1978 ANNUAL REPORT

COMTECH
Telecommunications Corp.

Photo courtesy of NASA

The Space Shuttle, shown above, is a strong contender as a replacement for the rocket as the launch vehicle for future communication satellites. In comparison, the shuttle will be able to place heavier payloads in orbit at significantly lower costs. Future satellites, free of the constraints in the size, shape, and weight imposed by the rocket, will have greater latitude in configuration, larger circuit capacity, and higher levels of transmission power. Among those planning to use the Shuttle in the near term are the International Telecommunications Satellite Organization for the launch of Intelsat V (shown right), and the Tracking and Data Relay Satellite System (TDRSS) which will provide satellites for communications to and from low-orbit space vehicles for NASA, as well as common carrier communications for Western Unions' Advanced Westar System.

Photo courtesy of Comsat

Financial Highlights*

	Fiscal Year Ended July 31, 1978	1977
Sales	$27,788,367	$19,042,473
Income From Continuing Operations	$ 1,356,275	$ 843,866
Earnings (Loss) Per Share:		
Continuing Operations	$ .76	$ .49
Discontinued Operation	(.12)	(.04)
Net Earnings Per Share	$ .64	$ .45
Book Value Per Share	$ 6.18	$ 5.50
Backlog	$34,650,000	$22,125,000

* Refer to the financial statements and accompanying notes for further information.
Book value is based on outstanding shares as of July 31, 1978 and 1977.

Cover

In March of 1978 Comtech was awarded a prime contract from the U.S. Army Materiel Readiness Command to supply 15 fixed site and 6 transportable AN/GSC-39 (V) Satellite Communication Terminals for use in the Department of Defense World Wide Satellite Communications Network. Both the transportable configuration (front cover) and the fixed site configuration, will employ Comtech designed communication equipment, including frequency conversion subsystems used extensively in previous programs such as the AN/MSC-46, AN/TSC-54, AN/FSC-78 and AN/FSC-79. The design and manufacture of these new terminals will be accomplished by Comtech under the auspices and direction of the U.S. Army Satellite Communication Agency.

COMTECH
Telecommunications Corp.

135 ENGINEERS ROAD • SMITHTOWN, NEW YORK 11787 • (516) 231-5454 • TWX: 510 227-6235

To Our Shareholders and Employees:

During fiscal 1978 we began to realize results from our ongoing and recently intensified capability and facility expansion program. Some of these results approached our expectations, others did not.

I am pleased to report that fiscal 1978 provided us with a record sales level of over $27.7 million, and a record year-end backlog of over $34.6 million. Comparatively, fiscal 1977's sales were approximately $19 million, and backlog, a previous record, was approximately $22 million.

Earnings for fiscal 1978 were $1,144,891 or 64¢ a share after a charge of $211,384 or $.12 a share resulting from a discontinued West Coast operation. This reflected an increase of about 42% per share over fiscal 1977's earnings which were $780,037 or $.45 a share after a $63,829 or $.04 a share charge related to the West Coast activity.

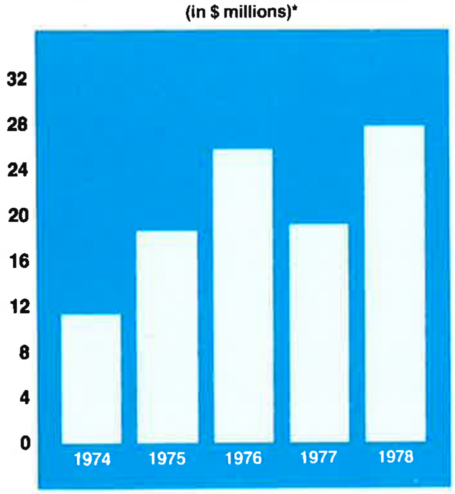
In March of 1978, Comtech was awarded a $46 million multi-year prime contract by the U.S. Army Materiel Readiness Command, of which approximately $21 million of the first years funding of $22 million is included in the year end backlog. This contract represented a significant event for our Company. To my mind, it clearly established Comtech as a viable contender for major prime contracts and demonstrated that our continuing expansion program has contributed to our objectives in this area. This contract also brings us closer to reestablishing a mix of approximately 50% U.S. Government and 50% Commercial business; a ratio we had maintained prior to a decline in Government business in recent years.

Our role as a direct supplier to the overseas international satellite and troposcatter markets also began to materialize in fiscal 1978. Although doing business abroad continues to involve extended lead times, our comparatively recent entry as a prime contractor in the foreign market achieved solid recognition for our Company. The experience we have gained in this market over the past two years has heightened our expectations for the future.

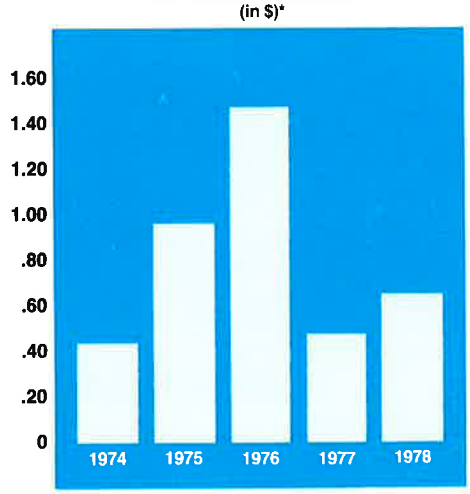
Comtech's largest overseas program to date has been a $19 million contract for a troposcatter communications network awarded in November 1976 by the Libyan Post and Telecommunications Corp. The system, which accounted for approximately 48% of net sales in fiscal 1978, has been installed and is in the final check out phases before turnover to our customer. In December, 1977, we were awarded a contract add-on of $7.8 million to extend the system to include additional Libyan cities.

The commercial domestic earth station market, which is a key part of our long-range growth expectations, has not yet moved from its present digestion stage to a new requirement level. Affected by excess capacity, this market continues to encounter delays in the planning and timing of contract awards. The industry hoped that the emergence of a new business-oriented common carrier such as SBS would lead to the type of fast-paced demand for earth stations experienced between 1974 and 1976. This IBM/Comsat/Aetna satellite venture, however, is currently embroiled in litigation relating to the initial FCC approval for SBS service. Although the outlook here is cloudy at the moment, and substantial delays are possible, we expect this system to go forward at some time and that despite our lack of success in the initial phase award made by SBS, this venture and others like it should be of importance to Comtech in the future.

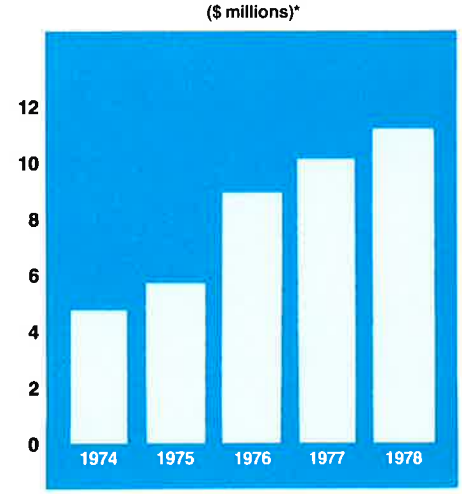
SALES AND OTHER INCOME
(in $ millions)*



EARNINGS PER SHARE
(in $)*



SHAREHOLDERS' EQUITY
($ millions)*



* Restated to reflect the acquisition of RF Systems, Inc., for the years 1974-1976.

In April 1978, Comtech Data Corporation was formed in Scottsdale, Arizona to address a segment of the digital communications market. At about the same time we discontinued operations of a West Coast subsidiary which was established in fiscal 1977 to focus on a different aspect of that market. The West Coast operation had not met the minimum milestones we considered indicative of a successful venture.

An important element in our plans for the future is the availability of resources to draw upon for working capital and letters of credit. In April 1978, to strengthen these resources, we arranged a $20 million line of credit with Chemical Bank and The Chase Manhattan Bank, N.A., the details of which are covered in the notes to the financial statements in this Report.

Basically, we are continuing along the lines charted earlier, and, in doing so, have reinforced our ability to compete and produce. Emphasis has been and will continue to be placed on maintaining pace if not leadership in communications technology; on enhancing our production capabilities; and on broadening the scope of our overall business activity. As we have stated in the past, our plans and their implementation are not directed solely to immediate profits, but rather to a combination of sustained and responsible earnings growth and longer-term expansion of business activity. Thus oriented, we consider after-tax profit margins in the 5 to 7% range as appropriate goals for Comtech. Among the factors that may affect these goals, however, is the impact during the early pre-fabrication phase, of the percentage of completion accounting method adopted for Comtech's multi-year U.S. Government contract.

We believe certain telecommunications markets will provide greater opportunities than others, and our strategy for the future is so directed. Through internal development, perhaps supplemented by selective, closely-related acquisitions that may become available, we intend to take advantage of opportunities within our current markets and their logical extensions. At the same time, we would consider augmenting our activities with less directly related operations that might benefit from the application of Comtech technology.

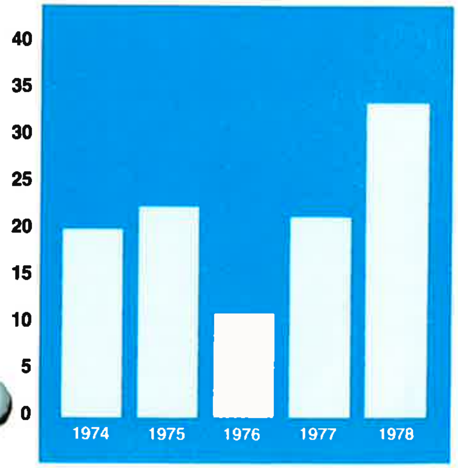
During fiscal 1979 we have been placing increasing emphasis on marketing, and intend to continue to do so. Plans for a major expansion of both international and domestic sales representation are well underway. We will continue emphasizing product improvement as well as new product development. We have not yet reached every goal we have set for ourselves. We want to make more progress. We want to do an even better job of getting to know our customers, potential customers, and their problems – and we will strive to become part of the solution.

Looking back over the substantial progress Comtech has made over the years, we take particular pride in the men and women who have turned many of our goals into realities. Our employees and their contributions represent the single most important asset Comtech possesses, and form the basis for our confidence in the future.

President and
Chairman of the Board

October 25, 1978

BACKLOG
(in $ millions)*



It is the policy of Comtech to provide equal opportunity to all employees and applicants for employment without regard to race, sex, religion, color, or national origin, and affirmative action is taken to ensure the implementation of this policy.

Highlights in the Company's History

In 1962, in response to President John F. Kennedy's proposal to create a global communications satellite system, Congress passed the Communications Satellite Act which, in turn, provided the impetus for the formation of the Communications Satellite Corporation (COMSAT). In 1965, COMSAT launched Intelsat I, the first commercial satellite dedicated to global communications. This was a major milestone in the creation of the satellite communications industry. The story of this industry is, in part, the story of Comtech.

Comtech was founded in August 1967 by a group of dedicated individuals who recognized a potentially strong demand for noise-free first stage amplifier systems in the receiving link of satellite comunication earth stations. The success of this initial line of low noise amplifiers, coupled with the phenomenal growth of satellite communications over the ensuing years, provided the resources from which the Company expanded its products, its technological base, and its facilities.

Early in Comtech's history, Management formed a disciplined business strategy with the objective of developing the Company into a broad-based communications equipment and systems supplier. Phase one of this strategy evolved from a concept of vertical integration – to build a Company capable of engineering, manufacturing, and integrating all of the vital electronic subsystems and components for turnkey communication systems in a developing satellite communication market. Phase two of this strategy evolved from a concept of horizontal integration – to assimilate the skills and resources necessary to provide products peripheral and complementary to the prime market of satellite communication earth stations.

The total communications equipment and systems business is estimated to be in the area of 30 billion dollars per year, with a significant portion of that market dominated by entrenched suppliers addressing the long established terrestrial components and systems markets. From the beginning, Comtech believed that satellite communications would be one of the markets offering substantially strong growth potential, and that the earth station segment of that market would offer the greatest leverage for new-entry, growth orientated companies.

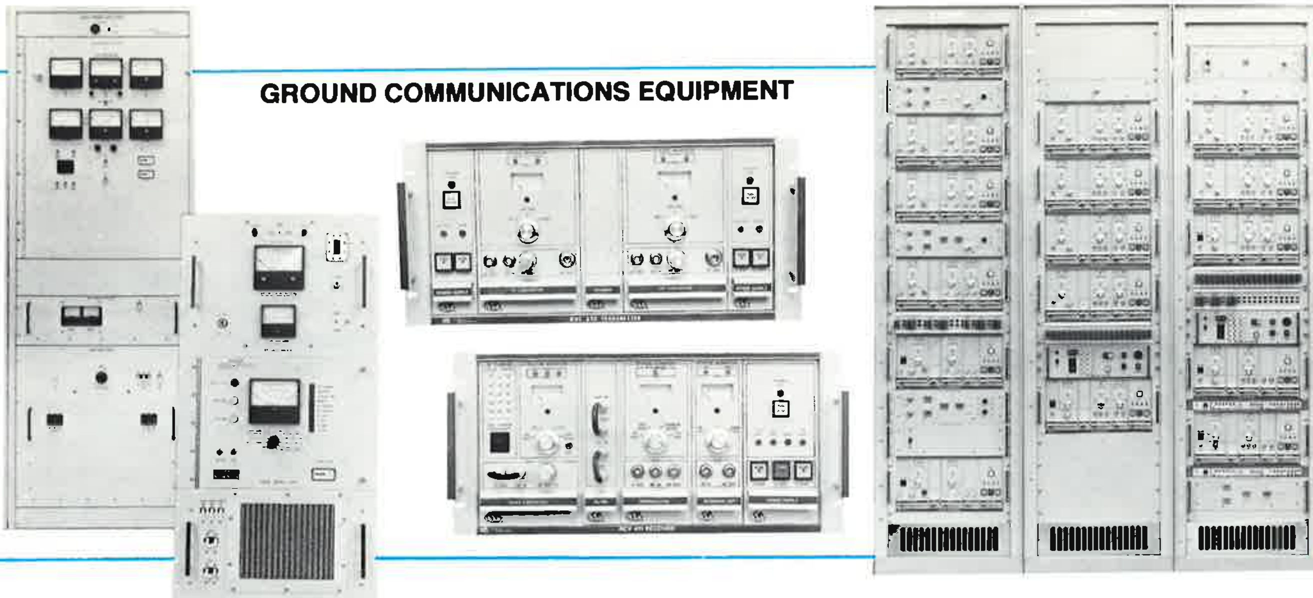
Comtech's first low noise parametric amplifier was designed and manufactured in a 6000 square-foot facility located in Plainview, New York. The initial product line was sold primarily to systems suppliers marketing to the member nations of Intelsat, a consortium formed to implement the global satellite communications system.

In 1970, the Company relocated into larger quarters in an industrial park located in Smithtown, New York. The new plant increased the production capabilities and provided space for the first major step in the Company's vertical integration plan; the design and development of a comprehensive line of receiving/transmitting subsystems and high power amplifiers. The new product line, commonly called ground communication equipment, gave Comtech the capability of manufacturing and supplying all of the major electronic equipment used in the satellite communication earth station. One of the earlier applications of this equipment was in an earth station used in conjunction with a weather satellite for the U.S. Department of Commerce.

By mid-1972, the Company's product line was receiving widespread industry interest. Low noise amplifiers had been installed in over 30 Intelsat earth stations; over 30 earth stations in the Canadian Domestic Satellite Communications System; and various military shipboard, airborne, and ground-based communication systems.

In March of 1972, the Company became a publicly held corporation which provided the capital needed to continue the product, facility, and capability expansion initiated over the preceding years. Consistent with this, the Company expanded its engineering and management staffs to include disciplines experienced in system installation, and the design of control, monitoring and interface equipment. These individuals formed the nucleus of Comtech's commercial systems capability and provided the next logical step in the vertical integration plan; the ability to design and install complete earth stations on a turnkey basis. At about the same time, the Company started to develop a line of digital baseband and processing equip-

LOW NOISE AMPLIFIERS



GROUND COMMUNICATIONS EQUIPMENT

ment. This type of equipment, being peripheral to the basic radio frequency product line, represented Comtech's initial step in the horizontal integration plan.

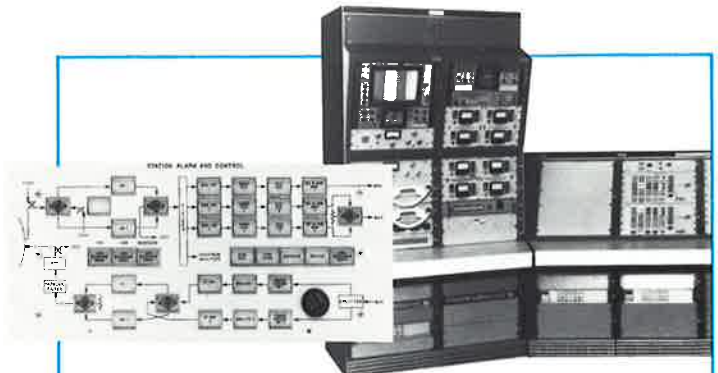
The effects of the Company's expanded technological base were positive. By mid-1973, Comtech had supplied turnkey earth stations for Intelsat sites in Alaska and Kwajalein Island, and had installed receiving and transmitting links in two earth stations located in China.

On the Government side, the Company installed a complete earth station near Washington, D.C. to provide digital communications at the military transmission frequencies, and delivered production quantities of Comtech designed frequency conversion subsystems to the U.S. Army. The performance of this equipment, initially used to upgrade the AN/MSC-46 Satellite Communications Terminals, led to the award of a subsequent contract to upgrade a similar military system, the AN/TSC-54.

In other areas, the Company supplied production quantities of low noise amplifiers for Intelsat stations deployed throughout the world, including the U.S., Canada, Taiwan, France, Spain, Nicaragua, Ecuador and Yugoslavia. Comtech's low noise amplifiers were also used in the "Hot Line" satellite link in both the U.S. and Moscow stations.

During 1974 and 1975, Comtech designed and installed over seven turnkey earth stations, three of which included tracking telemetry and command equipment used to support the launch and subsequent positioning of communication satellites. Transmit and receive subsystems were installed in domestic, international, and foreign domestic systems in the U.S., Panama, Canada, Norway, China, and offshore drilling platforms in the North Sea. Comtech's digital interface unit/processor was installed in a nationwide high-speed digital network, and single carrier per channel equipment was supplied to Comsat and to China for use in digital communication links via satellite. Low noise amplifiers were sold in production quantities for use in earth stations in the U.S., Great Britain, the Dominican Republic and Australia.

At this point in time, Comtech was firmly established as a leading supplier of technically advanced, highly reliable equipment and turnkey earth stations. By the end of 1976,



CONTROL, MONITORING AND INTERFACE EQUIPMENT

TURNKEY SATELLITE STATIONS

DIGITAL SYSTEMS

MILITARY SYSTEMS

the Company had provided equipment and systems for more than 100 earth stations in more than 80 countries in the Intelsat network, including the installation of new ground communication equipment into all existing U.S. based COMSAT stations.

On the domestic scene, the Company developed a strong position in the commercial market. All four U.S. domestic carriers, Western Union, ATT, American Satellite, and RCA incorporated equipment designed and manufactured by Comtech. All of the earth stations used in the initial RCA domestic system were supplied on a turnkey basis by Comtech.

Comtech's highly ruggedized frequency conversion subsystems continued to provide the main thrust in the U.S. Military market. The Company had received a contract to modify all previously delivered equipment with a capability to handle wide-band, high speed digital data as well as analog communications traffic. Additional subsystems incorporating this feature were delivered in production quantities for use in the AN/FSC-78 and AN/FSC-79 terminals. Today, there are over 500 of these subsystems in use in the Department of Defense Satellite Communications Network.

During 1976, the Company recognized a potential slow down in the demand for U.S. domestic earth stations. The situation was viewed as temporary, resulting from the rapid deployment of four separate U.S. carriers within the same time frame. To offset this, Comtech directed greater effort to the foreign domestic satellite markets, and implemented its plans to develop and market a line of troposcatter communications equipment and systems. The Company was successful with this equipment and was awarded a contract to manufacture and install a troposcatter communications network in Libya. In addition to diversifying the product base, this contract established Comtech as a viable prime contractor in the international marketplace.

The years 1977 and 1978 demonstrated Comtech's ability to adjust to both negative and positive factors in the business environment. During 1977, the Company acquired RF Systems Inc., currently located in St. Cloud, Florida; and formed Comtech Advanced Systems, Inc., in Sunnyvale, California.

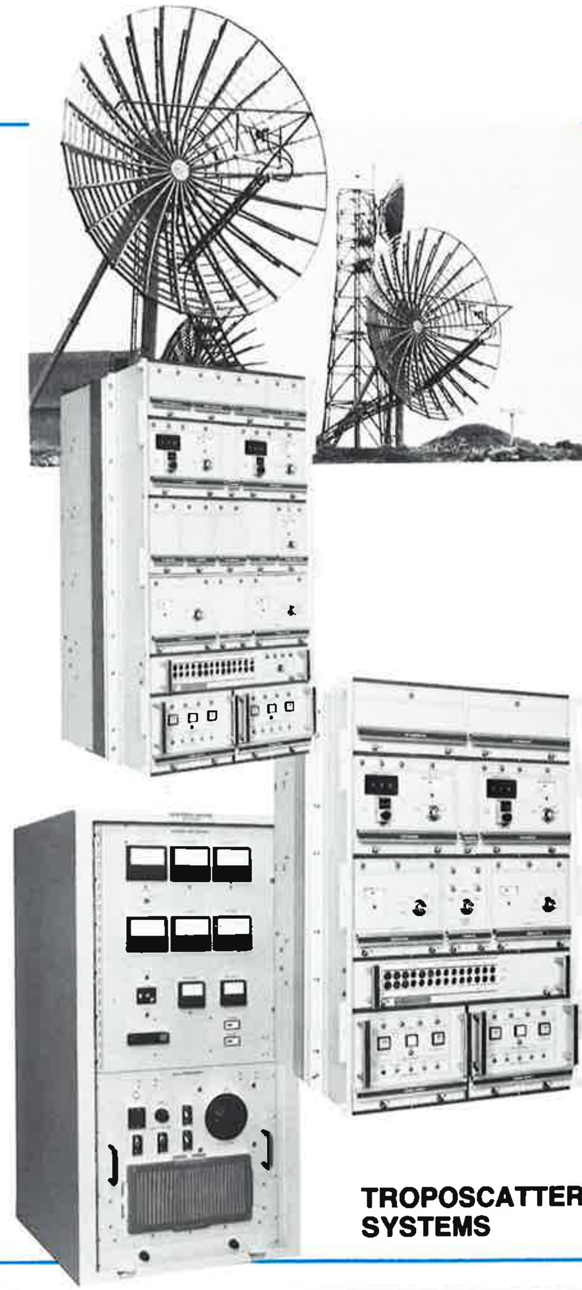
RF Systems brought to the Company an "in-house" capability for the manufacture of satellite and troposcatter antenna systems, a high-cost and major pacing item for turnkey installations. The acquisition of this subsidiary also provided entree into the cable television (CATV) earth station market. To date, the Company has installed approximately 100 of these receive-only earth stations for cable TV distribution.

Comtech Advanced Systems was created in response to what appeared to be an attractive opportunity to enter the Government intelligence equipment market. Results did not reach expectations and this operation was closed down coincidental with the formation of Comtech Data

Corporation in 1978. This new subsidiary, located in Scottsdale, Arizona, was chartered to develop and market digital equipment, primarily of the type required to condition digital signals for interface between satellite earth station transmission/reception equipment and existing land based systems/sources. All of Comtech's activities in this area were consolidated and assigned to Comtech Data Corporation upon its formation.

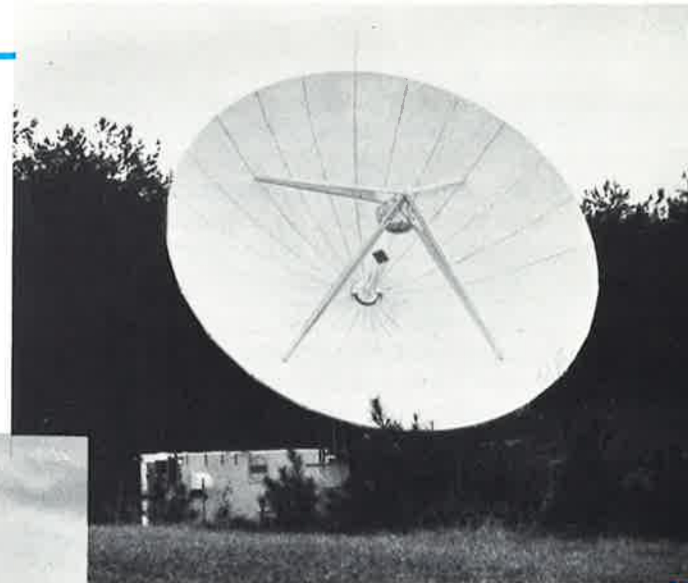
Toward the close of 1977, construction was completed on a new plant to provide for centralization and expansion of manufacturing operations in Smithtown. The construction of the new building proved to be a timely one. In early 1978, the Company was awarded a prime contract from the U.S. Army to supply transportable and fixed-site earth terminals for the Department of Defense Satellite Communications Network. This contract, which totals about 46 million dollars on a multi-year procurement, is the largest in the Company's history.

The year 1978, covered in detail in this annual report, has again demonstrated Comtech's ability to move aggressively and positively toward long-range goals. Today, the Company has over 450 employees and occupies a total of 226,000 square feet in facilities located in New York, Arizona, and Florida. Over the years, the Company's growth has been a consequence of several factors: the first is the rapid growth of the satellite communications industry; the second is the Company's ability to respond to technological and market changes through well defined objectives in product design, manufacturing, and management; and the third factor, but certainly not the least, is the continuing dedication and loyalty demonstrated by Comtech's employees.



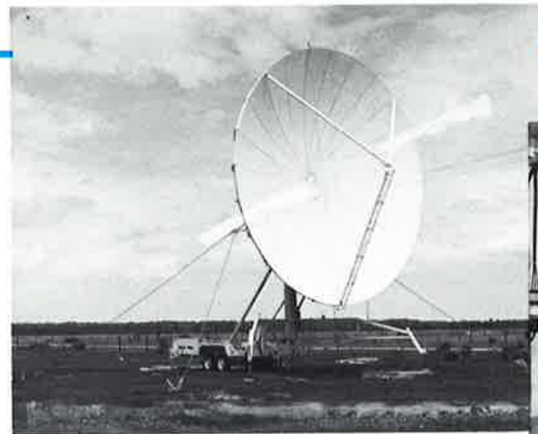
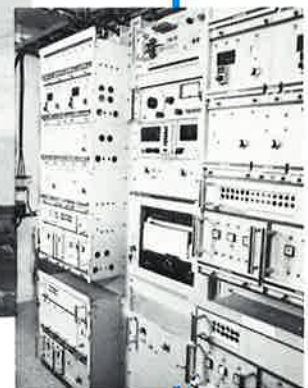
TROPOSCATTER SYSTEMS

ACCOMPLISHMENTS



TURNKEY
SATELLITE EARTH STATIONS

CATV
RECEIVE ONLY STATIONS

TROPOSCATTER SYSTEMS

DATA MODEMS

X-BAND TERMINAL


COMPUTER FACILITY AT SMITHTOWN

Consolidated Balance Sheets

ASSETS

	July 31, 1978	July 31, 1977
Current assets:		
Cash (Note 10)	$ 351,146	$ 384,204
U.S. treasury bills	–	395,167
Certificates of deposit (Note 13)	1,900,000	1,000,000
Accounts receivable (Notes 1 and 3)	5,481,836	5,285,291
Inventories (Notes 1 and 4)	3,274,657	3,524,549
Other current assets	123,920	83,688
	11,131,559	10,672,899
Property, plant and equipment less accumulated depreciation and amortization (Notes, 1, 5, 6 and 13)	6,798,410	3,704,669
Non-current receivables (Note 3)	265,415	–
Other assets	40,283	68,925
	$18,235,667	$14,446,493

LIABILITIES AND SHAREHOLDERS' EQUITY

	1978	1977
Current liabilities:		
Notes payable (Note 10)	$1,704,000	$ –
Accounts payable	1,117,830	2,475,580
Accrued expenses and taxes withheld	1,112,189	1,031,821
Income taxes currently payable (receivable) (Notes 1 and 7)	(149,335)	(125,103)
Advance contract payments received	193,091	591,023
Current maturities of mortgage notes	86,000	58,000
	4,063,775	4,031,321
Mortgage notes due after one year (Note 6)	2,803,225	601,599
Deferred income taxes (Notes 1 and 7)	668,300	308,300
Shareholders' equity (Notes 2, 8 and 9):		
Common stock, $.10 par value:		
Authorized – 3,000,000 shares		
Outstanding – 1978 – 1,730,373		
1977 – 1,728,703	173,037	172,870
Additional paid-in capital	2,853,033	2,802,997
Retained earnings	7,674,297	6,529,406
	10,700,367	9,505,273
Commitments and contingencies (Note 13)		
	$18,235,667	$14,446,493

The accompanying Notes to Financial Statements are an integral part of these statements.

Consolidated Statements of Income and Retained Earnings

	Year ended July 31, 1978	1977
Net sales	$27,788,367	$19,042,473
Costs and expenses:		
Cost of sales	21,961,682	14,328,056
Selling, general and administrative	2,983,985	2,564,604
Depreciation and amortization	510,557	435,210
Interest	170,868	80,737
	25,627,092	17,408,607
Income from continuing operations before income taxes	2,161,275	1,633,866
Provision for income taxes (Note 7)	805,000	790,000
Income from continuing operations	1,356,275	843,866
Loss from operation of discontinued subsidiary, net of income tax benefit of $200,000 – 1978; $70,000 – 1977 (Note 12)	(211,384)	(63,829)
Net Income	1,144,891	780,037
Retained earnings at beginning of year	6,529,406	5,749,369
Retained earnings at end of year	$ 7,674,297	$ 6,529,406
Earnings (loss) per share (Note 1):		
Continuing operations	$ .76	$ .49
Discontinued operation	(.12)	(.04)
Net earnings per share	$ .64	$ .45

The accompanying Notes to Financial Statements are an integral part of these statements.

Consolidated Statements of Changes in Financial Position

	Year ended July 31, 1978	1977
Financial resources were provided by:		
Continuing Operations:		
Net income from continuing operations	$1,356,275	$843,866
Add (deduct) income charges not affecting working capital:		
Depreciation and amortization	510,557	435,278
Deferred income taxes	360,000	(173,000)
Total from continuing operations	2,226,832	1,106,144
Discontinued operations:		
Loss from discontinued operation	(211,384)	(63,829)
Depreciation	13,515	–
Total from operations	2,028,963	1,042,315
Net proceeds from exercise of stock options and warrants	28,995	6,214
Stock issued in connection with the organization of a subsidiary	52,289	31,276
Stock cancelled upon dissolution of subsidiary	(31,081)	–
Tax benefit from disqualifiying disposition of stock option	–	23,000
Retirement of fixed assets, net	71,834	51,672
Increase in long-term debt	2,291,648	–
	4,442,648	1,154,477
Financial resources were used for:		
Purchase of building and equipment	3,689,647	742,631
Reduction in long-term debt	90,022	263,278
Other	236,773	(35,506)
	4,016,442	970,403
Increase in working capital	$ 426,206	$ 184,074

The accompanying Notes to Financial Statements are an integral part of these statements.

Analysis of changes in working capital

	Year ended July 31, 1978	1977
Increases (decreases) in current assets:		
Cash	($ 33,058)	($ 423,169)
U.S. treasury bills	(395,167)	395,167
Certificates of deposit	900,000	1,000,000
Accounts receivable	196,545	2,590,155
Inventories	(249,892)	(2,686,876)
Other current assets	40,232	27,153
	458,660	902,430
(Increases) decreases in current liabilities:		
Notes payable	(1,704,000)	–
Accounts payable	1,357,750	(1,146,604)
Accrued expenses and taxes withheld	(80,368)	37,629
Income taxes currently payable	24,232	972,392
Advance contract payments received	397,932	(591,023)
Current maturities of mortgage notes	(28,000)	9,250
	(32,454)	(718,356)
Increase in working capital	$ 426,206	$ 184,074

The accompanying Notes to Financial Statements are an integral part of these statements.

Notes to Consolidated Financial Statements

NOTE 1 – ACCOUNTING POLICIES:

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions have been eliminated.

Contract Accounting: –

Sales Recognition:

Sales are generally recorded under the unit of delivery method of accounting except for a large multi-year funded military program which utilizes the percentage of completion method of accounting. Progress payment retainage and estimated earnings are reflected as unbilled receivables.

Costs and Expenses:

Cost of sales is based upon the actual contract costs incurred and, in the case of partial shipments, estimated final contract costs. Contract costs include material, direct labor, manufacturing overhead and certain selling and finance costs associated with contracts. All other selling, general and administrative expenses are charged to operations as incurred. Under all contracts, when estimates indicate a probable future loss, an immediate provision for the full amount thereof is charged to cost of sales.

Inventories

Raw materials and components are stated at first-in, first-out cost, which is not in excess of market. Work in process is valued at the total material, direct labor, manufacturing overhead and other costs incurred under each contract, less estimated cost of sales.

Property, Plant and Equipment

Property, plant and equipment (including major renewals and betterments) are recorded at cost; expenditures for maintenance and repairs are charged to operations as incurred. At the time property is retired or otherwise disposed of, the cost and accumulated depreciation or amortization of such property is eliminated and the gain or loss on disposition is reflected in operations. Annual depreciation is provided utilizing the straight-line method over the estimated useful life of the asset.

Research and Development Costs

The Company charges research and product development costs to operations as incurred except where such costs are reimbursable under customer-funded contracts. Research and development costs not relating to customer-funded contracts amounted to $296,992 in 1978 and $474,173 in 1977.

Income Taxes

The Company provides deferred income tax expense (credits) for transactions reported in different periods for financial and income tax reporting purposes. Investment tax credits are accounted for as a reduction of income taxes in the year the related asset is placed in service.

Income taxes have not been provided on the undistributed earnings (cumulatively $1,479,000) of the Company's Domestic International Sales Corporation (DISC) subsidiary since the Company intends to permanently reinvest these earnings in export related activities.

Earnings Per Share

Earnings per share is based upon the weighted average common shares and common share equivalents outstanding during the year. The number of common shares and common share equivalents used in computing earnings per share were 1,781,042 and 1,740,635 in 1978 and 1977, respectively. The effect of full dilution is immaterial.

Retroactive effect has been given to the shares issued in connection with the acquisition of R. F. Systems, Inc.

NOTE 2 – SUBSIDIARIES:

In March 1978, the Company entered into agreements with a group of individuals and established Comtech Data Corporation, a digital communications subsidiary. Under the agreements the Company sold to these individuals 5,000 shares of common stock at par value ($.10 par value) and will sell to these individuals up to 90,000 shares of common stock at par value upon the achievement of earnings levels defined in the agreements.

The greater of the excess of market value over the proceeds received for such shares on the date of the agreement or upon the achievement of the earnings milestone will be charged to compensation expense over the estimated period of earnings achievement. This expense was approximately $52,000 in 1978.

In February 1977, the Company exchanged approximately 51,000 shares of unregistered and previously unissued common stock for all the outstanding shares of R.F. Systems, Inc., and subsidiaries, an antenna manufacturer. This exchange resulted in a combination which has been accounted for as a pooling of interests, and the effect of financial statement adjustments resulting therefrom, have been previously reported.

NOTE 3 – ACCOUNTS RECEIVABLE:

	July 31, 1978	July 31, 1977
Amounts receivable from the United States Government ..	$1,486,404	$ 244,576
Unbilled costs and accrued profits on government contracts in progress	183,203	–
Amounts receivable from others	4,077,644	5,040,715
	5,747,251	5,285,291
Less: Unbilled costs and other amounts receivable in excess of one year	265,415	–
	$5,481,836	$5,285,291

NOTE 4 – INVENTORIES:

	July 31, 1978	July 31, 1977
Raw materials and components	$1,159,758	$1,217,374
Work in process	2,876,312	5,902,604
	4,036,070	7,119,978
Less – progress payments	761,413	3,595,429
	$3,274,657	$3,524,549

Work in process relating to contracts is expected to be delivered over a period of less than twelve months. Approximately 72% in 1978 and 84% in 1977 of the Company's work in process represents work performed pursuant to contracts. The remainder represents parts and components being manufactured for stock.

Title to work in process is vested in the customer on contracts which provide for progress, partial, or advance payments to the extent of such payments received.

During 1978 and 1977, the Company included in work in process inventory certain selling and finance expenses of $916,000 and $1,078,000, respectively, which are associated with a particular contract. At July 31, 1978 and 1977, approximately $95,000 and $706,000, respectively, of these specific expenses remain in work in process inventory.

NOTE 5 – PROPERTY, PLANT AND EQUIPMENT:

	Estimated Useful Lives	July 31, 1978	July 31, 1977
Land	–	$ 840,728	$ 190,728
Building	40 years	3,818,475	1,356,108
Leasehold Improvements ..	Lease Term	286,339	275,099
Equipment	3-8 years	4,048,394	3,571,318
		8,993,936	5,393,253
Less–accumulated depreciation and amortization ...		2,195,526	1,688,584
		$6,798,410	$3,704,669

NOTE 6 – MORTGAGE NOTES:

	July 31, 1978	July 31, 1977
9.4% First mortgage indebtedness to a bank payable monthly, maturing in 1980	$458,912	$471,594
6.5% Second mortgage indebtedness to the New York State Job Development Authority payable monthly, maturing in 1981	142,313	188,005
9% First Mortgage indebtedness to a bank payable monthly, maturing in 1983	360,852	–
9.5% First Mortgage indebtedness to an insurance company payable monthly, maturing in 1992 (Note 13)	1,927,148	–
	2,889,225	659,599
Less – portion due within one year	86,000	58,000
	$2,803,225	$601,599

The 9% First Mortgage agreement contains an option to refinance the balance, approximately $321,000 at the completion of the initial term, for three successive five year periods at the initial interest rate.

At July 31, 1978 the aggregate principal amount maturing annually during each of the the four fiscal years ending July 1983 is as follows: 1980 – $523,000; 1981 – $67,000; 1982 – $35,000; 1983 – $35,000. These mortgages are secured by the land and building referred to in Note 5.

NOTE 7 – INCOME TAXES:

The provisions for income taxes for the years ended July 31, 1978 and 1977 were as follows:

	July 31, 1978	July 31, 1977
Current:		
Federal	$ 100,000	$ 698,000
State	145,000	195,000
Deferred	360,000	(173,000)
Total	$ 605,000	$ 720,000

The tax provision as of July 31, 1978 and 1977 are net of tax benefit on loss of discontinued operations of $200,000 and $70,000, respectively.

In 1978, the Company applied for permission from the Internal Revenue Service to change its method of income recognition for tax reporting purposes to the "Completed Contract Method" effective with the Company's taxable year ended July 31, 1978. In the event that this request is approved, Company's management estimates that it will receive an additional refund of taxes paid in prior periods of approximately $2,000,000, which will be repaid in future periods as the Company's long-term contracts are completed.

The following tabulation sets forth the difference between the statutory and effective income tax rates for the years ended July 31, 1978 and 1977.

	July 31, 1978	July 31, 1977
Federal statutory income tax rate	48%	48%
State income taxes, net of federal tax benefit	5	4
Tax exempt DISC income	(15)	–
Investment credit	(3)	(4)
Effective income tax rate	35%	48%

NOTE 8 – SHAREHOLDERS' EQUITY:

Changes in Shareholders' Equity during the years ended July 31, 1978 and 1977 are as follows:

	No. of Shares	Common Stock	Additional Paid-in Capital	Retained Earnings
Balance July 31, 1976	1,716,303	$171,630	$2,743,747	$5,749,369
Exercise of stock options	2,400	240	5,974	–
Net income for the period	–	–	–	780,037
Shares issued in connection with the organization of a subsidiary	10,000	1,000	30,276	–
Tax benefit resulting from disqualifying disposition by employees of stock purchased under stock option plans	–	–	23,000	–
Balance July 31, 1977	1,728,703	172,870	2,802,997	6,529,406
Exercise of stock options and warrants	4,720	472	28,523	–
Net income for the period	–	–	–	1,144,891
Shares issued in connection with organization of a subsidiary	5,000	500	51,789	–
Shares repurchased and retired in connection with the dissolution of Comtech Advanced Systems, Inc.	(8,050)	(805)	(30,276)	–
Balance July 31, 1978	1,730,373	$173,037	$2,853,033	$7,674,297

NOTE 9 – STOCK OPTION PLANS:

Options to purchase common stock of the Company have been granted under various plans to officers and other key employees. Options granted under the Company's 1970 qualified option plan are at prices equal to the fair market value of such stock on the date of grant and are exercisable over a period of not more than five years. Options granted under the Company's 1976 Incentive Stock Option Plan are at prices which may not be less than 85% of the fair market value of such stock on the date of grant and are exercisable over a period determined by the Board of Directors at the time of grant.

In December 1977, the shareholders approved the Company's Incentive Warrant Plan for directors of the Company who are neither officers nor employees of the Company or its subsidiaries. Under the plan, a maximum of 25,000 shares of common stock were available for grant under provisions to be established at the discretion of a committee of the Board of Directors. Warrants which have been granted under the plan become exercisable over a period of ten years and are limited to a maximum of 3,750 shares for each qualified director.

NOTE 9 - STOCK OPTION PLANS (con't)

The following tabulation sets forth the activity in stock options and warrants for the years ended July 31, 1978 and 1977.

	July 31, 1978		July 31, 1977	
	Number of Shares	Option Price Per Share	Number of Shares	Option Price Per Share
Qualified stock options:				
Outstanding, beginning of the year	36,050	$4.25-18.13	72,450	$1.25-18.13
Granted	52,000	6.50-12.63	20,500	6.50
Exercised	(3,300)	4.25- 7.50	(2,400)	1.25- 9.88
Cancelled	(19,450)	4.25-18.13	(54,500)	1.25-24.75
Outstanding, end of year	65,300	5.50-12.63	36,050	4.25-18.13
Incentive stock options:				
Outstanding, beginning of year	108,600	$5.53	–	–
Granted	5,000	11.38	108,600	5.53
Exercised	(1,170)	5.53	–	
Cancelled	(8,900)	5.53	–	
Outstanding, end of year	103,530	5.53-11.38	108,600	5.53
Incentive warrants:				
Outstanding, beginning of the year	7,500	6.50	–	
Granted	7,500	6.50- 7.75	7,500	6.50
Exercised	(250)	6.50	–	
Outstanding, end of year	14,750	6.50- 7.75	7,500	6.50
Total options and warrants outstanding, end of year	183,580	$5.50-12.63	152,150	$4.25-18.13
Exercisable, end of year	93,220	$5.53- 9.25	89,220	$4.25-18.13

At July 31, 1978 and 1977, 52,050 and 100,500 shares, respectively, were available for grant under the stock option plan and 10,000 shares under the incentive warrant plan.

In connection with options issued under the 1976 Incentive Stock Option Plan, the difference between the option price and the fair market value on the date of grant is compensation expense and is charged to operations over the period during which the options become exercisable. There was no compensation expense in 1978 and $71,000 during 1977.

In October 1978, the Board of Directors adopted amendments to the Company's 1976 Incentive Stock Option Plan, subject to shareholder approval. The amendments increase the number of shares available for future grants under the plan by 150,000 and authorize the grant of stock appreciation rights ("SARs"), which will be related to options previously or subsequently granted under the plan. The SARs, in general, would entitle the optionee to receive upon exercise cash, shares of Common Stock of the Company, or a combination of both (as determined by the Committee administering the plan) equal to the difference between the exercise price of the related option and the market price of the Company's stock on the date of exercise of the SAR. Upon exercise of the SARs, the related options must be surrendered.

NOTE 10 – LINES OF CREDIT:

The Company has agreements with two banks which provide credit lines for working capital and letters of credit of $20,000,000. Of this amount, a maximum of $14,000,000 is available for working capital and a minimum of $6,000,000 is available for letter of credit financing. The interest rate to be charged varies according to each banking agreement, and ranges from the prevailing prime rate to 1/2% over such rate depending upon the individual bank and cumulative bank debt. One bank requires average compensating balances of $300,000 plus 10% of any outstanding borrowings.

Borrowings under these arrangements averaged $1,236,000 during 1978 at an average interest rate of 8.4%. During 1977 the Company borrowed a maximum of $600,000 for a period of two months at a rate of 6¾%. Borrowings outstanding at July 31, 1978 were $1,050,000.

NOTE 11 – PROFIT SHARING AND INCENTIVE COMPENSATION PLANS:

The Company has a profit sharing plan covering all eligible employees. The plan, which has been approved by the IRS, provides for the Company to contribute such amounts as the Board of Directors determines. During the years ended July 31, 1978 and 1977, the Board approved contributions of $100,000 which were charged to income.

The Company has an incentive compensation plan for officers and other key employees. Under the plan, an amount equal to 5% of income before income taxes without taking into consideration extraordinary items and before amounts allocated thereunder is payable to selected key employees of the Company. A provision of $87,500 and $83,000 was charged against income in fiscal 1978 and 1977, respectively.

NOTE 12 – DISCONTINUED OPERATION:

In April 1978, the Company discontinued operations of its wholly owned subsidiary, Comtech Advanced Systems, Inc. and terminated agreements with a group of individuals. The subsidiary, which started operations in April 1977, had sales in fiscal 1978 of $53,000 and losses from operations in 1978 and 1977, net of applicable income taxes, of approximately $211,000 and $64,000, respectively. In management's opinion a future loss (if any) on the disposal of the subsidiary will be immaterial.

NOTE 13 – COMMITMENTS AND CONTINGENCIES:

The Company had leased a new manufacturing facility under a 20 year agreement with annual rentals of approximately $277,000 plus property taxes and other specific costs and the agreement included an option to purchase the facility. On July 25, 1978, the Board of Directors approved the purchase of the facility. This option to purchase was exercised in August 1978 and title conveyed on September 29, 1978. The purchase price ($2,627,000) has been reflected in the financial statements as of July 31, 1978.

Certain sales of the Company are subject to the Renegotiation Act of 1951, as amended. Clearance has been received through fiscal year 1974. In the opinion of management, no refunds are anticipated for sales subject to renegotiation.

In connection with a contract, as amended, for $26,700,000, the Company was required to establish customary standby letters of credit for 20% of the contract value (which represents an amount equal to the down payment received under the contract). Under the terms of the contract, the letter of credit for the advance payment is reduced as shipments are made against the contract. As of July 31, 1978 and 1977, such reductions amounted to approximately $3,170,000 and $700,000, respectively. In addition, the Company is required to establish performance guarantees of approximately $3,400,000.

In connection with issuance of the initial standby letters of credit, the Company agreed in April 1977, to secure $1,900,000, the initial performance guarantee by March 1978, and in the event of default thereunder, the Company would, upon request, grant the bank a security interest in its assets. At July, 1978, the Company had secured the performances guarantee with $1,900,000 of Certificates of Deposit. In August, 1978, the Company was released from all requirements under the agreement.

NOTE 14 – QUARTERLY DATA (UNAUDITED):

Quarter	Net Sales	Gross Profit	Net Income (Loss)	Earnings (Loss) Per Share
Fiscal 1978				
First	$ 4,494,743	$1,127,421	$ 41,082	$.02
Second .	10,662,954	2,042,018	530,800	.30
Third	5,725,410	1,199,118	205,609	.12
Fourth ..	6,905,260	1,458,128	367,400	.20
Fiscal 1977				
First	5,215,994	1,670,380	496,584	.29
Second .	4,221,122	946,325	158,534	.09
Third	3,399,231	207,246	(276,073)	(.16)
Fourth ..	6,206,400	1,807,131	400,992	.23

NOTE 15 – SEGMENT INFORMATION:

For the purpose of segment reporting, management considers the Company to operate in one industry, the Communications Equipment Industry.

During the fiscal years ended July 31, 1978 and 1977, approximately 16% and 27%, respectively, of the Company's revenues resulted from contracts with U.S. Government agencies and prime contractors and approximately 57% and 28%, respectively, resulted from export sales. Sales to Libya accounted for approximately 48% in 1978 and 19% in 1977 of the Company's revenues.

Report of Independent Accountants

To the Board of Directors and Shareholders of
Comtech Telecommunications Corp.

We have examined the consolidated balance sheets of Comtech Telecommunications Corp. (a New York Corporation) and subsidiaries as of July 31, 1978 and July 31, 1977, and the related consolidated statements of income and retained earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Comtech Telecommunications Corp. and subsidiaries as of July 31, 1978 and July 31, 1977, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the years.

ARTHUR ANDERSEN & CO.

Huntington, N.Y.
October 5, 1978

Five-Year Summary of Operations

	Year Ended July 31,				
	1974 (A)	1975 (A)	1976 (A)	1977	1978
Net sales and other income	$11,284,377	$18,399,784	$25,492,915	$19,042,473	$27,788,367
Costs and expenses:					
Cost of sales	8,723,722	13,722,678	18,095,121	14,328,056	21,961,682
Selling, general and administrative	893,002	1,169,838	1,983,210	2,564,604	2,983,985
Depreciation and amortization	223,351	314,350	403,509	435,210	510,557
Interest	135,510	158,385	92,027	80,737	170,868
	9,975,585	15,365,251	20,573,867	17,408,607	25,627,092
Income from continuing operations before income taxes	1,308,792	3,034,533	4,919,048	1,633,866	2,161,275
Provision for income taxes (B)	591,925	1,439,075	2,426,500	790,000	805,000
Income from continuing operations	716,867	1,595,458	2,492,548	843,866	1,356,275
Loss from operation of discontinued subsidiary, net of income tax benefit of $200,000 in 1978; $70,000 in 1977 (C)	–	–	–	(63,829)	(211,384)
Net income	$ 716,867	$ 1,595,458	$ 2,492,548	$ 780,037	$ 1,144,891
Earning (loss) per share (D):					
Continuing Operations	$ .43	$ .95	$1.45	$ .49	$ .76
Discontinued Operations	–	–	–	(.04)	(.12)
Net Earnings Per Share	$ .43	$ .95	$1.45	$ .45	$ .64
Average common shares and common share equivalents	1,679,384	1,680,323	1,714,712	1,740,635	1,781,042

(A) Restated to reflect the acquisition of R.F. Systems, Inc. which has been accounted for as a pooling of interests.
(B) See Note 7 of the Notes to Consolidated Financial Statements.
(C) See Note 12 of the Notes to Consolidated Financial Statements.
(D) Earning per share is based upon the weighted average, common shares and common share equivalents outstanding during the year. Retroactive effect has been given to the shares issued in connection with the acquisition of R.F. Systems, Inc. The effect of full dilution is immaterial.

Management Discussion and Analysis of Summary of Operations

Sales

During the fiscal year 1978 as compared to 1977, sales increased by approximately 46%. This increase is principally due to a higher level of deliveries on a major contract with the PTC of Libya. Sales for the fiscal year 1977 as compared to 1976 decreased by approximately 25%. This decrease was attributable to previous reductions in backlog and the delivery schedules on major contracts.

Costs and Expenses

Cost of sales as a percentage of sales for fiscal 1978 compared to 1977 increased by approximately 4%. Cost of sales for fiscal 1977 compared to 1976 increased by approximately 4%. These increases principally reflected changes in the mix of sales which generated lower profit margins and for 1977, start-up expenses associated with a new facility and comparatively higher research and development cost.

Selling, general and administrative expenses in fiscal 1978 compared to 1977 and 1977 compared to 1976 increased by approximately 16% and 29%, respectively. These increases are attributable to marketing expenses, increased salaries and related fringe benefits.

Depreciation and amortization in fiscal 1978 as compared to 1977, and 1977 compared to 1976 increased by 17% and 8%, respectively, due to the addition of new equipment.

Interest expense in fiscal 1978 as compared to 1977 increased reflecting increased borrowings and higher interest rates.

Income taxes

The effective income tax rate for fiscal 1978 was 35% as compared to 48% in fiscal 1977. This decrease is attributable to a higher level of qualifying export sales of the Company's Domestic International Sales Corporation (DISC) subsidiary, a portion of which income is permanently reinvested in export related activities resulting in permanent tax deferral.

Stock Prices

The common stock of Comtech Telecommunications Corp. is traded in the Over-The-Counter market. The prices shown are representative quotations supplied by the National Association of Securities Dealers, Inc., through NASDAQ and do not include retail mark-up, mark-down or commissions and do not necessarily reflect actual transactions.

	Fiscal Year 1978		Fiscal Year 1977	
Quarter	Bid, Low-High	Asked, Low-High	Bid, Low-High	Asked, Low-High
1st	6-8¼	7-9¼	12¼-20¾	13¼-21¾
2nd	6-8½	7-9¼	11-15	12-16
3rd	8½-12½	9¼-13¼	8¼-13¾	9¼-14¾
4th	10½-14	11¼-14¾	5¾-8¾	6¾-9¾

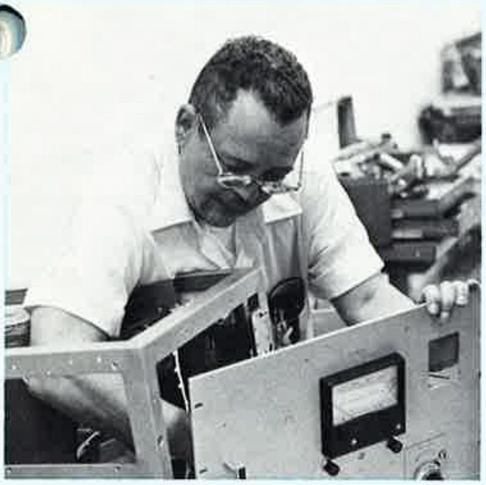
Dividends

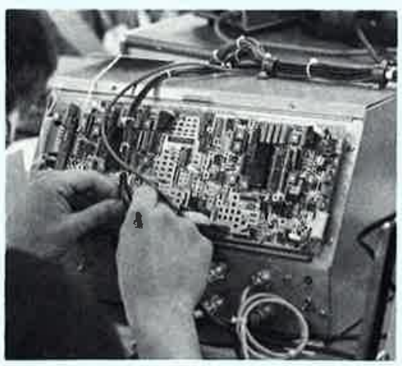
No dividends have been paid on the Company's common stock.

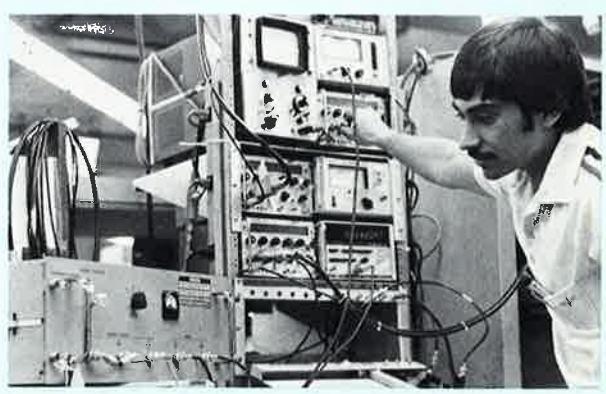
Form 10-K

A copy of the Company's Annual Report on Form 10-K for fiscal year 1978 as filed with the Securities and Exchange Commission (excluding exhibits) will be furnished, without charge, to any owner of common stock of the Company entitled to vote at its Annual Meeting, upon written request to J.P. Windus, Jr., Secretary-Treasurer, Comtech Telecommunications Corp., 135 Engineers Rd., Smithtown, NY 11787.

Comtech at Work







Board of Directors

F. Kornberg – Chairman
B. Adler – Business and Engineering Consultant
G. Bugliarello – President, Polytechnic Institute of New York
G. R. Nocita – Consultant to the Company
J. E. Rosenblum
J. A. Tokar – Vice President, Combustion Equipment Associates, Inc.

Officers

F. Kornberg – President and Chief Executive Officer
M. L. Deever – Vice President
A. K. Fowler – Vice President
E. Ladin – Vice President
J. E. Rosenblum – Vice President
J. P. Windus, Jr. – Secretary/Treasurer

Banks

Chemical Bank
1455 Veterans Memorial Highway
Hauppauge, New York 11787

The Chase Manhattan Bank, N.A.
1 Chase Manhattan Plaza
New York, N.Y. 10015

Legal Counsel

Botein, Hays, Sklar & Herzberg
200 Park Avenue
New York, New York 10017

Registrar and Transfer Agent

Chemical Bank
55 Water Street
New York, New York 10041

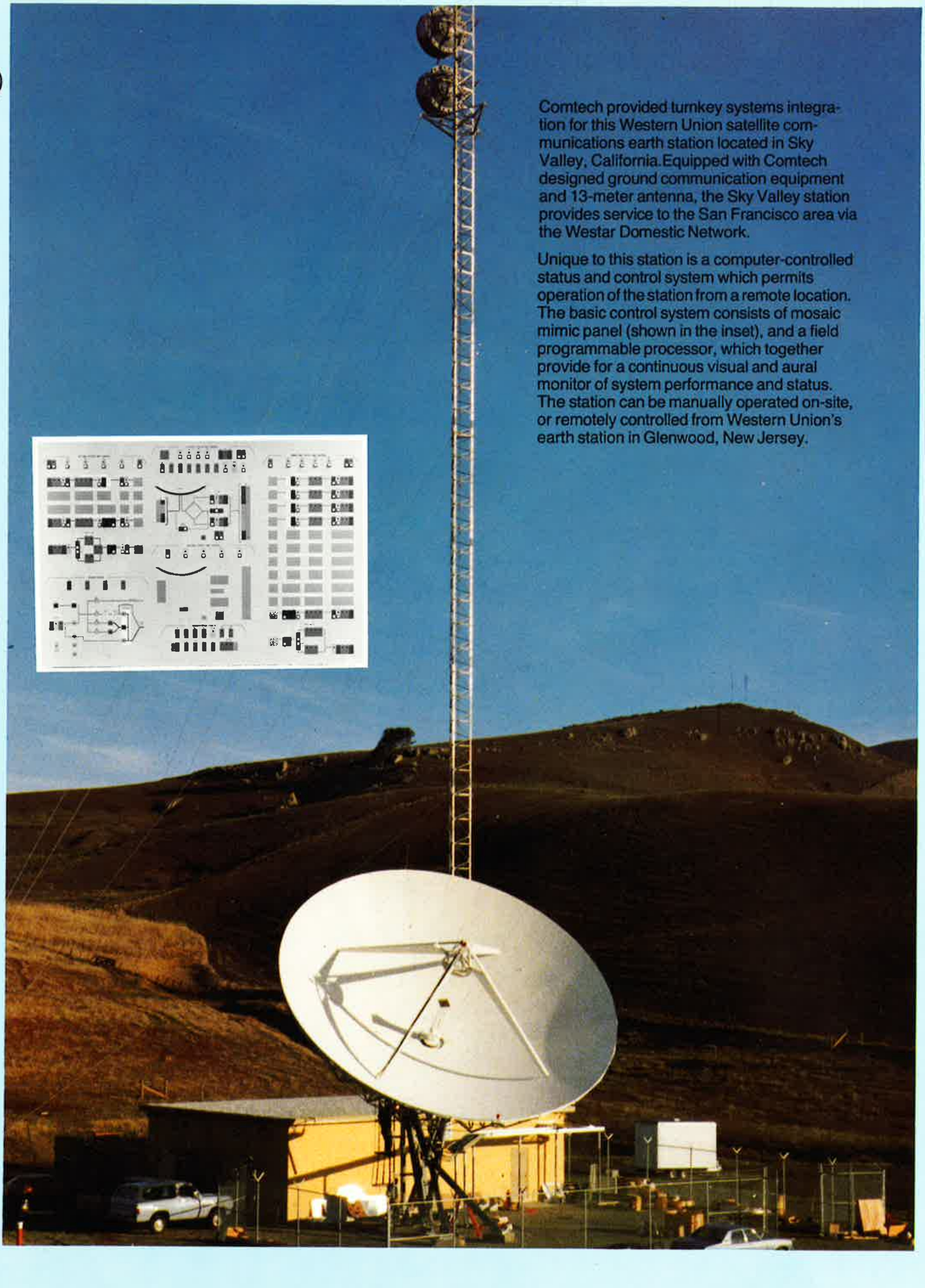
Independent Accountants

Arthur Andersen & Co.
1 Huntington Quadrangle
Huntington, Long Island, New York 11746

Stock Traded – OTC **NASDAQ Symbol – CMTL**

COMTECH Telecommunications Corp.

135 ENGINEERS ROAD • SMITHTOWN, NEW YORK 11787 • (516) 231-5454 • TWX: 510 227-6235



Comtech provided turnkey systems integration for this Western Union satellite communications earth station located in Sky Valley, California. Equipped with Comtech designed ground communication equipment and 13-meter antenna, the Sky Valley station provides service to the San Francisco area via the Westar Domestic Network.

Unique to this station is a computer-controlled status and control system which permits operation of the station from a remote location. The basic control system consists of mosaic mimic panel (shown in the inset), and a field programmable processor, which together provide for a continuous visual and aural monitor of system performance and status. The station can be manually operated on-site, or remotely controlled from Western Union's earth station in Glenwood, New Jersey.

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