Avenue Income Credit Strategies Fund
Form N-CSR
January 07, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number 811-22485

Avenue Income Credit Strategies Fund
(Exact name of registrant as specified in charter)

399 Park Avenue, 6th Floor

New York, NY 10022
(Address of principal executive offices) (Zip code)

	Copy to:
Randolph Takian	
Avenue Capital Group	Stuart Strauss
399 Park Avenue, 6th Floor	Dechert LLP
New York, NY 10022	1095 Avenue of the Americas
(212) 878-3500	New York, NY 10036

(Name and address of agent for service)

Registrant s telephone number, including area code: (212) 878-3500

Date of fiscal year end: October 31, 2015

Date of reporting period: October 31, 2015

Item 1. Shareholder Report

Avenue Income Credit Strategies Fund

Manager Commentary

October 31, 2015

Dear Shareholder,

We are pleased to present the 2015 Annual Report for Avenue Income Credit Strategies Fund (the Fund). The following Manager Commentary covers the one year period ended October 31, 2015.

Fund Objective and Principal Investment Strategy

The Fund s primary investment objective is to seek a high level of current income with a secondary objective of capital appreciation. Depending on market conditions and the Fund s outlook over time, the Fund seeks to achieve its investment objectives by opportunistically investing primarily in loan and debt instruments (and loan-related or debt-related instruments, including repurchase and reverse repurchase agreements and derivative instruments) of issuers that operate in a variety of industries and geographic regions.

Performance[1]

For the one year period ended October 31, 2015, the Fund had a total return of -6.36% based on net asset value, and -9.29% based on market value. The average annual total return from January 27, 2011 (inception) through October 31, 2015, was 4.01% based on net asset value, and 0.23% based on market value.[2,3] The closing price of the Fund s shares as of October 31, 2015 on the New York Stock Exchange was $13.09 representing a -12.21% discount to the Fund s net asset value per share of $14.91.

Returns

The Fund invests across a range of assets. The below indices cover asset classes that Avenue Capital Management II, L.P. (the Adviser) believes are the same as, or similar to, the asset classes to which the Fund s assets are exposed (in whole or in part).

Fund/Index	Return Over the Period 11/1/2014 10/31/2015
Avenue Income Credit Strategies Fund (ACP) based on net asset value	-6.36%
Avenue Income Credit Strategies Fund (ACP) based on market value	-9.29%
Barclays U.S. Corporate High Yield Index[4]	-1.94%
CS Leveraged Loan Index[4]	0.81%

Performance data shown represents past performance and does not guarantee future results. Current performance may be lower or higher than the performance data shown. Investment returns and principal value will fluctuate, and when sold, your investment may be worth more or less than its original cost. All returns assume reinvestment of all dividends. The Fund is subject to various fees and expenses which include advisory fees, operating expenses, investment related expenses (including but not limited to interest on borrowings) and extraordinary expenses, and the performance shown above reflects the deduction of such fees and expenses. The performance above reflects fee waivers and/or expense reimbursements made by the Fund s Investment Adviser. Absent such waivers and/or reimbursements, the Fund s returns would be lower. Performance information is not annualized, unless otherwise noted. The Fund commenced operations on January 27, 2011. Current performance for the most recent month end can be obtained by calling (877) 525-7330. An independent accountant has not audited, reviewed or compiled the performance results.

Factors Affecting Performance

The Fund underperformed the Barclays Index and CS Index over the period. The Fund continues to utilize fundamental analysis to drive our investment approach and individual security selection.

Avenue Income Credit Strategies Fund

Manager Commentary (continued)

October 31, 2015

We believe that our approach of analyzing each investment on the merits of issuer, industry and rating has benefitted performance and should, in our opinion, continue to allow us to select credits that are likely to be drivers of alpha.

The top issuer contributors were:

- Accellent Inc., JC Penney Corporation Inc., Stackpole International Intermediate Co SA / Stackpole International Powder Metal, Surgery Center Holdings, Inc. and KIK Custom Products Inc.[5]

The top issuer detractors were:

- Connacher Oil and Gas Limited, Bennu Holdings LLC, Chassix Inc., iHeart Communications, Inc. and KCA Deutag UK Finance PLC[6]

During the year, the Fund s use of leverage increased from 29.8% to 31.6% as a percentage of Managed Assets and the leverage amount decreased from $100,000,000 to $90,000,000.

Market Outlook

While the Adviser focuses the majority of its research on fundamental company and industry analysis, it is also cognizant of the macro risks that could positively or negatively impact the asset classes we invest in and risk assets in general. The following is a summary of the key macro risks we are currently monitoring:

- Monetary policy divergence is underway as the Federal Reserve is widely expected to move away from zero rates on December 16, when it moves to raise the Fed Funds rate upward by an estimated 25 basis points; while on December 3, the European Central Bank expanded its Quantitative Easing program via a reduction of deposit rates from -0.2% to -0.3% as it extended its asset purchase program by adding EUR 10bn per month to its planned purchases, and extended the program by six additional months.[7] This could result in a further deterioration of the Euro into 2016.

- We believe overcapacity and reduced demand continue to put more downward pressure on commodity prices, which will likely result in an increase in distressed exchanges and defaults, especially in the energy sector.

- The Chinese economy is expected to slow further to a sub 7% growth rates[8], which could lead to lower demand for commodities and a possible further devaluation of emerging market currencies.

- Strengthening of the US Dollar continues to be a major concern for corporate earnings, especially for multinational firms that rely on non-US revenues.

While there is likely to be continued volatility in the near term for credit and risk assets[9], we believe that the current yield to worst for the high yield market is attractive for the medium-to-long term.

The Adviser s investment team will continue working diligently to identify attractive investment opportunities across the performing, stressed and distressed universe on a global basis. We appreciate your continued interest and support.

Avenue Capital Management II, L.P.

December, 2015

Alternative investments are speculative and involve substantial risks. It is possible that investors may lose some or all of their investment. An investment in the Fund is not appropriate for all investors, and the Fund is not intended to be a complete investment program.

Avenue Income Credit Strategies Fund

Manager Commentary (concluded)

October 31, 2015

The views and opinions in the preceding discussion are subject to change. There is no guarantee that any market forecast set forth in the discussion will be realized. This material represents an assessment of the market environment at a specific point in time, should not be relied upon as investment advice and is not intended to predict or depict performance of any investment.

---

1 Performance data shown represents past performance and does not guarantee future results. Current performance may be lower or higher than the performance data shown. Investment returns and principal value will fluctuate, and when sold, your investment may be worth more or less than its original cost. All returns assume reinvestment of all dividends. The Fund is subject to various fees and expenses which include advisory fees, operating expenses, investment related expenses (including but not limited to interest on borrowings) and extraordinary expenses, and the performance shown above reflects the deduction of such fees and expenses. The performance above reflects fee waivers and/or expense reimbursements made by the Fund s Investment Adviser. Absent such waivers and/or reimbursements, the Fund s returns would be lower. Performance information is not annualized, unless otherwise noted. The Fund commenced operations on January 27, 2011. Current performance for the most recent month end can be obtained by calling (877) 525-7330. An independent accountant has not audited, reviewed or compiled the performance results.

2 Includes dilution of approximately $0.97 to NAV per share resulting from the Fund s transferable rights offering, which expired on May 17, 2013. In connection with such offering, the Fund issued 3,268,518 additional common shares at a subscription price per share below the then-current NAV per share of the Fund.

3 Includes dilution of approximately $0.94 to NAV per share resulting from the Fund s transferable rights offering, which expired on March 23, 2012. In connection with such offering, the Fund issued 2,450,466 additional common shares at a subscription price per share below the then-current NAV per share of the Fund.

4 Index information was compiled from sources that Avenue Capital Management II, L.P. believes to be reliable. No representation or guarantee is made hereby with respect to the accuracy or completeness of such data. The Barclays U.S. Corporate High Yield Index comprises issues that have at least $150 million par value outstanding, a maximum credit rating of Ba1 or BB+ (excluding defaulted issues) and at least one year to maturity. The CS Leveraged Loan Index is designed to mirror the investible universe of the $US-denominated leveraged loan market. Investors cannot invest directly in an index, and index performance does not reflect the deduction of any fees or expenses. There are material differences between such indices and the Fund, including without limitation that such indices are unmanaged, broadly-based indices, do not reflect payment of management or brokerage fees and differ in numerous other respects from the portfolio composition of the Fund; as a result, the Fund s investment portfolio is materially different from any given index. Indices include reinvestment of dividends and other income.

5 The top contributors are evaluated on a total profit and loss basis, which includes realized and unrealized market value gains and losses, impact from foreign exchange transactions, and accrued interest. The list of top contributors does not represent all investments held, purchased or sold during the reporting period and is based on the Adviser s books and records. As of the reporting date of October 31, 2015, the positions listed represented the following percentages of the Fund on a market value basis: Accellent Inc. 0.0%, JC Penney Corporation Inc. 2.2%, Stackpole International Intermediate Co SA / Stackpole International Powder Metal 1.7%, Surgery Center Holdings, Inc. 1.7%

and KIK Custom Products Inc. 0.0%.

6 The top detractors are evaluated on a total profit and loss basis, which includes realized and unrealized market value gains and losses, impact from foreign exchange transactions, and accrued interest. The list of top detractors does not represent all investments held, purchased or sold during the reporting period and is based on the Adviser s books and records. As of the reporting date of October 31, 2015, the positions listed represented the following percentages of the Fund on a market value basis: Connacher Oil and Gas Limited 0.2%, Bennu Holdings LLC 1.1%, Chassix Inc. 4.5%, iHeart Communications, Inc. 4.4%, and KCA Deutag UK Finance PLC 0.4%.

7 *European Central Bank, Introductory Statement to the Press Conference (with Q&A),* December 3, 2015.

8 Bloomberg, December 16, 2015.

9 Risk assets generally refer to assets that have a significant degree of price volatility, such as equities, commodities, high-yield bonds and loans, and currencies.

Avenue Income Credit Strategies Fund

Financial Data(a)

October 31, 2015 (unaudited)

Security Type(b)

Ratings(c)

Geographic Allocation(d)

Top Five Industries(f)

Top 10 Largest Holdings(g)

1	Inventiv Health Inc.	3.3%
2	Endemol NV	3.2%
3	Chassix Inc.	3.1%
4	iHeart Communications, Inc.	3.0%
5	IMG Worldwide Inc.	2.6%
6	ConvaTec Finance International	2.6%
7	K Hovanian Enterprises Inc.	2.6%
8	Faenza GMBH	2.6%
9	Ardagh Glass	2.2%
10	BWAY Holding Company	2.0%
	Total Top 10:	**27.2%**

(a) Holdings are subject to change without notice. Calculated as a percent of managed assets as of the date of this document. Where applicable, percentages may not add to 100% due to rounding.

(b) Security Type, as defined by Avenue Capital Management II, L.P. (the Investment Adviser), is sourced from Bloomberg as well as developed via internal classifications.
(c) Ratings information represent Standard & Poor s ratings on instruments in the portfolio. Ratings are provided for informational purposes only and may change over time. Standard & Poor s rates securities from AAA (highest quality) to C (lowest quality), and D to indicate securities in default. BB and below are considered below investment grade securities. Greater risk, such as increased volatility, limited liquidity, prepayment, non-payment and increased default risk, is inherent in portfolios that invest in high yield (junk) bonds. The Fund may invest all or a substantial portion of its assets in below investment grade securities which are often referred to as high yield or junk securities.
(d) The geographic allocation is based on where the Investment Adviser believes the country of risk to be. Country of risk is the country where the majority of the company s operations are based or where it is headquartered. Investment in non-U.S. securities is subject to the risk of currency fluctuations and to economic and political risks associated with such foreign countries.
(e) Cash and Cash Equivalents includes cash as well as other non-investment asset and liabilities (net), excluding borrowings under credit facilities.
(f) Industries are represented using GICS classifications.
(g) The holdings of the Fund are calculated based on Issuer as opposed to Issue. The number of Issues the Fund owns will be significantly higher than the number of Issuers set forth herein.
(h) Loans may include senior secured, senior unsecured and subordinated loan obligations.

Avenue Income Credit Strategies Fund

Schedule of Investments

October 31, 2015

Security Description	Coupon	Maturity	Principal Amount (000)	Value
CORPORATE BONDS & NOTES 94.3%				
Aerospace & Defense 3.6%				
Accudyne Industries Borrower / Accudyne Industries LLC (a)	7.75%	12/15/2020	$ 1,914	$ 1,660,395
US Airways 2000-3C Pass Through Trust (b)	8.39%	3/1/2022	4,956	5,401,750
				7,062,145
Auto Components 1.7%				
Stackpole International Intermediate Co. SA (a)	7.75%	10/15/2021	2,902	3,250,240
Banks 0.9%				
Royal Bank of Scotland Group PLC	7.65%	(c)	1,400	1,743,000
Chemicals 3.2%				
Hexion, Inc.:				
	6.63%	4/15/2020	3,177	2,692,507
	10.00%	4/15/2020	1,000	950,000
Perstorp Holding AB (a)	8.75%	5/15/2017	2,425	2,503,813
				6,146,320
Commercial Services & Supplies 1.8%				
Light Tower Rentals, Inc. (a)	8.13%	8/1/2019	5,017	3,461,730
Communications Equipment 2.0%				
Avaya, Inc.:				
	9.00%	4/1/2019(a)	3,700	3,015,500
	10.50%	3/1/2021(a)	2,199	852,113
				3,867,613
Construction Materials 3.7%				
CeramTec Group GmbH (a)	8.25%	8/15/2021	EUR 6,100	7,269,651
Consumer Finance 2.2%				
Springleaf Finance Corp.	6.90%	12/15/2017	$ 4,000	4,210,000
Containers & Packaging 6.1%				
Ardagh Finance Holdings SA (d)	8.38%	6/15/2019	EUR 652	710,096
Ardagh Finance Holdings SA PIK (a)	8.63%	6/15/2019	$ 5,357	5,437,377
BWAY Holding Co. (a)	9.13%	8/15/2021	6,001	5,835,973
				11,983,446
Diversified Telecommunication Services 4.8%				
Frontier Communications Corp.:				
	8.88%	9/15/2020(a)	181	187,900
	10.50%	9/15/2022(a)	181	187,788
	11.00%	9/15/2025(a)	2,903	3,042,692
Intelsat Jackson Holdings SA:				
	6.63%	12/15/2022	2,398	1,894,420
	7.50%	4/1/2021	565	509,912
Wind Acquisition Finance SA (a)	7.38%	4/23/2021	3,550	3,576,625
				9,399,337
Energy Equipment & Services 4.2%				
CHC Helicopter SA	9.38%	6/1/2021	2,007	802,620
Drill Rigs Holdings, Inc. (a)	6.50%	10/1/2017	2,250	1,534,230
Globe Luxembourg SCA (a)	9.63%	5/1/2018	1,015	857,675
Pacific Drilling V Ltd. (a)	7.25%	12/1/2017	1,610	1,094,800
Tervita Corp.:				
	8.00%	11/15/2018(a)	4,225	3,105,375
	10.88%	2/15/2018(a)	1,422	711,000
				8,105,700
Health Care Equipment & Supplies 4.0%				
ConvaTec Finance International SA PIK (a)	8.25%	1/15/2019	7,500	7,481,250

Greatbatch Ltd. (a)	9.13%	11/1/2023	320	326,000
				7,807,250

See Accompanying Notes to Financial Statements.

5

Avenue Income Credit Strategies Fund

Schedule of Investments (continued)

October 31, 2015

Security Description	Coupon	Maturity		Principal Amount (000)	Value
Health Care Providers & Services 7.1%					
HCA, Inc.:					
	7.05%	12/1/2027	$	745	$ 789,700
	7.50%	11/6/2033		120	127,800
	7.58%	9/15/2025		555	604,950
	7.69%	6/15/2025		900	994,500
inVentiv Health, Inc. (a)	9.00%	1/15/2018		5,075	5,239,937
inVentiv Health, Inc. PIK (a)	10.00%	8/15/2018		4,155	4,026,153
Kindred Healthcare, Inc.	8.75%	1/15/2023		1,412	1,472,010
Tenet Healthcare Corp.	8.13%	4/1/2022		525	555,188
					13,810,238
Hotels, Restaurants & Leisure 8.5%					
Caesars Entertainment Operating Co, Inc.:					
	9.00%	2/15/2020(e)(f)		3,245	2,612,225
	11.25%	6/1/2017(e)(f)		2,820	2,234,850
Gala Electric Casinos PLC (d)	11.50%	6/1/2019	GBP	2,900	4,755,641
Scientific Games International, Inc.:					
	7.00%	1/1/2022(a)	$	310	311,550
	10.00%	12/1/2022		3,723	3,294,855
The Unique Pub Finance Co. Plc	6.46%	3/30/2032	GBP	2,530	3,354,212
					16,563,333
Household Durables 6.2%					
Beazer Homes USA, Inc.:					
	7.25%	2/1/2023	$	2,225	2,097,062
	7.50%	9/15/2021		2,639	2,573,025
K Hovnanian Enterprises, Inc.:					
	7.00%	1/15/2019(a)		1,353	1,075,635
	8.00%	11/1/2019(a)		213	164,010
	9.13%	11/15/2020(a)		7,000	6,160,000
					12,069,732
Independent Power and Renewable Electricity Producers 1.7%					
Illinois Power Generating Co.:					
	6.30%	4/1/2020		2,536	2,003,440
	7.95%	6/1/2032		1,750	1,365,000
					3,368,440
Industrial Conglomerates 0.1%					
Trinseo Materials Operating SCA / Trinseo Materials Finance, Inc. (a)	6.38%	5/1/2022	EUR	135	147,970
IT Services 1.1%					
Syniverse Holdings, Inc.	9.13%	1/15/2019	$	2,672	2,237,800
Machinery 0.9%					
Waterjet Holdings, Inc. (a)	7.63%	2/1/2020		1,840	1,853,800
Marine 3.4%					
Navios Maritime Acquisition Corp. / Navios Acquisition Finance US, Inc.	8.13%	11/15/2021(a)		1,544	1,478,380
Navios Maritime Holdings, Inc. / Navios Maritime Finance II US, Inc.:					
	7.38%	1/15/2022(a)		3,711	2,917,774
	8.13%	2/15/2019		3,179	2,320,670
					6,716,824

See Accompanying Notes to Financial Statements.

Avenue Income Credit Strategies Fund

Schedule of Investments (continued)

October 31, 2015

Security Description	Coupon	Maturity	Principal Amount (000)	Value
Media 11.4%				
Altice Finco SA	7.63%	2/15/2025(a)	$ 1,800	$ 1,705,500
Altice Luxembourg SA:				
	6.25%	2/15/2025(a)	EUR 100	97,594
	7.63%	2/15/2025(a)	$ 1,540	1,416,030
Altice SA	7.75%	5/15/2022(a)	2,030	1,953,875
Altice US Finance II Corp.	7.75%	7/15/2025(a)	5,101	4,909,713
Clear Channel Communications, Inc.:				
	10.63%	3/15/2023	410	344,400
	11.25%	3/1/2021	8,610	7,361,550
Clear Channel Communications, Inc. PIK	14.00%	2/1/2021	1,909	782,750
Clear Channel Worldwide Holdings, Inc.	7.63%	3/15/2020	3,500	3,631,250
				22,202,662
Metals & Mining 3.7%				
Constellium NV:				
	7.00%	1/15/2023(d)	EUR 800	727,616
	8.00%	1/15/2023(a)	$ 1,500	1,271,250
Schmolz & Bickenbach Luxembourg SA (a)	9.88%	5/15/2019	EUR 2,157	2,424,878
Wise Metals Group LLC / Wise Alloys Finance Corp. (a)	8.75%	12/15/2018	$ 820	774,900
Wise Metals Intermediate Holdings LLC/Wise Holdings Finance Corp. PIK (a)	9.75%	6/15/2019	2,263	2,104,590
				7,303,234
Multiline Retail 4.1%				
JC Penney Corp, Inc.	5.65%	6/1/2020	4,595	4,204,425
The Neiman Marcus Group, Inc. PIK (a)	8.75%	10/15/2021	3,645	3,786,061
				7,990,486
Oil, Gas & Consumable Fuels 2.4%				
Halcon Resources Corp. (a)	8.63%	2/1/2020	2,411	2,079,488
Memorial Production Partners LP / Memorial Production Finance Corp.	6.88%	8/1/2022	78	49,140
Northern Oil and Gas, Inc.:				
	8.00%	6/1/2020	1,590	1,314,930
	8.00%	6/1/2020	872	721,144
US Shale Solutions, Inc. (f)	12.50%	9/1/2017	1,781	445,250
				4,609,952
Pharmaceuticals 2.6%				
JLL/Delta Dutch Pledgeco BV (a)	8.75%	5/1/2020	4,926	5,030,677
Wireless Telecommunication Services 2.9%				
Arqiva Broadcast Finance PLC (a)	9.50%	3/31/2020	GBP 3,375	5,651,648
TOTAL CORPORATE BONDS & NOTES (Cost $200,807,627)				183,863,228
SENIOR LOANS 27.1% (g)(h)				
Aerospace & Defense 0.8%				
AM General LLC Term Loan	10.25%	3/22/2018	$ 2,000	1,540,000
Auto Components 1.6%				
Chassix Holdings Inc. Exit Term Loan	12.00%	7/29/2019	2,993	3,023,380
Chemicals 2.2%				
Solenis International, LP USD 2nd Lien Term Loan	7.75%	7/31/2022	4,633	4,319,806
Containers & Packaging 2.6%				
Mauser Holdings Term Loan	8.75%	7/31/2022	5,481	5,141,178
Diversified Consumer Services 0.9%				
Cengage Learning Acquisitions, Inc. Term Loan	7.00%	3/31/2020	1,649	1,637,419

Electric Utilities 1.5%				
La Paloma Generating Co. LLC 2nd Lien Term Loan (b)	9.25%	2/20/2020	4,000	2,920,000
Health Care Providers & Services 1.7%				
Surgery Center Holdings Inc. 2nd Lien Term Loan	8.50%	11/3/2021	3,377	3,334,539

See Accompanying Notes to Financial Statements.

Avenue Income Credit Strategies Fund

Schedule of Investments (continued)

October 31, 2015

Security Description	Coupon	Maturity	Principal Amount (000)	Value
Media 8.5%				
Endemol (AP NMT Acquisition) 2nd Lien Term Loan	10.00%	8/13/2022	$ 6,899	$ 6,105,615
Endemol (AP NMT Acquisition) USD 1st Lien Term Loan	6.75%	8/13/2021	3,079	2,929,220
IMG Worldwide, Inc. 2nd Lien Term Loan	8.25%	5/6/2022	7,900	7,524,750
				16,559,585
Oil, Gas & Consumable Fuels 1.8%				
Bennu Oil & Gas LLC Replacement Loans PIK	9.75%	11/1/2018	5,389	2,155,696
Connacher Oil And Gas Ltd. Term Loan PIK (b)	9.00%	5/23/2018	180	133,759
Endeavour International Holdings Term Loan	11.00%	1/2/2017	2,280	1,014,521
Southern Pacific Resource Corp. 1st Lien Term Loan (b)(e)(f)	14.25%	3/31/2019	1,519	277,131
				3,581,107
Technology Hardware, Storage & Peripherals 2.5%				
Eastman Kodak Co. 2nd Lien Term Loan	10.75%	9/3/2020	5,130	4,905,754
Trading Companies & Distributors 3.0%				
Neff Rental LLC 2nd Lien Term Loan	7.25%	6/9/2021	6,434	5,822,496
TOTAL SENIOR LOANS (Cost $62,528,319)				52,785,264
CONVERTIBLE BONDS 6.5%				
Banks 4.1%				
Lloyds Banking Group PLC	7.50%	(c)	2,900	3,081,250
Societe Generale SA (a)(h)	7.88%	(c)	2,185	2,191,839
UniCredit SpA (d)(h)	8.00%	(c)	2,905	2,857,794
				8,130,883
Oil, Gas & Consumable Fuels 0.1%				
Connacher Oil and Gas Ltd. (b)	12.00%	8/31/2018	201	150,601
Thrifts & Mortgage Finance 2.3%				

	2010	%	March 27, 2009	%	2010	%	2009	%
Net sales	$ 60,977		$ 69,292		$ 163,220		$ 223,562	
Cost of goods sold	44,472		50,141		122,182		161,386	
Gross profit	16,505	27.1 %	19,151	27.6 %	41,038	25.1 %	62,176	27.8 %

Marketing, engineering and administrative expenses		14,555	23.9		14,517	21.0		42,228	25.9			47,843	21.4
Earnings from operations	$	1,950	3.2	$	4,634	6.7	$	(1,190)	(0.7)		$	14,333	6.4

Comparison of the Third Quarter of FY 2010 with the Third Quarter of FY 2009

Net sales for the third quarter decreased 12.0%, or $8.3 million, to $61.0 million from $69.3 million in the same period a year ago. Compared to the third quarter of fiscal 2009, the U.S. Dollar weakened against the Euro and Asian currencies. The net translation effect of this on foreign operations was to increase revenues by approximately $1.5 million versus the prior year, before eliminations. Adjusting for the impact of foreign currency translation on the third fiscal quarter, sales would have been down just over 14% versus the same period last fiscal year. Sales continued to be affected by the impact the global recession is having on the Company's markets, specifically from customers in the mega yacht and industrial markets. This weakness was partially offset by strengthening demand from customers in the oil and gas market as well as continued demand from the airport, rescue and fire fighting (ARFF) market and stable demand from land- and marine-based military, and Asian-Pacific commercial marine markets. On a sequential basis, third quarter sales were 11% and 30% higher than in the second and first fiscal quarters, respectively.

Sales at our manufacturing segment were down 23.8%, or $15.7 million, to $50.2 million from $65.9 million in the same period last year. Sales at our U.S. domestic manufacturing location were down just over 19%, primarily due to continued softening in industrial product, land-based oil and gas transmission, and commercial marine transmission shipments in the quarter. This was partially offset by strong shipments of ARFF and military transmissions, and Arneson Surface Drives in the quarter. This operation saw strong growth in its six month backlog during the quarter, primarily driven by orders for the 8500 series transmission for the land-based oil and gas market. The Company's Belgian and Italian manufacturing operations, which were adversely impacted by the softness in the European mega yacht and industrial markets, experienced decreases of approximately 41% and 18%, respectively, compared to the prior fiscal year's third quarter. The Company's Swiss manufacturing operation, which supplies customized propellers for the global mega yacht and patrol boat markets, experienced a 17% increase in sales, as softness in the mega yacht market was more than offset by growth in the patrol boat market. Compared to the third quarter of fiscal 2009, the U.S. Dollar weakened against the Euro and Asian currencies. The net translation effect of this on foreign manufacturing operations was to increase revenues by approximately $0.9 million versus the prior year, before eliminations.

Our distribution segment, buoyed by continued growth in Asia Pacific, experienced a decrease of only 6.1% in sales compared to the third quarter of fiscal 2009. The Company's distribution operations in Singapore continued to experience strong demand for marine transmission products for use in various commercial applications. This operation saw a 2% increase in sales versus the same period a year ago, and set a new sales record for its third fiscal quarter. The Company's distribution operation in the Northwest of the United States and Southwest of Canada experienced a double-digit increase in sales due to strong transmission shipments in the oil and gas market. The Company's distribution operations in Italy, which provides boat accessories and propulsion systems for the Italian pleasure craft market, saw a 23% decrease in sales due to continued weakness in that market. Sales at the Company's joint venture in Japan were down 38% due to lower shipments of marine transmissions for commercial markets. Compared to the third quarter of fiscal 2009, the U.S. Dollar weakened against the Euro and Asian currencies. The net translation effect of this on foreign distribution operations was to increase revenues by approximately $2.1 million versus the prior year, before eliminations.

The elimination for net inter/intra segment sales decreased $8.9 million, accounting for the remainder of the net change in sales versus the same period last year. This change reflects the overall volume decline in shipments primarily to our European and North American subsidiaries.

Gross profit as a percentage of sales decreased 50 basis points to 27.1% of sales, compared to 27.6% of sales for the same period last year. Profitability for fiscal 2010's third quarter was impacted by lower volumes, unfavorable product mix, higher pension expenses and unfavorable plant absorption, partially offset by lower warranty expense. The Company estimates that the majority of the deterioration was the result of unfavorable absorption due to the impact of lower volumes and the effect of the temporary plant shutdowns along with government sponsored layoffs, and normal seasonal actions, to adjust production levels to near term demand. In the third quarter of fiscal 2009, the Company recorded $0.2 million of pension expense for its defined benefit pension plans, compared to pension expense of $0.6 million in the third quarter of fiscal 2010, for a net year over year increase in pension expense of $0.4 million. It is estimated that the fiscal year impact of the increase in pension expense to cost of goods sold will be $2.8 million. These were partially offset by a net reduction in warranty expense of $1.7 million, from $2.1 million in the prior year's third fiscal quarter to $0.4 million for the current fiscal quarter. The prior year warranty expense was impacted by a specific quality campaign in the Company's domestic land-based transmission business.

Marketing, engineering, and administrative (ME&A) expenses of $14.6 million were up slightly compared to last year's third fiscal quarter. As a percentage of sales, ME&A expenses increased to 23.9% of sales versus 21.0% of sales in the third quarter of fiscal 2009. In the prior year's fiscal third quarter, there was a $0.7 million reversal of corporate bonus expense that reduced ME&A expenses. Stock-based compensation expense for the quarter was $0.1 million compared to $0.4 million in fiscal 2009's third quarter, for a net reduction of $0.3 million. Compared to the third quarter of fiscal 2009, the U.S. Dollar weakened against the Euro and Asian currencies. The net translation effect of this was to increase ME&A expenses by approximately $0.5 million versus the prior year, before eliminations. The net remaining decrease in ME&A expenses is primarily the result of previously announced cost reduction initiatives across the Company's global operations. The table below summarizes significant changes in certain ME&A Expenses for the fiscal year:

$ thousands – (Income)/Expense	Three Months Ended March 26, 2010	March 27, 2009	Increase/ (Decrease)
Bonus	$ -	$ (733)	$ 733
Stock Based Compensation	122	428	(306)
Defined Benefit Pension Plans	460	265	195
			622
	Foreign Currency Translation		485
			1,107
		All Other, Net	(1,069)
			$ 38

Interest expense of $0.6 million for the quarter was up 21.5% versus last year's third fiscal quarter. For the third quarter of fiscal 2009, the interest rate on the Company's revolving credit facility was in the range of 1.67% to 3.16%, whereas for the third quarter of fiscal 2010 the rate was 4.0%. The average balance of the Company's revolving credit facility decreased by $14.8 million, or nearly 55%. The net impact of the higher interest rate and lower average balance on the revolver was that the interest expense was flat. The interest expense on the Company's $25 million Senior Note was flat year over year, at a fixed rate of 6.05%, at $0.4 million. The net increase in interest of $0.1 million was primarily driven by higher interest expense at the Company's Swiss manufacturing operation, as the result of a prepayment penalty for the early extinguishment of nearly $2 million of debt.

Other income, net of $0.4 million for the quarter compared to other expense, net of $1.0 million in the prior fiscal year's third quarter. The net change of $1.4 million from the prior year was primarily due to an increase in exchange gains recognized at the Company's Japanese joint venture versus exchange losses in the prior year caused by the strengthening of the U.S. Dollar in the third quarter of fiscal 2010.

The effective tax rate for the nine months ended March 26, 2010 was 52.4% compared to 29.2% for the nine months ended March 27, 2009. The increase in fiscal 2010 is the result of the magnified impact of foreign non-deductible expenses on the current year rate. While these non-deductible expenses have remained relatively constant year over year, they are a larger percentage of the current year projected foreign earnings which results in a greater impact to the current year annualized effective tax rate. The effective tax rate for the three months ended March 26, 2010 was 14.0% compared to 11.8% for the three months ended March 27, 2009. The effective tax rate for the third quarter was reduced by the impact of applying the new annualized effective tax rate discussed above to the losses recorded in the first six months of fiscal 2010. In addition, during the third quarter of 2010, the Company completed and filed its 2009 Federal and State income tax returns. Subsequently, the Company completed its return-to-provision reconciliation to determine differences between positions taken per the year-end 2009 book tax provision and the actual positions taken per the 2009 returns. This reconciliation identified an error in the fiscal 2009 tax provision, which resulted in understating fiscal 2009 earnings by $188,000. To correct this error, the company reduced tax expense by $188,000 in the third quarter of fiscal 2010. The Company believes that the error was not material to the current or any previously issued financial statements. The prior year rate of 11.8% was reduced by foreign tax credits and favorable adjustments following the filing of the prior year tax return. The Company maintains valuation allowances when it is more likely than not that all or a portion of a net deferred tax asset will not be realized. Changes in valuation allowances from period to period are included in the tax provision in the period of change. In determining whether a valuation allowance is required, the Company takes into account such factors as prior earnings history, expected future earnings, carry-back and carry-forward periods, and tax strategies that could potentially enhance the likelihood of realization of a net deferred tax asset. Due to the operating losses in the first half of the fiscal year, the Company has evaluated the realizability of the deferred tax assets in all relevant jurisdictions. This evaluation concluded that it continues to be more likely than not that all net deferred tax assets will be realized, and no valuation allowance is warranted. The Company will continue to evaluate the realizability of its net deferred tax assets in the future, and will establish a valuation allowance in the event that it becomes more likely than not that all or a portion of a net deferred tax asset will not be realized.

Comparison of the First Nine Months of FY 2010 with the First Nine Months of FY 2009

Net sales for the first nine months of fiscal 2010 decreased 27.0%, or $60.3 million, to $163.2 million from $223.6 million in the same period a year ago. Compared to the first nine months of fiscal 2009, the Euro and Asian currencies strengthened, on average, against the U.S. Dollar. The translation effect of this strengthening on foreign operations was to increase revenues by approximately $4.0 million versus the prior year, before eliminations. Sales continued to be affected by the impact the global recession is having on the Company's markets, specifically from customers in the mega yacht and industrial markets. This weakness was partially offset by continued demand from the airport, rescue and fire fighting (ARFF) market and stable demand from land- and marine-based military, and Asian-Pacific commercial marine markets. The Company saw increased order activity in the second and third fiscal quarters, with particularly strong growth in the order backlog for land-based transmissions for its oil and gas markets. The six month backlog for ARFF and military transmissions remain steady. While order activity for pleasure craft and commercial marine markets remains soft, the Company continues to experience growth in its patrol boat business.

Sales at our manufacturing segment were down 35.5% or $71.4 million, to $129.9 million from $201.3 million in the same period last year. Year-to-date, sales at our U.S. domestic manufacturing locations were down over 31%. Except for growth in its ARFF transmission and Arneson Surface Drive businesses, all of the markets served by our domestic operation have seen double-digit decreases on a year-to-date basis. However, the Company saw an increase in both order inquiries and backlog in the second and third fiscal quarters. The Company's European manufacturing operations, which have been adversely impacted by the slowdown in the European mega yacht and industrial markets, experienced 20% to 60% decreases versus the first nine months of fiscal 2009.

Our distribution segment experienced a decrease of 9.7% in sales, or $8.1 million, to $75.6 million from $83.7 million in the same period a year ago. The Company's Asian distribution operations in Singapore continued to experience growth in the commercial marine transmission market, posting a nearly 5% increase in sales year-to-date. Offsetting this increase, the Company's distribution operations in Italy saw a significant decrease in pleasure craft marine transmission and boat management system product sales. In addition, North American distribution operations continue to see weakness in the pleasure craft marine markets as well as continued softness in the Canadian oil and gas markets, although the latter showed increased order activity and shipments in the third quarter of fiscal 2010. Compared to the first nine months of fiscal 2009, the Euro and Asian currencies strengthened, on average, against the U.S. dollar. The translation effect of this strengthening on foreign distribution operations was to increase revenues by approximately $4.1 million versus the prior year, before eliminations.

The elimination for net inter/intra segment sales decreased $19.2 million, accounting for the remainder of the net change in sales versus the same period last year. This change reflects the overall volume decline in shipments primarily to our European and North American subsidiaries.

Gross profit as a percentage of sales decreased nearly 270 basis points to 25.1% of sales, compared to 27.8% of sales for the same period last year. Profitability for fiscal 2010's first nine months was significantly impacted by lower volumes, unfavorable product mix, higher pension expenses and unfavorable plant absorption, partially offset by lower warranty expense. The Company estimates that the majority of the deterioration was the result of unfavorable absorption due to the impact of lower volumes and the effect of the temporary plant shutdowns along with government sponsored layoffs, and normal seasonal actions, to adjust production levels to near term demand. In the first nine months of fiscal 2009, the Company recorded $0.6 million of pension expense for its defined benefit pension plans, compared to pension expense of $1.8 million in the first nine months of fiscal 2010, for a net year over year increase in pension expense of $1.2 million. It is estimated that the fiscal year impact of the increase in pension expense to cost of goods sold will be $2.8 million. These were partially offset by a net reduction in warranty expense of $1.4 million, from $4.2 million in the prior fiscal year's first nine months to $2.8 million for the current fiscal year's first nine months. The prior year warranty expense was impacted by a specific quality campaign in the Company's domestic land-based transmission business.

Marketing, engineering, and administrative (ME&A) expenses of $42.2 million were down 12% compared to prior year's results through three quarters. As a percentage of sales, ME&A expenses increased to 25.9% of sales versus 21.4% of sales in the first nine months of fiscal 2009. Compared to the first nine months of fiscal 2009, the U.S. Dollar weakened against the Euro and Asian currencies. The translation effect of this weakening was to increase ME&A expenses by approximately $1.0 million versus the prior year, before eliminations. In addition, the prior year's fiscal first nine months included $1.3 million of severance costs and approximately $1.1 million of additional corporate IT expenses primarily related to the Company's implementation of its global ERP system. The net remaining decrease in ME&A expenses is primarily the result of previously announced cost reduction initiatives across the Company's global operations. The table below summarizes significant changes in certain ME&A Expenses for the fiscal year:

$ thousands – (Income)/Expense	Nine Months Ended March 26, 2010	March 27, 2009	Increase/ (Decrease)
Domestic/Corporate IT Expenses	$ 3,520	$ 4,602	$ (1,082)
Severance	-	1,308	(1,308)
Stock Based Compensation	384	524	(140)
Defined Benefit Pension Plans	1,379	676	703
			(1,827)

Foreign Currency Translation		1,033
		(794)
All Other, Net		(4,821)
Net Decrease	$	(5,615)

Interest expense of $1.8 million for the first nine months was flat versus last fiscal year's first nine months. For the first nine months of fiscal 2009, the interest rate on the Company's revolving credit facility was in the range of 1.67% to 4.00%, whereas for the first nine months of fiscal 2010 the rate was 4.0%. The average balance of the Company's revolving credit facility decreased by $8.1 million, or over 34%, and the total interest on the revolver decreased nearly 11% to $0.5 million. The interest expense on the Company's $25 million Senior Note was flat year over year, at a fixed rate of 6.05%, at $1.1 million. The net remaining increase in interest of $0.1 million was primarily driven by higher interest expense at the Company's Swiss manufacturing operation, as the result of a prepayment penalty for the early extinguishment of nearly $2 million of debt.

Other income of $0.2 million for the nine months ended March 26, 2010 improved from other expense of $0.0 million for the comparable period in the prior year. This improvement is due primarily to favorable foreign currency movements from period to period.

The effective tax rate for the nine months ended March 26, 2010 was 52.4% compared to 29.2% for the nine months ended March 27, 2009. The increase in fiscal 2010 is the result of the magnified impact of foreign non-deductible expenses on the current year rate. While these non-deductible expenses have remained relatively constant year over year, they are a larger percentage of the current year projected foreign earnings which results in a greater impact to the current year annualized effective tax rate. During the third quarter of 2010, the Company completed and filed its 2009 Federal and State income tax returns. Subsequently, the Company completed its return-to-provision reconciliation to determine differences between positions taken per the year-end 2009 book tax provision and the actual positions taken per the 2009 returns. This reconciliation identified an error in the fiscal 2009 tax provision, which resulted in understating fiscal 2009 earnings by $188,000. To correct this error, the company reduced tax expense by $188,000 in the third quarter of fiscal 2010. The Company believes that the error was not material to the current or any previously issued financial statements. The Company maintains valuation allowances when it is more likely than not that all or a portion of a net deferred tax asset will not be realized. Changes in valuation allowances from period to period are included in the tax provision in the period of change. In determining whether a valuation allowance is required, the Company takes into account such factors as prior earnings history, expected future earnings, carry-back and carry-forward periods, and tax strategies that could potentially enhance the likelihood of realization of a net deferred tax asset. Due to the operating losses in the first half of the fiscal year, the Company has evaluated the realizability of the deferred tax assets in all relevant jurisdictions. This evaluation concluded that it continues to be more likely than not that all net deferred tax assets will be realized, and no valuation allowance is warranted. The Company will continue to evaluate the realizability of its net deferred tax assets in the future, and will establish a valuation allowance in the event that it becomes more likely than not that all or a portion of a net deferred tax asset will not be realized.

Financial Condition, Liquidity and Capital Resources

Comparison between March 26, 2010 and June 30, 2009

As of March 26, 2010, the Company had net working capital of $92.8 million, which represents a decrease of $10.8 million, or 10%, from the net working capital of $103.7 million as of June 30, 2009.

Cash increased 9.6% to $14.5 million as of March 26, 2010. The majority of the cash as of March 26, 2010 is at the Company's overseas operations in Europe ($9.8 million) and Asia-Pacific ($3.9 million). In the third fiscal quarter, the Company used roughly $2 million of cash at its Swiss operation to pay down a portion of its local debt.

Trade receivables of $42.2 million were down $11.2 million, or nearly 21%, from last fiscal year-end. The net effect of foreign currency translation due to the strengthening of the U.S. Dollar versus the Euro, and the weakening of the U.S. Dollar versus Asian currencies was to decrease trade accounts receivables by just over $0.3 million versus the end of the prior fiscal year. The overall decrease in accounts receivable was consistent with the lower sales volume experienced in the first nine months of fiscal 2010. Sales for the first nine months of fiscal 2009 were $223.6 million compared to $163.2 million for the first nine months of fiscal 2010. Sales in the fourth fiscal quarter of 2009 were $72.1 million versus $61.0 in the most recent fiscal quarter, a 15% decrease. Management continues to actively monitor accounts receivables and work with customers on a global basis.

Net inventory decreased by $13.2 million, or 14.3%, versus June 30, 2009 to $79.1 million. Foreign currency translation did not have a material effect on the comparison of inventories at March 26, 2010 and June 30, 2009. The majority of the net decrease in inventory came at the Company's European manufacturing locations and Asian distribution operation. On a consolidated basis, as of March 26, 2010, the Company's manufacturing backlog of orders to be shipped over the next six months approximates $72.8 million, compared to $60.6 million at June 30, 2009 and $70.0 million at December 25, 2009. The over 20% increase in backlog since the start of the fiscal year was driven primarily by higher order activity for the 8500 series transmission, which is used by oilfield services companies for pressure pumping oil and natural gas wells. The net effect of foreign currency translation on the six month backlog was to reduce it by nearly $0.7 million, primarily as a result of a weakening Euro versus the U.S. Dollar since the start of the fiscal year. The continued reduction of inventory levels at both the Company's manufacturing and distribution operations around the world continues to be a priority for the balance of fiscal 2010 and beyond.

Net property, plant and equipment (PP&E) decreased $4.7 million versus June 30, 2009. This includes the addition of $2.8 million in capital expenditures, primarily at the Company's domestic and Belgian manufacturing operations, which was offset by depreciation of $6.7 million. The net remaining decrease is due to foreign currency translation effects. As a result of current external business factors, the Company expects to invest between $4 and $7 million in capital assets in fiscal 2010. The Company continues to review its capital plans based on overall market conditions and availability of capital, and may make changes to its capital plans accordingly. In addition, the quoted lead times on certain manufacturing equipment purchases may push some of the capital expenditures into the next fiscal year. This compares to $8.9 million and $15.0 million in capital expenditures in fiscal 2009 and fiscal 2008, respectively. The Company's capital program is focusing on modernizing key core manufacturing, assembly and testing processes at its facilities around the world as well as the implementation of a global ERP system.

Accounts payable as of March 26, 2010 of $22.9 million were down $1.9 million, or 7.7%, from June 30, 2009. The effect of foreign currency translation due to the weakening U.S. Dollar versus the Euro and Asian currencies was to decrease accounts payable by just under $0.1 million versus the end of the prior fiscal year. The net decrease in accounts payable was consistent with the overall decrease in inventory at the Company's manufacturing locations in the quarter.

Total borrowings and long-term debt, as of March 26, 2010 decreased by $15.7 million, or 31%, to $35.1 million versus June 30, 2009. This decrease was driven by the overall increase in operating cash flow primarily driven by a decrease in inventory and receivables levels. For the first nine months of fiscal 2010, the Company generated $23.1 million of cash from operating activities. At March 26, 2010, the Company is in compliance with all covenants and other requirements set forth in its revolving loan and note agreements.

Total equity decreased $3.7 million to $104.1 million as March 26, 2010 compared to June 30, 2009. Retained earnings decreased by $3.8 million. The net decrease in retained earnings included $1.4 million in net losses reported year-to-date and $2.4 million in dividend payments. Net unfavorable foreign currency translation of $1.2 million was reported. The remaining movement of $1.4 million represents an adjustment for the amortization of net actuarial loss and prior service cost on the Company's defined benefit pension plans.

In December 2002, the Company entered into a $20,000,000 revolving loan agreement with M&I Marshall & Ilsley Bank ("M&I"), which had an original expiration date of October 31, 2005. In September 2004, the revolving loan agreement was amended to increase the commitment to $35,000,000 and the termination date of the agreement was extended to October 31, 2007. During the first quarter of fiscal 2007, the term was extended by an additional two years to October 31, 2009. An additional amendment was agreed to in the first quarter of fiscal 2008 to extend the term by an additional year to October 31, 2010, and eliminate the covenants limiting capital expenditures and restricted payments (dividend payments and stock repurchases). During the fourth quarter of fiscal 2009, the term was further extended to May 31, 2012 and the funded debt to EBITDA maximum was increased from 2.5 to 3.0. This agreement contains certain covenants, including restrictions on investments, acquisitions and indebtedness. Financial covenants include a minimum consolidated net worth, minimum EBITDA for the most recent four fiscal quarters of $11,000,000 at March 26, 2010, and a maximum total funded debt to EBITDA ratio of 3.0 at March 26, 2010. As of March 26, 2010, the Company was in compliance with these covenants with a four quarter EBITDA total of $14,750,000 and a funded debt to EBITDA ratio of 2.38. The minimum net worth covenant fluctuates based upon actual earnings and is subject to adjustment for certain pension accounting adjustments to equity. As of March 26, 2010 the minimum equity requirement was $101,122,000 compared to an actual result of $137,282,000 after all required adjustments. The outstanding balance of $9,250,000 and $22,450,000 at March 26, 2010 and June 30, 2009, respectively, is classified as long-term debt. In accordance with the loan agreement as amended, the Company has the option of borrowing at the prime interest rate or LIBOR plus an additional "Add-On," between 2% and 3.5%, depending on the Company's Total Funded Debt to EBITDA ratio, subject to a minimum interest rate of 4%. The rate was 4.0% at March 26, 2010 and June 30, 2009, respectively.

On April 10, 2006, the Company entered into a Note Agreement (the "Note Agreement") with The Prudential Insurance Company of America and certain other entities (collectively, "Purchasers"). Pursuant to the Note Agreement, Purchasers acquired, in the aggregate, $25,000,000 in 6.05% Senior Notes due April 10, 2016 (the "Notes"). The Notes mature and become due and payable in full on April 10, 2016 (the "Payment Date"). Prior to the Payment Date, the Company is obligated to make quarterly payments of interest during the term of the Notes, plus prepayments of principal of $3,571,429 on April 10 of each year from 2010 to 2015, inclusive. The outstanding balance was $25,000,000 at March 26, 2010 and June 30, 2009, respectively. Of the outstanding balance, $3,571,000 was classified as a current maturity of long-term debt at March 26, 2010 and June 30, 2009, respectively. The remaining $21,429,000 is classified as long-term debt. The Company also has the option of making additional prepayments subject to certain limitations, including the payment of a Yield-Maintenance Amount as defined in the Note Agreement. In addition, the Company will be required to make an offer to purchase the Notes upon a Change of Control, and any such offer must include the payment of a Yield-Maintenance Amount. The Note Agreement includes certain financial covenants which are identical to those associated with the revolving loan agreement discussed above. The Note Agreement also includes certain restrictive covenants that limit, among other things, the incurrence of additional indebtedness and the disposition of assets outside the ordinary course of business. The Note Agreement provides that it shall automatically include any covenants or events of default not previously included in the Note Agreement to the extent such covenants or events of default are granted to any other lender of an amount in excess of $1,000,000. Following an Event of Default, each Purchaser may accelerate all amounts outstanding under the Notes held by such party.

Four quarter EBITDA and total funded debt are non-GAAP measures, and are included herein for the purpose of disclosing the status of the Company's compliance with the four quarter EBITDA covenant and the total funded debt to four quarter EBITDA ratio covenant described above. In accordance with the Company's revolving loan agreement with M&I and the Note Agreement:

- "Four quarter EBITDA" is defined as "the sum of (i) Net Income plus, to the extent deducted in the calculation of Net Income, (ii) interest expense, (iii) depreciation and amortization expense, and (iv) income tax expense;" and

- "Total funded debt" is defined as "(i) all Indebtedness for borrowed money (including without limitation, Indebtedness evidenced by promissory notes, bonds, debentures and similar interest-bearing instruments), plus (ii) all purchase money Indebtedness, plus (iii) the principal portion of capital lease obligations, plus (iv) the maximum amount which is available to be drawn under letters of credit then outstanding, all as determined for the Company and its consolidated Subsidiaries as of the date of determination, without duplication, and in accordance with generally accepted accounting principles applied on a consistent basis."

- "Total funded debt to four quarter EBITDA" is defined as the ratio of total funded debt to four quarter EBITDA calculated in accordance with the above definitions.

The Company's total funded debt as of March 26, 2010 and June 30, 2009 was equal to the total debt reported on the Company's March 26, 2010 and June 30, 2009 Consolidated Balance Sheet, and therefore no reconciliation is included herein. The following table sets forth the reconciliation of the Company's reported Net Earnings to the calculation of four quarter EBITDA for the four quarters ended March 26, 2010:

Four Quarter EBITDA Reconciliation	
Net Earnings	$ 1,311,000
Depreciation & Amortization	9,804,000
Interest Expense	2,471,000
Income Taxes	1,164,000
Four Quarter EBITDA	$14,750,000
Total Funded Debt to Four Quarter EBITDA	
Total Debt	$35,100,000
Divided by: Four Quarter EBITDA	14,750,000
Total Funded Debt to Four Quarter EBITDA	2.38

As of March 26, 2010, the Company was in compliance with all of the covenants described above. In the fourth fiscal quarter of 2009, the Company announced $25 million of cost avoidance and savings actions in light of softening that was anticipated in many of its key markets. Based on its annual and long range financial plans, which reflects these actions and the softening forecast, the Company does not expect to violate any of its financial covenants in fiscal 2010. The current margin surrounding ongoing compliance with the above covenants, in particular, minimum EBITDA for the most recent four fiscal quarters and total funded debt to EBITDA, may narrow in the Company's fourth fiscal quarter with an improvement beginning in the first quarter of fiscal 2011 and continuing thereafter. Please see the factors discussed under Item 1A, Risk Factors, of this Form 10-Q for further discussion of this topic.

The Company's balance sheet remains very strong, there are no off-balance-sheet arrangements other than the operating leases listed below, and we continue to have sufficient liquidity for near-term needs. The Company had $25.8 million of available borrowings on our $35 million revolving loan agreement as of March 26, 2010, and continues to generate enough cash from operations to meet our operating and investing needs. For the nine months ended March 26, 2010, the Company generated net cash from operating activities of $23.1 million. As of March 26, 2010, the Company also had cash of $14.5 million, primarily at its overseas operations. These funds, with limited restrictions, are available for repatriation as deemed necessary by the Company. In the third fiscal quarter, the Company used roughly $2 million of cash at its European operations to pay down some of its local debt. In fiscal 2010, the Company expects to contribute $547,000 to its defined benefit plans, the minimum contributions required. However, if the Company elects to make voluntary contributions in fiscal 2010, it intends to do so using cash from operations and, if necessary, from available borrowings under existing credit facilities.

As of March 26, 2010, the Company has obligations under non-cancelable operating lease contracts and loan and senior note agreements for certain future payments. A summary of those commitments follows (in thousands):

Contractual Obligations	Total	Less than 1 year	1-3 Years	3-5 Years	After 5 Years
Revolver borrowing	$9,250		$9,250		
Long-term debt	$25,850	$3,978	$7,533	$7,166	$7,173
Operating leases	$9,847	$3,501	$4,314	$1,822	$210
Total obligations	$44,947	$7,479	$21,097	$8,988	$7,383

The table above does not include tax liabilities related to uncertain income tax positions totaling $823,000, excluding related interest and penalties, as the timing of their resolution can not be estimated. See Note H of the Condensed Consolidated Financial Statements for disclosures surrounding uncertain income tax positions.

The Company maintains defined benefit pension plans for some of its operations in the United States and Europe. The Company has established the Pension Committee to manage the operations and administration of the defined benefit plans. The Company estimates that fiscal 2010 contributions to all defined benefit plans will total $547,000.

New Accounting Releases

In February 2010, the Financial Accounting Standards Board ("FASB") issued a standards update removing the requirement for an SEC filer to disclose a date through which subsequent events have been evaluated in both issued and revised financial statements. This update was effective upon issuance, and has been incorporated in this report.

In August 2009, the FASB issued a clarification on fair value measurements. This clarification provides that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using one or more of the techniques provided for in this update. This clarification was effective in the first reporting period following issuance (the Company's first quarter of fiscal 2010), and did not have a material impact on the Company's financial statements.