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ESPEY MFG & ELECTRONICS CORP  
Form 10QSB  
May 14, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-QSB

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

For the Quarterly Period Ended March 31, 2008

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number I-4383

ESPEY MFG. & ELECTRONICS CORP.  
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(Exact name of registrant as specified in charter)

NEW YORK  
-----

14-1387171  
-----

(State of Incorporation) (I.R.S. Employer's Identification No.)

233 Ballston Avenue, Saratoga Springs, New York 12866

(Address of principal executive offices)

Issuer's telephone number, including area code 518-584-4100  
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Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.

Class -----	Outstanding at May 14, 2008 -----
Common stock, \$.33-1/3 par value	2,324,773 shares

Transitional Small Business Disclosure Format YES  NO

ESPEY MFG. & ELECTRONICS CORP.

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Quarterly Report on Form 10-QSB

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## PART I: FINANCIAL INFORMATION

ESPEY MFG. & ELECTRONICS CORP.

Balance Sheet (Unaudited)

March 31, 2008

### ASSETS:

Cash and cash equivalents	\$ 6,588,780
Short term investments	6,847,000
Trade accounts receivable, net	3,795,069
Other receivables	4,873
ESOP receivable due to dividends on unallocated shares	129,681
 Inventories:	
Raw materials	1,622,904
Work-in-process	2,852,379
Costs relating to contracts in process, net of advance payments of \$230,700 at March 31, 2008	6,086,123
	-----

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Total inventories	10,561,406
Deferred income taxes	180,769
Prepaid expenses and other current assets	340,970
	-----
Total current assets	28,448,548
	-----
Property, plant and equipment, net	2,989,879
Loan receivable	73,605
	-----
Total assets	\$ 31,512,032
	=====

LIABILITIES AND STOCKHOLDERS' EQUITY:

Accounts payable	\$ 1,127,907
Accrued expenses:	
Salaries, wages and commissions	182,515
Vacation	527,616
Other	41,974
Payroll and other taxes withheld and accrued	41,983
Income taxes payable	175,723
	-----
Total current liabilities	2,097,718
	-----
Deferred income taxes	148,036
	-----
Total liabilities	2,245,754
	-----
Common stock, par value \$.33-1/3 per share.	
Authorized 10,000,000 shares; issued 3,029,874 shares	
on March 31, 2008. Outstanding 2,324,773 (includes	
231,042 Unearned ESOP Shares) on March 31, 2008	1,009,958
Capital in excess of par value	13,252,634
Retained earnings	25,278,350
Less: Unearned ESOP Shares	(3,600,459)
Treasury shares, cost of 705,101 shares on March 31, 2008	(6,674,205)
	-----
Total stockholders' equity	29,266,278
	-----
Total liabilities and stockholders' equity	\$ 31,512,032
	=====

See accompanying notes to the financial statements.

ESPEY MFG. & ELECTRONICS CORP.  
 Statements of Income (Unaudited)  
 Three and Nine Months Ended March 31, 2008 and 2007

Three Months		Nine Months	
2008	2007	2008	2007
-----	-----	-----	-----

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Net sales	\$ 6,479,020	\$ 8,059,695	\$19,512,950	\$20,25
Cost of sales	4,301,589	6,443,561	14,303,824	15,97
	-----	-----	-----	-----
Gross profit	2,177,431	1,616,134	5,209,126	4,27
Selling, general and administrative expenses	647,998	697,740	2,017,370	2,13
	-----	-----	-----	-----
Operating income	1,529,433	918,394	3,191,756	2,13
	-----	-----	-----	-----
Other income (expense)				
Interest and dividend income	137,594	151,896	537,039	44
Other	16,186	9,589	64,748	4
	-----	-----	-----	-----
	153,780	161,485	601,787	49
	-----	-----	-----	-----
Income before income taxes	1,683,213	1,079,879	3,793,543	2,62
Provision for income taxes	584,008	365,849	1,305,669	88
	-----	-----	-----	-----
Net income	\$ 1,099,205	\$ 714,030	\$ 2,487,874	\$ 1,73
	=====	=====	=====	=====
Net income per share:				
Basic	\$ 0.53	\$ 0.35	\$ 1.20	\$
Diluted	\$ 0.53	\$ 0.34	\$ 1.18	\$
	-----	-----	-----	-----
Weighted average number of shares outstanding:				
Basic	2,083,659	2,053,545	2,074,743	2,04
Diluted	2,098,596	2,077,994	2,101,177	2,06
	-----	-----	-----	-----
Dividends per share:	\$ 1.70	\$ 0.15	\$ 2.05	\$
	=====	=====	=====	=====

See accompanying notes to the financial statements.

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ESPEY MFG. & ELECTRONICS CORP.  
Statements of Cash Flows (Unaudited)  
Nine Months Ended March 31, 2008 and 2007

Cash Flows From Operating Activities:  
Net income

2008  
-----  
\$ 2,487,874

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Adjustments to reconcile net income to net cash provided by operating activities:	
Excess tax benefits from share-based compensation	83,471
Stock option compensation	115,822
Depreciation	368,147
ESOP compensation expense	381,111
Loss on disposal of assets	(385)
Deferred income tax	(33,968)
Changes in assets and liabilities:	
Increase in trade receivable, net	(774,588)
(Increase) decrease in other receivables	(1,425)
Increase in ESOP receivable due to dividends on unallocated shares	(129,681)
Decrease in inventories	587,921
Decrease (increase) in prepaid expenses and other current assets	207,242
Increase in accounts payable	146,956
Increase in accrued salaries, wages and commissions	20,313
Decrease in other accrued expenses	(4,061)
(Decrease) increase in vacation accrual	(54,865)
(Decrease) increase in payroll and other taxes withheld and accrued	(83)
Decrease in income taxes payable	(107,691)
Decrease in ESOP payable	(381,111)
	-----
Net cash provided by operating activities	2,910,999
	-----
Cash Flows From Investing Activities:	
Additions to property, plant and equipment	(423,131)
Proceeds on sale of assets, net	--
Payment for loan receivable	(80,000)
Proceeds from return of loan receivable	6,395
Purchase of short term investments	(5,887,000)
Maturity of short term investments	3,360,000
	-----
Net cash used in investing activities	(3,023,736)
	-----
Cash Flows From Financing Activities:	
Sale of treasury stock	--
Dividends on common stock	(4,263,849)
Purchase of treasury stock	(716,363)
Proceeds from exercise of stock options	502,147
Excess tax benefits from share-based compensation	83,471
	-----
Net cash (used in) provided by financing activities	(4,394,594)
	-----
(Decrease) increase in cash and cash equivalents	(4,507,331)
Cash and cash equivalents, beginning of period	11,096,111
	-----
Cash and cash equivalents, end of period	6,588,780
	=====
Supplemental disclosures of cash flow information:	
Income Taxes Paid	\$ 1,290,000
	=====
Non-cash investing and financing activities:	
See accompanying notes to the financial statements.	

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ESPEY MFG. & ELECTRONICS CORP.  
Notes to Financial Statements (Unaudited)  
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### Note 1. Basis of Presentation

In the opinion of management the accompanying unaudited financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of the results for such periods. The results for any interim period are not necessarily indicative of the results to be expected for the full fiscal year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with United States generally accepted accounting principles have been condensed or omitted. These financial statements should be read in conjunction with the Company's most recent audited financial statements included in its report on Form 10-KSB for the year ended June 30, 2007.

### Note 2. Net income per Share

Basic net income per share excludes dilution and is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the income of the Company. As Unearned ESOP shares are released or committed-to-be-released the shares become outstanding for earnings-per-share computations.

### Note 3. Stock Based Compensation

Effective July 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (Revised 2004), "Share-Based Payment" ("SFAS No. 123 (R)"), which amends SFAS No. 123 and supersedes Accounting Principles Board Opinion ("APB") No. 25 in establishing standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, as well as transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that maybe settled by the issuance of those equity instruments. SFAS No. 123(R) requires that the cost resulting from all share-based payment transactions be recognized in the financial statements based on the fair value of the share-based payment. SFAS No.123(R) establishes fair value as the measurement objective in accounting for share-based payment transactions with employees, except for equity instruments held by employee share ownership plans. As allowed under SFAS No. 123(R), the Company elected the modified prospective method of adoption, under which compensation cost is recognized in the financial statements beginning with the effective date of SFAS No. 123(R) for all share-based payments granted after that date, and for all unvested awards granted prior to the effective date of SFAS No. 123(R). Accordingly, prior period amounts have not been restated.

Total stock-based compensation expense recognized in the Statement of Income for the three months ended March 31, 2008 and 2007, was \$32,491 and \$43,836, respectively, before income taxes. The related total deferred tax benefit was approximately \$2,487 and \$3,470, for the three months ended March 31, 2008 and 2007, respectively. Total stock-based compensation expense recognized in the Statement of Income for the nine months ended March 31, 2008 and 2007, was \$115,822 and \$119,856, respectively, before income taxes. The related total deferred tax benefit was approximately \$8,991 and \$9,462, for the nine months ended March 31, 2008 and 2007, respectively. Prior to the adoption of SFAS No. 123(R), the Company presented all tax benefits for deductions resulting from the

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exercise of stock options as operating cash flows in the Statements of Cash Flows. SFAS No. 123(R) requires the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options to be classified and reported as both an operating cash outflow and a financing cash inflow on a prospective basis upon adoption.

As of March 31, 2008, there was approximately \$55,201 of unrecognized compensation cost related to stock option awards that is expected to be recognized as expense over a period of 1 year.

The Company has one employee stock option plan under which options may be granted, the 2007 Stock Option and Restricted Stock Plan (the "2007 Plan"). The Board of Directors may grant options to acquire shares of common stock to employees of the Company at the fair market value of the common stock on the date of grant. Generally, options granted have a two-year vesting period based on two years of continuous service and have a ten-year

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contractual life. Option grants provide for accelerated vesting if there is a change in control. Shares issued upon the exercise of options are from those held in Treasury. The 2007 Plan was approved by the Company's shareholders at the Company's Annual Meeting on November 30, 2007 and supercedes the Company's 2000 Stock Option Plan (the "2000 Plan"). Options covering 400,000 shares are authorized for issuance under the 2007 Plan, of which zero have been granted as of March 31, 2008. While no further grants of options may be made under the 2000 Plan, as of March 31, 2008, 96,100 options were outstanding of which 28,700 are vested and exercisable.

SFAS No. 123(R) requires the use of a valuation model to calculate the fair value of stock-based awards. The Company has elected to use the Black-Scholes option valuation model, which incorporates various assumptions including those for volatility, expected life and interest rates.

The table below outlines the weighted average assumptions that the Company used to calculate stock-based employee compensation for the three and nine months ended March 31, 2008:

	Three Months Ended March 31, 2008	Nine Months Ended March 31, 2008
	-----	-----
Dividend yield	2.59%	2.40%
Expected stock price volatility	20.50%	22.29%
Risk-free interest rate	4.80%	4.54%
Expected option life (in years)	5	5
Weighted average fair value per share of options granted during the period	\$3.95	\$4.04

The Company pays dividends quarterly and does plan to pay dividends in the foreseeable future. Expected stock price volatility is based on the historical volatility of the Company's stock. The risk-free interest rate is based on the implied yield available on U.S. Treasury issues with an equivalent term approximating the expected life of the options. The expected option life (in years) represents the estimated period of time until exercise and is based on the safe harbor calculation under SFAS No. 123.

The following table summarizes stock option activity during the nine months ended March 31, 2008:

Employee Stock Options Plan

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	Number of Shares Subject To Option	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Balance at July 1, 2007	138,800	\$15.77	7.38
Granted	--	--	--
Exercised	(41,100)	\$12.22	--
Forfeited or expired	(1,600)	\$18.05	--
Balance at March 31, 2008	96,100	\$17.25	8.03
Exercisable at March 31, 2008	28,700	\$15.37	6.88

The intrinsic value of stock options exercised was \$240,245 and \$106,108 during the nine months ended March 31, 2008 and 2007, respectively. The intrinsic value of stock options outstanding and exercisable as of March 31, 2008 and 2007 was \$132,828 and \$389,485, respectively.

Note 4. Commitments and Contingencies

The Company at certain times enters into standby letters of credit agreements with financial institutions primarily relating to the guarantee of future performance on certain contracts. Contingent liabilities on outstanding standby letters of credit agreements aggregated to zero at March 31, 2008. As a government contractor, the Company is continually subject to audit by various agencies of the U.S. Government to determine compliance with various procurement laws and regulations. As a result of such audits and as part of normal business operations of the Company, various claims and charges can be asserted against the Company. It is not possible to predict the outcome of such actions. Currently the Company has no claims or assertions against it.

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Note 5. Recently Issued Accounting Standards

In July 2006, the FASB issued Interpretation No. ("FIN") 48, Accounting for Uncertainty in Income Taxes-An Interpretation of FASB Statement No. 109, which prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In particular, this interpretation requires uncertain tax positions to be recognized only if they are "more-likely-than-not" to be upheld based on their technical merits. Additionally, the measurement of the tax position will be based on the largest amount that is determined to have greater than a 50% likelihood of realization upon ultimate settlement. Any resulting cumulative effect of applying the provisions of FIN 48 upon adoption would be reported as an adjustment to the beginning balance of retained earnings in the period of adoption. FIN 48 was effective beginning July 1, 2007. The adoption of FIN 48 did not have a material effect on the Company's financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standard ("SFAS") No. 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies to other accounting pronouncements that require or permit fair value measurements, but does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those years. The Company is currently evaluating the effect of the guidance contained in SFAS 157 and does not expect the implementation to have a material



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effect on the Company's financial statements.

### Note 6. Employee Stock Ownership Plan

The Company sponsors a leveraged employee stock ownership plan (the "ESOP") that covers all nonunion employees who work 1,000 or more hours per year and are employed on June 30.

The Company makes annual contributions to the ESOP equal to the ESOP's debt service less dividends on unallocated shares received by the ESOP. All dividends on unallocated shares received by the ESOP are used to pay debt service. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings. As the debt is repaid, shares are released and allocated to active employees, based on the proportion of debt service paid in the year. The Company accounts for its ESOP in accordance with Statement of Position 93-6. Accordingly, the shares purchased by the ESOP are reported as Unearned ESOP Shares in the statement of financial position. As shares are released or committed-to-be-released, the Company reports compensation expense equal to the current average market price of the shares, and the shares become outstanding for earnings-per-share (EPS) computations. ESOP compensation expense was \$117,937 for the quarter ended March 31, 2008 and \$381,111 for the nine-month period ending March 31, 2008. The ESOP shares as of March 31, 2008 were as follows:

Allocated Shares	418,076
Committed-to-be-released shares	18,125
Unreleased shares	231,042
	-----
Total shares held by the ESOP	667,243
	=====
Fair value of unreleased shares at March 31, 2008	\$ 4,620,840
	=====

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

Espey Mfg. & Electronics Corp. (the "Company") located in Saratoga Springs, New York, is engaged principally in the development, design, production and sale of specialized electronic power supplies, a wide variety of transformers and other types of iron-core components, and electronic system components. In some cases, the Company manufactures such products in accordance with pre-developed mechanical and electrical requirements ("build to print"). In other cases, the Company is responsible for both the overall design and manufacture of the product. The Company does not generally manufacture standardized components and does not have a product line. The products manufactured by the Company find application principally in (i) shipboard and land based radar, (ii) locomotives, (iii) aircraft, (iv) short and medium range communication systems, (v) navigation systems, and (vi) land-based military vehicles.

Business is solicited from large industrial manufacturers and defense companies, the government of the United States, foreign governments and major foreign electronic equipment companies. In certain countries the Company has external sales representatives to help solicit and coordinate foreign contracts. The Company is also on the eligible list of contractors of the United States

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Department of Defense and generally is automatically solicited by such agencies for procurement needs falling within the major classes of products produced by the Company. In addition, the Company directly solicits bids from the United States Department of Defense for prime contracts.

There is competition in all classes of products manufactured by the Company from divisions of the largest electronic companies, as well as many small companies. The Company's sales do not represent a significant share of the industry's market for any class of its products. The principal methods of competition for electronic products of both a military and industrial nature include, among other factors, price, product performance, the experience of the particular company and history of its dealings in such products. The Company, as well as other companies engaged in supplying equipment for military use, is subject to various risks, including, without limitation, dependence on United States and foreign government appropriations and program allocations, the competition for available military business, and government termination of orders for convenience.

In the first nine months of fiscal 2008, the Company received approximately \$16.3 million in new orders. These orders include both follow-on production quantities for mature products and engineering development orders which will enable the Company to utilize its engineering expertise in developing new customer specific products. Some of these products, once developed, will be produced in the Company's manufacturing facility and are expected to provide large production order quantities over several years. These orders are in line with the Company's strategy of getting involved in long-term high quantity military and industrial products. The Company's backlog is \$41.8 million at May 12, 2008, which includes \$27.5 million from the two most significant customers in the first nine months of fiscal 2008.

The sales backlog of approximately \$33.0 million at March 31, 2008 gives the Company a solid base of future sales. Management expects sales for fiscal 2008 to be slightly less than fiscal 2007 sales. In addition to the backlog, the Company currently has outstanding quotations and expected business representing approximately \$34.7 million in the aggregate for both repeat and new programs.

Sales to two significant customers in the first nine months of fiscal 2008 and 2007 represented 58.0% and 58.9%, respectively, of the Company's total sales. While the Company has always had a small number of customers that account for a large percentage of its total sales in any given year, management is pursuing business opportunities involving significant product programs with new and current customers with an overall objective of lowering the concentration of sales and minimizing the impact of a significant customer or excessive reliance upon a single major product program of a particular customer. The backlog at March 31, 2008 of \$33.0 million includes \$23.0 million from the two most significant customers in the first nine months of fiscal 2008.

The outstanding quotations encompass various new and previously manufactured power supplies, transformers, and subassemblies. However, there can be no assurance that the Company will acquire any or all of the anticipated orders described above, many of which are subject to allocations of the United States defense spending and factors affecting the defense industry and military procurement generally.

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The total backlog for the Company of \$33.0 million at March 31, 2008, up \$0.9 million from March 31, 2007, and up \$1.6 million from December 31, 2007, represents the estimated remaining sales value of work to be performed under firm contracts. These contracts include significant orders for military and industrial power supplies, and contracts to manufacture certain customer

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products in accordance with pre-engineered requirements.

Management, along with the Board of Directors, continues to evaluate the need and use of the Company's working capital. Expectations are that the working capital will be required to fund any increase in orders over the next several quarters, dividend payments, and general operations of the business. Also, the Mergers and Acquisitions Committee of the Board of Directors continues to evaluate potential strategic options on a periodic basis.

### Critical Accounting Policies and Estimates

Management believes our most critical accounting policies include revenue recognition and estimates to completion.

A significant portion of our business is comprised of development and production contracts. Generally, revenues on long-term fixed-price contracts are recorded on a percentage of completion basis using units of delivery as the measurement basis for progress toward completion.

Percentage of completion accounting requires judgment relative to expected sales, estimating costs and making assumptions related to technical issues and delivery schedule. Contract costs include material, subcontract costs, labor and an allocation of overhead costs. The estimation of cost at completion of a contract is subject to numerous variables involving contract costs and estimates as to the length of time to complete the contract. Given the significance of the estimation processes and judgments described above, it is possible that materially different amounts of expected sales and contract costs could be recorded if different assumptions were used, based on changes in circumstances, in the estimation process. When a change in expected sales value or estimated cost is determined, changes are reflected in current period earnings.

### Results of Operations

Net sales for the three months ended March 31, 2008 were \$6,479,020 as compared to \$8,059,695 for the same period in 2007, representing a 19.6% decrease. Net sales for the nine months ended March 31, 2008 were \$19,512,950 as compared to \$20,250,921 for the same period in 2007, representing a 3.6% decrease. Generally, these decreases can be attributed to the contract specific nature of the Company's business. Also, one large program currently in production experienced vendor delays with material needed to produce power supplies, which caused decreased sales for the quarter. New orders received in the first nine months of fiscal 2008 were approximately \$16.3 million, representing a 10.9% increase over the amount of new orders received in the first nine months of fiscal 2007. The sales order backlog has been over \$30 million for twelve consecutive fiscal quarters and expectations are this trend will continue.

For the three months ended March 31, 2008 and 2007 gross profits were \$2,177,431 and \$1,616,134, respectively. Gross profit as a percentage of sales was 33.6% and 20.1%, for the three months ended March 31, 2008 and 2007, respectively. For the nine months ended March 31, 2008 and 2007 gross profits were \$5,209,126 and \$4,271,663, respectively. Gross profit as a percentage of sales was 26.7% and 21.1%, for the nine months ended March 31, 2008 and 2007, respectively. The primary factor in determining gross profit and net income is product mix. The gross profits on mature products and build to print contracts are higher as compared to products which are still in the engineering development stage or in the early stages of production. In any given accounting period the mix of product shipments between higher margin mature programs and less mature programs including loss contracts, has a significant impact on gross profit and net income. The improved gross profit and gross profit percentage in the three and nine months ended March 31, 2008, was the result of shipping mature products with favorable margins. Management continues to evaluate the Company's workforce to ensure that production and overall execution of the backlog orders and

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additional anticipated orders are successfully obtained and executed. Employment of full time equivalents at March 31, 2008 was 173 compared to 182 people at March 31, 2007.

Selling, general and administrative expenses were \$647,998 for the three months ended March 31, 2008; a decrease of \$49,742 compared to the three months ended March 31, 2007. Selling, general and administrative expenses were \$2,017,370 for the nine months ended March 31, 2008; a decrease of \$120,093 compared to the nine months ended March 31, 2007. The decrease is due primarily to reduced headcount.

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Other income for three months ended March 31, 2008 decreased as compared to the three months ended March 31, 2007 due to decreased interest income on the Company's cash and cash equivalents and short-term investments. Lower interest rates and lower cash and cash equivalents due to the special dividend of \$1.50 per share paid to shareholders on March 20, 2008, caused this decrease. Other income for the nine months ended March 31, 2008 increased as compared to the nine months ended March 31, 2007 due to higher balances of cash and cash equivalents for a majority of the nine month period ended March 31, 2008. The Company does not believe that there is a significant risk associated with its investment policy, since at March 31, 2008 all of the investments are primarily represented by short-term liquid investments including certificates of deposit and money market funds.

The effective income tax rate at March 31, 2008 and 2007 was 34.4% and 33.8%, respectively. The effective tax rate is less than the statutory tax rate mainly due to the foreign exportation benefit the Company receives on its international sales, the Qualified Production Activities benefit, and the benefit derived from the ESOP dividends paid on allocated shares.

Net income for the three months ended March 31, 2008, was \$1,099,205 or \$.53 per share, both basic and diluted, compared to \$714,030 or \$.35 and \$.34 per share, basic and diluted, respectively, for the three months ended March 31, 2007. Net income for the nine months ended March 31, 2008, was \$2,487,874 or \$1.20 and \$1.18 per share, basic and diluted, respectively, compared to \$1,736,991 or \$.85 and \$.84 per share, basic and diluted, respectively, for the nine months ended March 31, 2007. The increase in net income per share was due to higher gross profit as a percentage of sales, a decrease in selling, general and administrative expenses, and increased interest income.

### Liquidity and Capital Resources

The Company's working capital is an appropriate indicator of the liquidity of its business, and during the past three fiscal years, the Company, when possible, has funded all of its operations with cash flows resulting from operating activities and when necessary from its existing cash and investments. The Company did not borrow any funds during the last three fiscal years. Management had available a \$3,000,000 line of credit to help fund further growth or working capital needs, but did not anticipate the need for any borrowed funds in the foreseeable future and therefore did not renew the line of credit which expired November 30, 2007.

The Company's working capital as of March 31, 2008 was approximately \$26.4 million. During the three months ended March 31, 2008 and 2007 the Company repurchased 7,500 and 10,196 shares, respectively, of its common stock from the Company's Employee Retirement Plan and Trust ("ESOP"), for a total purchase price of \$144,600 and \$187,861, respectively. During the nine months ended March 31, 2008 and 2007 the Company repurchased 33,220 and 16,269 shares, respectively, of its common stock for a total purchase price of \$716,363 and

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\$298,064, respectively. Under existing authorizations from the Company's Board of Directors, as of March 31, 2008, management is authorized to purchase an additional \$1,283,637 million of Company stock.

	Nine Months Ended March 31,	
	2008	2007
	-----	-----
Net cash provided by operating activities	\$2,910,999	\$2,542,439
Net cash used in investing activities	(3,023,736)	(659,691)
Net cash used in financing activities	(4,394,594)	(817,279)

Net cash provided by operating activities fluctuates between periods primarily as a result of differences in net income, the timing of the collection of accounts receivable, purchase of inventory, level of sales and payment of accounts payable. Net cash used in investing activities increased in the first nine months of fiscal 2008 due to the increase in purchases of short-term investments. The increase in cash used in financing activities is due primarily to the increase in purchases of treasury stock and the increase in dividends paid.

The Company currently believes that the cash flow generated from operations and when necessary, from cash and cash equivalents, will be sufficient to meet its long-term funding requirements for the foreseeable future.

During the nine months ended March 31, 2008 and 2007, the Company expended \$423,131 and \$371,701, respectively, for plant improvements and new equipment. The Company has budgeted approximately \$400,000 for new equipment and plant improvements in fiscal 2008 (and does not anticipate additional expenditures of this nature during the fourth quarter).

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The Company at certain times enters into standby letters of credit agreements with financial institutions primarily relating to the guarantee of future performance on certain contracts. Contingent liabilities on outstanding standby letters of credit agreements aggregated to zero at March 31, 2008.

### CAUTIONARY STATEMENT FOR PURPOSES OF THE "SAFE HARBOR" PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This report contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. The terms "believe," "anticipate," "intend," "goal," "expect," and similar expressions may identify forward-looking statements. These forward-looking statements represent the Company's current expectations or beliefs concerning future events. The matters covered by these statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those set forth in the forward-looking statements, including the Company's dependence on timely development, introduction and customer acceptance of new products, the impact of competition and price erosion, supply and manufacturing constraints, potential new orders from customers and other risks and uncertainties. The foregoing list should not be construed as exhaustive, and the Company disclaims any obligation subsequently to revise any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made.

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### Item 3. Controls and Procedures

(a) The Company's management, with the participation of the Company's chief executive officer and chief financial officer, carried out an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report on Form 10-QSB. Based on such evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

(b) There have been no changes in our internal controls over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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### PART II: Other Information and Signatures

#### Item 1. Legal Proceedings

None

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

(a) None

(c) Securities Repurchased

#### Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program	Maximum (or Appr Dollar V of Sha that Ma Be Purc Under th or Progr
March 1 to March 31, 2008	7,500	\$19.28	7,500	\$1,283,637

(1) Pursuant to a prior Board of Directors authorization, as of March 31, 2008 the Company can repurchase up to \$1,283,637 of its common stock pursuant to an ongoing plan.

#### Item 3. Defaults on Senior Securities

None

#### Item 4. Submission of Matters to a Vote of Security Holders

None

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Item 5. Other Information

None

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Item 6. Exhibits

(a) Exhibits

- 31.1 Certification of the Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of the Principal Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of the Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

S I G N A T U R E S

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.

ESPEY MFG. & ELECTRONICS CORP.

/s/ Howard Pinsley

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Howard Pinsley, President and  
Chief Executive Officer

/s/ David O'Neil

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David O'Neil, Treasurer and  
Principal Financial Officer

May 14, 2008

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Date

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