

AEROFLEX HOLDING CORP.
Form 10-Q
November 07, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013
Commission File Number 001-34974

AEROFLEX HOLDING CORP.

(Exact name of Registrant as specified in its Charter)

DELAWARE
(State or other jurisdiction
of incorporation or organization)

01-0899019
(I.R.S. Employer
Identification No.)

35 South Service Road
P.O. Box 6022
Plainview, N.Y.
(Address of principal executive offices)

11803-0622
(Zip Code)

(516) 694-6700
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer
Non-accelerated filer
(Do not check if a smaller reporting company)

Accelerated filer
Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

November 6, 2013
(Date)

84,942,690
(Number of Shares)

**AEROFLEX HOLDING CORP.
AND SUBSIDIARIES
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Aeroflex Holding Corp. and Subsidiaries
Unaudited Condensed Consolidated Balance Sheets

(In thousands, except share and per share data)

| | September 30, 2013 | June 30, 2013 |
|--|-----------------------|------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 62,793 | \$ 39,424 |
| Accounts receivable, less allowance for doubtful accounts of \$3,379 and \$3,422 | 119,320 | 151,163 |
| Inventories | 171,782 | 156,516 |
| Deferred income taxes | 35,509 | 35,491 |
| Prepaid expenses and other current assets | 12,826 | 9,374 |
| Total current assets | 402,230 | 391,968 |
| Property, plant and equipment, net of accumulated depreciation of \$118,014 and \$122,479 | 101,890 | 101,546 |
| Deferred financing costs, net | 11,152 | 11,580 |
| Other assets | 31,541 | 31,886 |
| Intangible assets with definite lives, net | 55,683 | 65,552 |
| Intangible assets with indefinite lives | 112,373 | 110,779 |
| Goodwill | 316,155 | 315,643 |
| Total assets | \$ 1,031,024 | \$ 1,028,954 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 35,209 | \$ 34,768 |
| Advance payments by customers and deferred revenue | 22,762 | 23,490 |
| Income taxes payable | 401 | 12,003 |
| Accrued payroll expenses | 22,002 | 21,694 |
| Accrued expenses and other current liabilities | 33,568 | 37,184 |
| Total current liabilities | 113,942 | 129,139 |
| Long-term debt | 587,000 | 587,000 |
| Deferred income taxes | 64,970 | 67,296 |
| Other long-term liabilities | 21,378 | 23,061 |
| Total liabilities | 787,290 | 806,496 |
| Stockholders' equity: | | |
| Preferred stock, par value \$.01 per share; 50,000,000 shares authorized, no shares issued and outstanding | - | - |
| Common stock, par value \$.01 per share; 300,000,000 shares authorized, 84,942,690 and 84,936,582 shares issued and outstanding | 849 | 849 |
| Additional paid-in capital | 652,144 | 651,950 |
| Accumulated other comprehensive income (loss) | (32,831) | (43,406) |
| Accumulated deficit | (376,428) | (386,935) |
| Total stockholders' equity | 243,734 | 222,458 |
| Total liabilities and stockholders' equity | \$ 1,031,024 | \$ 1,028,954 |

See notes to unaudited condensed consolidated financial statements.

Aeroflex Holding Corp. and Subsidiaries

Unaudited Condensed Consolidated Statements of Operations

(In thousands, except per share data)

| | Three Months Ended September 30, | |
|---|----------------------------------|-------------|
| | 2013 | 2012 |
| Net sales | \$ 132,732 | \$ 137,635 |
| Cost of sales | 66,914 | 69,413 |
| Gross profit | 65,818 | 68,222 |
| Operating expenses: | | |
| Selling, general and administrative costs | 33,168 | 35,520 |
| Research and development costs | 21,485 | 20,878 |
| Amortization of acquired intangibles | 10,518 | 14,580 |
| Restructuring charges | 684 | 3,267 |
| Total operating expenses | 65,855 | 74,245 |
| Operating income (loss) | (37) | (6,023) |
| Other income (expense): | | |
| Interest expense | (7,252) | (10,078) |
| Write-off of deferred financing costs | - | (597) |
| Other income (expense), net | (51) | (289) |
| Total other income (expense), net | (7,303) | (10,964) |
| Income (loss) from continuing operations before income taxes | (7,340) | (16,987) |
| Provision (benefit) for income taxes | (3,385) | (2,471) |
| Income (loss) from continuing operations | (3,955) | (14,516) |
| Discontinued operations: | | |
| Income from discontinued operations, net of tax provision of \$105 and \$117 | 360 | 377 |
| Gain on disposal of operations, net of tax of \$0 | 14,102 | - |
| Income from discontinued operations | 14,462 | 377 |
| Net income (loss) | \$ 10,507 | \$ (14,139) |
| Income (loss) per common share - basic and diluted: | | |
| Continuing operations | \$ (0.05) | \$ (0.17) |
| Discontinued operations | 0.17 | - |
| Net income (loss) | \$ 0.12 | \$ (0.17) |
| Weighted average number of common shares outstanding: | | |
| Basic and diluted | 84,916 | 84,836 |

See notes to unaudited condensed consolidated financial statements.

Aeroflex Holding Corp. and Subsidiaries
Unaudited Condensed Consolidated Statements of Comprehensive Income (Loss)
(In thousands)

| | Three Months Ended September 30, | |
|--|----------------------------------|-------------|
| | 2013 | 2012 |
| Net income (loss) | \$ 10,507 | \$ (14,139) |
| Other comprehensive income (loss): | | |
| Minimum pension liability adjustment, net of tax provision (benefit) of \$21 and \$0 | 25 | - |
| Foreign currency translation adjustment, net of tax provision (benefit) of \$410 and \$192 | 10,550 | 5,477 |
| | 10,575 | 5,477 |
| Total comprehensive income (loss) | \$ 21,082 | \$ (8,662) |

See notes to unaudited condensed consolidated financial statements.

Aeroflex Holding Corp. and Subsidiaries

Unaudited Condensed Consolidated Statements of Cash Flows

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(In thousands)

| | Three Months Ended September 30, 2013 | 2012 |
|---|--|-------------|
| Cash flows from operating activities: | | |
| Net income (loss) | \$ 10,507 | \$ (14,139) |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) | | |
| operating activities: | | |
| Depreciation and amortization | 16,449 | 20,123 |
| Gain on disposal of operations | (14,102) | - |
| Write-off of deferred financing costs | - | 597 |
| Deferred income taxes | (3,341) | (2,629) |
| Share-based compensation | 882 | 636 |
| Amortization of deferred financing costs | 428 | 554 |
| Other, net | (14) | 511 |
| Change in operating assets and liabilities, net of effects from sale of business: | | |
| Decrease (increase) in accounts receivable | 29,457 | 33,023 |
| Decrease (increase) in inventories | (14,572) | 94 |
| Decrease (increase) in prepaid expenses and other assets | (1,904) | (1,438) |
| Increase (decrease) in accounts payable, accrued expenses and other liabilities | (16,054) | (5,338) |
| Net cash provided by (used in) operating activities | 7,736 | 31,994 |
| Cash flows from investing activities: | | |
| Net proceeds from the sale of business | 18,389 | - |
| Capital expenditures | (5,307) | (4,087) |
| Other, net | 115 | 248 |
| Net cash provided by (used in) investing activities | 13,197 | (3,839) |
| Cash flows from financing activities: | | |
| Debt repayments | - | (25,000) |
| Other, net | (901) | (21) |
| Net cash provided by (used in) financing activities | (901) | (25,021) |
| Effect of exchange rate changes on cash and cash equivalents | 3,337 | 777 |
| Net increase (decrease) in cash and cash equivalents | 23,369 | 3,911 |
| Cash and cash equivalents at beginning of period | 39,424 | 41,324 |
| Cash and cash equivalents at end of period | \$ 62,793 | \$ 45,235 |

See notes to unaudited condensed consolidated financial statements.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial information of Aeroflex Holding Corp. and subsidiaries (“we”, “our”, “us”, or the “Company”) has been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) and the rules and regulations of the United States Securities and Exchange Commission (“SEC”), and reflects all adjustments, consisting of normal recurring adjustments, which in management’s opinion are necessary for a fair presentation. The June 30, 2013 balance sheet information has been derived from audited financial statements, but does not include all information or disclosures required by U.S. GAAP.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of sales and expenses during the reporting period. Actual results may differ from those estimates, and such differences may be material to the financial statements.

These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in our annual report on Form 10-K for the fiscal year ended June 30, 2013 (“the fiscal 2013 Form 10-K”).

Unless the context requires otherwise, “fiscal” refers to the twelve months ended June 30 of the applicable year. For example, “fiscal 2013” refers to the twelve months ended June 30, 2013.

Results of operations for interim periods are not necessarily indicative of results to be expected for the full fiscal year or any future periods.

2. Recent Accounting Pronouncements

In February 2013, the FASB issued guidance which improves the reporting of reclassifications out of accumulated other comprehensive income. The new guidance requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under U.S. GAAP to be reclassified in its entirety to net income. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety from accumulated other comprehensive income to net income in the same reporting period, an entity is required to cross-reference other disclosures required under U.S. GAAP that provide additional detail about those amounts. This new guidance became effective for us in our first quarter of fiscal 2014. The adoption of this presentation and disclosure only guidance is reflected in our consolidated financial statements.

In March 2013, the FASB issued authoritative guidance to resolve the diversity in practice concerning the release of the cumulative translation adjustment (“CTA”) into net income (i) when a parent sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets within a foreign entity, and (ii) in connection with a step acquisition of a foreign entity. This amended guidance requires that CTA be released into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided, and that a pro rata portion of the CTA be released into net income upon a partial sale of an equity method investment in a foreign entity only. In addition, the amended guidance clarifies the definition of a sale of an investment in a foreign entity to include both events that result in the loss of a controlling financial interest in a foreign entity and events that result in an acquirer obtaining control of an acquiree in which it held an equity interest immediately prior to the date of acquisition. The CTA should be released into net income upon the occurrence of such events. This new guidance becomes effective prospectively for us in our

first quarter of fiscal 2015. The adoption of this new guidance is not expected to have a significant impact on our consolidated financial statements

In July 2013, the FASB issued guidance that clarifies when an entity should present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. If either (i) a net operating loss carryforward, a similar tax loss, or tax credit carryforward is not available as of the reporting date under the governing tax law to settle taxes that would result from the disallowance of the tax position or (ii) the entity does not intend to use the deferred tax asset for this purpose (provided that the tax law permits a choice), an entity should present an unrecognized tax benefit in the financial statements as a liability and should not net the unrecognized tax benefit with a deferred tax asset. This new guidance becomes effective prospectively for us in our first quarter of fiscal 2015, with retrospective application and early adoption permitted. We are currently evaluating the impact of this presentation and disclosure only guidance, but we do not expect it to have a significant impact our consolidated financial statements.

3. Discontinued Operations

On September 5, 2013, we sold the net assets of Aeroflex Test Equipment Services (“ATES”), a division of our U.K. subsidiary, Aeroflex Limited, for \$18.4 million in cash. The consideration is subject to a working capital adjustment, based on the amount by which the final working capital at the date of closing differs from the target set forth in the purchase agreement. ATES provided calibration and repair services of non-Aeroflex test and measurement equipment in the United Kingdom and was previously included in our ATS segment. As a result of this sale, we recorded a gain on disposal of \$14.1 million. The gain is not subject to U.K. taxes.

We have reported the results of operations of ATES as income from discontinued operations. The prior period statement of operations has been restated to conform to the current presentation. Net sales from the ATES operations were \$2.4 million from July 1, 2013 to the date of sale and \$3.5 million for the three months ended September 30, 2012.

4. Inventories

Inventories consisted of the following:

| | September 30, 2013 | June 30, 2013 |
|-----------------|-----------------------|------------------|
| | (In thousands) | |
| Raw materials | \$ 84,114 | \$ 76,762 |
| Work in process | 56,353 | 52,221 |
| Finished goods | 31,315 | 27,533 |
| | \$ 171,782 | \$ 156,516 |

5. Intangible Assets

The components of amortizable intangible assets were as follows:

| | September 30, 2013 | | | June 30, 2013 | | |
|------------------------------|-----------------------|--------------------------|----------------------|-----------------------|--------------------------|----------------------|
| | Gross Carrying Amount | Accumulated Amortization | Total Net Book Value | Gross Carrying Amount | Accumulated Amortization | Total Net Book Value |
| | (In thousands) | | | | | |
| Developed technology | \$ 203,594 | \$ 198,228 | \$ 5,366 | \$ 201,447 | \$ 192,574 | \$ 8,873 |
| Customer related intangibles | 227,529 | 178,633 | 48,896 | 226,406 | 171,514 | 54,892 |
| Non-compete arrangements | 10,413 | 9,764 | 649 | 10,344 | 9,401 | 943 |
| Trade names | 3,377 | 2,605 | 772 | 3,332 | 2,488 | 844 |
| Total | \$ 444,913 | \$ 389,230 | \$ 55,683 | \$ 441,529 | \$ 375,977 | \$ 65,552 |

We assess goodwill and other intangible assets with indefinite lives at least annually for impairment, in the fourth quarter of our fiscal year, or more frequently if certain events or circumstances indicate an impairment may have occurred. We test goodwill for impairment at the reporting unit level, which is one level below our operating segments.

The carrying amount of goodwill, by segment, was as follows:

| | Microelectronic Solutions | Test Solutions | Total |
|---|---------------------------|----------------|------------|
| | (In thousands) | | |
| Balance at June 30, 2013 | | | |
| Goodwill | \$ 339,859 | \$ 159,284 | \$ 499,143 |
| Accumulated impairments | (90,100) | (93,400) | (183,500) |
| | 249,759 | 65,884 | 315,643 |
| Changes for the three months ended September 30, 2013 | | | |
| Translation and other adjustments | 684 | (172) | 512 |
| Balance at September 30, 2013 | | | |
| Goodwill | 340,543 | 159,112 | 499,655 |
| Accumulated impairments | (90,100) | (93,400) | (183,500) |
| | \$ 250,443 | \$ 65,712 | \$ 316,155 |

6. Restructuring Charges

The following table sets forth the charges and payments related to the restructuring liability, which is reflected in accrued expenses and other current liabilities in the accompanying condensed consolidated balance sheets and primarily relates to our ATS Wireless and Avionics/Communications (“AVComm”) groups, for the period indicated:

| | Balance | Three Months Ended | | | Balance |
|--------------------------|--|--------------------|------------------|----------------------------------|----------------------------|
| | June 30, 2013 | September 30, 2013 | | | September 30, 2013 |
| | Restructuring Liability (In thousands) | Net Additions | Cash Payments | Effect of Foreign Currency | Restructuring Liability |
| Severance costs | \$ 904 | \$ 25 | \$ (743) | \$ 15 | \$ 201 |
| Facilities closure costs | 88 | 659 | (621) | - | 126 |
| Total | \$ 992 | \$ 684 | \$ (1,364) | \$ 15 | \$ 327 |

7. Derivative Financial Instruments

We address certain financial exposures through a controlled program of risk management that includes the use of derivative financial instruments. When deemed appropriate to do so, we enter into interest rate swap derivatives to manage the effects of interest rate movements on portions of our debt. We routinely enter into foreign currency forward contracts, not designated as hedging instruments, to protect us from fluctuations in exchange rates.

Foreign Currency Contract Derivatives

Foreign currency contracts are used to protect us from fluctuations in exchange rates. Our foreign currency contracts are not designated as hedges and therefore the change in fair value is included in other income (expense) as it occurs. As of September 30, 2013, we had \$44.6 million of notional value foreign currency forward contracts maturing through October 31, 2013. Notional amounts do not quantify risk or represent assets or liabilities of the Company, but are used in the calculation of cash settlements under the contracts.

The fair values of our derivative financial instruments included in the condensed consolidated balance sheets as of September 30, 2013 and June 30, 2013 were as follows:

| (In thousands) | Asset (Liability) Derivatives | | Asset (Liability) Derivatives | |
|--|---|---------------------------|--|---------------------------|
| | September 30, 2013 | | June 30, 2013 | |
| | Location | Fair Value ⁽¹⁾ | Location | Fair Value ⁽¹⁾ |
| Derivatives not designated as hedging instruments: | | | | |
| Foreign currency forward contracts | Prepaid expenses and other current assets | \$ 396 | Accrued expenses and other current liabilities | \$ (359) |

(1)

The fair values of derivative assets and liabilities are determined based on observable market data and are considered level 2 in the fair value hierarchy.

The amounts of the gains and losses related to our derivative financial instruments not designated as hedging instruments for the three months ended September 30, 2013 and 2012 were as follows:

| Derivatives Not Designated as Hedging Instruments | Location of Gain or (Loss) Recognized in Earnings on Derivative | Amount of Gain or (Loss) Recognized in Earnings on Derivative | |
|---|---|---|---------|
| | | Three Months Ended September 30, 2013 | 2012 |
| | | (In thousands) | |
| Foreign currency forward contracts | Other income (expense) | \$ 755 | \$ (25) |

8. Long Term Debt and Credit Agreements

As of September 30, 2013, we were in compliance with all of the financial covenants contained in our senior secured credit facility.

Interest paid was \$6.9 million and \$9.2 million for the three months ended September 30, 2013 and 2012, respectively. Accrued interest of \$2.3 million and \$2.5 million was included in accrued expenses and other current liabilities at September 30, 2013 and June 30, 2013, respectively.

The fair value of our debt instruments was as follows:

| | As of September 30, 2013 (In thousands) | |
|-----------------------------------|--|----------------------|
| | Carrying Amount | Estimated Fair Value |
| Senior secured term loan facility | \$ 587,000 | \$ 591,036 |

As of June 30, 2013, our total debt had a carrying value of \$587.0 million and a fair value of \$585.5 million.

The estimated fair value of our senior secured term loan facility was based on quoted prices and is considered a Level 1 measurement.

9. Accumulated Other Comprehensive Income (Loss)

The changes in accumulated other comprehensive income (loss), net of tax, for the three months ended September 30, 2013 were as follows:

| | Net Minimum Pension Liability (In thousands) | Net Cumulative Translation Adjustment | Total |
|---|---|--|-------------|
| Accumulated other comprehensive income (loss) at June 30, 2013 | \$ (1,403) | \$ (42,003) | \$ (43,406) |
| Other comprehensive income (loss) | | | |
| Other comprehensive income (loss) before reclassifications | 16 | 10,550 | 10,566 |
| Amounts reclassified from accumulated other comprehensive income | 9 | - | 9 |
| Total other comprehensive income (loss) | 25 | 10,550 | 10,575 |
| Accumulated other comprehensive income (loss) at September 30, 2013 | \$ (1,378) | \$ (31,453) | \$ (32,831) |

10. Share-Based Payment ArrangementsRestricted Stock Units

During the three months ended September 30, 2013, the compensation committee awarded restricted stock units, or RSUs, covering a total of 60,000 shares. The average grant date fair value per share of these RSUs was \$7.00 and they vest in equal tranches over service periods between three and four years.

11. Income (Loss) Per Common Share

Our consolidated statements of operations present basic and diluted income (loss) per common share. Basic income (loss) per common share is computed by dividing income (loss) by the weighted average number of common shares outstanding for the period. Diluted income (loss) per common share reflects the dilutive effects of RSUs and performance restricted stock units, or PRSUs, if any. The treasury stock method is used to determine the dilutive effect of these potentially dilutive securities.

Due to the loss from continuing operations for the three months ended September 30, 2013, 1.3 million shares of common stock equivalents (which includes PRSUs that have been earned, but are subject to the continued employment of the respective participants with the Company) were excluded from diluted income (loss) per common share because they were anti-dilutive. Also, if all maximum performance metrics are achieved, an additional 727,000 PRSUs could potentially vest. Due to the loss from continuing operations for the three months ended September 30, 2012, 340,000 shares of common stock equivalents were excluded from diluted income (loss) per common share because they were anti-dilutive.

12. Legal Matters

To resolve all those outstanding violations of the Arms Export Control Act, or AECA, and the International Traffic in Arms Regulations, or ITAR, during the period from 1999 to 2009 that were disclosed by us voluntarily to the U.S. State Department concerning space related hardware items that were exported to China and, without the requisite State Department licenses, to end users in numerous other foreign countries, without admitting or denying the allegation of the violations, we have entered into a Consent Agreement effectively as of August 6, 2013, with the U.S. Department of State, Office of Defense Trade Controls Compliance. The Consent Agreement involves, among other things, a fine of \$8.0 million payable over a two year period, \$4.0 million of which is suspended and eligible for credit based on pre and post Consent Agreement compliance expenditures and investments made by the Company and approved by the State Department. During fiscal 2013, we recorded a charge of \$8.0 million representing the legal obligation to the State Department under the then proposed terms of the Consent Agreement. In accordance with the terms of the Consent Agreement, in August 2013 we paid \$2.0 million of the fine. Going forward, the Consent Agreement will not impact our ability to transact business internationally.

In March 2005, we sold the net assets of our shock and vibration control device manufacturing business, which we refer to as VMC. Under the terms of the sale agreements, we retained certain liabilities relating to adverse environmental conditions that existed at the premises occupied by VMC as of the date of sale. We recorded a liability for the estimated remediation costs related to adverse environmental conditions that existed at the VMC premises when it was sold. The accrued environmental liability at September 30, 2013 was \$1.3 million, of which \$300,000 was expected to be paid within one year.

We are also involved in various other claims and legal actions that arise in the ordinary course of business. We do not believe that the ultimate resolution of any of these actions will have a material adverse effect on our business, results of operations, financial position, liquidity or capital resources.

13. Income Taxes

The income tax benefit was \$3.4 million for the three months ended September 30, 2013 on a pre-tax loss from continuing operations of \$7.3 million. We recorded an income tax benefit for the three months ended September 30, 2012 of \$2.5 million on a pre-tax loss from continuing operations of \$17.0 million. The effective income tax rate for both periods differed from the amount computed by applying the U.S. federal income tax rate to income from continuing operations before taxes primarily due to foreign, state and local income taxes, including U.S. income tax on certain foreign income that we anticipate will be repatriated to the U.S.

The income tax benefit for the three months ended September 30, 2013 reflects a discrete benefit of \$1.0 million relating to a reduction in the statutory income tax rate in the U.K. The income tax benefit for the three months ended September 30, 2012 reflects a discrete benefit of \$116,000 relating to a statutory income tax rate reduction in the U.K. and a reduction of a deferred tax liability related to the repatriation of funds from our Chinese subsidiary largely offset by a true-up of a deferred tax item in the U.K.

Absent the discrete items, the effective tax rates were 32% and 14% for the three months ended September 30, 2013 and 2012, respectively. The current year's provision was a combination of a U.S. tax benefit on a domestic book loss and a foreign tax benefit on foreign book income. The prior year's provision was a combination of a U.S. tax expense on domestic earnings and a foreign tax expense on foreign earnings.

In the three months ended September 30, 2013 and 2012, we paid income taxes of \$11.6 million and \$1.2 million and received refunds of \$4,000 and \$843,000, respectively.

14. Business Segments

We are a global provider of radio frequency, or RF, and microwave integrated circuits, components and systems used in the design, development and maintenance of technically demanding, high-performance wireless communication systems. Our solutions include highly specialized microelectronic components and test and measurement equipment used by companies in the space, avionics, defense, commercial wireless communications, medical and other markets. Our sales to agencies of the United States government or to prime defense contractors or subcontractors of the United States government were approximately 33% for both of the three month periods ended September 30, 2013 and 2012. No customer constituted more than 10% of sales during any of the periods presented. Inter-segment sales were not material and have been eliminated from the tables below.

The majority of our operations are located in the United States. We also have operations in Europe and Asia, with our most significant non-U.S. operations in the U.K. Net sales from facilities located in the U.K. were \$30.6 million and \$31.8 million for the three months ended September 30, 2013 and 2012, respectively. Total assets of the U.K. operations were \$203.9 million as of September 30, 2013 and \$177.3 million as of June 30, 2013.

Net sales, based on the customers' locations, attributed to the United States and other regions were as follows:

| | Three Months Ended September 30, | |
|--------------------------|----------------------------------|------------|
| | 2013 | 2012 |
| | (In thousands) | |
| United States of America | \$ 84,727 | \$ 79,792 |
| Europe and Middle East | 19,685 | 32,290 |
| Asia and Australia | 23,482 | 22,149 |
| Other regions | 4,838 | 3,404 |
| | \$ 132,732 | \$ 137,635 |

We organize our operations into two segments: Aeroflex Microelectronic Solutions, or AMS, and Aeroflex Test Solutions, or ATS. We engineer, manufacture and market a diverse range of products in each of our segments. The segment data which follows, reflects a reclassification of our frequency synthesizer product line from our ATS segment to our AMS segment for all periods presented to better align it with its end markets. Our synthesizer reporting unit had sales of \$3.7 million and \$3.6 million for the three months ended September 30, 2013 and 2012, respectively.

AMS offers a broad range of microelectronics products and is a leading provider of high-performance, high reliability specialty microelectronics components. Its products include high reliability, or HiRel, microelectronics/semiconductors, RF and microwave components, mixed-signal/digital Application Specific Integrated Circuits ("ASICs") and motion control products. ATS is a leading provider of a broad line of specialized test and measurement equipment. Its products include wireless test equipment, military radio and private mobile radio test equipment, avionics test equipment, synthetic test equipment and other general purpose test equipment.

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Selected financial data by segment was as follows:

| | Three Months Ended September 30, | |
|--|----------------------------------|-------------|
| | 2013 | 2012 |
| | (In thousands) | |
| Net sales | | |
| - Microelectronic solutions ("AMS") | \$ 74,006 | \$ 78,072 |
| - Test solutions ("ATS") | 58,726 | 59,563 |
| Net sales | \$ 132,732 | \$ 137,635 |
| Segment adjusted operating income | | |
| - AMS | \$ 12,458 | \$ 16,205 |
| - ATS | 2,809 | 920 |
| - Corporate expense | (3,218) | (4,026) |
| Adjusted operating income | 12,049 | 13,099 |
| Amortization of acquired intangibles | | |
| - AMS | (6,724) | (8,966) |
| - ATS | (3,794) | (5,614) |
| Restructuring charges | | |
| - AMS | (5) | (204) |
| - ATS | (679) | (3,063) |
| Inventory write-off related to discontinued product line - ATS | 7 | - |
| Share-based compensation | | |
| - AMS | (238) | (111) |
| - ATS | (231) | (67) |
| - Corporate | (413) | (458) |
| Business acquisition and divestiture related costs - Corporate | - | (597) |
| Current period impact of acquisition related adjustments | | |
| - AMS | 25 | (9) |
| - ATS | 21 | 22 |
| - Corporate | (55) | (55) |
| Operating income (loss) (GAAP) | (37) | (6,023) |
| Interest expense | (7,252) | (10,078) |
| Write-off of deferred financing costs | - | (597) |
| Other income (expense), net | (51) | (289) |
| Income (loss) from continuing operations before income taxes | \$ (7,340) | \$ (16,987) |

Management evaluates the operating results of our two segments based upon Adjusted EBITDA (as defined in our credit agreement) as well as adjusted operating income, which is pre-tax operating income before certain non-cash, non-recurring and other items. We have set out above our adjusted operating income by segment and in the aggregate, and have provided a reconciliation of adjusted operating income to operating income (loss) on a GAAP basis and income (loss) from continuing operations before income taxes for the periods presented.

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

Unless the context requires otherwise: (i) "we," "our," "us," or the "Company" refer to Aeroflex Holding Corp. and its subsidiaries; (ii) "fiscal" refers to the twelve months ended June 30 of the applicable year. For example, "fiscal 2013" refers to the twelve months ended June 30, 2013.

Forward-Looking Statements

This report contains "forward-looking statements." All statements other than statements of historical fact are "forward-looking statements" for purposes of the U.S. federal and state securities laws. These statements may be identified by the use of forward looking terminology such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "might," "plan," "potential," "predict," "should" or "will" or the negative thereof or other variations thereon or comparable terminology.

We have based these forward-looking statements on our current expectations, assumptions, estimates and projections. While we believe these expectations, assumptions, estimates and projections are reasonable, such forward-looking statements are only predictions and involve known and unknown risks and uncertainties, many of which are beyond our control. These and other important factors may cause our actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by these forward-looking statements. A listing of some of the key factors that could cause actual results to differ from our expectations is included under the caption "Risk Factors" in our fiscal 2013 Form 10-K.

Given these risks and uncertainties, you are cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to update or revise any forward-looking statements, either to reflect new developments, or for any other reason, except as required by law.

Overview

Company Background

We are a leading global provider of RF and microwave integrated circuits, components and systems used in the design, development and maintenance of technically demanding, high-performance wireless communication systems. Our solutions include highly specialized microelectronic components and test and measurement equipment used by companies in the: (i) commercial wireless communications (ii) space, avionics and defense; and (iii) medical and other markets. We have targeted customers in these end markets because we believe our solutions address their technically demanding requirements. We were founded in 1937 and have proprietary technology that is based on extensive know-how and a long history of research and development focused on specialized technologies, often in collaboration with our customers.

Business Segments

Our business segments and major products included in each segment are as follows:

Aeroflex Microelectronic Solutions ("AMS")

HiRel microelectronics/semiconductors

RF and microwave components

Mixed-signal/digital Application Specific Integrated Circuits ("ASICs")

Motion control products

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Aeroflex Test Solutions (“ATS”)

Wireless test equipment
 Military radio and Private Mobile Radio, or PMR, test equipment
 Avionics test equipment
 Synthetic test equipment
 General purpose test equipment

Results of Operations

The following table sets forth our historical results of operations as a percentage of net sales for the periods indicated below:

| | Three Months Ended September 30, | | | |
|--|----------------------------------|---|--------|---|
| | 2013 | % | 2012 | % |
| Net sales | 100.0 | % | 100.0 | % |
| Cost of sales | 50.4 | | 50.4 | |
| Gross profit | 49.6 | | 49.6 | |
| Operating expenses: | | | | |
| Selling, general and administrative costs | 25.0 | | 25.8 | |
| Research and development costs | 16.2 | | 15.2 | |
| Amortization of acquired intangibles | 7.9 | | 10.6 | |
| Restructuring charges | 0.5 | | 2.4 | |
| Total operating expenses | 49.6 | | 54.0 | |
| Operating income (loss) | - | | (4.4) | |
| Other income (expense): | | | | |
| Interest expense | (5.5) | | (7.3) | |
| Write-off of deferred financing costs | - | | (0.4) | |
| Other income (expense), net | - | | (0.2) | |
| Income (loss) from continuing operations before income taxes | (5.5) | | (12.3) | |
| Provision (benefit) for income taxes | (2.6) | | (1.8) | |
| Income (loss) from continuing operations | (2.9) | | (10.5) | |
| Discontinued operations: | | | | |
| Income from discontinued operations, net of tax | 0.3 | | 0.3 | |
| Gain on disposal of operations, net of tax | 10.6 | | - | |
| Income from discontinued operations | 10.9 | | 0.3 | |
| Net income (loss) | 8.0 | % | (10.2) | % |

The end markets that we operate in continue to be challenged by worldwide economic factors including the uncertainty over U.S. government spending, which has caused customers to be more conservative with their buying patterns.

Three Months Ended September 30, 2013 Compared to Three Months Ended September 30, 2012

On September 5, 2013, we sold the net assets of Aeroflex Test Equipment Services (“ATES”), a division of our U.K. subsidiary, Aeroflex Limited, for \$18.4 million in cash. ATES provided calibration and repair services of non-Aeroflex test and measurement equipment in the United Kingdom and was previously included in our ATS segment. As a result of this sale the results of ATES are reported in income from discontinued operations in all periods, and we recorded a gain on disposal of \$14.1 million. The gain is not subject to U.K. taxes.

Net Sales. Net sales decreased \$4.9 million, or 4%, to \$132.7 million for the three months ended September 30, 2013 from \$137.6 million for the three months ended September 30, 2012.

Net Sales

| Three Months Ended | AMS | % of Consolidated Net Sales | ATS | % of Consolidated Net Sales | Total |
|--|-----------|-----------------------------|-----------|-----------------------------|------------|
| September 30, (In thousands, except percentages) | | | | | |
| 2013 | \$ 74,006 | 55.8 % | \$ 58,726 | 44.2 % | \$ 132,732 |
| 2012 | \$ 78,072 | 56.7 % | \$ 59,563 | 43.3 % | \$ 137,635 |

Net sales in the AMS segment decreased \$4.1 million, or 5%, to \$74.0 million for the three months ended September 30, 2013 from \$78.1 million for the three months ended September 30, 2012. This sales decrease was primarily attributable to volume reductions of HiRel microelectronics/semiconductors due to government budgetary constraints that have caused delays on defense and space programs; offset in part by increased sales volume of mixed-signal/digital ASICs, which are predominantly sold to our commercial customers.

Net sales from continuing operations in the ATS segment decreased \$837,000, or 1%, to \$58.7 million for the three months ended September 30, 2013 from \$59.6 million for the three months ended September 30, 2012. Reductions in the sales volume of nearly all of our ATS product groups were partially offset by a \$2.7 million volume driven increase in sales of Avionics test equipment.

Gross Profit. Gross profit equals net sales less cost of sales. Cost of sales includes materials, direct labor, amortization of capitalized software development costs and overhead expenses such as engineering labor, fringe benefits, depreciation, allocable occupancy costs and manufacturing supplies.

On a consolidated basis, gross profit was \$65.8 million, or 49.6%, of net sales for the three months ended September 30, 2013 compared to \$68.2 million, or 49.6%, of net sales for the three months ended September 30, 2012.

Gross Profit

| Three Months Ended | AMS | % of Net Sales | ATS | % of Net Sales | Total | % of Net Sales |
|--|-----------|----------------|-----------|----------------|-----------|----------------|
| September 30, (In thousands, except percentages) | | | | | | |
| 2013 | \$ 34,294 | 46.3 % | \$ 31,524 | 53.7 % | \$ 65,818 | 49.6 % |

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| | | | | | | | | | | | | |
|------|----|--------|------|---|----|--------|------|---|----|--------|------|---|
| 2012 | \$ | 37,783 | 48.4 | % | \$ | 30,439 | 51.1 | % | \$ | 68,222 | 49.6 | % |
|------|----|--------|------|---|----|--------|------|---|----|--------|------|---|

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Gross margins in the AMS segment were 46.3% for the three months ended September 30, 2013 and 48.4% for the three months ended September 30, 2012. Gross profit decreased \$3.5 million for the three months ended September 30, 2013 as compared to the three months ended September 30, 2012 largely due to the reduction in sales, including a reduction in sales of HiRel microelectronics/semiconductors which have margins higher than the segment average. The decrease in gross margin is principally attributable to a reduction in sales of HiRel microelectronics/semiconductors.

Gross margins in the ATS segment were 53.7% for the three months ended September 30, 2013 and 51.1% for the three months ended September 30, 2012. Gross profit increased \$1.1 million, and gross margins improved for the three months ended September 30, 2013 as compared to the three months ended September 30, 2012 largely due to an increase in software content in our wireless products, which has a higher margin than the segment average.

Selling, General and Administrative Costs. Selling, general and administrative (“SG&A”) costs include office and management salaries, fringe benefits, commissions, insurance and professional fees.

On a consolidated basis, SG&A costs decreased \$2.4 million, or 7%, when comparing the three months ended September 30, 2013 to the three months ended September 30, 2012. As a percentage of sales, SG&A decreased to 25.0% from 25.8% when comparing the three months ended September 30, 2013 to the three months ended September 30, 2012.

Selling, General and Administrative Costs

| Three Months Ended | AMS | % of Net Sales | ATS | % of Net Sales | Corporate | Total | % of Net Sales |
|--------------------|-----------|----------------|-----------|----------------|-----------|-----------|----------------|
| September 30, 2013 | \$ 12,827 | 17.3 % | \$ 16,655 | 28.4 % | \$ 3,686 | \$ 33,168 | 25.0 % |
| September 30, 2012 | \$ 12,745 | 16.3 % | \$ 17,639 | 29.6 % | \$ 5,136 | \$ 35,520 | 25.8 % |

(In thousands, except percentages)

In the AMS segment, costs were virtually unchanged, but, as a percentage of sales, increased 1.0% due to the reduction in sales.

In the ATS segment, SG&A costs decreased \$984,000, primarily due to cost reduction activities in our Wireless group, and to a lesser extent, actions recently initiated to restructure our AVComm group.

Corporate general and administrative costs decreased \$1.4 million, primarily due to reductions in employee related expenses and legal fees, combined with acquisition related costs occurring in the three months ended September 30, 2012 that did not recur.

Research and Development Costs. Research and development costs include materials, engineering labor and allocated overhead.

On a consolidated basis, research and development costs increased \$607,000 for the three months ended September 30, 2013 from the three months ended September 30, 2012, primarily due to increased costs for the development of ATS Wireless products.

Research and Development Costs

| Three Months Ended | | % of Net Sales | | % of Net Sales | | % of Net Sales | | | |
|------------------------------------|----------|----------------|-----|----------------|-------|----------------|-----------|------|---|
| September 30, | AMS | | ATS | | Total | | | | |
| (In thousands, except percentages) | | | | | | | | | |
| 2013 | \$ 9,224 | 12.5 | % | \$ 12,261 | 20.9 | % | \$ 21,485 | 16.2 | % |
| 2012 | \$ 8,952 | 11.5 | % | \$ 11,926 | 20.0 | % | \$ 20,878 | 15.2 | % |

Restructuring Charges. On a consolidated basis, restructuring charges were \$684,000 for the three months ended September 30, 2013 compared to \$3.3 million for the three months ended September 30, 2012. For both of the three month periods ended September 30, 2013 and 2012, the restructuring charges were primarily related to cost savings initiatives in the ATS segment which resulted in reductions in personnel at various locations worldwide.

Interest Expense. Interest expense decreased by \$2.8 million to \$7.3 million for the three months ended September 30, 2013 from \$10.1 million for the three months ended September 30, 2012. Interest expense decreased due to: (i) a lower outstanding principal amount resulting from voluntary debt payments made throughout fiscal 2013 totaling \$60 million; and (ii) a 125 basis point interest rate reduction in connection with the May 29, 2013 amendment to our senior secured credit facility.

Income Taxes. The income tax benefit was \$3.4 million for the three months ended September 30, 2013 on a pre-tax loss from continuing operations of \$7.3 million. We recorded an income tax benefit for the three months ended September 30, 2012 of \$2.5 million on a pre-tax loss from continuing operations of \$17.0 million. The effective income tax rate for both periods differed from the amount computed by applying the U.S. federal income tax rate to income from continuing operations before taxes primarily due to foreign, state and local income taxes, including U.S. income tax on certain foreign income that we anticipate will be repatriated to the U.S.

Income (Loss) from Continuing Operations. Loss from continuing operations was \$(4.0) million for the three months ended September 30, 2013 and \$(14.5) million for the three months ended September 30, 2012. The \$10.5 million improvement resulted primarily from reductions in operating expenses of \$8.4 million and interest expense of \$2.8 million, partially offset by decreased gross profit of \$2.4 million.

Discontinued Operations. As a result of the sale of ATES, its results of operations have been removed from continuing operations for all periods. Net sales from the ATES operations were \$2.4 million from July 1, 2013 to the date of sale and \$3.5 million for the three months ended September 30, 2012. The gain on disposal was \$14.1 million.

Net Income (Loss). Net income (loss) was \$10.5 million for the three months ended September 30, 2013 and \$(14.1) million for the three months ended September 30, 2012.

Liquidity and Capital Resources

As of September 30, 2013, we had \$62.8 million of cash and cash equivalents, \$288.3 million in working capital and our current ratio was 3.53 to 1, versus \$39.4 million, \$262.8 million and 3.04 to 1, respectively, at June 30, 2013.

Our principal liquidity requirements are to service our debt and interest and meet our working capital and capital expenditure needs. As of September 30, 2013, we had \$587.0 million of debt outstanding, all of which was long-term, under our senior secured term loan facility. Additionally, at September 30, 2013, we were able to borrow \$57.1 million under the revolving portion of our senior secured credit facility, of which none was outstanding.

The financial covenant was eliminated from the term loan portion of our senior secured credit facility, when it was amended on May 29, 2013. To the extent that, at quarter end, we have outstanding borrowings under the revolving credit portion of our senior secured term loan facility, we would be subject to a financial covenant based on Adjusted EBITDA. Adjusted EBITDA is defined as EBITDA (net income (loss) before interest expense, income taxes, depreciation and amortization), adjusted to add back or subtract certain non-cash, non-recurring and other items, as permitted by our debt agreement. Our use of the term Adjusted EBITDA may vary from others in our industry. EBITDA and Adjusted EBITDA are not measures of operating income (loss), performance or liquidity under U.S. GAAP and are subject to important limitations. A reconciliation of net income (loss), which is a U.S. GAAP measure of our operating results, to Adjusted EBITDA, as defined in our debt agreement, is as follows:

| | Three Months Ended September 30, | |
|---|----------------------------------|-------------|
| | 2013 | 2012 |
| | (In thousands) | |
| Net income (loss) | \$ 10,507 | \$ (14,139) |
| Income from discontinued operations | (14,462) | (377) |
| Income (loss) from continuing operations | (3,955) | (14,516) |
| Interest expense | 7,252 | 10,078 |
| Provision (benefit) for income taxes | (3,385) | (2,471) |
| Depreciation and amortization | 16,449 | 20,123 |
| EBITDA | 16,361 | 13,214 |
| Restructuring related costs, including pro forma savings(a) | 684 | 4,608 |
| Share-based compensation | 882 | 636 |
| Write-off of deferred financing costs | - | 597 |
| Other defined items(b) | 14 | 797 |
| Adjusted EBITDA | \$ 17,941 | \$ 19,852 |

- (a) Primarily reflects costs associated with the reorganization of our European operations and consolidation of certain of our U.S. operations. Pro forma savings reflect the costs that we estimate would have been eliminated during the fiscal year in which a restructuring occurred had the restructuring occurred as of the first day of that fiscal year. Pro forma savings were estimated to be \$0 and \$1.3 million for the three months ended September 30, 2013 and 2012, respectively. The pro forma savings for the three months ended September 30, 2012 includes an additional \$906,000 which was not reflected in our Adjusted EBITDA as reported in our September 30, 2012 report on Form 10-Q as it relates to restructuring activities recorded throughout fiscal 2013.
- (b) Reflects other adjustments required in calculating our debt covenant compliance. These other defined items include legal fees related to certain litigation and business acquisition and divestiture related costs.

The maximum leverage ratio of total debt (less up to \$15.0 million of unrestricted cash) to Adjusted EBITDA, as defined in our senior secured credit facility, as amended, is only in effect if as of the last day of the fiscal quarter there are any outstanding borrowings under our senior secured revolving credit facility. The maximum leverage ratio permitted for the twelve months ended September 30, 2013 was 5.50, whereas our actual leverage ratio was 4.58.

As of September 30, 2013, there were no outstanding amounts under our senior secured revolving credit facility, therefore, the maximum leverage ratio covenant was not applicable. As of September 30, 2013, we were in compliance with all of the covenants contained in our debt agreement.

Our senior secured credit facility contains restrictions on our activities, including but not limited to covenants that restrict us and our restricted subsidiaries, as defined in our senior secured credit facility, from:

- incurring additional indebtedness and issuing disqualified stock or preferred stock;
- making certain investments or other restricted payments;
- paying dividends and making other distributions with respect to capital stock, or repurchasing, redeeming or retiring capital stock or subordinated debt;
- selling or otherwise disposing of assets;
- under certain circumstances, issuing or selling equity interests;
- creating liens on our assets;
- consolidating or merging with, or acquiring in excess of specified annual limitations, another business, or selling or disposing of all or substantially all of our assets; and
- entering into certain transactions with our affiliates.

If for any reason we fail to comply with the covenants in the senior secured credit facility, we would be in default under the terms of the agreements governing our outstanding debt. If such a default were to occur, the lenders under the senior secured credit facility could elect to declare all amounts outstanding thereunder immediately due and payable, and the lenders would not be obligated to continue to advance funds to us. If the amounts outstanding under these debt agreements are accelerated, our assets may not be sufficient to repay in full the amounts owed.

We expect that cash generated from operating activities and availability under the revolving portion of our senior secured credit facility will be our principal sources of liquidity. Our ability to make payments on and to refinance our indebtedness and to fund working capital needs and planned capital expenditures will depend on our ability to generate cash in the future. This, to a certain extent, is subject to general economic, financial, competitive and other factors that are beyond our control. In addition, to the extent we have consolidated excess cash flows, as defined in the credit agreement governing the senior secured credit facility, we must use specified portions of the excess cash flows to prepay the senior secured credit facility. Based on our current level of operations, we believe our cash flow from operations and available borrowings under our senior secured credit facility will be adequate to meet our liquidity needs for at least the next twelve months. We cannot assure you, however, that our business will generate sufficient cash flow from operations, or those future borrowings will be available under the senior secured credit facility in an amount sufficient to enable us to repay our indebtedness at maturity or to fund other liquidity needs. We may need to refinance all or a portion of our indebtedness on or before the maturity thereof. We cannot assure you that we will be able to refinance any of our indebtedness on commercially reasonable terms or at all.

Cash Flows

For the three months ended September 30, 2013, our cash flow provided by operations was \$7.7 million. Our investing activities provided cash of \$13.2 million, primarily due to \$18.4 million of proceeds from the sale of ATES, partially offset by capital expenditures of \$5.3 million. Our financing activities used cash of \$901,000.

For the three months ended September 30, 2012, our cash flow provided by operations was \$32.0 million, which included cash generated by reductions in accounts receivable of \$33.0 million. Our investing activities used cash of \$3.8 million, primarily for capital expenditures of \$4.1 million. Our financing activities used cash of \$25.0 million,

primarily for voluntary debt prepayments.

The decrease of \$24.3 million in cash provided by operating activities resulted primarily from a current quarter increase in inventory of \$14.6 million and increased income tax payments of \$10.4 million.

Capital Expenditures

Capital expenditures were \$5.3 million and \$4.1 million for the three months ended September 30, 2013 and 2012, respectively. Our capital expenditures consist primarily of equipment replacements.

Contractual Obligations

There have been no material changes in our contractual obligations as disclosed in our fiscal 2013 Form 10-K.

Off-Balance Sheet Arrangements

We do not maintain any off-balance sheet arrangements, transactions, obligations or other relationships with unconsolidated entities that would be expected to have material current or future effect upon our results of operations or financial condition.

Critical Accounting Policies and Estimates

Information regarding our critical accounting policies and estimates appears within the “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in our fiscal 2013 Form 10-K. During the three month period ended September 30, 2013, there were no significant changes to any critical accounting policies or to the related estimates and judgments involved in applying those policies.

Recent Accounting Pronouncements

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our consolidated financial statements, see Note 2 of Notes to Unaudited Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk. We are subject to interest rate risk in connection with borrowings under our senior secured credit facility, including any outstanding borrowings under our revolving credit facility. We currently do not have interest rate swap agreements hedging this debt. As of September 30, 2013, \$587.0 million was outstanding under the term-loan portion of the senior secured credit facility, bearing interest at 4.50% based on the adjusted LIBOR rate, which consists of a floor of 100 basis points, plus an applicable margin of 350 basis points above the floor. Our outstanding debt balance is subject to variable interest rates dependent upon fluctuations of the LIBOR rate. Based on the LIBOR rate at September 30, 2013, which was 0.25%, an increase of 1% in interest rates would only result in a 0.25% increase on the interest rate relating to our outstanding borrowings due to the 1.00% LIBOR floor, or a \$1.5 million increase in our annual interest expense. An increase of 1% in the LIBOR rate above the 1.00% floor would result in a \$6.0 million increase in our annual interest expense. In addition, as of September 30, 2013, our revolving credit facility of \$57.1 million, which would bear interest at 3.75% based on the LIBOR rate of 0.25% plus 350 basis points, was undrawn. Assuming the entire amount available to us was outstanding, a 1% change in interest rates would result in a \$579,000 change in our annual interest expense. Any debt we incur in the future may also bear interest at floating rates.

Foreign Currency Risk. Foreign currency contracts are used to protect us from exchange rate fluctuation from the time customers are invoiced in local currency until such currency is exchanged for U.S. dollars. We periodically enter into foreign currency contracts, which are not designated as hedges, and the change in the fair value is included in income currently within other income (expense). As of September 30, 2013, we had \$44.6 million of notional value foreign currency forward contracts maturing through October 31, 2013. Notional amounts do not quantify risk or represent assets or liabilities, but are used in the calculation of cash settlements under the contracts. The fair value of these contracts at September 30, 2013 was an asset of \$396,000. If foreign currency exchange rates (primarily the British pound and the Euro) change by 10% from the levels at September 30, 2013, the effect on our comprehensive income would be approximately \$19.0 million.

Inflation Risk. Inflation has not had a material impact on our results of operations or financial condition during the preceding three years.

ITEM 4. CONTROLS AND PROCEDURES

Our disclosure controls and procedures under the Securities Exchange Act of 1934, as amended, are designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the Securities and Exchange Commission. Our disclosure controls and procedures are also designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure. Our Principal Executive Officer and our Principal Financial Officer, with the assistance from other members of management, have reviewed the effectiveness of our disclosure controls and procedures as of September 30, 2013 and, based on their evaluation, have concluded that the disclosure controls and procedures were effective as of such date.

There have been no changes in our internal control over financial reporting that occurred during the quarter ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

There have been no material changes in our legal proceedings disclosed in our fiscal 2013 Form 10-K.

Item 1A. Risk Factors

There have been no material changes in our risk factors disclosed in our fiscal 2013 Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

Item 6. Exhibits

See index of exhibits included on page 26.

SIGNATURE

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

AEROFLEX HOLDING CORP.

/s/ John Adamovich, Jr.
John Adamovich, Jr.
Senior Vice President and
Chief Financial Officer
(Principal Financial Officer)

November 7, 2013

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EXHIBIT INDEX

| Exhibit No. | Exhibit Description |
|-------------|--|
| 31.1 | Certification pursuant to Rules 13a-14(a)/15d-14a as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (Chief Executive Officer) |
| 31.2 | Certification pursuant to Rules 13a-14(a)/15d-14a as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (Chief Financial Officer) |
| 31.3 | Certification pursuant to Rules 13a-14(a)/15d-14a as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (Principal Accounting Officer) |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (Chief Executive Officer) |
| 32.2 | Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (Chief Financial Officer) |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |