
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-Q

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

For the quarterly period ended December 31, 2005

Commission File Number 1-10981



SBS Technologies, Inc.

(Exact name of Registrant as Specified in its Charter)

New Mexico

(State or Other Jurisdiction of Incorporation or Organization)

85-0359415

(I.R.S. Employer Identification Number)

7401 Snaproll NE

Albuquerque, New Mexico 87109

(Address of Principal Executive Offices including Zip Code)

(505) 875-0600

(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).
YES ☒ NO ☐

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

The total number of shares outstanding of the registrant's Common Stock as of January 27, 2006 was 15,663,665.

SBS Technologies, Inc. and Subsidiaries
Form 10-Q for the Quarter Ended December 31, 2005
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FORWARD-LOOKING STATEMENTS

This Form 10-Q contains forward-looking statements with respect to the financial condition, results of operations, and business of SBS Technologies, Inc. and subsidiaries (referred to variously as “SBS”, “we”, “us” and “our”). You may find many of these statements by looking for words like “intends,” “expects,” “projects,” “believes,” “anticipates” or similar expressions in this Form 10-Q. We consider all statements regarding anticipated or future matters, including the following, to be forward-looking statements:

- statements regarding future events and the future financial performance of SBS;
- expected sales levels for the fiscal year ending June 30, 2006;
- expected sales levels for the quarter ending March 31, 2006;
- expected growth anticipated in the second half of the fiscal year ending June 30, 2006;
- the expectation to close additional AdvancedMC™ product design wins;
- the expectation of increased sales of AdvancedMC products from low rate initial production in the second half of fiscal 2006, and from significant production in fiscal 2007;
- expected levels of research and development expense;
- the expectation of internally-generated cash flows;
- expected renewal of the Credit Agreement with Wells Fargo Bank National Association;
- the continued health of the end markets we serve;
- the expectation that we will continue to grow through strategic acquisitions; and
- the expectation that 30% to 40% of our sales in each fiscal quarter will be based on orders received and booked during that same fiscal quarter.

These statements are not guarantees of our future performance. They are based upon our assumptions and assessments only on the date we made them and in light of our experience and our perception of historical trends, current conditions, expected future developments, and other factors we believe to be appropriate. Our assumptions and assessments include the volume and product mix of sales, estimates of costs, inventory and receivable levels based on preliminary information, and others. Risks, uncertainties, and other important factors could cause actual performance or achievements to be materially different from those we may project. These risks, uncertainties, and factors include:

- business and economic conditions generally affecting our customers and their end customers, including but not limited to the changes in size and program priorities of military procurement budgets, which may be less favorable than we expect, resulting in lower sales and earnings;
- a high degree of uncertainty and rapid change in the markets addressed by our products that could reduce sales or render certain SBS products obsolete, resulting in reduced gross profit levels;
- customer demand for and acceptance of our products, which may be less than we expect, affecting both sales and margins;
- our ability to design, test and introduce new products on a timely basis, which, if we are not able, may decrease both sales and margins;
- the other risk factors listed under “Risk Factors” included in SBS’ Annual Report on Form 10-K for the year ended June 30, 2005.

Many of the factors that will determine these items are beyond our ability to control or predict. We caution you not to place undue reliance on our forward-looking statements, which speak only as of the date of this Form 10-Q. We do not undertake any obligation to update publicly or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

SBS Technologies, Inc. and Subsidiaries

Consolidated Balance Sheets

Thousands (except share amounts)

(Unaudited)

	December 31, 2005	June 30, 2005
<u>Assets</u>		
Current assets:		
Cash and cash equivalents.....	\$ 53,180	55,195
Receivables, net	28,658	27,535
Inventories.....	22,752	21,815
Deferred income taxes.....	1,356	1,361
Prepaid expenses.....	1,050	1,676
Other current assets.....	999	718
Total current assets.....	107,995	108,300
Property and equipment, net.....	7,026	7,635
Goodwill.....	16,932	16,995
Intangible assets, net.....	2,506	3,108
Deferred income taxes.....	15,325	15,529
Other assets.....	917	891
Total assets.....	\$ 150,701	152,458
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities:		
Accounts payable.....	\$ 4,667	4,509
Accrued representative commissions.....	688	819
Income taxes payable.....	2,095	3,051
Accrued compensation.....	3,666	4,851
Accrued severance and consolidation costs.....	183	424
Other current liabilities	2,977	2,785
Total current liabilities.....	14,276	16,439
Other long-term liabilities.....	198	132
Total liabilities.....	14,474	16,571
Stockholders' equity:		
Common stock, no par value; 200,000,000 shares authorized; 15,663,665 issued and outstanding at December 31, 2005, 15,645,929 issued and outstanding at June 30, 2005	99,314	98,369
Unearned compensation	(693)	(84)
Accumulated other comprehensive income.....	1,494	2,014
Retained earnings.....	36,112	35,588
Total stockholders' equity.....	136,227	135,887
Total liabilities and stockholders' equity.....	\$ 150,701	152,458

See accompanying notes to condensed consolidated financial statements

SBS Technologies, Inc. and Subsidiaries
Consolidated Statements of Operations
Thousands (except per share amounts)
(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Sales.....	\$ 37,284	42,246	71,422	77,130
Cost of sales:				
Cost of products sold.....	20,788	23,039	40,448	42,079
Amortization of intangible assets.....	260	450	519	817
Total cost of sales.....	21,048	23,489	40,967	42,896
Gross profit.....	16,236	18,757	30,455	34,234
Selling, general and administrative expense.....	8,413	9,121	17,075	17,145
Research and development expense.....	6,530	6,102	13,222	11,608
Amortization of intangible assets.....	80	79	159	148
Operating income (loss).....	1,213	3,455	(1)	5,333
Interest and other income, net.....	410	204	806	345
Foreign exchange gains (losses).....	13	(342)	1	(444)
	423	(138)	807	(99)
Income before income taxes.....	1,636	3,317	806	5,234
Income tax expense.....	572	1,161	282	1,832
Net income.....	\$ 1,064	2,156	524	3,402
Earnings per share data:				
Net income per share.....	\$ 0.07	0.14	0.03	0.22
Net income per share - assuming dilution.....	\$ 0.07	0.14	0.03	0.22
Weighted average shares used in net income per share computations.....	15,654	15,527	15,650	15,516
Weighted average shares used in net income per share - assuming dilution computations.....	15,715	15,763	15,702	15,714

See accompanying notes to condensed consolidated financial statements

SBS Technologies, Inc. and Subsidiaries
Consolidated Statement of Changes in Stockholders' Equity and Comprehensive Income
For Six Months Ended December 31, 2005
Thousands (except share amounts)
(Unaudited)

	<u>Common stock</u>		<u>Unearned</u>	<u>Accumulated</u>	<u>Retained</u>	<u>Total</u>	<u>Compre-</u>
	<u>Shares</u>	<u>Amount</u>	<u>compen-</u>	<u>other</u>	<u>earnings</u>	<u>stock-</u>	<u>hensive</u>
			<u>sation</u>	<u>compre-</u>		<u>holders'</u>	<u>income</u>
				<u>hensive</u>		<u>Equity</u>	<u>(loss)</u>
				<u>income</u>			
Balances at June 30, 2005.....	15,645,929	\$ 98,369	(84)	2,014	35,588	135,887	
Exercise of stock options.....	716	4	--	--	--	4	
Stock-based compensation.....	--	137	195	--	--	332	
Restricted stock awards issued to independent directors.....	17,020	804	(804)	--	--	--	
Comprehensive income:							
Net income.....	--	--	--	--	524	524	\$ 524
Other comprehensive income:							
Foreign currency translation adjustments.....	--	--	--	(520)	--	(520)	(520)
Comprehensive income.....							\$ 4
Balances at December 31, 2005.....	<u>15,663,665</u>	<u>\$ 99,314</u>	<u>(693)</u>	<u>1,494</u>	<u>36,112</u>	<u>136,227</u>	

See accompanying notes to condensed consolidated financial statements

SBS Technologies, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Thousands
(Unaudited)

	Six Months Ended December 31,	
	2005	2004
Cash flows from operating activities:		
Net income.....	\$ 524	3,402
Adjustments to reconcile net income to net cash (used) provided by operating activities:		
Depreciation and amortization.....	2,479	2,925
Bad debt expense.....	170	61
Deferred income taxes.....	307	(40)
Loss (gain) on disposition of assets	3	(13)
Foreign exchange (gains) losses.....	(1)	444
Stock-based compensation.....	332	68
Changes in assets and liabilities:		
Receivables.....	(1,501)	(3,648)
Inventories.....	(1,139)	(2,196)
Prepaid expenses and other.....	315	115
Accounts payable.....	144	(3,017)
Accrued representative commissions.....	(119)	(76)
Income taxes.....	(919)	4,266
Accrued compensation.....	(1,168)	(493)
Accrued severance and consolidation costs.....	(241)	(218)
Other liabilities.....	263	799
Net cash (used) provided by operating activities.....	(551)	2,379
Cash flows from investing activities:		
Acquisition of property and equipment.....	(1,232)	(1,399)
Net cash used in investing activities.....	(1,232)	(1,399)
Cash flows from financing activities:		
Proceeds from exercise of stock options.....	4	665
Net cash provided by financing activities.....	4	665
Effect of exchange rate changes on cash.....	(236)	943
Net change in cash and cash equivalents.....	(2,015)	2,588
Cash and cash equivalents at beginning of period.....	55,195	47,943
Cash and cash equivalents at end of period.....	\$ 53,180	50,531
Supplemental disclosure of cash flow information:		
Income taxes paid, net.....	\$ 645	2,093

See accompanying notes to condensed consolidated financial statements

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
December 31, 2005
(Unaudited)

1) Summary of Significant Accounting Policies

The accounting policies as set forth in SBS Technologies, Inc.'s (SBS or the Company) Annual Report on Form 10-K for the year ended June 30, 2005 have been adhered to in preparing the accompanying interim condensed consolidated financial statements. These statements are unaudited but include all adjustments, consisting of normal recurring adjustments, that SBS considers necessary for a fair presentation of the financial position, results of operations, and cash flows for such interim periods. Results for such interim periods are not necessarily indicative of results for the full fiscal year 2006 or any other future periods.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the Condensed Consolidated Financial Statements and accompanying notes. Actual results could differ from these estimates.

Effective July 1, 2005, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123R, *Share-Based Payment*, (SFAS 123R) using the modified prospective method. See Note 12 for additional information regarding stock-based compensation.

2) Receivables, net

Receivables, net consist of the following:

Thousands	December 31, 2005	June 30, 2005
Accounts receivable.....	\$ 29,085	27,836
Less allowance for doubtful accounts.....	(427)	(301)
	<u>\$ 28,658</u>	<u>27,535</u>

3) Inventories

Inventories consist of the following:

Thousands	December 31, 2005	June 30, 2005
Raw materials.....	\$ 11,990	9,711
Work in process.....	3,917	3,880
Finished goods.....	6,845	8,224
	<u>\$ 22,752</u>	<u>21,815</u>

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

4) Goodwill and Intangible Assets

The Company completed the required annual goodwill impairment analysis for the fiscal year ended June 30, 2005, as of April 1, 2005, and the estimated fair value of goodwill was determined to be in excess of its carrying value, indicating the underlying goodwill was not impaired at that date.

Changes in the carrying amount of goodwill for the six months ended December 31, 2005 are as follows:

Total Goodwill by Operating Segment			
Thousands	Americas	Europe	Total
Balance at June 30, 2005.....	\$ 3,697	13,298	\$ 16,995
Foreign currency translation adjustments	175	(238)	(63)
Balance at December 31, 2005.....	<u>\$ 3,872</u>	<u>13,060</u>	<u>\$ 16,932</u>

See Note 11 for additional information regarding the Company's operating segments.

The following table discloses information regarding the carrying amounts and associated accumulated amortization for intangible assets subject to amortization.

Amortized Intangible Assets				
Thousands	Estimated useful life	Gross carrying amount	Accumulated amortization	Net carrying amount
<u>As of December 31, 2005</u>				
Current technology.....	2 - 7 yrs	\$ 9,510	7,923	1,587
License agreements.....	2 - 5 yrs	227	144	83
Covenant not to compete.....	3 - 5 yrs	1,385	691	694
Other intangibles.....	8 - 17 yrs	380	238	142
Total		<u>\$ 11,502</u>	<u>8,996</u>	<u>2,506</u>
<u>As of June 30, 2005</u>				
Current technology.....	2 - 7 yrs	\$ 9,816	7,767	2,049
License agreements.....	2 - 5 yrs	2,452	2,345	107
Covenant not to compete.....	3 - 5 yrs	2,965	2,176	789
Other intangibles.....	8 - 17 yrs	376	213	163
Total.....		<u>\$ 15,609</u>	<u>12,501</u>	<u>3,108</u>

The net change in the gross carrying amount and accumulated amortization balances reflected above are primarily the result of the removal of assets which were fully amortized as of June 30, 2005 and changes as a result of foreign currency translation adjustments. Accordingly, the net change in accumulated amortization for the period does not agree to amortization expense reported in the accompanying statements of operations for the period.

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

The following table summarizes estimated amortization expense for future periods as follows:

Estimated amortization expense:	Thousands
Remainder of fiscal year ending June 30, 2006.....	\$ 735
For the fiscal years ending:	
June 30, 2007.....	1,209
June 30, 2008.....	520
June 30, 2009.....	5
June 30, 2010 and thereafter.....	37
	<u>\$ 2,506</u>

5) Revolving Line of Credit

SBS maintains a revolving line of credit agreement (Credit Agreement) with Wells Fargo Bank National Association. The Credit Agreement provides for borrowings for working capital and general corporate purposes of up to \$20 million and any outstanding borrowings are due and payable in full on March 28, 2006. The Credit Agreement is secured by a first priority lien on substantially all assets of SBS. Interest on borrowings is set forth in each promissory note executed under the terms of the Credit Agreement and is either payable on a variable basis at the Wells Fargo Bank prime rate or payable for a fixed rate term of either one, two or three months at a rate of LIBOR plus 1.75%. There have been no borrowings under the Credit Agreement through December 31, 2005.

The terms of the Credit Agreement, as amended, require SBS to comply with certain financial and other covenants. Effective on May 9, 2005, the Credit Agreement was amended (First Amendment to Credit Agreement) to modify the minimum tangible net worth requirement defined in Section 4.9(a) of the agreement to exclude the impact of foreign currency translation adjustments from the minimum required balance. As of December 31, 2005, SBS was in compliance with all financial covenants required under the terms of the amended Credit Agreement. In addition, SBS is required to maintain its primary operating accounts with Wells Fargo Bank or maintain a balance of not less than \$20 million on deposit with the bank. As of December 31, 2005, the Company's balance on deposit with Wells Fargo Bank was in excess of the \$20 million requirement.

6) Accrued Compensation

In fiscal 2006, in connection with our adoption of SFAS 123R on July 1, 2005, management reviewed and evaluated the potential impact of the future recognition of stock-based compensation associated with stock option grants if the Company continued to grant stock options to employees at levels consistent with prior year grants. Based on this evaluation, management recommended to the Board of Directors that the Company adopt a pay-for-performance model based on cash compensation, together with limited restricted stock award grants, as the primary form of incentive compensation for employees. This decision represents a change from our historical granting of stock options to employees as the primary form of incentive compensation. Accordingly, on July 25, 2005, the Company's Board of Directors approved the following incentive compensation plans: the SBS Technologies FY 2006 Employee Bonus Plan (FY 2006 EBP); the SBS Technologies FY 2006 Executive Incentive Plan (FY 2006 EIP); and the SBS Technologies FY 2006 Long-Term Executive Incentive Plan (FY 2006 LTEIP).

FY 2006 Employee Bonus Plan

Under the FY 2006 EBP, non-executive employees of the Company in the United States who are not covered by sales commission arrangements are entitled to receive cash bonuses depending on the achievement of certain specified performance goals. The FY 2006 EBP commenced on July 1, 2005 and concludes on June 30, 2006. Awards are targeted at 7% of an employee's eligible income as defined in the FY 2006 EBP. Individual awards will be based on the Company meeting certain specified levels of (i) revenue and (ii) earnings before interest expense, income taxes,

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

depreciation and amortization (“EBITDA”) and (iii) the achievement of individual performance goals. The specific thresholds with respect to the the Company’s performance and the percentage weighting for the required metrics under the FY 2006 EBP were approved by the Company’s Board of Directors. The FY 2006 EBP will be administered in six-month performance periods that coincide with each half of the Company’s fiscal year ending on June 30, 2006. Participants will be entitled to receive bonuses ranging from 0% to 120% of their targeted award per six-month performance period, depending on the level of the Company’s performance and the individual employee’s performance. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$412,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 EBP which is included under the caption accrued compensation in the accompanying consolidated balance sheets.

FY 2006 Executive Incentive Plan

Under the FY 2006 EIP, certain designated executives identified as participants in this plan are entitled to receive cash bonuses if the Company’s actual performance meets certain specified levels of (i) revenue and (ii) EBITDA as established by the Board of Directors, as well as (iii) the achievement of financial goals at different levels of the Company’s operating structure (referred to as “Division Goals”) and (iv) individual performance goals as established by the Chief Executive Officer. The FY 2006 EIP commenced on July 1, 2005 and concludes on June 30, 2006. The designated executives will be entitled to receive cash incentive bonus payments up to 20% of the designated executive’s eligible income as defined in the EIP for attainment of Threshold I and up to 40% of the designated executive’s eligible income for attainment of Threshold II, depending on the level of the Company’s performance, the level of financial performance of the respective employees operating group (if applicable), and the individual employee’s performance. In the event Company revenue and EBITDA performance levels at Threshold I are not achieved, there will be no bonus payment. In the event Company revenue and EBITDA performance levels attained are above Threshold I, but less than Threshold II, the percentage payouts will be adjusted appropriately based on the level of achievement. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$147,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 EIP which is included under the caption accrued compensation in the accompanying consolidated balance sheets.

FY 2006 Long-Term Executive Incentive Plan

Under the FY 2006 LTEIP, certain designated executives identified as participants in this plan are entitled to receive cash bonuses if the Company’s actual performance for average annual earnings per share growth and operating margin over the three-year period beginning July 1, 2005 and ending June 30, 2008 exceed certain performance levels (Threshold I, Threshold II, and Threshold III) as established by the Board of Directors. The Board also established and approved the relative weighting that will be used to determine the amount of the overall incentive compensation awards. The term of the LTEIP is July 1, 2005 through June 30, 2008. Performance of the Company above any Threshold but less than the next Threshold will result in a graduated proportional pay-out; below Threshold I performance results in no pay-out. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$137,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 LTEIP which is included under the caption accrued compensation in the accompanying consolidated balance sheets.

Restricted Stock Award under the FY 2006 LTEIP

Under the FY 2006 LTEIP, restricted stock awards, made out of SBS’ 1998 Long-Term Equity Incentive Plan, for 53,462 shares of the Company’s common stock were granted to certain designated executives on July 25, 2005. The restrictions on the restricted stock awards lapse on June 30, 2008, regardless of whether any cash incentive awards are paid under the LTEIP, provided the designated executive remains an employee of the Company throughout the term of the LTEIP. If a change in control of SBS occurs, the shares of restricted stock will vest on the date of the close of the change in control transaction. The restricted stock awards were issued under the terms of the Company’s 1998 Long-Term Equity Incentive Plan. See discussion regarding stock-based compensation associated with the restricted stock awards included in Note 12, “*Stock-Based Compensation*.”

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

7) Product Warranty Liability

The Company's customers receive a warranty, generally for a period of two years, upon purchase of products. The Company accrues estimated costs to repair or replace potentially defective products when products are shipped and revenue is recognized. Estimated warranty costs are based on prior warranty costs for substantially similar products. The following table presents the activity in the product warranty liability for the six months ended December 31:

Thousands	2005	2004
Balance at beginning of period.....	\$ 765	599
Estimated warranty costs for product sales.....	242	369
Adjustments to settle warranty activity.....	(245)	(276)
Balance at end of period.....	<u>\$ 762</u>	<u>692</u>

8) Accrued Consolidation Costs

On June 12, 2003, the Company announced the closure of its Carlsbad, California facility and the consolidation of its manufacturing operations into the Company's St. Paul, Minnesota facility. The costs associated with the closure included certain lease termination costs recorded on the cease use date in accordance with SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities*. The lease termination charge, recorded on the cease use date, represents the estimated fair value of the remaining future lease payments and related obligations, net of estimated sublease income, over the term of the lease. The remaining accrued costs represent primarily lease obligations expected to be paid monthly through April 2006.

9) Earnings Per Share

Net income per share is based on weighted average shares outstanding. Net income per share – assuming dilution includes the dilutive effects of potential common shares outstanding during the period.

Thousands (except per share amounts)	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Net income.....	\$ 1,064	2,156	524	3,402
Net income per share:				
Weighted-average common shares outstanding used in earnings per share computations.....	<u>15,654</u>	<u>15,527</u>	<u>15,650</u>	<u>15,516</u>
Net income per share.....	<u>\$ 0.07</u>	<u>0.14</u>	<u>0.03</u>	<u>0.22</u>
Net income per share - assuming dilution:				
Weighted-average common shares outstanding used in earnings per share computations.....	<u>15,715</u>	<u>15,763</u>	<u>15,702</u>	<u>15,714</u>
Net income per share - assuming dilution.....	<u>\$ 0.07</u>	<u>0.14</u>	<u>0.03</u>	<u>0.22</u>
Shares Used in Per Share Computations:				
Weighted average common shares outstanding.....	15,654	15,527	15,650	15,516
Incremental shares from assumed conversions - potential common shares	<u>61</u>	<u>236</u>	<u>52</u>	<u>198</u>
Shares used in computations - assuming dilution.....	<u>15,715</u>	<u>15,763</u>	<u>15,702</u>	<u>15,714</u>

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

For the three and six month periods ended December 31, 2005, options to purchase 2,871,828 and 2,871,527 shares of common stock, respectively, were outstanding but were not included in the computation of earnings per share – assuming dilution because the options' exercise prices were greater than the average market price of the common shares. For the three and six month periods ended December 31, 2004, options to purchase 1,452,869 and 1,550,059 shares of common stock, respectively, were outstanding but were not included in the computation of earnings per share – assuming dilution because the options' exercise prices were greater than the average market price of the common shares.

10) Comprehensive Income

Comprehensive income for the three and six months ended December 31, 2005 was \$0.3 million and \$4,000, respectively. Comprehensive income for the three and six months ended December 31, 2004 was \$6.8 million and \$9.1 million, respectively. The difference between comprehensive income and net income was related to foreign currency translation adjustments.

11) Segment Financial Data

The Company is engaged in the design, research, development, integration and production of embedded computer products and we operate worldwide through two operating segments: the Americas Group and the Europe Group. Both the Americas Group and the Europe Group offer our complete portfolio of embedded computer products to customers in the government, commercial and communications end markets. Each segment has management who report directly to the Company's Chief Executive Officer and its own sales and distribution channels. The Americas Group consists of the Company's operations based in the United States and Canada including the sales, engineering and test activities in Albuquerque, New Mexico; Mansfield, Massachusetts; Newark, California; Raleigh, North Carolina; St. Paul, Minnesota; and Waterloo, Ontario, Canada; the manufacturing and assembly operations located in St. Paul, Minnesota and Albuquerque, New Mexico; and the sales and support activities based in Shenzhen, China. The Europe Group consists of the Company's operations based in Germany which include the sales, engineering, test, assembly, and manufacturing activities located in Augsburg and Mindelheim, Germany.

SBS measures the results of operations for segments (segment profit (loss)) based on income before income taxes and prior to (a) the allocation of corporate overhead expenses other than marketing costs, (b) substantially all amortization associated with acquisitions and (c) interest and other income from our U.S. operations. The accounting policies used to measure segment profit (loss) are the same as those referred to in Note 1.

Thousands		Americas Group	Europe Group	Corporate & Unallocated (1)	Total
Three month periods ended December 31					
Gross sales.....	2005	\$ 23,140	18,098	-	\$ 41,238
Inter-segment sales.....		(1,877)	(2,077)	-	(3,954)
Sales to external customers.....		<u>\$ 21,263</u>	<u>16,021</u>	<u>-</u>	<u>\$ 37,284</u>
Gross sales.....	2004	\$ 28,778	18,663	-	\$ 47,441
Inter-segment sales.....		(1,726)	(3,469)	-	(5,195)
Sales to external customers.....		<u>\$ 27,052</u>	<u>15,194</u>	<u>-</u>	<u>\$ 42,246</u>
Segment profit (loss).....	2005	\$ 1,388	3,491	(3,243)	\$ 1,636
	2004	\$ 2,935	3,877	(3,495)	\$ 3,317

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

Thousands		Americas Group	Europe Group	Corporate & Unallocated (1)	Total
Six month periods ended December 31					
Gross sales.....	2005	\$ 48,442	32,400	-	\$ 80,842
Inter-segment sales.....		(5,210)	(4,210)	-	(9,420)
Sales to external customers.....		<u>\$ 43,232</u>	<u>28,190</u>	<u>-</u>	<u>\$ 71,422</u>
Gross sales.....	2004	\$ 53,816	32,221	-	\$ 86,037
Inter-segment sales.....		(3,343)	(5,564)	-	(8,907)
Sales to external customers.....		<u>\$ 50,473</u>	<u>26,657</u>	<u>-</u>	<u>\$ 77,130</u>
Segment profit (loss)	2005	\$ 2,279	5,270	(6,743)	\$ 806
	2004	\$ 5,430	6,266	(6,462)	\$ 5,234
Total assets					
	As of December 31, 2005	\$ 30,577	41,519	78,605	\$ 150,701
	As of June 30, 2005	\$ 34,349	38,067	80,042	\$ 152,458

- (1) The corporate and unallocated column includes amounts for corporate items. With regard to results of operations, corporate and unallocated includes corporate overhead expenses other than corporate marketing costs, interest income and interest expense from our U.S. operations, and substantially all amortization associated with acquisitions. Corporate assets primarily include cash and cash equivalents from our U.S. operations, deferred and current income tax assets, goodwill and intangible assets.

12) Stock-Based Compensation

Effective on July 1, 2005, the Company adopted SFAS 123R using the modified prospective method. SFAS 123R requires measurement of compensation cost for all stock-based awards at fair value on the grant date and recognition of compensation expense over the requisite service period for awards expected to vest. The fair value of stock option grants is determined using the Black-Scholes valuation model, which is consistent with our valuation techniques previously utilized for options in footnote disclosures required under SFAS No. 123, *Accounting for Stock Based Compensation*, (SFAS 123) as amended by SFAS No. 148, *Accounting for Stock-Based Compensation — Transition and Disclosure* (SFAS 148). The fair value of restricted stock awards is determined based on the number of shares granted and the quoted price of our common stock on the grant date. Such fair values will be recognized as compensation expense over the requisite service period, net of estimated forfeitures, using the accelerated method under SFAS 123R.

The fair value method under SFAS 123R is similar to the fair value method under SFAS 123 as amended by SFAS 148 with respect to measurement and recognition of stock-based compensation. However, SFAS 123 permitted us to recognize forfeitures as they occur, while SFAS 123R requires us to estimate future forfeitures and adjust our estimate on a quarterly basis. SFAS 123R also requires a classification change in the statement of cash flows; whereby, the income tax benefits from stock option exercises are reported as a financing cash flow rather than an operating cash flow as previously reported.

The Company has several Board and shareholder approved stock option plans for which stock options and restricted stock awards are available to grant to employees and directors. All employee and director stock options granted under the Company's stock option plans have an exercise price equal to the market value of the underlying common stock on the grant date. There are no vesting provisions tied to performance conditions for any options as vesting for all outstanding option grants was based only on continued service as an employee of the Company. All of the Company's outstanding stock options and restricted stock awards are classified as equity instruments.

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

On April 21, 2005, the Board of Directors of SBS approved the acceleration of the vesting of all outstanding unvested stock options with an exercise price greater than \$9.22 (the Acceleration). The Acceleration was effective for all such options outstanding on April 21, 2005, all of which were granted by the Company when the Company used the intrinsic-value method of accounting for stock options. All of the other terms and conditions applicable to such outstanding stock option grants still apply. The Company's decision to accelerate the vesting of these options was in anticipation of compensation expense to be recorded subsequent to the effective date of the Company's adoption of SFAS 123R in connection with outstanding unvested stock options issued to employees.

As a result of the Acceleration, options to purchase approximately 1.3 million shares of SBS' common stock became immediately exercisable on April 21, 2005. Due to the Acceleration, the Company will not recognize stock-based compensation expense of approximately \$2.5 million in fiscal years ending June 30, 2006 and beyond (estimated using the Black-Scholes fair value model). The stock-based compensation expense which otherwise would have been reported in future periods, has been reflected in pro forma footnote disclosures for periods prior to the adoption of SFAS 123R, as permitted under the provisions of SFAS 123 prior to its revision.

Stock Options

On the date of adoption of SFAS 123R, there were 3,397,414 outstanding stock options, of which 3,296,080 were fully vested. During the six months ended December 31, 2005, 122,094 stock options were granted to the Company's independent directors in connection with their election to serve on the Company's Board of Directors at the 2005 Annual Meeting of Shareholders. Based on the terms of the Company's stock option plans, 69,000 of these options vest upon the completion of service on the board for the 2005/2006 term in November 2006 and 53,094 of these options vest ratably on annual anniversary dates for three years from the grant date. The per share weighted average fair value of the options granted was \$4.84. The estimated fair value was determined using the Black-Scholes option valuation model with the following weighted average assumptions based on prior experience for option grants to the Company's independent directors: expected term (years) – 3.7 to 5.7; risk free interest rate – 4.4%; expected volatility – 57%; and dividend yield – 0%.

For the three and six months ended December 31, 2005, the Company recorded approximately \$101,000 and \$137,000, respectively, of stock-based compensation associated with outstanding unvested stock options in selling, general and administrative expense in the accompanying consolidated statements of operations. As of December 31, 2005, there was approximately \$682,000 of remaining unamortized stock-based compensation associated with unvested stock options which will be expensed over the remaining service periods through November 2008.

The following table summarizes our stock option activity in fiscal 2006:

	Number of options	Weighted avg Exercise Price
Outstanding at June 30, 2005	3,397,414	\$ 14.39
Granted	122,094	9.92
Exercised	716	5.44
Cancelled	112,985	18.83
Outstanding at December 31, 2005	<u>3,405,807</u>	\$ 14.08
As of December 31, 2005:		
Options exercisable	<u>3,190,713</u>	
Shares available for grant	<u>2,201,946</u>	

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements – Continued
December 31, 2005
(Unaudited)

Significant option groups outstanding and exercisable at December 31, 2005 and related weighted average price and life information follows:

Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life (yrs)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 5.44 - \$ 10.75	696,667	6.9	\$ 9.24	481,573	\$ 9.29
\$ 10.77 - \$ 12.49	871,884	7.1	12.05	871,884	12.05
\$ 12.69 - \$ 14.50	813,256	6.0	13.63	813,256	13.63
\$ 14.61 - \$ 17.00	714,500	4.2	15.77	714,500	15.77
\$ 18.22 - \$ 34.50	309,500	5.0	28.00	309,500	28.00
\$ 5.44 - \$ 34.50	<u>3,405,807</u>	6.0	\$ 14.08	<u>3,190,713</u>	\$ 14.42

Restricted Stock Awards

For the three and six months ended December 31, 2005, approximately \$101,000 and \$195,000, respectively, of stock-based compensation associated with restricted stock awards was recorded in selling, general and administrative expense in the accompanying consolidated statements of operations. As of December 31, 2005, there was approximately \$693,000 of remaining unamortized deferred compensation associated with restricted stock awards, reflected as a separate component of stockholders' equity in the accompanying consolidated condensed balance sheets, which will be expensed over the remaining service period through June 2008.

On the date of adoption of SFAS 123R, there were 17,020 outstanding restricted stock awards issued to Independent Directors in 2004 in connection with their service on the Company's Board of Directors. The restricted stock awards vested in November 2005 upon completion of the 2004/2005 term and the trading restrictions will be removed equally over a three-year period from the date of grant. The fair value of these awards was based on the closing price of the Company's common stock on the grant date. The total compensation of approximately \$249,000 was amortized to expense over the requisite service period to November 2005. For the three and six months ended December 31, 2005, the Company recorded approximately \$23,000 and \$86,000, respectively, of stock-based compensation associated with these restricted stock awards.

On July 25, 2005, restricted stock awards for 53,462 shares of the Company's common stock were granted to certain designated executives in connection with the FY 2006 LTEIP. The restricted stock awards vest on June 30, 2008 provided the designated executive remains an employee of the Company through June 30, 2008. In the event of a change in control of SBS, the shares of restricted stock will vest on the date of the close of the change in control transaction. The restricted stock awards were issued under the Company's 1998 Long-Term Equity Incentive Plan. The fair value for each of the 53,462 restricted stock awards granted was \$10 per share based on the closing price of the Company's common stock on July 25, 2005. The total compensation of \$534,620 was recorded as deferred compensation and will be amortized to expense over the requisite service period from July 2005 to June 2008. For the three and six months ended December 31, 2005, the Company recorded approximately \$46,000 and \$76,000, respectively, of stock-based compensation associated with the FY 2006 LTEIP restricted stock awards.

SBS Technologies, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements - Continued
December 31, 2005
(Unaudited)

On November 17, 2005, restricted stock awards for 26,985 shares of the Company's common stock were granted to Independent Directors in connection with their service on the Company's Board of Directors. The restricted stock awards vest upon the completion of the 2005/2006 term in November 2006 and the trading restrictions will be removed equally over a three-year period from the grant date. The fair value of these awards of \$9.96 was based on the closing price of the Company's common stock on the grant date. The total compensation of approximately \$268,800 was recorded as deferred compensation and will be amortized to expense over the requisite service period from November 2005 to November 2006. For the three and six months ended December 31, 2005, the Company recorded approximately \$33,000 of stock-based compensation associated with these restricted stock awards.

Fair Value Disclosures – Prior to Adoption of SFAS 123R

Prior to July 1, 2005, the Company accounted for stock-based awards under the intrinsic value method, which followed the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. Under this method, compensation expense was recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. Substantially all stock-based compensation reflected in reported net income related to restricted stock award grants to members of the Company's Board of Directors. The following table illustrates the effect on net income and net income per common share in prior periods if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation prior to adoption of SFAS 123R.

Thousands (except per share amounts)	Three months ended Dec. 31, 2004	Six months ended Dec. 31, 2004
Net income, as reported.....	\$ 2,156	\$ 3,402
Stock-based compensation, net of tax effects:		
Add: compensation included in reported net income.....	28	41
Deduct: compensation determined under fair value method.....	(683)	(1,062)
Pro forma net income.....	\$ <u>1,501</u>	\$ <u>2,381</u>
Net income per common share, as reported.....	\$ <u>0.14</u>	\$ <u>0.22</u>
Net income per common share, pro forma.....	\$ <u>0.10</u>	\$ <u>0.15</u>
Net income per common share - assuming dilution, as reported.....	\$ <u>0.14</u>	\$ <u>0.22</u>
Net income per common share - assuming dilution, pro forma.....	\$ <u>0.10</u>	\$ <u>0.15</u>

13) Contingencies

SBS is subject to various claims that arise in the ordinary course of its business. In the opinion of management, the amount of ultimate liability with respect to these actions will not materially affect the financial position, results of operations, or liquidity of SBS.

Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

For a description of SBS’ critical accounting policies and an understanding of the significant factors that influenced SBS’ performance during the three and six months ended December 31, 2005 and 2004, this “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (MD&A) should be read in conjunction with the consolidated financial statements, including the related notes, appearing in Item 1 of this Form 10-Q, as well as our Annual Report on Form 10-K for the year ended June 30, 2005.

Company Overview

We design and build open-architecture embedded computer products that enable OEMs to serve the government, commercial, and communications end markets. Embedded computer products are put inside or made part of larger systems to process information, control machines, move computer data between machines, and interact with people. The companies that use our products manufacture very sophisticated, expensive devices, such as MRI machines, flight simulators, wireless networks, fighter jets and industrial robots.

The SBS product line is strategically focused on embedded computing, and we serve virtually all parts of the market. We currently list more than 550 products in the product section of our website, www.sbs.com. We offer components like I/O modules, bus adapters, carrier cards, system enclosures, FPGA boards and single board computers, as well as network switches, blades and fully integrated systems. Many of these products are available in ruggedized versions, which can operate in conditions of extreme temperature, vibration, shock and humidity.

We serve a broad range of customers. We help our customers get to market faster, more reliably and more economically, by providing a wide range of standard and customized embedded computer products. Our products have application in diverse industries, including space and aviation, telecommunications, military and government, transportation, robotics, networking, broadcasting, wireless communications and medical imaging.

The embedded computer industry is highly competitive and fragmented. The size of the total addressable embedded computer market has been estimated by industry publications to be approximately \$4 billion for board-level products, exclusive of complete embedded computer systems. This market is addressed by many competitors. No single competitor holds a dominant position in the embedded computer market.

We have grown because we understand our role in the embedded computing process: we make components which are part of larger, more complicated devices. As embedded computer applications expand, we broaden our product line to meet our customers’ needs and to attract new customers. We invest in technology and customer service so that we can grow with our customers.

We have grown organically and through strategic acquisitions, acquiring companies that supplement our core competencies – a pattern we expect to continue. Our organic growth is driven by adding new products, improving existing products through our research and development program, and attracting new customers with our products and service. We have completed eleven acquisitions since 1992 that broadened our product offerings and our customer base.

Executive Summary

During the quarter ended December 31, 2005, we continued to make excellent progress in implementing our long-term growth strategy. The December quarter was the fourth consecutive quarter of increased bookings, with \$42.0 million reported. Due to the recent decision by a government customer to change its project requirements, a \$4.7 million order received in fiscal year 2005 was cancelled, resulting in net bookings for the quarter of \$37.3 million. The order cancellation was not caused by a funding issue or dissatisfaction with SBS. Total backlog at the end of the quarter was \$49.9 million.

We are beginning to see the effects of the cost control initiatives we began implementing in fiscal year 2006. These events, plus our strong backlog, have reinforced our confidence in the growth we anticipate in the second half of the fiscal year.

During the quarter and six months ended December 31, 2005:

- Sales for the quarter were \$37.3 million and sales for the six months were \$71.4 million;

On a sequential basis, total sales increased 9.2%, compared to \$34.1 million in sales for the quarter ended September 30, 2005. Sales for the six months decreased 7.4%, compared to \$77.1 million in sales for the comparable period of the prior fiscal year.

- Net income for the quarter was \$1.1 million and net income for the six months was \$524,000. Net income per share – assuming dilution for the quarter was \$0.07 compared to \$0.14 for the comparable period of the prior year. Net income per share – assuming dilution for the six months was \$0.03 compared to \$0.22 for the comparable period of the prior year.
- Customer orders received and booked during the quarter and six months were \$42.0 million and \$82.1 million, respectively. This resulted in a book-to-bill ratio of 1.13 to 1 for the quarter and a six-month book-to-bill ratio of 1.15 to 1. For the December 2005 quarter, net bookings were \$37.3 million, due to the cancellation of a \$4.7 million order received in fiscal 2005.

Book-to-bill ratio represents the net value of customer orders received and booked each period divided by total sales. Historically, 30% to 40% of our sales in each fiscal quarter will be based on orders received and booked during that same fiscal quarter, and we expect this pattern to continue.

- Order backlog was \$49.9 million as of December 31, 2005, compared to \$50.4 million at the end of the preceding quarter on September 30, 2005 and \$45.9 million as of December 31, 2004;

Order backlog represents customer orders that have been contracted for future delivery. Accordingly, these orders have not yet been recognized as revenue, but represent potential future revenue.

- We achieved fifteen design wins during the quarter, bringing the total to twenty-six for the first six months of fiscal year 2006 ended December 31, 2005. This compares with sixteen design wins achieved during the first six months of the prior fiscal year.

In the government and commercial markets, each reported design win represents a minimum initial purchase order of \$100,000; in the communications market, each reported design win represents a minimum initial purchase order of \$10,000. All design wins are forecasted to produce a minimum of \$500,000 in sales annually when in production.

By end market, the design wins included eleven in the government market, three in the communications market and one in the commercial market.

- For the quarter ended December 31, 2005, as a percentage of total sales, sales to one communications customer, Ericsson, represented 16%, and no other customer represented more than 5% of sales.

Financial Highlights

Selected financial highlights during the three and six month periods ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 follows:

Thousands (except per share amounts)	Three Months Ended				Six Months Ended			
	December 31,		%	Sept. 30,	%	December 31,		%
	2005	2004		2005		2005	2004	
Sales.....	\$ 37,284	42,246	-11.7%	\$ 34,138	9.2%	\$ 71,422	\$ 77,130	-7.4%
Net income (loss).....	\$ 1,064	2,156	-50.6%	\$ (539)	297.4%	\$ 524	\$ 3,402	-84.6%
Net income (loss) per share - assuming dilution.....	\$ 0.07	0.14		\$ (0.03)		\$ 0.03	\$ 0.22	

See detailed analysis of the financial results below.

Stock-Based Compensation

Effective on July 1, 2005, we adopted the provisions of Statement of Financial Accounting Standards No. 123R, *Share-Based Payment*, (SFAS 123R) using the modified prospective method. SFAS 123R requires measurement of compensation cost for all stock-based awards at fair value on the grant date and recognition of compensation expense over the requisite service period for awards expected to vest.

The fair value method under SFAS 123R is similar to the fair value method under SFAS No. 123, *Accounting for Stock Based Compensation*, (SFAS 123) as amended by SFAS No. 148, *Accounting for Stock-Based Compensation — Transition and Disclosure* (SFAS 148) with respect to measurement and recognition of stock-based compensation. However, SFAS 123 permitted us to

recognize forfeitures as they occur, while SFAS 123R requires us to estimate future forfeitures and adjust our estimate on a quarterly basis. SFAS 123R also requires a classification change in the statement of cash flows; whereby, the income tax benefit from stock option exercises is reported as a financing cash flow rather than an operating cash flow as previously reported.

We have several Board and shareholder approved stock option plans from which stock options and restricted stock awards are available to grant to employees and directors. All employee and director stock options granted under our stock option plans have an exercise price equal to the market value of the underlying common stock on the grant date. There are no vesting provisions tied to performance conditions for any option, as vesting for all outstanding option grants was based only on continued service as an employee of SBS. All of our outstanding stock options and restricted stock awards are classified as equity instruments.

On April 21, 2005, our Board of Directors approved the acceleration of the vesting of all outstanding unvested stock options with an exercise price greater than \$9.22 (the Acceleration). The Acceleration was effective for all such options outstanding on April 21, 2005, all of which were granted by us when we used the intrinsic-value method of accounting for stock options. All of the other terms and conditions applicable to such outstanding stock option grants still apply. Our decision to accelerate the vesting of these options was in anticipation of compensation expense to be recorded subsequent to the effective date of SFAS 123R on July 1, 2005 in connection with outstanding unvested stock options issued to employees. As a result of the Acceleration, options to purchase approximately 1.3 million shares of SBS' common stock became immediately exercisable on April 21, 2005. Due to the Acceleration, SBS will not recognize stock-based compensation expense of approximately \$2.5 million in fiscal years ending June 30, 2006 and beyond (estimated using the Black-Scholes fair value model).

Stock Options

On the date of adoption of SFAS 123R, there were 3,397,414 outstanding stock options, of which 3,296,080 were fully vested.

During the six months ended December 31, 2005, 122,094 stock options were granted to the Company's independent directors in connection with their election to serve on the Company's Board of Directors at the 2005 Annual Meeting of Shareholders. Based on the terms of the Company's stock option plans, 69,000 of these options vest upon the completion of service on the board for the 2005/2006 term in November 2006 and 53,094 of these options vest ratably on annual anniversary dates for three years from the grant date. The per share weighted average fair value of the options granted was \$4.84. The estimated fair value was determined using the Black-Scholes option valuation model with the following weighted average assumptions which are based on prior experience for option grants to the Company's independent directors: expected term (years) – 3.7 to 5.7; risk free rate of interest – 4.4%; expected volatility – 57%; and dividend yield – 0%.

For the three and six months ended December 31, 2005, we recorded approximately \$101,000 and \$137,000, respectively, of stock-based compensation associated with outstanding unvested stock options in selling, general and administrative expense. As of December 31, 2005, there was approximately \$682,000 of remaining unamortized stock-based compensation expense associated with unvested stock options which will be recognized over the remaining service period through April 2008.

Restricted Stock Awards

For the three and six months ended December 31, 2005, approximately \$101,000 and \$195,000, respectively, of stock-based compensation associated with restricted stock awards was recorded in selling, general and administrative expense. At December 31, 2005, there was approximately \$693,000 of remaining unamortized deferred compensation associated with restricted stock awards, reflected as a separate component of stockholders' equity in the accompanying consolidated condensed balance sheets, which will be recognized as stock-based compensation expense over the remaining service period through June 2008.

Managements Evaluation of Incentive Compensation Plans

In fiscal 2006, in connection with our adoption of SFAS 123R on July 1, 2005, management reviewed and evaluated the potential impact of the future recognition of stock-based compensation associated with stock option grants if we continued to grant stock options to employees at levels consistent with prior year grants. Based on this evaluation, management recommended to the Board of Directors that we adopt a pay-for-performance model based on cash compensation, together with limited restricted stock award grants, as the primary form of incentive compensation for employees. This decision represents a change from our historical granting of stock options to employees as the primary form of incentive compensation. As a result, on July 25, 2005, our Board of Directors approved the following incentive compensation plans: the SBS Technologies FY 2006 Employee Bonus Plan (FY 2006 EBP); the SBS Technologies FY 2006 Executive Incentive Plan (FY 2006 EIP); and the SBS Technologies FY 2006 Long-Term Executive Incentive Plan (FY 2006 LTEIP).

FY 2006 Employee Bonus Plan

Under the FY 2006 EBP, non-executive employees of SBS in the United States who are not covered by sales commission arrangements are entitled to receive cash bonuses depending on the achievement of certain specified performance goals. The FY 2006 EBP commenced on July 1, 2005 and concludes on June 30, 2006. Awards are targeted at 7% of an employee's eligible income as defined in the FY 2006 EBP. Individual awards will be based on SBS meeting certain specified levels of (i) revenue and (ii) earnings before interest expense, income taxes, depreciation and amortization ("EBITDA") and (iii) the achievement of individual performance goals. The specific thresholds with respect to SBS' performance and the percentage weighting for the required metrics under the FY 2006 EBP were approved by our Board of Directors. The FY 2006 EBP will be administered in six-month performance periods that coincide with each half of our fiscal year ending on June 30, 2006. Participants will be entitled to receive bonuses ranging from 0% to 120% of their targeted award per six-month performance period, depending on the level of SBS' performance and the individual employee's performance. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$412,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 EBP.

FY 2006 Executive Incentive Plan

Under the FY 2006 EIP, certain designated executives identified as participants in this plan are entitled to receive cash bonuses if our actual performance meets certain specified levels of (i) revenue and (ii) EBITDA as established by the Board of Directors, as well as (iii) the achievement of financial goals at different levels of our operating structure (referred to as "Division Goals") and (iv) individual performance goals as established by the Chief Executive Officer. The FY 2006 EIP commenced on July 1, 2005 and concludes on June 30, 2006. Designated executives will be entitled to receive cash incentive bonus payments up to 20% of the designated executive's eligible income as defined in the EIP for attainment of Threshold I and up to 40% of the designated executive's eligible income for attainment of Threshold II, depending on the level of SBS' performance, the level of financial performance of the respective employee's operating group (if applicable), and the individual employee's performance. If our revenue and EBITDA performance levels at Threshold I are not achieved, we will not make bonus payments. If our revenue and EBITDA performance levels attained are above Threshold I, but less than Threshold II, the percentage payouts will be adjusted appropriately based on the level of achievement. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$147,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 EIP.

FY 2006 Long-Term Executive Incentive Plan

Under the FY 2006 LTEIP, certain designated executives identified as participants in this plan are entitled to receive cash bonuses if our actual performance for average annual earnings per share growth and operating margin over the three-year period beginning July 1, 2005 and ending June 30, 2008 exceeds certain performance levels (Threshold I, Threshold II, and Threshold III) as established by the Board of Directors. The Board also established and approved the relative weighting that will be used to determine the amount of the overall incentive compensation awards. The term of the LTEIP is July 1, 2005 through June 30, 2008. Performance of SBS above any Threshold but less than the next Threshold will result in a graduated proportional pay-out; below Threshold I performance results in no pay-out. For the six months ended December 31, 2005, management has recorded an estimate of approximately \$137,000 for incentive compensation in fiscal 2006 in connection with the FY 2006 LTEIP.

Restricted Stock Award under the FY 2006 LTEIP

Under the FY 2006 LTEIP, restricted stock awards, made out of SBS' 1998 Long-Term Equity Incentive Plan, for 53,462 shares of the Company's common stock were granted to certain designated executives on July 25, 2005. The restrictions on the restricted stock awards lapse on June 30, 2008, regardless of whether any cash incentive awards are paid under the LTEIP, provided the designated executive remains an employee of the Company throughout the term of the LTEIP. If a change in control of SBS occurs, the shares of restricted stock will vest on the date of the close of the change in control transaction. The fair value for each restricted stock award was \$10 based on the closing price of our common stock on July 25, 2005. The total compensation for the restricted stock awards of \$534,620 will be recognized as an expense over the requisite service period from July 2005 to June 2008. For the six months ended December 31, 2005, approximately \$76,000 of stock-based compensation associated with these restricted stock awards was recorded in selling, general and administrative expenses in the accompanying consolidated statements of operations.

Results of Operations

(references to fiscal 2006 and fiscal 2005 relate to interim periods of the fiscal years ending on June 30)

The following table sets forth for the periods indicated certain operating data as a percentage of sales:

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2005	2004	2005	2004
Sales.....	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales:				
Cost of products sold.....	55.8 %	54.5 %	56.6 %	54.6 %
Amortization of intangible assets.....	0.7 %	1.1 %	0.7 %	1.1 %
Total cost of sales.....	56.5 %	55.6 %	57.4 %	55.6 %
Gross profit.....	43.5 %	44.4 %	42.6 %	44.4 %
Selling, general and administrative expense.....	22.6 %	21.6 %	23.9 %	22.2 %
Research and development expense.....	17.5 %	14.4 %	18.5 %	15.0 %
Amortization of intangible assets.....	0.1 %	0.2 %	0.2 %	0.3 %
Operating income (loss).....	3.3 %	8.2 %	-- %	6.9 %
Interest and other income, net.....	1.1 %	0.5 %	1.1 %	0.4 %
Foreign exchange gains (losses).....	0.0 %	(0.8)%	-- %	(0.5)%
	1.1 %	(0.3)%	1.1 %	(0.1)%
Income before income taxes.....	4.4 %	7.9 %	1.1 %	6.8 %
Income tax expense.....	1.5 %	2.8 %	0.4 %	2.4 %
Net income.....	2.9 %	5.1 %	0.7 %	4.4 %

Three and Six Month Periods Ended December 31, 2005 compared to the Three and Six Month Periods Ended December 31, 2004

SALES

Our total sales during the quarter and six months ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 follows:

Thousands	Three Months Ended				Six Months Ended		
	December 31,		%	Sept. 30,	December 31,		%
	2005	2004	change	2005	2005	2004	change
Sales.....	\$ 37,284	42,246	-11.7%	\$ 34,138	9.2%	\$ 71,422	\$ 77,130 -7.4%

Sales for the three and six months ended December 31, 2005 decreased compared to the same periods of the prior fiscal year due primarily to reduced sales to semiconductor manufacturing equipment customers. On a sequential basis, sales for the quarter ended December 31, 2005 increased from the prior quarter due primarily to increased sales to government customers, partially offset by slight declines in sales to commercial and communications customers.

For the quarter ended December 31, 2005, as a percentage of total sales, sales to one communications customer, Ericsson, represented 16%, and no other customer represented more than 5% of sales. For the quarter ended December 31, 2004, as a percentage of total sales, sales to one communications customer, Ericsson, represented 15%; sales to one commercial customer, Applied Materials, represented 12%; sales to another European-based communications customer represented 6%; and no other customer represented more than 5% of sales.

For the six months ended December 31, 2005, as a percentage of total sales, sales to one communications customer, Ericsson, represented 16%, sales to one commercial customer, Applied Materials, represented 6%; and no other customer represented more than 5% of sales. For the six months ended December 31, 2004, as a percentage of total sales, sales to one communications customer, Ericsson, represented 14%; sales to one commercial customer, Applied Materials, represented 12%; sales to another European-based communications customer represented 5%; and no other customer represented more than 5% of sales.

Sales by end market for the quarter and six months ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 as indicated below:

SALES BY END MARKET
(dollars in thousands)

Three months ended:	Dec. 31, 2005	% of total	Dec. 31, 2004	% of total	Sept. 30, 2005	% of total
Government.....	\$ 19,403	52%	\$ 18,805	45%	\$ 14,465	42%
Communications.....	9,977	27%	11,441	27%	10,718	31%
Commercial.....	7,904	21%	12,000	28%	8,955	27%
Total.....	<u>\$ 37,284</u>	<u>100%</u>	<u>\$ 42,246</u>	<u>100%</u>	<u>\$ 34,138</u>	<u>100%</u>
Six months ended:	Dec. 31, 2005	% of total	Dec. 31, 2004	% of total		
Government.....	\$ 33,868	47%	\$ 34,104	44%		
Communications.....	20,695	29%	20,787	27%		
Commercial.....	16,859	24%	22,239	29%		
Total.....	<u>\$ 71,422</u>	<u>100%</u>	<u>\$ 77,130</u>	<u>100%</u>		

By end market, for the quarter ended December 31, 2005, sales to government customers increased 3.2%, sales to communications customers decreased 12.8%, and sales to commercial customers decreased 34.1%, all compared to the second quarter of the prior fiscal year. On a sequential basis, sales to government customers increased 34.1%, sales to communications customers decreased 6.9%, and sales to commercial customers decreased 11.7%, all compared to the preceding quarter ended September 30, 2005. For the six months ended December 31, 2005, sales to government customers decreased 1%, sales to communications customers decreased 0.5%, and sales to commercial customers decreased 24.2%, all compared to the same period of the prior fiscal year. The reduction in sales to commercial customers in fiscal 2006 compared to fiscal 2005 was due to reduced demand from semiconductor manufacturing equipment customers.

GROSS PROFIT

Gross profit during the quarter and six months ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 follows:

Thousands	Three months ended					Six Months Ended		
	December 31,		Incr/	Sept. 30,	Incr/	December 31,		Incr/
	2005	2004	(decr)	2005	(decr)	2005	2004	(decr)
Gross profit.....	\$ 16,236	18,757	\$ (2,521)	\$ 14,218	\$ 2,018	\$ 30,455	\$ 34,234	\$ (3,779)
Gross profit as a percent of sales:								
Cost of products sold.....	55.8%	54.5%		57.6%		56.6%	54.6%	
Intangible asset amortization.....	0.7%	1.1%		0.8%		0.7%	1.1%	
Gross profit.....	43.5%	44.4%		41.6%		42.6%	44.4%	

For the three and six months of fiscal 2006 ended December 31, 2005, gross profit as a percent of sales declined from levels noted in the prior fiscal year due primarily to the overall sales mix, which resulted in an increased proportion of sales of lower margin products, and competitive pricing. Compared to the preceding quarter ended September 30, 2005, an increased proportion of higher margin government sales favorably impacted gross profit as a percentage of sales.

Consistent with our Form 10-K for the year ended June 30, 2005, we have included the amortization of intangible assets associated with completed technology and license agreements as a separate component of cost of sales. The decrease in fiscal 2006 compared with fiscal 2005 resulted from the completion of amortization of certain license agreements in June 2005.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSE

Selling, general and administrative (SG&A) expense during the quarter and six months ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 follows:

Thousands	Three Months Ended					Six Months Ended		
	December 31,		Incr/ (decr)	Sept. 30,		Incr/ (decr)	December 31,	
	2005	2004		2005	(decr)		2005	2004
SG&A expense.....	\$ 8,413	9,121	\$ (708)	\$ 8,661	(248)	\$ 17,075	\$ 17,145	(70)
As a percent of sales.....	22.6%	21.6%		25.4%		23.9%	22.2%	

The decrease in SG&A expense for the quarter ended December 31, 2005 compared to the same period of the prior fiscal year and the preceding quarter was primarily the result of benefits from cost control initiatives we began implementing in fiscal 2006. These decreases were partially offset by increased incentive compensation costs discussed previously and stock-based compensation associated with unvested stock options as a result of our adoption of the fair value method of accounting for stock options required in SFAS 123R, "Share Based Payment," effective July 1, 2005. The decline in sales in fiscal 2006 compared to fiscal 2005 negatively impacted SG&A expense as a percent of sales.

RESEARCH AND DEVELOPMENT EXPENSE

Research and development (R&D) expense during the quarter and six months ended December 31, 2005 compared to the same periods of the prior fiscal year and the preceding quarter ended September 30, 2005 follows:

Thousands	Three Months Ended					Six Months Ended		
	December 31,		Incr/ (decr)	Sept. 30,		Incr/ (decr)	December 31,	
	2005	2004		2005	(decr)		2005	2004
R&D expense.....	\$ 6,530	6,102	\$ 428	\$ 6,693	(163)	\$ 13,222	\$ 11,608	1,614
As a percent of sales.....	17.5%	14.4%		19.6%		18.5%	15.0%	

Increasing our intellectual property continues to be a key element of our growth strategy. During the quarter and six months ended December 31, 2005, we introduced 4 new products and a new product line. The increase in R&D expense for the three and six months of fiscal 2006 compared to the same periods of the prior fiscal year was primarily the result of our fiscal 2005 mid-year investment in additional engineering resources to serve the government and international markets, the timing of outside development costs associated with our product development efforts, and increased incentive compensation costs associated with the incentive compensation plans approved by the Board of Directors on July 25, 2005. On a sequential basis, R&D expense decreased slightly from the preceding quarter as a result of the timing of outside development costs associated with our product development efforts. Looking forward, we expect our R&D expense level to remain relatively constant. The decline in sales in fiscal 2006 compared to fiscal 2005 negatively impacted R&D expense as a percent of sales.

INTEREST AND OTHER INCOME, NET

Net interest and other income of \$410,000 and \$806,000 for the three and six months ended December 31, 2005, respectively, represent an increase from amounts received during the comparable periods of fiscal 2005 due primarily to improvements in interest rates earned for cash balances and increased cash balances.

FOREIGN EXCHANGE GAINS (LOSSES)

Foreign exchange gains (losses) in fiscal 2006, which represent primarily realized and unrealized losses on transactions denominated in non-functional currencies, decreased from fiscal 2005 levels primarily as a result of reduced payables in non-functional currencies and changes in the Euro to U.S. dollar exchange rates during the periods.

INCOME TAX EXPENSE

We record income tax expense based on our estimated worldwide effective tax rates for the respective fiscal years. For fiscal 2006 and 2005, our estimated worldwide effective tax rate was approximately 35.0%. Our estimated worldwide effective income tax rate incorporates a projected mix of pre-tax income from domestic and foreign sources, together with benefits from certain income tax planning strategies, including benefits from foreign sales and research and experimentation tax credits. We continue to evaluate the potential impact of the foreign dividend repatriation provisions of the American Jobs Creation Act of 2004 on our estimated worldwide effective tax rate.

In assessing the realizability of our deferred tax assets, management considers projected future sources of taxable income together with tax planning strategies. A valuation allowance has been established that applies to certain U.S. State and foreign operating loss and tax credit carryforwards that, in the opinion of management, may expire unused due to uncertainty regarding future taxable income. Based on SBS' historical taxable transactions, the timing of the reversal of existing temporary differences, and the evaluation of tax planning strategies, management believes it is more likely than not that SBS' future

AMERICAS GROUP

Thousands	Three Months Ended					Six Months Ended		
	December 31,		%	Sept. 30,		December 31,		%
	2005	2004	change	2005	change	2005	2004	change
Sales to External Customers.....	\$ 21,263	27,052	-21.4%	\$ 21,969	-3.2%	\$ 43,232	50,473	-14.3%
Segment Profit.....	\$ 1,388	2,935	-52.7%	\$ 891	55.8%	\$ 2,279	5,430	-58.0%
Segment Profit as % of Sales.....	6.5%	10.8%		4.1%		5.3%	10.8%	

Sales to External Customers. For the three and six months ended December 31, 2005, (fiscal 2006) sales to external customers declined compared to the same periods of fiscal year 2005 due primarily to reduced sales to semiconductor equipment manufacturing customers. During the three and six months ended December 31, 2005, sales to one commercial customer, Applied Materials, represented \$1.7 million and \$4.0 million, respectively, compared to \$5.1 million and \$8.9 million in the same periods of fiscal 2005 ended December 31, 2004.

Segment Profit. For the three and six months ended December 31, 2005, segment profit decreased from fiscal 2005 levels primarily as a result of decreased gross profit together with increased R&D expenses, partially offset by reduced SG&A expenses as a result of certain cost control initiatives we began to implement in fiscal 2006. The decrease in gross profit as a percent of sales was the result of a change in sales mix resulting in a higher proportion of sales of lower margin products and competitive pricing. The increased R&D expenses were due primarily to our mid-year decision in fiscal 2005 to invest in our infrastructure to pursue opportunities in the government systems market, the timing of outside development costs associated with our product development efforts, and increased incentive compensation as discussed previously.

EUROPE GROUP

Thousands	Three Months Ended					Six Months Ended		
	December 31,		%	Sept. 30,		December 31,		%
	2005	2004	change	2005	change	2005	2004	change
Sales to External Customers.....	\$ 16,021	15,194	5.4%	\$ 12,169	31.7%	\$ 28,190	26,657	5.8%
Segment Profit.....	\$ 3,491	3,877	-10.0%	\$ 1,779	96.2%	\$ 5,270	6,266	-15.9%
Segment Profit as % of Sales.....	21.8%	25.5%		14.6%		18.7%	23.5%	

Sales to External Customers. For the three and six months ended December 31, 2005, sales to external customers increased approximately \$0.8 million and \$1.5 million, respectively, both compared to the same periods of the prior fiscal year. During the three and six months ended December 31, 2005, currency exchange rates used to translate the Group's financial statements to U.S. dollars declined by 9.6% and 5.4%, respectively, compared to the same periods of the prior fiscal year. During the three and six months ended December 31, 2005, sales to one communications customer, Ericsson, represented \$5.9 million and \$11.7 million, respectively, compared to \$6.4 million and \$10.9 million in the same periods of fiscal 2005 ended December 31, 2004.

Segment Profit. For the three and six month periods ended December 31, 2005, segment profit decreased approximately \$0.4 million and \$1.0 million, respectively, both compared to the comparable periods of the prior fiscal year. The decrease was due primarily to reduced gross profit as a result of a higher mix of lower margin production orders and increases in R&D expenses commensurate with the growth in the business, partially offset by the increase in sales and decreased SG&A expenses as a result of certain cost control initiatives we began to implement in fiscal 2006.

Liquidity, Capital Resources and Financial Condition

Our objective is to maintain adequate financial resources and liquidity to finance our operations. We use a combination of proceeds from the sale or issuance of equity securities and internally generated funds to finance our working capital requirements, capital expenditures, and operations.

Our cash balance of \$53.2 million at December 31, 2005 represented a decrease of \$2.0 million during the six months ended December 31, 2005. This decrease was due primarily to the timing of cash payments and collections during the period and we do not expect this to continue; however, actual results may vary. For the six months ended December 31, 2005 and 2004, net cash flows from operating activities and proceeds from the exercise of employee stock options were the principal sources of funding, and cash was used for a mix of activities including working capital needs and capital expenditures. We anticipate that our cash sources and uses will continue in this manner during the remainder of the fiscal year ending June 30, 2006; however, future cash inflows from employee stock option exercises are generally dependent upon the amount of excess, if any, between the current market price of our common stock and the price the employee must pay to exercise the option and are therefore difficult to predict with certainty.

Cash Flows

Changes to our cash balance during the six months ended December 31, 2005, and 2004 follows:

Comparison of Condensed Consolidated Statements of Cash Flows

	Six Months Ended December 31,	
	2005	2004
	<i>Thousands</i>	
Cash Flow Provided by (Used in)		
Operating activities.....	\$ (551)	\$ 2,379
Investing activities.....	(1,232)	(1,399)
Financing activities.....	4	665
Net effect on cash from:		
Exchange rate changes.....	<u>(236)</u>	<u>943</u>

Operating Activities

Cash flows from operating activities during the six months ended December 31, 2005, were principally impacted by the timing of payments for working capital needs and cash collections from customers during the period. Operating cash flows were provided by net income and the impact of certain non-cash and non-operating activities, including depreciation and amortization expenses totaling approximately \$2.5 million and stock-based compensation costs of approximately \$332,000, of which approximately \$137,000 was the result of our adoption of SFAS 123R on July 1, 2005.

The underlying drivers of the changes in working capital during the first six months of fiscal 2006 were as follows:

- The increase in accounts receivable used operating cash of \$1.5 million, before foreign currency translation adjustments of approximately \$378,000, due principally to the timing of shipments and cash collections during the period.
- The increase in inventory used cash of \$1.1 million, before foreign currency translation adjustments of approximately \$202,000, due primarily to inventory on hand for products that are scheduled to begin production commensurate with the anticipated growth in sales during the second half of fiscal year 2006.
- The decrease in total liabilities used cash from operations of \$2.0 million, before foreign currency translation adjustments of \$57,000, due primarily to the timing of cash payments for working capital needs, partially offset by incentive compensation accruals during the period in connection with the Company's pay-for-performance incentive plans implemented in fiscal 2006.

Investing Activities

Our principal recurring investing activity is the funding of capital expenditures necessary to support the growth of our business and to enhance the productivity of our operations. During the six month period ended December 31, 2005, purchases of property and equipment were \$1.2 million.

Financing Activities

Our principal source of cash inflows from financing activities is proceeds from the issuance of common stock associated with the exercise of employee stock options.

Exchange Rates

Changes in foreign currency exchange rates during the six months ended December 31, 2005 negatively impacted our cash balances by approximately \$236,000. Due to our international operations, where transactions are recorded in functional currencies other than the U.S. dollar, the effects of changes in foreign currency exchange rates on existing cash balances during any given period result in amounts on the consolidated statements of cash flows that may not reflect the changes in the corresponding accounts on the consolidated balance sheets.

Cash Requirements

On March 30, 2005, we entered into a revolving line of credit agreement (Credit Agreement) with Wells Fargo Bank National Association. The credit agreement provides for borrowings for working capital and general corporate purposes of up to \$20 million. Any outstanding borrowings are due and payable in full on March 28, 2006. The Credit Agreement is secured by a first priority lien on substantially all assets of SBS. Interest on borrowings is set forth in each promissory note executed under the terms of the Credit Agreement and is either payable on a variable basis at the Wells Fargo Bank prime rate or payable for a fixed rate term of either one, two or three months at a rate of LIBOR plus 1.75%.

Effective on May 9, 2005, the Credit Agreement was amended (First Amendment to Credit Agreement) to modify the minimum tangible net worth requirement defined in Section 4.9(a) of the agreement to exclude the impact of foreign currency translation adjustments from the minimum required balance.

The terms of the Credit Agreement, as amended, require SBS to comply with certain financial and other covenants, including but not limited to:

- an Adjusted Tangible Net Worth balance of not less than \$109,129,000, plus 50% of quarterly net income beginning with the quarter ended March 31, 2005, excluding any loss quarters, plus all proceeds from equity offerings;

(Adjusted Tangible Net Worth defined as total stockholders' equity minus the aggregate of any intangible assets; any treasury stock; any receivables from stockholders, employees and/or affiliates; and foreign currency translation adjustments)

- a Leverage Ratio of not greater than 0.50 to 1;

(Leverage Ratio defined as total liabilities divided by Tangible Net Worth. Tangible Net Worth defined as total stockholders' equity minus the aggregate of any intangible assets; any treasury stock; and any receivables from stockholders, employees and/or affiliates)

- a Quick Ratio of not less than 1.75 to 1;

(Quick Ratio calculated as total current assets excluding inventory, divided by total current liabilities)

- an average Accounts Receivable Days Outstanding balance of no more than 90 days; and

(Accounts Receivable Days Outstanding calculated as average net trade receivables divided by net sales for the period times the number of days in reporting period)

- a requirement to maintain profitable operations defined as no more than two (2) consecutive loss quarters or a net loss for the total fiscal year.

In addition, under the terms of the Credit Agreement, we are required to maintain our primary operating accounts with Wells Fargo Bank or maintain a balance of not less than \$20 million on deposit with the bank. As of December 31, 2005, our balance on deposit with the bank was in excess of \$20 million.

As of the date of this report, we have no borrowings outstanding under the Credit Agreement and we were in compliance with all financial covenants required under the terms of the amended Credit Agreement as of December 31, 2005. In addition, we anticipate renewing this revolving Credit Agreement with Wells Fargo Bank National Association prior to the expiration of the current agreement.

We believe the funds available under the Credit Agreement and our internally generated cash flows will provide us with sufficient capital resources and liquidity to manage our operations, meet our contractual obligations, and fund capital expenditures, excluding acquisitions, for at least the next twelve months. Because long-term cash flow cannot be predicted with certainty, it is possible that we could require additional external financing in the future and that the financing may not be available on terms acceptable to us or at all.

Capital Resources

As of the date of this report, we do not have any material capital expenditure commitments.

Contractual Obligations

SBS is committed under non-cancelable operating leases for buildings and equipment that expire at various dates through fiscal 2015. There was no material change in our contractual obligations during the six months ended December 31, 2005.

Off-Balance Sheet Arrangements

As of December 31, 2005, we had no transactions that would be considered off-balance sheet arrangements in accordance with the definition under SEC rules.

Inflation

For the three and six month periods ended December 31, 2005 and 2004, we experienced no significant impact from inflation.

Business Outlook

We are pleased with the order activity we saw in the first half of the year, reinforcing our confidence in the growth we anticipate in the second half of the fiscal year. Our confidence is based on strong backlog, increases in government orders, excellent sales growth from our European markets, and, in the commercial market, recent strengthening of orders from semiconductor manufacturing equipment customers. Additionally, we are encouraged by the amount of activity in the marketplace for our AdvancedMC products, which we believe will generate increased sales in the second half of the fiscal year.

Once again, we are pleased with the results of our business development activities in the government market as indicated by the 31% increase in our government backlog since June 30, 2005. In the December quarter, we had eleven design wins and strong bookings for follow-on production for several pre-existing design wins. Increasing production orders in the government market is one of the key indicators for our anticipated second half growth.

In the communications market, we captured our first design win for AdvancedMC products. We are continuing to see strong interest in our AdvancedMC product line and expect to close more design wins during the last half of the fiscal year. In addition to the market opportunity for our AdvancedMC products in systems based on AdvancedTCA, the IBM Bladecenter, and proprietary telecommunications systems, we are well suited to serve the emerging MicroTCA market.

MicroTCA is a high performance system level form-factor comprised of AdvancedMC modules, an enclosure with cooling, and a power supply. These systems are smaller, and lower cost than the high end AdvancedTCA systems designed for the core of the network. A MicroTCA system is very attractive in a wide variety of edge applications in communications networks and is also gaining interest with both commercial and government customers who require a small high performance system.

We took an early leadership position with the introduction of our comprehensive line of AdvancedMC products at SuperComm in June 2005 and have many customers who have expressed interest in building MicroTCA systems based upon our new products. The MicroTCA specification is currently scheduled for release in the first half of calendar 2006 and we are well positioned to take an early lead in this emerging market. Market forecasts for MicroTCA systems estimated by industry publications indicate that these systems have the potential for high volume production.

As stated previously, we believe the communications market opportunities are progressing as planned, with the remainder of fiscal year 2006 targeted to capture new design wins and low rate initial production, and significant production to follow in fiscal year 2007.

In the commercial market, we are continuing to follow our strategy of developing opportunities for semiconductor manufacturing equipment, image processing, and medical electronics applications. These are segments of the market that require high performance solutions which are a good fit for our product portfolio.

Based on our backlog and our customers' forecasts, we expect sales for the third quarter of fiscal year 2006 ending March 31, 2006 to be between \$40 million and \$44 million. For the fiscal year ending June 30, 2006, we are reducing our guidance by \$5 million due to the recent order cancellation and now expect sales to be between \$160 million and \$170 million.

Management expects that corporate representatives of SBS will meet privately during the quarter with investors, investment analysts, the media and others and may reiterate the Business Outlook published in this Form 10-Q. Unless a notice stating otherwise is published or filed with the Securities and Exchange Commission on Form 8-K, the public can continue to rely on this Business Outlook as representing our current expectations on matters covered. At the same time, this Form 10-Q and the included Business Outlook will remain publicly available on our Web site (www.sbs.com).

Recently Issued Accounting Standards

In May 2005, the FASB, as part of an effort to conform to international accounting standards, issued SFAS No. 154, *Accounting Changes and Error Corrections*, (SFAS 154). SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after Dec. 15, 2005 or beginning on July 1, 2006. SFAS 154 requires that all voluntary changes in accounting principles be retrospectively applied to prior financial statements as if that principle had always been used, unless it is impracticable to do so. When it is impracticable to calculate the effects on all prior periods, SFAS No. 154 requires that the new principle be applied to the earliest period practicable. SFAS 154 also redefines "restatement" as the revising of previously issued financial statements to reflect the correction of an error. The adoption of SFAS No. 154 is not anticipated to have a material effect on our financial position or results of operations.

Item 3 – Quantitative and Qualitative Disclosures about Market Risk

Our principal investment is cash invested in either money market accounts or in overnight repurchase agreements. Due to the nature of these investments, we believe that the market risk related to these investments is minimal. As a result of our German and Canadian operating and financing activities, we are exposed to market risk from changes in foreign currency exchange rates. At present we do not utilize any derivative instruments to manage this risk.

Currency translation. The results of operations of our foreign subsidiaries are translated into U.S. dollars at the average exchange rates for each period concerned. The balance sheets of foreign subsidiaries are translated into U.S. dollars at the closing exchange rates. Any adjustments resulting from the translation are recorded as translation adjustments in other comprehensive income. Foreign currency exchange rate exposure is most significant with respect to the euro. For the three and six months ended December 31, 2005, net sales were negatively impacted by declines in foreign currency exchange rates of 9.6% and 5.4%, primarily the euro, respectively, compared to the same periods of the prior fiscal year.

Currency transaction exposure. Currency transaction exposure arises where a business or company makes actual sales and purchases in a currency other than its own functional currency. We generally source raw materials and sell our products within our local markets in their functional currencies and therefore have limited currency transaction exposure.

Item 4 – Controls and Procedures

Quarterly Controls Evaluation and Related CEO and CFO Certifications

As of the end of the period covered by this Quarterly Report on Form 10-Q, we evaluated the effectiveness of the design and operation of "disclosure controls and procedures" (Disclosure Controls). The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO).

Attached as Exhibits to this Quarterly Report on Form 10-Q are certifications of the CEO (Exhibit 31.1) and the CFO (Exhibit 31.2), which are required in accordance with Rule 13a-14 of the Securities Exchange Act of 1934 (the Exchange Act). This Controls and Procedures section includes the information concerning the controls evaluation referred to in the certifications and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

Disclosure Controls and Internal Controls

Disclosure Controls are procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the U.S. Securities and Exchange Commission's rules and forms. Disclosure Controls are also designed to ensure that the information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Internal control over financial reporting (Internal Controls) are procedures which are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America and includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of SBS; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of SBS are being made only in accordance with authorizations of management and directors of SBS; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of SBS' assets that could have a material effect on the financial statements. To the extent that components of our Internal Controls are included in our Disclosure Controls, they are included in the scope of our quarterly controls evaluation.

Limitations on the Effectiveness of Controls

Our management, including the CEO and CFO, does not expect that our Disclosure Controls or Internal Controls will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and we cannot assure that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Conclusions

Based on our controls evaluation (with the participation of our CEO and CFO), as of the end of the period covered by this report, our CEO and CFO have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) are effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

There were no changes to our internal control over financial reporting during the quarter ended December 31, 2005 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1 – Legal Proceedings

We are subject to various claims that arise in the ordinary course of our business. In our opinion, the amount of ultimate liability with respect to these actions will not materially affect our financial position, results of operations, or liquidity. We are not a party to, and none of our property is subject to, any material pending legal proceedings. We know of no material proceedings contemplated by governmental authorities.

Item 4 – Submission of Matters to a Vote of Security Holders

The following items were submitted to a vote at the Annual Meeting of Shareholders held on November 17, 2005:

- To elect seven Directors;
- To ratify the appointment of KPMG LLP as our independent registered public accountants for the fiscal year ending June 30, 2006

TABULATION OF VOTES

<u>Item Voted</u>	<u>For</u>	<u>Against or Withheld</u>	<u>Abstentions</u>	<u>Broker Non-Votes</u>
The nominees for Directors were elected based upon the following votes:				
Warren W. Andrews	14,546,197	93,293		
Lawrence A. Bennigson	14,362,102	277,388		
Peter D. Fenner	14,363,102	276,388		
Harold E. Kennedy	14,555,097	84,393		
Clarence W. Peckham	14,567,047	72,443		
Richard Szafranski	14,288,256	351,234		
Alan F. White	14,356,452	283,038		
Ratification of KPMG LLP as our independent registered public accountants for the fiscal year ending June 30, 2006	14,492,160	141,861	5,469	-

Item 6 – Exhibits

(a) Exhibits (exhibit reference numbers refer to Item 601 of Regulation S-K)

- 03.i (1) Restated Articles of Incorporation.
- 03.ii (1) Second Restated and Amended Bylaws.
- 04.a (1) Article VI of the Restated Articles of Incorporation, as included in the Restated Articles of Incorporation of SBS Technologies, Inc.
- 04.b (1) Articles I and II of the Second Restated and Amended Bylaws of SBS Technologies, Inc.
- 04.c (1) Form of certificate evidencing Common Stock.
- 04.1 (1) Rights Agreement dated September 15, 1997 between SBS Technologies, Inc. and First Security Bank (now Wells Fargo), National Association, as Rights Agent, which includes the form of Right Certificate as Exhibit A and the Summary of Rights to Purchase Common Stock as Exhibit B.2 and Agreement to Serve as Rights Agent; on January 21, 1998, pursuant to Section 21 of the Shareholder Rights Agreement dated September 15, 1997, we appointed Norwest Bank Minnesota N.A. (now Wells Fargo) as Successor Rights Agent.
- 10.be (1) 2000 Long-Term Equity Incentive Plan
- 10.cs (1) Amendment #3 to Lease between Oakview Eagan Investors, LLC (a Delaware Limited Liability Company), as successor in interest to Lutheran Brotherhood, (a Minnesota Corporation), and SBS Technologies, Inc., Commercial Group, formerly known as Bit 3 Computer Corporation, a wholly-owned subsidiary of SBS Technologies, Inc., dated July 12, 2005, together with the original lease agreement dated September 5, 1997 (the “original lease”), as amended by amendment #1 dated December 23, 1997, and amendment #2 dated May 22, 2002.
- 10.ct (1) SBS Technologies, Inc. FY 2006 Employee Bonus Plan
- 10.cu (1) SBS Technologies, Inc. FY 2006 Executive Incentive Plan
- 10.cv (1) SBS Technologies, Inc. FY 2006 Long-term Executive Incentive Plan
- 14 (1) Code of Ethics.
- 31.1 (1) Certification of the Company’s Chief Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 (1) Certification of the Company’s Chief Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 (1) Certification of the Chief Executive Officer, Pursuant to 18 U.S.C. Section 1350 As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 (1) Certification of the Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350 As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) See Exhibit Index

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.

SBS TECHNOLOGIES, INC.
(Registrant)

By: /s/ Clarence W. Peckham
Clarence W. Peckham
Chief Executive Officer

By: /s/ James E. Dixon Jr.
James E. Dixon Jr.
*Executive Vice President and
Chief Financial Officer*

Date: February 8, 2006

INDEX TO EXHIBITS

<u>Exhibit Number</u>	<u>Exhibit Description</u>	<u>Incorporated by Reference from</u>				<u>Filed Here- with</u>
		<u>Form</u>	<u>File No.</u>	<u>Exhibit</u>	<u>Fiscal period ended</u>	
3.i	Restated Articles of Incorporation dated November 10, 2000	10-Q	001-10981	3.i	9-30-2005	
3.ii	Second Restated and Amended By-laws dated November 13, 2003	10-Q	001-10981	3.ii	12-31-2003	
4.a	Article VI of the Articles of Incorporation, as amended, as included in the Articles of Incorporation of SBS Technologies, Inc.	10-Q	001-10981	4.a	9-30-2005	
4.b	Articles I and II of the Second Restated and Amended By-laws of SBS Technologies, Inc.	10-Q	001-10981	3.ii	12-31-2003	
4.c	Form of certificate evidencing Common Stock	10-Q	001-10981	4.c	3-31-2001	
4.1	Rights Agreement dated as of September 15, 1997 between SBS Technologies, Inc. and First Security Bank (now Wells Fargo), National Association, as Rights Agent, which includes the form of Right Certificate as Exhibit A, and the Summary of Rights to Purchase Common Stock as Exhibit B.2. Agreement to Serve as Rights Agent. On January 21, 1998, pursuant to Section 21 of the Rights Agreement, SBS appointed Norwest Bank Minnesota, N.A. (now Wells Fargo) as Successor Rights Agent.	10-K	001-10981	4.1	6-30-2002	
10.be	2000 Long-Term Equity Incentive Plan					X
10.cs	Amendment #3 to Lease between Oakview Eagan Investors, LLC (a Delaware Limited Liability Company), as successor in interest to Lutheran Brotherhood, (a Minnesota Corporation), and SBS Technologies, Inc., Commercial Group, formerly known as Bit 3 Computer Corporation, a wholly-owned subsidiary of SBS Technologies, Inc., dated July 12, 2005, together with the original lease agreement dated September 5, 1997 (the "original lease"), as amended by amendment #1 dated Dec. 23, 1997, and amendment #2 dated May 22, 2002.	8-K	001-10981	10.cs	7-13-2005	
10.ct	SBS Technologies FY 2006 Employee Bonus Plan.	8-K	001-10981	10.ct	7-28-2005	
10.cu	SBS Technologies FY 2006 Executive Incentive Plan.	8-K	001-10981	10.cu	7-28-2005	
10.cv	SBS Technologies FY 2006 Long-Term Executive Incentive Plan.	8-K	001-10981	10.cv	7-28-2005	
14	Code of Ethics.	8-K	001-10981	14	11-21-2003	
31.1	CEO Section 302 certification					X
31.2	CFO Section 302 certification					X
32.1	CEO Section 906 certification					X
32.2	CFO Section 906 certification					X