

INTEVAC INC

FORM 10-Q (Quarterly Report)

Filed 08/10/98 for the Period Ending 06/27/98

Address	3560 BASSETT STREET SANTA CLARA, CA, 95054
Telephone	4089869888
CIK	0001001902
Symbol	IVAC
SIC Code	3559 - Special Industry Machinery, Not Elsewhere Classified
Industry	Industrial Machinery & Equipment
Sector	Industrials
Fiscal Year	12/31

INTEVAC INC

FORM 10-Q (Quarterly Report)

Filed 8/10/1998 For Period Ending 6/27/1998

Address	356O BASSETT ST SANTA CLARA, California 95054
Telephone	408-986-9888
CIK	0001001902
Industry	Computer Storage Devices
Sector	Technology
Fiscal Year	12/31

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 27, 1998

OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____ .

COMMISSION FILE NUMBER 0-26946

INTEVAC, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

CALIFORNIA
(STATE OR OTHER JURISDICTION OF
INCORPORATION OR ORGANIZATION)

94-3125814
(IRS EMPLOYER IDENTIFICATION NO.)

3550 BASSETT STREET
SANTA CLARA, CALIFORNIA 95054
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICE, INCLUDING ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (408) 986-9888

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

On June 27, 1998 approximately 11,960,024 shares of the Registrant's Common Stock, no par value, were outstanding.

INTEVAC, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

INTEVAC, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS)

	JUNE 27, 1998	DECEMBER 31, 1997
	-----	-----
	(UNAUDITED)	
ASSETS		
Current assets:		
Cash and cash equivalents.....	\$ 765	\$ 3,338
Short-term investments.....	66,272	67,804
Accounts receivable, net of allowances of \$1,746 and \$1,505 at June 27, 1998 and December 31, 1997, respectively.....	8,714	9,634
Inventories.....	24,837	35,915
Short-term note receivable, net of allowance of \$395 at June 27, 1998 and December 31, 1997.....	--	--
Prepaid expenses and other current assets.....	680	641
Deferred tax asset.....	6,572	6,572
	-----	-----
Total current assets.....	107,840	123,904
Property, plant, and equipment, net.....	14,137	13,760
Investment in 601 California Avenue LLC.....	2,431	2,431
Goodwill and other intangibles.....	4,347	5,344
Debt issuance costs.....	1,864	2,029
Deferred tax assets and other assets.....	2,434	326
	-----	-----
Total assets.....	\$133,053	\$147,794
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable.....	\$ 4,414	\$ 4,585
Accrued payroll and related liabilities.....	2,729	1,949
Other accrued liabilities.....	10,788	10,304
Customer advances.....	10,847	28,247
Net liabilities of discontinued operations.....	--	794
	-----	-----
Total current liabilities.....	28,778	45,879
Convertible notes.....	57,500	57,500
Long-term notes payable & other long-term liabilities.....	1,960	1,980
Shareholders' equity:		
Common stock, no par value.....	15,237	17,336
Retained earnings.....	29,578	25,099
	-----	-----
Total shareholders' equity.....	44,815	42,435
	-----	-----
Total liabilities and shareholders' equity.....	\$133,053	\$147,794
	=====	=====

See accompanying notes.

INTEVAC, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

(UNAUDITED)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JUNE 27, 1998	JUNE 28, 1997	JUNE 27, 1998	JUNE 28, 1997
Net revenues.....	\$35,801	\$33,763	\$70,036	\$64,904
Cost of net revenues.....	26,758	23,622	50,332	44,619
Gross profit.....	9,043	10,141	19,704	20,285
Operating expenses:				
Research and development.....	3,398	1,902	6,960	4,462
Selling, general and administrative.....	2,946	2,821	6,051	5,421
Restructuring.....	--	--	1,164	--
Total operating expenses.....	6,344	4,723	14,175	9,883
Operating income.....	2,699	5,418	5,529	10,402
Interest expense.....	(1,057)	(1,048)	(2,073)	(1,448)
Interest income and other, net.....	959	1,218	1,730	1,973
Income from continuing operations before income taxes.....	2,601	5,588	5,186	10,927
Provision for income taxes.....	857	2,011	1,712	3,934
Income from continuing operations.....	1,744	3,577	3,474	6,993
Gain from discontinued operations, net of applicable income taxes.....	473	--	1,005	--
Net income.....	\$ 2,217	\$ 3,577	\$ 4,479	\$ 6,993
Basic earnings per share:				
Income from continuing operations.....	\$ 0.14	\$ 0.29	\$ 0.29	\$ 0.56
Net income.....	\$ 0.18	\$ 0.29	\$ 0.37	\$ 0.56
Shares used in per share amounts.....	12,111	12,533	12,151	12,519
Diluted earnings per share:				
Income from continuing operations.....	\$ 0.14	\$ 0.26	\$ 0.28	\$ 0.52
Net income.....	\$ 0.18	\$ 0.26	\$ 0.36	\$ 0.52
Shares used in per share amounts.....	12,440	15,861	12,476	14,995

See accompanying notes.

INTEVAC, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

(UNAUDITED)

	SIX MONTHS ENDED	
	JUNE 27, 1998	JUNE 28, 1997
OPERATING ACTIVITIES		
Net income.....	\$ 4,479	\$ 6,993
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities:		
Depreciation and amortization.....	3,873	2,337
Gain on sale of Chorus Investment.....	--	(785)
Gain on sale of discontinued operations.....	(794)	--
Foreign currency loss.....	6	--
Loss on IMAT investment.....	66	--
Restructuring charge -- non-cash portion.....	194	--
Loss on disposal of equipment.....	95	21
Changes in assets and liabilities.....	(5,930)	7,637
Total adjustments.....	(2,490)	9,210
Net cash and cash equivalents provided by operating activities.....	1,989	16,203
INVESTING ACTIVITIES		
Purchase of investments.....	(72,583)	(82,570)
Proceeds from sale of investments.....	71,939	13,557
Proceeds from sale of Chorus Investment.....	--	785
Investment in IMAT.....	--	(436)
Purchase of leasehold improvements and equipment.....	(1,819)	(3,626)
Net cash and cash equivalents used in investing activities.....	(2,463)	(72,290)
FINANCING ACTIVITIES		
Net borrowings under line of credit agreement.....	--	(2)
Notes payable repayments.....	--	(25)
Proceeds from issuance of common stock.....	561	425
Repurchase of common stock.....	(2,660)	--
Proceeds from convertible bond offering.....	--	55,207
Net cash and cash equivalents provided by (used in) financing activities.....	(2,099)	55,605
Net decrease in cash and cash equivalents.....	(2,573)	(482)
Cash and cash equivalents at beginning of period.....	3,338	938
Cash and cash equivalents at end of period.....	\$ 765	\$ 456
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION		
Cash paid for:		
Interest.....	\$ 1,930	\$ 53
Income taxes.....	4,065	3,750

See accompanying notes.

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BUSINESS ACTIVITIES AND BASIS OF PRESENTATION

Intevac, Inc. ("Intevac" or the "Company") is a leading supplier of static sputtering systems and related manufacturing equipment used to manufacture thin-film disks for computer hard disk drives. Sputtering is a complex vacuum deposition process used to deposit multiple thin-film layers on a disk. The Company's primary objective is to be the industry leader in supplying disk sputtering equipment by providing disk sputtering systems which have both the highest overall performance and the lowest cost of ownership in the industry. The Company's principal product, the MDP-250 disk sputtering system, enables disk manufacturers to produce high performance, high capacity disks. The Company sells its static sputtering systems and related manufacturing equipment to both captive and merchant thin-film disk manufacturers. The Company sells and markets its products directly in the United States, and through exclusive distributors in Japan and Korea. The Company has established subsidiaries in Singapore and Malaysia and a branch office in Taiwan to support its customers in Southeast Asia.

The Company also realizes revenues from the sales of system components, contract research and development activities, flat panel display ("FPD") manufacturing equipment and electron beam processing equipment. Intevac's system component business consists primarily of sales of spare parts and after-sale service to purchasers of the Company's disk sputtering systems, as well as sales of components to other manufacturers of vacuum equipment. Contract research and development revenues have been derived primarily from prime contracts awarded by and subcontracts awarded under various Department of Defense ("DOD") and NASA development projects for the FPD industry and various photonics products. FPD manufacturing equipment consists of sputtering and rapid thermal processing equipment for the manufacture of FPD's. Electron beam processing equipment is used for curing inks, coatings and adhesives, in the manufacture of shrink wrap films and for in-line sterilization.

The financial information at June 27, 1998 and for the three- and six-month periods ended June 27, 1998 and June 28, 1997 is unaudited, but includes all adjustments (consisting only of normal recurring accruals) that the Company considers necessary for a fair presentation of the financial information set forth herein, in accordance with generally accepted accounting principles for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, it does not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. For further information, refer to the Consolidated Financial Statements and footnotes thereto included or incorporated by reference in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1997.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

The results for the three- and six-month periods ended June 27, 1998 are not considered indicative of the results to be expected for any future period or for the entire year.

2. COMPREHENSIVE INCOME

As of January 1, 1998, the Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130"). SFAS 130 establishes new rules for the reporting and display of comprehensive income and its components; however, the adoption of this statement has no impact on the Company's net income or shareholders' equity. The Company's total comprehensive income was the same as its net income for all periods presented.

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

3. INVENTORIES

The components of inventory consist of the following:

	JUNE 27, 1998	DECEMBER 31, 1997

(IN THOUSANDS)		
Raw materials.....	\$ 9,450	\$ 8,784
Work-in-progress.....	9,998	18,756
Finished goods.....	5,389	8,375
	-----	-----
	\$24,837	\$35,915
	=====	=====

A significant portion of the finished goods inventory is represented by completed units at customer sites undergoing installation and acceptance testing.

4. DISCONTINUED OPERATIONS

During the quarter, the Company recognized a gain of \$473,000 (net of income taxes) resulting from the reimbursement of excess warranty reserves related to the sale of the Company's night vision business in 1995. Basic and diluted earnings per share on the gain from discontinued operations were both \$0.04.

5. NET INCOME PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JUNE 27, 1998	JUNE 28, 1997	JUNE 27, 1998	JUNE 28, 1997

(IN THOUSANDS)				
Numerator:				
Income from continuing operations.....	\$1,744	\$3,577	\$3,474	\$6,993
	=====	=====	=====	=====
Net income.....	\$2,217	\$3,577	\$4,479	\$6,993
	=====	=====	=====	=====
Numerator for basic earnings per share -- income available to common stockholders.....	2,217	3,577	4,479	6,993
Effect of dilutive securities:				
6 1/2% convertible notes(1).....	--	563	--	761
	-----	-----	-----	-----
Numerator for diluted earnings per share -- income available to common stockholders after assumed conversions....	\$2,217	\$4,140	\$4,479	\$7,754
	=====	=====	=====	=====
Denominator:				
Denominator for basic earnings per share -- weighted-average shares.....	12,111	12,533	12,151	12,519
Effect of dilutive securities:				
Employee stock options.....	329	540	325	575
6 1/2% convertible notes(1).....	--	2,788	--	1,901
	-----	-----	-----	-----
Dilutive potential common shares.....	329	3,328	325	2,476
	-----	-----	-----	-----
Denominator for diluted earnings per share -- adjusted weighted-average shares and assumed conversions.....	12,440	15,861	12,476	14,995
	=====	=====	=====	=====

(1) Diluted EPS for the three-and six-month periods ended June 27, 1998 excludes "as converted" treatment of the Convertible Notes as their inclusion would be anti-dilutive.

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6. RESEARCH AND DEVELOPMENT COST SHARING AGREEMENT

The Company entered into an agreement with a Japanese company to perform best efforts joint research and development work. The nature of the project is to develop a glass coating machine to be used in the production of flat panel displays. As of June 27, 1998, the Company was funded for one-half of the actual costs of the project up to a ceiling of \$6,750,000. Discussions with the Company's development partner have led to an increase of \$1,150,000 in the ceiling. This additional amount has been invoiced to the Company's development partner and the Company will recognize this funding during the second half of 1998.

7. RESTRUCTURING

On March 2, 1998, as a result of weak demand for its disk sputtering systems, the Company's management adopted a plan to reduce expenses. The expense reduction plan included a reduction in force of approximately 90 employees out of the Company's staff of contract and regular personnel. The reductions took place at the Company's facilities in Santa Clara, CA; Los Gatos, CA; Rocklin, CA; and Taiwan. Additionally, the Company relocated its Rapid Thermal Processing ("RTP") Operation from Rocklin to the Company's Santa Clara headquarters and closed the Rocklin facility.

In the first quarter of 1998, the Company incurred a restructuring charge of \$1,164,000 related to the expense reduction plan. The significant components of this charge include \$290,000 for closure of the Rocklin facility, \$462,000 for the balance of the rent due on the lease for such facility and \$392,000 for employee severance costs. Closure of the facility was complete at June 27, 1998.

As of June 27, 1998, of the foregoing amounts, approximately \$370,000 in termination benefits had been paid out to affected employees and \$265,000 had been spent related to the relocation of the RTP Operation and the closure of the Rocklin facility.

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

This Quarterly Report on Form 10-Q contains forward-looking statements which involve risks and uncertainties. The Company's actual results may differ materially from those discussed in the forward-looking statements. Factors that might cause such a difference, include but are not limited to, the risk factors set forth elsewhere in this Quarterly Report on Form 10-Q under "Certain Factors Which May Affect Future Operating Results" and in other documents the Company files from time to time with the Securities and Exchange Commission, including the Company's Annual Report on Form 10-K filed in March 1998, Form 10-Q's and Form 8-K's.

OVERVIEW

The Company's revenues are generated by the sale of disk sputtering systems and related disk manufacturing equipment; system components; contract research and development activities; flat panel display manufacturing equipment; and electron beam processing equipment. Disk sputtering systems and related disk manufacturing equipment generally represent the majority of the Company's revenue, and Intevac is a leading supplier of this equipment. Sputtering is a complex vacuum deposition process used to deposit multiple thin-film layers on a disk. Intevac's system component business consists primarily of sales of spare parts and after-sale service to purchasers of the Company's disk sputtering systems, as well as sales of components to other manufacturers of vacuum equipment. Contract research and development revenues have been derived primarily from prime contracts awarded by and subcontracts awarded under various DOD and NASA development projects for the FPD industry and various photonics products. Flat panel display manufacturing equipment consists of sputtering and rapid thermal processing equipment for the manufacture of FPD's. Electron beam processing equipment is used for curing inks, coatings and adhesives, in the manufacture of shrink-wrap films and for sterilization.

In the first quarter of 1997, the Company completed the sale of \$57.5 million of its 6 1/2% Convertible Subordinated Notes Due 2004 (the "Convertible Notes"). In the second quarter of 1997, the Company paid \$0.4 million for a 49% interest in IMAT Inc. ("IMAT"), a joint venture formed with its Japanese distributor, Matsubo, to market the Company's flat panel manufacturing equipment in the Far East. In the fourth quarter of 1997, the Company purchased all of the assets of RPC Industries ("RPC"). RPC is a manufacturer of electron beam processing systems. This acquisition was accounted for under the purchase method. The total purchase price was approximately \$1.0 million plus contingent payments equal to 25% of the future earnings of RPC. The total of these contingent payments is limited to approximately \$7.7 million.

In March 1998, as a result of weak orders for its disk sputtering systems and an expectation that revenues would decline significantly in the third quarter of 1998, the Company implemented an expense reduction plan that involved the termination of approximately 20% of the Company's work force. As part of the expense reduction plan, the Company also decided to close its Rocklin, California facility and transfer its Rapid Thermal Processing Operation from Rocklin to the Company's headquarters in Santa Clara. The Company is continuing to investigate its options for the further reduction of expenses.

During the first quarter of 1998, the Company incurred a restructuring charge of approximately \$1.2 million related to the expense reduction plan. As of June 27, 1998, approximately \$370,000 in termination benefits had been paid out to affected employees and \$265,000 had been spent related to the relocation of the RTP Operation and the closure of the Rocklin facility.

The Company's backlog was \$28.1 million and \$77.9 million at June 27, 1998 and June 28, 1997, respectively. The Company includes in backlog the value of purchase orders for its products with scheduled delivery dates. Delivery dates may be rescheduled from time to time. The Company's backlog at the beginning of a quarter may not include all system orders needed to achieve the Company's revenue objectives for that quarter. The Company expects that the reduction in backlog from prior periods will result in a substantial decline in revenue in the second half of fiscal 1998 relative to the first half of fiscal 1998.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 27, 1998 AND JUNE 28, 1997

Net revenues. Net revenues consist primarily of sales of the Company's disk sputtering systems and related equipment used to manufacture thin-film disks for computer hard disk drives, and, to a lesser extent, flat panel display manufacturing equipment, system components, and contract research and development. Net revenues from the sales of sputtering systems and electron beam processing equipment are recognized upon customer acceptance. Sales of related equipment and system components are recognized upon product shipment, and contract research and development is recognized in accordance with contract terms, typically as costs are incurred. Net revenues increased by 6% to \$35.8 million for the three months ended June 27, 1998 from \$33.8 million for the three months ended June 28, 1997. The increase in net revenues was due to an increase in the net revenues from flat panel display manufacturing equipment, system components and electron beam processing equipment, which was partially offset by a reduction in net revenues from disk sputtering systems. Based upon its current backlog of orders and the scheduled shipment dates, the Company expects that net revenues during the three months ended September 26, 1998 will decline substantially from the net revenues experienced during the three months ended June 27, 1998.

International sales increased by 55% to \$25.6 million for the three months ended June 27, 1998 from \$16.5 million for the three months ended June 28, 1997. The increase in international sales was primarily due to an increase in the percentage of sales of disk sputtering systems to international customers. International sales constituted 72% of net revenues for the three months ended June 27, 1998 and 49% of net revenues for the three months ended June 28, 1997.

Gross margin. Cost of net revenues consists primarily of purchased materials, fabrication, assembly, test, installation, warranty costs, scrap and costs attributable to contract research and development. Gross margin was 25.3% for the three months ended June 27, 1998 as compared to 30.0% for the three months ended June 28, 1997. Gross margins declined primarily as the result of a negative gross margin realized on the RIGEL flat panel sputtering system accepted for revenue during the quarter. The Company believes that the ongoing cost of producing additional RIGEL systems will be significantly lower than the cost of the first system. The Company also believes that lower sales volumes expected in the third quarter of 1998 will cause lower absorption of factory overhead, which will negatively impact gross margins.

Research and development. Research and development expense consists primarily of prototype materials, salaries and related costs of employees engaged in ongoing research, design and development activities for disk manufacturing equipment, flat panel manufacturing equipment, electron beam processing equipment and research by the Photonics Division. Company funded research and development expense increased by 79% to \$3.4 million for the three months ended June 27, 1998 from \$1.9 million for the three months ended June 28, 1997, representing 9.5% and 5.6%, respectively, of net revenue. This increase was primarily the result of the absence in the three months ended June 27, 1998 of cost sharing from the Company's D-STAR development partner, and research and development expense transferred to cost of sales under a DARPA development contract, both of which occurred in the three months ended June, 28, 1997.

Research and development expenses do not include costs of \$1.0 million in the three months ended June 28, 1997, reimbursed under the terms of a research and development cost sharing agreement with the Company's D-STAR development partner, nor do they include costs of \$1.0 million in the three months ended June 28, 1997 reimbursed to the Company under a DARPA development contract funding development of the D-STAR and delivery of a beta-site unit.

Selling, general and administrative. Selling, general and administrative expense consists primarily of selling, marketing, customer support, financial, travel, management, legal and professional services. Domestic sales are made by the Company's direct sales force, whereas international sales are made by distributors that typically provide sales, installation, warranty and ongoing customer support. The Company also has subsidiaries in Singapore and Malaysia and a branch office in Taiwan to support customers in Southeast Asia and markets its flat panel manufacturing equipment to the Far East through its Japanese joint venture, IMAT. Selling, general and administrative expense increased by 4% to \$2.9 million for the three months ended

June 27, 1998 from \$2.8 million for the three months ended June 28, 1997, representing 8.2% and 8.4%, respectively, of net revenue. The increase in expense was primarily the result of additional selling, general and administrative expenses associated with the electron beam equipment business which was acquired during the fourth quarter of 1997. Selling, general and administrative headcount grew to 90 employees at June 27, 1998 from 87 employees at June 28, 1997.

Interest expense. Interest expense consists primarily of interest on the Convertible Notes, and, to a lesser extent, interest on approximately \$2.0 million of long term debt related to the purchase of Cathode Technology in 1996. Interest expense for the three months ended June 27, 1998 was essentially unchanged when compared to the three months ended June 28, 1997.

Interest and other income, net. Interest and other income, net consists primarily of interest income on the Company's investments, income related to the sale of the Company's 20% interest in the capital stock of Chorus and early payment discounts on the purchase of inventories, goods and services, partially offset by the Company's 49% share of the loss incurred by IMAT. Interest and other income, net decreased by 21% to \$1.0 million for the three months ended June 27, 1998 from \$1.2 million for the three months ended June 28, 1997 as the result of increased interest income on funds raised from the sale of the Company's 6 1/2% Convertible Subordinated Notes due 2004, which was largely offset by decreased income related to the sale of the Company's 20% interest in the capital stock of Chorus and to a lesser extent the Company's 49% share of the loss incurred by IMAT.

Discontinued operations. The Company recorded a gain from discontinued operations of \$0.5 million resulting from the reimbursement of excess warranty reserves related to the sale of the Company's night vision business in 1995.

Provision for income taxes. Income tax expense as a percentage of pretax income for the three months ended June 27, 1998 and June 28, 1997, was 33% and 36%, respectively. The Company's tax rate differs from the applicable statutory rates primarily due to benefits from the Company's foreign sales corporation and tax-exempt interest income partially offset by nondeductible goodwill amortization. The tax rate declined in 1998 because a larger percentage of 1998 income is expected to be derived through the Company's foreign sales corporation and from tax-exempt interest income.

SIX MONTHS ENDED JUNE 27, 1998 AND JUNE 28, 1997

Net revenues. Net revenues increased by 8% to \$70.0 million for the six months ended June 27, 1998 from \$64.9 million the six months ended June 28, 1997. The increase in net revenues was due to an increase in the net revenues from flat panel display manufacturing equipment, system components and electron beam processing equipment which was partially offset by a reduction in net revenues from disk sputtering systems. Based upon its current backlog of orders and the scheduled shipment dates, the Company expects that net revenues during the six months ended December 31, 1998 will decline substantially from the net revenues experienced during the six months ended June 27, 1998.

International sales increased by 42% to \$44.2 million for the six months ended June 27, 1998 from \$31.2 million for the six months ended June 28, 1997. The increase in revenues from international sales was primarily due to an increase in the percentage of sales of disk sputtering systems to international customers and to a lesser extent the sales of electron beam processing equipment. International sales constituted 63% of net revenues for the six months ended June 27, 1998 and 48% of net revenues for the six months ended June 28, 1997.

Gross margin. Gross margin was 28.1% for the six months ended June 27, 1998 as compared to 31.3% for the six months ended June 28, 1997. The reduction in gross margins was primarily due to the negative gross margin incurred on the RIGEL system acceptance.

Research and development. Research and development expense increased to \$7.0 million for the six months ended June 27, 1998 from \$4.5 million for the six months ended June 28, 1997, representing 9.9% and 6.9%, respectively, of net revenues. The increase was primarily the result of increased development expense in disk manufacturing products, and the absence in the six months ended June 27, 1998 of cost sharing from the

Company's D-STAR development partner, and research and development expense transferred to cost of sales under a DARPA development contract, which both occurred in the six months ended June, 28, 1997.

Research and development expenses in the six months ended June 28, 1997 do not include costs of \$1.0 million reimbursed to the Company under the terms of a research and development cost sharing agreement with the Company's D-STAR development partner, nor do they include costs of \$1.5 million reimbursed to the Company under a DARPA development contract funding development of the D-STAR and delivery of a beta-site unit. In addition, research and development expenses do not include other expenditures in connection with contract research and development activities as these are charged to cost of sales.

Selling, general and administrative. Selling, general and administrative expense increased by 12% to \$6.1 million for the six months ended June 27, 1998 from \$5.4 million for the six months ended June 28, 1997, representing 8.6% and 8.4%, respectively, of net revenues. The increase in selling, general and administrative expense was the result of additional selling, general and administration expenses associated with the electron beam equipment business which was acquired during the fourth quarter of 1997, partially offset by decreased expenses elsewhere.

Restructuring expense. In March 1998, the Company's management adopted a restructuring plan to relocate its Rapid Thermal Processing Operation from Rocklin, California to the Company's Santa Clara, California headquarters and to close the Rocklin facility. The restructuring plan also included an approximate 20% reduction in the worldwide staff of the Company's contract and regular employees. As a result of this plan, the Company expensed approximately \$1.2 million of restructuring expense in the six months ended June 27, 1998. The restructuring expense included approximately \$0.8 million related to closure of the Rocklin facility and approximately \$0.4 million of severance pay for terminated employees.

Interest expense. Interest expense consists primarily of interest on the Company's 6 1/2% Convertible Notes issued in the first quarter of 1997.

Interest and other income, net. Interest and other income consists primarily of interest income on the Company's investments, income related to the sale of the Company's 20% interest in the capital stock of Chorus, and early payment discounts on the purchase of inventories, goods and services. Interest and other income, net decreased to \$1.7 million for the six months ended June 27, 1998 from \$2.0 million for the six months ended June 28, 1997 as the result of increased interest income on funds raised from the sale of the Company's 6 1/2% Convertible Subordinated Notes due 2004, which was more than offset by decreased income related to the sale of the Company's 20% interest in the capital stock of Chorus and an increase in the Company's 49% share of the loss incurred by IMAT.

Provision for income taxes. Income tax expense as a percentage of pretax income for the six months ended June 27, 1998 and June 28, 1997 was 33% and 36%, respectively. The Company's tax rate for these periods differs from the applicable statutory rates primarily due to benefits from the Company's foreign sales corporation and tax-exempt interest income, partially offset by nondeductible goodwill amortization.

LIQUIDITY AND CAPITAL RESOURCES

The Company's operating activities provided cash of \$2.0 million for the six months ended June 27, 1998. The cash generated in 1998 was due primarily to net income, reductions in accounts receivable and inventory and increased depreciation and amortization, which were partially offset by a decrease in customer advances.

The Company's investing activities used cash of \$2.5 million for the six months ended June 27, 1998 due to the purchase of fixed assets and the net purchase of investments.

The Company's financing activities used cash of \$2.1 million for the six months ended June 27, 1998, primarily due to the repurchase of 297,500 shares of the Company's stock for \$2.7 million, which was partially offset by the sale of the Company's stock to its employees through the Company's employee benefit plans.

YEAR 2000

The Company is currently evaluating the software and computer systems it uses in order to ensure compliance with Year 2000 issues. This evaluation, and any corrective actions required, is estimated to be largely completed no later than December 31, 1998. The Company does not expect to encounter significant problems or that material expenditures will be required to comply with Year 2000 issues. These expectations are based primarily on the fact that the Company purchases all business software from third party vendors.

Specific actions to be taken include: reviewing all software used and assessing the vendor's plans to comply with Year 2000; testing of all hardware to ensure its ability to recognize dates after 1999; and contacting significant suppliers to determine their ability to comply with Year 2000.

The expectations of the findings of this project and the date on which the Company believes it will be completed are based on management's best estimates. However, there can be no guarantee that these expectations will be achieved, and actual results could differ materially.

CERTAIN FACTORS WHICH MAY AFFECT FUTURE OPERATING RESULTS

Fluctuations of Results of Operations

The Company's operating results have historically been subject to significant quarterly and annual fluctuations. The Company believes that its operating results will continue to fluctuate on a quarterly and annual basis due to a variety of factors. These factors include the cyclicity of the thin-film disk manufacturing and disk drive industries, patterns of capital spending by customers, the timing of significant orders, order cancellations or reschedulings, market acceptance of the Company's products, unanticipated delays in design, engineering or production or in customer acceptance of product shipments, changes in pricing by the Company or its competitors, the timing of product announcements or introductions by the Company or its competitors, the mix of systems sold, the relative proportions of sputtering systems, system components and subassemblies, electron beam processing systems, and contract research and development net revenues, the availability and cost of components and subassemblies, changes in product development costs, expenses associated with acquisitions and exchange rate fluctuations.

The Company derives the majority of its net revenues from the sale of a relatively small number of sputtering systems. Over the last ten quarters, the number of systems accepted by customers in any particular quarter has varied from four to thirteen and, as a result, the Company's net revenues and operating results for a particular period could be materially adversely affected if an anticipated order for even one system is not received in time to permit shipment and customer acceptance during that accounting period. Over the last ten quarters the Company's gross margin and operating income (loss) as a percentage of net revenues has fluctuated from approximately 25% to 40% of net revenues and from (9)% to 18% of net revenues, respectively. The Company anticipates that its unit shipments, revenues, gross and operating margins will continue to fluctuate. As a result, the Company believes that period-to-period comparisons of its results of operations are not necessarily meaningful and should not be relied upon as indications of future performance.

The Company's backlog at the beginning of a quarter may not include all system orders needed to achieve the Company's revenue objectives for that quarter. In addition, orders in backlog are subject to cancellation, and although the Company generally requires a deposit on orders for its systems, such deposits may not be sufficient to cover the expenses incurred by the Company for the manufacture of the canceled systems or fixed operating expenses associated with such systems. The Company may from time to time manufacture a system in anticipation of an order that may not be placed during the period or at all. In any given quarter in which such a system is manufactured, the Company may not receive funds to cover its manufacturing costs. Orders may be subject to delay, deferral or rescheduling by a customer. From the date the Company receives an order, it often takes more than six months before the net revenues from such order are recognized and even longer before final payment is received. The relatively long manufacturing cycles of many of the Company's products has caused and could cause shipments of such products to be delayed from one quarter to the next, which could materially adversely affect the Company's business, financial condition and results of operations for a particular quarter. Announcements by the Company or its competitors of new products and technologies

could cause customers to defer purchases of the Company's existing systems, which would have a material adverse effect on the Company's business, financial condition and results of operations.

Installing and integrating new sputtering systems into the thin-film disk manufacturing process requires a substantial investment by a customer. Sales of the Company's systems depend, in significant part, upon the decision of a prospective customer to replace obsolete equipment or to increase manufacturing capacity by upgrading or expanding existing manufacturing facilities or constructing new manufacturing facilities, all of which typically involve a significant capital commitment. Therefore, customers often require a significant number of product presentations and demonstrations, as well as substantial interaction with the Company's senior management, before making a purchasing decision. Accordingly, the Company's systems typically have a lengthy sales cycle, during which the Company may expend substantial funds and management time and effort with no assurance that a sale will result. Furthermore, the Company's expense levels are based, in part, on its expectations as to future net revenues. If revenue levels are below expectations, operating results are likely to be adversely affected. Net income, if any, may be disproportionately affected by a reduction in net revenues because a proportionately smaller amount of the Company's expenses varies with its net revenues. The impact of these and other factors on the Company's sales and operating results in any future period cannot be forecasted with certainty.

Due to all of the foregoing factors, the Company expects its quarterly operating results to fluctuate significantly and may in certain quarters be below the expectations of securities analysts and investors. In such event it is likely the price of the Company's Common Stock would be materially adversely affected.

Cyclicity of the Media Industry

The cyclicity of the disk drive industry, among other factors, may cause prospective customers to postpone decisions regarding major capital expenditures, including purchases of the Company's systems. The Company recently received a request for a two quarter push-out of deliveries by one of its customers. The Company's business depends upon capital expenditures by manufacturers of thin-film disks, including manufacturers that are opening new fabrication facilities or entering the market, expanding or upgrading existing facilities, or replacing obsolete equipment, which in turn depend upon the current and anticipated market demand for hard disk drives. In recent years, the disk drive industry has experienced significant growth, which, in turn, has caused significant growth in the capital equipment industry supplying manufacturers of thin-film disks. However, the disk drive industry is cyclical and historically has experienced periods of oversupply, resulting in significantly reduced demand for thin-film disks and for the capital equipment used to manufacture such disks, including the systems manufactured and marketed by the Company.

A number of manufacturers of hard disk drives and hard disk drive component suppliers have recently reported both substantial reductions in revenues and substantial financial losses. Many of these manufacturers attributed their problems to an excess supply of hard drives, or, in the case of component suppliers, an excess supply of components for hard drives (including thin-film disks) and the rapid change of technology which caused a number of products to become obsolete. This industry-wide over-capacity has led to a period of reduced demand for thin-film disk production and for the capital equipment used in such production. In March of 1998, as a result of weak orders for its disk sputtering systems, the Company implemented an expense reduction plan that involved the termination of approximately 20% of the Company's work force. Based upon its current backlog of orders and the scheduled shipment dates, the Company expects that net revenues during the six months ended December 31, 1998 will decline substantially from the net revenues experienced during the six months ended June 27, 1998.

Cyclical downturns in the hard disk drive industry are likely to materially adversely affect the Company's business, financial condition and results of operations.

Intense Competition

The Company's disk sputtering business experiences intense competition worldwide from two principal competitors, Balzars A.G. ("Balzars") and Anelva Corporation ("Anelva"), each of which is a large manufacturer of complex vacuum equipment and thin-film disk manufacturing systems and has sold a

substantial number of thin-film disk sputtering machines worldwide. Both Balzars and Anelva are manufacturers of static sputtering systems, and each has substantially greater financial, technical, marketing, manufacturing and other resources than the Company. The Company also experiences competition from two other manufacturers of static sputtering systems as well as from the manufacturers of thin-film disks that have developed the capability to manufacture their own sputtering systems. There can be no assurance that the Company's competitors will not develop enhancements to, or future generations of, competitive products that offer superior price or performance features or that new competitors will not enter the Company's markets and develop such enhanced products. Furthermore, the failure of manufacturers of thin-film disks currently using in-line machines and manufacturers using internally developed sputtering systems to switch to static sputtering systems in the future could adversely affect the Company's ability to increase its sputtering system market share.

In addition, the Company's two principal competitors are based in foreign countries and have cost structures and system prices based on foreign currencies. Accordingly, currency fluctuations could cause the Company's dollar-priced products to be less competitive than its competitors' products priced in other currencies. Currency fluctuations could also increase the Company's cost structure relative to those of its competitors, which could make it more difficult for the Company to maintain its gross margins. For example, between 12/31/97 and 8/4/98, the exchange rate for Japanese Yen has increased from 130.15 Yen/\$ to 144.80 Yen/\$, which all else equal, increases the cost of Intevac's products by approximately 11.3% compared to Japanese manufacturers.

Given the lengthy sales cycle and the significant investment required to integrate a disk sputtering system into the manufacturing process, the Company believes that once a thin-film disk manufacturer has selected a particular supplier's disk sputtering equipment, the manufacturer generally relies upon that equipment for the specific production line application and frequently will continue to purchase its other disk sputtering equipment from the same supplier. The Company expects to experience difficulty in selling to a particular customer for a significant period of time if that customer selects a competitor's disk sputtering equipment. Accordingly, competition for customers in the disk sputtering equipment industry is particularly intense, and suppliers of disk sputtering equipment may offer pricing concessions and incentives to attract customers, which could adversely affect the Company's business, financial condition, gross margins and results of operations. Because of these competitive factors, there can be no assurance that the Company will be able to compete successfully in the future.

Customer Concentration

Historically, a significant portion of the Company's revenues in any particular period have been attributable to sales to a limited number of customers. For example, Matsubo, HMT Technology and Trace Storage Technology accounted for 37%, 17% and 15%, respectively of the Company's total net revenues in 1997, and Matsubo, Seagate and HMT Technology accounted for 32%, 32% and 13%, respectively, of the Company's total net revenues in 1996. Seagate, HMT Technology, and Matsubo accounted for 40%, 20% and 17%, respectively, of the Company's total net revenues in 1995. The Company's largest customers change from period to period as large thin-film disk fabrication facilities are completed and new projects are initiated. The Company expects that sales of its products to relatively few customers will continue to account for a high percentage of its net revenues in the foreseeable future. For example, 68% of the Company's backlog at December 31, 1997 was represented by two customers for disk sputtering systems, with each representing 10% or more of the Company's backlog at December 31, 1997. None of the Company's customers has entered into a long-term agreement requiring it to purchase the Company's products. As purchases related to a particular new or expanded fabrication facility are completed, sales to that customer may decrease sharply or cease altogether. If completed contracts are not replaced on a timely basis by new orders from the same or other customers, the Company's net revenues could be adversely affected. The loss of a significant customer, any reduction in orders from any significant customer or the cancellation of a significant order from a customer, including reductions or cancellations due to customer departures from recent buying patterns, financial difficulties of a customer or market, economic or competitive conditions in the disk drive industry, could materially adversely affect the Company's business, financial condition and results of operations.

Limited Number of Opportunities

The Company's business depends upon capital expenditures by manufacturers of thin-film disks, of which there are a limited number worldwide. According to a April 1997 report by TrendFocus, an independent market research firm, as of the end of 1996 there were 231 installed disk sputtering lines (sputtering systems and related equipment such as plating, polishing, texturing, lubrication and test equipment as well as related handling equipment) worldwide and only 15 companies in the world with five or more installed disk sputtering lines. Therefore, winning or losing an order from any particular customer could significantly affect the Company's operating results. In addition, the Company's opportunities to sell its systems are further limited by the fact that some of the manufacturers of thin-film disks have adopted an in-line approach as opposed to the Company's static approach to thin-film disk manufacturing. These manufacturers have invested significant amounts of capital in their in-line systems, and there may be significant resistance to change to a static approach in the future. The construction of new thin-film disk fabrication facilities involves extremely large capital expenditures, resulting in few thin-film disk fabrication facilities being constructed worldwide at any particular time. A substantial investment is also required by disk manufacturers to install and integrate additional thin-film disk manufacturing equipment in connection with upgrading or expanding their existing fabrication facilities. These costs are far in excess of the cost of purchasing the Company's system. The magnitude of such capital expenditures has caused certain thin-film disk manufacturers to forego purchasing significant additional thin-film disk manufacturing equipment. Consequently, only a limited number of opportunities for the Company to sell its systems may exist at any given time.

Rapid Technological Change; New Products

The disk drive industry in general, and the thin-film disk manufacturing industry in particular, is characterized by rapid technological change and evolving industry standards. The Company maintains an active development program to make sputter system improvements, to add additional capabilities that will improve disk performance, increase machine throughput, permit optimum utilization of alternative substrates, lower cost of ownership and respond to future market requirements. The Company's ability to remain competitive has required and will continue to require substantial investments in research and development to advance its technologies. The failure to develop, manufacture and market new systems, or to enhance existing systems, would have a material adverse effect on the Company's business, financial condition and results of operations. In the past, the Company has experienced delays from time to time in the introduction of, and certain technical difficulties with, certain of its systems and enhancements. In addition, the Company's competitors can be expected to continue to develop and introduce new and enhanced products, any of which could cause a decline in market demand for the Company's systems or a reduction in the Company's margins as a result of intensified price competition.

Changes in the manufacturing processes for thin-film disks could also have a material adverse effect on the Company's business, financial condition and results of operations. The Company anticipates continued changes in the requirements of the disk drive industry and thin-film disk manufacturing technologies. There can be no assurance that the Company will be able to develop, manufacture and sell systems that respond adequately to such changes. In addition, the data storage industry is subject to constantly evolving technological standards. There can be no assurance that future technological innovations will not reduce demand for thin-film disks. The Company's business, financial condition and results of operations could be materially adversely affected by any trend toward technology that would replace thin-film disks as a storage medium.

The Company's success in developing and selling enhanced disk sputtering systems and other new products depends upon a variety of factors, including accurate prediction of future customer requirements, technology advances, cost of ownership, introduction of new products on schedule, cost-effective manufacturing and product performance in the field. The Company's new product decisions and development commitments must anticipate the requirements for the continuously evolving disk drive industry approximately two or more years in advance of sales. Any failure to accurately predict customer requirements and to develop new generations of products to meet those requirements would have a sustained material adverse effect on the Company's business, financial condition and results of operations. New product transitions could adversely

affect sales of existing systems, and product introductions could contribute to quarterly fluctuations in operating results as orders for new products commence and orders for existing products decline. There can be no assurance that the Company will be successful in selecting, developing, manufacturing and marketing new products or enhancements of existing products.

Flat Panel Display Manufacturing Equipment Risks

In 1997, the Company spent approximately \$4.9 million on various programs to fund the development of equipment for use in the FPD industry, of which approximately 54% was paid for by the Company's development partners. In exchange for certain development funding, the Company has granted to one of its development partners the exclusive rights to manufacture and market the Company's FPD sputtering systems in Japan. As of June 27, 1998 all of the approximately \$6.75 million advanced by the Company's development partner had been applied to qualifying costs. The Company has limited experience in the development, manufacture, sale and marketing of FPD manufacturing equipment, having sold only three rapid thermal processing ("RTP") systems to date and two of its FPD sputtering systems. Although during the first half of 1998 the Company delivered and the customer accepted a larger version of its FPD sputtering machine, there can be no assurance that the market for FPD manufacturing equipment targeted by the Company will develop as quickly or to the degree the Company currently anticipates, or that the Company's proposed FPD manufacturing equipment will achieve market acceptance. There can be no assurance the Company will receive additional customer sponsored research and development funding in the future. The failure to receive additional customer sponsored research and development funds could result in the Company internally funding the development of such FPD manufacturing equipment, and the costs of such research and development may have a material adverse effect on the Company's business, financial condition and results of operations. There can be no assurance that the Company in any event will continue to fund research and development in the FPD area.

Risks Associated With International Sales and Operations

Foreign sales accounted for 64%, 41% and 20% of revenues in 1997, 1996 and 1995, respectively. Substantially all of the Company's Disk Equipment foreign sales are to companies in the Far East. The Company anticipates that sales to customers in the Far East will continue to be a significant portion of its revenues in the foreseeable future. In order to effectively service customers located in Southeast Asia, the Company has established sales and service operations in Singapore, Taiwan and Malaysia and a joint venture in Japan. Sales and operating activities outside of the United States are subject to certain inherent risks, including fluctuations in the value of the United States dollar relative to foreign currencies, tariffs, quotas, taxes and other market barriers, political and economic instability, restrictions on the export or import of technology, potentially limited intellectual property protection, difficulties in staffing and managing international operations and potentially adverse tax consequences. The Company's products have been sold to companies headquartered in the United States, Japan, Taiwan and Korea and have been installed in factories in the United States, Japan, Singapore, Malaysia, Korea and Taiwan. All of the Far Eastern countries with which the Company does business have banking systems and foreign currency exposures that have experienced serious troubles recently and therefore subject the Company's customers to substantial business risks. There can be no assurance that any of these factors will not have a material adverse effect on the Company's business, financial condition or results of operations. In particular, although the Company's international sales have been denominated in United States dollars, such sales and expenses may not be denominated in dollars in the future, and currency exchange fluctuations in countries where the Company does business could materially adversely affect the Company's business, financial condition and results of operations.

Dependence on Key Employees

The Company's operating results will depend significantly upon the continued contributions of its officers and key management, engineering, marketing, customer support and sales personnel, many of whom would be difficult to replace. The Company does not have an employment agreement with any of its employees or

maintain key person life insurance with respect to any employee. The loss of any key employee could have a material adverse effect on the Company's business, financial condition and results of operations. Employees of the Company are currently required to enter into a confidentiality agreement as a condition of their employment. However, these agreements do not expressly prohibit the employees from competing with the Company after leaving its employ.

Ability to Attract Qualified Personnel

The Company's operating results depend in significant part upon its ability to retain and attract qualified management, engineering, marketing, customer support and sales personnel. Competition for such personnel is intense and there can be no assurance that the Company will be successful in attracting and retaining such personnel. The failure to attract and retain such personnel could make it difficult to undertake or could significantly delay the Company's research and development efforts and the expansion of its manufacturing capabilities or other activities, which could have a material adverse effect on the Company's business, financial condition and results of operations.

Leverage

In connection with the sale of the Convertible Notes, the Company incurred a substantial increase in the Company's ratio of long-term debt to total capitalization (shareholders' equity plus long-term debt). The ratio at June 27, 1998 and December 31, 1997 was approximately 57.0% and 58.4%, respectively. As a result of this indebtedness, the Company incurred substantial principal and interest obligations. The degree to which the Company is leveraged could have a material adverse effect on the Company's ability to obtain additional financing for working capital, acquisitions or other purposes and could make it more vulnerable to industry downturns and competitive pressures. The Company's ability to meet its debt service obligations will be dependent on the Company's future performance, which will be subject to financial, business and other factors affecting the operations of the Company, many of which are beyond its control.

Manufacturing Risks

The Company's systems have a large number of components and are highly complex. The Company may experience delays and technical and manufacturing difficulties in future introductions or volume production of new systems or enhancements. In addition, some of the systems built by the Company must be customized to meet individual customer site or operating requirements. The Company may be unable to complete the development or meet the technical specifications of its new systems or enhancements or to manufacture and ship these systems or enhancements in a timely manner. Such an occurrence would materially adversely affect the Company's business, financial condition and results of operations as well as its relationships with customers. In addition, the Company may incur substantial unanticipated costs early in a product's life cycle, such as increased cost of materials due to expediting charges, other purchasing inefficiencies and greater than expected installation and support costs which cannot be passed on to the customer. Any of such events could materially adversely affect the Company's business, financial condition and results of operations.

In certain instances, the Company is dependent upon a sole supplier or a limited number of suppliers, or has qualified only a single or limited number of suppliers, for certain complex components or sub-assemblies utilized in its products. The Company has a key supplier program in which it appoints certain key vendors as sole suppliers for certain parts with the goal of improving response time and reducing costs. In addition, the Company makes extensive use of suppliers serving the semiconductor equipment business and such suppliers may choose to give priority to their semiconductor equipment customers that are much larger than the Company. Any prolonged inability to obtain adequate deliveries could require the Company to pay more for inventory, parts and other supplies, seek alternative sources of supply, delay its ability to ship its products and damage relationships with current and prospective customers. Any such delay or damage could have a material adverse effect on the Company's business, financial condition and results of operations.

The Company conducts substantially all of its manufacturing activities at its leased facilities in Santa Clara and Los Gatos, California. The Company's Santa Clara and Los Gatos facilities are located in a

seismically active area. A major catastrophe (such as an earthquake or other natural disaster) could result in a prolonged interruption of the Company's business.

Acquisitions

The Company's business strategy includes acquiring related businesses, products or technologies. The Company completed one acquisition during 1997 and three acquisitions during 1996 and expects that it may pursue additional acquisitions in the future. Any future acquisition may result in potentially dilutive issuance of equity securities, the write-off of in-process research and development and the assumption of debt and contingent liabilities, any of which could materially adversely affect the Company's business, financial condition and results of operations. Additionally, as a result of the Company's ongoing repurchase of its stock in the open market, the Company may not be able to use the "pooling of interests" method of accounting in some acquisitions, and the Company may therefore be required to amortize any intangible assets acquired in connection with any acquisition.

The Company incurred a charge to operations of \$0.3 million in the fourth quarter of 1997 and \$5.8 million in the second quarter of 1996 to reflect the purchase of in-process research and development related to the acquisitions completed in those quarters. In addition, the Company is amortizing intangible assets of approximately \$9.0 million gross, and \$4.2 million net at June 27, 1998, relating to the four acquisitions. The amortization period for such costs is over the useful lives, which range from two years to seven years. Additionally, unanticipated expenses may be incurred relating to the integration of technologies, research and development and administrative functions. Any acquisition will involve numerous risks, including difficulties in the assimilation of the acquired company's employees, operations and products, uncertainties associated with operating in new markets and working with new customers, and the potential loss of the acquired company's key employees.

Patents and Other Intellectual Property

The Company currently has 25 patents issued in the United States and 3 patents issued in foreign countries, and has pending patent applications in the United States and foreign countries. Of the 25 U.S. patents, 8 relate to sputtering, 10 relate to RTP, 1 relates to lubrication systems and 6 relate to photonics. Two foreign patent relates to sputtering and one relates to photonics. In addition, the Company has the right to utilize certain patents under licensing arrangements with Litton Industries, Varian Associates, Stanford University, Lawrence Livermore Laboratories and Alum Rock Technology.

There can be no assurance that any of the Company's patent applications will be allowed or that any of the allowed applications will be issued as patents. There can be no assurance that any patent owned by the Company will not be invalidated, deemed unenforceable, circumvented or challenged, that the rights granted thereunder will provide competitive advantages to the Company or that any of the Company's pending or future patent applications will be issued with claims of the scope sought by the Company, if at all. Furthermore, there can be no assurance that others will not develop similar products, duplicate the Company's products or design around the patents owned by the Company. In addition, there can be no assurance that foreign patent rights, intellectual property laws or the Company's agreements will protect the Company's intellectual property rights. Failure to protect the Company's intellectual property rights could have a material adverse effect upon the Company's business, financial condition and results of operations.

There has been substantial litigation in the technology industry regarding intellectual property rights. The Company has from time to time received claims that it is infringing third parties' intellectual property rights. In August 1993, Rockwell International Corporation ("Rockwell") sued the Federal government alleging infringement of certain patent rights with respect to the contracts the Federal government has had with a number of companies, including Intevac. The Federal government has notified Intevac that it may be liable in connection with contracts for certain products from the Company's discontinued night vision business. Although the Company believes it will have no material liability under these contracts, there can be no assurance that the resolution of the claims by Rockwell with the Federal government will not have a material adverse effect on the Company's business, operating results and financial condition. In the first quarter of

1997, Rockwell's patent in suit was held invalid. Rockwell appealed that decision, and in the second quarter of 1998, the appellate court ruled that the patent was not invalid and referred the case back to the court of origin.

There can be no assurance that other third parties will not in the future claim infringement by the Company with respect to current or future patents, trademarks, or other proprietary rights relating to the Company's disk sputtering systems, flat panel display manufacturing equipment or other products. Any present or future claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays or require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company, or at all. Any of the foregoing could have a material adverse effect upon the Company's business, operating results and financial condition.

In addition, the Company believes that one of its competitors may be infringing the Company's patent rights in connection with products currently being offered by this competitor. Although the Company has not undertaken formal legal proceedings, the Company has informed this competitor that the Company believes its patent rights are being infringed and that the Company may undertake litigation to protect its patent rights if necessary. If undertaken, such litigation could be costly, time-consuming and result in legal claims being made against the Company, which could have a material adverse effect on the Company's business, operating results and financial condition. In addition, there can be no assurance that the Company would ultimately prevail in any such litigation.

Environmental Regulations

The Company is subject to a variety of governmental regulations relating to the use, storage, discharge, handling, emission, generation, manufacture, treatment and disposal of toxic or other hazardous substances, chemicals, materials or waste. Any failure to comply with current or future regulations could result in substantial civil penalties or criminal fines being imposed on the Company, or its officers, directors or employees, suspension of production, alteration of its manufacturing process or cessation of operations. Such regulations could require the Company to acquire expensive remediation or abatement equipment or to incur substantial expenses to comply with environmental regulations. Any failure by the Company to properly manage the use, disposal or storage of, or adequately restrict the release of, hazardous or toxic substances could subject the Company to significant liabilities.

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There are no material legal proceedings to which the Company is a party or to which any of its property is subject.

ITEM 2. CHANGES IN SECURITIES

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

The Company's annual meeting of shareholders was held on May 14, 1998. The following actions were taken at this meeting:

	AFFIRMATIVE VOTES	NEGATIVE VOTES	VOTES WITHHELD	ABSTENTIONS AND BROKER NON-VOTES
	-----	-----	-----	-----
(a) Election of Directors				
Norman H. Pond.....	11,649,398	279,213	--	319,914
Edward Durbin.....	11,648,898	279,713	--	319,914
Robert D. Hempstead.....	11,648,398	280,213	--	319,914
David N. Lambeth.....	11,648,398	280,213	--	319,914
H. Joseph Smead.....	11,648,698	279,913	--	319,914
(b) Approval of an amendment to the Company's 1995 Stock Option/Stock Issuance Plan.....	11,036,320	862,593	--	349,612
(c) Ratification of Ernst & Young as independent auditors.....	11,907,622	8,082	--	332,821

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following exhibits are filed herewith:

EXHIBIT NUMBER	DESCRIPTION
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10.1	Amendment to Line of Credit Agreement dated May 1, 1998
27.1	Financial Data Schedule

(b) Reports on Form 8-K:

None.

SIGNATURES

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

INTEVAC, INC.

Date: August 10, 1998

By: /s/ NORMAN H. POND

*Norman H. Pond
Chairman of the Board, President and
Chief
Executive Officer (Principal
Executive Officer)*

Date: August 10, 1998

By: /s/ CHARLES B. EDDY III

*Charles B. Eddy III
Vice President, Finance and
Administration, Chief Financial
Officer, Treasurer and Secretary
(Principal Financial and Accounting
Officer)*

EXHIBIT INDEX

EXHIBIT NUMBER -----	DESCRIPTION -----
10.1	Amendment to Line of Credit Agreement dated May 1, 1998
27.1	Financial Data Schedule

Exhibit 10.1

[WELLS FARGO BANK LETTERHEAD]

May 1, 1998

Intevac, Inc.
3560 Bassett Street
Santa Clara, CA 95054

Gentlemen:

This letter is to confirm the changes agreed upon between Wells Fargo Bank, National Association ("Bank") and Intevac, Inc. ("Borrower") to the terms and conditions of that certain letter agreement between Bank and Borrower dated as of April 30, 1997, as amended from time to time (the "Agreement"). For valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Bank and Borrower hereby agree that the Agreement shall be amended as follows to reflect said changes.

1. The Agreement is hereby amended by deleting "May 1, 1998" as the last day on which Bank will make advances under the Line of Credit, and by substituting for said date "May 1, 1999," with such change to be effective upon the execution and delivery to Bank of a promissory note substantially in the form of Exhibit A attached hereto (which promissory note shall replace and be deemed the Line of Credit Note defined in and made pursuant to the Agreement) and all other contracts, instruments and documents required by Bank to evidence such change.
2. Paragraphs V.3.(c) and (d) are hereby deleted in their entirety, without substitution.
3. Paragraph V.3.(e) shall be renumbered to Paragraph V.3.(c).
4. Paragraph V.8.(a) is hereby deleted in its entirety, and the following substituted therefor:

"(a) Tangible Net Worth not at any time less than \$90,000,000.00, with "Tangible Net Worth" defined as the sum of the capital stock and additional paid in capital, plus retained earnings, plus subordinated debt of the Borrower and its subsidiaries, minus intangible assets on a consolidated basis and minus any permitted stock repurchase."

5. The following is hereby added to the Agreement as Paragraph V.15.:

"15. Year 2000 Compliance. Perform all acts reasonably necessary to ensure that (a) Borrower and any business in which Borrower holds a substantial interest, and (b) all customers, suppliers and vendors that are material to Borrower's business, become Year 2000 Compliant in a timely manner. Such acts shall include, without limitation, performing a comprehensive review and assessment of all of Borrower's systems and adopting a detailed plan, with itemized budget, for the remediation, monitoring and testing of such systems. As used herein, "Year 2000 Compliant" shall mean, in regard to any entity, that all software, hardware, firmware, equipment, goods or systems utilized by or material to the business operations or financial condition of such entity, will properly perform date sensitive functions before, during and after the year 2000. Borrower shall, immediately upon request, provide to Bank such certifications or other evidence of Borrower's compliance with the terms hereof as Bank may from time to time require."

6. Except as specifically provided herein, all terms and conditions of the Agreement remain in full force and effect, without waiver or modification. All terms defined in the Agreement shall have the same meaning when used herein. This letter and the Agreement shall be read together, as one document.

7. Borrower hereby remakes all representations and warranties contained in the Agreement and reaffirms all covenants set forth therein. Borrower further certifies that as of the date of Borrower's acknowledgement set forth below there exists no default or defined event of default under the Agreement or any promissory note or other contract, instrument or document executed in connection therewith, nor any condition, act or event which with the giving of notice or the passage of time or both would constitute such a default or defined event of default.

Intevac, Inc.
May 1, 1998

Page 3

Your acknowledgment of this letter shall constitute acceptance of the foregoing terms and conditions.

Sincerely,

**WELLS FARGO BANK,
NATIONAL ASSOCIATION**

By: /s/ Gus Martin

Gus Martin
Vice President

Acknowledged and accepted as of _____:

INTEVAC, INC.

By: /s/

Title: CFO

\$10,000,000.00

San Jose, California
May 1, 1998

FOR VALUE RECEIVED, the undersigned INTEVAC, INC. ("Borrower") promises to pay to the order of WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank") at its office at Santa Clara Valley RCBO, 121 Park Center Plaza 3rd Flr, San Jose, CA 98115, or at such other place as the holder hereof may designate, in lawful money of the United States of America and in immediately available funds, the principal sum of \$10,000,000.00, or so much thereof as may be advanced and be outstanding, with interest thereon, to be computed on each advance from the date of its disbursement as set forth herein.

DEFINITIONS:

As used herein, the following terms shall have the meanings set forth after each, and any other term defined in this Note shall have the meaning set forth at the place defined:

- (a) "Business Day" means any day except a Saturday, Sunday or any other day on which commercial banks in California are authorized or required by law to close.
- (b) "Fixed Rate Term" means a period commencing on a Business Day and continuing for 1, 2 or 3 months, as designated by Borrower, during which all or a portion of the outstanding principal balance of this Note bears interest determined in relation to LIBOR; provided however, that no Fixed Rate Term may be selected for a principal amount less than \$500,000.00; and provided further, that no Fixed Rate Term shall extend beyond the scheduled maturity date hereof. If any Fixed Rate Term would end on a day which is not a Business Day, then such Fixed Rate Term shall be extended to the next succeeding Business Day.
- (c) "LIBOR" means the rate per annum (rounded upward, if necessary, to the nearest whole 1/8 of 1%) determined by dividing Base LIBOR by a percentage equal to 100% less any LIBOR Reserve Percentage.
- (i) "Base LIBOR" means the rate per annum for United States dollar deposits quoted by Bank as the Inter-Bank Market Offered Rate, with the understanding that such rate is quoted by Bank for the purpose of calculating effective rates of interest for loans making reference thereto, on the first day of a Fixed Rate Term for delivery of funds on said date for a period of time approximately equal to the number of days in such Fixed Rate Term and in an amount approximately equal to the principal amount to which such Fixed Rate Term applies. Borrower understands and agrees that Bank may base its quotation of the Inter-Bank Market Offered Rate upon such offers or other market indicators of the Inter-Bank Market as Bank in its discretion deems appropriate including, but not limited to, the rate offered for U.S. dollar deposits on the London Inter-Bank Market.
- (ii) "LIBOR Reserve Percentage" means the reserve percentage prescribed by the Board of Governors of the Federal Reserve System (or any successor) for "Eurocurrency Liabilities" (as defined in Regulation D of the Federal Reserve Board, as amended), adjusted by Bank for expected changes in such reserve percentage during the applicable Fixed Rate Term.
- (d) "Prime Rate" means at any time the rate of interest most recently announced within Bank at its principal office as its Prime Rate, with the understanding that the Prime Rate is one of Bank's base rates and serves as the basis upon which effective rates of interest are calculated for those loans making reference thereto, and is evidenced by the recording thereof after its announcement in such internal publication or publications as Bank may designate.

INTEREST:

- (a) Interest. The outstanding principal balance of this Note shall bear interest (computed on the basis of a 360-day year, actual days elapsed) either
- (i) at a fluctuating rate per annum equal to the Prime Rate in effect from time to time, or (ii) at a fixed rate per annum determined by Bank to be 1.78000% above LIBOR in effect on the first day of the applicable Fixed Rate Term. When interest is determined in relation to the Prime Rate, each change in the rate of interest hereunder shall become effective on the date each Prime Rate change is announced within Bank. With respect to each LIBOR selection option selected hereunder, Bank is hereby authorized to not the date, principal amount, interest rate and Fixed Rate Term applicable thereto and any payments made thereon on Bank's books and records (either manually or by electronic entry) and/or on any schedule attached to this Note, which notations shall be prima facie evidence of the accuracy of the information noted.
- (b) Selection of Interest Rate Options. At any time any portion of this Note bears interest determined in relation to LIBOR, it may be continued by Borrower at the end of the Fixed Rate Term applicable thereto so that all or a portion thereof bears interest determined in relation to the Prime Rate or to LIBOR for a new Fixed Rate Term designated by Borrower. At any time any portion of this Note bears interest determined in relation to the Prime Rate, Borrower may convert all or a portion thereof so that it bears interest determined in relation to LIBOR for a Fixed Rate Term designated by Borrower. At such time as Borrower requests an advance hereunder or wishes to select a LIBOR option for all or a portion of the outstanding principal balance hereof, and at the end of each Fixed Rate Term, Borrower shall give Bank notice specifying: (i) the interest rate option selected by Borrower; (ii) the

principal amount subject thereto, and (iii) each LIBOR selection, the length of the applicable Fixed Rate Term. Any such notice may be given by telephone so long as, with respect to each LIBOR selection, (A) Bank receives written confirmation from Borrower not later than 3 Business Days after such telephone notice is given, and (B) such notice is given to Bank prior to 10:00 a.m., California time, on the first day of the Fixed Rate Term. For each LIBOR option requested hereunder, Bank will quote the applicable fixed rate to Borrower at approximately 10:00 a.m., California time, on the first day of the Fixed Rate Term. If Borrower does not immediately accept the rate quoted by Bank, any subsequent acceptance by Borrower shall be subject to a redetermination by Bank of the applicable fixed rate; provided however, that if Borrower fails to accept any such rate by 11:00 a.m., California time, on the Business Day such quotation is given, then the quoted rate shall expire and Bank shall have no obligation to permit a LIBOR option to be selected on such day. If no specific designation of interest is made at the time any advance is requested hereunder or at the end of any Fixed Rate Term, Borrower shall be deemed to have made a Prime Rate Interest selection for such advance or the principal amount to which such Fixed Rate Term applied.

(c) Additional LIBOR Provisions

(i) If Bank at any time shall determine that for any reason adequate and reasonable means do not exist for ascertaining LIBOR, then Bank shall promptly give notice thereof to Borrower. If such notice is given and until such notice has been withdrawn by Bank, then (A) no new LIBOR option may be selected by Borrower, and (B) any portion of the outstanding principal balance hereof which bears interest determined in relation to LIBOR, subsequent to the end of the Fixed Rate Term applicable thereto, shall bear interest determined in relation to the Prime Rate.

(ii) If any law, treaty, rule, regulation or determination of a court or governmental authority or any change therein or in the interpretation or application thereof (each, a "Change in Law") shall make it unlawful for Bank (A) to make LIBOR options available hereunder, or (B) to maintain interest rates based on LIBOR, then in the former event, any obligation of Bank to make available such unlawful LIBOR options shall immediately be cancelled, and in the latter event, any such unlawful LIBOR-based interest rates then outstanding shall be converted, at Bank's option, so that interest on the portion of the outstanding principal balance subject thereto is determined in relation to the Prime Rate; provided however, that if any such Change in Law shall permit any LIBOR-based interest rates to remain in effect until the expiration of the Fixed Rate Term applicable thereto, then such permitted LIBOR-based interest rates shall continue in effect until the expiration of such Fixed Rate Term. Upon the occurrence of any of the foregoing events, Borrower shall pay to Bank immediately upon demand such amounts as may be necessary to compensate Bank for any fines, fees, charges, penalties or other costs incurred or payable by Bank as a result thereof and which are attributable to any LIBOR options made available to Borrower hereunder, and any reasonable allocation made by Bank among its operations shall be conclusive and binding upon Borrower.

(iii) If any Change in Law or compliance by Bank with any request or directive (whether or not having the force of law) from any central bank or other governmental authority shall:

(A) subject Bank to any tax, duty or other change with respect to any LIBOR options, or change the basis of taxation of payments to Bank of principal, interests, fees or any other amount payable hereunder (except for changes in the rate of tax on the overall net income of Bank); or

(B) impose, modify or hold applicable any reserve, special deposit, compulsory loan or similar requirement against assets held by, deposits or other liabilities in or for the account of, advances or loans by, or any other acquisition of funds by any office of Bank; or

(C) impose on Bank any other condition;

and the result of any of the foregoing is to increase the cost to Bank of making, renewing or maintaining any LIBOR options hereunder and/or to reduce any amount receivable by Bank in connection therewith, then in any such case, Borrower shall pay to Bank immediately upon demand such amounts as may be necessary to compensate Bank for any additional costs incurred by Bank and/or reductions in amounts received by Bank which are attributable to such LIBOR options. In determining which costs incurred by Bank and/or reductions in amounts received by Bank are attributable to any LIBOR options made available to Borrower hereunder, any reasonable allocation made by Bank among its operations shall be conclusive and binding upon Borrower.

(d) Payment of Interest. Interest accrued on this Note shall be payable on the 1st day of each month, commencing June 1, 1998.

(e) DEFAULT INTEREST. From and after the maturity date of this Note, or such earlier date as all principal owing hereunder becomes due and payable by acceleration or otherwise, the outstanding principal balance of this Note shall bear interest until paid in full at an increased rate per annum (computed on the basis of a 360-day year, actual days elapsed) equal to 4% above the rate of interest from time to time applicable to this Note.

BORROWING AND REPAYMENT:

(a) Borrowing and Repayment. Borrower may from time to time during the term of this Note borrow, partially or wholly repay its outstanding borrowings, and reborrow, subject to all of the limitations, terms and conditions of this Note and of any document executed in connection with or governing this Note; provided however, that the total outstanding borrowings under this Note shall not at any time exceed the principal amount stated above. The unpaid principal balance of this obligation at any time shall be the total amounts advanced hereunder by the holder hereof less the amount of principal payments made hereon by or for any Borrower, which balance may be endorsed hereon

from time to time by the holder. The outstanding principal balance of this Note shall be due and payable in full on May 1, 1999.

(b) Advances. Advances hereunder, to the total amount of the principal sum available hereunder, may be made by the holder at the oral or written request of (i) RUTH UPDAGRAFF or CHARLES EDDY or KEVIN SOULSBY or NORMAN POND, any one acting alone, who are authorized to request advances and direct the disposition of any advances until written notice of the revocation of such authority is received by the holder at the office designated above, or (ii) any person, with respect to advances deposited to the credit of any account of any Borrower with the holder, which advances, when so deposited, shall be conclusively presumed to have been made to or for the benefit of each Borrower regardless of the fact that persons other than those authorized to request advances may have authority to draw against such account. The holder shall have no obligation to determine whether any person requesting an advance is or has been authorized by any Borrower.

(c) Application of Payments. Each payment made on this Note shall be credited first, to any interest then due and second, to the outstanding principal balance hereof. All payments credited to principal shall be applied first, to the outstanding principal balance of this Note which bears interest determined in relation to the Prime Rate, if any, and second, to the outstanding principal balance of this Note which bears interest determined in relation to LIBOR, with such payments applied to the oldest Fixed Rate Term first.

PREPAYMENT:

(a) Prime Rate. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to the Prime Rate at any time, in any amount and without penalty.

(b) LIBOR. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to LIBOR at any time and in the minimum amount of \$10,000,000; provided however, that if the outstanding principal balance of such portion of this Note is less than said amount, the minimum prepayment amount shall be the entire outstanding principal balance thereof. In consideration of Bank providing this prepayment option to Borrower, or if any such portion of this Note shall become due and payable at any time prior to the last day of the Fixed Rate Term applicable thereto by acceleration or otherwise, Borrower shall pay to Bank immediately upon demand a fee which is the sum of the discounted monthly differences for each month from the month of prepayment through the month in which such Fixed Rate Term matures, calculated as follows for each such month;

(i) Determine the amount of interest which would have accrued each month on the amount prepaid at the interest rate applicable to such amount had it remained outstanding until the last day of the Fixed Rate Term applicable thereto.

(ii) Subtract from the amount determined in (i) above the amount of interest which would have accrued for the same month on the amount prepaid for the remaining term of such Fixed Rate Term at LIBOR in effect on the date of prepayment for new loans made for such term and in a principal amount equal to the amount prepaid.

(iii) If the result obtained in (ii) for any month is greater than zero, discount that difference by LIBOR used in (ii) above.

Each Borrower acknowledges that prepayment of such amount may result in Bank incurring additional costs, expenses and/or liabilities, and that it is difficult to ascertain the full extent of such costs, expenses and/or liabilities. Each Borrower, therefore, agrees to pay the above-described prepayment fee and agrees that said amount represents a reasonable estimate of the prepayment costs, expenses and/or liabilities of Bank. If Borrower fails to pay any prepayment fee when due, the amount of such prepayment fee shall thereafter bear interest until paid at a rate per annum 2.000% above the Prime Rate in effect from time to time (computed on the basis of a 360-day year, actual days elapsed). Each change in the rate of interest on any such past due prepayment fee shall become effective on the date each Prime Rate change is announced within Bank.

EVENTS OF DEFAULT:

The occurrence of any of the following shall constitute an "Event of Default" under this Note:

(a) The failure to pay any principal, interest, fees or other charges when due hereunder or under any contract, instrument or document executed in connection with this Note.

(b) The filing of a petition by or against any Borrower, any guarantor of this Note or any general partner or joint venturer in any Borrower which is a partnership or a joint venture (with each such guarantor, general partner and/or joint venturer referred to herein as a "Third Party Obligor") under any provisions of the Bankruptcy Reform Act, Title 11 of the United States Code, as amended or recodified from time to time, or under any similar or other law relating to bankruptcy, insolvency, reorganization or other relief for debtors; the appointment of a receiver, trustee, custodian or liquidator of or for any part of the assets or property of any Borrower or Third Party Obligor; any Borrower or Third Party Obligor becomes insolvent, makes a general assignment for the benefit of creditors or is generally not paying its debts as they become due; or any attachment or like levy on any property of any Borrower or Third Party Obligor.

(c) The death or incapacity of any individual Borrower or Third Party Obligor, or the dissolution or liquidation of any Borrower or Third Party Obligor which is a corporation, partnership, joint venture or other type of entity.

(d) Any default in the payment or performance of any obligation, or any defined event of default, under any provisions of any contract, instrument or document pursuant to which any Borrower or Third Party Obligor has incurred any obligation for borrowed money, any purchase obligation, or any other liability of any kind to any person or entity, including the holder.

(e) Any financial statement provided by any Borrower or Third Party Obligor to Bank proves to be incorrect, false or misleading in any material respect.

(f) Any sale or transfer of all or a substantial or material part of the assets of any Borrower or Third Party Obligor other than in the ordinary course of its business.

(g) Any violation or breach of any provision of, or any defined event of default under, any addendum to this Note or any loan agreement, guaranty, security agreement, deed of trust, mortgage or other document executed in connection with or securing this Note.

MISCELLANEOUS:

(a) Remedies. Upon the occurrence of any Event of Default, the holder of this Note, at the holder's option, may declare all sums of principal and interest outstanding hereunder to be immediately due and payable without presentment, demand, notice of nonperformance, notice of protest, protest or notice of dishonor, all of which are expressly waived by each Borrower, and the obligation, if any, of the holder to extend any further credit hereunder shall immediately cease and terminate. Each Borrower shall pay to the holder immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of the holder's in-house counsel), expended or incurred by the holder in connection with the enforcement of the holder's rights and/or the collection of any amounts which become due to the holder under this Note, and the prosecution or defense of any action in any way related to this Note, including without limitation, any action for declaratory relief, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to any Borrower or any other person or entity.

(b) Obligations Joint and Several. Should more than one person or entity sign this Note as a Borrower, the obligations of each such Borrower shall be joint and several.

(c) Governing Law. This Note shall be governed by and construed in accordance with the laws of the state of California.

IN WITNESS WHEREOF, the undersigned has executed this Note as of the date first written above.

INTEVAC, INC.

By: [SIG]

Title: CFO

Revolving Line of Credit Note (02/98), Page 4

WELLS FARGO BANK, N.A.

ACCOUNT OF:

Intevac, Inc.

Santa Clara RCBO #2690

Office

Documentation

Department

121 Park Center Plaza,

San Jose, CA 95115

Address

May 1, 1998

Date

Customer Obligation No. 4401788691

Fee for renewing Line of Credit in the \$13,000.0 amount of \$10,000,000.00

Total

\$13,000.00

- Check is attached for payment in full of the above amount.
- Wells Fargo Bank is authorized to charge account #4584-704118 for the above amount.
-

WELLS FARGO BANK CORPORATE RESOLUTION:BORROWING

TO: WELLS FARGO BANK, NATIONAL ASSOCIATION

RESOLVED: That this corporation, INTEVAC, INC., proposes to obtain credit from time to time, or has obtained credit, from Wells Fargo Bank, National Association ("Bank").

BE IT FURTHER RESOLVED, that any one of the following officers:

CHIEF FINANCIAL OFFICER OR PRESIDENT

together with any ONE of the following officers:

NONE

of this corporation be and they are hereby authorized and empowered for and on behalf of and in the name of this corporation and as its corporate act and deed:

(a) To borrow money from Bank and to assume any liabilities of any other person or entity to Bank, in such form and on such terms and conditions as shall be agreed upon by those authorized above and Bank, and to sign and deliver to Bank such promissory notes and other evidences of indebtedness for money borrowed or advanced and/or for indebtedness assumed as Bank shall require; such promissory notes or other evidences of indebtedness may provide that advances be requested by telephone communication and by any officer, employee or agent of this corporation so long as the advances are deposited into any deposit account of this corporation with Bank; this corporation shall be bound to Bank by, and Bank may rely upon, any communication or act, including telephone communications, purporting to be done by any officer, employee or agent of this corporation provided that Bank believes, in good faith, that the same is done by such person.

(b) To contract for the issuance by Bank of letters of credit, to discount with Bank notes, acceptances and evidences of indebtedness payable to or due this corporation, to endorse the same and execute such contracts and instruments for repayment thereof to Bank as Bank shall require, and to enter into foreign exchange transactions with or through Bank.

(c) To mortgage, encumber, pledge, convey, grant, assign or otherwise transfer all or any part of this corporation's real or personal property for the purpose of securing the payment of any of the promissory notes, contracts, instruments and other evidences of indebtedness authorized hereby, and to execute and deliver to Bank such deeds of trust, mortgages, pledge agreements, security agreements and/or other related documents as Bank shall require.

(d) To perform all acts and to execute and deliver all documents described above and all other contracts and instruments which Bank deems necessary or convenient to accomplish the purposes of this resolution and/or to perfect or continue the rights, remedies and security interests to be given to Bank pursuant hereto, including without limitation, any modifications, renewals and/or extensions of any of this corporation's obligations to Bank, however evidenced; provided that the aggregate principal amount of all sums borrowed and credits established pursuant to this resolution shall not at any time exceed the sum of \$10,200,000.00 outstanding and unpaid.

Loans made pursuant to a special resolution and loans made by offices of Bank other than the office to which this resolution is delivered shall be in addition to foregoing limitation.

BE IT FURTHER RESOLVED, that the authority hereby conferred is in addition to that conferred by any other resolution heretofore or hereafter delivered by this corporation to Bank and shall continue in full force and effect until Bank shall have received notice in writing, certified by the Secretary of this corporation, of the revocation hereof by a resolution duly adopted by the Board of Directors of this corporation. Any such revocation shall be effective only as to credit which is extended or committed by Bank, or actions which are taken by this corporation

CORPORATE RESOLUTION:BORROWING (08/96), PAGE 1

pursuant to the resolutions contained herein, subsequent to Bank's receipt of such notice. The authority hereby conferred shall be deemed retroactive, and any and all acts authorized herein which were performed prior to the passage of this resolution are hereby approved and ratified.

CERTIFICATION

I, CHARLES B. EDDY III, Secretary of INTEVAC, INC., a corporation created and existing under the laws of the state of CALIFORNIA, do hereby certify and declare that the foregoing is a full, true and correct copy of the resolutions duly passed and adopted by the Board of Directors of said corporation, by written consent of all Directors of said corporation or at a meeting of said Board duly and regularly called, noticed and held on 4/30/98, at which meeting a quorum of the Board of Directors was present and voted in favor of said resolutions; that said resolutions are now in full force and effect; that there is no provision in the Articles of Incorporation or Bylaws of said corporation, or any shareholder agreement, limiting the power of the Board of Directors of said corporation to pass the foregoing resolutions and that such resolutions are in conformity with the provisions of such Articles of Incorporation and Bylaws; and that no approval by the shareholders of, or of the outstanding shares of, said corporation is required with respect to the matters which are the subject of the foregoing resolutions.

IN WITNESS WHEREOF, I have hereunto set my hand and if required by Bank affixed the corporate seal of said corporation, as of 4/30/98.

[sig]

CHARLES B. EDDY III, Secretary

[SEAL]

ARTICLE 5

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM (A) THE CONDENSED CONSOLIDATED BALANCE SHEET AT JUNE 27, 1998 (UNAUDITED) AND THE CONDENSED CONSOLIDATED STATEMENT INCOME (UNAUDITED) FOR THE SIX MONTHS ENDED JUNE 27, 1998 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH (B) FINANCIAL STATEMENTS.

MULTIPLIER: 1,000

PERIOD TYPE	6 MOS
FISCAL YEAR END	DEC 31 1998
PERIOD START	JAN 01 1998
PERIOD END	JUN 27 1998
CASH	765
SECURITIES	66,272
RECEIVABLES	10,460
ALLOWANCES	1,746
INVENTORY	24,837
CURRENT ASSETS	107,840
PP&E	23,097
DEPRECIATION	8,960
TOTAL ASSETS	133,053
CURRENT LIABILITIES	28,778
BONDS	59,460
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	15,237
OTHER SE	29,578
TOTAL LIABILITY AND EQUITY	133,053
SALES	70,036
TOTAL REVENUES	70,036
CGS	50,332
TOTAL COSTS	50,332
OTHER EXPENSES	13,925
LOSS PROVISION	250
INTEREST EXPENSE	2,073
INCOME PRETAX	5,186
INCOME TAX	1,712
INCOME CONTINUING	3,474
DISCONTINUED	1,005
EXTRAORDINARY	0
CHANGES	0
NET INCOME	4,479
EPS PRIMARY	0.37
EPS DILUTED	0.36

End of Filing

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