

GIGA TRONICS INC
Form 10-Q
November 06, 2003

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE
SECURITIES EXCHANGE ACT OF 1934
for the period ended September 27, 2003 or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE
SECURITIES EXCHANGE ACT OF 1934
for the transition period from _____ to _____

Commission File No. 0-12719

GIGA-TRONICS INCORPORATED

(Exact name of Registrant as specified in its charter)

California _____

(State or other jurisdiction of
incorporation or organization)

94-2656341

(IRS Employer Identification No.)

4650 Norris Canyon Road, San Ramon, CA _____

(Address of principal executive offices)

94583

(Zip Code)

Registrant's telephone number: (925) 328-4650

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 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

Common stock outstanding as of November 3, 2003:

4,703,786 shares

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b of the Act).

Yes No

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ITEM 1

GIGA-TRONICS INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share data)

| | <u>Sept. 27, 2003</u> | <u>March 29, 2003</u> |
|--|-----------------------|---------------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 4,132 | \$ 5,005 |
| Trade accounts receivable, net | 2,292 | 3,245 |
| Inventories | 7,190 | 10,244 |
| Income tax refund receivable | | 100 |
| Prepaid expenses | 347 | 488 |
| | <u> </u> | <u> </u> |
| Total current assets | 13,961 | 19,082 |
| Property and equipment, net | 1,689 | 2,274 |
| Other assets | 388 | 433 |
| | <u> </u> | <u> </u> |
| Total assets | \$ 16,038 | \$ 21,789 |
| | <u> </u> | <u> </u> |
| Liabilities and shareholders equity | | |
| Current liabilities | | |
| Accounts payable | \$ 976 | \$ 1,723 |
| Accrued commissions | 240 | 249 |
| Accrued payroll and benefits | 1,005 | 1,038 |
| Accrued warranty | 784 | 859 |
| Customer advances | 70 | 796 |
| Obligations under capital lease | 45 | 76 |
| Other current liabilities | 737 | 719 |
| | <u> </u> | <u> </u> |
| Total current liabilities | 3,857 | 5,460 |
| Obligations under capital lease, net of current portion | | 10 |
| Deferred rent | 325 | 359 |
| | <u> </u> | <u> </u> |
| Total liabilities | 4,182 | 5,829 |
| | <u> </u> | <u> </u> |
| Shareholders equity | | |
| Preferred stock of no par value | | |
| Authorized 1,000,000 shares; no shares outstanding at Sept. 27, 2003 and March 29, 2003 | | |
| Common stock of no par value; | | |
| Authorized 40,000,000 shares; 4,703,786 shares at Sept. 27, 2003 and 4,693,080 shares at March 29, 2003 issued and outstanding | 12,706 | 12,695 |
| Retained earnings (deficit) | (850) | 3,265 |
| | <u> </u> | <u> </u> |
| Total shareholders equity | 11,856 | 15,960 |
| | <u> </u> | <u> </u> |

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| | | |
|--|-----------|-----------|
| Total liabilities and shareholders equity | \$ 16,038 | \$ 21,789 |
|--|-----------|-----------|

See accompanying notes to unaudited condensed consolidated financial statements.

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GIGA-TRONICS INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share data)

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|----------------|------------------|----------------|
| | Sept. 27, 2003 | Sept. 28, 2002 | Sept. 27, 2003 | Sept. 28, 2002 |
| Net sales | \$5,135 | \$ 5,112 | \$ 10,374 | \$ 10,843 |
| Cost of sales | 3,220 | 3,384 | 7,096 | 7,314 |
| Gross profit | 1,915 | 1,728 | 3,278 | 3,529 |
| Product development | 865 | 1,042 | 1,853 | 2,530 |
| Selling, general and administrative | 1,420 | 1,571 | 3,064 | 3,252 |
| Amortization of intangibles | | 6 | | 10 |
| Operating expenses | 2,285 | 2,619 | 4,917 | 5,792 |
| Operating loss | (370) | (891) | (1,639) | (2,263) |
| Other expense | | (45) | | (71) |
| Interest income, net | 13 | 18 | 10 | 30 |
| Loss from continuing operations before income taxes | (357) | (918) | (1,629) | (2,304) |
| Provision (benefit) for income taxes | | | 4 | (100) |
| Loss from continuing operations | \$ (357) | \$ (918) | \$ (1,633) | \$ (2,204) |
| Loss on discontinued operations, net of income taxes | (126) | (380) | (2,482) | (693) |
| Net loss | \$ (483) | \$ (1,298) | \$ (4,115) | \$ (2,897) |
| Basic and diluted net loss per share: | | | | |
| From continuing operations | \$ (0.08) | \$ (0.20) | \$ (0.35) | \$ (0.47) |
| On discontinued operations | (0.02) | (0.08) | (0.53) | (0.15) |
| Basic and diluted net loss per share | \$ (0.10) | \$ (0.28) | \$ (0.88) | \$ (0.62) |
| Shares used in per share calculation: | | | | |
| Basic and dilutive | 4,696 | 4,666 | 4,695 | 4,661 |

See accompanying notes to unaudited condensed consolidated financial statements.

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GIGA-TRONICS INCORPORATED
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)
 (In thousands)

| | Six Months Ended | |
|---|-----------------------|-----------------------|
| | September 27, 2003 | September 28, 2002 |
| <i>Cash flows provided from operations:</i> | | |
| Net loss | \$(4,115) | \$ (2,897) |
| Adjustments to reconcile net loss to net cash used in operations: | | |
| Depreciation and amortization | 671 | 1,006 |
| Loss/(Gain) on sale of equipment | 8 | (4) |
| Deferred income taxes | | (3) |
| Changes in operating assets and liabilities | 2,676 | 1,305 |
| | (760) | (593) |
| <i>Cash flows from investing activities:</i> | | |
| Purchases of property and equipment | (29) | (100) |
| Proceeds from sale of equipment | | 14 |
| Other assets | (20) | 136 |
| | (49) | 50 |
| <i>Cash flows from financing activities:</i> | | |
| Issuance of common stock | 11 | 44 |
| Payments on capital lease and other long term obligations | (75) | (80) |
| | (64) | (36) |
| Decrease in cash and cash equivalents | (873) | (579) |
| Cash and cash equivalents at beginning of period | 5,005 | 7,180 |
| | \$ 4,132 | \$ 6,601 |

Supplementary disclosure of cash flow information:

- (1) Cash paid for income taxes in the six month period ended Sept. 27, 2003 was \$4. Cash paid for income taxes in the six month period ended Sept. 28, 2002 was \$2.

See accompanying notes to unaudited condensed consolidated financial statements.

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GIGA-TRONICS INCORPORATED
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation

The condensed financial statements included herein have been prepared by Giga-tronics (the Company), pursuant to the rules and regulations of the Securities and Exchange Commission. The results of operations for the interim periods shown in this report are not necessarily indicative of results to be expected for the fiscal year. In the opinion of management, the information contained herein reflects all adjustments necessary to make the results of operations for the interim periods a fair statement of such operations. For further information, refer to the financial statements and footnotes thereto, included in the Annual Report on Form 10-K, filed with the Securities and Exchange Commission for the year ended March 29, 2003.

Certain prior period amounts have been reclassified to conform with the current period's presentation.

(2) Discontinued Operations

During the first quarter of fiscal year 2004, the Company decided to discontinue the operations of DYMATiX, which was previously a separately reported segment. Individual customers were notified of these plans and the necessary staffing reductions have taken place in order to substantially complete the shut-down of the division. The long lived assets of DYMATiX were effectively abandoned as of June 28, 2003. The Company will make arrangements for ongoing service for existing DYMATiX customers. Beginning in the first quarter of Fiscal 2004, the Company's results of operations have been adjusted to reflect the results of the discontinued operations of the DYMATiX segment for all periods presented herein. For the three months ended September 27, 2003, the net impact of the discontinuance of this segment was a reduction in revenue and net loss of \$266,000 and \$126,000, respectively. For the six months ended September 27, 2003, the net impact of the discontinuance of this segment was a reduction in revenue and net loss of \$440,000 and \$2,482,000, respectively. For the three months ended September 28, 2002, the net impact of the discontinuance of this segment was a reduction in revenue and net loss of \$427,000 and \$380,000, respectively. For the six months ended September 28, 2002, the net impact of the discontinuance of this segment was a reduction in revenue and net loss of \$704,000 and \$693,000, respectively.

(3) Revenue

The Company records revenue in accordance with SAB 101, *Revenue Recognition in Financial Statements*. As such, revenue is recorded when there is evidence of an arrangement, delivery has occurred, the price is fixed and determinable, and collectability is assured. This occurs when products are shipped, unless the arrangement involves acceptance terms. If the arrangement involves acceptance terms, the Company defers revenue until product acceptance is received.

The Company provides for estimated costs that may be incurred for product warranties at the time of shipment. The Company's warranty policy generally provides 3 years for Fast Switching Microwave Synthesizers and Universal Power Meters and one year for all other products. The estimated cost of warranty coverage is based on the Company's actual historical experience with its current products or similar products.

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(4) Inventories

Inventories consist of the following (in thousands):

| | <u>Sept. 27, 2003</u> | <u>March 29, 2003</u> |
|------------------|-----------------------|-----------------------|
| Raw materials | \$4,310 | \$ 4,669 |
| Work-in-process | 2,120 | 3,427 |
| Finished goods | 570 | 1,096 |
| Loaned Inventory | 190 | 1,052 |
| | <u> </u> | <u> </u> |
| Total inventory | \$ 7,190 | \$10,244 |
| | <u> </u> | <u> </u> |

(5) Earnings Per Share

Basic earnings per share is calculated by dividing net income or loss by the weighted average common shares outstanding during the period. Diluted earnings per share reflects the net incremental shares that would be issued if dilutive outstanding stock options were exercised, using the treasury stock method. In the case of a net loss, it is assumed that no incremental shares would be issued because they would be antidilutive. In addition, certain options are considered antidilutive because the options' exercise price was above the average market price during the period. The shares used in per share computations are as follows (in thousands):

| | <u>Three Months Ended</u> | | <u>Six Months Ended</u> | |
|---|---------------------------|---------------------------|---------------------------|---------------------------|
| | <u>Sept. 27, 2003</u> | <u>Sept. 28, 2002</u> | <u>Sept. 27, 2003</u> | <u>Sept. 28, 2002</u> |
| Weighted average: | | | | |
| Common shares outstanding | 4,696 | 4,666 | 4,695 | 4,661 |
| Dilutive potential common shares | | | | |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Common shares assuming dilution | 4,696 | 4,666 | 4,695 | 4,661 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Number of stock options not included in the computation | 571 | 587 | 571 | 587 |

All stock options outstanding were excluded from the computation of diluted EPS for the three and six month periods ended September 27, 2003 and September 28, 2002 because the options are antidilutive. The weighted average exercise price of excluded options was \$3.37 and \$3.76 as of Sept. 27, 2003 and Sept. 28, 2002, respectively.

- (6) During the first quarter of fiscal year 2004, the Company adopted SFAS No. 148 (SFAS 148), *Accounting for Stock-Based Compensation Transition and Disclosure - an Amendment of FAS 123*. The Company accounts for stock-based employee compensation using the intrinsic value method under Accounting Principles Board Opinion No. 25 (APB 25), *Accounting for Stock Issued to Employees*, and related interpretations and complies with the disclosure provisions of Statement of Financial Accounting Standards No. 123 (SFAS 123), *Accounting for Stock-Based Compensation*. The following table illustrates the effect on net loss and loss per share if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation:

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| (In thousands except per share data) | Three Months Ended | | Six Months Ended | |
|--|--------------------|----------------|------------------|----------------|
| | Sept. 27, 2003 | Sept. 28, 2002 | Sept. 27, 2003 | Sept. 28, 2002 |
| Net loss, as reported | \$ (483) | \$ (1,298) | \$ (4,115) | \$ (2,897) |
| Deduct: | | | | |
| Stock-based compensation expense included in reported net loss, net of related tax effects | | | | |
| Add: | | | | |
| Total stock-based employee compensation determined under fair value based method for all awards net of related tax effects | (49) | (47) | (97) | (93) |
| Pro forma net loss | \$ (532) | \$ (1,345) | \$ (4,212) | \$ (2,990) |
| Net loss per share Basic: | | | | |
| As reported | \$ (0.10) | \$ (0.28) | \$ (0.88) | \$ (0.62) |
| Pro forma | (0.11) | (0.29) | (0.90) | (0.64) |
| Net loss per share Diluted: | | | | |
| As reported | (0.10) | (0.28) | (0.88) | (0.62) |
| Pro forma | (0.11) | (0.29) | (0.90) | (0.64) |

(7) Significant Customers and Industry Segment Information

The Company has four reportable segments: Giga-tronics Instrument Division, ASCOR, Microsource and Corporate. Giga-tronics Instrument division produces a broad line of test and measurement equipment used in the development, test and maintenance of wireless communications products and systems, flight navigational equipment, electronic defense systems and automatic testing systems. ASCOR designs, manufactures, and markets a line of switching devices that link together many specific purpose instruments that comprise automatic test systems. Microsource develops and manufactures a broad line of YIG (Yttrium, Iron, Garnet) tuned oscillators, filters and microwave synthesizers, which are used in a wide variety of microwave instruments and devices. Corporate handles the financing needs of each segment and lends funds to each segment as required.

Information on reportable segments is as follows (in thousands):

| | Three Months Ended | | September 28, 2002 | |
|-------------------------|--------------------|-----------------------|--------------------|-----------------------|
| | September 27, 2003 | September 28, 2002 | September 27, 2003 | September 28, 2002 |
| | Net Sales | Pre-tax Income (loss) | Net Sales | Pre-tax Income (loss) |
| Giga-tronics Instrument | \$ 2,381 | \$ (440) | \$ 2,092 | \$ (969) |
| ASCOR | 1,046 | 55 | 971 | (85) |
| Microsource | 1,708 | (150) | 2,049 | 12 |
| Corporate | | 178 | | 124 |
| Total | \$ 5,135 | \$ (357) | \$ 5,112 | \$ (918) |

Six Months Ended

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| | September 27, 2003 | | September 28, 2002 | |
|-------------------------|--------------------|--------------------------|--------------------|--------------------------|
| | Net Sales | Pre-tax Income (loss) | Net Sales | Pre-tax Income (loss) |
| Giga-tronics Instrument | \$ 4,488 | \$ (1,252) | \$ 4,219 | \$ (2,712) |
| ASCOR | 2,440 | (139) | 2,183 | (158) |
| Microsource | 3,446 | (569) | 4,441 | 321 |
| Corporate | | 331 | | 245 |
| Total | \$ 10,374 | \$ (1,629) | \$ 10,843 | \$ (2,304) |

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(8) Warranty Obligations

The Company's warranty policy generally provides three years for Fast Switching Microwave Synthesizers and Universal Power Meters and one year for all other products. The Company's policy is to accrue the estimated cost of warranty coverage at the time the sale is recorded. The estimated cost of warranty coverage is based on the Company's actual historical experience with its current products or similar products. For new products, the required reserve is based on historical experience of similar products until such time as sufficient historical data has been collected on the new product.

The Company records a liability for estimated warranty obligations at the date products are sold. Adjustments are made as new information becomes available. The provisions of FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness to Others", which the Company adopted in December 2002, require disclosures about the guarantees that an entity has issued, including a reconciliation of changes in the entity's product warranty liabilities. The following provides a reconciliation of changes in the Company's warranty reserve. The Company provides no other guarantees.

| (In thousands) | Three Months Ended | | Six Months Ended | |
|------------------------------------|--------------------|-------------------|-------------------|-------------------|
| | Sept. 27, 2003 | Sept. 28, 2002 | Sept. 27, 2003 | Sept. 28, 2002 |
| Balance at beginning of period | \$ 805 | \$ 773 | \$ 859 | \$ 779 |
| Provision for current period sales | 95 | 192 | 269 | 448 |
| Warranty costs incurred | (116) | (190) | (344) | (452) |
| Balance at end of period | <u>\$ 784</u> | <u>\$ 775</u> | <u>\$ 784</u> | <u>\$ 775</u> |

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ITEM 2

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF OPERATIONS AND FINANCIAL CONDITION

The forward-looking statements included in this report including, without limitation, statements containing the words "believes", "anticipates", "estimates", "expects", "intends" and words of similar import, which reflect management's best judgment based on factors currently known, involve risks and uncertainties. Actual results could differ materially from those anticipated in these forward-looking statements as a result of a number of factors, including but not limited to those listed in Giga-tronics' Annual Report on Form 10-K for the fiscal year ended March 29, 2003 Part I, under the heading "Certain Factors Which May Adversely Affect Future Operations or an Investment in Giga-tronics", and Part II, under the heading "Management's Discussion and Analysis of Financial Conditions and Results of Operations".

GENERAL

Giga-tronics designs, manufactures, and markets microwave and radio frequency signal generation and power measurement instruments, switching devices, and YIG tuned oscillators. These products have broad applications in both defense electronics and wireless telecommunications.

THREE AND SIX MONTHS ENDED SEPTEMBER 27, 2003 AND SEPTEMBER 28, 2002

During the latter part of the first quarter, Giga-tronics decided to discontinue the operations at its DYMATiX division due to the substantial losses incurred over the last two years. Losses related to the discontinued operations were \$126,000 for the second quarter and \$2,482,000 for the six months ended September 27, 2003.

Total orders from continuing operations increased 2% (\$58,000) for the three-month period to \$3,930,000 compared to \$3,872,000 for the comparable period last year. New orders rose slightly primarily due to strength in military orders coupled with an incremental increase in commercial business. Orders at the Instrument division increased 11% (\$256,000) in the second quarter of FY 2004 versus the prior year. Orders at ASCOR were 33% (\$283,000) lower for the second quarter versus last year. Orders at Microsource increased 11% (\$85,000) versus the comparable quarter last year. For the six months ended September 27, 2003, new orders were \$6,748,000 compared to \$6,700,000 for the same period last year. Backlog at September 27, 2003 was \$13,111,000 (about \$5,438,000 is expected to be shipped within one year) as compared to \$17,068,000 (about \$6,916,000 was expected to be shipped within one year) on September 28, 2002. Of the \$6,916,000 in orders considered shippable within one year as of September 28, 2002, since that date through September 27, 2003, the Company rescheduled (and reclassified as not shippable within one year) shipments for orders of \$1,034,000 net and recorded cancellations of orders for \$49,000.

Net sales from continuing operations for the three-month period ended September 27, 2003 increased \$23,000 and decreased 4% (\$469,000) over the six-month period versus the same periods last year. Sales at the Instrument division increased 14% (\$289,000) for the quarter and increased 6% (\$269,000) for the six months ended September 27, 2003, primarily due to increases in commercial orders as compared to the same periods a year ago. ASCOR sales during the quarter increased 8% (\$75,000) and for the six months increased 12% (\$257,000) versus the respective periods of a year ago primarily due to strong backlog. Sales at Microsource decreased 17% (\$341,000) in the quarter and decreased 22% (\$995,000) for the six months ended September 27, 2003 primarily due to timing of delivery commitments on existing orders in backlog.

Cost of sales on continuing operations decreased 5% (\$164,000) in the quarter ended September 27, 2003 from the similar period a year ago. The decrease was primarily attributable to the product mix shipped in the quarter coupled with lower manufacturing costs. For the six months ended September 27, 2003, cost of sales on continuing operations decreased 3% (\$218,000) primarily due to the 4% decrease in sales and the product mix.

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Operating expenses on continuing operations for the three-month period decreased 13% (\$334,000) compared with the same period last year due to decreases of \$151,000 in SG&A, \$177,000 in product development costs and \$6,000 in amortization expense. For the six-month period, operating expenses decreased 15% (\$875,000) due to decreases of \$188,000 in SG&A, \$677,000 in product development costs and \$10,000 in amortization expense. Research and development expenses on continuing operations for the three and six-month periods decreased 17% (\$177,000) and 27% (\$677,000), respectively, compared with the prior year. The decrease was primarily due to a reduction in product development costs associated with a new product being designed at the Instrument division that was discontinued last year. Selling, general and administrative expenses on continuing operations were down 10% (\$151,000) for the three months ended September 27, 2003 compared to the prior year. The decrease is a result of lower marketing expenses of \$141,000 and administrative expenses of \$53,000, offset by higher commission expenses of \$43,000, due to an increase in commissionable sales in the quarter. For the six months, selling, general and administrative expenses on continuing operations were down 6% (\$188,000) as compared to the same period a year ago. The reduction is a result of decreases in marketing expenses of \$203,000 and administrative expenses of \$124,000, offset by higher commission expenses of \$139,000, due to an increase in commissionable sales in the period. These expense reductions were primarily personnel reductions, but also include decreases in rent expense due to renegotiated lease terms. Amortization of intangibles decreased 100% (\$6,000) for the three months and 100% (\$10,000) for the six months as compared to the prior year. The decrease in the amortization of intangibles is a result of the full amortization of patents and licenses that occurred in the fourth quarter of fiscal year 2003 at the Microsource division. Interest income for the three and six month periods increased from the prior year due to favorable interest rates on cash available for investment.

The pre-tax loss from continuing operations for the three and six month periods ended September 27, 2003 decreased 61% (\$561,000) and 29% (\$675,000), respectively, compared to the same period last year as our improved cost structure helped offset the reduction in sales that occurred during the first half of the year versus last year. The net loss from continuing operations for the first half of the year decreased 26% (\$571,000) to \$1,633,000 versus \$2,204,000 for the same period last year.

FINANCIAL CONDITION AND LIQUIDITY

Giga-tronics had working capital of \$10,104,000 and a ratio of current assets to current liabilities of 3.6 to 1.0 at September 27, 2003. Giga-tronics continues to fund all of its working capital needs from existing cash and operating cash flows.

Cash and cash equivalents at September 27, 2003 decreased \$873,000 from March 29, 2003, and increased \$321,000 from the prior quarter. Cash provided from operations during the quarter was \$361,000. In addition, Giga-tronics spent \$29,000 on new manufacturing and test equipment and other capital items. Giga-tronics intends to continue investing in capital items that support growth and new product development, raise productivity, and improve the quality of its products. Historically, the Company has satisfied its cash needs internally for both operating and capital expenditures, and management expects to continue to do so for at least the next twelve months.

Management believes that cash and cash equivalents remain adequate to meet anticipated operating needs. Discontinued operations should reduce cash used in operations. In the prior year, the discontinued operations used approximately \$1,000,000 in cash. From time to time, Giga-tronics considers a variety of acquisition opportunities to also broaden its product lines and expand its market. Such acquisition activity could also increase the Company's operating expenses and require the additional use of capital resources. The Company also intends to maintain research and development expenditures for the purpose of broadening its product line.

OUTLOOK

Giga-tronics is experiencing an increase in inquiries for its products and that has resulted in an incremental increase in new orders in the first half of the year. New orders in the military sector are showing indications of increased strength, however it is still too early to determine if the commercial wireless telecommunications market we serve has

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rebounded. Our cost reduction programs, including reductions in personnel and new lease terms, are on track and have positioned Giga-tronics to take advantage of any potential opportunities in our market. Giga-tronics will continue monitoring our cost structure and will make appropriate changes when needed. With the discontinuing of operations at the Dymatix division, Giga-tronics will be able to focus on its core business in order to release new products more quickly to market. The Company has recently released the first in a new line of microwave synthesizers that have been well received in the marketplace. This release demonstrates our commitment in new product development. We intend to continue research and development in order to expand our product lines and update our existing lines with additional features. While the management at the Microsource division hopes that prospects for new orders will improve results for the balance of the fiscal year, its short-term growth will be less than previously anticipated as there are timing delays associated with currently booked orders.

FORWARD-LOOKING STATEMENTS

Certain statements contained in this section of the report, including statements regarding sales under **OUTLOOK** and statements under **FINANCIAL CONDITION**, are forward-looking. While Giga-tronics believes that these statements are accurate, Giga-tronics' business is dependent upon general economic conditions and various conditions specific to the test and measurement, wireless and semiconductor industries. Future trends and these factors could cause actual results to differ materially from the forward-looking statements that we have made. In particular:

Giga-tronics' core business is test and measurement, as well as components for the wireless communications market, which continues to be soft. The Company's commercial product backlog has a number of risks and uncertainties such as the cancellation or deferral of orders, dispute over performance and our ability to collect amounts due. If the commercial market should decline further, then shipments in the current year could fall short of plan resulting in a decline in earnings. Also, Giga-tronics has a significant number of defense-related orders. While Giga-tronics has seen some improvement in the defense sector, it is not significant enough to offset the decline in the commercial sector. If the defense market should decline, shipments in the current year could be less than anticipated and cause a decrease in earnings.

The market for electronics equipment is characterized by rapidly changing technology and evolving industry standards. Giga-tronics believes that its future success will depend, in part, upon its ability to develop and commercialize its existing products, develop new products and applications and in part to develop, manufacture and successfully introduce new products and product lines with improved capabilities and continue enhancing existing products. There can be no assurance that Giga-tronics will successfully complete the development of current or future products or that such products will achieve market acceptance. Giga-tronics may also experience difficulty obtaining critical parts or components required in the manufacturing of our products, resulting in our inability to fulfill orders in a timely manner, which may have a negative impact on our earnings. Also, the Company may not timely ramp manufacturing capacity to meet order demand and quickly adapt cost structures to changing market conditions.

As part of our business strategy, Giga-tronics has in the past broadened its product lines and expanded its markets, in part through the acquisition of other business entities, and it may do so in the future. The Company acquired Microsource, Inc. in fiscal 1999 in a transaction accounted for as a purchase. The Company is subject to various risks in connection with past and any future acquisitions. Such risks include, among other things, the difficulty of assimilating the operations and personnel of the acquired companies, the potential disruption of the Company's business, the inability of the Company's management to maximize the financial and strategic position of the Company by the successful incorporation of acquired technology and rights into the Company's product offerings, the maintenance of uniform standards, controls, procedures and policies, and the potential loss of key employees of acquired companies. No assurance can be given that any acquisition by Giga-tronics will or will not occur, that if an acquisition does occur, that it will not materially and adversely affect the Company or that any such acquisition will be successful in enhancing the Company's business. Giga-tronics currently contemplates that future acquisitions may involve the issuance of additional shares of the Company's common stock. Any such issuance may result in dilution to all shareholders of the Company, and sales of such shares in significant volume by the shareholders of acquired companies may depress the price of the Company's common stock.

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ITEM 3

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Financial instruments that expose the Company to market risk are cash and cash equivalents. The Company's cash and cash equivalents are held in recognized financial institutions and have limited market risk due to the short-term maturities of the instruments.

ITEM 4

CONTROLS AND PROCEDURES

Within the 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

PART II - OTHER INFORMATION

ITEM 1

LEGAL PROCEEDINGS

As of November 4, 2003, Giga-tronics has no material pending legal proceedings. From time to time, Giga-tronics is involved in various disputes and litigation matters that arise in the ordinary course of business.

ITEM 4

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

(A.) Annual Meeting of stockholders was held on September 9, 2003.

- (1) The vote for the nominated Directors was as follows:

| <u>Nominee</u> | <u>In Favor</u> | <u>Withheld</u> |
|----------------------|-----------------|-----------------|
| George H. Bruns, Jr. | 4,283,152 | 176,056 |
| James A. Cole | 4,302,252 | 156,956 |
| Kenneth A. Harvey | 4,301,603 | 157,605 |
| Robert C. Wilson | 4,301,503 | 157,705 |
| William E. Wilson | 4,287,971 | 171,237 |

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- (2) Other matters voted upon at the meeting were as follows:
Ratification of the selection of KPMG LLP as independent public accountants for the fiscal year 2004 was approved as follows:

| | <u>Number of Votes on Proposal</u> | <u>Percent of Votes Cast</u> |
|-----------------------------------|--|----------------------------------|
| For | 4,408,800 | 95.78% |
| Against | 34,670 | .75% |
| Abstain | 159,738 | 3.47% |
| Shares represented at the meeting | 4,603,208 | 100.00% |

Broker non-voted Shares = 0

Outstanding shares on Record Date = 4,693,080

ITEM 6

EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

31.1 Certification of Chief Executive Officer pursuant to Section 302 of Sarbanes-Oxley Act.

31.2 Certification of Chief Financial Officer pursuant to Section 302 of Sarbanes-Oxley Act.

32.1 Certification of Chief Executive Officer pursuant to Section 906 of Sarbanes-Oxley Act.

32.2 Certification of Chief Financial Officer pursuant to Section 906 of Sarbanes-Oxley Act.

(b) Reports on Form 8-K

Form 8-K filed on August 5, 2003, reporting under Item 9, announcing the Company's results for the fiscal quarter ended June 28, 2003.

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SIGNATURES

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

GIGA-TRONICS INCORPORATED
(Registrant)

By:

Date: November 4, 2003

/s/ GEORGE H. BRUNS, JR.

George H. Bruns, Jr.
Chairman and Chief Executive Officer
(Principal Executive Officer)

Date: November 4, 2003

/s/ MARK H. COSMEZ II

Mark H. Cosmez II
Vice President, Finance
Chief Financial Officer and Secretary
(Principal Accounting Officer)