compound annual growth rate. This was largely led by our cabin electronics products which provide in-seat power for passengers and power to in-flight entertainment systems. We do not expect this rate of growth in the future. We continue to believe that this market is strong and will remain strong provided the commercial transports continue to improve their financial positions and the global economy remains strong. We continue to see many retrofit opportunities in this market including inquiries from many of the North American airlines. There were a number of factors that contributed to the rapid growth of the past few years. Years of under investing by the airlines created significant pent up demand for cabin upgrades. From 2001 until roughly 2005 commercial airlines around the world invested very little in terms of upgrading their cabin interiors and took delivery of few new aircraft. Beginning in 2005, the Asian airlines began to invest in upgrading their cabins, adding more in-seat power and in-flight entertainment systems and demand for our products grew. This combined with the introduction of better in seat power technology and our market leading position relative to our competition created an unusually steep growth curve for us through 2007. Going forward we expect there will continue to be retrofit opportunities around the world, however, predicting if and when these airlines choose to install our products is difficult. Additionally we expect next generation aircraft such as the Airbus A380 and the Boeing 787 will be equipped with more in-seat power than the older aircraft which they will be replacing. This will provide us with an opportunity to compete for that work. We estimate that our market share for our cabin electronics products to be about 75%. Continued growth will depend not only on growth of the overall market but our ability to either sustain or increase market share and continued development of our teaming arrangements with major in-flight entertainment suppliers. Cabin electronics products, which are principally sold to the commercial transport market, accounted for 52.6% of our sales in 2007 and 41.3% of our sales in 2006.

Another market we serve is the business jet market. In 2007 we saw volume and average ship set value increase in the business jet market as business jet airframe manufacturers production increased. The Cessna Mustang (exterior and cockpit lighting) and Eclipse 500 (exterior, cockpit and power distribution) Very Light Jets (VLJ) entered production and illuminated cockpit display panel assembly deliveries increased to Piaggio for the Avanti II. We anticipate production for each of these platforms to increase in 2008. In 2007 we were selected to provide exterior lighting and cockpit lighting controllers for the Embraer Phenom 300 jet that is expected to begin production in 2009. We will provide similar parts for the Phenom 100 which is expected to begin production in 2008. We continue to see a wide range of opportunities to employ our technology in the business jet markets. There is risk involved in the development of any new aircraft. We are encouraged to see the VLJ market continue to develop but it is not without risk. Much of the demand for the VLJ market is expected to be driven by the start up Air Taxi industry. Overall, we believe that the VLJ market will develop and we are positioning ourselves to participate having won work on key programs such as the Cessna Mustang, Embraer Phenom 100, Phenom 300 and the Eclipse 500.

Our Military market sales are typically comprised of several significant programs such as the power converter for the Tactical Tomahawk and Taurus missiles and the V22 Osprey, complemented by many spare part orders covering many aircraft platforms. Over the past several years we have been developing the exterior

lighting suite for the F-35 Joint Strike Fighter. This aircraft is expected to enter low rate production in 2008 and we are in the process of negotiating a contract to support the low rate production phase of the program. The Military market is dependent on governmental funding which can change from year to year. Risks are that overall spending may be reduced in the future and that specific programs may be eliminated. Astronics does not have significant reliance on any one program such that cancellation of a particular program will cause material financial loss. We believe that we will continue to have opportunities similar to past years regarding this market.

Each of the markets that we serve is presenting opportunities that we expect will provide continued growth for the Company over the long-term. We continue to look for opportunities in all three markets to capitalize on our core competencies to expand our existing business and to grow through strategic acquisitions.

In 2008 we expect to see our revenue grow approximately 7%. We are projecting 2008 revenues to be about \$170 million. The aerospace market continues to be strong with many quality opportunities for us to pursue. Airframe manufacturers have record backlogs representing several years of production which we expect will result in continued demand for our products provided the global economy maintains its strength. Continuing ramp up in production of some platforms such as the Cessna Mustang and Eclipse 500 will be tempered by fairly flat sales to the commercial transport market and military markets. Despite the slow down in year over year growth expected in 2008 as compared with the past year we still see many opportunities for long term growth and expect to continue investing in developmental programs to push our capabilities. In the commercial transport market, our largest and fastest growing market during the past few years, we expect our revenue in 2008 will be flat with 2007 revenue due to the timing of cabin upgrade programs which impacts our cabin electronics sales. From 2005 to 2007 sales to the commercial transport market grew by 82.4% compounded annually, principally driven by large cabin up grade programs. The nature of these programs is such that they tend to have choppy revenue and booking streams. Forecasting if and when the upgrades will take place is difficult. While there are still significant opportunities for cabin upgrades, particularly in North America, we expect that if these opportunities are converted to bookings, revenue from these programs would likely occur in the latter part of 2008 and beyond. Beyond 2008 we expect that the next generation of commercial transports such as the Boeing 787 and Airbus A380 will be equipped with more in-seat power and in-flight entertainment than the aircraft they are replacing. We expect this will provide a significant opportunity for us. In 2008 we expect our sales to the business jet market to provide most of the growth for the Company as airframe manufacturers delivery of new aircraft increases as compared with 2007. There are a number of new high quality opportunities we expect will be presented to us during the year that we will be prepared to invest in. We expect that our engineering and development costs will increase during 2008 as compared with last year to over \$20 million as compared with \$14.8 million in 2007.

Challenges facing us include improving shareholder value through profitability. Increasing profitability is dependent on many things such as increased build rates for existing aircraft, market acceptance and economic success of new aircraft such as the Cessna Mustang and Eclipse 500 business jets, continued government funding of defense programs such as the F-35 Joint Strike Fighter and V-22 Osprey and the Company's ability to obtain production contracts for parts we currently supply or have been selected to design and develop for these programs. In addition we are faced with continued increasing health care and corporate governance costs, particularly those required by Sarbanes-Oxley legislation. Many of our newer development programs are based on new and unproven technology. We are challenged to develop the technology on a schedule that is consistent with specific aircraft development programs. We will continue to address these challenges by working to improve operating efficiencies and focusing on executing on the growth opportunities currently in front of us. Finally, demand for our products is driven by the discretionary spending of aircraft owners and airlines and new aircraft build rates. A weakening economy would likely result in reduced demand for our products, lowering our profitability.

## **CRITICAL ACCOUNTING POLICIES**

Our financial statements and accompanying notes are prepared in accordance with U.S. generally accepted accounting principles. The preparation of the Company's financial statements requires management to make estimates, assumptions and judgments that affect the amounts reported. These estimates, assumptions and

judgments are affected by management's application of accounting policies, which are discussed in Note 1 of Item 8, Financial Statements and Supplementary Data of this report. The critical accounting policies have been reviewed with the audit committee of our board of directors.

### **Revenue Recognition**

Revenue is recognized on the accrual basis at the time of shipment of goods and transfer of title. There are no significant contracts allowing for right of return. The Company does evaluate and record an allowance for any potential returns based on experience and any known circumstances. For the years ended December 31, 2007 and 2006, no allowances were recorded for contracts allowing for right of return. A trade receivable is recorded at the value of the sale. The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral.

### **Accounts Receivable and Allowance for Doubtful Accounts**

The Company records a valuation allowance to account for potentially uncollectible accounts receivable. The allowance is determined based on Management's knowledge of the business, specific customers, review of receivable agings and a specific identification of accounts where collection is at risk. At December 31, 2007, the Company's allowance for doubtful accounts for accounts receivable was \$0.5 million, or 2.4% of gross accounts receivable. At December 31, 2006, the Company's allowance for doubtful accounts for accounts receivable was \$0.3 million, or 1.8% of gross accounts receivable.

### **Inventory Valuation**

The Company records valuation reserves to provide for slow moving or obsolete inventory or to reduce inventory to the lower of cost or market value. In determining the appropriate reserve, Management considers the age of inventory on hand, the overall inventory levels in relation to forecasted demands as well as reserving for specifically identified inventory that the Company believes is no longer salable. At December 31, 2007, the Company's reserve for inventory valuation was \$4.1 million, or 10.0% of gross inventory. At December 31, 2006, the Company's reserve for inventory valuation was \$4.1 million, or 11.6% of gross inventory.

### **Deferred Tax Asset Valuation Allowances**

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. We record a valuation allowance to reduce deferred tax assets to the amount of future tax benefit that we believe is more likely than not to be realized. We consider recent earnings projections, allowable tax carryforward periods, tax planning strategies and historical earnings performance to determine the amount of the valuation allowance. Changes in these factors could cause us to adjust our valuation allowance, which would impact our income tax expense when we determine that these factors have changed.

As of December 31, 2007, the Company had a net deferred tax asset of \$2.6 million, net of a \$0.8 million valuation allowance, net of the federal tax benefit. These assets relate principally to liabilities or asset valuation reserves that result in timing difference between generally acceptable accounting principles recognition and treatment for income tax purposes, as well as a state investment tax credit carry-forwards and foreign research and development tax credit carryforwards.

### **Goodwill**

The Company's goodwill is the result of the excess of purchase price over net assets acquired from acquisitions. As of December 31, 2007, the Company had \$3.0 million of goodwill. The Company tests goodwill for impairment at least annually during the fourth quarter, and whenever events occur or circumstances change that indicates there may be impairment. The process of evaluating the Company's goodwill for impairment is subjective and requires significant estimates. These estimates include judgments about future cash flows that are dependent on internal forecasts, long-term growth rates and estimates of the

weighted average cost of capital used to discount projected cash flows. Based on the discounted projected cash flows, management has concluded that there is no impairment of the Company's goodwill.

### **Supplemental Retirement Plan**

The Company maintains a supplemental retirement plan for certain executives. The accounting for this plan is based in part on certain assumptions that may be highly uncertain and may have a material impact on the financial statements if different reasonable assumptions had been used. The assumptions for increases in compensation and the discount rate for determining the cost recognized in 2007 were 5.00% and 5.75%, respectively. The discount rate used for the projected benefit obligation as of December 31, 2007 was 5.75%. The assumption for compensation increases takes a long-term view of inflation and performance based salary adjustments based on the Company's approach to executive compensation. For determining the discount rate the Company considers long-term interest rates for high-grade corporate bonds.

## **RESULTS OF OPERATIONS**

### **Sales**

Sales for 2007 increased by \$47.4 million or 42.9%, to \$158.2 million from \$110.8 million in 2006. By market, the increase was primarily the result of an increase in sales to the commercial transport market of \$39.2 million to \$100.5 million and an increase in sales to the business jet market of \$8.3 million to \$31.2 million. The military market and other markets remained flat at \$25.4 million and \$1.1 million, respectively. The increase in sales to the commercial transport market was primarily a result of \$37.4 million increase from Cabin Electronics and a \$1.0 million increase from Cockpit Lighting products. The Cabin Electronics increase resulted from increased volume driven by increasing installations of in-seat power and power for in-flight entertainment systems as retrofits for existing aircraft. Sales increases of Cockpit Lighting were a result of increased volume as new aircraft build rates increase as compared to last year. The increase of sales to the business jet market was primarily a result of \$3.8 million increase from Airframe power sales, a \$3.3 million increase in Cockpit Lighting and a \$1.2 million increase of Exterior Lighting sales, all driven by increasing product demand of aircraft containing our products and increasing ship set content on those new aircraft.

Sales for 2006 increased by \$36.4 million to \$110.8 million, up from \$74.4 million in 2005, an increase of 48.9%. By market, the increase was primarily the result of an increase in sales to the commercial transport market of \$31.0 million, an increase in sales to the business jet market of \$7.5 million, partially offset by a \$2.2 million decrease in sales to the military market. The increase in sales to the commercial transport market was primarily a result of \$30.2 million increase from Cabin Electronics and a \$1.3 million increase from Cabin Lighting products. The Cabin Electronics increase resulted from increased volume driven by increasing installations of in-seat power and in-flight entertainment systems. The increased sales from Cabin Lighting was a result of increased volume. The increase of sales to the business jet market was primarily a result of \$4.3 million increase from cockpit lighting, a \$2.6 million increase in Airframe power sales and a \$0.6 million increase of Exterior Lighting sales all driven by increasing production volumes of aircraft containing our products and increasing ship set content on those aircraft. The decrease of sales to the military was primarily related to a \$4.8 million decrease in the night vision retro fit kits program for the Korean Air Force which was concluded in 2005, offset by increased sales to the Tactical Tomahawk and Taurus Missile programs of \$2.5 million.

### **Expenses and Margins**

Cost of products sold as a percentage of sales decreased by 4.8 percentage points to 74.2% in 2007 from 79.0% in 2006. This decrease was due to leverage provided by the increased sales volume offset by an increase in engineering



and design costs of \$3.9 million. It is our intention to continue investing in capabilities and technologies as needed that allows us to execute our strategy to increase the ship set content and value we provide on aircraft in all markets that we serve. The rate of spending on these activities, however, will largely be driven by market opportunities.

Cost of products sold as a percentage of sales remained flat at 79.0% in 2006 from 80.0% in 2005. Leverage provided by the increased sales volume was offset somewhat by an increase in engineering and design costs. Engineering and design spending related primarily to product development increased by \$2.0 million to \$10.9 million in 2006 as compared with \$8.9 million in 2005.

Selling, general and administrative expenses ( SG&A ) increased \$2.8 million to \$16.4 million in 2007 from \$13.6 million in 2006 primarily the result of increased wages and benefits. As a percentage of sales, SG&A expense was 10.4% compared to 12.3% for the same period of 2006 as sales grew at a faster pace than SG&A spending.

Selling, general and administrative expenses were \$13.6 million in 2006, compared to \$10.2 million in 2005. During 2006, the increase was primarily due to increased wages and benefits as well as increased costs for audit and other professional services related to Sarbanes-Oxley 404 implementation. As a percentage of sales, SG&A expense was 12.3% compared to 13.8% for the same period of 2005 as sales grew at a faster pace than SG&A spending. Also, a portion of the 2006 year to date SG&A increase is due to the timing of the AES acquisition. The acquisition date was February 3, 2005 and as such, 2005 contained only forty seven weeks of expenses for AES as compared with fifty two weeks in 2006.

Net interest expense was \$1.4 million and \$0.9 million in 2007 and 2006 respectively. The Series 2007 Industrial Revenue Bonds issued in April of 2007 to finance the building and manufacturing expansion project in New York, higher average borrowing levels throughout the year on our revolving credit facility and increased averaged interest rates on our variable rate debt were the reasons for the increase when compared to 2006.

Net interest expense for 2006 was \$0.9 million, an increase of \$0.2 million from \$0.7 million in 2005. The increase was due to increased debt levels and an increase in interest rates on our variable rate debt.

### **Income Taxes**

The effective tax rate was 33.1% in 2007, 1.4 percentage points lower than the effective tax rate of 34.5% in 2006. The majority of the change was due to the impact of permanent differences and lower state and foreign taxes as a percentage of pretax income, which were partially offset by a non-cash charge to income tax expense of \$0.5 million to reduce our deferred tax assets relating primarily to 2007 New York State investment tax credits on the new building and equipment and foreign research and development tax credit carryforwards. We expect in future years, the effective tax rate will continue to approximate statutory rates in effect.

The effective tax rate was 34.5% in 2006, 11.8 percentage points lower than the effective tax rate of 46.3% in 2005. The majority of the decrease was due to a reserve that we recorded to reduce our deferred tax assets relating to New York State investment tax credit carry forwards in the second quarter of 2005, a non-cash charge to income tax expense of \$0.3 million, net of federal taxes combined with the impact of lower state income taxes.

### **Off Balance Sheet Arrangements**

We do not have any material off balance sheet arrangements that have or are reasonably likely to have a material future effect on our results of operations or financial condition.

**Contractual Obligations**

|                               | Total     | Payments Due by Period |           |           |            |
|-------------------------------|-----------|------------------------|-----------|-----------|------------|
|                               |           | 2008                   | 2009-2010 | 2011-2012 | After 2012 |
| (In thousands)                |           |                        |           |           |            |
| Note Payable                  | \$ 7,300  | \$ 7,300               | \$        | \$        | \$         |
| Long-Term Debt                | 15,635    | 951                    | 2,169     | 2,544     | 9,971      |
| Interest on Long-Term Debt    | 912       | 134                    | 265       | 230       | 283        |
| Operating Leases              | 865       | 635                    | 230       |           |            |
| Purchase Obligations          | 21,519    | 21,156                 | 363       |           |            |
| Other Long Term Liabilities*  | 1,059     | 175                    | 437       | 206       | 241        |
| Total Contractual Obligations | \$ 47,290 | \$ 30,351              | \$ 3,464  | \$ 2,980  | \$ 10,495  |

\* Excludes Supplemental Retirement Plan and related Post Retirement Obligations for which we anticipate making \$0.4 million in annual payments in 2008 through 2012.

**Notes to Contractual Obligations Table**

*Note Payable and Long-Term Debt* See Item 8, Financial Statements and Supplementary Data, Note 2, Long-Term Debt and Note Payable in this report.

*Interest on Long-Term Debt* Interest on Long-Term Debt consists of payments on the Series 1999 Industrial Revenue Bonds issued through the Erie County, New York Industrial Development Agency taking into account the interest rate swap entered into on February 6, 2006 which effectively fixes the interest rate on this obligation at 3.99% through January 2016. We have excluded the variable rate interest on our note payable and other long-term debt.

*Operating Leases* Operating lease obligations are primarily related to facility and equipment leases for our Astronics AES operations and facility leases for our Canadian operations. The Astronics AES lease expires in March 2008. The Company expects the lease to be extended for up to five years per the lease agreement and is currently negotiating the terms of the extension.

*Purchase Obligations* Purchase obligations are comprised of the Company's commitments for goods and services in the normal course of business.

**LIQUIDITY AND CAPITAL RESOURCES**

Cash flow provided by operating activities was \$8.6 million in 2007 compared with \$0.05 million used for operating activities in 2006. The increase of \$8.6 million as compared with 2006 was mainly a result of an increase in net income of \$9.7 million to \$15.4 million in 2007 from net income in 2006 of \$5.7 million, adjustments for non-cash charges such as depreciation and amortization of \$3.4 million, being offset by a net increase in investment in working capital components, primarily receivables, inventory and payables. The increase in investment in working capital components during 2007 was driven by the Company's sales growth.

Cash flow used by operating activities was \$0.05 million in 2006 compared with \$5.0 million provided by operations in 2005. The decrease in 2006 relates to higher net income adjusted for non-cash charges such as depreciation and amortization, offset by a net increase in investment in working capital components driven by the Company's sales growth.

The Company's cash flows from operations are primarily dependent on its sales, profit margins and the timing of collections of receivables, volume of inventory and payments to suppliers. Sales are influenced significantly by the build rates of new aircraft, which amongst other things are subject to general economic conditions, government appropriations and airline passenger travel. Over time, sales will also be impacted by the Company's success in executing its strategy to increase ship set content and obtain production orders for programs currently in the development stage. A significant change in new aircraft build rates could be

expected to impact the Company's profits and cash flow. A significant change in government procurement and funding and the overall health of the worldwide airline industry could be expected to impact the Company's profits and cash flow as well.

Cash used for investing activities in 2007 was \$10.3 million, primarily due to capital expenditures of \$9.6 million. In 2006, cash used for investing activities was \$5.5 million compared with \$15.0 million in 2005, a \$9.5 million decrease. This decrease was primarily due to a combination of 2005 including the Astronics AES acquisition of \$13.4 million with no comparable acquisition in 2006 offset by increased capital expenditures of approximately \$2.9 million in 2006.

The Company's cash required for capital equipment purchases for the last three years ranged between \$2.5 million and \$9.6 million. Our expectation for 2008 is that capital equipment expenditures will approximate \$6.0 million to \$8.0 million. Future capital requirements depend on numerous factors, including expansion of existing product lines and introduction of new products. Management believes that the Company's cash flow from operations and current borrowing arrangements will provide for these necessary capital expenditures.

At December 31, 2007, the Company was in compliance with all of the covenants pursuant to the credit facility in existence with HSBC Bank USA at that time.

The Company's cash needs for debt service for 2008 are expected to be consistent with 2007 levels as principal payments on the Series 2007 Industrial Revenue Bonds do not begin until 2010.

The Company's ability to maintain sufficient liquidity is highly dependent upon achieving expected operating results. During 2007 the Company negotiated new credit terms with its lender in order to provide more operating flexibility. However, failure to achieve expected operating results could have a material adverse effect on our liquidity and our operations in the future.

The Company's cash needs for working capital, capital equipment and debt service during 2008 and the foreseeable future, are expected to be met by cash flows from operations and if necessary, utilization of its revolving credit facility.

#### **DIVIDENDS**

Management believes that it should retain the capital generated from operating activities for investment in advancing technologies, acquisitions and debt retirement. Accordingly, there are no plans to institute a cash dividend program.

#### **BACKLOG**

At December 31, 2007, the Company's backlog was \$92.4 million compared with \$99.5 million at December 31, 2006.

#### **RELATED-PARTY TRANSACTIONS**

See the discussion in Item 8, Financial Statements and Supplementary Data, Note 12, Discontinued Operations in this report.

#### **RECENT ACCOUNTING PRONOUNCEMENTS**

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This statement establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), clarifies the definition of fair

value within that framework, and expands disclosures about the use of fair value measurement. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is in the process of determining the effect, if any; the adoption of SFAS No. 157 will have on our consolidated financial statements in the first quarter of 2008.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which allows measurement of specified financial instruments, warranty and insurance contracts at fair value on a contract by contract basis, with changes in fair value recognized in earnings in each period. SFAS 159 is effective at the beginning of the fiscal year that begins after November 15, 2007, and will be effective for the Company in fiscal 2008. The Company has not yet determined the effect that the implementation of this standard will have on its consolidated financial position or results of operations in the first quarter of 2008.

In December 2007, the FASB Statement 141R, Business Combinations ( SFAS 141R ) was issued. SFAS 141R replaces SFAS 141. SFAS 141R requires the acquirer of a business to recognize and measure the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree at fair value. SFAS 141R also requires transactions costs related to the business combination to be expensed as incurred. SFAS 141R applies prospectively to business combinations; the effective date for the Company will be January 1, 2009. The Company has not yet determined the impact of SFAS 141R related to future acquisitions, if any, on the Company's consolidated financial statements.

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

The Company has limited exposure to fluctuation in Canadian currency exchange rates to the U.S. dollar. Nearly all of the Company's consolidated sales, expenses and cash flows are transacted in U.S. dollars. Net assets held in or measured in Canadian dollars amounted to \$1.2 million at December 31, 2007. Annual disbursements of approximately \$6.9 million are transacted in Canadian dollars. A 10% change in the value of the U.S. dollar versus the Canadian dollar would impact net income by approximately \$0.5 million.

Risk due to fluctuation in interest rates is a function of the Company's floating rate debt obligations, which total approximately \$22.9 million at December 31, 2007. To offset this exposure, the Company entered into an interest rate swap in February 2006, on its Series 1999 New York Industrial Revenue Bond which effectively fixes the rate at 3.99% on this \$3.6 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.

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

**REPORT OF ERNST & YOUNG LLP, INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Shareholders and Board of Directors of Astronics Corporation:

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

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

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

As discussed in Note 1 to the consolidated financial statements, on January 1, 2006, the Company changed its method of accounting for stock based compensation and on December 31, 2006, the Company changed its method of accounting for defined benefit pension plans and other post retirement benefits.

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

/s/ Ernst & Young LLP

Buffalo, New York  
February 29, 2008



**MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act. Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2007 based upon the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on that evaluation, our management concluded that our internal control over financial reporting is effective as of December 31, 2007.

Ernst & Young LLP, independent registered public accounting firm, has audited our consolidated financial statements included in this Annual Report on Form 10-K and, as part of their audit, has issued their report, included herein, on the effectiveness of our internal control over financial reporting.

By: /s/ Peter J. Gundermann

February 29, 2008

Peter J. Gundermann  
President & Chief Executive Officer  
(Principal Executive Officer)

/s/ David C. Burney

February 29, 2008

David C. Burney  
Vice President-Finance, Chief Financial Officer & Treasurer  
(Principal Financial and Accounting Officer)

**REPORT OF ERNST & YOUNG LLP, INDEPENDENT REGISTERED PUBLIC ACCOUNTING  
FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

The Shareholders and Board of Directors of Astronics Corporation:

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

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

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

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

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

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

/s/ Ernst & Young LLP

Buffalo, New York

February 29, 2008

**ASTRONICS CORPORATION**  
**CONSOLIDATED STATEMENT OF EARNINGS**

|   | <b>Year Ended December 31,</b> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <b>2007</b>                    | <b>2006</b> | <b>2005</b> |
| (In thousands, except per share data)                           |                                |             |             |
| Sales   | \$ 158,240                     | \$ 110,767  | \$ 74,354   |
| Cost of products sold   | 117,370                        | 87,519      | 59,484      |
| Gross Profit  | 40,870                         | 23,248      | 14,870      |
| Selling, general and administrative expenses                    | 16,408                         | 13,582      | 10,246      |
| Interest expense, net of interest income of \$50, \$15 and \$29 | 1,370                          | 896         | 735         |
| Other expense (income)  | 94                             | 11          | (278)       |
| Income Before Income Taxes                                      | 22,998                         | 8,759       | 4,167       |
| Provision for Income Taxes                                      | 7,607                          | 3,023       | 1,930       |
| Net Income  | \$ 15,391                      | \$ 5,736    | \$ 2,237    |
| Basic Earnings per Share  | \$ 1.90                        | \$ 0.72     | \$ 0.28     |
| Diluted Earnings per Share                                      | \$ 1.80                        | \$ 0.69     | \$ 0.28     |

See notes to consolidated financial statements.

**ASTRONICS CORPORATION**  
**CONSOLIDATED BALANCE SHEET**

**December 31,**  
**2007                      2006**

(In thousands, except share and per share data)

**ASSETS**

|  |                   |                  |
|--|-------------------|------------------|
| Current Assets:  |                   |                  |
| Cash and Cash Equivalents  | \$ 2,818          | \$ 222           |
| Accounts Receivable, Net of Allowance for Doubtful Accounts of \$514 in 2007 and \$314 in 2006 | 20,720            | 17,165           |
| Inventories  | 36,920            | 31,570           |
| Prepaid Expenses   | 942               | 853              |
| Prepaid Income Taxes   | 1,040             | 214              |
| Deferred Income Taxes  | 1,581             | 1,632            |
| <b>Total Current Assets</b>  | <b>64,021</b>     | <b>51,656</b>    |
| Property, Plant and Equipment, at Cost:  |                   |                  |
| Land   | 1,636             | 1,143            |
| Buildings and Improvements   | 16,285            | 12,007           |
| Machinery and Equipment  | 25,978            | 20,670           |
| Construction in progress   | 2,179             | 2,701            |
|  | 46,078            | 36,521           |
| Less Accumulated Depreciation and Amortization   | 15,995            | 13,085           |
| Net Property, Plant and Equipment  | 30,083            | 23,436           |
| Deferred Income Taxes  | 991               | 622              |
| Intangibles net of accumulated amortization of \$884 in 2007 and \$637 in 2006                 | 2,088             | 2,335            |
| Restricted Cash  | 1,088             |                  |
| Other Assets   | 2,802             | 1,821            |
| Goodwill   | 3,048             | 2,668            |
| <b>Total Assets</b>  | <b>\$ 104,121</b> | <b>\$ 82,538</b> |

**LIABILITIES AND SHAREHOLDERS EQUITY**

|   |               |               |
|---|---------------|---------------|
| Current Liabilities:                            |               |               |
| Current Maturities of Long-term Debt            | \$ 951        | \$ 923        |
| Note Payable                                    | 7,300         | 8,100         |
| Accounts Payable                                | 7,667         | 12,472        |
| Accrued Payroll and Employee Benefits           | 6,140         | 4,403         |
| Customer Advanced Payments and Deferred Revenue | 7,822         | 6,864         |
| Other Accrued Expenses                          | 2,041         | 1,457         |
| <b>Total Current Liabilities</b>                | <b>31,921</b> | <b>34,219</b> |

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|   |                   |                  |
|---|-------------------|------------------|
| Long-term Debt  | 14,684            | 9,426            |
| Supplemental Retirement Plan and Other Liabilities for Pension Benefits   | 6,808             | 6,190            |
| Other Liabilities   | 1,476             | 1,355            |
| <b>Total Liabilities</b>  | <b>54,889</b>     | <b>51,190</b>    |
| <b>Shareholders Equity</b>  |                   |                  |
| Common Stock, \$.01 par value Authorized 20,000,000 Shares, Issued 7,511,774 in 2007; 7,313,726 in 2006             | 75                | 73               |
| Convertible Class B Stock, \$.01 par value Authorized 5,000,000 Shares, Issued 1,421,240 in 2007; 1,496,006 in 2006 | 14                | 15               |
| Additional Paid-in Capital  | 7,833             | 5,504            |
| Accumulated Other Comprehensive Loss  | (541)             | (704)            |
| Retained Earnings   | 45,570            | 30,179           |
|   | 52,951            | 35,067           |
| Less Treasury Stock: 784,250 Shares in 2007 and 2006  | 3,719             | 3,719            |
| <b>Total Shareholders Equity</b>  | <b>49,232</b>     | <b>31,348</b>    |
| <b>Total Liabilities and Shareholders Equity</b>  | <b>\$ 104,121</b> | <b>\$ 82,538</b> |

See notes to consolidated financial statements.

**ASTRONICS CORPORATION**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**

|   | <b>Year Ended December 31,</b> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <b>2007</b>                    | <b>2006</b> | <b>2005</b> |
| (In thousands)  |                                |             |             |
| <b>Cash Flows from Operating Activities</b>   |                                |             |             |
| Net Income  | \$ 15,391                      | \$ 5,736    | \$ 2,237    |
| Adjustments to Reconcile Net Income to Cash Provided By (Used For)                                  |                                |             |             |
| Operating Activities:   |                                |             |             |
| Depreciation and Amortization   | 3,440                          | 2,929       | 2,373       |
| Provision for Non-Cash Losses on Inventory and Receivables  | 747                            | 138         | 124         |
| Stock Compensation Expense  | 771                            | 619         |             |
| Other   | (185)                          | 26          | (41)        |
| Deferred Tax (Benefit) Provision  | (122)                          | (529)       | 93          |
| Cash Flows from Changes in Operating Assets and Liabilities, Excluding the Effects of Acquisitions: |                                |             |             |
| Accounts Receivable   | (3,399)                        | (4,572)     | (828)       |
| Inventories   | (5,599)                        | (12,298)    | (4,874)     |
| Prepaid Expenses  | (137)                          | (379)       | (67)        |
| Accounts Payable  | (4,895)                        | 7,047       | 677         |
| Accrued Expenses  | 2,273                          | 869         | 2,079       |
| Customer Advanced Payments and Deferred Revenue   | 958                            | 1,462       | 4,722       |
| Contract Loss Reserves  |                                | (830)       | (2,909)     |
| Prepaid Income Taxes  | (815)                          | (385)       | 1,147       |
| Supplemental Retirement Plan and Other Liabilities  | 173                            | 120         | 282         |
| Cash Provided By (Used For) Operating Activities  | 8,601                          | (47)        | 5,015       |
| <b>Cash Flows from Investing Activities</b>   |                                |             |             |
| Capital Expenditures  | (9,592)                        | (5,400)     | (2,498)     |
| Other   | (745)                          | (65)        | (177)       |
| Proceeds from Sale of Short-term Investments  |                                |             | 1,000       |
| Business Acquisition  |                                |             | (13,366)    |
| Cash Used For Investing Activities  | (10,337)                       | (5,465)     | (15,041)    |
| <b>Cash Flows from Financing Activities</b>   |                                |             |             |
| Proceeds from Long Term Debt  | 6,000                          |             |             |
| Principal Payments on Long-term Debt  | (944)                          | (920)       | (897)       |
| Proceeds from Note Payable  | 20,800                         | 10,300      | 7,000       |
| Payments on Note Payable  | (21,600)                       | (9,200)     |             |
| Debt Acquisition Costs  | (392)                          |             |             |
| Unexpended Industrial Revenue Bond Proceeds   | (1,088)                        |             |             |
| Proceeds from Exercise of Stock Options   | 1,162                          | 984         | 343         |
| Income Tax Benefit from Exercise of Stock Options   | 397                            | 94          | 35          |

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|  |                 |               |                 |
|--|-----------------|---------------|-----------------|
| Cash Provided By Financing Activities                      | 4,335           | 1,258         | 6,481           |
| Effect of Exchange Rates on Cash                           | (3)             | 3             | (11)            |
| Cash Provided By (Used For) Continuing Operations          | 2,596           | (4,251)       | (3,556)         |
| Cash Used For Discontinued Operations Operating Activities |                 |               | (447)           |
| Cash and Cash Equivalents at Beginning of Year             | 222             | 4,473         | 8,476           |
| <b>Cash and Cash Equivalents at End of Year</b>            | <b>\$ 2,818</b> | <b>\$ 222</b> | <b>\$ 4,473</b> |
| Disclosure of Cash Payments for:                           |                 |               |                 |
| Interest   | \$ 1,421        | \$ 903        | \$ 764          |
| Income Taxes, net  | 8,159           | 4,001         | 651             |

See notes to consolidated financial statements.



## ASTRONICS CORPORATION

## CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY

|   | Common Stock  |           | Class B Stock |           | Treasury Stock |            | Accumulated Other |                             |                   |                      |
|---|---------------|-----------|---------------|-----------|----------------|------------|-------------------|-----------------------------|-------------------|----------------------|
|   | Shares Issued | Par Value | Shares Issued | Par Value | Shares         | Cost       | Paid-In Capital   | Comprehensive Income (Loss) | Retained Earnings | Comprehensive Income |
| (Dollars and shares in thousands)                                       |               |           |               |           |                |            |                   |                             |                   |                      |
| Balance at January 1, 2005  | 6,634         | \$ 66     | 1,950         | \$ 19     | 784            | \$ (3,719) | \$ 3,432          | \$ 656                      | \$ 22,206         |                      |
| Net Income for 2005   |               |           |               |           |                |            |                   |                             | 2,237             | \$ 2,237             |
| Currency Translation Adjustments  |               |           |               |           |                |            |                   | 83                          |                   | 83                   |
| Mark to Market Adjustments for Derivatives, net of income taxes of \$33 |               |           |               |           |                |            |                   | 60                          |                   | 60                   |
| Total Comprehensive Income  |               |           |               |           |                |            |                   |                             |                   | \$ 2,380             |
| Exercise of Stock Options, including income tax benefit of \$35         | 84            | 1         | 17            | 1         |                |            | 376               |                             |                   |                      |
| Class B Stock converted to Common Stock                                 | 364           | 4         | (364)         | (4)       |                |            |                   |                             |                   |                      |
| Balance at December 31, 2005  | 7,082         | \$ 71     | 1,603         | \$ 16     | 784            | \$ (3,719) | \$ 3,808          | \$ 799                      | \$ 24,443         |                      |
| Net Income for 2006   |               |           |               |           |                |            |                   |                             | 5,736             | \$ 5,736             |
| Currency Translation  |               |           |               |           |                |            |                   | (24)                        |                   | (24)                 |



**Total  
Comprehensive  
Income****Exercise of  
Stock Options  
and Stock  
Compensation  
Expense  
including  
income tax**

|                         |            |          |          |  |              |
|-------------------------|------------|----------|----------|--|--------------|
| <b>benefit of \$397</b> | <b>115</b> | <b>1</b> | <b>8</b> |  | <b>2,329</b> |
|-------------------------|------------|----------|----------|--|--------------|

**Class B Stock  
converted to  
Common Stock**

|  |           |          |             |            |  |
|--|-----------|----------|-------------|------------|--|
|  | <b>83</b> | <b>1</b> | <b>(83)</b> | <b>(1)</b> |  |
|--|-----------|----------|-------------|------------|--|

**Balance at  
December 31,  
2007**

|              |              |              |              |            |                   |                 |                 |                  |
|--------------|--------------|--------------|--------------|------------|-------------------|-----------------|-----------------|------------------|
| <b>7,512</b> | <b>\$ 75</b> | <b>1,421</b> | <b>\$ 14</b> | <b>784</b> | <b>\$ (3,719)</b> | <b>\$ 7,833</b> | <b>\$ (541)</b> | <b>\$ 45,570</b> |
|--------------|--------------|--------------|--------------|------------|-------------------|-----------------|-----------------|------------------|

See notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES AND PRACTICES

#### Description of the Business

Astronics Corporation, through its subsidiaries Luminescent Systems, Inc., Luminescent Systems Canada Inc. and Astronics Advanced Electronic Systems Corp. (AES) designs and manufactures lighting components and subsystems, electrical power generation, in-flight control and power distribution systems for aircraft. The Company serves the three primary markets for aircraft which are the military, commercial transport and the business jet markets.

#### Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany transactions and balances have been eliminated.

Acquisitions are accounted for under the purchase method and, accordingly, the operating results for the acquired companies are included in the consolidated statements of earnings from the respective dates of acquisition.

#### Revenue and Expense Recognition

Revenue is recognized on the accrual basis at the time of shipment of goods and transfer of title. There are no significant contracts allowing for right of return. The Company does evaluate and record an allowance for any potential returns based on experience and any known circumstances. For the years ended December 31, 2007 and 2006, no significant allowances were recorded for contracts allowing for right of return. A trade receivable is recorded at the value of the sale. The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral. The Company records a valuation allowance to account for potentially uncollectible accounts receivable. The allowance is determined based on Management's knowledge of the business, specific customers, review of the receivable's aging and a specific identification of accounts where collection is at risk. At December 31, 2007, the Company's allowance for doubtful accounts for accounts receivable was \$0.5 million, or 2.4% of gross accounts receivable. At December 31, 2006, the Company's allowance for doubtful accounts for accounts receivable was \$0.3 million, or 1.8% of gross accounts receivable. At December 31, 2006, the Company's non-current note receivable in the amount of \$0.6 million remained fully reserved. This note receivable was written off against the reserve in 2007.

Cost of products sold includes the costs to manufacture products such as direct materials and labor and manufacturing overhead as well as all engineering and developmental costs. Shipping and handling costs are expensed as incurred and are included in costs of products sold. Selling, general and administrative expenses include costs primarily related to our sales and marketing departments and administrative departments.

The Company is engaged in a variety of engineering and design activities as well as basic research and development activities directed to the substantial improvement or new application of the Company's existing technologies. These costs are expensed when incurred and included in cost of sales. Research and development, design and related engineering amounted to \$14.8 million in 2007, \$10.9 million in 2006 and \$8.9 million in 2005.

#### Stock-Based Compensation

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's prior years do not reflect

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

any restated amounts. For awards with graded vesting, 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. Prior to the first quarter of 2006 the Company accounted for its stock-based awards using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25 and its related interpretations. The measurement prescribed by APB Opinion No. 25 does not recognize compensation expense if the exercise price of the stock option equals the market price of the underlying stock on the date of grant and the number of stock options granted is fixed. Accordingly, no compensation expense related to stock options has been recorded in the financial statements prior to the first quarter of 2006.

Under SFAS 123(R), 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 vest with graded vesting over a five-year period, 20% each year, from the date of grant.

The following table provides pro forma earnings information as if the Company recorded compensation expense based on the fair value of stock options for the years ended December 31, 2007, 2006 and 2005:

|   | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|---|-------------|-------------|-------------|
| (In thousands, except per share data)                             |             |             |             |
| Net Income, as reported(1)  | \$ N/A      | \$ N/A      | \$ 2,237    |
| Stock compensation expense included in net income as reported     | (771)       | (619)       | (365)       |
| Tax benefit   | 136         | 86          | 63          |
| Stock compensation expense, net of tax(2)                         | \$ 635      | \$ (533)    | \$ (302)    |
| Net Income, including the effect of stock compensation expense(3) | \$ 15,391   | \$ 5,736    | \$ 1,935    |
| Net earnings per share:   |             |             |             |
| Basic, as reported in prior years(1)                              | \$ N/A      | \$ N/A      | \$ .28      |
| Basic, including the effect of stock compensation expense(3)      | 1.90        | .72         | .25         |
| Diluted, as reported in prior years(1)                            | N/A         | N/A         | .28         |
| Diluted, including the effect of stock compensation expense(3)    | 1.80        | .69         | .24         |

(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(R).

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

Consistent with SFAS 123(R), we classified \$0.4 million and \$0.1 million of excess tax benefits from share based payment arrangements as cash flows from financing activities in 2007 and 2006, respectively.

**Cash and Cash Equivalents**

All highly liquid instruments with a maturity of three months or less at the time of purchase are considered cash equivalents. Cash and cash equivalents excludes amounts which are restricted for use for capital expenditures under the series 2007 Industrial Revenue Bonds.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Inventories**

Inventories are stated at the lower of cost or market, cost being determined in accordance with the first-in, first-out method. Inventories at December 31 are as follows:

|                  | <b>2007</b>      | <b>2006</b>      |
|------------------|------------------|------------------|
| (In thousands)   |                  |                  |
| Finished Goods   | \$ 7,226         | \$ 5,575         |
| Work in Progress | 8,553            | 9,651            |
| Raw Material     | 21,141           | 16,344           |
|                  | <b>\$ 36,920</b> | <b>\$ 31,570</b> |

The Company records valuation reserves to provide for slow moving or obsolete inventory or to reduce inventory to the lower of cost or market value. In determining the appropriate reserve, Management considers the age of inventory on hand, the overall inventory levels in relation to forecasted demands as well as reserving for specifically identified inventory that the Company believes is no longer salable. At December 31, 2007, the Company's reserve for inventory valuation was \$4.1 million, or 10.0% of gross inventory. At December 31, 2006, the Company's reserve for inventory valuation was \$4.1 million, or 11.6% of gross inventory.

**Property, Plant and Equipment**

Depreciation of property, plant and equipment is computed on the straight-line method for financial reporting purposes and on accelerated methods for income tax purposes. Estimated useful lives of the assets are as follows: buildings, 40 years; machinery and equipment, 4-10 years. Leasehold improvements are amortized over the terms of the lease or the lives of the assets, whichever is shorter.

The cost of properties sold or otherwise disposed of and the accumulated depreciation thereon are eliminated from the accounts, and the resulting gain or loss, as well as maintenance and repair expenses, are reflected in income. Replacements and improvements are capitalized.

Depreciation expense was \$2.9 million, \$2.4 million and \$1.9 million in 2007, 2006 and 2005, respectively. Interest capitalized relating to the building expansion, in East Aurora, New York amounted to approximately \$0.1 million in 2007. Interest costs capitalized in 2006 and 2005 were insignificant.

**Goodwill and Intangible Assets**

The Company tests goodwill at the reporting unit level on an annual basis or more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The Company has one reporting unit for purposes of the goodwill impairment test. The impairment test consists of comparing the fair value of the reporting unit, determined using discounted cash flows, with its carrying amount including goodwill, and, if the carrying amount of the reporting unit exceeds its fair value, comparing the implied fair value of goodwill with its carrying amount. An impairment loss would be recognized for the carrying



amount of goodwill in excess of its implied fair value.

Intangibles are valued based upon future economic benefits such as discounted earnings and cash flows. Acquired identifiable intangible assets are recorded at cost and are amortized over their estimated useful lives. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of those assets may not be recoverable. Trade name intangibles have an indefinite life and are tested for impairment on an annual basis or more frequently if an event occurs or circumstances change that would more likely than not reduce its fair value below its carrying amount.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### Long-Lived Assets

Long-lived assets to be held and used are initially recorded at cost. The carrying value of these assets is evaluated for recoverability whenever adverse effects or changes in circumstances indicate that the carrying amount may not be recoverable. Impairments are recognized if future undiscounted cash flows and earnings from operations are not expected to be sufficient to recover long-lived assets. The carrying amounts are then reduced by the estimated shortfall of the discounted cash flows.

### Financial Instruments

The Company's financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, notes payable, long-term debt and an interest rate swap. The carrying value of the Company's financial instruments approximate fair value. The Company does not hold or issue financial instruments for trading purposes.

### Derivatives

The Company records all derivatives on the balance sheet at fair value and as long term. The accounting for changes in the fair value of derivatives depends on the intended use and resulting designation. During 2007 and 2006, the Company's use of derivative instruments was limited to a cash flow hedge for interest rate risk. For a derivative designated as a cash flow hedge, the effective portion of the derivative's gain or loss is initially reported as a component of other comprehensive income (OCI) and subsequently reclassified into earnings when the hedged exposure affects earnings. The Company entered into an interest rate swap in February 2006, on its Series 1999 New York Industrial Revenue Bonds which effectively fixes the rate at 3.99% on this obligation through January 2016. This arrangement replaced a swap agreement that expired in December 2005 which effectively fixed the interest rate at 4.09%. The ineffective portions of all derivatives are recognized immediately into earnings as other income or expense. Ineffectiveness was not material in 2007, 2006, and 2005. For a derivative not designated as a hedging instrument, the gain or loss is recognized in earnings in the period of change. The Company classifies the cash flows from hedging transactions in the same category as the cash flows from the respective hedged items. The Company reclassified \$0.01 million; \$0.02 million and \$0.1 million from accumulated other comprehensive income to interest expense during 2007, 2006 and 2005, respectively.

### Income Taxes

The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial reporting and tax basis of assets and liabilities. Deferred tax assets are reduced, if deemed necessary, by a valuation allowance for the amount of tax benefits which are not expected to be realized. Investment tax credits are recognized on the flow through method.

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting and disclosure for uncertainty in tax positions, as defined. FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to accounting for income taxes. The Company is subject to the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company believes that its income tax filing positions and deductions will be sustained on audit. Therefore, no reserves for uncertain income tax positions have been recorded pursuant to FIN 48 and the Company was not required to record a cumulative effect

adjustment related to the adoption of FIN 48.

In the future, should the Company need to accrue a liability for unrecognized tax benefits, any interest associated with that liability will be recorded as interest expense. Penalties, if any, would be recognized as operating expenses. There are no penalties or interest liability accrued as of December 31, 2007. In years previous, any interest and penalties were insignificant and recorded as income tax expense. The years under

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

which we conducted our evaluation coincided with the tax years currently still subject to examination by major federal and state tax jurisdictions, those being 2004, 2005, 2006 and 2007.

Prior to January 1, 2007, the Company recorded accruals for tax contingencies and related interest when it was probable that a liability had been incurred and the amount of the contingency could be reasonably estimated based on specific events such as an audit or inquiry by a taxing authority.

**Earnings per Share**

Earnings per share computations are based upon the following table:

|  | 2007      | 2006     | 2005     |
|--|-----------|----------|----------|
| (In thousands, except per share data)    |           |          |          |
| Net Income                               | \$ 15,391 | \$ 5,736 | \$ 2,237 |
| Basic earnings weighted average shares   | 8,083     | 7,956    | 7,855    |
| Net effect of dilutive stock options     | 486       | 313      | 183      |
| Diluted earnings weighted average shares | 8,569     | 8,269    | 8,038    |
| Basic earnings per share                 | \$ 1.90   | \$ 0.72  | \$ 0.28  |
| Diluted earnings per share               | \$ 1.80   | \$ 0.69  | \$ 0.28  |

**Reserved Common Stock**

At December 31, 2007, approximately 2.8 million shares of common stock were reserved for issuance upon conversion of the Class B stock, exercise of stock options and purchases under the Employee Stock Purchase Plan. Class B Stock is identical to Common Stock, except Class B Stock has ten votes per share, is automatically converted to Common Stock on a one for one basis when sold or transferred, and cannot receive dividends unless an equal or greater amount of dividends is declared on Common Stock.

**Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities and the reported amounts of revenues and expenses during the reporting periods in the financial statements and accompanying notes. Actual results could differ from those estimates.

**Comprehensive Income**

Comprehensive income (loss) consists primarily of net earnings and the after-tax impact of currency translation adjustments, mark to market adjustment for derivatives and retirement liability adjustments. Income taxes related to derivatives and retirement liability adjustments within other comprehensive income are generally recorded based on an effective tax rate of approximately 36%. No income tax effect is recorded for currency translation adjustments.



**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The accumulated balances of the components of other comprehensive (loss) income net of tax, at December 31, 2007 and 2006 are as follows:

|   | 2007     | 2006     |
|---|----------|----------|
| (In millions)                               |          |          |
| Accumulated foreign currency translation    | \$ 1.3   | \$ 0.8   |
| Accumulated loss on derivative adjustment   | (0.1)    |          |
| Accumulated retirement liability adjustment | (1.7)    | (1.5)    |
|   | \$ (0.5) | \$ (0.7) |

**Recent Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This statement establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), clarifies the definition of fair value within that framework, and expands disclosures about the use of fair value measurement. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is in the process of determining the effect, if any; the adoption of SFAS No. 157 will have on our consolidated financial statements in the first quarter of 2008.

In September 2006, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No 87, 88, 106, and 132(R). SFAS No. 158 requires plan sponsors of defined benefit pension and other postretirement benefit plans (collectively, postretirement benefit plans ) to recognize the funded status of their postretirement benefit plans in the statement of financial position, measure the fair value of plan assets and benefit obligations as of the date of the fiscal year-end statement of financial position, and provide additional disclosures. On December 31, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158. The effect of adopting SFAS No. 158 on the Company s financial condition at December 31, 2006 has been included in the accompanying consolidated financial statements. SFAS No. 158 did not have an effect on the Company s consolidated financial condition at December 31, 2005 or 2004. SFAS No. 158 s provisions regarding the change in the measurement date of postretirement benefit plans are not applicable as the Company already uses a measurement date of December 31 for its benefit plans. The Company has adopted the provisions of SFAS No. 158 as of December 31, 2006. See Note 6 for further discussion of the effect of adopting SFAS No. 158 on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which allows measurement of specified financial instruments, warranty and insurance contracts at fair value on a contract by contract basis, with changes in fair value recognized in earnings in each period. SFAS 159 is effective at the beginning of the fiscal year that begins after November 15, 2007, and will be effective for the Company in fiscal 2008. The Company is in the process of determining the effect, if any; the adoption of SFAS No. 159 will have on our consolidated financial statements in the first quarter of 2008.

In December 2007, the FASB Statement 141R, Business Combinations ( SFAS 141R ) was issued. SFAS 141R replaces SFAS 141. SFAS 141R requires the acquirer of a business to recognize and measure the identifiable assets

acquired, the liabilities assumed, and any non-controlling interest in the acquiree at fair value. SFAS 141R also requires transactions costs related to the business combination to be expensed as incurred. SFAS 141R applies prospectively to business combinations; the effective date for the Company will be January 1, 2009. The Company has not yet determined the impact of SFAS 141R related to future acquisitions, if any, on the Company's consolidated financial statements.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 2 LONG-TERM DEBT AND NOTE PAYABLE**

Long-term debt consists of the following:

|  | 2007      | 2006     |
|--|-----------|----------|
| (In thousands)   |           |          |
| Note Payable at Canadian Prime payable \$15 monthly through 2016 plus interest (Canadian prime was 6.0% at December 31, 2007)  | \$ 1,438  | \$ 1,376 |
| Series 1998 Industrial Revenue Bonds issued through the Business Finance Authority of the State of New Hampshire payable \$400 annually through 2018 with interest reset weekly (3.65% at December 31, 2007)               | 4,450     | 4,850    |
| Series 1999 Industrial Revenue Bonds issued through the Erie County, New York Industrial Development Agency payable \$350 annually through 2019 with interest reset weekly (3.55% at December 31, 2007)                    | 3,645     | 3,995    |
| Series 2007 Industrial Revenue Bonds issued through the Erie County, New York Industrial Development Agency payable \$260 in 2010 and \$340 from 2011 through 2027 with interest reset weekly (3.55% at December 31, 2007) | 6,000     |          |
| Other  | 102       | 128      |
|  | 15,635    | 10,349   |
| Less current maturities  | 951       | 923      |
|  | \$ 14,684 | \$ 9,426 |

Principal maturities of long-term debt for each of the next five years are \$1.0 million for 2008 and 2009, \$1.2 million for 2010 and \$1.3 million for 2011 and 2012.

The Company is in compliance with all its debt and credit facility covenants at December 31, 2007 and believes it will continue to be compliant in the future.

The Industrial Revenue Bonds are held by institutional investors and are guaranteed by a bank letter of credit, which is collateralized by certain property, plant and equipment assets, the carrying value of which approximates the principal balance on the bonds.

The Company has a standby unsecured bank letter of credit guaranteeing the note payable in Canada, the carrying value of which approximates the principal balance on the note.

To offset risks due to fluctuation in interest rates, the Company entered into an interest rate swap through December 2005 on the Series 1999 Industrial Revenue Bonds issued through the Erie County, New York Industrial Development Agency payable \$350 annually through 2019, which effectively fixed the interest rate at 4.09%. In February 2006, the Company entered into a new interest rate swap, for this \$3.6 million obligation which effectively fixes the rate at 3.99% on this obligation through January 2016.



On January 5, 2007 the Company entered into a new agreement with HSBC Bank USA which increased its available revolving credit facility to \$20 million. The agreement is a committed two year facility through January 5, 2009, with interest at bank prime minus between 0 and 25 basis points or LIBOR plus between 87.5 and 175 basis points. The Company is also required to pay a commitment fee of between 0.125% and 0.30% on the unused portion of the line limit borrowing availability for the previous quarter. The Company may allocate up to \$0.5 million of its availability for the issuance of new letters of credit. This new credit facility is collateralized by accounts receivable and inventory. On July 25, 2007 the Company amended this borrowing agreement, increasing the revolving credit facility from \$20 million to \$25 million. All other provisions of the January 5th agreement remain in force. The Company believes it will continue to be compliant with all the new credit facility covenants in the future.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

At December 31, 2007 and 2006 the Company had outstanding \$7.3 million and \$8.1 million respectively, on its revolving credit facility. At December 31, 2007 and 2006, the Company had available \$17.7 million and \$6.9 million, respectively, on the facility.

**NOTE 3 STOCK OPTION AND PURCHASE PLANS**

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 schedules.

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 Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options. The weighted average fair value of the options was \$13.98, \$7.58 and \$3.97 for options granted during the year ended December 31, 2007, 2006 and 2005 respectively.

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

|                         | <b>2007</b> | <b>2006</b> | <b>2005</b>  |
|-------------------------|-------------|-------------|--------------|
| Risk-free interest rate | 3.7% - 4.5% | 4.5% - 4.7% | 4.3% - 4.5%  |
| Dividend yield          | 0.0%        | 0.0%        | 0.0%         |
| Volatility factor       | 0.34 - 0.38 | 0.33 - 0.34 | 0.33         |
| Expected life in years  | 7.00 - 8.00 | 7.00 - 8.00 | 7.00 - 10.00 |

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.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

A summary of the Company's stock option activity and related information for the years ended December 31 follows:

|  | <b>2007</b>    |  |  | <b>2006</b>    |  |  | <b>2005</b>    |  |  |
|--|----------------|--|--|----------------|--|--|----------------|--|--|
|  | <b>Options</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> | <b>Options</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> | <b>Options</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
| (Aggregate intrinsic value in thousands) |                |  |  |                |  |  |                |  |  |
| Outstanding at the Beginning of the Year | 818,182        | \$ 7.31  | \$ 28,792                                | 801,583        | \$ 6.49  | \$ 8,529                                 | 724,080        | \$ 5.83  | \$ 3,562                                 |
| Options Granted                          | 52,190         | 29.17  | 696                                      | 78,600         | 16.10  | 81                                       | 165,100        | 8.10   | 438                                      |
| Options Exercised                        | (72,333)       | 6.69   | (2,590)                                  | (62,001)       | 7.80   | (578)                                    | (61,459)       | 2.96   | (479)                                    |
| Options Forfeited                        | (800)          | 5.49   | (30)                                     |                |  |  | (26,138)       | 6.76   | (104)                                    |
| Outstanding at the End of the Year       | 797,239        | 8.80   | \$ 26,868                                | 818,182        | 7.31   | \$ 8,032                                 | 801,583        | 6.49   | \$ 3,417                                 |
| Exercisable at December 31               | 568,669        | \$ 7.24  | \$ 20,049                                | 518,729        | \$ 6.52  | \$ 5,504                                 | 468,967        | \$ 6.28  | \$ 2,096                                 |

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 which would have been received by the option holders had all option holders exercised their options as of that date. The Company's closing stock price of Common Stock was \$42.50, \$17.13 and \$10.75 as of December 31, 2007, 2006 and 2005, respectively.

The fair value of options vested during 2007, 2006 and 2005 was \$4.38, \$3.95 and \$3.24, respectively. At December 31, 2007, total compensation costs related to non-vested awards not yet recognized amounts to \$1.3 million and will be recognized over a weighted average period of 2.4 years.

The following is a summary of weighted average exercise prices and contractual lives for outstanding and exercisable stock options as of December 31, 2007:

| <b>Exercise Price Range</b> | <b>Shares</b> | <b>Outstanding</b>                              | <b>Weighted Average Exercise Price</b> | <b>Exercisable</b>                     |
|-----------------------------|---------------|---|--|--|
|                             |               | <b>Weighted Average Remaining Life in Years</b> |  | <b>Weighted Average Exercise Price</b> |
|                             |               |   |  |  |

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|                 |         |      |    |       |         |    |       |
|-----------------|---------|------|----|-------|---------|----|-------|
| \$4.60          | 28,188  | 0.1  | \$ | 4.60  | 28,188  | \$ | 4.60  |
| \$5.09-\$7.65   | 519,295 | 5.6  |    | 5.62  | 403,817 |    | 5.59  |
| \$9.83-\$13.41  | 145,524 | 6.4  |    | 10.63 | 101,256 |    | 10.98 |
| \$17.36-\$17.60 | 77,042  | 9.0  |    | 17.44 | 35,408  |    | 17.53 |
| \$39.81         | 27,190  | 10.0 |    | 39.81 |         |    |       |
|                 | 797,239 | 6.0  |    | 8.80  | 568,669 |    | 7.24  |

The Company established Incentive Stock Option Plans for the purpose of attracting and retaining executive officers and key employees, and to align management's interest with those of the shareholders. Generally, the options must be exercised within ten years from the grant date and vest ratably over a five-year period. The exercise price for the options is equal to the fair market value at the date of grant. The Company had options outstanding for 610,591 shares under the plan. At December 31, 2007, 434,771 options were available for future grant under the plan established in 2001.

The Company established the Directors Stock Option Plans for the purpose of attracting and retaining the services of experienced and knowledgeable outside directors, and to align their interest with those of the

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

shareholders. The options must be exercised within ten years from the grant date. The exercise price for the option is equal to the fair market value at the date of grant and vests six months from the grant date. At December 31, 2007, the Company had options outstanding for 186,648 shares under the plans. At December 31, 2007, there were 155,602 options available for future grants under the plan established in 2005.

In addition to the options discussed above, the Company has established the Employee Stock Purchase Plan to encourage employees to invest in Astronics Corporation. The plan provides employees that have been with the Company for at least a year the opportunity to invest up to 20% of their cash compensation (up to an annual maximum of approximately \$21,000) in Astronics common stock at a price equal to 85% of the fair market value of the Astronics common stock, determined each October 1. Employees are allowed to enroll annually. Employees indicate the number of shares they wish to obtain through the program and their intention to pay for the shares through payroll deductions over the annual cycle of October 1 through September 30. Employees can withdraw anytime during the annual cycle, and all money withheld from the employees pay is returned with interest. If an employee remains enrolled in the program, enough money will have been withheld from the employees pay during the year to pay for all the shares that the employee opted for under the program. At December 31, 2007, employees had subscribed to purchase 27,039 shares at \$37.38 per share on September 30, 2008. The weighted average fair value of the options was \$11.39, \$3.79 and \$2.25 for options granted during the year ended December 31, 2007, 2006 and 2005 respectively.

The fair value for the options granted under the Employee Stock Purchase plan was estimated at the date of grant using a Black- Scholes option pricing model with the following weighted-average assumptions:

|                         | 2007  | 2006  | 2005  |
|-------------------------|-------|-------|-------|
| Risk-free interest rate | 3.20% | 4.90% | 4.40% |
| Dividend yield          | 0.0%  | 0.0%  | 0.0%  |
| Volatility factor       | .380  | .343  | .332  |
| Expected life in years  | 1.00  | 1.00  | 1.00  |

**NOTE 4 INCOME TAXES**

Pretax income (losses) from the Company's foreign subsidiary amounted to \$1.2 million, \$(0.1) million and \$(0.5) million for 2007, 2006 and 2005 respectively. The balances of pretax earnings for each of those years were domestic.

The provision (benefit) for income taxes for continuing operations consists of the following:

|                | 2007     | 2006     | 2005     |
|----------------|----------|----------|----------|
| (In thousands) |          |          |          |
| Current        |          |          |          |
| US Federal     | \$ 7,495 | \$ 3,563 | \$ 1,817 |
| Foreign        | 141      | (123)    | (109)    |
| State          | 93       | 112      | 129      |

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|          |          |          |          |
|----------|----------|----------|----------|
| Deferred | (122)    | (529)    | 93       |
|          | \$ 7,607 | \$ 3,023 | \$ 1,930 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The effective tax rates differ from the statutory federal income tax as follows:

|   | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|---|-------------|-------------|-------------|
| Statutory Federal Income Tax Rate                   | 35.0%       | 34.0%       | 34.0%       |
| Permanent Items, Net                                | (1.0)%      | 0.5%        | (0.9)%      |
| Foreign Taxes (benefits)                            | (1.2)%      |             | 2.8%        |
| State Income Tax, Net of Federal Income Tax Benefit | 0.4%        | 1.0%        | 9.4%        |
| Other   | (0.1)%      | (1.0)%      | 1.0%        |
|   | 33.1%       | 34.5%       | 46.3%       |

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Significant components of the Company's deferred tax assets and liabilities as of December 31, 2007 and 2006 are as follows:

|   | <b>2007</b> | <b>2006</b> |
|---|-------------|-------------|
| (In thousands)  |             |             |
| Deferred tax assets:  |             |             |
| Deferred compensation   | \$ 3,456    | \$ 3,085    |
| Asset reserves  | 1,300       | 993         |
| State and Foreign tax credit carryforwards, net of federal benefit  | 769         | 340         |
| Customer Advanced Payments and Deferred Revenue   | 557         | 639         |
| Reserves and obligations related to discontinued operation  | 67          | 65          |
| Other   | 239         | 165         |
| Total gross deferred tax assets   | 6,388       | 5,287       |
| Valuation allowance for deferred tax assets related to state and foreign tax credit carryforwards, net of federal benefit | (769)       | (313)       |
| Deferred tax assets   | 5,619       | 4,974       |
| Deferred tax liabilities:   |             |             |
| Depreciation  | 2,595       | 2,228       |
| Intangibles   | 452         | 492         |
| Deferred tax liabilities  | 3,047       | 2,720       |
| Net deferred tax asset  | \$ 2,572    | \$ 2,254    |



The net deferred tax assets and liabilities are presented in the consolidated balance sheet as follows at December 31, 2007 and 2006:

|                                 | <b>2007</b> | <b>2006</b> |
|---------------------------------|-------------|-------------|
| (In thousands)                  |             |             |
| Deferred tax asset    current   | \$ 1,581    | \$ 1,632    |
| Deferred tax asset    long-term | 991         | 622         |
| Net deferred tax asset          | \$ 2,572    | \$ 2,254    |

In the fourth quarter of 2007, the Company recorded an increase of \$0.6 million in its valuation allowance, reducing the Company's deferred tax asset relating to state and foreign tax credit carryforwards to \$0.0 million. As a result, the Company recorded a non-cash charge to income tax expense of \$0.5 million net

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

of the federal tax benefit. In the second quarter of 2005, the Company recorded a valuation allowance of \$0.5 million relating to state investment tax credits. As a result of this valuation allowance, the Company recorded a non-cash charge to income tax expense of \$0.3 million net of the federal tax benefit.

**NOTE 5 PROFIT SHARING/401(K) PLAN**

The Company has a qualified Profit Sharing/401(k) Plan for the benefit of its eligible full-time employees. The Profit Sharing/401(k) Plan provides for annual contributions based on percentages of pretax income. In addition, employees may contribute a portion of their salary to the 401(k) plan which is partially matched by the Company. The plan may be amended or terminated at any time. Total charges to income from continuing operations for the plan were \$1.9 million, \$1.4 million and \$1.0 million in 2007, 2006 and 2005, respectively.

**NOTE 6 SUPPLEMENTAL RETIREMENT PLAN AND RELATED POST RETIREMENT BENEFITS**

On December 31, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158. SFAS No. 158 requires the Company to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of its pension plan in its balance sheet, with a corresponding adjustment to accumulated other comprehensive income, net of tax. The adjustment to accumulated other comprehensive income at adoption represented the net unrecognized actuarial losses, unrecognized prior service costs, and unrecognized transition obligation remaining from the initial adoption of SFAS No. 87, all of which were previously netted against the plan's funded status in the Company's balance sheet pursuant to the provisions of SFAS No. 87. These amounts will be subsequently recognized as net periodic pension cost pursuant to the Company's historical accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic pension cost in the same periods will be recognized a component of other comprehensive income. Those amounts will be subsequently recognized as a component of net periodic pension cost on the same basis as the amounts recognized in accumulated other comprehensive income at adoption of SFAS No. 158. SFAS No. 158's provisions regarding the change in the measurement date of postretirement benefit plans are not applicable as the Company has historically used a measurement date of December 31 for all benefit plans.

The incremental effects of adopting the provisions of SFAS No. 158 on the Company's statement of financial position at December 31, 2006 are presented in the following table. The adoption of SFAS No. 158 had no effect on the Company's consolidated statement of earnings or earnings per share for the year ended December 31, 2006, or for any prior period presented, and it will not effect the Company's operating results in future periods. Had the Company not been required to adopt SFAS No. 158 at December 31, 2006, it would have recognized an additional minimum liability pursuant to the provisions of SFAS No. 87. The effect of recognizing the additional minimum liability is included in table below in the column labeled Prior to Application of Statement 158.

|                  | <b>At December 31, 2006</b>                    |   | <b>As Reported at</b>        |
|------------------|--|---|------------------------------|
|                  | <b>Prior to<br/>Adopting<br/>Statement 158</b> | <b>Effect of<br/>Adopting<br/>Statement 158</b> | <b>December 31,<br/>2006</b> |
| (In thousands)   |  |   |                              |
| Intangible Asset | \$ 757   | \$ (757)  | \$                           |

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|  |           |         |         |         |
|--|-----------|---------|---------|---------|
| Supplemental Retirement Plan Liabilities | Current   | (391)   |         | (391)   |
| Supplemental Retirement Plan Liabilities | Long-Term | (4,657) | (1,533) | (6,190) |
| Deferred Income Tax Assets               | Current   | 133     |         | 133     |
| Deferred Income Tax Assets               | Long-term | 1,403   | 859     | 2,262   |
| Accumulated Other Comprehensive Loss     |           |         | 1,431   | 1,431   |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Unrecognized prior service costs of \$1.3 million (\$0.8 million net of tax) and unrecognized actuarial losses \$1.4 million (\$0.9 million net of tax) are included in accumulated other comprehensive income at December 31, 2007 and have not yet been recognized in net periodic pension cost. The prior service cost, and actuarial loss included in accumulated other comprehensive income and expected to be recognized in net periodic pension cost during the fiscal year-ended December 31, 2008 is \$0.1 million (\$0.1 million net of tax), \$0.03 million (\$0.02 million net of tax), respectively.

The Company has a nonqualified supplemental retirement defined benefit plan (the Plan) for certain current and retired executives. The Plan provides for benefits based upon average annual compensation and years of service, less offsets for Social Security and Profit Sharing benefits. It is the Company's intent to fund the benefits as they become payable.

The reconciliation of the beginning and ending balances of the projected benefit obligation and the fair value of plans assets for the year ended December 31, 2007 and 2006 and the accumulated benefit obligation at December 31, 2007 and 2006 is as follows:

|   | <b>December 31,<br/>2007</b> | <b>December 31,<br/>2006</b> |
|---|------------------------------|------------------------------|
| (In thousands)  |                              |                              |
| <b>Funded Status</b>                                  |                              |                              |
| Projected Benefit Obligation                          |                              |                              |
| Beginning of Year January 1                           | \$ 5,761                     | \$ 5,794                     |
| Service Cost  | 38                           | 35                           |
| Interest Cost   | 321                          | 309                          |
| Actuarial Loss (Gain)                                 | 570                          | (30)                         |
| Benefits Paid   | (347)                        | (347)                        |
| End of Year December 31                               | \$ 6,343                     | \$ 5,761                     |
| Fair Value of Plan Assets End of Year December 31     | \$                           | \$                           |
| Accumulated Benefit Obligation Recognized December 31 | \$ 6,343                     | \$ 5,761                     |

The assumptions used to calculate the benefit obligation as of December 31, 2007 and 2006 are as follows:

|                                       | <b>2007</b> | <b>2006</b> |
|---------------------------------------|-------------|-------------|
| Discount Rate                         | 5.75%       | 5.75%       |
| Future Average Compensation Increases | 5.00%       | 5.00%       |

The unfunded status of the plan of \$6.3 million at December 31, 2007 is recognized in the accompanying statement of financial position as a current accrued pension liability of \$0.3 million and a long-term accrued pension liability of

\$6.0 million. This also is the expected Company contribution to the plan, as it is unfunded.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table summarizes the components of the net periodic cost for the years ended December 31, 2007, 2006 and 2005:

|  | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|--|-------------|-------------|-------------|
| (In thousands)                             |             |             |             |
| Net Periodic Cost                          |             |             |             |
| Service Cost Benefits Earned During Period | \$ 38       | \$ 35       | \$ 25       |
| Interest Cost                              | 321         | 309         | 307         |
| Amortization of Prior Service Cost         | 109         | 109         | 109         |
| Amortization of Losses                     | 4           | 5           |             |
| Net Periodic Cost                          | \$ 472      | \$ 458      | \$ 441      |

The assumptions used to determine the net periodic cost are as follows:

|                                       | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|---------------------------------------|-------------|-------------|-------------|
| Discount Rate                         | 5.75%       | 5.50%       | 5.75%       |
| Future Average Compensation Increases | 5.00%       | 5.00%       | 5.00%       |

The Company expects the benefits to be paid in each of the next five years to be \$0.3 million and \$1.7 million in the aggregate for the next five years after that. This also is the expected Company contribution to the plan, since the plan is unfunded.

Participants in the nonqualified supplemental retirement plan are entitled to paid medical, dental and long-term care insurance benefits upon retirement under the plan. The measurement date for determining the plan obligation and cost is December 31. The reconciliation of the beginning and ending balances of the projected benefit obligation and the fair value of plans assets for the year ended December 31, 2007 and the accumulated benefit obligation at December 31, 2007 is as follows:

|                              | <b>December 31,<br/>2007</b> | <b>December 31,<br/>2006</b> |
|------------------------------|------------------------------|------------------------------|
| (In thousands)               |                              |                              |
| Funded Status                |                              |                              |
| Projected Benefit Obligation |                              |                              |
| Beginning of Year January 1  | \$ 820                       | \$ 856                       |
| Service Cost                 | 6                            | 6                            |
| Interest Cost                | 46                           | 46                           |
| Actuarial Loss (Gain)        | 34                           | (46)                         |
| Benefits Paid                | (47)                         | (42)                         |

|   |             |    |     |    |     |
|---|-------------|----|-----|----|-----|
| End of Year                               | December 31 | \$ | 859 | \$ | 820 |
| Fair Value of Plan Assets                 |             |    |     |    |     |
| End of Year                               | December 31 | \$ |     | \$ |     |
| Accumulated Benefit Obligation Recognized | December 31 | \$ | 859 | \$ | 820 |

The assumptions used to calculate the post retirement benefit obligation as of December 31, 2007 and 2006 are as follows:

|               | <b>2007</b> | <b>2006</b> |
|---------------|-------------|-------------|
| Discount Rate | 5.75%       | 5.75%       |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table summarizes the components of the net periodic cost for the years ended December 31, 2007, 2006 and 2005:

|  | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|--|-------------|-------------|-------------|
| (In thousands)                             |             |             |             |
| Net Periodic Cost                          |             |             |             |
| Service Cost Benefits Earned During Period | \$ 6        | \$ 6        | \$ 5        |
| Interest Cost                              | 46          | 46          | 40          |
| Amortization of Prior Service Cost         | 34          | 34          | 37          |
| Amortization of Losses                     | 7           | 7           |             |
| Net Periodic Cost                          | \$ 93       | \$ 93       | \$ 82       |

The assumptions used to determine the net periodic cost are as follows:

|   | <b>2007</b> | <b>2006</b> | <b>2005</b> |
|---|-------------|-------------|-------------|
| Discount Rate                               | 5.75%       | 5.50%       | 5.75%       |
| Future Average Healthcare Benefit Increases | 12.00%      | 12.00%      | 12.00%      |

The Company estimates that \$0.03 million of prior Service Costs and \$0.01 million of net losses in accumulated other comprehensive income for medical, dental and long-term care insurance benefits as of December 31, 2007 will be recognized as components of net periodic benefit cost during the year ended December 31, 2008 for the Plan. For measurement purposes, a 12% annual increase in the cost of health care benefits was assumed for 2007 and 2006 respectively, gradually decreasing to 5.0% in 2014 and years thereafter. A one percentage point increase in this rate would increase the post retirement benefit obligation by approximately \$0.1 million, and a one percentage point decrease in this rate would decrease the post retirement benefit obligation by approximately \$0.1 million. The Company expects the benefits to be paid in each of the next five years to be \$0.05 million and \$0.3 million in the aggregate for the next five years after that. This also is the expected Company contribution to the plan, as it is unfunded.

**NOTE 7 SELECTED QUARTERLY FINANCIAL INFORMATION**

The following table summarizes selected quarterly financial information for 2007 and 2006:

| <b>Quarter Ended</b> |                  |                 |                  |                 |                  |                |                 |
|----------------------|------------------|-----------------|------------------|-----------------|------------------|----------------|-----------------|
| <b>Dec. 31,</b>      | <b>Sept. 29,</b> | <b>June 30,</b> | <b>March 31,</b> | <b>Dec. 31,</b> | <b>Sept. 30,</b> | <b>July 1,</b> | <b>April 1,</b> |
| <b>2007</b>          | <b>2007</b>      | <b>2007</b>     | <b>2007</b>      | <b>2006</b>     | <b>2006</b>      | <b>2006</b>    | <b>2006</b>     |

(Unaudited)



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(In thousands,  
except for per  
share data)

|  |           |           |           |           |           |           |           |           |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Sales  | \$ 36,273 | \$ 37,724 | \$ 41,368 | \$ 42,875 | \$ 28,920 | \$ 27,752 | \$ 28,832 | \$ 25,263 |
| Gross Profit<br>(sales less cost<br>of products<br>sold) | 7,643     | 10,142    | 11,435    | 11,650    | 4,951     | 6,119     | 6,766     | 5,412     |
| Income before<br>Tax                                     | 3,389     | 5,869     | 6,654     | 7,086     | 1,004     | 2,423     | 3,126     | 2,206     |
| Net Income   | 2,069     | 4,126     | 4,501     | 4,695     | 807       | 1,648     | 1,963     | 1,318     |
| Basic Earnings<br>per Share                              | 0.25      | 0.51      | 0.56      | 0.58      | 0.10      | 0.21      | 0.25      | 0.17      |
| Diluted<br>Earnings per<br>Share                         | 0.24      | 0.48      | 0.53      | 0.56      | 0.10      | 0.20      | 0.24      | 0.16      |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 8 SALES BY GEOGRAPHIC REGION, MAJOR CUSTOMERS AND CANADIAN OPERATIONS**

The following table summarizes the Company's sales by geographic region:

|                | <b>2007</b>       | <b>2006</b>       | <b>2005</b>      |
|----------------|-------------------|-------------------|------------------|
| (In thousands) |                   |                   |                  |
| North America  | \$ 128,563        | \$ 89,089         | \$ 50,579        |
| Asia           | 12,802            | 7,309             | 11,090           |
| Europe         | 15,891            | 13,650            | 10,857           |
| South America  | 632               | 469               | 863              |
| Other          | 352               | 250               | 965              |
|                | <b>\$ 158,240</b> | <b>\$ 110,767</b> | <b>\$ 74,354</b> |

Sales recorded by the Company's Canadian operations were \$11.2 million in 2007, \$8.6 million in 2006 and \$7.6 million in 2005. Net income (loss) from this operation was \$1.1 million in 2007, \$(0.1) million in 2006 and \$(0.4) million in 2005. Net Assets held outside of the United States total \$2.2 million at December 31, 2007 and \$0.5 million at December 31, 2006. The exchange gain (loss) included in determining net income for the years ended December 31, 2007, 2006 and 2005 was \$0.0 million, \$0.0 million and \$0.1 million, respectively. Cumulative translation adjustments amounted to \$1.3 million, \$0.8 million and \$0.8 million at December 31, 2007, 2006 and 2005 respectively.

The Company has a significant concentration of business with one major customer and the U.S. Government. Sales to Panasonic Avionics accounted for 27.7% of sales in 2007, 21.2% of sales in 2006 and 2.1% of sales in 2005. Accounts receivable from this customer at December 31, 2007 and 2006 were \$4.0 million and \$1.9 million, respectively. Sales to the U.S. Government accounted for 4.0% of sales in 2007, 6.5% of sales in 2006 and 10.8% of sales in 2005. Accounts receivable from the U.S. Government at December 31, 2007 and 2006 were \$0.6 million and \$0.6 million, respectively.

**NOTE 9 COMMITMENTS AND CONTINGENCIES**

The Company leases certain office and manufacturing facilities as well as equipment under various lease contracts with terms that meet the accounting definition of operating leases. These arrangements may include fair market renewal or purchase options. Rental expense for the years ended December 31, 2007, 2006 and 2005 was \$1.8 million, \$1.7 million and \$2.1 million, respectively. The following table represents future minimum lease payment commitments as of December 31, 2007:

|                        | <b>2008</b> | <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012</b> |
|------------------------|-------------|-------------|-------------|-------------|-------------|
| (In thousands)         |             |             |             |             |             |
| Minimum Lease Payments | \$ 635      | \$ 221      | \$ 8        | \$          | \$          |

From time to time the Company may enter into purchase agreements with suppliers under which there is a commitment to buy a minimum amount of product. Purchase commitments outstanding at December 31, 2007 were \$21.5 million. These commitments are not reflected as liabilities in the Company's Balance Sheet. The Company leases its operating facility in Redmond Washington. The lease is scheduled to expire in March of 2008, the Company expects the lease to be extended for up to five years per the lease agreement and is currently negotiating the terms of the extension.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 10 GOODWILL AND INTANGIBLE ASSETS**

The following table summarizes the changes in the carrying amount of goodwill for 2007 and 2006:

|                               | <b>2007</b> | <b>2006</b> |
|-------------------------------|-------------|-------------|
| (In thousands)                |             |             |
| Balance at January 1,         | \$ 2,668    | \$ 2,686    |
| Foreign currency translations | 380         | (18)        |
| Balance at December 31,       | \$ 3,048    | \$ 2,668    |

The following table summarizes acquired intangible assets as follows:

|                                     | <b>Weighted<br/>Average<br/>Life</b> | <b>December 31, 2007</b>             |                                     | <b>December 31, 2006</b>             |                                     |
|-------------------------------------|--------------------------------------|--------------------------------------|-------------------------------------|--------------------------------------|-------------------------------------|
|                                     |                                      | <b>Gross<br/>Carrying<br/>Amount</b> | <b>Accumulated<br/>Amortization</b> | <b>Gross<br/>Carrying<br/>Amount</b> | <b>Accumulated<br/>Amortization</b> |
| (In thousands)                      |                                      |                                      |                                     |                                      |                                     |
| Patents                             | 12 Years                             | \$ 1,271                             | \$ 289                              | \$ 1,271                             | \$ 190                              |
| Trade Names                         | N/A                                  | 553                                  |                                     | 553                                  |                                     |
| Completed and Unpatented Technology | 10 Years                             | 487                                  | 142                                 | 487                                  | 93                                  |
| Government Contracts                | 6 Years                              | 347                                  | 168                                 | 347                                  | 111                                 |
| Backlog                             | 4 Years                              | 314                                  | 285                                 | 314                                  | 243                                 |
| Total Intangible Assets             |                                      | \$ 2,972                             | \$ 884                              | \$ 2,972                             | \$ 637                              |

Amortization is computed on the straight-line method for financial reporting purposes. Amortization expense was \$0.2 million, \$0.3 million and \$0.3 million for 2007, 2006 and 2005 respectively. Amortization expense for each of the next five years will amount to approximately \$0.2 million for each of the years ended December 31, 2008, 2009, 2010, 2011 and \$0.1 million for 2012.

**NOTE 11 WARRANTY**

In the ordinary course of business, the Company warrants its products against defects in design, materials and workmanship typically over periods ranging from twelve to sixty months. The Company determines warranty reserves needed by product line based on experience and current facts and circumstances. Activity in the warranty accrual is summarized as follows:

|                              | 2007     | 2006   | 2005   |
|------------------------------|----------|--------|--------|
| (In thousands)               |          |        |        |
| Balance at beginning of year | \$ 823   | \$ 338 | \$ 82  |
| Increase due to acquisitions |          |        | 200    |
| Warranties issued            | 751      | 492    | 103    |
| Warranties settled           | (410)    | (7)    | (47)   |
| Balance at end of year       | \$ 1,164 | \$ 823 | \$ 338 |

**NOTE 12 DISCONTINUED OPERATIONS**

In December 2002, Astronics announced the discontinuance of the Electroluminescent Lamp Business Group, whose primary business has involved sales of microencapsulated EL lamps to customers in the consumer electronics industry. All liabilities relating to this discontinued operation have been settled by December 31, 2005. These liabilities consisted of minimum lease payments under operating leases.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**NOTE 13 BUSINESS COMBINATIONS**

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 acquired the business for \$13.0 million in cash. The Company financed the acquisition and related costs by borrowing \$7.0 million on its revolving line of credit and used \$6.4 million of cash on hand. For the year ended December 31, 2005, AES had sales of \$27.6 million and a pre-tax profit of \$2.4 million.

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

Not applicable.

**ITEM 9A. CONTROLS AND PROCEDURES**

Disclosure Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of Company Management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures are effective as of the end of the period covered by this report, to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is made known to them on a timely basis, and that these disclosure controls and procedures are effective to ensure such information is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms.

Management's Report on Internal Control over Financial Reporting

See the report appearing under item 8, Financial Statements and Supplemental Data on page 20 of this report.

Changes in Internal Control over Financial Reporting

There have been no changes in the Company's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION**

Not applicable.

**PART III****ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

The information regarding directors is contained under the captions Election of Directors and Security Ownership of Certain Beneficial Owners and Management is incorporated herein by reference to the 2008 Proxy.

The executive officers of the Company, their ages, their positions and offices with the Company, and the date each assumed their office with the Company, are as follows:

| <b>Name and Age<br/>of Executive Officer</b> | <b>Positions and Offices with Astronics</b>   | <b>Year First<br/>Elected<br/>Officer</b> |
|--|---|---|
| Peter J. Gundermann<br>Age 45                | President, Chief Executive Officer and Director of the Company                          | 2001                                      |
| David C. Burney<br>Age 45                    | Vice President-Finance, Treasurer, Secretary and Chief Financial Officer of the Company | 2003                                      |

The principal occupation and employment for all executives listed above for the past five years has been with the Company.

The Company has adopted a Code of Business Conduct and Ethics that applies to the Chief Executive Officer, Chief Financial Officer as well as other directors, officers and employees of the Company. This Code of Business Conduct and Ethics is available upon request without charge by contacting Astronics Corporation, Investor Relations at (716) 805-1599. The Code of Business Conduct and Ethics is also available on the Investor Relations section of the Company's website at [www.astronics.com](http://www.astronics.com).

**ITEM 11. EXECUTIVE COMPENSATION**

The information contained under the caption Executive Compensation and Summary Compensation Table in the Company's definitive Proxy Statement to be filed within 120 days of the end of our fiscal year is incorporated herein by reference.

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

The information contained under the captions Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters and Executive Compensation in the Company's definitive Proxy Statement to be filed within 120 days of the end of our fiscal year is incorporated herein by reference.

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

The information contained under the captions Certain Relationships and Related Party Transactions and Director Independence and Proposal One: Election of Directors Board Independence in the Company's definitive Proxy Statement to be filed within 120 days of the end of our fiscal year is incorporated herein by reference.



**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information contained under the caption "Audit and Non-Audit Fees" in the Company's definitive Proxy Statement to be filed within 120 days of the end of our fiscal year is incorporated herein by reference.

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a) The documents filed as a part of this report are as follows:

1. The following financial statements are included:

- (i) Consolidated Statement of Earnings for the years ended December 31, 2007, December 31, 2006 and December 31, 2005
- (ii) Consolidated Balance Sheet as of December 31, 2007 and December 31, 2006
- (iii) Consolidated Statement of Cash Flows for the years ended December 31, 2007, December 31, 2006 and December 31, 2005
- (iv) Consolidated Statement of Shareholders' Equity for the years ended December 31, 2007, December 31, 2006 and December 31, 2005
- (v) Notes to Consolidated Financial Statements
- (vi) Reports of Ernst & Young LLP, Independent Registered Public Accounting Firm
- (vii) Management's Report on Internal Control Over Financial Reporting

2. Financial Statement Schedules

Schedule II. Valuation and Qualifying Accounts

All other consolidated financial statement schedules are omitted because they are inapplicable, not required, or the information is included elsewhere in the consolidated financial statements or the notes thereto.

3. Exhibits

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 3(a)               | Restated Certificate of Incorporation, as amended; incorporated by reference to exhibit 3(a) of the Registrant's December 31, 1988 Annual Report on Form 10-K.                                 |
| (b)                | By-Laws, as amended; incorporated by reference to exhibit 3(b) of the Registrant's December 31, 1996 Annual Report on Form 10-K.   |
| 4.1(a)             | Unsecured \$8,000,000 Credit Agreement with HSBC Bank USA, dated February 20, 2003; incorporated by reference to Exhibit 4.1 to the Registrant's December 31, 2002 Annual Report on Form 10-K. |
| (b)                | Amendment numbers 1 and 3 dated March 18, 2005 incorporated by reference to Exhibit 4.1 to the registrant's December 31, 2005 Annual Report on Form 10-K.                                      |
| (c)                | Amendment numbers 2 and 4 dated March 31, 2005 incorporated by reference to Exhibit 4.1 to the registrant's December 31, 2005 Annual Report on Form 10-K.                                      |
| (d)                | Line of credit note dated March 31, 2005 filed herewith incorporated by reference to Exhibit 4.1 to the registrant's December 31, 2005 Annual Report on Form 10-K.                             |
| (e)                | Amendment number 5 dated December 22, 2005 incorporated by reference to Exhibit 4.1 to the registrant's December 31, 2005 Annual Report on Form 10-K.  |
| (f)                | Secured \$20,000,000 Credit Agreement with HSBC Bank USA, dated January 5, 2007 incorporated by reference to the registrant's Form 8-K, Exhibit 10.1, filed January 9, 2007.                   |

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- (g) Amended \$20,000,000 Credit Agreement with HSBC Bank USA, dated January 5, 2007 on July 15, 2007, increasing the revolving credit limit to \$25,000,000 2007 incorporated by reference to the registrant's Form 8-K, Exhibit 10.1, filed July 26, 2007.
- 10.1\* Restated Thrift and Profit Sharing Retirement Plan; incorporated by reference to exhibit 10.1 of the Registrant's December 31, 1994 Annual Report on Form 10-KSB.
- 10.2\* Incentive Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 26, 1982.
- 10.3\* Director Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 16, 1984.

| Exhibit No. | Description   |
|-------------|---|
| 10.4*       | 1992 Incentive Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 30, 1992.  |
| 10.5*       | 1993 Director Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 19, 1993.   |
| 10.6*       | 1997 Director Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 14, 1997.   |
| 10.7*       | 2001 Stock Option Plan; incorporated by reference to the Registrant's definitive proxy statement dated March 19, 2001.  |
| 10.8*       | Non-Qualified Supplemental Retirement Plan; incorporated by reference from the Registrant's 1999 Annual Report on Form 10-K.  |
| 10.10       | Tax Sharing Agreement Dated December 7, 2002 by and between MOD-PAC CORP. and the Registrant; Incorporated by reference to exhibit 10.1 of MOD-PAC CORP.'s Form 10/A registration statement dated January 28, 2003.   |
| 10.12*      | Employment Termination Benefits Agreement Dated December 16, 2003 between Astronics Corporation and Peter J. Gundermann, President and Chief Executive Officer of Astronics Corporation ; incorporated by reference from the Registrant's 2003 Annual Report on Form 10-K.  |
| 10.13*      | Employment Termination Benefits Agreement Dated December 16, 2003 between Astronics Corporation and David C. Burney, Vice President and Chief Financial Officer of Astronics Corporation ; incorporated by reference from the Registrant's 2003 Annual Report on Form 10-K. |
| 10.14       | Asset Purchase Agreement Dated February 3, 2005 between General Dynamics OTS (Aerospace), Inc. and Astronics Acquisition Corp. incorporated by reference to Exhibit 10.14 to the Registrant's 2004 Annual Report on Form 10-K.  |
| 10.15*      | 2005 Director Stock Option Plan incorporated by reference to Exhibit 10.15 to the Registrant's 2004 Annual Report on Form 10-K.   |
| 21          | Subsidiaries of the Registrant; filed herewith.   |
| 23          | Consent of Independent Registered Public Accounting Firm; filed herewith.   |
| 31.1        | Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) as adopted pursuant to Section 302 of the Sarbanes- Oxley Act of 2002; filed herewith.   |
| 31.2        | Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a) as adopted pursuant to Section 302 of the Sarbanes- Oxley Act of 2002; filed herewith.   |
| 32          | Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002; furnished herewith.  |

\* identifies a management contract or compensatory plan or arrangement as required by Item 15(a)(3) of Form 10-K.

**SCHEDULE II****Valuation and Qualifying Accounts**

| <b>Year</b><br>(In thousands) | <b>Description</b>               | <b>Balance at<br/>the<br/>Beginning<br/>of<br/>Period</b> | <b>Acquisitions</b> | <b>Charged<br/>to<br/>Cost and<br/>Expense</b> | <b>(Write-Offs)<br/>Recoveries</b> | <b>Balance<br/>at<br/>End of<br/>Period</b> |
|-------------------------------|----------------------------------|---|---------------------|--|------------------------------------|---|
| 2007                          | Allowance for Doubtful Accounts  | \$ 314  | \$                  | \$ 230   | \$ (30)                            | \$ 514                                      |
|                               | Reserve for Inventory Valuation  | 4,134   |                     | 517  | (569)                              | 4,082                                       |
|                               | Allowance for Notes Receivable   | 590   |                     |  | (590)                              |   |
|                               | Deferred Tax Valuation Allowance | 313   |                     | 456  |                                    | 769   |
|                               | Warranty                         | 823   |                     | 751  | (410)                              | 1,164                                       |
| 2006                          | Allowance for Doubtful Accounts  | 365   |                     | 17   | (68)                               | 314   |
|                               | Reserve for Inventory Valuation  | 4,771   |                     | 121  | (758)                              | 4,134                                       |
|                               | Allowance for Notes Receivable   | 590   |                     |  |                                    | 590   |
|                               | Deferred Tax Valuation Allowance | 297   |                     | 16   |                                    | 313   |
|                               | Program Loss Reserves            | 830   |                     |  | (830)                              |   |
|                               | Warranty                         | 338   |                     | 492  | (7)                                | 823   |
| 2005                          | Allowance for Doubtful Accounts  | 259   | 100                 | 124  | (118)                              | 365   |
|                               | Reserve for Inventory Valuation  | 684   | 3,972               | 140  | (25)                               | 4,771                                       |
|                               | Allowance for Notes Receivable   | 590   |                     |  |                                    | 590   |
|                               | Deferred Tax Valuation Allowance |   |                     | 297  |                                    | 297   |
|                               | Program Loss Reserves            |   | 3,739               |  | (2,909)                            | 830   |
|                               | Warranty                         | 82  | 200                 | 103  | (47)                               | 338   |

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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, on March 12, 2008.

**Astronics Corporation**

By  
/s/ Peter J. Gundermann

By  
/s/ David C. Burney

Peter J. Gundermann President and Chief  
Executive Officer  
(Principal Executive Officer)

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

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

| <b>Signature</b>                               | <b>Title</b> | <b>Date</b>    |
|--|--------------|----------------|
| /s/ Raymond W. Boushie<br>Raymond W. Boushie   | Director     | March 12, 2008 |
| /s/ Robert T. Brady<br>Robert T. Brady         | Director     | March 12, 2008 |
| /s/ John B. Drenning<br>John B. Drenning       | Director     | March 12, 2008 |
| /s/ Peter J. Gundermann<br>Peter J. Gundermann | Director     | March 12, 2008 |
| /s/ Kevin T. Keane<br>Kevin T. Keane           | Director     | March 12, 2008 |
| /s/ Robert J. McKenna<br>Robert J. McKenna     | Director     | March 12, 2008 |