COMTECH TELECOMMUNICATIONS CORP /DE/
Form 10-Q
March 06, 2014
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 January 31, 2014
Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-7928

(Exact name of registrant as specified in its charter)

Delaware	11-2139466
(State or other jurisdiction of incorporation /organization)	(I.R.S. Employer Identification Number)

68 South Service Road, Suite 230, Melville, NY	11747
(Address of principal executive offices)	(Zip Code)

(631) 962-7000
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of March 4, 2014, the number of outstanding shares of Common Stock, par value $.10 per share, of the registrant was 15,326,717 shares.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

Assets	January 31, 2014 (Unaudited)	July 31, 2013
Current assets:		
Cash and cash equivalents	$317,993,000	356,642,000
Accounts receivable, net	56,879,000	49,915,000
Inventories, net	70,095,000	65,482,000
Prepaid expenses and other current assets	11,846,000	7,428,000
Deferred tax asset, net	10,030,000	10,184,000
Total current assets	466,843,000	489,651,000
Property, plant and equipment, net	20,332,000	20,333,000
Goodwill	137,354,000	137,354,000
Intangibles with finite lives, net	29,341,000	32,505,000
Deferred financing costs, net	471,000	1,093,000
Other assets, net	873,000	879,000
Total assets	$655,214,000	681,815,000
Liabilities and Stockholders' Equity		
Current liabilities:		
Convertible senior notes, current	$200,000,000	200,000,000
Accounts payable	18,600,000	18,390,000
Accrued expenses and other current liabilities	25,926,000	29,892,000
Dividends payable	4,731,000	4,531,000
Customer advances and deposits	15,337,000	14,749,000
Interest payable	1,529,000	1,529,000
Total current liabilities	266,123,000	269,091,000
Other liabilities	4,161,000	3,958,000
Income taxes payable	3,162,000	2,963,000
Deferred tax liability, net	1,823,000	1,741,000
Total liabilities	275,269,000	277,753,000
Commitments and contingencies (See Note 19)		
Stockholders' equity:		
Preferred stock, par value $.10 per share; shares authorized and unissued 2,000,000	—	—
Common stock, par value $.10 per share; authorized 100,000,000 shares; issued 29,186,440 shares and 29,066,792 shares at January 31, 2014 and July 31, 2013, respectively	2,919,000	2,907,000
Additional paid-in capital	366,889,000	363,888,000
Retained earnings	405,375,000	403,398,000
	775,183,000	770,193,000
Less:		
Treasury stock, at cost (13,544,493 shares and 12,608,501 shares at January 31, 2014 and July 31, 2013, respectively)	(395,238,000)	(366,131,000)
Total stockholders' equity	379,945,000	404,062,000
Total liabilities and stockholders' equity	$655,214,000	681,815,000

See accompanying notes to condensed consolidated financial statements.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
Net sales	$85,499,000	74,577,000	168,867,000	165,530,000
Cost of sales	48,130,000	42,337,000	95,120,000	91,487,000
Gross profit	37,369,000	32,240,000	73,747,000	74,043,000
Expenses:				
Selling, general and administrative	16,349,000	15,433,000	32,547,000	32,243,000
Research and development	8,266,000	9,278,000	16,765,000	19,327,000
Amortization of intangibles	1,582,000	1,582,000	3,164,000	3,164,000
	26,197,000	26,293,000	52,476,000	54,734,000
Operating income	11,172,000	5,947,000	21,271,000	19,309,000
Other expenses (income):				
Interest expense	1,998,000	2,030,000	4,016,000	4,141,000
Interest income and other	(228,000)	(315,000)	(501,000)	(591,000)
Income before provision for income taxes	9,402,000	4,232,000	17,756,000	15,759,000
Provision for income taxes	3,419,000	1,867,000	6,468,000	5,959,000
Net income	$5,983,000	2,365,000	11,288,000	9,800,000
Net income per share (See Note 5):				
Basic	$0.37	0.14	0.70	0.57
Diluted	$0.32	0.14	0.60	0.51
Weighted average number of common shares outstanding – basic	15,970,000	17,300,000	16,212,000	17,340,000
Weighted average number of common and common equivalent shares outstanding – diluted	22,487,000	17,401,000	22,552,000	23,394,000
Dividends declared per issued and outstanding common share as of the applicable dividend record date	$0.30	0.275	0.575	0.55

See accompanying notes to condensed consolidated financial statements.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
SIX MONTHS ENDED JANUARY 31, 2014 AND 2013
(Unaudited)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Treasury Stock		Stockholders' Equity
	Shares	Amount			Shares	Amount	
Balance as of July 31, 2012	28,931,679	$2,893,000	$361,458,000	$404,227,000	11,564,059	$(339,177,000)	$429,401,000
Equity-classified stock award compensation	—	—	1,532,000	—	—	—	1,532,000
Proceeds from exercise of options	25,800	3,000	443,000	—	—	—	446,000
Proceeds from issuance of employee stock purchase plan shares	21,222	2,000	476,000	—	—	—	478,000
Cash dividends declared	—	—	—	(9,562,000)	—	—	(9,562,000)
Net excess income tax benefit from settlement of stock-based awards	—	—	14,000	—	—	—	14,000
Reversal of deferred tax assets associated with expired and unexercised stock-based awards	—	—	(2,955,000)	—	—	—	(2,955,000)
Repurchases of common stock	—	—	—	—	397,798	(10,477,000)	(10,477,000)
Net income	—	—	—	9,800,000	—	—	9,800,000
Balance as of January 31, 2013	28,978,701	$2,898,000	$360,968,000	$404,465,000	11,961,857	$(349,654,000)	$418,677,000
Balance as of July 31, 2013	29,066,792	$2,907,000	$363,888,000	$403,398,000	12,608,501	$(366,131,000)	$404,062,000
Equity-classified stock award compensation	—	—	1,990,000	—	—	—	1,990,000

Equity-classified stock awards issued	—	—	139,000	—	—	—	139,000
Proceeds from exercise of options	95,425	10,000	2,549,000	—	—	—	2,559,000
Proceeds from issuance of employee stock purchase plan shares	20,727	2,000	428,000	—	—	—	430,000
Issuance of common stock for vested performance shares, net of minimum withholding tax and deferrals	3,496	—	(25,000)	—	—	—	(25,000)
Cash dividends declared	—	—	—	(9,260,000)	—	—	(9,260,000)
Accrual of dividend equivalents	—	—	—	(51,000)	—	—	(51,000)
Net income tax shortfall from settlement of stock-based awards	—	—	(155,000)	—	—	—	(155,000)
Reversal of deferred tax assets associated with expired and unexercised stock-based awards	—	—	(1,925,000)	—	—	—	(1,925,000)
Repurchases of common stock	—	—	—	—	935,992	(29,107,000)	(29,107,000)
Net income	—	—	—	11,288,000	—	—	11,288,000
Balance as of January 31, 2014	29,186,440	$2,919,000	$366,889,000	$405,375,000	13,544,493	$(395,238,000)	$379,945,000

See accompanying notes to condensed consolidated financial statements.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six months ended January 31,	
	2014	2013
Cash flows from operating activities:		
Net income	$11,288,000	9,800,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property, plant and equipment	3,383,000	4,019,000
Amortization of intangible assets with finite lives	3,164,000	3,164,000
Amortization of stock-based compensation	2,016,000	1,551,000
Deferred financing costs	697,000	706,000
Change in fair value of contingent earn-out liability	(239,000)	(3,267,000)
Loss on disposal of property, plant and equipment	42,000	32,000
Provision for (benefit from) allowance for doubtful accounts	92,000	(107,000)
Provision for excess and obsolete inventory	1,485,000	1,276,000
Excess income tax benefit from stock-based award exercises	(16,000)	(19,000)
Deferred income tax (benefit) expense	(1,689,000)	1,029,000
Changes in assets and liabilities:		
Accounts receivable	(7,056,000)	14,113,000
Inventories	(5,939,000)	905,000
Prepaid expenses and other current assets	(4,308,000)	(740,000)
Other assets	6,000	15,000
Accounts payable	210,000	(6,899,000)
Accrued expenses and other current liabilities	(3,574,000)	(8,645,000)
Customer advances and deposits	409,000	(3,986,000)
Other liabilities	149,000	588,000
Income taxes payable	(66,000)	(2,141,000)
Net cash provided by operating activities	54,000	11,394,000
Cash flows from investing activities:		
Purchases of property, plant and equipment	(3,424,000)	(2,457,000)
Net cash used in investing activities	(3,424,000)	(2,457,000)
Cash flows from financing activities:		
Repurchases of common stock	(29,107,000)	(10,477,000)
Cash dividends paid	(9,053,000)	(14,335,000)
Proceeds from exercises of stock options	2,559,000	446,000
Proceeds from issuance of employee stock purchase plan shares	430,000	478,000
Excess income tax benefit from stock-based award exercises	16,000	19,000
Payment of contingent consideration related to business acquisition	(49,000)	(10,000)
Fees related to line of credit	(75,000)	(25,000)
Net cash used in financing activities	(35,279,000)	(23,904,000)
Net decrease in cash and cash equivalents	(38,649,000)	(14,967,000)
Cash and cash equivalents at beginning of period	356,642,000	367,894,000
Cash and cash equivalents at end of period	$317,993,000	352,927,000

See accompanying notes to condensed consolidated financial statements.
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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)

	Six months ended January 31,	
	2014	2013
Supplemental cash flow disclosures:		
Cash paid during the period for:		
Interest	$3,178,000	3,177,000
Income taxes	$8,224,000	7,070,000
Non-cash investing and financing activities:		
Cash dividends declared (including accrual of dividend equivalents)	$4,789,000	—
Equity-classified stock awards issued	$139,000	—

See accompanying notes to condensed consolidated financial statements.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) General

The accompanying condensed consolidated financial statements of Comtech Telecommunications Corp. and Subsidiaries (“Comtech,” “we,” “us,” or “our”) as of and for the three and six months ended January 31, 2014 and 2013 are unaudited. In the opinion of management, the information furnished reflects all material adjustments (which include normal recurring adjustments) necessary for a fair presentation of the results for the unaudited interim periods. Our results of operations for such periods are not necessarily indicative of the results of operations to be expected for the full fiscal year.

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amount of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results may differ from those estimates.

Our condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements, filed with the Securities and Exchange Commission (“SEC”), for the fiscal year ended July 31, 2013 and the notes thereto contained in our Annual Report on Form 10-K, and all of our other filings with the SEC.

(2) Adoption of Accounting Standards and Updates

We are required to prepare our consolidated financial statements in accordance with the Financial Accounting Standards Board's (“FASB”) Accounting Standards Codification (“ASC”) which is the source for all authoritative U.S. generally accepted accounting principles, which is commonly referred to as “GAAP.” The FASB ASC is subject to updates by FASB, which are known as Accounting Standards Updates (“ASUs”).

On August 1, 2013, we adopted FASB ASU No. 2011-11, which requires entities to disclose both gross and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement. In addition, we also adopted ASU No. 2013-01, which clarifies that the scope of ASU No. 2011-11 applies to derivatives accounted for in accordance with Topic 815, "Derivatives and Hedging," including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset or subject to an enforceable master netting arrangement or similar arrangement. Our adoption of this ASU, as amended, did not have any impact on our consolidated financial statements.

(3) Reclassifications

Certain reclassifications have been made to previously reported financial statements to conform to our current financial statement format.

(4) Fair Value Measurements and Financial Instruments

In accordance with FASB ASC 825, “Financial Instruments,” we determined that, as of January 31, 2014 and July 31, 2013, the fair value of our 3.0% convertible senior notes was approximately $206,780,000 and $208,080,000, respectively, based on quoted market prices in an active market. Our 3.0% convertible senior notes are not marked-to-market and are shown on the accompanying balance sheet at their original issuance value. As such, changes in the estimated fair value of our 3.0% convertible senior notes are not recorded in our condensed consolidated financial statements.

As of January 31, 2014 and July 31, 2013, we had approximately $39,192,000 and $50,182,000, respectively, of money market mutual funds which are classified as cash and cash equivalents in our Condensed Consolidated Balance Sheets. These money market mutual funds are recorded at their current fair value. FASB ASC 820, “Fair Value Measurements and Disclosures,” requires us to define fair value as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, using the fair value hierarchy described in FASB ASC 820, we valued our money market mutual funds using Level 1 inputs that were based on quoted market prices.

As of January 31, 2014 and July 31, 2013, other than our cash and cash equivalents, we have no other significant assets or liabilities included in our Condensed Consolidated Balance Sheets recorded at current fair value. If we acquire different types of assets or incur different types of liabilities in the future, we might be required to use different FASB ASC fair value methodologies.

(5) Earnings Per Share

Our basic earnings per share ("EPS") is computed based on the weighted average number of shares, including vested but unissued stock units, share units, performance shares and restricted stock units ("RSUs"), outstanding during each respective period. Our diluted EPS reflects the dilution from potential common stock issuable pursuant to the exercise of equity-classified stock-based awards and convertible senior notes, if dilutive, outstanding during each respective period. Pursuant to FASB ASC 260, "Earnings Per Share," equity-classified stock-based awards that are subject to performance conditions are not considered in our diluted EPS calculations until the respective performance conditions have been satisfied. When calculating our diluted earnings per share, we consider (i) the amount a recipient must pay upon assumed exercise of stock-based awards; (ii) the amount of stock-based compensation cost attributed to future services and not yet recognized; and (iii) the amount of excess tax benefits, if any, that would be credited to additional paid-in capital assuming exercise of in-the-money stock-based awards. This excess tax benefit is the amount resulting from a tax deduction for compensation in excess of compensation expense recognized for financial reporting purposes.

Weighted average stock options outstanding to purchase 573,000 and 2,658,000 shares for the three months ended January 31, 2014 and 2013, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive. Weighted average stock options outstanding to purchase 2,308,000 and 2,680,000 shares for the six months ended January 31, 2014 and 2013, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive.

Our diluted EPS calculations exclude 92,000 and 35,000 weighted average RSUs with performance measures (which we refer to as performance shares) outstanding for the three months ended January 31, 2014 and 2013, respectively, and 70,000 and 35,000 weighted average performance shares outstanding for the six months ended January 31, 2014 and 2013, respectively, as the respective performance conditions had not yet been satisfied. However, the compensation expense related to these awards is included in net income (the numerator) for EPS calculations for each respective period.

Our diluted EPS calculation for the three months ended January 31, 2013 excludes the effect of 5,992,000 shares and $1,117,000 of interest expense (net of tax) related to our 3.0% convertible senior notes, because their effect would have been anti-dilutive for the period.

In addition, the weighted average basic and diluted shares outstanding for the three months ended January 31, 2014 and 2013 reflects a reduction of approximately 439,000 and 102,000 shares as a result of the repurchase of our common shares during the respective periods. The weighted average basic and diluted shares outstanding for the six months ended January 31, 2014 and 2013 reflects a reduction of approximately 289,000 and 51,000 shares as a result of the repurchase of our common shares during the respective periods. See Note (18) – "Stockholders' Equity" for more information on our stock repurchase program.

Liability-classified stock-based awards do not impact and are not included in the denominator for EPS calculations.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

The following table reconciles the numerators and denominators used in the basic and diluted EPS calculations:

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
Numerator:				
Net income for basic calculation	$5,983,000	2,365,000	11,288,000	9,800,000
Effect of dilutive securities:				
Interest expense (net of tax) on 3.0% convertible senior notes	1,117,000	—	2,234,000	2,234,000
Numerator for diluted calculation	$7,100,000	2,365,000	13,522,000	12,034,000
Denominator:				
Denominator for basic calculation	15,970,000	17,300,000	16,212,000	17,340,000
Effect of dilutive securities:				
Stock-based awards	287,000	101,000	141,000	105,000
Conversion of 3.0% convertible senior notes	6,230,000	—	6,199,000	5,949,000
Denominator for diluted calculation	22,487,000	17,401,000	22,552,000	23,394,000

(6) Accounts Receivable

Accounts receivable consist of the following at:

	January 31, 2014	July 31, 2013
Billed receivables from commercial customers	$36,018,000	40,005,000
Billed receivables from the U.S. government and its agencies	8,757,000	8,114,000
Unbilled receivables on contracts-in-progress	12,799,000	2,399,000
Total accounts receivable	57,574,000	50,518,000
Less allowance for doubtful accounts	695,000	603,000
Accounts receivable, net	$56,879,000	49,915,000

Unbilled receivables on contracts-in-progress include $1,334,000 and $699,000 at January 31, 2014 and July 31, 2013, respectively, due from the U.S. government and its agencies. We had virtually no retainage included in unbilled receivables at both January 31, 2014 and July 31, 2013. In the opinion of management, a substantial portion of the unbilled balances will be billed and collected within one year.

As of January 31, 2014, one customer, which is also the prime contractor that we perform work for on our two North African country end-customer over-the-horizon microwave system contracts, accounts for 17.9% of total accounts receivable.

(7) Inventories

Inventories consist of the following at:

	January 31, 2014	July 31, 2013
Raw materials and components	$55,791,000	52,169,000
Work-in-process and finished goods	30,030,000	29,539,000

Total inventories	85,821,000	81,708,000
Less reserve for excess and obsolete inventories	15,726,000	16,226,000
Inventories, net	$70,095,000	65,482,000

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

At January 31, 2014 and July 31, 2013, the amount of inventory directly related to long-term contracts (including contracts-in-progress) was $1,370,000 and $1,910,000, respectively.

At January 31, 2014 and July 31, 2013, $617,000 and $592,000, respectively, of the inventory above related to contracts from third party commercial customers who outsource their manufacturing to us.

(8) Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following at:

	January 31, 2014	July 31, 2013
Accrued wages and benefits	$9,783,000	11,526,000
Accrued warranty obligations	8,291,000	7,797,000
Accrued commissions and royalties	2,985,000	4,206,000
Accrued business acquisition payments	—	288,000
Other	4,867,000	6,075,000
Accrued expenses and other current liabilities	$25,926,000	29,892,000

Accrued Warranty Obligations
We provide warranty coverage for most of our products for a period of at least one year from the date of shipment. We record a liability for estimated warranty expense based on historical claims, product failure rates and other factors. Some of our product warranties are provided under long-term contracts, the costs of which are incorporated into our estimates of total contract costs.

Changes in our product warranty liability were as follows:

	Six months ended January 31,	
	2014	2013
Balance at beginning of period	$7,797,000	7,883,000
Provision for warranty obligations	3,548,000	3,709,000
Charges incurred	(3,054,000)	(2,928,000)
Balance at end of period	$8,291,000	8,664,000

Accrued Business Acquisition Payments
In October 2010, we acquired the WAN optimization technology assets and assumed certain liabilities of Stampede for an estimated total purchase price of approximately $5,303,000, including the initial fair value of contingent earn-out payments which aggregated $3,803,000. Almost all of the purchase price for Stampede was allocated to the estimated fair value of technologies acquired and was assigned an estimated amortizable life of five years.

In the first quarter of fiscal 2014, the fair value of the contingent earn-out liability was reduced by $239,000, which is reflected as a reduction to selling, general and administrative expenses in our Condensed Consolidated Statement of Operations for the six months ended January 31, 2014. In November 2013, we made our final earn-out payment of $43,000. In fiscal 2013, the fair value of the contingent earn-out liability was reduced by $889,000 and $3,267,000 during the three and six months ended January 31, 2013, respectively, which is reflected as a reduction to selling, general and administrative expenses in our Condensed Consolidated Statement of Operations for the respective periods.

There was no interest accreted on the contingent earn-out liability for the three and six months ended January 31, 2014. Interest accreted on the contingent earn-out liability was $25,000 and $133,000 for the three and six months ended January 31, 2013, respectively. Total interest accreted through January 31, 2014 was $986,000.

Through January 31, 2014, we paid $1,865,000 of the total purchase price in cash, including $365,000 of earn-out payments.

(9) Cost Reduction Actions

Wind-Down of Microsatellite Product Line
During fiscal 2013, we completed our fiscal 2012 plan to wind-down our mobile data communications segment's microsatellite product line. In connection with this plan, we recorded a pre-tax benefit of $253,000 in the three months ended January 31, 2013, resulting from the reversal of previously accrued costs that were lower than expected. For the six months ended January 31, 2013, we recorded a net pre-tax restructuring charge of $569,000 related to this plan. Almost all of these amounts are reflected in selling, general and administrative expenses in our Condensed Consolidated Statements of Operations. There were no such charges or benefits in the three and six months ended January 31, 2014.

The activity pertaining to the accruals with respect to this plan, since July 31, 2013, is summarized as follows:

	Facility exit costs	Other	Total
Balance as of July 31, 2013	$413,000	50,000	$463,000
Payments made	(75,000)	—	(75,000)
Balance as of January 31, 2014	$338,000	50,000	$388,000

Of the total remaining microsatellite product line wind-down liabilities of $388,000, $282,000 is included in accrued expenses and other current liabilities and $106,000 is included in other long-term liabilities in our Condensed Consolidated Balance Sheet as of January 31, 2014.

Radyne Acquisition-Related Restructuring Plan
In connection with our August 1, 2008 acquisition of Radyne, we adopted a restructuring plan for which we recorded $2,713,000 of estimated restructuring costs. Of this amount, $613,000 related to severance for Radyne employees which was paid in fiscal 2009. The remaining estimated amounts relate to facility exit costs and were determined as follows:

	At August 1, 2008
Total non-cancelable lease obligations	$12,741,000
Less: Estimated sublease income	8,600,000
Total net estimated facility exit costs	4,141,000
Less: Interest expense to be accreted	2,041,000
Present value of estimated facility exit costs	$2,100,000

Our total non-cancelable lease obligations were based on the actual lease term which runs from November 1, 2008 through October 31, 2018. We estimated sublease income based on (i) the terms of a fully executed sublease agreement, whose lease term runs from November 1, 2008 through October 31, 2015 and (ii) our assessment of future uncertainties relating to the commercial real estate market. Based on our assessment of commercial real estate market conditions, we currently believe that it is not probable that we will be able to sublease the facility beyond the current sublease terms. As such, in accordance with grandfathered accounting standards that were not incorporated into the FASB’s ASC, we recorded these costs, at fair value, as assumed liabilities as of August 1, 2008, with a corresponding increase to goodwill.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

As of January 31, 2014, the amount of the acquisition-related restructuring reserve is as follows:

	Cumulative Activity Through January 31, 2014
Present value of estimated facility exit costs at August 1, 2008	$2,100,000
Cash payments made	(5,855,000)
Cash payments received	6,347,000
Accreted interest recorded	956,000
Net liability as of January 31, 2014	3,548,000
Amount recorded as prepaid expenses in the Condensed Consolidated Balance Sheet	454,000
Amount recorded as other liabilities in the Condensed Consolidated Balance Sheet	$4,002,000

As of July 31, 2013, the present value of the estimated facility exit costs was $3,331,000. During the six months ended January 31, 2014, we made cash payments of $528,000 and we received cash payments of $625,000. Interest accreted for the three and six months ended January 31, 2014 and 2013 was $61,000 and $120,000, respectively, and $53,000 and $105,000, respectively, and is included in interest expense for each respective fiscal period.

As of January 31, 2014, future cash payments associated with our restructuring plan are summarized below:

	As of January 31, 2014
Future lease payments to be made in excess of anticipated sublease payments	$4,002,000
Less net cash to be received in next twelve months	(454,000)
Interest expense to be accreted in future periods	1,084,000
Total remaining net cash payments	$4,632,000

(10) Credit Facility

We have a committed $100,000,000 secured revolving credit facility (the “Credit Facility”) with a syndicate of bank lenders. The Credit Facility, as amended December 6, 2013, expires on October 31, 2014 but may be extended by us to December 31, 2016, subject to certain conditions relating primarily to the repurchase, redemption or conversion of our 3.0% convertible senior notes and compliance with all other Credit Facility covenants.

The Credit Facility provides for the extension of credit to us in the form of revolving loans, including letters of credit, at any time and from time to time during its term, in an aggregate principal amount at any time outstanding not to exceed $100,000,000 for both revolving loans and letters of credit, with sub-limits of $15,000,000 for commercial letters of credit and $35,000,000 for standby letters of credit. Subject to covenant limitations, the Credit Facility may be used for acquisitions, equity securities repurchases, dividends, working capital and other general corporate purposes. Since the inception of our Credit Facility in 2009, we have had no revolving loans under the Credit Facility. At January 31, 2014, we had $1,791,000 of standby letters of credit outstanding related to our guarantees of future performance on certain customer contracts and no outstanding commercial letters of credit.

At our election, borrowings under the Credit Facility will bear interest either at LIBOR plus an applicable margin or at the base rate plus an applicable margin, as amended. The interest rate margin over LIBOR ranges from 1.75 percent up to a maximum amount of 2.50 percent. The base rate is a fluctuating rate equal to the highest of (i) the Prime Rate; (ii) the Federal Funds Effective Rate from time to time plus fifty (50) basis points; and (iii) two hundred (200) basis points in excess of the floating rate of interest determined, on a daily basis, in accordance with the terms of the agreement. The interest rate margin over the base rate ranges from 0.75 percent up to a maximum amount of 1.50 percent. In both cases, the applicable interest rate margin is based on the ratio of our consolidated total indebtedness to our consolidated earnings before interest, taxes, depreciation and amortization (“Consolidated Adjusted EBITDA”). As defined in the Credit Facility, Consolidated Adjusted EBITDA is adjusted for certain items and, in the event of an acquisition with a purchase price in excess of $10,000,000, provides for the inclusion of the last twelve months of consolidated EBITDA of a target.

As amended December 6, 2013, the Credit Facility contains covenants, including covenants limiting certain debt, certain liens on assets, certain sales of assets and receivables, certain payments (including dividends), certain repurchases of equity securities, certain sale and leaseback transactions, certain guaranties, certain investments and certain minimum levels of cash and cash equivalents. Under certain conditions, the Credit Facility also contains financial condition covenants requiring that we (i) not exceed a maximum ratio of consolidated total indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (ii) not exceed a maximum ratio of consolidated senior secured indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (iii) maintain a minimum fixed charge ratio (as defined in the Credit Facility); (iv) maintain a minimum consolidated net worth; in each case measured on the last day of each fiscal quarter and (v) in the event total consolidated indebtedness (as defined in the Credit Facility) is less than $200,000,000, we must maintain a minimum level of Consolidated Adjusted EBITDA (as defined in the Credit Facility).

At January 31, 2014, had borrowings been outstanding under the Credit Facility, the interest rate would have been approximately 2.70 percent (LIBOR plus 2.50 percent). We are also subject to an undrawn line fee based on the ratio of our consolidated total indebtedness to our Consolidated Adjusted EBITDA, as defined and adjusted for certain items specified in the Credit Facility. Interest expense, including amortization of deferred financing costs, related to our credit facility recorded during the three and six months ended January 31, 2014 was $167,000 and $353,000, respectively, as compared to $184,000 and $363,000 during the three and six months ended January 31, 2013, respectively.

As of January 31, 2014, based on our Consolidated Adjusted EBITDA (as defined in the Credit Facility) and our business outlook and related business plans, we believe we will be able to meet or obtain waivers for the applicable financial covenants that we are required to maintain.

(11) 3.0% Convertible Senior Notes

In May 2009, we issued $200,000,000 of our 3.0% convertible senior notes in a private offering pursuant to Rule 144A under the Securities Act of 1933, as amended. The net proceeds from this transaction were $194,541,000 after deducting the initial purchasers' discount and other transaction costs of $5,459,000.

Our 3.0% convertible senior notes bear interest at an annual rate of 3.0%. Pursuant to the terms of the 3.0% convertible senior notes indenture, cash dividends require an adjustment to the conversion rate, effective on the record date. Effective January 17, 2014 (the record date of our dividend declared on December 9, 2013), our 3.0%

convertible senior notes are convertible into shares of our common stock at a conversion price of $31.85 per share (a conversion rate of 31.3953 shares per $1,000 original principal amount of notes) at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, subject to adjustment in certain circumstances.

We may, at our option, redeem some or all of our 3.0% convertible senior notes on or after May 5, 2014. Holders of the 3.0% convertible senior notes will have the right to require us to repurchase some or all of our outstanding 3.0% convertible senior notes, solely for cash, on May 1, 2014, May 1, 2019 and May 1, 2024 and upon certain events, including a change in control. If not redeemed by us or repaid pursuant to the holders' right to require repurchase, our 3.0% convertible senior notes mature on May 1, 2029. Because it is possible that the holders of our 3.0% convertible senior notes will require us to repurchase some or all of the outstanding notes on May 1, 2014, our 3.0% convertible senior notes are reflected as a current liability in our Condensed Consolidated Balance Sheet at January 31, 2014 and July 31, 2013.

The 3.0% convertible notes are senior unsecured obligations of Comtech.

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(12) Income Taxes

Excluding the impact of any discrete tax items, our fiscal 2014 effective tax rate is expected to approximate 36.5%. This rate reflects the expiration of the federal research and experimentation credit on December 31, 2013.

At January 31, 2014 and July 31, 2013, total unrecognized tax benefits, all of which were recorded as non-current income taxes payable in our Condensed Consolidated Balance Sheets, were $3,162,000 and $2,963,000, respectively, including interest of $113,000 and $90,000, respectively. Of these amounts, $2,474,000 and $2,348,000, respectively, net of the reversal of the federal benefit recognized as deferred tax assets relating to state reserves, excluding interest, would positively impact our effective tax rate, if recognized. Unrecognized tax benefits result from income tax positions taken or expected to be taken on our income tax returns for which a tax benefit has not been recorded in our financial statements. Our policy is to recognize interest and penalties relating to uncertain tax positions in income tax expense.

Our federal income tax returns for fiscal 2010 through 2013 are subject to potential future IRS audit. Future tax assessments or settlements could have a material adverse effect on our consolidated results of operations and financial condition.

(13) Stock Based Compensation

Overview

We issue stock-based awards to certain of our employees and our Board of Directors pursuant to our 2000 Stock Incentive Plan, as amended, (the "Plan") and our 2001 Employee Stock Purchase Plan (the "ESPP") and recognize related stock-based compensation for both equity and liability-classified stock-based awards in our consolidated financial statements. The Plan provides for the granting to employees and consultants of Comtech (including prospective employees and consultants): (i) incentive and non-qualified stock options, (ii) restricted stock units ("RSUs"), (iii) RSUs with performance measures (which we refer to as "performance shares"), (iv) restricted stock, (v) stock units (reserved for issuance to non-employee directors) and share units (reserved for issuance to employees) (collectively, "share units") and (vi) stock appreciation rights ("SARs"), among other types of awards. Our non-employee directors are eligible to receive non-discretionary grants of stock-based awards, subject to certain limitations. The aggregate number of shares of common stock which may be issued, pursuant to the Plan, may not exceed 8,962,500. Stock options granted may not have a term exceeding ten years or, in the case of an incentive stock award granted to a stockholder who owns stock representing more than 10.0% of the voting power, no more than five years. We expect to settle all outstanding awards under the Plan and ESPP with new shares, except for SARs which may only be settled with cash.

As of January 31, 2014, we had granted stock-based awards pursuant to the Plan representing the right to purchase and/or acquire an aggregate of 6,827,882 shares (net of 2,757,610 expired and canceled awards), of which an aggregate of 3,922,027 have been exercised or converted into common stock, substantially all of which related to stock options.

As of January 31, 2014, the following stock-based awards, by award type, were outstanding:

	January 31, 2014
Stock options	2,737,445

Performance shares	117,210
RSUs and restricted stock	37,326
Share units	6,874
SARs	7,000
Total	2,905,855

Our ESPP, approved by our shareholders on December 12, 2000, provides for the issuance of 675,000 shares of our common stock. Our ESPP is intended to provide our eligible employees the opportunity to acquire our common stock at 85% of fair market value at the date of issuance. Through January 31, 2014, we have cumulatively issued 536,899 shares of our common stock to participating employees in connection with our ESPP.

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Stock-based compensation for awards issued is reflected in the following line items in our Condensed Consolidated Statements of Operations:

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
Cost of sales	$84,000	74,000	137,000	119,000
Selling, general and administrative expenses	832,000	614,000	1,603,000	1,215,000
Research and development expenses	153,000	118,000	276,000	217,000
Stock-based compensation expense before income tax benefit	1,069,000	806,000	2,016,000	1,551,000
Estimated income tax benefit	(403,000)	(346,000)	(749,000)	(610,000)
Net stock-based compensation expense	$666,000	460,000	1,267,000	941,000

Stock-based compensation for equity-classified awards is measured at the date of grant, based on an estimate of the fair value of the award and is generally expensed over the vesting period of the award. Stock-based compensation for liability-classified awards is determined the same way, except that the fair value of liability-classified awards is re-measured at the end of each reporting period until the award is settled, with changes in fair value recognized pro-rata for the portion of the requisite service period rendered. At January 31, 2014, unrecognized stock-based compensation of $9,310,000, net of estimated forfeitures of $580,000, is expected to be recognized over a weighted average period of 3.1 years. Total stock-based compensation capitalized and included in ending inventory at January 31, 2014 and July 31, 2013 was $52,000 and $72,000, respectively. Included in accrued expenses at January 31, 2014 and July 31, 2013 is $7,000 and $1,000, respectively, relating to the potential cash settlement of liability-classified SARs.

Stock-based compensation expense, by award type, is summarized as follows:

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
Stock options	$719,000	638,000	1,367,000	1,211,000
Performance shares	230,000	86,000	407,000	172,000
ESPP	43,000	48,000	88,000	101,000
RSUs and restricted stock	68,000	28,000	136,000	60,000
Share units	6,000	6,000	12,000	12,000
Equity-classified stock-based compensation expense	1,066,000	806,000	2,010,000	1,556,000
Liability-classified stock-based compensation expense (benefit) (SARs)	3,000	—	6,000	(5,000)
Stock-based compensation expense before income tax benefit	1,069,000	806,000	2,016,000	1,551,000
Estimated income tax benefit	(403,000)	(346,000)	(749,000)	(610,000)
Net stock-based compensation expense	$666,000	460,000	1,267,000	941,000

ESPP stock-based compensation expense primarily relates to the 15% discount offered to employees participating in the ESPP.

The estimated income tax benefit, as shown in the above table, was computed using income tax rates expected to apply when the awards are settled and results in a deferred tax asset which is netted in our long-term deferred tax liability in our Condensed Consolidated Balance Sheet. The actual income tax benefit recognized for tax reporting is based on the fair market value of our common stock at the time of settlement and can significantly differ from the estimated income tax benefit recorded for financial reporting.

The following table provides the components of the actual income tax benefit recognized for tax deductions relating to the settlement of stock-based awards:

	Six months ended January 31,	
	2014	2013
Actual income tax benefit recorded for the tax deductions relating to the settlement of stock-based awards	$174,000	79,000
Less: Tax benefit initially recognized on settled stock-based awards vesting subsequent to the adoption of accounting standards that require us to expense stock-based awards, excluding income tax shortfalls	145,000	60,000
Excess income tax benefit recorded as an increase to additional paid-in capital	29,000	19,000
Less: Tax benefit initially disclosed but not previously recognized on settled equity-classified stock-based awards vesting prior to the adoption of accounting standards that require us to expense stock-based awards, excluding income tax shortfalls	13,000	—
Excess income tax benefit from settled equity-classified stock-based awards reported as a cash flow from financing activities in our Condensed Consolidated Statements of Cash Flows	$16,000	19,000

As of January 31, 2014 and July 31, 2013, the amount of hypothetical tax benefits related to stock-based awards, recorded as a component of additional paid-in capital, was $17,901,000 and $19,981,000, respectively. These amounts represent the initial hypothetical tax benefit of $8,593,000 determined upon adoption of ASC 718 (which reflects our estimate of cumulative actual tax deductions for awards issued and settled prior to the August 1, 2005), adjusted for actual excess income tax benefits or shortfalls since that date. During the six months ended January 31, 2014 and 2013, we recorded $2,080,000 and $2,941,000, respectively, as a net reduction to additional paid-in capital and accumulated hypothetical tax benefits, which primarily represents the reversal of unrealized deferred tax assets associated with certain vested equity-classified stock-based awards that expired during the respective periods.

Stock Options

The following table summarizes the Plan's activity (including SARs) during the six months ended January 31, 2014:

	Awards (in Shares)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at July 31, 2013	3,047,910	$29.94		
Granted	247,000	27.23		
Expired/canceled	(413,240)	45.66		
Exercised	(4,050)	19.54		
Outstanding at October 31, 2013	2,877,620	27.46		
Granted	11,000	31.29		
Expired/canceled	(52,800)	27.80		
Exercised	(91,375)	27.14		
Outstanding at January 31, 2014	2,744,445	$27.48	5.47	$8,134,000
Exercisable at January 31, 2014	1,408,803	$27.18	3.00	$4,612,000
Vested and expected to vest at January 31, 2014	2,678,766	$27.47	5.42	$7,971,000

Stock options (including SARs) outstanding as of January 31, 2014 have exercise prices ranging between $13.19-$35.79. The total intrinsic value relating to stock options exercised during the three months ended January 31, 2014 and 2013 was $391,000 and $125,000, respectively. The total intrinsic value relating to stock options exercised during the six months ended January 31, 2014 and 2013 was $432,000 and $264,000, respectively. Stock options granted during the six months ended January 31, 2014 and 2013 had exercise prices equal to the fair market value of our common stock on the date of grant, a contractual term of ten years and a vesting period of five years. There were no SARs granted or exercised during the three and six months ended January 31, 2014 and 2013. The estimated per-share weighted average grant-date fair value of stock options granted during the three and six months ended January 31, 2014 was $6.26 and $5.50, respectively, and $5.46 during the three and six months ended January 31, 2013, which was determined using the Black-Scholes option pricing model, and included the following weighted average assumptions:

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
Expected dividend yield	3.84 %	4.29 %	4.03 %	4.29 %
Expected volatility	32.00 %	37.00 %	32.85 %	37.00 %
Risk-free interest rate	1.50 %	0.61 %	1.39 %	0.61 %
Expected life (years)	5.31	5.31	5.44	5.31

Expected dividend yield is the expected annual dividend as a percentage of the fair market value of our common stock on the date of grant, based on our Board's annual dividend target at the time of grant, which was increased from $1.10 per share to $1.20 per share during the three months ended January 31, 2014. We estimate expected volatility by considering the historical volatility of our stock, the implied volatility of publicly-traded call options on our stock, the implied volatility of call options embedded in our 3.0% convertible senior notes and our expectations of volatility for the expected life of stock options. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for an instrument which closely approximates the expected term. The expected term is the number of years we estimate that awards will be outstanding prior to exercise and is determined by employee groups with sufficiently distinct behavior patterns. Assumptions used in computing the fair value of stock-based awards reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by recipients of stock-based awards.

Performance Shares, RSUs, Restricted Stock and Share Unit Awards

The following table summarizes the Plan's activity relating to performance shares, RSUs, restricted stock and share units:

	Awards (in Shares)	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
Outstanding at July 31, 2013	102,334	$25.80	
Granted	68,167	24.58	
Converted to common stock	(4,509)	26.25	
Outstanding at October 31, 2013	165,992	25.28	
Granted	4,988	31.32	
Converted to common stock	—	—	
Forfeited	(9,570)	24.82	
Outstanding at January 31, 2014	161,410	$25.50	$4,910,000
Vested at January 31, 2014	12,529	$26.93	$381,000
Vested and expected to vest at January 31, 2014	156,337	$25.51	$4,756,000

Performance shares granted to employees prior to fiscal 2014 vest over a 5.3 year period, beginning on the date of grant if pre-established performance goals are attained, and are convertible into shares of our common stock generally at the time of vesting, on a one-for-one basis for no cash consideration. The performance shares granted to employees during the three and six months ended January 31, 2014 principally vest over a three year performance period that ends on July 31, 2016, if pre-established performance goals are attained or as specified pursuant to the Plan and related agreement. As of January 31, 2014, the number of outstanding performance shares included in the above table, and the related compensation expense, assume achievement of the pre-established goals at a target level. During the six months ended January 31, 2014, our Board of Directors determined that the pre-established performance goals for 35,003 performance shares granted in fiscal 2012 had been attained and, as a result, the first tranche of 6,996 performance shares vested and converted into 3,496 net shares of our common stock, after reduction of 1,013 shares retained to satisfy minimum tax withholding and 2,487 shares for deferral requirements.

RSUs and restricted stock granted to non-employee directors have a vesting period of three years and are convertible into shares of our common stock generally at the time of termination, on a one-for-one basis for no cash consideration, or earlier under certain circumstances. RSUs granted to employees have a vesting period of five years and are convertible into shares of our common stock generally at the time of vesting, on a one-for-one basis for no cash consideration.

Share units are vested when issued and are convertible into shares of our common stock generally at the time of termination, on a one-for-one basis for no cash consideration, or earlier under certain circumstances.

No RSUs, restricted stock or share units granted to date have been converted into common stock.

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The fair value of performance shares, RSUs, restricted stock and share units is determined using the closing market price of our common stock on the date of grant, less the present value of any estimated future dividend equivalents such awards are not entitled to receive. RSUs and performance shares granted in fiscal 2012 are not entitled to dividend equivalents. RSUs, performance shares and restricted stock granted in fiscal 2013 and 2014 are entitled to dividend equivalents unless forfeited before vesting occurs; however, performance shares granted in fiscal 2013 are not entitled to such dividend equivalents until our Board of Directors has determined that the pre-established performance goals have been met. Share units granted prior to fiscal 2014 are not entitled to dividend equivalents. Share units granted in fiscal 2014 are entitled to dividend equivalents while the underlying shares are unissued.

Dividend equivalents are subject to forfeiture, similar to the terms of the underlying stock-based awards, and are payable in cash generally at the time of conversion of the underlying shares into our common stock. As of January 31, 2014 and July 31, 2013, accrued dividend equivalents were $58,000 and $7,000, respectively. Such amounts were recorded as a reduction to retained earnings.

(14) Customer and Geographic Information

Sales by geography and customer type, as a percentage of consolidated net sales, are as follows:

	Three months ended January 31,		Six months ended January 31,	
	2014	2013	2014	2013
United States				
U.S. government	31.2 %	32.8 %	28.4 %	38.6 %
Commercial	11.3 %	12.9 %	14.3 %	13.3 %
Total United States	42.5 %	45.7 %	42.7 %	51.9 %
International				
North African country	13.7 %	8.2 %	13.1 %	5.0 %
Other international	43.8 %	46.1 %	44.2 %	43.1 %
Total International	57.5 %	54.3 %	57.3 %	48.1 %

Sales to U.S. government end customers include the Department of Defense ("DoD") and intelligence and civilian agencies, as well as sales directly to or through prime contractors.

Excluding sales in our mobile data communications segment, aggregate sales to U.S. government end customers for our telecommunications transmission and RF microwave amplifiers segments were 25.7% and 25.8% of the combined net sales of these two segments for the three months ended January 31, 2014 and 2013, respectively. Excluding sales in our mobile data communications segment, aggregate sales to U.S. government end customers for our telecommunications transmission and RF microwave amplifiers segments were 23.2% and 31.5% of the combined net sales of these two segments for the six months ended January 31, 2014 and 2013, respectively.

International sales for the three months ended January 31, 2014 and 2013 (which include sales to U.S. domestic companies for inclusion in products that will be sold to international customers) were $49,144,000 and $40,471,000, respectively. International sales for the six months ended January 31, 2014 and 2013 (which include sales to U.S. domestic companies for inclusion in products that will be sold to international customers) were $96,684,000 and $79,689,000, respectively.

For the three and six months ended January 31, 2014, sales to a prime contractor represented approximately 13.5% and 13.0%, respectively, of consolidated net sales (almost all of which related to our North African country end-customer).

For the three and six months ended January 31, 2013, except for the U.S. government, no other customer or individual country (including sales to U.S. domestic companies for inclusion in products that will be sold to a foreign country) represented more than 10% of consolidated net sales.

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(15) Segment Information

Reportable operating segments are determined based on Comtech's management approach. The management approach, as defined by FASB ASC 280, "Segment Reporting," is based on the way that the chief operating decision-maker organizes the segments within an enterprise for making decisions about resources to be allocated and assessing their performance. Our chief operating decision-maker is our President and Chief Executive Officer.

While our results of operations are primarily reviewed on a consolidated basis, the chief operating decision-maker also manages the enterprise in three operating segments: (i) telecommunications transmission, (ii) RF microwave amplifiers, and (iii) mobile data communications.

Telecommunications transmission products include satellite earth station products (such as analog and digital modems, frequency converters, power amplifiers, transceivers and voice gateways) and over-the-horizon microwave communications products and systems (such as digital troposcatter modems).

RF microwave amplifier products include traveling wave tube amplifiers and solid-state, high-power narrow and broadband amplifier products that use the microwave and radio frequency spectrums.

Mobile data communications products and services substantially relate to our support of the U.S. Army's Blue Force Tracking ("BFT-1") and the U.S. Army's Movement Tracking System ("MTS") programs, which are currently in a sustainment mode. Pursuant to a two-year $44,279,000 indefinite delivery/indefinite quantity BFT-1 sustainment contract, which performance period ends on March 31, 2014, we license certain of our intellectual property to the U.S. Army and provide satellite network and related engineering services (including program management) on a cost-plus-fixed-fee basis.

Corporate management defines and reviews segment profitability based on the same allocation methodology as presented in the segment data tables below:

	Three months ended January 31, 2014				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$56,521,000	22,041,000	6,937,000	—	$85,499,000
Operating income (loss)	10,268,000	1,077,000	3,273,000	(3,446,000)	11,172,000
Interest income and other (expense)	(18,000)	(13,000)	3,000	256,000	228,000
Interest expense (income)	61,000	—	(3,000)	1,940,000	1,998,000
Depreciation and amortization	2,231,000	945,000	63,000	1,085,000	4,324,000
Expenditure for long-lived assets, including intangibles	1,981,000	163,000	246,000	7,000	2,397,000
Total assets at January 31, 2014	244,478,000	90,733,000	7,114,000	312,889,000	655,214,000

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	Three months ended January 31, 2013				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$45,769,000	20,362,000	8,446,000	—	$74,577,000
Operating income (loss)	5,549,000	645,000	2,994,000	(3,241,000)	5,947,000
Interest income and other (expense)	(26,000)	(7,000)	3,000	345,000	315,000
Interest expense (income)	80,000	—	(6,000)	1,956,000	2,030,000
Depreciation and amortization	2,427,000	977,000	134,000	844,000	4,382,000
Expenditure for long-lived assets, including intangibles	1,228,000	135,000	26,000	5,000	1,394,000
Total assets at January 31, 2013	226,656,000	93,208,000	10,651,000	354,232,000	684,747,000

	Six months ended January 31, 2014				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$110,886,000	42,238,000	15,743,000	—	$168,867,000
Operating income (loss)	19,197,000	1,668,000	7,379,000	(6,973,000)	21,271,000
Interest income and other (expense)	(12,000)	(18,000)	6,000	525,000	501,000
Interest expense (income)	120,000	—	(3,000)	3,899,000	4,016,000
Depreciation and amortization	4,490,000	1,888,000	137,000	2,048,000	8,563,000
Expenditure for long-lived assets, including intangibles	2,914,000	257,000	246,000	7,000	3,424,000
Total assets at January 31, 2014	244,478,000	90,733,000	7,114,000	312,889,000	655,214,000

	Six months ended January 31, 2013				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$99,096,000	45,651,000	20,783,000	—	$165,530,000
Operating income (loss)	17,808,000	2,363,000	6,465,000	(7,327,000)	19,309,000
Interest income and other (expense)	(35,000)	(29,000)	12,000	643,000	591,000
Interest expense (income)	239,000	—	(6,000)	3,908,000	4,141,000
Depreciation and amortization	4,863,000	1,957,000	286,000	1,628,000	8,734,000
Expenditure for long-lived assets, including intangibles	2,069,000	342,000	41,000	5,000	2,457,000
Total assets at January 31, 2013	226,656,000	93,208,000	10,651,000	354,232,000	684,747,000

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

Operating income in our telecommunications transmission segment for the six months ended January 31, 2014 includes a benefit of $239,000 related to a change in fair value of the earn-out liability associated with our acquisition of Stampede. There was no such benefit during the three months ended January 31, 2014. Operating income in our telecommunications transmission segment for the three and six months ended January 31, 2013 includes a benefit of $889,000 and $3,267,000, respectively, related to a change in fair value of the earn-out liability associated with our acquisition of Stampede. See Note (8) - "Accrued Expenses and Other Current Liabilities."

Operating income in our mobile data communications segment for the three months ended January 31, 2013 includes a benefit of $253,000 relating to an adjustment for actual pre-tax restructuring charges that were lower than expected and, for the six months ended January 31, 2013, includes a net pre-tax restructuring charge of $569,000 related to the wind-down of our microsatellite product line. See Note (9) - "Cost Reduction Actions."

Unallocated expenses include corporate expenses such as executive compensation, accounting, legal and other regulatory compliance related costs. In addition, for the three and six months ended January 31, 2014 and 2013, unallocated expenses include $1,069,000 and $2,016,000, respectively, and $806,000 and $1,551,000, respectively, of stock-based compensation expense. Interest expense (which includes amortization of deferred financing costs) associated with our convertible senior notes and our Credit Facility is not allocated to the operating segments. Depreciation and amortization includes amortization of stock-based compensation. Unallocated assets consist principally of cash, deferred financing costs and deferred tax assets. Substantially all of our long-lived assets are located in the U.S.

Intersegment sales for the three months ended January 31, 2014 and 2013 by the telecommunications transmission segment to the RF microwave amplifiers segment were $464,000 and $423,000, respectively. Intersegment sales for the six months ended January 31, 2014 and 2013 by the telecommunications transmission segment to the RF microwave amplifiers segment were $765,000 and $1,657,000, respectively.

Intersegment sales for the three months ended January 31, 2014 and 2013 by the telecommunications transmission segment to the mobile data communications segment were $134,000 and $112,000, respectively. Intersegment sales for the six months ended January 31, 2014 and 2013 by the telecommunications transmission segment to the mobile data communications segment were $172,000 and $2,619,000, respectively.

Intersegment sales for the three months ended January 31, 2014 and 2013 by the RF microwave amplifiers segment to the telecommunications transmission segment were $68,000 and $3,000, respectively. Intersegment sales for the six months ended January 31, 2014 and 2013 by the RF microwave amplifiers segment to the telecommunications transmission segment were $134,000 and $6,000, respectively.

All intersegment sales have been eliminated from the tables above.

(16) Goodwill

The carrying amount of goodwill by segment as of January 31, 2014 and July 31, 2013 are as follows:

	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Total
Goodwill	$107,779,000	29,575,000	13,249,000	$150,603,000

Accumulated impairment	—	—	(13,249,000)	(13,249,000)
Balance	$107,779,000	29,575,000	—	$137,354,000

In accordance with FASB ASC 350, "Intangibles - Goodwill and Other," we perform goodwill impairment testing at least annually, unless indicators of impairment exist in interim periods. The impairment test for goodwill uses a two-step approach. Step one compares the estimated fair value of a reporting unit with goodwill to its carrying value. If the carrying value exceeds the estimated fair value, step two must be performed. Step two compares the carrying value of the reporting unit to the fair value of all of the assets and liabilities of the reporting unit (including any unrecognized intangibles) as if the reporting unit was acquired in a business combination. If the carrying amount of a reporting unit's goodwill exceeds the implied fair value of its goodwill, an impairment loss is recognized in an amount equal to the excess.

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For purposes of reviewing impairment and the recoverability of goodwill and other intangible assets, each of our three operating segments constitutes a reporting unit and we must make various assumptions in determining the fair values of the reporting unit.

On August 1, 2013 (the first day of our fiscal 2014), we performed our annual impairment test and estimated the fair value of each of our reporting units based on the income approach (also known as the discounted cash flow (“DCF”) method, which utilizes the present value of cash flows to estimate fair value). The future cash flows for our reporting units were projected based on our estimates, at that time, of future revenues, operating income and other factors (such as working capital and capital expenditures). We took into account expected challenging global industry and market conditions, including expected significant reductions in the overall budget for U.S. defense spending. As such, although both our telecommunications transmission and RF microwave amplifiers reporting units have historically achieved significant long-term revenue and operating income growth, we assumed growth rate estimates in our projections that were below our actual long-term expectations and below each reporting unit's actual historical growth rate. The discount rates used in our DCF method were based on a weighted-average cost of capital (“WACC”) determined from relevant market comparisons, adjusted upward for specific reporting unit risks (primarily the uncertainty of achieving projected operating cash flows). A terminal value growth rate was applied to the final year of the projected period and reflected our estimate of stable, perpetual growth. We then calculated a present value of the respective cash flows for each reporting unit to arrive at an estimate of fair value under the income approach and then used the market approach to corroborate this value. Under the market approach, we estimated a fair value based on comparable companies' market multiples of revenues and earnings before interest, taxes, depreciation and amortization and factored in a control premium. In each case, the estimated fair value determined under the market approach exceeded our estimate of fair value determined under the income approach. Finally, we compared our estimates to our August 1, 2013 total public market capitalization and assessed implied control premiums. Based on the aforementioned, we concluded that the estimated fair value determined under the income approach for each of our reporting units, as of August 1, 2013, was reasonable. In each case, the estimated fair value exceeded the respective carrying value and, as such, we concluded that the goodwill assigned to our telecommunications transmission and RF microwave amplifiers reporting units, as of August 1, 2013, was not impaired. We also concluded that our telecommunications transmission reporting unit was currently not at risk of failing step one of the goodwill impairment test as prescribed under the ASC. However, we concluded that as of August 1, 2013, our RF microwave amplifiers reporting unit was at risk of failing step one of the goodwill impairment test.

As of August 1, 2013, we determined that our RF microwave amplifiers reporting unit had an estimated fair value in excess of its respective carrying value of at least 13.2%, which represents an increase from the at least 5.0% excess we previously calculated as of January 31, 2013 (when we performed an interim fiscal 2013 impairment test). The increase from 5.0% to 13.2% was primarily driven by a decrease in the WACC from 12.0% to 11.0%. The WACC for any given impairment test is based on current market data as of the respective valuation date. Had we utilized a WACC of 12.0% for the fiscal 2014 annual impairment test, our RF microwave amplifiers reporting unit's estimated fair value would still exceed its carrying value as of August 1, 2013. The WACC of 11.0% used in our annual impairment test for fiscal 2013 was equal to the WACC utilized in our annual impairment test for fiscal 2013.

This estimated fair value of our RF microwave amplifiers reporting unit is closely aligned with the ultimate amount of revenue and operating income that it achieves over the projected period. Our discounted cash flows, for goodwill impairment testing purposes, assumed that, through fiscal 2019, this reporting unit would achieve a compounded annual revenue growth rate of approximately 1.0% and 4.0% from its actual fiscal 2012 and 2013 revenues of $102,497,000 and $86,939,000, respectively. Beyond fiscal 2019, we assumed a long-term revenue growth rate of 3.5% in the terminal year. Given current challenging market conditions, we believe these modest long-term growth rates and the WACC are appropriate to use for our future cash flow assumptions. We also believe that it is possible that our actual revenue growth rates could be significantly higher due to a number of factors, including: (i) continued reliance by our customers on our advanced communications systems; (ii) the continued shift toward information-based, network-centric warfare; and (iii) the need for developing countries to upgrade their communication systems. If we do not at least meet the assumed revenue growth utilized in this goodwill impairment analysis, our RF microwave amplifiers reporting unit will likely fail step one of a goodwill impairment test in a future period. Modest changes in other key assumptions used in our impairment analysis may also result in the requirement to proceed to step two of the goodwill impairment test in future periods. For example, keeping all other variables constant, a 160 basis point increase in the WACC applied to our RF microwave amplifiers reporting unit or an increase to our RF microwave amplifiers carrying value of more than $13,200,000 would likely result in a step one failure. If this reporting unit fails step one in the future, we would be required to perform step two of the goodwill impairment test. If we perform step two, up to $42,750,000 of goodwill and intangibles assigned to this reporting unit could be written off in the period that the impairment is triggered.

Our goodwill impairment analyses for the telecommunications transmission and RF microwave amplifiers reporting units are sensitive to the ultimate spending decisions by our global customers. Accordingly, we will continue to monitor key assumptions and other factors required to be utilized in evaluating impairment of goodwill. It is possible that, during fiscal 2014, business conditions (both in the U.S. and internationally) could deteriorate from the current state and our current or prospective customers could materially postpone, reduce or even forgo purchases of our products and services to a greater extent than we currently anticipate. A significant decline in defense spending that is greater than we anticipate or a shift in funding priorities may also have a negative effect on future orders, sales, income and cash flows and we might be required to perform a step one interim goodwill impairment test during fiscal 2014 for these two reporting units. In any event, we are required to perform the next annual step one goodwill impairment test on August 1, 2014 (the start of our fiscal 2015). If our assumptions and related estimates change in the future, or if we change our reporting structure or other events and circumstances change (e.g., such as a sustained decrease in the price of our common stock (considered on both absolute terms and relative to peers)), we may be required to record impairment charges when we perform these tests or in other future periods. Any impairment charges that we may take in the future could be material to our results of operations and financial condition.

(17) Intangible Assets

Intangible assets with finite lives as of January 31, 2014 and July 31, 2013 are as follows:

	January 31, 2014 Weighted Average Amortization Period	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Technologies	11.8	$47,370,000	34,711,000	$12,659,000
Customer relationships	10.0	29,831,000	16,556,000	13,275,000
Trademarks and other	20.0	5,794,000	2,387,000	3,407,000
Total		$82,995,000	53,654,000	$29,341,000

	July 31, 2013 Weighted Average Amortization Period	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Technologies	11.7	$47,494,000	33,264,000	$14,230,000
Customer relationships	10.0	29,831,000	15,081,000	14,750,000
Trademarks and other	20.0	5,944,000	2,419,000	3,525,000
Total		$83,269,000	50,764,000	$32,505,000

The weighted average amortization period in the above table excludes fully amortized intangible assets.

Amortization expense for both the three months ended January 31, 2014 and 2013 was $1,582,000. Amortization expense for both the six months ended January 31, 2014 and 2013 was $3,164,000.

The estimated amortization expense for the fiscal years ending July 31, 2014, 2015, 2016, 2017, and 2018 is $6,285,000, $6,211,000, $4,962,000, $4,782,000 and $4,782,000, respectively.

(18) Stockholders' Equity

Stock Repurchase Program
During the six months ended January 31, 2014, we repurchased 935,992 shares of our common stock in open-market transactions with an average price per share of $31.10 and at an aggregate cost of $29,107,000 (including transaction costs). During the six months ended January 31, 2013, we repurchased 397,798 shares of our common stock in open-market transactions with an average price per share of $26.34 and at an aggregate cost of $10,477,000 (including transaction costs).

As of January 31, 2014, we were authorized to repurchase up to an additional $55,247,000 of our common stock, pursuant to a stock repurchase program that was first authorized by our Board of Directors in December 2012 in the amount of $50,000,000 and increased to $100,000,000 effective December 9, 2013. Our stock repurchase program has no time restrictions and repurchases may be made in open-market or privately negotiated transactions and may be made pursuant to SEC Rule 10b5-1 trading plans. As of March 6, 2014, approximately $44,000,000 remains available for repurchases of our common stock.

Dividends

Since September 2010, we have paid quarterly dividends pursuant to an annual targeted dividend amount that was established by our Board of Directors. On December 9, 2013, our Board of Directors increased our annual target dividend from $1.10 per common share to $1.20 per common share.

During the six months ended January 31, 2014, our Board of Directors declared quarterly dividends of $0.275 per common share on October 3, 2013 and $0.30 per common share on December 9, 2013, which were paid to shareholders on November 19, 2013 and February 19, 2014, respectively.

On March 6, 2014 our Board of Directors declared a dividend of $0.30 per common share, payable on May 30, 2014, to shareholders of record at the close of business on May 7, 2014.

(19) Legal Proceedings and Other Matters

U.S. Government Investigations

In June 2012, certain officers and employees of the Company received subpoenas issued by the United States District Court for the Eastern District of New York (“EDNY”) seeking certain documents and records relating to our Chief Executive Officer (“CEO”). Although the EDNY subpoenas made no specific allegations, we believe the subpoenas related to a grand jury investigation stemming from our CEO's contacts with a scientific attaché to the Israeli Purchasing Mission in the United States who our CEO met in connection with the sale of our equipment to the State of Israel during the 1980's. This scientific attaché was later alleged to have conducted intelligence operations in the U.S. In August 2012, we were informed by the U.S. government that our CEO's security clearance was suspended. In order to maintain our qualification for government contracts requiring facility security clearance, we made certain internal organizational realignments. These changes restrict access to classified information to other Comtech senior executives, management and other employees who maintain the required level of clearance.

Separately, in connection with an investigation by the Securities and Exchange Commission (“SEC”) into trading in securities of CPI International, Inc. (“CPI”), in March and April 2012, we and our CEO received subpoenas for documents from the SEC concerning transactions in CPI stock by our CEO and other persons (including one subsidiary employee). Our CEO purchased CPI stock in November 2010 which was after the September 2010 termination of our May 2010 agreement to acquire CPI.

The independent members of our Board of Directors have monitored these matters with the assistance of independent counsel. We and our CEO have cooperated with the U.S. government regarding the above matters and have not been contacted by the government with respect to either matter since September 2012.

The outcome of any investigation is inherently difficult, if not impossible, to predict. However, based on our work to date in respect of the subpoenas in each matter, we do not believe that it is likely that either investigation will result in a legal proceeding against our CEO or the Company. If either of these investigations results in a legal proceeding, it could have a material adverse effect on our business and results of operations.

Defense Contract Audit Agency (“DCAA”) Audit

In May 2011, we were notified that our original BFT-1 contract, which was awarded to us on August 31, 2007 (our fiscal 2008), was selected for a post award audit by the DCAA. We received total funded orders against this contract, which expired December 31, 2011, of $376,246,000. A post-award audit (sometimes referred to as a Truth in

Negotiations Act or “TINA” audit) generally focuses on whether the contractor disclosed current, accurate and complete cost or pricing data in the contract negotiation process pursuant to TINA and the Federal Acquisition Regulation (“FAR”). Shortly after this audit began, the Defense Contract Management Agency (“DCMA”) advised us that the fiscal 2008 award of the BFT-1 contract triggered full coverage under the Cost Accounting Standards (“CAS”) and that we should submit an initial CAS disclosure statement. The CAS is a set of specialized rules and standards that the U.S. government uses for determining costs on large, negotiated contracts. We have cooperated fully with the DCAA and DCMA and provided them information that supports our view that the August 2007 BFT-1 contract is subject to a CAS and TINA exemption for fixed price commercial contract line items (such as our mobile satellite transceivers and other hardware), as defined by the FAR.

In March 2013, DCMA advised us that it was not making any determination with regard to the commerciality of our products and that it withdrew its request, at that time, for a CAS disclosure statement.

In May 2013, the DCAA provided a draft audit report which stated that the commercial item exemption to TINA did not apply because there was no official determination of commerciality for Delivery Order No. 1 at the time of award. Thus, according to DCAA, TINA applied and we were required to disclose current, accurate and complete cost or pricing data. The DCAA recommended a price adjustment of $11,819,000 (plus interest). This recommended price adjustment is approximately the same amount that was included in a draft audit report that was presented to us in December 2012.

Consistent with the position we have taken throughout the audit, we informed the DCAA that we believe the May 2013 draft audit report is erroneous. For example, we noted that the U.S. Army had previously determined, in July 2007, that the MT 2011F mobile satellite transceiver was a commercial item on a separate contract awarded to us. We also noted that the same contracting officer who signed the August 2007 BFT-1 contract, in an email sent four days after the BFT-1 contract was signed, indicated that certain of our mobile satellite transceivers and other equipment on the August 2007 BFT-1 contract were commercial. We advised the DCAA that, although the August 2007 BFT-1 contract did not initially incorporate FAR commercial clauses, the contract was modified in January 2008 to incorporate those clauses, and that an Administrative Contracting Officer confirmed, in January 2008, that Delivery Order No. 1 was for commercial items. Regardless of the commerciality determination, we informed the DCAA that we provided the U.S. government with all required information prior to August 31, 2007. We disagree with the DCAA's draft audit report and provided a written response in May 2013.

In October 2013, we were first advised verbally by a DCAA senior auditor that a final DCAA audit report was issued to our BFT-1 Contracting Officer. To date, we have not received a copy of a final report, nor any correspondence concerning issuance of a final report.

If the above matters are not resolved in our favor with the Contracting Officer, the U.S. government could issue a demand in the form of a Contracting Officer's Final Decision, which we would have the right to appeal to the Armed Services Board of Contract Appeals or the U.S. Court of Federal Claims. If it is ultimately determined that a cost or price adjustment for our BFT-1 contract is appropriate, we would be required to refund monies to the U.S. government, with interest. These amounts could have a material adverse effect on our results of operations in the period in which we believe it is probable that we will be required to refund monies to the U.S. government. However, based on our analysis of the facts and circumstances regarding this matter, we do not believe this matter will ultimately have a material adverse effect on our consolidated financial condition.

Other Proceedings
There are certain other pending and threatened legal actions which arise in the normal course of business. Although the ultimate outcome of litigation is difficult to accurately predict, we believe that the outcome of these other pending and threatened actions will not have a material adverse effect on our consolidated financial condition or results of operations.

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

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Certain information in this Quarterly Report on Form 10-Q contains forward-looking statements, including but not limited to, information relating to our future performance and financial condition, plans and objectives of our management and our assumptions regarding such future performance, financial condition, and plans and objectives that involve certain significant known and unknown risks and uncertainties and other factors not under our control which may cause our actual results, future performance and financial condition, and achievement of our plans and objectives to be materially different from the results, performance or other expectations implied by these forward-looking statements. These factors include the nature and timing of receipt of, and our performance on, new or existing orders that can cause significant fluctuations in net sales and operating results, the timing and funding of government contracts, adjustments to gross profits on long-term contracts, risks associated with international sales, rapid technological change, evolving industry standards, new product announcements and enhancements, changing customer demands, changes in prevailing economic and political conditions, risks associated with our legal proceedings and other matters, risks associated with certain U.S. government investigations, risks associated with our BFT-1 contracts and the post-award audit of our original BFT-1 contract, risks associated with our obligations under our revolving credit facility, and other factors described in this and other filings with the Securities and Exchange Commission ("SEC").

OVERVIEW

We design, develop, produce and market innovative products, systems and services for advanced communications solutions. We believe many of our solutions play a vital role in providing or enhancing communication capabilities when terrestrial communications infrastructure is unavailable, inefficient or too expensive. We conduct our business through three complementary operating segments: telecommunications transmission, RF microwave amplifiers and mobile data communications. We sell our products to a diverse customer base in the global commercial and government communications markets. We believe we are a leader in the market segments that we serve.

Our telecommunications transmission segment provides sophisticated equipment and systems that are used to enhance satellite transmission efficiency and that enable wireless communications in environments where terrestrial communications are unavailable, inefficient or too expensive. Our telecommunications transmission segment also operates our high-volume technology manufacturing center that can be utilized, in part, by our other two segments and by third-party commercial customers who can outsource a portion of their manufacturing to us. Accordingly, our telecommunications transmission segment's operating results are impacted positively or negatively by the level of utilization of our high-volume manufacturing center.

Our RF microwave amplifiers segment designs, develops, manufactures and markets traveling wave tube amplifiers and solid-state amplifiers, including high-power, narrow and broadband RF microwave amplifier products.

Our mobile data communications segment's products and services substantially relate to our support of the U.S. Army's Blue Force Tracking ("BFT-1") and the U.S. Army's Movement Tracking System ("MTS") programs, which are currently in a sustainment mode. We license certain of our intellectual property to the U.S. Army and provide satellite network and related engineering services (including program management) on a cost-plus-fixed-fee basis.

Quarterly and period-to-period sales and operating results may be significantly affected by either short-term or long-term contracts with our customers. In addition, our gross profit is affected by a variety of factors, including the mix of products, systems and services sold, production efficiencies, estimates of warranty expense, price competition and general economic conditions. Our gross profit may also be affected by the impact of any cumulative adjustments to contracts that are accounted for under the percentage-of-completion method.

Our contracts with the U.S. government can be terminated at any time and orders are subject to unpredictable funding, deployment and technology decisions by the U.S. government. Some of these contracts, such as the BFT-1 sustainment contract, are indefinite delivery/indefinite quantity ("IDIQ") contracts and, as such, the U.S. government is not obligated to purchase any equipment or services under these contracts. We have in the past experienced and we continue to expect significant fluctuations in sales and operating results from quarter-to-quarter and period-to-period. As such, comparisons between periods and our current results may not be indicative of a trend or future performance.

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As further discussed below, under “Critical Accounting Policies,” revenue from the sale of our products is generally recognized when the earnings process is complete, upon shipment or customer acceptance. Revenue from contracts relating to the design, development or manufacture of complex electronic equipment to a buyer’s specification or to provide services relating to the performance of such contracts is generally recognized in accordance with accounting standards that have been codified into Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 605-35, “Revenue Recognition - Construction-Type and Production-Type Contracts” (“ASC 605-35”). Revenue from contracts that contain multiple elements that are not accounted for under FASB ASC 605-35 is generally accounted for in accordance with FASB ASC 605-25, “Revenue Recognition - Multiple Element Arrangements,” which, among other things, requires revenue associated with multiple element arrangements to be allocated to each element based on the relative selling price method.

CRITICAL ACCOUNTING POLICIES

We consider certain accounting policies to be critical due to the estimation process involved in each.

Revenue Recognition on Long-Term Contracts. Revenues and related costs from long-term contracts relating to the design, development or manufacture of complex electronic equipment to a buyer’s specification or to provide services relating to the performance of such contracts are recognized in accordance with FASB ASC 605-35, “Revenue Recognition - Construction-Type and Production-Type Contracts” (“ASC 605-35”). We primarily apply the percentage-of-completion accounting method and generally recognize revenue based on the relationship of total costs incurred to total projected costs, or, alternatively, based on output measures, such as units delivered or produced. Profits expected to be realized on such contracts are based on total estimated sales for the contract compared to total estimated costs, including warranty costs, at completion of the contract.

Direct costs (which include materials, labor and overhead) are charged to work-in-progress (including our contracts-in-progress) inventory or cost of sales. Indirect costs relating to long-term contracts, which include expenses such as general and administrative, are charged to expense as incurred and are not included in our work-in-process (including our contracts-in-progress) inventory or cost of sales. Total estimates are reviewed and revised periodically throughout the lives of the contracts, and adjustments to profits resulting from such revisions are made cumulative to the date of the change. Estimated losses on long-term contracts are recorded in the period in which the losses become evident. Long-term U.S. government cost-reimbursable type contracts are also specifically covered by FASB ASC 605-35.

We have been engaged in the production and delivery of goods and services on a continual basis under long-term contractual arrangements for many years. Historically, we have demonstrated an ability to accurately estimate total revenues and total expenses relating to our long-term contracts. However, there exist inherent risks and uncertainties in estimating revenues, expenses and progress toward completion, particularly on larger or longer-term contracts. If we do not accurately estimate the total sales, related costs and progress towards completion on such contracts, the estimated gross margins may be significantly impacted or losses may need to be recognized in future periods. Any such resulting changes in margins or contract losses could be material to our results of operations and financial condition.

In addition, most government contracts have termination for convenience clauses that provide the customer with the right to terminate the contract at any time. Such terminations could impact the assumptions regarding total contract revenues and expenses utilized in recognizing profit under the percentage-of-completion method of accounting. Changes to these assumptions could materially impact our results of operations and financial condition. Historically, we have not experienced material terminations of our long-term contracts. We also address customer acceptance provisions in assessing our ability to perform our contractual obligations under long-term contracts. Our inability to perform on our long-term contracts could materially impact our results of operations and financial condition. Historically, we have been able to perform on our long-term contracts.

Accounting for Stock-Based Compensation. As discussed further in “Notes to Condensed Consolidated Financial Statements – Note (13) Stock-Based Compensation,” we issue stock-based awards to certain of our employees and members of our Board of Directors and we recognize related stock-based compensation for both equity and liability-classified stock-based awards in our condensed consolidated financial statements.

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We have used and expect to continue to use the Black-Scholes option pricing model to compute the estimated fair value of certain stock-based awards. The Black-Scholes option pricing model includes assumptions regarding dividend yield, expected volatility, expected option term and risk-free interest rates. The expected dividend yield is the expected annual dividend as a percentage of the fair market value of the stock on the date of grant. We estimate expected volatility by considering the historical volatility of our stock, the implied volatility of publicly traded call options on our stock, the implied volatility from call options embedded in our 3.0% convertible senior notes and our expectations of volatility for the expected life of stock options. The expected option term is the number of years that we estimate that stock options will be outstanding prior to exercise based upon exercise patterns. The risk-free interest rate is based on the U.S. treasury yield curve in effect at the time of grant for an instrument which closely approximates the expected option term.

The assumptions used in computing the fair value of stock-based awards reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by recipients of stock-based awards. As a result, if other assumptions or estimates had been used, stock-based compensation expense that was recorded could have been materially different. Furthermore, if different assumptions are used in future periods, stock-based compensation expense could be materially impacted in the future.

Impairment of Goodwill and Other Intangible Assets. As of January 31, 2014, goodwill recorded on our Condensed Consolidated Balance Sheet aggregated $137.4 million (of which $107.8 million relates to our telecommunications transmission segment and $29.6 million relates to our RF microwave amplifiers segment). Our mobile data communications segment has no goodwill recorded. Each of our three operating segments constitutes a reporting unit and we must make various assumptions in determining their estimated fair values.

In accordance with FASB ASC 350, “Intangibles - Goodwill and Other,” we perform goodwill impairment testing at least annually, unless indicators of impairment exist in interim periods. The impairment test for goodwill uses a two-step approach. Step one compares the estimated fair value of a reporting unit with goodwill to its carrying value. If the carrying value exceeds the estimated fair value, step two must be performed. Step two compares the carrying value of the reporting unit to the fair value of all of the assets and liabilities of the reporting unit (including any unrecognized intangibles) as if the reporting unit was acquired in a business combination. If the carrying amount of a reporting unit's goodwill exceeds the implied fair value of its goodwill, an impairment loss is recognized in an amount equal to the excess.

On August 1, 2013 (the first day of our fiscal 2014), we performed our annual impairment test and estimated the fair value of each of our reporting units based on the income approach (also known as the discounted cash flow (“DCF”) method, which utilizes the present value of cash flows to estimate fair value). The future cash flows for our reporting units were projected based on our estimates, at that time, of future revenues, operating income and other factors (such as working capital and capital expenditures). We took into account expected challenging global industry and market conditions, including expected significant reductions in the overall budget for U.S. defense spending. As such, although both our telecommunications transmission and RF microwave amplifiers reporting units have historically achieved significant long-term revenue and operating income growth, we assumed growth rate estimates in our projections that were below our actual long-term expectations and below each reporting unit's actual historical growth rate. The discount rates used in our DCF method were based on a weighted-average cost of capital (“WACC”) determined from relevant market comparisons, adjusted upward for specific reporting unit risks (primarily the uncertainty of achieving projected operating cash flows). A terminal value growth rate was applied to the final year of the projected period and reflected our estimate of stable, perpetual growth. We then calculated a present value of the respective cash flows for each reporting unit to arrive at an estimate of fair value under the income approach and then used the market approach to corroborate this value. Under the market approach, we estimated a fair value based on comparable companies' market multiples of revenues and earnings before interest, taxes, depreciation and amortization and factored in a control premium. In each case, the estimated fair value determined under the market approach exceeded our estimate of fair value determined under the income approach. Finally, we compared our estimates to our August 1, 2013 total public market capitalization and assessed implied control premiums. Based on the aforementioned, we concluded that the estimated fair value determined under the income approach for each of our reporting units, as of August 1, 2013, was reasonable. In each case, the estimated fair value exceeded the respective carrying value and, as such, we concluded that the goodwill assigned to our telecommunications transmission and RF microwave amplifiers reporting units, as of August 1, 2013, was not impaired. We also concluded that our telecommunications transmission reporting unit was currently not at risk of failing step one of the goodwill impairment test as prescribed under the ASC. However, we concluded that as of August 1, 2013, our RF microwave amplifiers reporting unit was at risk of failing step one of the goodwill impairment test.

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As of August 1, 2013, we determined that our RF microwave amplifiers reporting unit had an estimated fair value in excess of its respective carrying value of at least 13.2%, which represents an increase from the at least 5.0% excess we previously calculated as of January 31, 2013 (when we performed an interim fiscal 2013 impairment test). The increase from 5.0% to 13.2% was primarily driven by a decrease in the WACC from 12.0% to 11.0%. The WACC for any given impairment test is based on current market data as of the respective valuation date. Had we utilized a WACC of 12.0% for the fiscal 2014 annual impairment test, our RF microwave amplifiers reporting unit's estimated fair value would still exceed its carrying value as of August 1, 2013. The WACC of 11.0% used in our annual impairment test for fiscal 2014 was equal to the WACC utilized in our annual impairment test for fiscal 2013.

This estimated fair value of our RF microwave amplifiers reporting unit is closely aligned with the ultimate amount of revenue and operating income that it achieves over the projected period. Our discounted cash flows, for goodwill impairment testing purposes, assumed that, through fiscal 2019, this reporting unit would achieve a compounded annual revenue growth rate of approximately 1.0% and 4.0% from its actual fiscal 2012 and 2013 revenues of $102.5 million and $86.9 million, respectively. Beyond fiscal 2019, we assumed a long-term revenue growth rate of 3.5% in the terminal year. Given current challenging market conditions, we believe these modest long-term growth rates and the WACC are appropriate to use for our future cash flow assumptions. We also believe that it is possible that our actual revenue growth rates could be significantly higher due to a number of factors, including: (i) continued reliance by our customers on our advanced communications systems; (ii) the continued shift toward information-based, network-centric warfare; and (iii) the need for developing countries to upgrade their communication systems. If we do not at least meet the assumed revenue growth utilized in this goodwill impairment analysis, our RF microwave amplifiers reporting unit will likely fail step one of a goodwill impairment test in a future period. Modest changes in other key assumptions used in our impairment analysis may also result in the requirement to proceed to step two of the goodwill impairment test in future periods. For example, keeping all other variables constant, a 160 basis point increase in the WACC applied to our RF microwave amplifiers reporting unit or an increase to our RF microwave amplifiers carrying value of more than $13.2 million would likely result in a step one failure. If this reporting unit fails step one in the future, we would be required to perform step two of the goodwill impairment test. If we perform step two, up to $42.8 million of goodwill and intangibles assigned to this reporting unit could be written off in the period that the impairment is triggered.

Our goodwill impairment analyses for the telecommunications transmission and RF microwave amplifiers reporting units are sensitive to the ultimate spending decisions by our global customers. Accordingly, we will continue to monitor key assumptions and other factors required to be utilized in evaluating impairment of goodwill. It is possible that, during fiscal 2014, business conditions (both in the U.S. and internationally) could deteriorate from the current state and our current or prospective customers could materially postpone, reduce or even forgo purchases of our products and services to a greater extent than we currently anticipate. A significant decline in defense spending that is greater than we anticipate or a shift in funding priorities may also have a negative effect on future orders, sales, income and cash flows and we might be required to perform a step one interim goodwill impairment test during fiscal 2014 for these two reporting units. In any event, we are required to perform the next annual step one goodwill impairment test on August 1, 2014 (the start of our fiscal 2015). If our assumptions and related estimates change in the future, or if we change our reporting structure or other events and circumstances change (e.g., such as a sustained decrease in the price of our common stock (considered on both absolute terms and relative to peers)), we may be required to record impairment charges when we perform these tests, or in other future periods. Any impairment charges that we may take in the future could be material to our results of operations and financial condition.

In addition to our impairment analysis of goodwill, we are also required to evaluate the recoverability of net intangibles with finite lives recorded on our Condensed Consolidated Balance Sheet which, as of January 31, 2014, aggregated $29.3 million (of which $16.1 million relates to our telecommunications transmission segment and $13.2 million relates to our RF microwave amplifiers segment). Based on our most recent analysis of estimated undiscounted future cash flows expected to result from the use of these net intangibles with finite lives, we believe that their carrying values are recoverable as of January 31, 2014.

Provision for Warranty Obligations. We provide warranty coverage for most of our products, including products under long-term contracts, for a period of at least one year from the date of shipment. We record a liability for estimated warranty expense based on historical claims, product failure rates and other factors. Costs associated with some of our warranties that are provided under long-term contracts are incorporated into our estimates of total contract costs.

There exist inherent risks and uncertainties in estimating warranty expenses, particularly on larger or longer-term contracts. As such, if we do not accurately estimate our warranty costs, any changes to our original estimates could be material to our results of operations and financial condition.

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Accounting for Income Taxes. Our deferred tax assets and liabilities are determined based on temporary differences between financial reporting and tax bases of assets and liabilities, and applying enacted tax rates expected to be in effect for the year in which the differences are expected to reverse. Our provision for income taxes is based on domestic (including federal and state) and international statutory income tax rates in the tax jurisdictions where we operate, permanent differences between financial reporting and tax reporting and available credits and incentives. We recognize interest and penalties related to uncertain tax positions in income tax expense. The U.S. federal government is our most significant income tax jurisdiction.

Significant judgment is required in determining income tax provisions and tax positions. We may be challenged upon review by the applicable taxing authority and positions taken by us may not be sustained. We recognize all or a portion of the benefit of income tax positions only when we have made a determination that it is more-likely-than-not that the tax position will be sustained upon examination, based upon the technical merits of the position and other factors. For tax positions that are determined as more-likely-than-not to be sustained upon examination, the tax benefit recognized is the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. The development of reserves for income tax positions requires consideration of timing and judgments about tax issues and potential outcomes, and is a subjective critical estimate. In certain circumstances, the ultimate outcome of exposures and risks involves significant uncertainties. If actual outcomes differ materially from these estimates, they could have a material impact on our results of operations and financial condition.

Provisions for Excess and Obsolete Inventory. We record a provision for excess and obsolete inventory based on historical and future usage trends. Other factors may also influence our provision, including decisions to exit a product line, technological change and new product development. These factors could result in a change in the amount of excess and obsolete inventory on hand. Additionally, our estimates of future product demand may prove to be inaccurate, in which case we may have understated or overstated the provision required for excess and obsolete inventory. In the future, if we determine that our inventory was overvalued, we would be required to recognize such costs in our financial statements at the time of such determination. Any such charge could be material to our results of operations and financial condition.

Allowance for Doubtful Accounts. We perform credit evaluations of our customers and adjust credit limits based upon customer payment history and current creditworthiness, as determined by our review of our customers' current credit information. Generally, we will require cash in advance or payment secured by irrevocable letters of credit before an order is accepted from an international customer that we do not do business with regularly. In addition, we seek to obtain credit insurance for certain domestic and international customers.

We monitor collections and payments from our customers and maintain an allowance for doubtful accounts based upon our historical experience and any specific customer collection issues that we have identified. In light of ongoing tight credit market conditions, we continue to see requests from our customers for higher credit limits and longer payment terms. Because of our strong cash position and the nominal amount of interest we are earning on our cash and cash equivalents, we have, on a limited basis, approved certain customer requests.

We continue to monitor our accounts receivable credit portfolio and have not had any significant negative customer credit experiences to date. While our credit losses have historically been within our expectations of the allowances established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past, especially in light of the current global economic conditions and much tighter credit environment. Measurement of credit losses requires consideration of historical loss experience, including the need to adjust for current conditions, and judgments about the probable effects of relevant observable data, including present economic conditions such as delinquency rates and the financial health of specific customers. Changes to the estimated allowance for doubtful accounts could be material to our results of operations and financial condition.

Business Outlook for Fiscal 2014

Our consolidated results for the first half of fiscal 2014 were solid and driven by increased sales of over-the-horizon microwave products as compared to the first half of fiscal 2013. Our second quarter of fiscal 2014 results benefited from increased revenues attributable to certain over-the-horizon microwave system contracts which were previously expected to be recorded during the second half of fiscal 2014.

Market conditions remain difficult; however, based on our year-to-date results and anticipated second half performance, we continue to believe that consolidated net sales in fiscal 2014 will be higher than the $319.8 million we achieved in fiscal 2013. In addition, operating income is expected to be higher than the $34.5 million that we achieved in fiscal 2013 and, as a percentage of consolidated net sales, is anticipated to increase in fiscal 2014 as compared to fiscal 2013. Given expected timing of orders and related performance, our third quarter revenues and operating income are expected to be the lowest quarter in fiscal 2014, and our fourth quarter of fiscal 2014 is expected to be the peak.

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Total operating expenses (which include research and development expenses, selling, general and administrative expenses, amortization of intangibles and amortization of stock-based compensation) in fiscal 2014 are expected to be slightly higher than the dollar amount reported in fiscal 2013.

Based on our fiscal 2014 business outlook, and excluding the impact of any discrete tax items, we expect our fiscal 2014 estimated effective tax rate to approximate 36.5%, as compared to 36.0% in fiscal 2013.

On December 9, 2013, our Board of Directors increased our annual target dividend from $1.10 per common share to $1.20 per common share and, in connection with this target, on March 6, 2014, declared a dividend of $0.30 per common share, payable on May 30, 2014 to shareholders of record at the close of business on May 7, 2014.

As of January 31, 2014, we had $318.0 million of cash and cash equivalents. During our most recently completed quarter, we continued to repurchase our common stock pursuant to our existing $100.0 million stock repurchase program. As of March 6, 2014, we can repurchase approximately $44.0 million of additional common stock pursuant to this program. We expect to generate significant cash flow from operating activities in fiscal 2014, although the amount of cash we will have at the end of fiscal 2014 may be impacted by the outcome of certain events related to our 3.0% convertible senior notes. If appropriate acquisition opportunities arise, we may also use a portion of our cash.

As discussed further in “Notes to Condensed Consolidated Financial Statements - Note (11) 3.0% Convertible Senior Notes,” holders of $200.0 million of our 3.0% convertible senior notes may require us to repurchase some or all of the outstanding notes solely for cash on May 1, 2014. In addition, we also have the right to redeem the notes for cash on or after May 5, 2014. Our Business Outlook for Fiscal 2014 assumes that our 3.0% convertible senior notes will be redeemed, repurchased or converted in May 2014 and that related interest expense in fiscal 2014 will be significantly lower than fiscal 2013.

Our business outlook for the remainder of fiscal 2014 and future years is dependent, in part, on the outcome of ongoing U.S. government budget issues and the growth of the global economy. Approximately 19.6% of our consolidated backlog at January 31, 2014 consisted of orders for U.S. government end customers. Excluding sales in our mobile data communications segment (which derives a substantial majority of its net sales from the U.S. government), aggregate sales to U.S. government end customers were 25.7% and 23.2% for the three and six months ended January 31, 2014, respectively.

In January 2014, the President signed the Consolidated Appropriations Act of 2014, providing for federal spending levels for the U.S. government’s fiscal year 2014. The U.S. government’s budget for fiscal 2015 has not yet been approved, is currently being hotly debated, and the application of sequestration to spending may occur. The ongoing uncertainty of future U.S. government spending has resulted in and continues to result in uncertainty amongst our global customer base. In addition to debt reduction efforts already authorized or planned for, it is possible that the U.S. government could reduce or further delay its spending on, or reprioritize its spending away from, government programs we participate in. It remains difficult, if not impossible, to determine specific amounts that are or will be appropriated for many of our products and services and our assessment may prove to be incorrect.

In addition to ongoing U.S. government budget pressures, we believe we will continue to operate in an environment of challenging global economic conditions and with ongoing uncertainty throughout our global customer base that we believe exists due to: (i) significant U.S. and foreign government budget constraints; (ii) challenging global business conditions; and (iii) increasingly volatile political conditions in certain international markets. If business conditions further deteriorate or our current or prospective customers materially postpone, reduce or even forgo purchases of our products and services to a greater extent than we currently anticipate, our fiscal 2014 business outlook will be adversely affected.

Additional information related to our Business Outlook for Fiscal 2014 is included in the below section entitled "Comparison of the Results of Operations for the Three Months Ended January 31, 2014 and January 31, 2013."

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COMPARISON OF THE RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JANUARY 31, 2014 AND JANUARY 31, 2013

Net Sales. Consolidated net sales were $85.5 million and $74.6 million for the three months ended January 31, 2014 and 2013, respectively, representing an increase of $10.9 million, or 14.6%. As further discussed below, the period-over-period increase reflects higher sales in our telecommunications transmission and RF microwave amplifiers segments, partially offset by lower sales in our mobile data communications segment.

Telecommunications Transmission
Net sales in our telecommunications transmission segment were $56.5 million and $45.8 million for the three months ended January 31, 2014 and 2013, respectively, an increase of $10.7 million, or 23.4%. This significant increase was almost entirely driven by higher sales in our over-the-horizon microwave systems product line.

Sales of our satellite earth station products during the three months ended January 31, 2014 were slightly higher as compared to the three months ended January 31, 2013. Sales during the three months ended January 31, 2014 include our ongoing efforts related to cost-plus-incentive-fee development work on our contract to develop and manufacture the Advanced Time Division Multiple Access ("TDMA") Interface Processor ("ATIP") for the U.S. Navy's Space and Naval Warfare Systems Command. Development work on this contract (which was awarded to us in fiscal 2013 and has a potential value of approximately $29.0 million) is expected to continue for the remainder of fiscal 2014. During the three months ended January 31, 2014, we received a $5.4 million order and signed a purchasing agreement with a global service provider against which we anticipate receiving additional future orders for the supply of our Advanced Very Small Aperture Terminal ("VSAT") solutions. For the three months ended January 31, 2014, the book-to-bill ratio for our satellite earth station products was slightly over 1.0 and our related backlog was at its highest level in over two years; however, recent customer order flow appears to be significantly impacted by volatility in market conditions, particularly in emerging markets, where many of our customers are located as well as the timing of receipt of certain large orders that have not yet come in. Our Business Outlook for Fiscal 2014 assumes that order flow will increase from current levels. Ultimately, we expect that fiscal 2014 net sales in this product line will be slightly higher than the levels we achieved in fiscal 2013. If we do not receive and ship expected orders, we may not be able to achieve our expected level of bookings or net sales for this product line in fiscal 2014.

Sales of our over-the-horizon microwave systems were significantly higher during the three months ended January 31, 2014 as compared to the three months ended January 31, 2013, primarily as a result of our ongoing performance on both our three-year $58.6 million and four-year $57.4 million contracts to design and supply over-the-horizon microwave systems and equipment for use in a North African government's communications network. Overall net sales for over-the-horizon microwave systems are expected to be significantly higher in fiscal 2014 as compared to the level we achieved in fiscal 2013, with our most recent quarter expected to be the peak quarter of sales in fiscal 2014. As a result of the timing of expected performance related to our two large North African contracts and other contracts currently in our backlog, over-the-horizon microwave system sales during the second half of fiscal 2014 are expected to be slightly lower than the first half of fiscal 2014, with third quarter net sales expected to be significantly lower than our most recent quarter.

Our telecommunications transmission segment represented 66.1% of consolidated net sales for the three months ended January 31, 2014, as compared to 61.4% for the three months ended January 31, 2013. Bookings, sales and profitability in our telecommunications transmission segment can fluctuate from period-to-period due to many factors, including the book and ship nature of our satellite earth station product business, the current uncertain conditions in the global economy, and the timing of, and our related performance on, contracts from the U.S. government (including prime contractors to the U.S. government) and international customers.

RF Microwave Amplifiers

Net sales in our RF microwave amplifiers segment were $22.0 million for the three months ended January 31, 2014, as compared to $20.4 million for the three months ended January 31, 2013, an increase of $1.6 million, or 7.8%. This increase reflects significantly higher sales in our solid state high-power amplifier product line partially offset by slightly lower sales of our traveling wave tube amplifiers.

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We experienced a significant period-over-period and slight sequential quarterly increase in bookings for our RF microwave amplifier products during the three months ended January 31, 2014, and our book-to-bill ratio for the most recent quarter was slightly below 1.0. Based on discussions with our customers, we believe that certain end markets for our RF microwave amplifier products have stabilized and we are optimistic that bookings for the second half of fiscal 2014 will be significantly higher than the first half, with the large majority of these bookings expected to ship in fiscal 2015. Although overall market conditions remain difficult, based on the current level of our backlog and the timing of new orders we expect to receive, we expect net sales in this segment in fiscal 2014 to be slightly higher than the level we achieved in fiscal 2013. If business conditions deteriorate from current levels or we do not receive expected orders, we may not be able to achieve our expected level of net sales for this segment in fiscal 2014.

Our RF microwave amplifiers segment represented 25.8% of consolidated net sales for the three months ended January 31, 2014 as compared to 27.3% for the three months ended January 31, 2013. Bookings, sales and profitability in our RF microwave amplifiers segment can fluctuate from period-to-period due to many factors, including the challenging business conditions and U.S. and international military budget constraints that currently exist, and the timing of, and our related performance on, contracts from the U.S. government (including prime contractors to the U.S. government) and international customers.

Mobile Data Communications
Net sales in our mobile data communications segment were $6.9 million for the three months ended January 31, 2014 as compared to $8.4 million for the three months ended January 31, 2013, a decrease of $1.5 million, or 17.9%. This anticipated decrease is primarily attributable to a decline in BFT-1 sustainment sales to the U.S. Army.

During the three months ended January 31, 2014 and 2013, BFT-1 sustainment sales to the U.S. Army were $5.9 million, or 85.5%, and $6.9 million, or 82.1%, respectively, of our mobile data communications segment's sales. Sales in both periods include $2.5 million of revenue related to our annual $10.0 million BFT-1 intellectual property license fee. The remaining BFT-1 sustainment sales for both periods primarily related to certain satellite network and related engineering services (including program management) that are provided on a cost-plus-fixed-fee basis.

Sales to the U.S. Army for BFT-1 sustainment services (including the licensing of certain of our intellectual property to the U.S. Army) are pursuant to a two-year $44.3 million indefinite delivery/indefinite quantity ("IDIQ") BFT-1 sustainment contract. Funding for the first year of this BFT-1 sustainment contract (which had a performance period from April 1, 2012 through March 31, 2013) was definitized at $22.8 million and funding for the second year (which has a performance period from April 1, 2013 through March 31, 2014) is currently at $21.5 million (including the annual $10.0 million intellectual property license fee). Specific terms and conditions related to the intellectual property license fee are covered by a separate licensing agreement that provides for annual renewals, at the U.S. Army's option, for up to a five-year period ending March 31, 2017, after which time the U.S. Army will have a limited non-exclusive right to use certain of our intellectual property for no additional intellectual property licensing fee.

We expect net sales in our mobile data communications segment in fiscal 2014 to be significantly lower than the amount we achieved in fiscal 2013, primarily based on the current level of our backlog and the anticipated receipt of a new contract for BFT-1 sustainment services (including the annual $10.0 million intellectual property license fee). In addition, net sales in our mobile data communications segment in fiscal 2013 include revenue related to our Sensor Enabled Notification System ("SENS") technology-based solutions. In the first quarter of fiscal 2014, we sold certain of our SENS technology and products, including certain intellectual property, to one of our customers for approximately $2.0 million and only expect to generate a nominal amount of royalties in the second half of fiscal 2014 and for the foreseeable future. Through January 31, 2014, we have cumulatively recorded $18.5 million of total BFT-1 sustainment revenue (of which $7.0 million and $11.5 million was recorded in fiscal 2013 and fiscal 2014, respectively, with the remainder in backlog) against the $21.5 million of available funding discussed above. Although we have not yet received a draft contract, we have been informally notified by the U.S. Army that it intends to award us a new multi-year contract for BFT-1 sustainment services for performance periods beyond March 31, 2014. However, due to ongoing U.S. government budget pressures, future funding, contract modifications and new contract awards for BFT-1 sustainment services are difficult to predict. If the U.S. Army does not award us a new contract and does not exercise its option to renew the annual $10.0 million intellectual property license fee, it would have a material adverse effect on our fiscal 2014 business outlook.

Based on the expected amount of new BFT-1 sustainment funding, the timing of performance for new BFT-1 sustainment orders and the absence of $2.0 million of high margin revenue resulting from the sale of certain of our SENS technology-based solutions, our mobile data communications segment’s net sales are expected to be lower during the second half of fiscal 2014 as compared to the first half of fiscal 2014 and net sales during the third quarter of fiscal 2014 are expected to be lower as compared to our most recent quarter.

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Our mobile data communications segment represented 8.1% of consolidated net sales for the three months ended January 31, 2014, as compared to 11.3% for the three months ended January 31, 2013. Bookings, sales and profitability in our mobile data communications segment can fluctuate dramatically from period-to-period due to many factors, including unpredictable funding, deployment and technology decisions by the U.S. government. As such, period-to-period comparisons of our results may not be indicative of a trend or future performance.

Geography and Customer Type
Sales to U.S. government end customers approximated 31.2% and 32.8% of consolidated net sales for the three months ended January 31, 2014 and 2013, respectively. Excluding net sales in our mobile data communications segment (which derives a substantial majority of its net sales from the U.S. government), aggregate sales to U.S. government end customers were 25.7% and 25.8% for the three months ended January 31, 2014 and 2013, respectively.

International sales (which include sales to U.S. companies for inclusion in products that are sold to international customers) approximated 57.5% and 54.3% of consolidated net sales for the three months ended January 31, 2014 and 2013, respectively. Domestic commercial sales approximated 11.3% and 12.9% of consolidated net sales for the three months ended January 31, 2014 and 2013, respectively.

Gross Profit. Gross profit was $37.4 million and $32.2 million for the three months ended January 31, 2014 and 2013, respectively, representing an increase of $5.2 million, which was primarily driven by the increase in consolidated net sales and an increase in our gross profit, as a percentage of consolidated net sales, from 43.2% to 43.7%. Gross profit, as a percentage of related segment sales, is further discussed below.

Our telecommunications transmission segment's gross profit, as a percentage of related segment net sales, for the three months ended January 31, 2014, was slightly lower than the percentage achieved for the three months ended January 31, 2013. The slight decrease was primarily the result of changes in overall sales mix, including a significantly higher percentage of segment sales being comprised of our over-the-horizon-microwave systems which traditionally have lower gross margins than our satellite earth station products. Our gross profit percentage in this segment during three months ended January 31, 2014 also reflects low margin sales associated with developing the U.S. Navy's ATIP for which we recover our costs plus a nominal incentive fee. Based on the nature and type of orders that are currently in our backlog and anticipated orders we expect to receive, we expect gross profit, as a percentage of related segment net sales, in fiscal 2014 to be lower than the level we achieved in fiscal 2013.

Our RF microwave amplifiers segment experienced a lower gross profit, as a percentage of related segment net sales, for the three months ended January 31, 2014 as compared to the three months ended January 31, 2013. This decrease was primarily the result of changes in overall sales mix. Based on the nature and type of orders that are currently in our backlog and anticipated orders we expect to receive, we expect gross profit, both in dollars and as a percentage of related segment net sales, in fiscal 2014 to be slightly higher than the level we achieved in fiscal 2013.

Our mobile data communications segment's gross profit, as a percentage of related segment net sales, for the three months ended January 31, 2014 was significantly higher as compared to the three months ended January 31, 2013. The increase was primarily due to changes in overall sales mix. Gross profit in both periods reflects the benefit of $2.5 million of higher margin revenue related to our annual $10.0 million intellectual property license fee. Based on the level and expected composition of BFT-1 sustainment sales, our gross profit, as a percentage of sales in this segment, in fiscal 2014 is expected to be higher than the percentage we achieved in fiscal 2013.

Included in consolidated cost of sales for the three months ended January 31, 2014 and 2013 are provisions for excess and obsolete inventory of $0.8 million and $0.6 million, respectively. As discussed in “Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies - Provisions for Excess and Obsolete Inventory," we regularly review our inventory and record a provision for excess and obsolete inventory based on historical and projected usage assumptions.

Because our consolidated gross profit, as a percentage of consolidated net sales, depends on sales, sales mix and related gross profit for each individual segment, it is difficult to forecast. Nevertheless, based on our anticipated performance on orders currently in our consolidated backlog and on orders we expect to receive, we anticipate that our fiscal 2014 consolidated gross profit, in dollars, will be higher than the level we achieved in fiscal 2013 and, as a percentage of consolidated net sales, will be comparable to the percentage we achieved in fiscal 2013.

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Selling, General and Administrative Expenses. Selling, general and administrative expenses were $16.3 million and $15.4 million for the three months ended January 31, 2014 and 2013, respectively, representing an increase of $0.9 million.

As a percentage of consolidated net sales, selling, general and administrative expenses were 19.1% and 20.6% for the three months ended January 31, 2014 and 2013, respectively. For the three months ended January 31, 2013, excluding $1.1 million of benefits comprised of a $0.9 million change in the fair value of a contingent earn-out liability associated with our acquisition of Stampede Technologies, Inc. ("Stampede") and a reversal of $0.2 million of previously accrued costs associated with the wind-down of our microsatellite product line, selling, general and administrative expenses would have been $16.5 million or 22.1% of consolidated net sales. The decrease in selling, general and administrative expenses, as a percentage of consolidated net sales, from 22.1% to 19.1% is primarily related to an increase in consolidated net sales and our ongoing efforts to contain costs.

Amortization of stock-based compensation expense recorded as selling, general and administrative expenses increased to $0.8 million in the three months ended January 31, 2014 as compared to $0.6 million in the three months ended January 31, 2013. This increase is primarily related to changes in the timing of grants for certain stock-based awards.

In light of consolidated net sales growth expected in fiscal 2014, selling, general and administrative expenses, in dollars, are expected to be higher in fiscal 2014 as compared to fiscal 2013. As a percentage of consolidated net sales, we expect selling, general and administrative expenses in fiscal 2014 to be comparable to fiscal 2013.

Research and Development Expenses. Research and development expenses were $8.3 million and $9.3 million for the three months ended January 31, 2014 and 2013, respectively, representing a decrease of $1.0 million, or 10.8%.

For the three months ended January 31, 2014 and 2013, research and development expenses of $6.0 million and $7.1 million, respectively, related to our telecommunications transmission segment. Research and development expenses related to our RF microwave amplifiers segment were $2.1 million for both the three months ended January 31, 2014 and 2013 and were nominal for both periods in our mobile data communications segment. The remaining research and development expenses we incurred relate to the amortization of stock-based compensation expense, which is not allocated to our three reportable operating segments and was $0.2 million and $0.1 million for the three months ended January 31, 2014 and 2013, respectively.

As a percentage of consolidated net sales, research and development expenses were 9.7% and 12.5% for the three months ended January 31, 2014 and 2013, respectively. The decrease in research and development expenses, in dollars, is attributable to lower spending during the three months ended January 31, 2014 as compared to the three months ended January 31, 2013 and the decrease in research and development expenses, as a percentage of consolidated net sales, is attributable to both lower spending and increased net sales. We anticipate that fiscal 2014 research and development expenses (both in dollars and as a percentage of expected consolidated net sales) will be lower than the levels we reported in fiscal 2013.

As an investment for the future, we are continually enhancing our existing products and developing new products and technologies. Whenever possible, we seek customer funding for research and development to adapt our products to specialized customer requirements. During the three months ended January 31, 2014 and 2013, customers reimbursed us $3.6 million and $0.8 million, respectively, which is not reflected in the reported research and development expenses, but is included in net sales with the related costs included in cost of sales. Included in customer funded research and development for the three months ended January 31, 2014 is funding related to work performed on our cost-plus-incentive-fee development contract for the U.S. Navy's ATIP.

Amortization of Intangibles. Amortization relating to intangible assets with finite lives was $1.6 million for both the three months ended January 31, 2014 and 2013.

Operating Income. Operating income for the three months ended January 31, 2014 and 2013 was $11.2 million, or 13.1% of consolidated net sales, and $5.9 million, or 7.9% of consolidated net sales, respectively. Operating income for the three months ended January 31, 2013 reflects $1.1 million of benefits as discussed above in the selling, general and administrative expenses section. Excluding this benefit, operating income for the three months ended January 31, 2013 would have been $4.8 million, or 6.4%, of consolidated net sales, respectively.

This significant increase in operating income (both in dollars and as a percentage of consolidated net sales) is primarily attributable to higher consolidated net sales, changes in comparative sales mix, and a similar level of operating expenses in the three months ended January 31, 2014 as compared to the three months ended January 31, 2013. Operating income, by segment, is discussed further below.

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Operating income in our telecommunications transmission segment was $10.3 million, or 18.2% of related segment net sales, for the three months ended January 31, 2014, as compared to $5.5 million, or 12.0% of related segment net sales, for the three months ended January 31, 2013. Excluding the previously discussed $0.9 million change in fair value of the Stampede contingent earn-out liability, operating income, as a percentage of related net sales for the three months ended January 31, 2013, was 10.0%. The increase from 10.0% to 18.2% was primarily due to the significant increase in this segment's net sales, which were almost entirely driven by increased sales of our over-the-horizon-microwave system products, and lower research and development expenses, as previously discussed. Large fluctuations, in any given period, in over-the-horizon microwave system sales and production activities significantly impact our operating margins because this product line is supported by a relatively fixed cost structure. Given the expected lumpiness of over-the-horizon microwave system sales for the remainder of fiscal 2014, operating margins for this segment (both in dollars and as a percentage of related segment net sales), during the third quarter of fiscal 2014, are expected to significantly decline from the level we achieved in our most recent quarter and improve during the fourth quarter. However, based on our year-to-date performance and expected performance during the second half of fiscal 2014, we expect operating income in this segment in fiscal 2014 (both in dollars and as a percentage of related segment net sales) to be higher than the level we achieved in fiscal 2013.

Our RF microwave amplifiers segment generated operating income of $1.1 million, or 5.0% of related segment net sales, for the three months ended January 31, 2014 as compared to $0.6 million, or 2.9% of related segment net sales, for the three months ended January 31, 2013. The increase in operating income, both in dollars and as a percentage of related segment net sales, is primarily due to the increase in this segment's net sales. Based on the nature and type of orders that are currently in our backlog, anticipated orders we expect to receive, and anticipated research and development spending, we expect that operating income in this segment (both in dollars and as a percentage of related segment net sales) will improve from current levels during the second half of fiscal 2014 and will be higher in fiscal 2014 than the level we achieved in fiscal 2013.

Our mobile data communications segment generated operating income of $3.3 million, or 47.8% of related segment net sales, for the three months ended January 31, 2014 as compared to $3.0 million, or 35.7% of related segment net sales, for the three months ended January 31, 2013. Excluding the previously discussed reversal of $0.2 million of previously accrued costs associated with the wind-down of our microsatellite product line, operating income, for the three months ended January 31, 2013 was $2.8 million or 33.3%. The increase in operating income, both in dollars and as a percentage of related segment net sales, was primarily driven by overall changes in this segment's sales mix and cost reduction actions that we previously took, as discussed above. Given the expected level and composition of mobile data communication segment sales during the second half of fiscal 2014, operating income in this segment (both in dollars and a percentage of related segment net sales) is expected to decline from the level we achieved in our most recent quarter. However, based on our year-to-date performance and expected performance during the second half of fiscal 2014, we expect operating income in this segment (in dollars) for fiscal 2014 to be comparable to the level we achieved in fiscal 2013 and operating income in this segment (as a percentage of related segment net sales) to be higher than the level we achieved in fiscal 2013.

Unallocated operating expenses were $3.5 million for the three months ended January 31, 2014 as compared to $3.2 million for the three months ended January 31, 2013. The increase is primarily attributable to an increase in amortization of stock-based compensation expense.

Amortization of stock-based compensation expense, which is included in unallocated operating expenses, was $1.1 million for the three months ended January 31, 2014 as compared to $0.8 million in the three months ended January 31, 2013, primarily due to changes in the timing of grants for certain stock-based awards (as discussed above in the selling, general and administrative expenses section).

Based on the level and composition of sales that we expect to achieve in fiscal 2014, we are targeting operating income, as a percentage of consolidated net sales, to be at least 11.0% in fiscal 2014. Given expected product mix changes and the expected lumpiness of our sales, we expect operating income, as a percentage of consolidated net sales, in the third quarter of fiscal 2014 to approximate 8.0% and to reach its peak for the year in the fourth quarter.

Interest Expense. Interest expense was $2.0 million for both the three months ended January 31, 2014 and 2013 and primarily reflects interest on our 3.0% convertible notes. Our Business Outlook for Fiscal 2014 assumes that our 3.0% convertible notes will be converted, redeemed or repurchased in May 2014. As such, we currently anticipate that interest expense in fiscal 2014 will be significantly lower than fiscal 2013.

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Interest Income and Other. Interest income and other for the three months ended January 31, 2014 and 2013 was $0.2 million and $0.3 million, respectively. Interest income and other for both periods is primarily generated from interest earned on our cash and cash equivalents. All of our available cash and cash equivalents are currently invested in bank deposits, money market mutual funds, certificates of deposit, and short-term U.S. Treasury securities which, at this time, are currently yielding a blended annual interest rate of approximately 0.37%.

Provision for Income Taxes. The provision for income taxes was $3.4 million and $1.9 million for the three months ended January 31, 2014 and 2013, respectively. Our effective tax rate was 36.4% for the three months ended January 31, 2014, as compared to 44.1% for the three months ended January 31, 2013.

Our effective tax rate for the three months ended January 31, 2014 reflects a discrete tax benefit of less than $0.1 million. Our effective tax rate for the three months ended January 31, 2013 reflects a net discrete tax expense of approximately $0.4 million, principally related to the establishment of a valuation allowance on certain deferred tax assets of one of our foreign subsidiaries, offset, in part, by a discrete tax benefit related to the passage of legislation that included the retroactive extension of the federal research and experimentation credit from December 31, 2011 to December 31, 2013. Excluding these discrete tax items in both periods, our effective tax rate for the three months ended January 31, 2014 would have been 36.5% as compared to 35.5% for the three months ended January 31, 2013. The increase from 35.5% to 36.5% is principally attributable to the expiration of the federal research and experimentation credit on December 31, 2013, and expected product and geographical mix changes reflected in our fiscal 2014 business outlook.

Excluding the impact of any discrete tax items, our fiscal 2014 effective tax rate is expected to approximate 36.5%. This rate reflects the expiration of the federal research and experimentation credit on December 31, 2013.

Our federal income tax returns for fiscal 2010 through 2013 are subject to potential future IRS audit. Future tax assessments or settlements could have a material adverse effect on our consolidated results of operations and financial condition.

COMPARISON OF THE RESULTS OF OPERATIONS FOR THE SIX MONTHS ENDED JANUARY 31, 2014 AND JANUARY 31, 2013

Net Sales. Consolidated net sales were $168.9 million and $165.5 million for the six months ended January 31, 2014 and 2013, respectively, representing an increase of $3.4 million, or 2.1%. As further discussed below, the period-over-period increase reflects higher net sales in our telecommunications transmission segment, partially offset by lower net sales in our RF microwave amplifiers and mobile data communications segments.

Telecommunications Transmission
Net sales in our telecommunications transmission segment were $110.9 million and $99.1 million for the six months ended January 31, 2014 and 2013, respectively, an increase of $11.8 million, or 11.9%. This increase reflects significantly higher net sales in our over-the-horizon microwave systems product line, partially offset by slightly lower net sales in our satellite earth station product line.

Sales of our satellite earth station products were slightly lower during the six months ended January 31, 2014 as compared to the six months ended January 31, 2013. Sales during the six months ended January 31, 2014 include our efforts related to cost-plus-incentive-fee development work on our contract to develop and manufacture the TDMA ATIP for the U.S. Navy's Space and Naval Warfare Systems Command. Development work on this contract (which was awarded to us in fiscal 2013 and has a potential value of approximately $29.0 million) is expected to continue for the remainder of fiscal 2014. During the six months ended January 31, 2014, we received a $5.4 million order and signed a purchasing agreement with a global service provider against which we anticipate receiving additional future orders for the supply of our Advanced VSAT solutions. For the six months ended January 31, 2014, the book-to-bill ratio for our satellite earth station products was slightly over 1.0 and our related backlog was at its highest level in over two years; however, recent customer order flow appears to be significantly impacted by volatility in market conditions, particularly in emerging markets, where many of our customers are located as well as the timing of receipt of certain large orders that have not yet come in. Our Business Outlook for Fiscal 2014 assumes that order flow will increase from current levels. Ultimately, we expect that fiscal 2014 sales in this product line will be slightly higher than the levels we achieved in fiscal 2013. If we do not receive and ship expected orders, we may not be able to achieve our expected level of bookings or net sales for this product line in fiscal 2014.

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Sales of our over-the-horizon microwave systems were significantly higher during the six months ended January 31, 2014 as compared to the six months ended January 31, 2013, primarily as a result of our ongoing performance on both our three-year $58.6 million and four-year $57.4 million contracts to design and supply over-the-horizon microwave systems and equipment for use in a North African government's communications network. Overall net sales for over-the-horizon microwave systems are expected to be significantly higher in fiscal 2014 as compared to the level we achieved in fiscal 2013, with our most recent quarter expected to be the peak quarter of sales in fiscal 2014. As a result of the timing of expected performance related to our two large North African contracts and other contracts currently in our backlog, over-the-horizon microwave system sales during the second half of fiscal 2014 are expected to be slightly lower than the first half of fiscal 2014, with third quarter net sales expected to be significantly lower than our most recent quarter.

Our telecommunications transmission segment represented 65.7% of consolidated net sales for the six months ended January 31, 2014, as compared to 59.9% for the six months ended January 31, 2013. Bookings, sales and profitability in our telecommunications transmission segment can fluctuate from period-to-period due to many factors, including the book and ship nature of our satellite earth station product business, the current adverse conditions in the global economy, and the timing of, and our related performance on, contracts from the U.S. government (including prime contractors to the U.S. government) and international customers.

RF Microwave Amplifiers

Net sales in our RF microwave amplifiers segment were $42.2 million for the six months ended January 31, 2014, as compared to $45.7 million for the six months ended January 31, 2013, a decrease of $3.5 million, or 7.7%. This decline reflects significantly lower sales in our traveling wave tube amplifier product line, partially offset by higher sales in our solid state high-power amplifier product line.

Although sales in this segment during the six months ended January 31, 2014 were impacted by challenging market conditions and the timing of orders received and shipped, bookings in our RF microwave amplifiers segment for the six months ended January 31, 2014 were higher as compared to the six months ended January 31, 2013. Our book-to-bill ratio for the six months ended January 31, 2014 was slightly below 1.0. Based on discussions with our customers, we believe that certain end markets for our RF microwave amplifier products have stabilized and we are optimistic that bookings for the second half of fiscal 2014 will be significantly higher than the first half, with the large majority of these bookings expected to ship in fiscal 2015. Although overall market conditions remain difficult, based on the current level of our backlog and the timing of new orders we expect to receive, we expect net sales in this segment in fiscal 2014 to be slightly higher than the level we achieved in fiscal 2013. If business conditions deteriorate from current levels or we do not receive expected orders, we may not be able to achieve our expected level of net sales for this segment in fiscal 2014.

Our RF microwave amplifiers segment represented 25.0% of consolidated net sales for the six months ended January 31, 2014 as compared to 27.6% for the six months ended January 31, 2013. Bookings, sales and profitability in our RF microwave amplifiers segment can fluctuate from period-to-period due to many factors, including the challenging business conditions and U.S. and international military budget constraints that currently exist, and the timing of, and our related performance on, contracts from the U.S. government (including prime contractors to the U.S. government) and international customers.

Mobile Data Communications

Net sales in our mobile data communications segment were $15.7 million for the six months ended January 31, 2014 as compared to $20.8 million for the six months ended January 31, 2013, a decrease of $5.1 million, or 24.5%. This anticipated decrease is primarily attributable to a decline in BFT-1 sustainment sales to the U.S. Army.

During the six months ended January 31, 2014 and 2013, BFT-1 sustainment sales to the U.S. Army were $11.4 million, or 72.6%, and $16.9 million, or 81.3%, respectively, of our mobile data communications segment's sales. Sales in both the six months ended January 31, 2014 and 2013 include $5.0 million of revenue related to our annual $10.0 million BFT-1 intellectual property license fee. Sales for the six months ended January 31, 2013 also include shipments of MTS and BFT-1 mobile satellite transceivers, for which we did not have any related sales during the six months ended January 31, 2014 and currently have no orders in our backlog. The remaining BFT-1 sustainment sales for both periods primarily related to certain satellite network and related engineering services (including program management) that are provided on a cost-plus-fixed-fee basis.

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Sales to the U.S. Army for BFT-1 sustainment services (including the licensing of certain of our intellectual property to the U.S. Army) are pursuant to a two-year $44.3 million IDIQ BFT-1 sustainment contract. Funding for the first year of this BFT-1 sustainment contract (which had a performance period from April 1, 2012 through March 31, 2013) was definitized at $22.8 million and funding for the second year (which has a performance period from April 1, 2013 through March 31, 2014) is currently at $21.5 million (including the annual $10.0 million intellectual property license fee). Specific terms and conditions related to the intellectual property license fee are covered by a separate licensing agreement that provides for annual renewals, at the U.S. Army's option, for up to a five-year period ending March 31, 2017, after which time the U.S. Army will have a limited non-exclusive right to use certain of our intellectual property for no additional intellectual property licensing fee.

We expect net sales in our mobile data communications segment in fiscal 2014 to be significantly lower than the amount we achieved in fiscal 2013, primarily based on the current level of our backlog and the anticipated receipt of a new contract for BFT-1 sustainment services (including the annual $10.0 million intellectual property license fee). In addition, net sales in our mobile data communications segment in fiscal 2013 include revenue related to our SENS technology-based solutions. In the first quarter of fiscal 2014, we sold certain of our SENS technology and products, including certain intellectual property, to one of our customers for approximately $2.0 million and only expect to generate a nominal amount of royalties in the second half of fiscal 2014 and for the foreseeable future. Through January 31, 2014, we have cumulatively recorded $18.5 million of total BFT-1 sustainment revenue (of which $7.0 million and $11.5 million was recorded in fiscal 2013 and fiscal 2014, respectively, with the remainder in backlog) against the $21.5 million of available funding discussed above. Although we have not yet received a draft contract, we have been informally notified by the U.S. Army that it intends to award us a new multi-year contract for BFT-1 sustainment services for performance periods beyond March 31, 2014. However, due to ongoing U.S. government budget pressures, future funding, contract modifications and new contract awards for BFT-1 sustainment services are difficult to predict. If the U.S. Army does not award us a new contract and does not exercise its option to renew the annual $10.0 million intellectual property license fee, it would have a material adverse effect on our fiscal 2014 business outlook.

Based on the expected amount of new BFT-1 sustainment funding, the timing of performance for new BFT-1 sustainment orders and the absence of $2.0 million of high margin revenue resulting from the sale of certain of our SENS technology-based solutions, our mobile data communications segment’s net sales are expected to be lower during the second half of fiscal 2014 as compared to the first half of fiscal 2014 and net sales during the third quarter of fiscal 2014 are expected to be lower as compared to our most recent quarter.

Our mobile data communications segment represented 9.3% of consolidated net sales for the six months ended January 31, 2014, as compared to 12.6% for the six months ended January 31, 2013. Bookings, sales and profitability in our mobile data communications segment can fluctuate dramatically from period-to-period due to many factors, including unpredictable funding, deployment and technology decisions by the U.S. government. As such, period-to-period comparisons of our results may not be indicative of a trend or future performance.

Geography and Customer Type

Sales to U.S. government end customers approximated 28.4% and 38.6% of consolidated net sales for the six months ended January 31, 2014 and 2013, respectively. Excluding net sales in our mobile data communications segment (which derives a substantial majority of its net sales from the U.S. government), aggregate sales to U.S. government end customers were 23.2%% and 31.5% for the six months ended January 31, 2014 and 2013, respectively.

International sales (which include sales to U.S. companies for inclusion in products that are sold to international customers) approximated 57.3% and 48.1% of consolidated net sales for the six months ended January 31, 2014 and 2013, respectively. Domestic commercial sales approximated 14.3% and 13.3% of consolidated net sales for the six months ended January 31, 2014 and 2013, respectively.

Gross Profit. Gross profit was $73.7 million and $74.0 million for the six months ended January 31, 2014 and 2013, respectively, representing a decrease of $0.3 million which was primarily driven by a decrease in our gross profit, as a percentage of consolidated net sales, from 44.7% to 43.6%. Gross profit, as a percentage of related segment sales, is further discussed below.

Our telecommunications transmission segment's gross profit, as a percentage of related segment net sales, for the six months ended January 31, 2014, was significantly lower than the percentage achieved for the six months ended January 31, 2013. The decrease was primarily the result of changes in overall sales mix. Our gross profit percentage in this segment during the six months ended January 31, 2014 was impacted by: (i) a significantly higher percentage of segment sales being comprised of our over-the-horizon-microwave products which traditionally have lower gross margins than our satellite earth station products, (ii) low margin sales associated with developing the U.S. Navy's ATIP for which we recover our costs plus a nominal incentive fee, and (iii) the absence of MTTS hardware sales for end-use by the U.S. Army (for which we do not expect to ship any in fiscal 2014). Based on the nature and type of orders that are currently in our backlog and anticipated orders we expect to receive, we expect gross profit, as a percentage of related segment net sales, in fiscal 2014 to be lower than the level we achieved in fiscal 2013.

Our RF microwave amplifiers segment's gross profit, as a percentage of related segment net sales, was the same for both the six months ended January 31, 2014 and 2013. Based on the nature and type of orders that are currently in our backlog and anticipated orders we expect to receive, we expect gross profit, both in dollars and as a percentage of related segment net sales, in fiscal 2014 to be slightly higher than the level we achieved in fiscal 2013.

Our mobile data communications segment's gross profit, as a percentage of related segment net sales, for the six months ended January 31, 2014 was significantly higher as compared to the six months ended January 31, 2013. The increase was primarily due to changes in overall sales mix. Gross profit in both periods reflects the benefit of $5.0 million of higher margin revenue related to our annual $10.0 million intellectual property license fee. Our gross profit percentage in this segment during the six months ended January 31, 2014 also reflects the benefit of $2.0 million of high margin revenue related to the sale of certain SENS technology-based solutions. Based on the level and expected composition of BFT-1 sustainment sales, our gross profit, as a percentage of sales in this segment, in fiscal 2014 is expected to be higher than the percentage we achieved in fiscal 2013.

Included in consolidated cost of sales for the six months ended January 31, 2014 and 2013 are provisions for excess and obsolete inventory of $1.5 million and $1.3 million, respectively. As discussed in our “Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies - Provisions for Excess and Obsolete Inventory,” we regularly review our inventory and record a provision for excess and obsolete inventory based on historical and projected usage assumptions.

Because our consolidated gross profit, as a percentage of consolidated net sales, depends on sales, sales mix and related gross profit for each individual segment, it is difficult to forecast. Nevertheless, based on our anticipated performance on orders currently in our consolidated backlog and on orders we expect to receive, we anticipate that our fiscal 2014 consolidated gross profit, in dollars, will be higher than the level we achieved in fiscal 2013 and, as a percentage of consolidated net sales, will be comparable to the percentage we achieved in fiscal 2013.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $32.5 million and $32.2 million for the six months ended January 31, 2014 and 2013, respectively, representing a slight increase of $0.3 million.

As a percentage of consolidated net sales, selling, general and administrative expenses were 19.2% and 19.5% for the six months ended January 31, 2014 and 2013, respectively. Excluding a $2.7 million net benefit comprised of a $3.3 million change in the fair value of a contingent earn-out liability associated with our acquisition of Stampede and a charge of $0.6 million for costs associated with the wind-down of our microsatellite product line, selling, general and administrative expenses, for the six months ended January 31, 2013 would have been $34.9 million or 21.1% of consolidated net sales. Excluding a $0.2 million benefit resulting from a change in the fair value of a contingent earn-out liability associated with our acquisition of Stampede, selling, general and administrative expenses, for the six months ended January 31, 2014 would have been $32.7 million or 19.4% of consolidated net sales. The decrease in selling, general and administrative expenses, as a percentage of consolidated net sales, from 21.1% to 19.4% is primarily related to an increase in consolidated net sales and our ongoing efforts to contain costs.

Amortization of stock-based compensation expense recorded as selling, general and administrative expenses increased to $1.6 million in the six months ended January 31, 2014 as compared to $1.2 million in the six months ended January 31, 2013. This increase is primarily related to changes in the timing of grants for certain stock-based awards.

In light of consolidated net sales growth expected in fiscal 2014, selling, general and administrative expenses, in dollars, are expected to be higher in fiscal 2014 as compared to fiscal 2013. As a percentage of consolidated net sales, we expect selling, general and administrative expenses in fiscal 2014 to be comparable to fiscal 2013.

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Research and Development Expenses. Research and development expenses were $16.8 million and $19.3 million for the six months ended January 31, 2014 and 2013, respectively, representing a decrease of $2.5 million, or 13.0%.

For the six months ended January 31, 2014 and 2013, research and development expenses of $12.1 million and $14.6 million, respectively, related to our telecommunications transmission segment, and $4.4 million and $4.5 million, respectively, related to our RF microwave amplifiers segment. Research and development expenses in our mobile data communications segment were nominal for both the six months ended January 31, 2014 and 2013. The remaining research and development expenses we incurred relate to the amortization of stock-based compensation expense, which is not allocated to our three reportable operating segments. Amortization of stock-based compensation expense recorded as research and development expenses was $0.3 million and $0.2 million for the six months ended January 31, 2014 and 2013, respectively.

As a percentage of consolidated net sales, research and development expenses were 9.9% and 11.7% for the six months ended January 31, 2014 and 2013, respectively. The decrease in research and development expenses, in dollars, is attributable to lower spending during the six months ended January 31, 2014 as compared to the six months ended January 31, 2013 and the decrease in research and development expenses, as a percentage of consolidated net sales, is attributable to both lower spending and increased net sales. We anticipate that fiscal 2014 research and development expenses (both in dollars and as a percentage of expected fiscal 2014 consolidated net sales) will be lower than the levels we reported in fiscal 2013.

As an investment for the future, we are continually enhancing our existing products and developing new products and technologies. Whenever possible, we seek customer funding for research and development to adapt our products to specialized customer requirements. During the six months ended January 31, 2014 and 2013, customers reimbursed us $6.7 million and $2.1 million, respectively, which is not reflected in the reported research and development expenses, but is included in net sales with the related costs included in cost of sales. Included in customer funded research and development for the six months ended January 31, 2014 is funding related to work performed on our cost-plus-incentive-fee development contract for the U.S. Navy's ATIP.

Amortization of Intangibles. Amortization relating to intangible assets with finite lives was $3.2 million for both the six months ended January 31, 2014 and 2013.

Operating Income. Operating income for the six months ended January 31, 2014 and 2013 was $21.3 million, or 12.6% of consolidated net sales, and $19.3 million, or 11.7% of consolidated net sales, respectively. Operating income for the six months ended January 31, 2014 and 2013 reflects a benefit of $0.2 million and a net benefit of $2.7 million, respectively (as discussed above in the selling, general and administrative expenses section). Excluding these amounts, operating income for the six months ended January 31, 2014 and 2013 would have been $21.1 million, or 12.5%, and $16.6 million, or 10.0%, of consolidated net sales, respectively.

The significant increase in operating income (both in dollars and as a percentage of consolidated net sales) is primarily due to higher consolidated net sales, changes in comparative sales mix, and lower operating expenses during the six months ended January 31, 2014 as compared to the six months ended January 31, 2013. Operating income, by segment, is discussed further below.

Operating income in our telecommunications transmission segment was $19.2 million, or 17.3% of related segment net sales, for the six months ended January 31, 2014, as compared to $17.8 million, or 18.0% of related segment net sales, for the six months ended January 31, 2013. Excluding the previously discussed changes in fair value of the Stampede contingent earn-out liability in both the six months ended January 31, 2014 and 2013, operating income was $19.0 million or 17.1% of related segment net sales and $14.5 million or 14.6% of related segment net sales, respectively. The increase in operating income, both in dollars and as a percentage of related segment net sales, is primarily due to the significant increase in this segment's net sales, resulting from increased sales of our over-the-horizon-microwave system products, and lower research and development expenses, partially offset by a significantly lower gross profit percentage, as previously discussed. Large fluctuations, in any given period, in over-the-horizon microwave system sales and production activities significantly impact our operating margins because this product line is supported by a relatively fixed cost structure. Given the expected lumpiness of over-the-horizon microwave system sales for the remainder of fiscal 2014, operating margins for this segment (both in dollars and as a percentage of related segment net sales), during the third quarter of fiscal 2014, are expected to significantly decline from the level we achieved in our most recent quarter and improve during the fourth quarter. However, based on our year-to-date performance and expected performance during the second half of fiscal 2014, we expect operating income in this segment in fiscal 2014 (both in dollars and as a percentage of related segment net sales) to be higher than the level we achieved in fiscal 2013.

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Our RF microwave amplifiers segment generated operating income of $1.7 million, or 4.0% of related segment net sales, for the six months ended January 31, 2014 as compared to $2.4 million, or 5.3% of related segment net sales, for the six months ended January 31, 2013. This decrease in operating income, both in dollars and as a percentage of related segment net sales, is primarily due to lower net sales, partially offset by lower research and development expenses, as discussed above. Based on the nature and type of orders that are currently in our backlog, anticipated orders we expect to receive, and anticipated research and development spending, we expect that operating income in this segment (both in dollars and as a percentage of related segment net sales) will improve from current levels during the second half of fiscal 2014 and will be higher in fiscal 2014 than the levels we achieved in fiscal 2013.

Our mobile data communications segment generated operating income of $7.4 million, or 47.1% of related segment net sales, for the six months ended January 31, 2014 as compared to $6.5 million, or 31.3% of related segment net sales, for the six months ended January 31, 2013. Excluding the $0.6 million net pre-tax restructuring charge associated with the wind-down of our microsatellite product line, operating income for the six months ended January 31, 2013 was $7.1 million or 34.1%. The increase in operating income, both in dollars and as a percentage of related segment net sales, was primarily driven by overall changes in this segment's sales mix (including the benefit of $2.0 million of high margin revenue related to the sale of certain SENS technology-based solutions), as discussed above. Given the expected level and composition of mobile data communications segment sales during the second half of fiscal 2014, operating income in this segment (both in dollars and a percentage of related segment net sales) is expected to decline from the level we achieved in our most recent quarter. However, based on our year-to-date performance and expected performance during the second half of fiscal 2014, we expect operating income in this segment (in dollars) for fiscal 2014 to be comparable to the level we achieved in fiscal 2013 and operating income in this segment (as a percentage of related segment net sales) to be higher than the level we achieved in fiscal 2013.

Unallocated operating expenses were $7.0 million for the six months ended January 31, 2014 as compared to $7.3 million for the six months ended January 31, 2013. The decrease is primarily attributable to various cost reduction actions we previously took, partially offset by an increase in amortization of stock-based compensation expense.

Amortization of stock-based compensation expense, which is included in unallocated operating expenses, was $2.0 million for the six months ended January 31, 2014 as compared to $1.6 million in the six months ended January 31, 2013, primarily due to changes in the timing of grants for certain stock-based awards (as discussed above in the selling, general and administrative expenses section).

Based on the level and composition of sales that we expect to achieve in fiscal 2014, we are targeting operating income, as a percentage of consolidated net sales, to be at least 11.0% in fiscal 2014. Given expected product mix changes and the expected lumpiness of our sales, we expect operating income, as a percentage of consolidated net sales, in the third quarter of fiscal 2014 to approximate 8.0% and to reach its peak for the year in the fourth quarter.

Interest Expense. Interest expense was $4.0 million and $4.1 million for the six months ended January 31, 2014 and 2013, respectively, and primarily reflects interest on our 3.0% convertible notes. Our Business Outlook for Fiscal 2014 assumes that our 3.0% convertible notes will be converted, redeemed or repurchased in May 2014. As such, we currently anticipate that interest expense in fiscal 2014 will be significantly lower than fiscal 2013.

Interest Income and Other. Interest income and other for the six months ended January 31, 2014 and 2013 was $0.5 million and $0.6 million, respectively. Interest income and other for both periods is primarily generated from interest earned on our cash and cash equivalents. All of our available cash and cash equivalents are currently invested in bank deposits, money market mutual funds, certificates of deposit, and short-term U.S. Treasury securities which, at this time, are currently yielding a blended annual interest rate of approximately 0.37%.

Provision for Income Taxes. The provision for income taxes was $6.5 million and $6.0 million for the six months ended January 31, 2014 and 2013, respectively. Our effective tax rate was 36.4% for the six months ended January 31, 2014, as compared to 37.8% for the six months ended January 31, 2013.

Our effective tax rate for the six months ended January 31, 2014 reflects a discrete tax benefit of less than $0.1 million. Our effective tax rate for the six months ended January 31, 2013 reflects a net discrete tax expense of approximately $0.4 million, principally related to the establishment of a valuation allowance on certain deferred tax assets of one of our foreign subsidiaries, offset, in part, by a discrete tax benefit related to the passage of legislation that included the retroactive extension of the federal research and experimentation credit from December 31, 2011 to December 31, 2013. Excluding these discrete tax items in both periods, our effective tax rate for the six months ended January 31, 2014 would have been 36.5% as compared to 35.5% for the six months ended January 31, 2013. The increase from 35.5% to 36.5% is principally attributable to the expiration of the federal research and experimentation credit on December 31, 2013, and expected product and geographical mix changes reflected in our fiscal 2014 business outlook.

Excluding the impact of any discrete tax items, our fiscal 2014 effective tax rate is expected to approximate 36.5%. This rate reflects the expiration of the federal research and experimentation credit on December 31, 2013.

Our federal income tax returns for fiscal 2010 through 2013 are subject to potential future IRS audit. Future tax assessments or settlements could have a material adverse effect on our consolidated results of operations and financial condition.

LIQUIDITY AND CAPITAL RESOURCES

Our unrestricted cash and cash equivalents decreased to $318.0 million at January 31, 2014 from $356.6 million at July 31, 2013, a decrease of $38.6 million. The decrease in cash and cash equivalents during the six months ended January 31, 2014 was driven by the following:

- Net cash provided by operating activities was $0.1 million for the six months ended January 31, 2014 as compared to $11.4 million for the six months ended January 31, 2013. The decrease was primarily attributable to a significant increase in net working capital requirements, most notably the timing of shipments and payments received from customers during the six months ended January 31, 2014 as compared to the six months ended January 31, 2013 and our overall performance on our large over-the-horizon microwave system contracts, including the timing of billing and commissions payments related to such contracts. Although we expect to generate significant positive net cash from operating activities for the remainder of fiscal 2014, we are unable to accurately predict the amount, which will be largely dependent on the impact of timing associated with our overall sales efforts, including our efforts related to both our $58.6 million and $57.4 million over-the-horizon microwave systems contracts.

- Net cash used in investing activities for the six months ended January 31, 2014 was $3.4 million as compared to $2.5 million for the six months ended January 31, 2013. Both of these amounts primarily represent expenditures relating to ongoing equipment upgrades and enhancements.

- Net cash used in financing activities was $35.3 million for the six months ended January 31, 2014 as compared to $23.9 million for the six months ended January 31, 2013. During the six months ended January 31, 2014, we spent $29.1 million for repurchases of our common stock and we paid $9.1 million in cash dividends to our stockholders. During the six months ended January 31, 2013, we spent $10.5 million for repurchases of our common stock and paid $14.3 million in cash dividends.

Our investment policy relating to our unrestricted cash and cash equivalents is intended to minimize principal loss while at the same time maximizing the income we receive without significantly increasing risk. To minimize risk, we generally invest our cash and cash equivalents in money market mutual funds (both government and commercial), certificates of deposit, bank deposits, and U.S. Treasury securities. Many of our money market mutual funds invest in direct obligations of the U.S. government, bank securities guaranteed by the Federal Deposit Insurance Corporation, certificates of deposit and commercial paper and other securities issued by other companies. While we cannot predict future market conditions or market liquidity or the ultimate outcome of the current European monetary issues and related concerns, we believe our investment policies are appropriate in the current environment. Ultimately, the availability of our cash and cash equivalents is dependent on a well-functioning liquid market.

As of January 31, 2014, our material short-term cash requirements primarily consist of cash necessary to fund: (i) our ongoing working capital needs, including income tax payments, (ii) accrued and anticipated quarterly dividends, and (iii) repurchases of our common stock that we may make pursuant to our stock repurchase program. Our material short-term cash requirements also include the possible use of cash to repay $200.0 million of our 3.0% convertible senior notes if we call the notes on or after May 5, 2014 or holders of the notes require us to repurchase some or all of the outstanding notes on May 1, 2014. In addition, we may also redeploy a portion of our cash and cash equivalents for one or more acquisitions.

During the six months ended January 31, 2014, we repurchased 935,992 shares of our common stock in open-market transactions with an average price per share of $31.10 and at an aggregate cost of $29.1 million (including transaction costs). During the six months ended January 31, 2013, we repurchased 397,798 shares of our common stock in open-market transactions with an average price per share of $26.34 and at an aggregate cost of $10.5 million (including transaction costs).

As of January 31, 2014, we were authorized to repurchase up to an additional $55.2 million of our common stock, pursuant to a $100.0 million stock repurchase program that was first authorized by our Board of Directors in December 2012 in the amount of $50.0 million and increased to $100.0 million effective December 9, 2013. Our stock repurchase program has no time restrictions and repurchases may be made in open-market or privately negotiated transactions and may be made pursuant to SEC Rule 10b5-1 trading plans. As of March 6, 2014, approximately $44.0 million remains available for repurchases of our common stock.

In December 2013, our Board of Directors increased our annual target dividend from $1.10 per common share to $1.20 per common share. During the six months ended January 31, 2014, our Board of Directors declared quarterly dividends of $0.275 per common share on October 3, 2013, totaling $4.5 million, and $0.30 per common share on December 9, 2013, totaling $4.7 million, which were paid on November 19, 2013 and February 19, 2014, respectively. On March 6, 2014, our Board of Directors declared a quarterly dividend of $0.30 per common share, payable on May 30, 2014 to shareholders of record at the close of business on May 7, 2014. This latest dividend declaration represents our fifteenth consecutive quarterly dividend. Future dividends are subject to Board approval.

Our material long-term cash requirements primarily consist of payments relating to our operating leases. In addition, we expect to make future cash payments of approximately $4.6 million related to our 2009 Radyne-related restructuring plan, including accreted interest. For further information regarding our Radyne restructuring plan, see "Notes to Condensed Consolidated Financial Statements – Note (9) Cost Reduction Actions - Radyne Acquisition-Related Restructuring Plan."

We have historically met both our short-term and long-term cash requirements with funds provided by a combination of cash and cash equivalent balances, cash generated from operating activities and cash generated from financing transactions.

In light of ongoing tight credit market conditions and overall adverse business conditions, we continue to receive requests from our customers for higher credit limits and longer payment terms. Because of our strong cash position and the nominal amount of interest we are earning on our cash and cash equivalents, we have, on a limited basis, approved certain customer requests. We continue to monitor our accounts receivable credit portfolio and have not had any material negative customer credit experiences to date.

Although it is difficult in the current economic and credit environment to predict the terms and conditions of financing that may be available in the future, should our short-term or long-term cash requirements increase beyond our current expectations, we believe that we would have sufficient access to credit from financial institutions and/or financing from public and private debt and equity markets.

The outcome of legal proceedings and investigations, as discussed in "Notes to Condensed Consolidated Financial Statements – Note (19) Legal Proceedings and Other Matters," is inherently difficult to predict and an adverse outcome in one or more matters could have a material adverse effect on our consolidated financial condition and results of operations.

Based on our anticipated level of future sales and operating income, we believe that our existing cash and cash equivalent balances and our cash generated from operating activities will be sufficient to meet both our currently anticipated short-term and long-term operating cash requirements.

We currently expect capital expenditures for fiscal 2014 to be approximately $5.0 million to $7.0 million.

FINANCING ARRANGEMENTS

In May 2009, we issued $200.0 million of our 3.0% convertible senior notes in a private offering pursuant to Rule 144A under the Securities Act of 1933, as amended. The net proceeds from this transaction were approximately $194.5 million after deducting the initial purchasers' discount and transaction costs. For further information, see "Notes to Condensed Consolidated Financial Statements – Note (11) 3.0% Convertible Senior Notes."

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We have a committed $100.0 million secured revolving credit facility ("Credit Facility") with a syndicate of bank lenders. The Credit Facility, as amended December 6, 2013, expires on October 31, 2014 but may be extended by us to December 31, 2016, subject to certain conditions relating primarily to the repurchase, redemption or conversion of our 3.0% convertible senior notes and compliance with all other Credit Facility covenants. The Credit Facility provides for the extension of credit to us in the form of revolving loans, including letters of credit, at any time and from time to time during its term, in an aggregate principal amount at any time outstanding not to exceed $100.0 million for both revolving loans and letters of credit, with sub-limits of $15.0 million for commercial letters of credit and $35.0 million for standby letters of credit. Subject to covenant limitations, the Credit Facility may be used for acquisitions, equity securities repurchases, dividends, working capital and other general corporate purposes. Since the inception of our Credit Facility in 2009, we have had no revolving loans under the Credit Facility. At January 31, 2014, we had $1.8 million of standby letters of credit outstanding related to our guarantees of future performance on certain customer contracts and no outstanding commercial letters of credit.

As amended December 6, 2013, the Credit Facility contains covenants, including covenants limiting certain debt, certain liens on assets, certain sales of assets and receivables, certain payments (including dividends), certain repurchases of equity securities, certain sale and leaseback transactions, certain guaranties, certain investments and certain minimum levels of cash and cash equivalents. Under certain conditions, the Credit Facility also contains financial condition covenants requiring that we (i) not exceed a maximum ratio of consolidated total indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (ii) not exceed a maximum ratio of consolidated senior secured indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (iii) maintain a minimum fixed charge ratio (as defined in the Credit Facility); (iv) maintain a minimum consolidated net worth; in each case measured on the last day of each fiscal quarter and (v) in the event total consolidated indebtedness (as defined in the Credit Facility) is less than $200.0 million, we must maintain a minimum level of Consolidated Adjusted EBITDA (as defined in the Credit Facility).

For additional information related to our Credit Facility, see “Notes to Condensed Consolidated Financial Statements - Note (10) Credit Facility.”

OFF-BALANCE SHEET ARRANGEMENTS

As of January 31, 2014, we did not have any off-balance sheet arrangements as defined in Item 303(a)(4) of Regulation S-K.

COMMITMENTS

In the normal course of business, we routinely enter into binding and non-binding purchase obligations primarily covering anticipated purchases of inventory and equipment. We do not expect that these commitments, as of January 31, 2014, will materially adversely affect our liquidity. At January 31, 2014, cash payments due under long-term obligations, excluding interest on our 3.0% convertible senior notes and purchase orders that we entered into in our normal course of business, are as follows:

	Obligations Due by Fiscal Years or Maturity Date (in thousands)				
	Total	Remainder of 2014	2015 and 2016	2017 and 2018	After 2018
Operating lease commitments	$25,036	3,181	11,102	7,418	3,335
3.0% convertible senior notes (see below)	200,000	—	—	—	200,000
Total contractual cash obligations	225,036	3,181	11,102	7,418	203,335
Less contractual sublease payments	(2,247)	(632)	(1,615)	—	—
Net contractual cash obligations	$222,789	2,549	9,487	7,418	203,335

As discussed further in “Notes to Condensed Consolidated Financial Statements – Note (11) 3.0% Convertible Senior Notes” on May 8, 2009, we issued $200.0 million of our 3.0% convertible senior notes. On or after May 5, 2014, we have the option to call the 3.0% convertible senior notes and are required to provide notice of our intent, a maximum 60 days in advance and a minimum 30 days in advance, to holders of the notes. Holders of the notes also have the right to require us to repurchase some or all of the outstanding notes, solely for cash, on May 1, 2014, May 1, 2019 and May 1, 2024 and upon certain events, including a change in control. As such, although these notes have a maturity date of May 1, 2029, it is possible that they will be redeemed or repurchased for cash in May 2014.

As discussed further in “Notes to Condensed Consolidated Financial Statements – Note (18) Stockholders’ Equity,” on March 6, 2014, our Board of Directors declared a quarterly dividend of $0.30 per common share, payable on May 30, 2014 to shareholders of record at the close of business on May 7, 2014. Future dividends are subject to Board approval. No dividend amounts are included in the above table.

At January 31, 2014, we have approximately $1.8 million of standby letters of credit outstanding under our Credit Facility related to the guarantee of future performance on certain contracts. Such amounts are not included in the above table.

In the ordinary course of business, we include indemnification provisions in certain of our customer contracts. Pursuant to these agreements, we have agreed to indemnify, hold harmless and reimburse the indemnified party for losses suffered or incurred by the indemnified party, including but not limited to losses related to third-party intellectual property claims. To date, there have not been any material costs or expenses incurred in connection with such indemnification clauses. Our insurance policies may not cover the cost of defending indemnification claims or providing indemnification. As a result, if a claim were asserted against us by any party that we have agreed to indemnify, we could incur future legal costs and damages.

We have change in control agreements and indemnification agreements with certain of our executive officers and certain key employees. All of these agreements may require payments by us, in certain circumstances, including, but not limited to, a change in control of our Company.

Pursuant to an indemnification agreement with our CEO (see Exhibit 10.1, "Form of Indemnification Agreement" in our Current Report on Form 8-K filed with the Securities and Exchange Commission ("SEC") on March 8, 2007), our Board of Directors agreed to pay, on behalf of our CEO, expenses incurred by him in connection with an investigation conducted by the SEC and an investigation by the United States Attorney for the Eastern District Court of New York, on the condition that Mr. Kornberg repay such amounts to the extent that it is ultimately determined that he is not entitled to be indemnified by us. To-date, legal expenses paid on behalf of our CEO have been nominal. We have incurred approximately $1.5 million of expenses (of which approximately $1.0 million was incurred in fiscal 2012 and approximately $0.5 million was incurred in fiscal 2013) responding to the subpoenas that are discussed in “Notes to Condensed Consolidated Financial Statements - Note (19) Legal Proceedings and Other Matters.” Any amounts that may be advanced to our CEO in the future are not included in the above table.

Our Condensed Consolidated Balance Sheet at January 31, 2014 includes total liabilities of $3.2 million for uncertain tax positions, including interest, all of which may result in cash payment. The future payments related to uncertain tax positions have not been presented in the table above due to the uncertainty of the amounts and timing of any potential cash settlement with the taxing authorities.

RECENT ACCOUNTING PRONOUNCEMENTS

We are required to prepare our consolidated financial statements in accordance with the Financial Accounting Standards Board's (“FASB”) Accounting Standards Codification (“ASC”) which is the source for all authoritative U.S. generally accepted accounting principles, which is commonly referred to as “GAAP.” The ASC is subject to updates by the FASB, which are known as Accounting Standards Updates (“ASUs”).

As further discussed in “Note (2) Adoption of Accounting Standards and Updates” included in “Part I — Item 1. — Notes to Condensed Consolidated Financial Statements," during the six months ended January 31, 2014, we adopted FASB ASU No. 2011-11, which requires entities to disclose both gross and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement. In addition, we also adopted ASU No. 2013-01, which clarifies that the scope of ASU No. 2011-11 applies to derivatives accounted for in accordance with Topic 815, "Derivatives and Hedging," including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset or subject to an enforceable master netting arrangement or similar arrangement. Our adoption of this ASU, as amended, did not have any impact on our consolidated financial statements.

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In addition, the following FASB ASUs have been issued and incorporated into the ASC and have not yet been adopted by us as of January 31, 2014:

- FASB ASU No. 2013-04, issued in February 2013, which provides guidance for the recognition, measurement and disclosure of obligations resulting from joint and several liability arrangements, for which the total amount of the obligation is fixed at the reporting date. Examples of obligations within the scope of this ASU include debt arrangements, settled litigation and judicial rulings and other contractual obligations. This ASU is effective no later than the first quarter of our fiscal 2015, and should be applied retrospectively to all prior periods presented, for those obligations that exist at the beginning of the fiscal year of adoption. We are currently evaluating if this ASU will have any potential impact on our consolidated financial statements and or disclosures.

- FASB ASU No. 2013-05, issued in March 2013, which requires a parent company, that ceases to have a controlling interest in a subsidiary or group of assets that is a non profit entity or business within a foreign entity, to release any cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. This ASU is effective in our first quarter of fiscal 2015 and should be applied prospectively. Early adoption is permitted. We do not believe that the adoption of this ASU will have any impact on our consolidated financial statements, as we currently do not have cumulative translation adjustments in our Condensed Consolidated Balance Sheet.

- FASB ASU No. 2013-07, issued in April 2013, which clarifies that an entity should apply the liquidation basis of accounting when liquidation is imminent, as defined. This ASU also provides principles for the recognition and measurement of assets and liabilities and requirements for financial statements prepared using the liquidation basis of accounting. This ASU is effective prospectively for entities that determine liquidation is imminent during annual reporting periods beginning after December 15, 2013 (our first quarter of fiscal 2015) and interim reporting periods therein. Early adoption is permitted. As we do not believe that liquidation is imminent, we do not believe that adoption of this ASU will have any impact on our consolidated financial statements.

- FASB ASU No. 2013-11, issued in July 2013, which amends the presentation requirements of ASC 740, "Income Taxes," and which generally requires that unrecognized tax benefits, or portions of unrecognized tax benefits, relating to a net operating loss carryforward, a similar tax loss, or a tax credit carryforward be presented in the financial statements as a reduction to the associated deferred tax asset. This ASU is effective in our first quarter of fiscal 2015 and should be applied prospectively to all unrecognized tax benefits that exist at the effective date. Early adoption and retrospective application are permitted. We are currently evaluating the impact of this ASU on our consolidated financial statements and related disclosures. As this ASU relates to presentation and disclosure only, we do not expect this ASU to impact our consolidated results of operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our earnings and cash flows are subject to fluctuations due to changes in interest rates primarily from our investment of available cash balances. Under our current policies, we do not use interest rate derivative instruments to manage exposure to interest rate changes.

As of January 31, 2014, we had unrestricted cash and cash equivalents of $318.0 million, which consisted of cash and highly-liquid money market mutual funds, certificates of deposit, bank deposits and U.S. Treasury securities. Many of these investments are subject to fluctuations in interest rates, which could impact our results. Based on our investment portfolio balance as of January 31, 2014, a hypothetical change in interest rates of 10% would have a $0.1 million impact on interest income over a one-year period. Ultimately, the availability of our cash and cash equivalents is dependent on a well-functioning liquid market.

Our 3.0% convertible senior notes bear a fixed rate of interest. As such, our earnings and cash flows are not sensitive to changes in interest rates on our long-term debt. As of January 31, 2014, we estimate the fair market value on our 3.0% convertible senior notes to be $206.8 million based on quoted market prices in an active market.

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Item 4. Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was carried out by us under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by the report to provide reasonable assurance that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. A system of controls, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the system of controls are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

There have been no changes in our internal controls over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

The certifications of our Chief Executive Officer and Chief Financial Officer, that are Exhibits 31.1 and 31.2, respectively, should be read in conjunction with the foregoing information for a more complete understanding of the references in those Exhibits to disclosure controls and procedures and internal control over financial reporting.

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PART II
OTHER INFORMATION

Item 1. Legal Proceedings

See “Notes to Condensed Consolidated Financial Statements - Note (19) Legal Proceedings and Other Matters,” in Part I, Item 1. of this Form 10-Q for information regarding legal proceedings and other matters.

Item 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in our Form 10-K for the fiscal year ended July 31, 2013.

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

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The number and average price of shares purchased during the six months ended January 31, 2014 are set forth in the table below:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as part of Publicly Announced Program	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program
August 1 – August 31, 2013	—	$—	—	$34,334,000
September 1 – September 30, 2013	—	—	—	34,334,000
October 1 – October 31, 2013	124,753	28.73	124,753	30,752,000
November 1 – November 30, 2013	258,887	30.85	258,887	22,771,000
December 1 – December 31, 2013	363,215	31.75	363,215	61,246,000
January 1 – January 31, 2014	189,137	31.74	189,137	55,247,000
Total	935,992	31.10	935,992	55,247,000

During the six months ended January 31, 2014, we repurchased 935,992 shares of our common stock in open-market transactions with an average price per share of $31.10 and at an aggregate cost of $29.1 million (including transaction costs). As of January 31, 2014, we were authorized to repurchase up to an additional $55.2 million of our common stock, pursuant to our existing $100.0 million stock repurchase program. Our stock repurchase program has no time restrictions and repurchases may be made in open-market or privately negotiated transactions and may be made pursuant to SEC Rule 10b5-1 trading plans. As of March 6, 2014, approximately $44.0 million remains available for repurchases of our common stock.

See “Notes to Condensed Consolidated Financial Statements - Note (10) Credit Facility,” in Part I, Item 1. of this Form 10-Q for a description of certain restrictions on equity security repurchases.

Item 4. Mine Safety Disclosures

Not applicable.

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Item 6. Exhibits

(a) Exhibits

Exhibit 31.1 - Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 31.2 - Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32.1 - Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 32.2 - Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 101.INS - XBRL Instance Document

Exhibit 101.SCH - XBRL Taxonomy Extension Schema Document

Exhibit 101.CAL - XBRL Taxonomy Extension Calculation Linkbase Document

Exhibit 101.LAB - XBRL Taxonomy Extension Labels Linkbase Document

Exhibit 101.PRE - XBRL Taxonomy Extension Presentation Linkbase Document

Exhibit 101.DEF - XBRL Taxonomy Extension Definition Linkbase Document

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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.

COMTECH TELECOMMUNICATIONS CORP.
(Registrant)

Date: March 6, 2014	By: /s/ Fred Kornberg Fred Kornberg Chairman of the Board Chief Executive Officer and President (Principal Executive Officer)
Date: March 6, 2014	By: /s/ Michael D. Porcelain Michael D. Porcelain Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)