

VIRCO MFG CORPORATION

Form 10-Q

June 08, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Quarterly Report under Section 13 or 15(d)
of the Securities Exchange Act of 1934
FORM 10-Q
For Quarter Ended April 30, 2007
Commission File Number 1-8777
VIRCO MFG. CORPORATION
 (Exact Name of Registrant as Specified in its Charter)

| | |
|---|---|
| Delaware | 95-1613718 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 2027 Harpers Way, Torrance, CA | 90501 |
| (Address of principal executive offices) | (Zip Code) |
| Registrant's telephone number, including area code: <u>(310) 533-0474</u> | |
| No change | |

Former name, former address and former fiscal year, if changed since last report.

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

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

The number of shares outstanding for each of the registrant's classes of common stock, as of the latest practicable date:

Common Stock, \$.01 par value 14,379,506 shares as of May 30, 2007.

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Exhibit 31.2 Certification of Robert E. Dose, Vice President, Finance, pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act, as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002.

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

EXHIBIT 4.1

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Table of Contents**PART I****Item 1. Financial Statements**

VIRCO MFG. CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

| | 4/30/2007 | 1/31/2007 | 4/30/2006 |
|--|-----------------------------------|------------|------------|
| | (In thousands, except share data) | | |
| Assets | | | |
| Current assets | | | |
| Cash | \$ 1,523 | \$ 1,892 | \$ 752 |
| Trade accounts receivable | 14,133 | 18,796 | 18,247 |
| Less allowance for doubtful accounts | 208 | 200 | 234 |
| Net trade accounts receivable | 13,925 | 18,596 | 18,013 |
| Other receivables | 85 | 228 | 224 |
| Inventories | | | |
| Finished goods, net | 20,443 | 11,651 | 19,641 |
| Work in process, net | 25,376 | 19,690 | 22,816 |
| Raw materials and supplies, net | 7,031 | 6,496 | 9,194 |
| | 52,850 | 37,837 | 51,651 |
| Prepaid expenses and other current assets | 1,767 | 1,479 | 1,041 |
| Total current assets | 70,150 | 60,032 | 71,681 |
| Property, plant and equipment: | | | |
| Land and land improvements | 3,596 | 3,596 | 3,591 |
| Buildings and building improvements | 49,555 | 49,555 | 49,581 |
| Machinery and equipment | 110,607 | 109,730 | 106,981 |
| Leasehold improvements | 1,338 | 1,323 | 1,302 |
| | 165,096 | 164,204 | 161,455 |
| Less accumulated depreciation and amortization | 117,728 | 116,116 | 111,374 |
| Net property, plant and equipment | 47,368 | 48,088 | 50,081 |
| Goodwill and other intangible assets, net | 2,308 | 2,311 | 2,323 |
| Other assets | 5,846 | 5,846 | 8,727 |
| Total assets | \$ 125,672 | \$ 116,277 | \$ 132,812 |

See Notes to Condensed Consolidated Financial Statements.

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VIRCO MFG. CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

| | 4/30/2007 | 1/31/2007 | 4/30/2006 |
|--|-----------------------------------|-------------------|-------------------|
| | (In thousands, except share data) | | |
| Liabilities | | | |
| Current liabilities | | | |
| Checks released but not yet cleared bank | \$ 1,664 | \$ 2,563 | \$ 2,276 |
| Accounts payable | 13,414 | 14,463 | 23,474 |
| Accrued compensation and employee benefits | 5,860 | 8,094 | 5,063 |
| Current portion of long-term debt | 5,074 | 5,074 | 5,012 |
| Other accrued liabilities | 6,367 | 6,844 | 5,974 |
| Total current liabilities | 32,379 | 37,038 | 41,799 |
| Non-current liabilities | | | |
| Accrued self-insurance retention and other | 4,911 | 3,962 | 3,104 |
| Accrued pension expenses | 16,248 | 15,949 | 15,024 |
| Long-term debt, less current portion | 25,866 | 10,190 | 36,511 |
| Total non-current liabilities | 47,025 | 30,101 | 54,639 |
| Deferred income taxes, net | 260 | 260 | |
| Commitments and contingencies | | | |
| Stockholders' equity: | | | |
| Preferred stock | | | |
| Authorized 3,000,000 shares, \$.01 par value; none issued or outstanding | | | |
| Common stock | | | |
| Authorized 25,000,000 shares, \$.01 par value; issued 14,379,506 shares at 4/30/2007 and 1/31/2007, and 13,137,288 shares at 4/30/2006 | | | |
| | 143 | 143 | 131 |
| Additional paid-in capital | 113,847 | 113,737 | 108,684 |
| Accumulated deficit | (60,416) | (57,436) | (68,248) |
| Accumulated comprehensive loss | (7,566) | (7,566) | (4,193) |
| Total stockholders' equity | 46,008 | 48,878 | 36,374 |
| Total liabilities and stockholders' equity | \$ 125,672 | \$ 116,277 | \$ 132,812 |

See Condensed Consolidated Financial Statements.

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VIRCO MFG. CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 Unaudited (Note 1)

| | Three months ended | |
|---|-----------------------------------|------------|
| | 4/30/2007 | 4/30/2006 |
| | (In thousands, except share data) | |
| Net sales | \$31,122 | \$34,515 |
| Costs of goods sold | 19,572 | 23,021 |
| Gross profit | 11,550 | 11,494 |
| Selling, general and administrative expenses and other | 13,986 | 13,875 |
| Interest expense | 544 | 886 |
| Loss before income taxes | (2,980) | (3,267) |
| Provision for income taxes | | |
| Net loss | \$ (2,980) | \$ (3,267) |
| Net loss per common share | | |
| Basic | \$ (0.21) | \$ (0.25) |
| Weighted average shares outstanding | | |
| Basic | 14,380 | 13,137 |
| See Notes to Condensed Consolidated Financial Statements. | | |

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VIRCO MFG. VIRCO MFG. CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 Unaudited (Note 1)

| | Three months ended | |
|--|--------------------|------------|
| | 4/30/2007 | 4/30/2006 |
| | (In thousands) | |
| Operating activities | | |
| Net loss | \$ (2,980) | \$ (3,267) |
| Adjustments to reconcile net loss to net cash used in operating activities | | |
| Depreciation and amortization | 1,730 | 1,861 |
| Provision for doubtful accounts | 8 | 25 |
| Gain on sale of property, plant and equipment | (17) | |
| Stock based compensation | 110 | 294 |
| Changes in operating assets and liabilities | | |
| Trade accounts receivable | 4,663 | (768) |
| Other receivables | 143 | 153 |
| Inventories | (15,013) | (20,034) |
| Income taxes | 2 | 10 |
| Prepaid expenses and other current assets | (288) | 452 |
| Accounts payable and accrued liabilities | (3,423) | 6,086 |
| Net cash used in operating activities | (15,065) | (15,188) |
| Investing activities | | |
| Capital expenditures | (997) | (519) |
| Proceeds from sale of property, plant and equipment | 17 | |
| Net cash used in investing activities | (980) | (519) |
| Financing activities | | |
| Issuance of long-term debt | 15,694 | 14,970 |
| Repayment of long-term debt | (18) | |
| Net cash provided by financing activities | 15,676 | 14,970 |
| Net decrease in cash | (369) | (737) |
| Cash at beginning of year | 1,892 | 1,489 |
| Cash at end of year | \$ 1,523 | \$ 752 |
| Supplemental disclosures of cash flow information | | |
| Non-cash activities | | |
| Deferred compensation | \$ | \$ 247 |

See Notes to Condensed Consolidated Financial Statements.

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VIRCO MFG. CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
April 30, 2007

Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended April 30, 2007, are not necessarily indicative of the results that may be expected for the year ending January 31, 2008. The balance sheet at January 31, 2007 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended January 31, 2007.

Note 2. Seasonality

The market for educational furniture is marked by extreme seasonality, with over 50% of the Company's total sales typically occurring from June to September each year, which is the Company's peak season. Hence, the Company typically builds and carries significant amounts of inventory during and in anticipation of this peak summer season to facilitate the rapid delivery requirements of customers in the educational market. This requires a large up-front investment in inventory, labor, storage and related costs as inventory is built in anticipation of peak sales during the summer months. As the capital required for this build-up generally exceeds cash available from operations, the Company has historically relied on third-party bank financing to meet cash flow requirements during the build-up period immediately preceding the peak season.

In addition, the Company typically is faced with a large balance of accounts receivable during the peak season. This occurs for two primary reasons. First, accounts receivable balances typically increase during the peak season as shipments of products increase. Second, many customers during this period are government institutions, which tend to pay accounts receivable more slowly than commercial customers.

The Company's working capital requirements during and in anticipation of the peak summer season require management to make estimates and judgments that affect assets, liabilities, revenues and expenses, and related contingent assets and liabilities. On an on-going basis, management evaluates its estimates, including those related to market demand, labor costs, and stocking inventory.

Note 3. New Accounting Standards

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements (SFAS 157) which provides enhanced guidance for using fair value to measure assets and liabilities. SFAS 157 also expands the amount of disclosure regarding the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company does not anticipate any material impact to its financial statements from the adoption of this standard.

In October 2006, the FASB ratified EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements . This statement is effective for years beginning after December 15, 2007. This statement clarifies that FASB 106, Employers Accounting for Post-Retirement Benefits other than Pensions , applies to endorsement split-dollar life insurance arrangements. The Company estimates that adoption of this statement will increase the Company's recorded liabilities by approximately \$2,000,000 with no impact to the statement of operations or cash flows of the Company . The Company has purchased life insurance policies that are designed to pay a death benefit that is greater than the promised retirement benefit.

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In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159) which permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective of SFAS 159 is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is effective as of the beginning of any fiscal year beginning after November 15, 2007. The Company does not anticipate any material impact to its financial statements from the adoption of this standard.

Note 4. Inventories

Fiscal year end financial statements at January 31, 2007 reflect inventories verified by physical counts with the material content valued by the LIFO method. At April 30, 2007 and 2006, there were no physical verifications of inventory quantities. Cost of sales is recorded at current cost. The effect of penetrating LIFO layers is not recorded at interim dates unless the reduction in inventory is expected to be permanent. No such adjustments have been made for the periods ended April 30, 2007 and 2006. LIFO reserves at April 30, 2007, January 31, 2007 and April 30, 2006 were \$7,357,000, \$7,357,000 and \$6,423,000, respectively. Management continually monitors production costs, material costs and inventory levels to determine that interim inventories are fairly stated.

Note 5. Debt

The Company has entered into a revolving credit facility with Wells Fargo Bank, which was amended and restated in March and April 2007, and which provides a term loan of \$20,000,000 and a secured revolving line of credit that varies as a percentage of inventory and receivables, up to a maximum of \$40,000,000, with the maximum increasing to \$50,000,000 during certain months of the year. The amended agreement, which is effective March 2007, extended the maturity date from February 15, 2008 to February 15, 2009. The term note is a two-year loan, amortizing at \$10,000,000 per year with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate (8.25% at April 30, 2007) plus a 0.5% margin.

The amendment extended the maturity date of the revolving line from February 15, 2008 to February 15, 2009 with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate plus a fluctuating margin similar to the term note. The revolving line typically provides for advances of 80% on eligible accounts receivable and 20% - 60% on eligible inventory. The advance rates fluctuate depending on the time of the year and the types of assets. The agreement has an unused commitment fee of 0.375%. Approximately \$25,691,000 was available for borrowing as of April 30, 2007.

The credit facility with Wells Fargo Bank is subject to various financial covenants including a liquidity requirement, a leverage requirement, a cash flow coverage requirement and profitability requirements. The agreement also places certain restrictions on capital expenditures, new operating leases, dividends and the repurchase of the Company's common stock. The revolving credit facility is secured by the Company's accounts receivable, inventories, equipment and property. The Company is in compliance with its covenants at April 30, 2007.

Note 6. Income Taxes

On February 1, 2007, the Company adopted the provisions of FIN No. 48. As a result of the implementation of FIN No. 48, the Company recognized no material adjustment to the liability for unrecognized income tax benefits. At the adoption date of February 1, 2007, the Company had approximately \$760,000 of unrecognized tax benefits. At April 30, 2007, the Company had approximately \$760,000 of unrecognized tax benefits all of which would impact the effective tax rate if recognized. The Company estimates that no unrecognized tax benefits will decrease in the next twelve months due to the expiration of statute of limitations and completion of audits in progress. The Company records interest and penalties on uncertain tax positions to income tax expense. As of February 1, 2007 and April 30, 2007, the Company has accrued \$164,000 of interest and \$134,000 of penalties related to uncertain tax positions. The tax years 2004 to 2006 remain open to examination by the IRS for federal income taxes. The tax years 2003 to 2006 remain open for major state taxing jurisdictions. The Company is not being audited by a major taxing jurisdiction at April 30, 2007.

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At January 31, 2007, the Company had net operating losses that can potentially be carried forward for federal and state income tax purposes, expiring at various dates through 2027 if not utilized. Federal net operating losses that can potentially be carried forward total approximately \$15,409,000 at January 31, 2007. State net operating losses that can potentially be carried forward total approximately \$32,791,000 at January 31, 2007. Net operating losses carried forward will be utilized to offset taxable income realized for the three months ended April 30, 2007.

Note 7. Net Income / (Loss) per Share

| | Three Months Ended | |
|---|---------------------------------------|------------|
| | 4/30/2007 | 4/30/2006 |
| | (In thousands, except per share data) | |
| Numerators: | | |
| Numerator for both basic and diluted net loss per share | \$ (2,980) | \$ (3,267) |
| Denominators: | 14,380 | 13,137 |
| Denominator for basic net loss per share weighted-average common shares outstanding | | |
| Potentially dilutive shares from stock option plans | | |
| Denominator for diluted net loss per share | 14,380 | 13,137 |
| Net loss per share basic | \$ (0.21) | \$ (0.25) |

Certain exercisable and non-exercisable stock options were not included in the computation of diluted net loss per share at April 30, 2007 and 2006, because their inclusion would have been anti-dilutive. The number of stock options outstanding, which met this anti-dilutive criterion for the three months ended April 30, 2007 and 2006, was 148,000 and 68,000, respectively.

Note 8. Stock Based Compensation

The Company's two stock plans are the 1997 Employee Incentive Plan (the 1997 Plan) and the 1993 Employee Incentive Stock Plan (the 1993 Plan). Under the 1993 Plan, the Company was permitted to grant an aggregate of 707,384 shares (as adjusted for stock splits and stock dividends) to its employees and directors in the form of stock options. The 1993 Plan expired in 2003 and had no unexercised options outstanding at April 30, 2007. Under the 1997 Plan, the Company may grant an aggregate of 724,729 shares (as adjusted for stock splits and stock dividends) to its employees and directors in the form of stock options or awards. As of April 30, 2007, the 1997 Plan had 234,594 unexercised options outstanding and 109,262 shares remain available for future grant. Options granted under the plans have an exercise price equal to the market price at the date of grant, have a maximum term of 10 years and generally become exercisable ratably over a five-year period. The Company did not grant any stock based compensation during the three months ended April 30, 2007.

The shares of common stock issued upon exercise of a previously granted stock option are considered new issuances from shares reserved for issuance upon adoption of the various plans. While the Company does not have a formal written policy detailing such issuance, it requires that the option holders provides a written notice of exercise to the stock plan administrator and payment for the shares prior to issuance of the shares.

Accounting for the Plans

Effective February 1, 2006 the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment*, using the modified prospective-transition method. The modified prospective-transition method was applied to those unvested options issued prior to the Company's adoption that have historically been accounted for under the Intrinsic Value Method. All outstanding options were 100% vested prior to the adoption and no options were granted since the adoption of FASB Statement No. 123(R). Accordingly, no compensation expense was recorded on the Company's options during the three months ended April 30, 2007 or

April 30, 2006.

Table of Contents**Restricted Stock Unit Awards**

On June 30, 2004, the Company granted a total of 270,000 restricted stock units, with an estimated fair value of \$6.92 per unit and exercise price of \$0.01 per unit, to eligible employees under the 1997 Plan. Interests in such restricted stock units vest ratably over five years, with such units vesting 20% at each anniversary date. At such time that the restricted stock units vest, they become exchangeable for shares of common stock. Compensation expense is recognized based on the estimated fair value of restricted stock units and vesting provisions. Compensation expense incurred in connection with this award for the three months ended April 30, 2007 and 2006 was \$110,000 and \$88,000, respectively. As of April 30, 2007, there was approximately \$772,000 of unrecognized compensation cost related to non-vested restricted stock unit awards. Unrecognized compensation cost is expected to be recognized through June 2009.

On January 13, 2006, the Company granted a total of 73,881 restricted stock units, with an estimated fair value of \$5.21 per unit and exercise price of \$0.01 per unit, to non-employee directors under the 1997 Plan. Participants vest their interest in notional stock units ratably over the vesting period, with such units being 100% vested at July 5, 2006. Compensation expense is recognized based on the estimated fair value of restricted stock units and vesting provisions. For the quarter ended April 30, 2006, compensation expense incurred in connection with this award was \$206,000. As of April 30, 2007, there was no unrecognized compensation cost related to these Awards.

As the compensation cost for the restricted stock units was measured using the estimated fair value on the date of grant and recognized over the vesting period, there was no effect on the statements of operations, due to the adoption of FASB Statement No. 123(R). At February 1, 2006, the Company recorded a transitional reclassification of \$247,000 from current liabilities to additional paid-in capital.

Stockholders Rights

On October 15, 1996, the Board of Directors declared a dividend of one preferred stock purchase right (the Rights) for each outstanding share of the Company s common stock. Each of the Rights entitles a stockholder to purchase for an exercise price of \$50.00 (\$20.70, as adjusted for stock splits and stock dividends), subject to adjustment, one one-hundredth of a share of Series A Junior Participating Cumulative Preferred Stock of the Company, or under certain circumstances, shares of common stock of the Company or a successor company with a market value equal to two times the exercise price. The Rights are not exercisable, and would only become exercisable for all other persons when any person has acquired or commences to acquire a beneficial interest of at least 20% of the Company s outstanding common stock. The Rights have no voting privileges, and may be redeemed by the Board of Directors at a price of \$.001 per Right at any time prior to the acquisition of a beneficial ownership of 20% of the outstanding common shares. There are 200,000 shares (483,153 shares as adjusted by stock splits and stock dividends) of Series A Junior Participating Cumulative Preferred Stock reserved for issuance upon exercise of the Rights. On April 30, 2007, the Company and Mellon Investor Services LLC entered into an amendment to the Rights Agreement governing the Rights. The amendment, among other things, extends the term of the Rights issued under the Rights Agreement to October 25, 2016, removes the dead-hand provisions from the Rights Agreement, and formally replaces the former Rights Agent, The Chase Manhattan Bank, with its successor-in-interest, Mellon Investor Services LLC.

Note 9. Comprehensive Income (Loss)

Comprehensive income (loss) for the three months ended April 30, 2007 and 2006 was the same as net income (loss) reported on the statements of operations. Accumulated comprehensive income (loss) at April 30, 2007 and 2006 and January 31, 2007 is composed of minimum pension liability adjustments.

Note 10. Retirement Plans

The Company and its subsidiaries cover all employees under a noncontributory defined benefit retirement plan, entitled the Virco Employees Retirement Plan (the Plan). Benefits under the Plan are based on years of service and career average earnings. As more fully described in the Form 10-K for the period ended January 31, 2007, benefit accruals under this plan were frozen effective December 31, 2003.

The Company also provides a supplementary retirement plan for certain key employees, the VIP Retirement Plan (the VIP Plan). The VIP Plan provides a benefit of up to 50% of average compensation for the last five years in the VIP Plan, offset by benefits earned under the Plan. As more fully described in the Form 10-K for the period ended January 31, 2007, benefit accruals under this plan were frozen effective December 31, 2003.

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The Company also provides a non-qualified plan for non-employee directors of the Company (the Non-Employee Directors Retirement Plan). The Non-Employee Directors Retirement Plan provides a lifetime annual retirement benefit equal to the director's annual retainer fee for the fiscal year in which the director terminates his or her position with the Board, subject to the director providing 10 years of service to the Company. As more fully described in the Form 10-K for the period ended January 31, 2007, benefit accruals under this plan were frozen effective December 31, 2003.

The net periodic pension costs for the Plan, the VIP Plan, and the Non-Employee Directors Retirement Plan for the three months each ended April 30, 2007 and 2006 were as follows (in thousands):

| | Three Months Ended April 30, | | | | | |
|---|------------------------------|--------|---------------------|-------|--|------|
| | Pension Plan | | VIP Retirement Plan | | Non-Employee Directors Retirement Plan | |
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Service cost | \$ 41 | \$ 43 | \$ 50 | \$ 53 | \$ 6 | \$ 6 |
| Interest cost | 345 | 352 | 90 | 85 | 7 | 6 |
| Expected return on plan assets | (224) | (246) | | | | |
| Amortization of transition amount | (9) | (9) | | | | |
| Amortization of prior service cost | 117 | 117 | (134) | (134) | 6 | 22 |
| Recognized net actuarial (Gain) or loss | 49 | 41 | 30 | 34 | (7) | (7) |
| Settlement and curtailment | | | | | | |
| Net periodic pension cost | \$ 319 | \$ 298 | \$ 36 | \$ 38 | \$12 | \$27 |

Note 11. Warranty

The Company accrues an estimate of its exposure to warranty claims based upon both current and historical product sales data and warranty costs incurred. The majority of the Company's products sold through January 31, 2005, carry a five-year warranty. Effective February 1, 2005, the Company extended its standard warranty period to 10 years. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. The warranty liability is included in accrued liabilities in the accompanying consolidated balance sheet.

The following is a summary of the Company's warranty claim activity for the three month periods each ended April 30, 2007 and 2006 (in thousands):

| | April 30, | |
|-------------------|-----------|---------|
| | 2007 | 2006 |
| Beginning balance | \$1,750 | \$1,500 |
| Provision | 345 | 206 |
| Costs incurred | (245) | (206) |
| Ending balance | \$1,850 | \$1,500 |

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VIRCO MFG. CORPORATION

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

Results of Operations

For the first quarter of 2007, the Company incurred a net loss of \$2,980,000 on sales of \$31,122,000 compared to a net loss of \$3,267,000 on sales of \$34,515,000 in the same period last year.

Sales for the first quarter ended April 30, 2007 decreased by \$3,393,000, a 9.8% decrease, compared to the same period last year. Incoming orders for the same period were flat compared to the prior year. Backlog at April 30, 2007 increased by approximately 18% compared to the prior year.

Gross margin as a percentage of sales increased to 37.1% in 2007 compared to 33.3% in the prior year. Gross margin dollars were comparable to the prior year despite a \$3,393,000 reduction in sales volume. The improvement in margin was attributable to a price increase of approximately 7%, increased sales including service related expenses such as installation, and relatively stable material costs.

Selling, general and administrative expense for the quarter ended April 30, 2007 increased by approximately \$111,000 compared to the same period last year, and increased as a percentage of sales by 4.7%. The increase as a percentage of sales was primarily attributable to the reduction in first quarter sales and to a larger percentage of sales including service related expenses such as installation.

Interest expense decreased by approximately \$342,000 compared to the same period last year. The decrease is due to reduced interest rates in addition to lower loan balances.

Financial Condition

As a result of seasonally lower shipments in the first quarter compared to the fourth quarter and the first quarter last year, accounts and notes receivable were reduced at April 30, 2007 compared to January 31, 2007 and April 30, 2006. The Company traditionally builds large quantities of inventory during the first quarter in anticipation of seasonally high summer shipments. For the current quarter, the Company increased inventory by approximately \$15,000,000 compared to January 31, 2007. This increase in inventory was slightly less than the increase in the first quarter in the prior year. The increase in inventory during the first quarter was financed through the credit facility with Wells Fargo Bank.

At April 30, 2007 compared to April 30, 2006, accounts payable decreased by approximately \$10,000,000 and borrowings under the line of credit decreased by more than \$10,000,000. The cumulative impact of a prior year private placement to raise nearly \$5,000,000 of capital, net income of nearly \$8,000,000 during the rolling 12 months ending April 30, 2007, and depreciation in excess of capital expenditures have improved the financial strength of the Company.

The Company has established a goal of limiting capital spending to less than \$5,000,000 for 2007, which is approximately two-thirds of anticipated depreciation expense. Capital spending for the quarter ended April 30, 2007, was \$997,000 compared to \$519,000 for the same period last year. Capital expenditures are being financed through the Company's credit facility established with Wells Fargo Bank and operating cash flow.

Net cash used in operating activities for the first quarter ended April 30, 2007 was \$15,065,000 compared to \$15,188,000 for the same period last year, but the composition of the operating cash flows varied significantly. For the first quarter of 2007, the Company used approximately \$10,000,000 less for seasonal changes in trade receivables and inventory. During the same period the Company generated approximately \$10,000,000 less from changes in accounts payable.

The Company believes that cash flows from operations, together with the Company's unused borrowing capacity with Wells Fargo Bank will be sufficient to fund the Company's debt service requirements, capital expenditures and working capital needs for the next twelve months. Approximately \$25,691,000 was available for borrowing as of April 30, 2007.

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Off Balance Sheet Arrangements

During the first quarter, there were no material changes in the Company's off balance sheet arrangements or contractual obligations and commercial commitments from those disclosed in the Form 10-K for the fiscal year ended January 31, 2007.

Critical Accounting Policies and Estimates

The Company's critical accounting policies are outlined in its Form 10-K for fiscal year ended January 31, 2007.

Forward-Looking Statements

From time to time, including in this quarterly report, the Company or its representatives have made and may make forward-looking statements, orally or in writing, including those contained herein. Such forward-looking statements may be included in, without limitation, reports to stockholders, press releases, oral statements made with the approval of an authorized executive officer of the Company and filings with the Securities and Exchange Commission. The words or phrases anticipates, expects, will continue, believes, estimates, projects, or similar expressions are used to identify forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The results contemplated by the Company's forward-looking statements are subject to certain risks and uncertainties that could cause actual results to vary materially from anticipated results, including without limitation, material availability and cost of materials, especially steel, availability and cost of labor, demand for the Company's products, competitive conditions affecting selling prices and margins, capital costs and general economic conditions. Such risks and uncertainties are discussed in more detail in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2007.

The Company's forward-looking statements represent its judgment only on the dates such statements were made. By making any forward-looking statements, the Company assumes no duty to update them to reflect new, changed or unanticipated events or circumstances.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company has entered into a revolving credit facility with Wells Fargo Bank, which was amended and restated in March 2007, and which provides a term loan of \$20,000,000 and a secured revolving line of credit that varies as a percentage of inventory and receivables, up to a maximum of \$40,000,000, with the maximum increasing to \$50,000,000 during certain months of the year. The amended agreement, which is effective March 2007, extended the maturity date from February 15, 2008 to February 15, 2009. The term note is a two-year loan, amortizing at \$10,000,000 per year with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate (8.25% at April 30, 2007) plus a 0.5% margin.

The amendment extended the maturity date of the revolving line from February 15, 2008 to February 15, 2009 with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate plus a fluctuating margin similar to the term note. The revolving line typically provides for advances of 80% on eligible accounts receivable and 20% - 60% on eligible inventory. The advance rates fluctuate depending on the time of the year and the types of assets. The agreement has an unused commitment fee of 0.375%. Approximately \$25,691,000 was available for borrowing as of April 30, 2007.

The revolving credit facility with Wells Fargo Bank is subject to various financial covenants including a liquidity requirement, a leverage requirement, a cash flow coverage requirement and profitability requirements. The agreement also places certain restrictions on capital expenditures, new operating leases, dividends and the repurchase of the Company's common stock. The revolving credit facility is secured by the Company's accounts receivable, inventories, equipment and property. The Company is in compliance with its covenants at April 30, 2007.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in reports filed with the Securities and Exchange Commission (the Commission) pursuant to the Securities Exchange Act of 1934 (the Exchange Act) is recorded, processed, summarized and reported within the time periods

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specified in the Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its President and Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Assessing the costs and benefits of such controls and procedures necessarily involves the exercise of judgment by management, and such controls and procedures, by their nature, can provide only reasonable assurance that management's objectives in establishing them will be achieved.

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including its President and Chief Executive Officer along with its Principal Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of the end of the period covered by this Annual Report pursuant to Exchange Act Rule 13a-15. Based upon the foregoing, the Company's President and Chief Executive Officer along with the Company's Chief Financial Officer concluded that, subject to the limitations noted in this Part I, Item 4, Virco's disclosure controls and procedures are effective in ensuring that (i) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Internal Control Over Financial Reporting

There was no change in the Company's internal control over financial reporting during the first fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II

**VIRCO MFG. CORPORATION
OTHER INFORMATION**

Item 1A. Risk Factors

There have been no material changes from risk factors as disclosed in the Form 10-K for the period ended January 31, 2007.

Item 6. Exhibits

Exhibit 4.1 Amendment dated as of April 30, 2007 by and between the Company and Mellow Investor Services LLC to the Rights Agreement by and between the Company and The Chase Manhattan Bank dated as of October 18, 1996.

Exhibit 31.1 Certification of Robert A. Virtue, President, pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act, as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 31.2 Certification of Robert E. Dose, Vice President, Finance, pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act, as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002.

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

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VIRCO MFG. CORPORATION

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.

VIRCO MFG. CORPORATION

Date: June 8, 2007

By: /s/ Robert E. Dose

Robert E. Dose
Vice President Finance

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