RICHARDSON ELECTRONICS LTD/DE
Form 10-K
August 16, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-K

(Mark One)

x **FOR ANNUAL REPORTS PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended June 2, 2007

OR

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

For the transition period from to

Commission File Number: 0-12906

RICHARDSON ELECTRONICS, LTD.

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of incorporation or organization)**	**36-2096643** **(I.R.S. Employer Identification No.)**

40W267 Keslinger Road, P.O. Box 393,

LaFox, Illinois 60147-0393

(Address of principal executive offices)

Registrant s telephone number, including area code:(630) 208-2200

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

Title of each class	Name of each exchange of which registered
Common stock, $0.05 Par Value	**NASDAQ Global Market**

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

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

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

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

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

Large Accelerated Filer ¨ Accelerated Filer x Non-Accelerated Filer ¨

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

The aggregate market value of the registrant s common stock held by non-affiliates of the registrant as of December 2, 2006, was approximately $136,600,000.

As of August 14, 2007, there were outstanding 14,805,234 shares of Common Stock, $.05 par value, inclusive of 1,122,232 shares held in treasury, and 3,048,258 shares of Class B Common Stock, $.05 par value, which are convertible into Common Stock of the registrant on a one-for-one basis.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement for the Annual Meeting of Stockholders scheduled to be held October 9, 2007, which will be filed pursuant to Regulation 14A, are incorporated by reference in Part III of this report. Except as specifically incorporated herein by reference, the above mentioned Proxy Statement is not deemed filed as part of this report.

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PART I

Item 1. Business

Forward Looking Statements

All statements other than statements of historical facts included in this report are statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934. The words may, will, should, could, expect, plan, intend, estimate, anticipate, predict, believe, potential, continue, and similar expressions and variations thereof are intended to identify forward-looking statements. Such statements appear in a number of places in this report and include statements regarding the intent, belief or current expectations of the Company, its directors, or its officers with respect to, among other things: (i) trends affecting the Company s financial condition or results of operations; (ii) the Company s financing plans; (iii) the Company s business and growth strategies, including potential acquisitions; and (iv) other plans and objectives for future operations. Any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties and actual results may differ materially from those predicted in the forward-looking statements or which may be anticipated from historical results or trends.

The Company

Richardson Electronics, Ltd. (the Company) was originally incorporated in Illinois in 1947 and is currently incorporated in Delaware. The Company is a global provider of engineered solutions and a global distributor of electronic components to the radio frequency (RF), wireless and power conversion, electron device, and display systems markets with total sales in fiscal 2007 of $557.3 million. The Company is committed to a strategy of providing specialized technical expertise and value-added products, which the Company refers to as engineered solutions, in response to customers needs. These engineered solutions consist of:

- products which the Company manufactures or modifies;
- products which are manufactured to the Company s specifications by independent manufacturers under the Company s private labels; and
- value the Company adds through design-in support, systems integration, prototype design and manufacturing, testing, and logistics for end products of the Company s customers. The Company defines design-in support as modification of components or identification of lower-cost product alternatives or complementary products.

The Company s products include RF and microwave components, power semiconductors, electron tubes, microwave generators, and data display monitors. These products are used to control, switch or amplify electrical power signals, or as display devices in a variety of industrial, commercial, and communication applications.

The Company s broad array of technical services and products supports both the Company s customers and vendors.

Strategic Business Units

The Company serves its customers through three strategic business units, each of which is focused on different end markets with distinct product and application needs. The Company s three strategic business units are:

- RF, Wireless & Power Division;
- Electron Device Group; and

Display Systems Group.

Each strategic business unit has dedicated marketing, sales, product management, and purchasing functions to better serve its targeted markets. The strategic business units operate globally, serving North America, Asia/Pacific, Europe, and Latin America.

On May 31, 2007, the Company completed the sale of the Security Systems Division/Burtek Systems (SSD/Burtek) strategic business unit to Honeywell International Inc. for $80 million. After transaction expenses paid through June 2, 2007, net cash proceeds from the sale were $78.1 million. The transaction resulted in an after tax gain of $41.6 million after additional transactions costs of $2.5 million were accrued as of June 2, 2007. The Company has used the net proceeds received and will continue to use the net proceeds classified as restricted cash from the sale to pay down debt outstanding under its multi-currency revolving credit agreement (credit agreement). The Company presents SSD/Burtek as a discontinued operation in accordance with the criteria of Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, and prior period results and disclosures have been restated to reflect this reporting.

In an effort to reduce the Company s global operating costs related to logistics, selling, general, and administrative expenses and to better align its operating and tax structure on a global basis, the Company implemented a global restructuring plan during fiscal 2007 (2007 Restructuring Plan). The 2007 Restructuring Plan decreased the number of warehouses and streamlined much of the entire organization which is expected to reduce future corporate and administrative expense. During fiscal 2007, the Company centralized inventory distribution in Europe, restructured its Latin American operations, and reduced its total workforce, including the elimination and restructuring of layers of management.

The total restructuring and severance costs to implement the plan were approximately $6.0 million, a majority of which were $2.7 million of severance costs recorded in the fourth quarter of fiscal 2006 and $2.2 million of severance costs recorded in fiscal 2007.

Selected financial data attributable to each strategic business unit and geographic data for fiscal 2007, 2006, and 2005 is set forth in Note M of the notes to the consolidated financial statements and is incorporated by reference herein.

RF, Wireless & Power Division

The Company s RF, Wireless & Power Division (RFPD) serves the global RF and wireless communications market, including infrastructure and wireless networks and the power conversion markets. RFPD s team of RF and wireless engineers assists customers in designing circuits, selecting cost effective components, planning reliable and timely supply, prototype testing, and assembly. The team offers its customers and vendors a broad range of engineering and technical support including the design-in of RF, wireless and power components and the development of engineered solutions for their support system requirements. RFPD s team of power conversion engineers designs solutions for applications such as motor speed controls, industrial heating, laser technology, semiconductor manufacturing equipment, radar, and welding. The team builds on its expertise in power conversion technology to provide engineered solutions to its customers specifications using what the Company believes are the most competitive components from industry-leading vendors.

The Company expects continued growth in wireless applications as the demand for many types of wireless communication increases worldwide. In addition to voice communication, the Company believes the rising demand for high-speed data transmission will result in major investments in both system upgrades and new systems to handle broader bandwidth. The Company believes wireless and power conversion products for niche applications which will require engineered solutions using the latest RF technology and electronic components include:

Wireless Networks Wireless technologies used for short range interconnection, both within the home or office or last mile solutions from a neighborhood to the home.

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Wireless Infrastructure Equipment required to support the transmission of RF signals.

Power Conversion High power applications such as power suppliers, welding, motor controls, and converting AC/DC and DC/AC. RFPD s growth is supported by its collaboration with leading manufacturers. A key factor in the Company s ability to maintain a strong relationship with its vendors and to attract new vendors is its ability to supply them with worldwide demand forecasts for their existing products as well as products they have in development. The Company has developed internal systems to capture forecasted product demand by potential design opportunity based on ongoing dialogue between its sales team and its customers. The Company shares this information with its suppliers to help them predict near and long-term demand and product life cycles.

The Company has global distribution agreements with such leading suppliers as ANADIGICS, Advanced Power Technologies, Aavid, Anaren, ATC, Cornell-Dubilier, Freescale, HUBER+SUHNER, International Rectifier, M/A-COM, Peregrine, Vishay, Wakefield, and WJ Communications. In addition, the Company has relationships with many niche RF, wireless, and power suppliers to allow it to serve as a comprehensive RF, wireless, and power resource.

The Company participates in most RF, wireless, and power applications and markets in the world, focusing on infrastructure applications rather than consumer-driven subscriber applications.

The following is a description of RFPD s major product areas:

RF and Microwave Active Devices a wide variety of components, such as RF transistors, mixers, switches, amplifiers, oscillators, and RF diodes, which are used in infrastructure, wireless networking, and other related markets, such as broadcast, cable TV, cellular and personal communications service telephony, satellite, wireless local area networks, and various other wireless applications.

RF & Microwave Passive Devices components used to connect all types of electronic equipment including those employing RF technology.

Digital Broadcast Systems components and assemblies used in a broad range of applications in the digital broadcast market, including satellite, transmission, and communication.

Power Conversion Products Silicon Controlled Rectifiers, Heat Sink Assemblies and Power Semiconductor Modules components used in many industrial control applications because of their ability to switch large amounts of power at high speeds. These silicon power devices are capable of operating at up to 4,000 volts at 2,000 amperes.

High Voltage and Power Capacitors devices used in industrial, avionics, medical, and broadcast applications for filtering, high-current bypass, feed-through capacitance for harmonic attenuation, pulse shaping, grid and plate blocking, tuning and tank circuits, antenna coupling, and energy discharge.

Electron Device Group

The Company s Electron Device Group (EDG) provides engineered solutions and distributes electronic components to customers in diverse markets including the steel, automotive, textile, plastics, semiconductor manufacturing, and broadcast industries. EDG s team of engineers designs solutions for applications such as industrial heating, laser technology, semiconductor manufacturing equipment, radar, and welding. The group builds on its expertise in high power, high frequency vacuum devices to provide engineered solutions to fit its customers specifications using what the Company believes are the most competitive components from industry-leading vendors.

EDG serves the industrial market s need for both vacuum tube and semiconductor manufacturing equipment technologies. The Company provides replacement products for systems using electron tubes as well as design and assembly services for new systems employing semiconductor manufacturing equipment. The Company s customers demand for higher power and shorter processing times increases the need for tube-based systems.

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EDG represents leading manufacturers of electronic tubes and semiconductor manufacturing equipment used in industrial power applications. Among the suppliers EDG supports are Amperex, CPI, Eimac, General Electric, Jennings, Litton, Hitachi, NJRC, Thales, L3, National, and Draloric.

The following is a description of EDG s major product areas and services:

Power Amplifier/Oscillator Tubes vacuum or gas-filled tubes used in applications where current or voltage amplification and/or oscillation is required. Applications include induction heating, diathermy equipment, communications, broadcast, and radar systems, and power supplies for voltage regulation or amplification.

Microwave Generators devices that incorporate magnetrons, which are high vacuum oscillator tubes used to generate energy at microwave frequencies. The pulsed magnetron is primarily used to generate high-energy microwave signals for radar applications. Magnetrons are also used in vulcanizing rubber, food processing, packaging, wood/glue drying, in the manufacture of wafers for the semiconductor industry and other industrial heating applications such as microwave ovens, and by the medical industry for sterilization and cancer therapy.

Hydrogen Thyratrons electron tubes capable of high speed and high voltage switching. They are used to control the power in laser and radar equipment and in linear accelerators for cancer treatment.

Thyratrons and Rectifiers vacuum or gas-filled tubes used to control the flow of electrical current. Thyratrons are used to control ignitrons, electric motor speed controls, theatrical lighting, and machinery such as printing presses and various types of medical equipment. Rectifiers are used to restrict electric current flow to one direction in power supply applications.

Ignitrons mercury pool tubes used to control the flow of large amounts of electrical current. Their primary applications are in welding equipment, power conversion, fusion research, and power rectification equipment.

Magnetrons microwave tubes used in industrial applications ranging from industrial scale food processing and plasma generation for semi conductor fabrication processes, to marine and avionics radar.

Contract Manufacturing specializing in projects requiring use of sophisticated processes, low to medium volume, and for industries insisting upon a high level of quality including copy exact discipline. The semi conductor equipment, medical equipment, and industrial equipment markets have been the primary market segments targeted to date.

Display Systems Group

The Display Systems Group (DSG) is a global provider of integrated display products and systems to the public information, financial, point-of-sale, industrial, and healthcare markets. The group works with leading hardware vendors to offer the highest quality liquid crystal display, plasma, cathode ray tube, and customized computing platforms. The group s engineers design custom display solutions that include touch screens, protective panels, custom enclosures, specialized finishes, application specific software, and privately branded products.

The medical imaging market has been transitioning from film-based technology to digital technology. DSG s medical imaging hardware partnership program allows it to deliver integrated hardware and software solutions for this growing market by combining the Company s hardware expertise in medical imaging engineered solutions with its software partners expertise in picture archiving and communications systems. Through such collaborative arrangements, the Company is able to provide integrated imaging workstation systems to the end user and resellers, as well as other medically approved display solutions for various other modalities in the hospital.

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The Company s legacy business of supplying replacement cathode ray tubes continues to be an important market. The Company believes it is successful in supplying replacement cathode ray tubes because of its extensive cross-reference capability. This database, coupled with custom mounting hardware installed by the Company, enables it to provide replacement tubes for more than 200,000 models.

DSG has long-standing relationships with key manufacturers including 3M, AUO, CMO, HP, IBM, Intel, LG, NEC Displays, Philips Displays, Planar Systems, Sharp Electronics, Samsung, and Siemens Displays. The Company believes these relationships and its private label brands allow it to maintain a well-balanced and technologically advanced line of products.

The following is a description of DSG s major product areas:

Cathode Ray Tubes vacuum tubes that convert an electrical signal into a visual image to display information on data display monitors. Cathode ray tubes are used in various environments, including hospitals, financial institutions, airports, and numerous other applications wherever large user groups share electronic data visually. This product line includes both monochrome and color tubes.

Custom LCD Displays flat panel display monitors incorporating a liquid crystal as an alternative to the traditional cathode ray tube technology, typically a few inches in depth and ranging from 10 to 52 measured diagonally. These displays are usually integrated with touchscreen technology or special mounting configurations based on the customer s requirements.

High Resolution Medical Displays an integral component of picture archiving and communications systems, displays are used in diagnostic and non-diagnostic imaging to display the digital image generated from computed tomography, magnetic resonance imaging, radiography, and other digital modalities.

Custom Systems Custom server platforms for the infrastructure/back office of financial exchanges, small profile workstations for digital signage, flight information and kiosk applications, and imaging workstations for radiologists.

Discontinued Operations Security Systems Division/Burtek Systems

Discontinued operations includes the results of the Security Systems Division/Burtek Systems (SSD/Burtek), which the Company sold to Honeywell International Inc. on May 31, 2007. SSD/Burtek was a global provider of closed circuit television, fire, burglary, access control, sound, and communication products and accessories for the residential, commercial, and government markets. The unit specialized in closed circuit television design-in support, offering extensive expertise with applications requiring digital technology. The products SSD/Burtek provided were primarily used for security and access control purposes but are also utilized in industrial applications, mobile video, and traffic management.

Business Strategies

The Company is pursuing a number of strategies designed to enhance its business and, in particular, to increase sales of engineered solutions. The Company s strategies are to:

Capitalize on Engineering and Manufacturing Expertise. The Company believes that its success is largely attributable to its core engineering and manufacturing competency and skill in identifying cost-competitive solutions for its customers, and the Company believes that these factors will be significant to its future success. Historically, the Company s primary business was the distribution and manufacture of electron tubes and the Company continues to be a major supplier of these products. This business enabled the Company to develop manufacturing and design engineering capabilities. Today, the Company uses this expertise to identify engineered solutions for customers applications not only in electron tube technology but also in new and growing end markets and product applications. The Company works closely with its customers engineering departments that allow it to identify engineered solutions for a broad range of applications. The Company believes its customers use its engineering and manufacturing expertise as well as its in-depth knowledge of the components best suited to deliver a solution that meets their performance needs cost-effectively.

Target Selected Niche Markets. The Company focuses on selected niche markets that demand a high level of specialized technical service, where price is not the predominant competitive factor. These niche markets include wireless infrastructure, high power/high frequency power conversion, custom display, and digital imaging. In most cases, the Company does not compete against pure commodity distributors. The Company often functions as an extension of its customers and vendors engineering teams. Frequently, the Company s customers use its design and engineering expertise to provide a product solution that is not readily available from a traditional distributor. By utilizing the Company s expertise, the Company s customers and vendors can focus their engineering resources on more critical core design and development issues.

Focus on Growth Markets. A majority of the Company s sales are in markets it believes have high growth potential and can benefit from its engineering and manufacturing expertise and from its strong vendor relationships. These markets are characterized by substantial end-market growth and rapid technological change. For RFPD, the continuing demand for wireless communications is driving wireless application growth, and power conversion demand continues to grow due to increasing system complexity and the need for intelligent, efficient power management.

Leverage the Existing Customer Base. An important part of the Company s growth is derived from offering new products to its existing customer base. The Company supports the migration of its customers from electron tubes to newer solid-state technologies. In addition, the Company s salespeople are able to sell products from all strategic business units to customers who currently may only purchase from one strategic business unit and sell engineered solutions to customers who currently may only purchase standard components.

Growth and Profitability Strategies

Although the Company has reported net losses from continuing operations of approximately $12.4 million in fiscal 2003, $18.8 million in fiscal 2005, and $4.0 million in fiscal 2006, its long-range growth plan centers around three distinct strategies by which it seeks to maximize its overall profitability:

Focus on Internal Growth. The Company believes that, in most circumstances, internal growth provides the best means of expanding its business, both on a geographic and product line basis. The Company believes there is increased outsourcing of engineering as companies focus on their own core competencies, which the Company believes contributed to the increased demand for its engineered solutions. As technologies change, the Company plans to continue to capitalize on its customers need for design engineering. In fiscal 2007, the Company made sales to approximately 25,000 customers. The Company has developed internal systems to capture forecasted product demand by potential design opportunity. This allows the Company to anticipate the customers future requirements and identify new product opportunities. In addition, the Company shares these future requirements with its manufacturing suppliers to help them predict near and long-term demand, technology trends, and product life cycles. Expansion of the Company s product offerings is an ongoing program. In particular, the following areas have generated significant sales increases in recent years: RF amplifiers; interconnect and passive devices; silicon controlled rectifiers; and custom and medical monitors.

Reduce Operating Costs Through Continuous Operational Improvements. The Company constantly strives to reduce costs in its business through initiatives designed to improve its business processes. The Company continues to embark on programs to improve operating efficiencies and asset utilization, with an emphasis on inventory control and cash generation. The Company revised its incentive programs in fiscal 2004 and fiscal 2007 to heighten its managers commitment to these objectives. In an effort to reduce the Company s global operating costs related to logistics, selling, general, and administrative expenses and to better align its operating and tax structure on a global basis, the Company implemented a global restructuring plan during fiscal 2007

(2007 Restructuring Plan). The 2007 Restructuring Plan decreased the number of warehouses and streamlined much of the entire organization, which is expected to reduce future corporate and administrative expense. During fiscal 2007, the Company centralized inventory distribution in Europe, restructured its Latin American operations, and reduced its total workforce, including the elimination and restructuring of layers of management. Additional programs are ongoing, including the centralization of inventory distribution in Asia/Pacific and continuing the Company s investment in enterprise resource planning software during fiscal 2008.

Products and Suppliers

The Company purchases numerous products from various suppliers as noted above under Strategic Business Units. During fiscal 2007, the Company added the following suppliers: Avago, Muegge, and Thales.

The Company evaluates its customers needs and attempts to maintain sufficient inventories in an effort to ensure its customers a reliable source of supply. While the Company stocks inventory that turns more or less than three months, the Company anticipates holding 90 days of inventory in the normal course of operations. This level of inventory is higher than some of its competitors due to the fact that the Company sells a number of products representing older, or trailing edge, technology that may not be available from other sources. The market for these trailing edge technology products is declining and as manufacturers for these products exit the business, the Company, at times, purchases a substantial portion of their remaining inventory. Also contributing to the Company s higher inventory levels is its commitment to maintaining an inventory of a broad range of products to be able to promptly service those customers who are buying product for replacement of components in equipment critical to preventing downtime of their operations. In other segments of the business, such as RFPD, the market for the Company s products is characterized by rapid change and obsolescence as a result of the development of new technologies, particularly in the semiconductor markets it serves.

The Company has written distribution agreements with many of its suppliers; however, a number of these agreements provide for nonexclusive distribution rights and often include territorial restrictions that limit the countries in which the Company can distribute the products. The agreements are generally short-term, subject to periodic renewal, and some contain provisions permitting termination by either party without cause upon relatively short notice. Although some of these agreements allow the Company to return inventory periodically, others do not, in which case the Company may have obsolete inventory that it cannot return to the supplier.

The Company s suppliers generally warrant the products the Company distributes and allow return of defective products, including those returned to the Company by its customers. Except with respect to certain displays, the Company generally does not provide additional warranties on the products it sells. For information regarding the warranty reserves, see Note A of the notes to the consolidated financial statements.

In addition to third party products, the Company sells proprietary products principally under certain trade names it owns including: A.C.T Kern , *Amperex*®, *Cetron*®, Image Systems *, National*®, Pixelink , and RF Gain . The Company s proprietary products which it manufactures or has manufactured for it, include RF amplifiers, transmitters and pallet assemblies, thyratrons and rectifiers, power tubes, ignitrons, CW magnetron tubes, phototubes, spark gap tubes, microwave generators, custom RF matching networks, heatsinks, silicon controlled rectifier assemblies, large screen display monitors, liquid crystal display monitors, and computer workstations. The materials used in the manufacturing process consist of glass bulbs and tubing, nickel, stainless steel and other metals, plastic and metal bases, ceramics, and a wide variety of fabricated metal components. These materials generally are readily available, but some components may require long lead times for production and some materials are subject to shortages or price fluctuations based on supply and demand.

Sales and Marketing

As of the end of fiscal 2007, the Company employed approximately 549 sales personnel worldwide. In addition, there were approximately 99 authorized representatives, who are not the Company s employees, selling its products, primarily in regions where the Company does not have a direct sales presence. Many of the

Company s sales representatives focus on just one of its strategic business units, while others focus on all of its strategic business units within a particular geographic area. The Company s sales representatives are compensated in part on a salaried basis and in part on a commission basis.

The Company offers various credit terms to qualifying customers as well as prepayment, credit card, and cash on delivery terms. The Company establishes credit limits prior to selling product to its customers and routinely reviews delinquent and aging accounts. The Company establishes reserves for estimated credit losses in the normal course of business.

Distribution

The Company maintains more than 830,000 part numbers in its product inventory database and estimates more than 80% of orders received by 6:00 p.m. local time are shipped complete the same day. Customers can access the Company s product inventory through electronic data interchange, either at the Company s web site, *www.rell.com,* through its catalog, *www.catalog.rell.com*, or by telephone. Customer orders are processed by the regional sales offices and supported by one of the Company s principal distribution facilities in LaFox, Illinois; Amsterdam, Netherlands; or Singapore, Republic of Singapore and/or its additional stocking locations throughout the world. The Company utilizes a sophisticated data processing network that provides on-line, real-time interconnection of all sales offices and central distribution operations, 24 hours per day, seven days per week. Information on stock availability, cross-reference information, customers, and market analyses are instantly obtainable throughout the entire distribution network.

International Sales

In fiscal 2007, 52.0% of the Company s sales and 51.9% of the Company s purchases of products were made outside the U.S. The Company believes that it may continue to expand its international operations to the extent that suitable opportunities become available. Accordingly, its future results could be adversely affected by a variety of factors which are not present for companies with operations and sales solely within the United States, including: changes in currency exchange rates; changes in a specific country s or region s political or economic conditions, particularly in emerging markets, including the possibility of military action or other hostilities and confiscation of property; increases in trade protection measures and import or export licensing requirements; changes in tax laws and international tax treaties; restrictions on the Company s ability to repatriate investments and earnings from foreign operations; difficulty in staffing and managing widespread operations; differing labor regulations; differing protection of intellectual property; changes in regulatory requirements; shipping costs and delays; and difficulties in accounts receivable collection. Such risks could result in substantial increases in costs, the reduction of profit, the inability to do business, and other adverse effects.

Backlog

The Company s backlog of orders was approximately $140.5 million and $120.1 million as of June 2, 2007 and June 3, 2006, respectively. The Company expects to fill all backlog orders within fiscal 2008.

Employees

As of June 2, 2007, the Company employed 991 individuals on a full-time basis. Of these, 549 were employed in the United States and 442 were employed internationally. The worldwide employee base included 549 in sales and product management, 76 in distribution support, 291 in administrative positions, and 75 in value-added and product manufacturing. All of the Company s employees are non-union. The Company considers its relationships with its employees to be good.

Competition

The Company believes that engineering capability, exclusive vendor relationships, and product diversity create segmentation among its competitors. The Company believes that the key competitive factors in its markets include the ability to provide engineered solutions, reliable delivery at competitive prices, provide marketing technical support, and maintain inventory availability and quality. The Company believes that, on a global basis, it is a significant provider of engineered solutions and products which utilize RF and power semiconductors and subassemblies, electron tubes, cathode ray tubes, and custom and medical monitors. In many instances, the Company s competition is its customer base and their decision to make or buy, as well as the original equipment manufacturer for sales of replacement parts and system upgrades to service existing installed equipment. In addition, the Company competes worldwide with other general line distributors and other distributors of electronic components.

Patents and Trademarks

The Company holds or licenses certain manufacturing patents and trademark rights. Although the Company s patents and trademarks have some value, they are not significant to the Company s success, which depends principally upon its ability to provide engineered solutions, reliable delivery at competitive prices, provide marketing technical support, and maintain inventory availability and quality.

Seasonal Variations

The Company experiences moderate seasonality in its business and typically realizes higher sequential sales in its second and fourth fiscal quarters, reflecting increased transaction volume after the summer and holiday months in its first and third fiscal quarter periods.

Website Access to SEC Reports

The Company maintains an Internet website at *www.rell.com*. The Company s annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act of 1934 are accessible through the website, free of charge, as soon as reasonably practicable after these reports are filed electronically with the Securities and Exchange Commission. To access these reports, go to the Company s website at *www.rell.com/investor.asp*. The foregoing information regarding the Company s website is provided for convenience and the contents of the Company s website are not deemed to be incorporated by reference in this report filed with the Securities and Exchange Commission.

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Item 1A. Risk Factors

Investors should consider carefully the following risk factors, in addition to the other information included and incorporated by reference in this Annual Report on Form 10-K. While the Company believes it has identified and discussed below the key risk factors affecting its business, there may be additional risks and uncertainties that are not presently known or that are not currently believed to be significant that may adversely affect its results of operations.

The Company has had significant operating and net losses from continuing operations in the past and may have future losses.

The Company reported net losses from continuing operations of approximately $12.4 million in fiscal 2003, $18.8 million in fiscal 2005, and $4.0 million in fiscal 2006. There is no assurance that the Company will not experience operating losses and net losses from continuing operations in the future. The Company may continue to lose money if its sales do not continue to increase or its expenses are not reduced. The Company cannot predict the extent to which sales will continue to increase across its businesses or how quickly its customers will consume their inventories of the Company s products.

The Company has exposure to economic downturns and operates in cyclical markets.

As a supplier of electronic components and services to a variety of industries, the Company can be adversely affected by general economic downturns. In particular, demand for the products and services of RFPD is dependent upon capital spending levels in the telecommunications industry and demand for products and services of EDG is dependent upon capital spending levels in the manufacturing industry, including steel, automotive, textiles, plastics, semiconductors, and broadcast, as well as the transportation industry. Many of its customers delay capital projects during economic downturns. Accordingly, the Company s operating results for any particular period are not necessarily indicative of the operating results for any future period. The markets served by its businesses have historically experienced downturns in demand that could harm its operating results. Future economic downturns could be triggered by a variety of causes, including outbreaks of hostilities, terrorist actions, or epidemics in the United States or abroad.

Because the Company derives a significant portion of its revenue by distributing products designed and manufactured by third parties, it may be unable to anticipate changes in the marketplace and, as a result, could lose market share.

The Company s business is driven primarily by customers needs and demands for new products and/or enhanced performance, and by the products developed and manufactured by third parties. Because the Company distributes products developed and manufactured by third parties, its business would be adversely affected if its suppliers fail to anticipate which products or technologies will gain market acceptance or if it cannot sell these products at competitive prices. The Company cannot be certain that its suppliers will permit the Company to distribute their newly developed products, or that such products will meet the Company s customers needs and demands. Additionally, because some of the Company s principal competitors design and manufacture new technology, those competitors may have a competitive advantage over the Company. To successfully compete, the Company must maintain an efficient cost structure, an effective sales and marketing team, and offer additional services that distinguish it from its competitors. Failure to execute these strategies successfully could harm its results of operations.

The Company faces intense competition in the markets it serves and, if it does not compete effectively, it could significantly harm its operating results.

The Company faces substantial competition in its markets, in the form of competition from hundreds of electronic component distributors of various sizes, locations, and market focuses as well as original equipment manufacturers, in each case for new products and replacement parts. Some of its competitors have significantly greater resources and broader name recognition than it. As a result, these competitors may be better able to withstand changing conditions within its markets and throughout the economy as a whole. In addition, new competitors could enter its markets.

Engineering capability, exclusive vendor relationships, and product diversity create segmentation among distributors. The Company s ability to compete successfully will depend on its ability to provide engineered solutions, reliable delivery at competitive prices, provide marketing technical support, and maintain inventory availability and quality.

To the extent the Company does not keep pace with technological advances or fails to timely respond to changes in competitive factors in its industry, it could lose market share or experience a decline in its revenue and net income. In addition, gross margins in the businesses in which it competes have declined in recent years due to competitive pressures and may continue to decline.

If the Company does not continue to reduce its costs, it may not be able to compete effectively in its markets.

The success of the Company s business depends, in part, on its continuous reduction of costs. The electronic component industries have historically experienced price erosion and will likely continue to experience such price erosion. If the Company is not able to reduce its costs sufficiently to offset future price erosion, its operating results may be adversely affected. The Company has recently engaged in various cost-cutting and other initiatives intended to reduce costs and increase productivity. In fiscal 2005, the Company recorded a $2.2 million restructuring charge as it eliminated over 60 positions or approximately 5% of its workforce.

In an effort to reduce the Company s global operating costs related to logistics, selling, general, and administrative expenses and to better align its operating and tax structure on a global basis, the Company implemented a global restructuring plan during fiscal 2007 (2007 Restructuring Plan). The 2007 Restructuring Plan decreased the number of warehouses and streamlined much of the entire organization which is expected to reduce future corporate and administrative expense. During fiscal 2007, the Company centralized inventory distribution in Europe, restructured its Latin American operations, and reduced its total workforce, including the elimination and restructuring of layers of management.

The total restructuring and severance costs to implement the plan were approximately $6.0 million, a majority of which were $2.7 million of severance costs recorded in the fourth quarter of fiscal 2006 and $2.2 million of severance costs recorded in fiscal 2007.

The Company cannot ensure that it will not incur further charges for restructuring as it continues to seek cost reduction initiatives. Alternatively, the Company cannot ensure that it will be able to continue to reduce its costs.

Because the Company generally does not have long-term contracts with its vendors, it may experience shortages of products that could harm its business and customer relationships.

The Company generally does not have long-term contracts or arrangements with any of its vendors that guarantee product availability. The Company cannot ensure that its vendors will meet its future requirements for timely delivery of products of sufficient quality or quantity. Any difficulties in the delivery of products could harm its relationships with customers and cause it to lose orders that could result in a significant decrease in its revenues. Further, the Company competes against certain of its vendors and its relationship with those vendors could be harmed as a result of this competition.

The Company s EDG is dependent on a limited number of vendors to supply it with essential products.

Electron tubes and certain other products supplied by EDG are currently produced by a relatively small number of manufacturers. The Company s future success will depend, in large part, on maintaining current

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vendor relationships and developing new relationships. The Company believes that vendors supplying products to some of the product lines of EDG are consolidating their distribution relationships or exiting the business. The five largest suppliers to EDG by percentage of overall EDG purchases in fiscal 2007 were Communications & Power Industries, Inc., New Japan Radio Co. Ltd., Covimag S.A., Thales Components Corp, and, Hitachi High Technologies America. These suppliers accounted for approximately 61% of the overall EDG purchases in fiscal 2007. The loss of one or more of the Company s key vendors and the failure to find new vendors could significantly harm its business and results of operations. The Company has in the past and may in the future experience difficulties obtaining certain products in a timely manner. The inability of suppliers to provide it with the required quantity or quality of products could significantly harm its business.

The Company maintains a significant investment in inventory and has incurred significant charges for inventory obsolescence and overstock, and may incur similar charges in the future.

The Company maintains significant inventories in an effort to ensure that customers have a reliable source of supply. The market for many of its products is characterized by rapid change as a result of the development of new technologies, particularly in the semiconductor markets served by RFPD, evolving industry standards, and frequent new product introductions by some of its customers. The Company does not have many long-term supply contracts with its customers. Generally, the Company s product sales are made on a purchase-order basis, which permits its customers to reduce or discontinue their purchases. If the Company fails to anticipate the changing needs of its customers and accurately forecast their requirements, its customers may not continue to place orders with them and the Company may accumulate significant inventories of products which it will be unable to sell or return to its vendors, or which may decline in value substantially.

In fiscal 2003, the Company recorded a pre-tax provision of $13.8 million, or $8.8 million net of tax, primarily for inventory obsolescence, overstock, and shrinkage, to write-down inventory to net realizable value as it sought to align its inventory and cost structure to then current sales levels amid continued economic slowdown and limited visibility. While the Company did not incur any material provisions for inventory in fiscal 2007 and 2006, incremental inventory write-down charges of $0.9 million were recorded during fiscal 2005 related to restructuring actions and certain product lines were discontinued. The Company cannot ensure that similar charges will not be incurred in the future.

Economic, political, and other risks associated with international sales and operations could adversely affect the Company s business.

In fiscal 2007, 52.0% of the Company s sales were made outside the U.S. and 51.9% of the Company s purchases of products were from suppliers located outside the U.S. The Company anticipates that it will continue to expand its international operations to the extent that suitable opportunities become available. Accordingly, the Company s future results of operations could be impacted by a variety of factors which are not present for companies with operations and sales predominantly within the U.S., including:

- changes in a specific country s or region s political or economic conditions, particularly in emerging markets, including the possibility of military action or other hostilities and confiscation of property;
- increases in trade protection measures and import or export licensing requirements;
- changes in tax laws and international tax treaties;
- restrictions on its ability to repatriate investments and earnings from foreign operations;
- difficulty in staffing and managing widespread operations;
- differing labor regulations;
- differing levels of protection of intellectual property;

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- changes in regulatory requirements;
- shipping costs and delays; or
- difficulties in accounts receivable collection.

If any of these risks materialize, the Company could face substantial increases in costs, the reduction of profit, and the inability to do business.

The Company s success depends on its executive officers and other key personnel.

The Company s future success depends to a significant degree on the skills, experience, and efforts of its executive officers and other key personnel. The loss of the services of any of its executive officers, particularly Edward J. Richardson, its chairman of the board and chief executive officer could significantly harm its business and results of operations.

The Company s future success will also depend on its ability to attract and retain qualified personnel, including technical and engineering personnel. Competition for such personnel is intense, and the Company cannot assure that it will be successful in retaining or attracting such persons. The failure to attract and retain qualified personnel could significantly harm its operations.

The Company s ability to service its debt and meet its other obligations depends on a number of factors beyond its control.

At June 2, 2007, the Company s total debt was approximately $121.4 million, resulting in a debt-to-equity ratio of 89%, and primarily consisted of:

- $11.0 million aggregate principal amount of its 8% convertible senior subordinated notes (8% notes), which bear interest at a rate of 8% per year payable on June 15 and December 15 and mature on June 15, 2011;
- $44.7 million aggregate principal amount of its 7 3/4% convertible senior subordinated notes (7 3/4% notes), which bear interest at a rate of 7 3/4% per year payable on June 15 and December 15 and mature on December 15, 2011; and
- $65.7 million principal amount of indebtedness under the Company s multi-currency revolving credit agreement (credit agreement), which expires on October 29, 2009, bears interest at London Interbank Offered Rate (LIBOR), plus a margin varying with certain financial performance criteria. The interest rate was 7.72% at June 2, 2007. The credit agreement balance of $65.7 million is classified as current as of June 2, 2007, due to the obligation to pay off the credit agreement with the proceeds from the SSD/Burtek sale. All borrowings under the credit agreement, $65.7 million as of June 2, 2007, are anticipated to be repaid by the end of the first quarter of fiscal 2008.

The debt-to-equity ratio has been calculated based on the Company s balance sheet dated June 2, 2007.

The Company s ability to service its debt and meet its other obligations as they come due is dependent on its future financial and operating performance. This performance is subject to various factors, including factors beyond the Company s control such as changes in global and regional economic conditions, changes in its industry or the end markets for its products, changes in interest or currency exchange rates, inflation in raw materials, energy and other costs.

If the Company s cash flow and capital resources are insufficient to enable it to service its debt and meet these obligations as they become due, the Company could be forced to:

- reduce or delay capital expenditures;

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- sell assets or businesses;
- limit or discontinue, temporarily or permanently, business plans or operations;
- obtain additional debt or equity financing; or
- restructure or refinance debt.

The Company cannot ensure the timing of these actions or the amount of proceeds that could be realized from them. Accordingly, the Company cannot ensure that it will be able to meet its debt service and other obligations as they become due or otherwise.

The Company s credit agreement and the indentures for its outstanding notes impose restrictions with respect to various business matters.

The Company entered into a new credit agreement (new credit agreement) on July 27, 2007 which contains numerous restrictive covenants that limit the discretion of management with respect to certain business matters. These covenants place restrictions on, among other things, the Company s ability to incur additional indebtedness, to create liens or other encumbrances, to pay dividends or make other payments in respect of its shares of common stock and Class B common stock, to engage in transactions with affiliates, to make certain payments and investments, to merge or consolidate with another entity, and to repay indebtedness junior to indebtedness under the credit agreement. The new credit agreement contains only one financial covenant related to the ratio of senior funded debt to cash flow. In addition, the indentures for its outstanding notes contain covenants that limit, among other things, its ability to incur additional indebtedness. If the Company fails to comply with the obligations in the new credit agreement and indentures, it could result in an event of default under those agreements. If an event of default occurs and is not cured or waived, it could result in acceleration of the indebtedness under those agreements, any of which could significantly harm its business and financial condition.

The Company was not in compliance with certain financial covenants of the Company s credit agreement in the past, and may not be able to comply with these financial covenants in the future.

In the past the Company has had recurring instances where it failed to meet certain financial covenants of the Company s credit agreement. The new credit agreement entered into on July 27, 2007 contains only one financial covenant related to the ratio of senior funded debt to cash flow. However, in the event that the Company fails to meet this financial covenant in the future, the Company may not be able to obtain the necessary waivers or amendments to remain in compliance with the new credit agreement and the Company s lenders may declare a default and cause all of the Company s outstanding indebtedness under the new credit agreement to become immediately due and payable. If the Company is unable to repay any borrowings when due, the lenders under the new credit agreement could proceed against their collateral, which includes most of the assets the Company owns. In addition, any default under the Company s new credit agreement could lead to an acceleration of debt under other debt instruments that contain cross acceleration or cross-default provisions. If the indebtedness under the Company s new credit agreement and the Company s other debt instruments is accelerated, the Company may not have sufficient assets to repay amounts due under the Company s new credit agreement or indebtedness under the Company s other debt instruments.

The Company is exposed to foreign currency risk.

The Company expects that international sales will continue to represent a significant percentage of its total sales, which expose it to currency exchange rate fluctuations. Since the revenues and expenses of the Company s foreign operations are generally denominated in local currencies, exchange rate fluctuations between local currencies and the U.S. dollar subject the Company to currency exchange risks with respect to the results of its foreign operations to the extent it were unable to denominate its purchases or sales in U.S. dollars or otherwise shift to its customers or suppliers the risk of currency exchange rate fluctuations. The Company currently does not engage in any significant currency hedging transactions. Fluctuations in exchange rates may affect the results of its international operations reported in U.S. dollars and the value of such operations net assets reported in U.S. dollars. Additionally, its competitive position may be affected by the relative strength of the currencies in countries where its products are sold. The Company cannot predict whether foreign currency exchange risks inherent in doing business in foreign countries will have a material adverse effect on its operations and financial results in the future.

If the Company does not maintain effective internal controls over financial reporting, it could be unable to provide timely and reliable financial information.

As disclosed in the Company s Management s Report on Internal Control over Financial Reporting in Part II, Item 9A, Controls and Procedures of this Form 10-K, during fiscal 2006, the Company reported one material weakness in its internal control over financial reporting. A material weakness is a deficiency in internal control over financial reporting that results in more than a remote likelihood that a material misstatement of annual or interim financial statements will not be prevented or detected. During 2006, the Company did not effectively perform an evaluation of the reasonableness of assumptions with respect to the realizability of certain deferred tax assets.

During fiscal 2007, the Company successfully remediated this material weakness by implementing the appropriate procedures to evaluate the realizability of all deferred tax assets. There can be no assurance that material deficiencies will not be identified in the future. Any failure to remediate material weaknesses in the future could have a material adverse effect on our business, results of operations, or financial condition. Furthermore, it is uncertain what impact an adverse opinion or a disclaimed opinion regarding internal controls would have upon the Company s stock price or business.

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Item 2. Properties

The Company owns six facilities and leases 62 facilities. The Company owns its corporate facility and largest distribution center, which is located on approximately 96 acres in LaFox, Illinois and consists of approximately 242,000 square feet of manufacturing, warehouse, and office space. The Company maintains geographically diverse facilities because it believes this will limit market risk and exchange rate exposure. The Company considers its properties to be generally well maintained, in sound condition and repair, and adequate for its present needs. The extent of utilization varies from property to property and from time to time during the year.

The principal facilities of the Company and the primary use and segments at those locations are as follows:

Location	Leased or Owned	Use	Segment
Brampton, Canada	Leased	Sales/Distribution	RFPD, EDG
Shanghai, China	Leased	Sales	RFPD, EDG, DSG
Beijing, China	Leased	Sales	RFPD, EDG, DSG
Shenzhen, China	Leased	Sales	RFPD, EDG, DSG
Colombes, France	Leased	Sales	RFPD, EDG, DSG
Puchheim, Germany	Leased	Sales	RFPD, EDG, DSG
Donaueschingen, Germany	Leased	Sales	DSG
Raanana, Israel	Leased	Sales	RFPD, EDG, DSG
Florence, Italy	Owned	Sales	RFPD, EDG, DSG
Tokyo, Japan	Leased	Sales/Distribution	RFPD, EDG, DSG
Seoul, Korea			