PHOTRONICS INC
Form 10-K
January 11, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended October 28, 2007

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ___ to ___

Commission file number 0-15451

PHOTRONICS, INC.
(Exact name of registrant as specified in its charter)

Connecticut	**06-0854886**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification Number)*

15 Secor Road, Brookfield, Connecticut 06804
(Address of principal executive offices and zip code)

(203) 775-9000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: **Common Stock, $0.01 par value per share - NASDAQ**

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No x

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 x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.
Large Accelerated Filer o Accelerated Filer x Non-Accelerated Filer o

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

As of April 29, 2007, which was the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the shares of the registrant common stock held by non-affiliates was approximately $601,210,952 (based upon the closing price of $15.38 per share as reported by the Nasdaq National Market on that date).

As of December 31, 2007, 41,886,362 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Proxy Statement for the 2008 Annual Meeting of Shareholders to be held in April 2008	Incorporated into Part III of this Form 10-K

Forward-Looking Information

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements made by or on behalf of Photronics, Inc. (the "Company"). These statements are based on management's beliefs, as well as assumptions made by and information currently available to management. Forward-looking statements may be identified by words like "expect", "anticipate", "believe", "plan", "projects", and similar expressions. All forward-looking statements involve risks and uncertainties that are difficult to predict. In particular, any statement contained in this annual report on Form 10-K, in press releases, written statements or other documents filed with the Securities and Exchange Commission, or in the Company's communications and discussions with investors and analysts in the normal course of business through meetings, phone calls and conference calls, regarding the consummation and benefits of future acquisitions, expectations with respect to future sales, financial performance, operating efficiencies and product expansion, are subject to known and unknown risks, uncertainties and contingencies, many of which are beyond the control of the Company. These factors may cause actual results, performance or achievements to differ materially from anticipated results, performances or achievements. Factors that might affect such forward-looking statements include, but are not limited to, overall economic and business conditions; the demand and receipt of orders for the Company's products; competitive factors in the industries and geographic markets in which the Company competes; changes in federal, state and international tax requirements (including tax rate changes, new tax laws and revised tax law interpretations); the Company's ability to place new equipment in service on a timely basis; interest rate fluctuations and other capital market conditions, including foreign currency rate fluctuations; economic and political conditions in international markets; the ability to obtain additional financings; the ability to achieve anticipated synergies and other cost savings in connection with acquisitions and productivity programs; uncertainties with respect to the integration and management of MP Mask Technology Center, LLC ("MP Mask"); delays in equipping, and ramp up of production of the state-of-the-art nanofab facility ("U.S. Nanofab"); the timing, impact and other uncertainties of future acquisitions; the seasonal and cyclical nature of the semiconductor and flat panel display industries; the availability of capital; management changes; damage or destruction to the Company's facilities by natural disasters, labor strikes, political unrest or terrorist activity; the ability to fully utilize its tools; the ability of the Company to receive desired yields, pricing, product mix, and market acceptance of its products; changes in technology; and the ability of the Company to obtain necessary export licenses. Any forward-looking statements should be considered in light of these factors. Accordingly, there is no assurance that the Company's expectations will be realized. The Company does not assume responsibility for the accuracy and completeness of the forward-looking statements and does not assume an obligation to provide revisions to any forward-looking statements.

PART I

ITEM 1. BUSINESS

General

Photronics, Inc. (the "Company") is a Connecticut corporation, organized in 1969. Its principal executive offices are located at 15 Secor Road, Brookfield, Connecticut 06804, telephone (203) 775-9000. Photronics, Inc. and its subsidiaries are collectively referred to herein as "Photronics" or the "Company." The Company's website is located at http://www.photronics.com. The Company makes available, free of charge through its website, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after such materials are electronically filed or furnished to the Securities and Exchange Commission. The information contained or incorporated in the Company's website is not part of these documents.

Photronics is one of the world's leading manufacturers of photomasks, which are high precision photographic quartz plates containing microscopic images of electronic circuits. Photomasks are a key element in the manufacture of semiconductors and flat panel displays ("FPD"), and are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates during the fabrication of integrated circuits ("IC") and a variety of FPDs and, to a lesser extent, other types of electrical and optical components. The Company operates principally from ten manufacturing facilities, two of which are located in the United States, three in Europe, two in Taiwan, and one each in Korea, Singapore and China. Also, under a build-to-suit lease, in the first quarter of fiscal 2008, a capital lease agreement commenced with Micron Technology, Inc. ("Micron") for a state-of-the-art nanofab facility ("U.S. Nanofab") in Boise, Idaho.

Manufacturing Technology

The Company manufactures photomasks, which are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates. The Company's photomasks are manufactured in accordance with circuit designs provided on a confidential basis by its customers. The typical manufacturing process for a photomask involves the receipt and conversion of circuit design data to manufacturing pattern data. A lithography system then exposes the circuit pattern onto the photomask blank. The exposed areas are developed and etched to produce that pattern on the photomask. The photomask is inspected for defects and conformity to the customer design data, any defects are repaired, any required pellicles (protective translucent cellulose membranes) are applied and, after final inspection, the photomask is shipped to the customer.

The Company currently supports customers across the full spectrum of IC production and large area technologies by manufacturing photomasks using electron beam or optical-based technologies. Electron beam and laser-based systems are the predominant technologies used for photomask manufacturing. These technologies are capable of producing the finer line resolution, tighter overlay and larger die size for the larger and more complex circuits currently being designed. Electron beam and laser generated photomasks can be used with the most advanced processing techniques to produce the most advanced semiconductor devices intended for use in an array of products. These include devices used for microprocessors, memory, telecommunications and related applications. The Company currently owns a number of high-end and mature electron beam and laser-based systems. The production of photomasks by the optical method is less expensive and less precise than those manufactured on high-end electron beam systems.

The first several layers of photomasks are sometimes required to be delivered by the Company within 24 hours from the time it receives customers' design data. The ability to manufacture high quality photomasks within short time periods is dependent upon efficient manufacturing methods, high yield and high equipment reliability. The Company works to meet these requirements by making significant investments in manufacturing and data processing systems and statistical process control methods to optimize the manufacturing process and reduce cycle times.

Quality control is an integral part of the photomask manufacturing process. Photomasks are manufactured in temperature, humidity and particulate controlled clean rooms because of the high level of precision, quality and yields required. Each photomask is inspected several times during the manufacturing process to ensure compliance with customer specifications. The Company continues to make substantial investments in equipment to inspect and repair photomasks to ensure that customer specifications are met. After inspection and any necessary repair, the Company utilizes proprietary processes to clean the photomasks prior to shipment.

The vast majority of photomask units produced for the semiconductor industry employ geometries of 130 nanometer or larger for ICs, and Generation 6 technologies or lower for FPDs. At these geometries, the Company can produce full lines of photomasks and there is no significant technology employed by the Company's competitors that is not available to the Company. Semiconductor fabrication also occurs below the 90 nanometer range for IC photomask technology and Generation 7 and above for FPD photomask technology. The Company is currently capable of producing a selective range of photomasks at these smaller geometries. However, as is typical of industries in the midst of technological change, some of the Company's competitors may be able to achieve higher manufacturing yields than the Company when producing these smaller geometry photomasks, in part because these competitors may have completed more cycles of learning than the Company in this area, and in part because of the Company's need to replicate production of these complex photomasks at its many locations worldwide. The Company believes that these cases are few and are not material to its business.

Sales and Marketing

The market for photomasks primarily consists of domestic and international semiconductor and FPD manufacturers and designers, including a limited number of manufacturers who have the capability to manufacture photomasks. Generally, the Company and each of its customers engage in a qualification and correlation process before the Company becomes an approved supplier. Thereafter, the Company typically negotiates pricing parameters for a customer's orders based on the customer's specifications. Some prices may remain in effect for an extended period. In some instances, the Company enters into sales arrangements, based on the understanding that, as long as the Company's performance is competitive, the Company will receive a specified percentage of that customer's photomask requirements.

The Company conducts its sales and marketing activities primarily through a staff of full-time sales personnel and customer service representatives who work closely with the Company's management and technical personnel. In addition to the sales personnel at the Company's manufacturing facilities, the Company has sales offices throughout the United States, Europe and Asia.

The Company supports international customers through both its domestic and international facilities. The Company considers its presence in international markets important to attracting new customers, providing global solutions to its existing customers, and serving customers that utilize manufacturing foundries outside of the United States, principally in Asia. For a statement of the amount of net sales, operating income or loss, and identifiable assets attributable to each of the Company's geographic areas of operations, see Note 16 to the Company's consolidated financial statements.

Customers

The Company primarily sells its products to leading semiconductor and FPD manufacturers. The Company's largest customers during the fiscal year ended October 28, 2007 ("fiscal 2007"), included the following:

Atmel Corp.	Magnachip Semiconductor
AU Optronics Corp.	Maxim Integrated Products, Inc.
Chartered Semiconductor Manufacturing, Ltd.	National Semiconductor Corporation
Fairchild Semiconductor Intl., Inc.	NXP Semiconductors
Freescale Semiconductor, Inc.	Samsung Electronics Co., Ltd.
HannStar Display Corp.	Skyworks Solutions, Inc.
IM Flash Technologies, LLC	ST Microelectronics, Inc.
Jazz Semiconductor, Inc.	Systems on Silicon Mfg. Co., Pte. Ltd.
Jenoptik Laser, Optik, Systeme GmbH	Texas Instruments Incorporated
LG Philips LCD Co., Ltd.	United Microelectronics Corp.

During fiscal year 2007, the Company sold its products and services to approximately 600 customers. Samsung Electronics Co., Ltd. accounted for approximately 25%, 25% and 24% of the Company's net sales in fiscal 2007, 2006 and 2005, respectively. This included sales of both IC and FPD photomasks. The Company's five largest customers, in the aggregate, accounted for approximately 43% in fiscal 2007, 46% in fiscal 2006 and 42% in fiscal 2005, of net sales. A significant decrease in the amount of sales to any of these customers could have a material adverse effect on the financial performance and business prospects of the Company.

Seasonality

The Company's quarterly revenues can be affected by the seasonal purchasing of its customers. The Company is typically impacted during its first fiscal quarter by the North American and European holiday periods as some customers reduce their effective workdays and orders during this period. Additionally, the Company can be impacted during its first or second quarter by the Asian New Year holiday period which also may reduce customer orders. For fiscal 2008, the Asian New Year holiday will be in the Company's second fiscal quarter, as it was in fiscal 2007. At times, the Company's first quarter revenues have been down sequentially by as much as 10%. During the past three years, the second quarter resulted in increased sequential revenues of 3% to 12%.

Research and Development

The Company conducts its primary research and development activities in the MP Mask Technology Center, LLC ("MP Mask") joint venture operation and in site-specific research and development programs in various locations around the world, primarily at its research and development centers at PK, Ltd. ("PKL") and Photronics Semiconductor Mask Corporation ("PSMC"). The MP Mask research and development programs coupled with site specific research and development initiatives are designed to advance the Company's leadership in technology and manufacturing efficiency. The Company also conducts research and development activities to support advanced product integration including but not limited to numerical modeling and simulation of photomask processes, fabrication, and delivery of product prototypes for next generation customer needs and development of software tools and workflows necessary for effective integration of the most advanced mask-based optical lithography solutions. Currently, research and development photomask activities are focused on 65, 45 and 32 nanometer node IC technology and Generation 8 FPD technology. The Company believes these core competencies will continue to be a critical part of semiconductor manufacturing as optical lithography continues to scale device capabilities at and below 90 nanometer. The Company has incurred research and development expenses of $17.3 million, $27.3 million and $32.2 million in fiscal 2007, 2006 and 2005, respectively. The Company believes that it owns or controls valuable proprietary information necessary for its business as presently conducted. This includes trade secrets as well as patents. Recently, the Company has either applied for or been granted patents pertaining to its manufacturing processes. The Company believes that its intellectual property is and will continue to be important to the Company's technical leadership in the field of photomasks.

Patents and Trademarks

The Company owns or has rights to approximately 34 patents in the United States. The general subject matter of these patents relates to the manufacture of photomasks themselves and the use of photomasks to manufacture other products. The expiration dates of these patents range from 2011 to 2023. Additionally, pursuant to the technology license agreement with Micron, the Company has access to certain technology of Micron and MP Mask. The Company also has a number of trademarks and trademark registrations in the United States and in other countries.

While the Company believes that its intellectual property is, and will continue to be, important to the Company's technical leadership in the field of photomasks, the Company's operations are not dependent on any one individual patent. The Company protects its intellectual property rights regarding products and manufacturing processes through patents and trade secrets. The Company also relies on non-disclosure agreements with employees and vendors to protect its intellectual property and proprietary processes.

Materials, Supplies and Equipment

Raw materials used by the Company generally include high precision quartz plates (including large area plates), which are used as photomask blanks, primarily obtained from Japanese and Korean suppliers; pellicles and electronic grade chemicals, which are used in the manufacturing process; and compacts, which are durable plastic containers in which photomasks are shipped. These materials are generally sourced from several suppliers and the Company is not dependent on any one supplier for its raw materials. The Company believes that its utilization of a select group of strategic suppliers enables it to access the most advanced materials technologically available. On an ongoing basis, the Company continues to consider additional supplier sources.

The Company relies on a limited number of equipment suppliers to develop and supply the equipment used in the photomask manufacturing process. Although the Company has been able to obtain equipment on a timely basis, the inability to obtain equipment when required could adversely affect the Company's business and results of operations. The Company also relies on these and additional suppliers to develop future generations of manufacturing systems to support the Company's requirements.

Backlog

The first several levels of a set of photomasks for a circuit pattern at times are often required to be shipped within 24 hours of receiving a customer's designs. Because of the short period between order and shipment dates (typically from 1 day to 2 weeks) for a significant amount of the Company's sales, the dollar amount of current backlog is not considered to be a reliable indication of future sales volume.

International Operations

International sales were approximately 75%, 73% and 69% of the Company's sales in fiscal 2007, 2006 and 2005, respectively. The Company believes that maintaining significant international operations requires it to have, among other things, a local presence in the markets in which it operates. This requires a significant investment in financial, management, operational and other resources.

Operations outside the United States are subject to inherent risks, including fluctuations in exchange rates, political and economic conditions in various countries, unexpected changes in regulatory requirements, tariffs and other trade barriers, difficulties in staffing and managing international operations, longer accounts receivable collection cycles and potentially adverse tax consequences. These factors may have a material adverse effect on the Company's ability to generate sales outside the United States and, consequently, on its business and results of operations.

Note 16 of the notes to the Company's consolidated financial statements reports net sales, operating income (loss) and total identifiable assets by geographic region.

Competition

The photomask industry is highly competitive and most of the Company's customers utilize multiple photomask suppliers. The Company's ability to compete depends primarily upon the consistency of product quality and timeliness of delivery, as well as pricing, technical capability and service. The Company also believes that proximity to customers is an important factor in certain markets where cycle time from order to delivery is critical. Certain competitors have substantially greater financial, technical, sales, marketing and other resources than the Company. The Company believes that consistency of product quality, timeliness of delivery and price are the principal factors considered by customers in selecting their photomask suppliers. The Company's inability to meet these requirements could adversely affect its sales. The Company believes that it is able to compete effectively because of its dedication to customer service, its investment in state-of-the-art photomask equipment and facilities and its experienced technical employees.

The Company estimates that for the types of photomasks it manufactures (IC and FPD) the size of the total market (captive and merchant) is approximately $3.5 billion. Competitors include Compugraphics, Inc., Dai Nippon Printing Co., Ltd., Hoya Corporation, Taiwan Mask Corporation, Toppan Printing Co., Ltd. and Toppan Chungwha Electronics. The Company also competes with semiconductor manufacturers' captive photomask manufacturing operations that supply photomasks for internal use and, in some instances, also for external customers and foundries. The Company expects to face continued competition, which in the past has led to pressure to reduce prices, which the Company believes contributed to the decrease in the number of independent manufacturers. This pressure to reduce prices may continue in the future.

Employees

As of October 28, 2007, the Company and its majority-owned subsidiaries had approximately 1,540 full-time and part-time employees. The Company believes it offers competitive compensation and other benefits and that its employee relations are good. None of the Company's employees were represented by a union as of October 28, 2007, however, effective the beginning of January 2008, certain employees in the United Kingdom are represented by a union.

ITEM 1A. RISKS RELATING TO THE COMPANY'S BUSINESS

The Company is dependent on the semiconductor industry which as a whole is volatile and could have a negative material impact on its business.

The Company sells substantially all of its photomasks to semiconductor designers, manufacturers and foundries, as well as to other high performance electronics manufacturers. The Company believes that the demand for photomasks depends primarily on design activity rather than sales volume from products using photomask technology. Consequently, an increase in semiconductor sales does not necessarily result in a corresponding increase in photomask sales. In addition, the reduced use of customized ICs, a reduction in design complexity or other changes in the technology or methods of manufacturing or designing semiconductors or a slowdown in the introduction of new semiconductor designs could reduce demand for photomasks even if demand for semiconductors increases. Further, advances in design and production methods for semiconductors and other high performance electronics could reduce the demand for photomasks. Historically, the semiconductor industry has been volatile, with sharp periodic downturns and slowdowns. These downturns have been characterized by, among other things, diminished product demand, excess production capacity and accelerated erosion of selling prices.

The Company's sales of photomasks for use in fabricating high performance electronic products such as FPDs decreased in fiscal 2007 as compared to fiscal 2006. The Company's results may suffer if the FPD photomask market does not grow or if the Company is unable to serve this market successfully. As is the case with semiconductor photomask demand, the Company believes that demand for photomasks for FPDs depends primarily on design activity, and to a lesser extent upon an increase in the number of production facilities used to manufacture FPDs. As a result, an increase in FPD sales will not necessarily lead to a corresponding increase in photomask sales. The technology for fabricating FPDs continues to develop in order to increase the size and improve the resolution of FPDs. A slowdown in the development of new technologies for fabricating FPDs could reduce the demand for related photomasks even if demand for FPDs increases.

The Company's quarterly operating results fluctuate significantly and may continue to do so in the future which could adversely impact the Company's business.

The Company has experienced fluctuations in its quarterly operating results and anticipates that such fluctuations will continue and could intensify in the future. Fluctuations in operating results may result in volatility in the prices of the Company's securities, particularly its common stock and securities linked to the value of the Company's common stock. Operating results may fluctuate as a result of many factors, including size and timing of orders and shipments, loss of significant customers, product mix, technological change, fluctuations in manufacturing yields, competition and general economic conditions. The Company operates in a high fixed cost environment and to the extent its revenues and asset utilization increase or decrease, operating margins will be positively or negatively impacted. The Company's customers generally order photomasks on an as needed basis, and substantially all of the Company's net sales in any quarter are dependent on orders received during that quarter. Since the Company operates with little backlog and the rate of new orders may vary significantly from month-to-month, the Company's capital expenditures and expense levels are based primarily on sales forecasts. Consequently, if anticipated sales in any quarter do not occur when expected, capital expenditures and expense levels could be disproportionately high, and the Company's operating results would be adversely affected. Due to the foregoing factors, the Company believes that period-to-period comparisons of its operating results are not necessarily meaningful and that these comparisons cannot be relied upon as indicators of future performance. In addition, in future quarters the Company's operating results could be below the expectations of public market analysts and investors, which, in turn, could materially adversely affect the market prices of the Company's common stock and of the debt securities.

The Company's industry is subject to rapid technological change and might fail to remain competitive which could have a material adverse effect on the Company's business and results of operations.

The photomask industry has been and is expected to continue to be characterized by technological change and evolving industry standards. In order to remain competitive, the Company will be required to continually anticipate, respond to and utilize changing technologies of increasing complexity in both traditional and emerging markets that it serves. In particular, the Company believes that, as semiconductor geometries continue to become smaller and FPDs become larger with improved performance, it will be required to manufacture increasingly complex photomasks. Additionally, demand

for photomasks has been, and could in the future be adversely affected by changes in methods of fabricating semiconductors and high performance electronics (that could affect the type or quantity of photomasks utilized), such as changes in semiconductor demand that favor field programmable gate arrays and other semiconductor designs that replace application-specific ICs. Additionally, increased market acceptance of alternative methods of IC designs onto semiconductor wafers, such as direct-write lithography, could reduce or eliminate the need for photomasks entirely in the production of semiconductors. Through fiscal 2007, direct-write lithography has not been proven to be a commercially viable alternative to photomasks, as it is considered too slow for high volume semiconductor wafer production. However, should direct-write or any other alternative methods of transferring IC designs to semiconductor wafers without the use of photomasks achieve market acceptance, the Company's business and results of operations would be materially adversely affected. If the Company is unable to anticipate, respond to or utilize these or other changing technologies, due to resource, technological or other constraints, its business and results of operations could be materially adversely affected.

Further, should sales volumes decrease based upon the flow of design releases from the Company's customers, the Company may have excess or underutilized production capacity that could significantly impact operating margins, or result in write-offs from asset impairments.

The Company's operations will continue to require substantial capital, which it may be unable to obtain.

The manufacture of photomasks requires substantial investments in high-end manufacturing capability at existing and new facilities. The Company expects that it will be required to continue to make substantial capital expenditures to meet the technological demands of its customers and to position it for future growth. The Company's capital expenditure payments for fiscal 2008 are expected to be in the range of $120 million to $150 million, of which $70 million was accrued as of October 28, 2007, though the range may be greater should conditions warrant. The Company cannot provide assurance that it will be able to obtain the additional capital required in connection with its operations on reasonable terms, if at all, or that any such expenditure will not have a material adverse effect on its business and results of operations.

The Company's agreements with Micron have several risks; should either company not comply or execute under these agreements it could significantly disrupt the Company's business and technology activities which could have a material effect on the Company's operations or cash flows.

On May 5, 2006, Photronics and Micron entered into a joint venture known as MP Mask. The joint venture develops and produces photomasks for leading-edge and advanced next generation semiconductors. As part of the formation of the joint venture, Micron contributed its existing photomask technology center located at its Boise, Idaho, headquarters to MP Mask and Photronics has paid Micron $127.5 million through October 28, 2007, and a final amount of $7.5 million is payable to Micron on May 5, 2008 in exchange for a 49.99% interest in MP Mask and a license for photomask technology of Micron and certain supply agreements. In 2007, the Company invested an additional $3.5 million in MP Mask for capital expenditure and working capital purposes.

In the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab for $61.7 million principal amount. Photronics' total investment in the purchase and equipping of its U.S. Nanofab is expected to fall within a range of $190 million to $200 million and may include redeployment of some existing Photronics assets. The U.S. Nanofab is expected to begin production in the first quarter of calendar 2008.

Failure by Photronics or Micron to comply or execute under any of these agreements, to capitalize on the use of existing technology or to further develop technology could result in a significant disruption to the Company's business and technology activities, and could adversely affect the Company's operations and cash flows.

The Company has been dependent on sales to a limited number of large customers; the loss of any of these customers or any reduction in orders from these customers could have a material adverse effect on its sales and results of operations.

Historically, the Company has sold a significant proportion of photomasks to a limited number of IC and FPD manufacturers. During fiscal 2007, one customer, Samsung Electronics Co., Ltd, accounted for approximately 25% of the Company's net sales. The Company's five largest customers, in the aggregate, accounted for 43% of net sales in fiscal 2007, 46% in fiscal 2006, and 42% in fiscal 2005. None of the Company's customers has entered into a long-term agreement with the Company requiring them to purchase the Company's products. The loss of a significant customer or any reduction or delay in orders from any significant customer, including reductions or delays due to customer departures from recent buying patterns, or market, economic or competitive conditions in the semiconductor or FPD industries, could have a material adverse effect on the Company's financial performance and business prospects. The continuing consolidation of semiconductor manufacturers may increase the likelihood and adverse effect of losing a significant customer.

The Company depends on a small number of suppliers for equipment and raw materials and, if the Company's suppliers do not deliver their products to them, the Company may be unable to deliver its products to its customers, which could adversely affect its business and results of operations.

The Company relies on a limited number of photomask equipment manufacturers to develop and supply the equipment it uses. These equipment manufacturers currently require lead times of up to 12 months between the order and the delivery of certain photomask imaging and inspection equipment. The failure of such manufacturers to develop or deliver such equipment on a timely basis could have a material adverse effect on the Company's business and results of operations. Further, the Company relies on equipment manufacturers to develop future generations of manufacturing equipment to meet its requirements. In addition, the manufacturing equipment necessary to produce advanced photomasks could become prohibitively expensive.

The Company uses high precision quartz photomask blanks, pellicles, and electronic grade chemicals in its manufacturing processes. There are a limited number of suppliers of these raw materials, and the Company has no long-term contract for the supply of these raw materials. Any delays or quality problems in connection with significant raw materials, particularly photomask blanks, could cause delays in shipments of photomasks, which could adversely affect the Company's business and results of operations. The fluctuation of exchange rates with respect to prices of significant raw materials used in manufacturing also could have a material adverse effect on the Company's business and results of operations, although they have not been material to date.

The Company faces risks associated with complex manufacturing processes, including the use of sophisticated equipment and manufacturing processes with complex technologies; should the Company be unable to effectively utilize such processes and technologies it could have a material adverse effect on its business and results of operations.

The Company's complex manufacturing processes require the use of expensive and technologically sophisticated equipment and materials and are continuously modified in an effort to improve manufacturing yields and product quality. Minute impurities, defects or other difficulties in the manufacturing process can lower manufacturing yields and make products unmarketable. Moreover, manufacturing leading-edge photomasks is more complex and time consuming than manufacturing less advanced photomasks, and may lead to general delays in the manufacturing of all levels of photomasks. The Company has, on occasion, experienced manufacturing difficulties and capacity limitations that have delayed the Company's ability to deliver products within the time frames contracted for by its customers. The Company cannot provide assurance that it will not experience these or other manufacturing difficulties, or be subject to increased costs or production capacity constraints in the future, any of which could result in a loss of customers or could otherwise have a material adverse effect on its business and results of operations.

In 2007, the Company completed construction of a new photomask manufacturing facility in Shanghai, China and, in the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab. The Company cannot provide assurance that these facilities will ramp up to anticipated production levels or that they will not experience any production or other difficulties.

The Company's prior and future acquisitions may entail certain operational and financial risks.

The Company has made significant acquisitions throughout its history. Acquisitions have focused on increasing its manufacturing presence in Asia, including its acquisition of PSMC, a Taiwanese photomask manufacturer, in 2000 and PKL, a Korean photomask manufacturer, in 2001 and increasing the technology base through the MP Mask joint venture between Photronics and Micron in 2006. The Company may make additional acquisitions in the future. Acquisitions place significant demands on the Company's administrative, operational and financial personnel and systems. Managing acquired operations entails numerous operational and financial risks, including difficulties in the assimilation of acquired operations, diversion of management's attention from other business concerns, managing assets in multiple geographic regions, amortization of acquired intangible assets and potential loss of key employees of acquired operations. Sales of acquired operations also may decline following an acquisition, particularly if there is an overlap of customers served by the Company and the acquired operation, and these customers transition to another vendor in order to ensure a second source of supply. Furthermore, the Company may be required to utilize its cash reserves and/or issue new securities for future acquisitions, which could have a dilutive effect on its earnings per share.

The Company operates in a highly competitive industry; should the Company be unable to meet its customers requirements for product quality, timelines of delivery or technical capabilities, it could adversely affect its sales.

The photomask industry is highly competitive, and most of the Company's customers utilize more than one photomask supplier. The Company's competitors include Compugraphics, Inc., Dai Nippon Printing Co., Ltd., Hoya Corporation, Taiwan Mask Corporation, Toppan Printing Co., Ltd. and Toppan Chungwha Electronics. The Company also competes with semiconductor manufacturers' captive photomask manufacturing operations. The Company expects to face continued competition from these and other suppliers in the future. Many of the Company's competitors have substantially greater financial, technical, sales, marketing and other resources than it does. Also, some of the Company's competitors may be able to more rapidly develop, produce, and achieve higher manufacturing yields than the Company, when producing smaller geometry photomasks. The Company believes that consistency of product quality and timeliness of delivery, as well as price, technical capability and service, are the principal factors considered by customers in selecting their photomask suppliers. The Company's inability to meet these requirements could adversely affect its sales. In the past, competition led to pressure to reduce prices which, the Company believes, contributed to the decrease in the number of independent manufacturers. This pressure to reduce prices may continue in the future. In addition, certain semiconductor manufacturers such as International Business Machines Corporation, Taiwan Semiconductor Manufacturing Company, Samsung Electronics Co., Ltd. and LG Phillips LCD Co., Ltd. possess their own captive facilities for manufacturing photomasks. Also, certain semiconductor manufacturers market their photomask manufacturing services to outside customers as well as to their internal organizations.

The Company's substantial international operations are subject to additional risks.

International sales accounted for approximately 75% of the Company's net sales for fiscal 2007, 73% in fiscal 2006, and 69% in fiscal 2005. The Company believes that maintaining significant international operations requires it to have, among other things, a local presence in the markets in which it operates. This requires a significant investment of financial, management, operational and other resources. Since 1996, the Company has significantly expanded its operations in international markets by acquiring existing businesses in Europe, establishing manufacturing operations in Singapore, acquiring majority equity interests in photomask manufacturing operations in Korea and Taiwan and building a new manufacturing facility for FPD photomasks in Taiwan and a new photomask manufacturing facility in Shanghai, China. As the served market continues to shift to Asia, the Company will continue to assess its manufacturing base and may close or open new facilities to adapt to these market conditions.

Operations outside the United States are subject to inherent risks, including fluctuations in exchange rates, political and economic conditions in various countries, unexpected changes in regulatory requirements, tariffs and other trade barriers, difficulties in staffing and managing international operations, longer accounts receivable payment cycles and potentially adverse tax consequences. These factors may have a material adverse effect on the Company's ability to generate sales outside the United States and, consequently, on its business and results of operations.

The Company's operating results are influenced by the performance of Asian economies which have been volatile and subject to fluctuations in local currencies, which could have a material adverse impact on the Company's financial position and results of operations.

In fiscal 2007, the Company derived approximately 58% of its net sales from Asia, compared to 56% in fiscal 2006 and 53% in fiscal 2005. As the Company continues to expand its operations in Asia, it expects sales in Asia will continue to represent a significant portion of its overall revenue mix. As a result, its business is exposed to risks presented by Asian economies. In recent years, Asian economies have been highly volatile and recessionary, resulting in significant fluctuations in local currencies, declining asset values and other instabilities. These instabilities may continue for some time or worsen, which could have a material adverse impact on its financial position and results of operations. Asian economies may also be adversely affected by the outbreak of the bird flu and any recurring outbreak of severe acute respiratory syndrome (SARS) in the region and by other geopolitical risks.

The Company's business depends on management and technical personnel, who are in great demand.

The Company's success, in part, depends upon key managerial, engineering and technical personnel, as well as its ability to continue to attract and retain additional personnel. The loss of certain key personnel could have a material adverse effect upon the Company's business and results of operations. There can be no assurance that the Company can retain its key managerial, engineering and technical employees or that it can attract similar additional employees in the future. The Company believes that it provides competitive compensation and incentive packages to its employees.

The Company may be unable to enforce or defend its ownership and use of proprietary technology.

The Company believes that the success of its business depends more on its proprietary technology, information and processes and know-how than on its patents or trademarks. Much of its proprietary information and technology relating to manufacturing processes is not patented and may not be patentable. The Company cannot offer assurance that:

* it will be able to adequately protect its technology;

* competitors will not independently develop similar technology; or

* international intellectual property laws will adequately protect its intellectual property rights.

The Company may become the subject of infringement claims or legal proceedings by third parties with respect to current or future products or processes. Any such claims or litigation, with or without merit, to enforce or protect its intellectual property rights or to defend the Company against claimed infringement of the rights of others could result in substantial costs, diversion of resources and product shipment delays or could force the Company to enter into royalty or license agreements rather than dispute the merits of these claims. Any of the foregoing could have a material adverse effect on the Company's business, results of operations and financial position.

The Company may be unprepared for changes to environmental laws and regulations and may have liabilities arising from environmental matters.

The Company is subject to numerous environmental laws and regulations that impose various environmental controls on, among other things, the discharge of pollutants into the air and water and the handling, use, storage, disposal and clean-up of solid and hazardous wastes. Changes in these laws and regulations may have a material adverse effect on the Company's financial position and results of operations. Any failure by the Company to adequately comply with these laws and regulations could subject it to significant future liabilities.

In addition, these laws and regulations may impose clean-up liabilities on current and former owners and operators of real property without regard to fault and these liabilities may be joint and several with other parties. In the past, the Company has been involved in remediation activities relating to its properties. The Company believes, based upon current information, that environmental liabilities relating to these activities or other matters will not be material to its financial statements. However, there can be no assurances that the Company will not incur any material environmental liabilities in the future.

The Company's production facilities could be damaged or disrupted by a natural disaster or labor strike.

The Company's facilities in Taiwan are located in a seismically active area. In addition, a major catastrophe such as an earthquake or other natural disaster or labor strikes or work stoppages at any of the Company's manufacturing facilities could result in a prolonged interruption of its business. Any disruption resulting from these events could cause significant delays in shipments of the Company's products and the loss of sales and customers.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None

ITEM 2. DESCRIPTION OF PROPERTY

The following table presents certain information about the Company's photomask manufacturing facilities:

Location	Type of Interest	
Allen, Texas	Owned	
Boise, Idaho	Leased	(1)
Brookfield, Connecticut (Building #1)	Owned	
Brookfield, Connecticut (Building #2)	Owned	
Bridgend, South Wales	Leased	
Cheonan, Korea	Owned	
Dresden, Germany	Leased	
Hsinchu, Taiwan	Leased	
Manchester, England	Owned	
Shanghai, China	Owned	(2)
Singapore	Leased	
Taichung, Taiwan	Owned	(2)

(1) In the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab.

(2) The Company owns its manufacturing facilities in Shanghai and Taichung, however, it leases the related land.

The Company believes that its existing manufacturing facilities are suitable and adequate for its present purposes. The Company also leases various sales offices. The Company's administrative headquarters are located in Brookfield, Connecticut in a building that it owns.

ITEM 3. LEGAL PROCEEDINGS

The Company is subject to various claims that arise in the ordinary course of business. The Company believes such claims, individually or in the aggregate, will not have a material adverse effect on the business of the Company.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of the Company's security holders during the fourth quarter of fiscal 2007.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED SHAREHOLDERS' MATTERS

The Common Stock of the Company is traded on the NASDAQ Stock Market, Inc. ("NASDAQ") under the symbol PLAB. The table below shows the range of high and low sale prices per share for each quarter for fiscal year 2007 and 2006, as reported on the NASDAQ.

	High	Low
Fiscal Year Ended October 28, 2007:		
Quarter Ended January 28, 2007	$16.97	$13.68
Quarter Ended April 29, 2007	16.88	15.00
Quarter Ended July 29, 2007	15.96	14.14
Quarter Ended October 28, 2007	14.54	10.38
Fiscal Year Ended October 29, 2006:		
Quarter Ended January 29, 2006	$19.04	$14.80
Quarter Ended April 30, 2006	20.50	16.58
Quarter Ended July 30, 2006	19.46	13.51
Quarter Ended October 29, 2006	15.38	13.00

On December 31, 2007, the closing sale price for the Common Stock as reported by NASDAQ was $12.47. Based on information available to the Company, the Company believes it has approximately 13,000 beneficial shareholders.

The Company has not paid any cash dividends to date and, for the foreseeable future, anticipates that earnings will continue to be retained for use in its business. Further, the Company's revolving credit facility ("credit facility") precludes it from paying cash dividends.

The information regarding the Company's equity compensation required to be disclosed by Item 201(d) of Regulation S-K is incorporated by reference from the Company's 2008 definitive Proxy Statement into Item 12 of Part III of this report.

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data is derived from the Company's audited consolidated financial statements. The data should be read in conjunction with the audited consolidated financial statements and notes thereto and other financial information included elsewhere in this Form 10-K (in thousands, except per share amounts):

Year Ended

	October 28, 2007	October 29, 2006	October 30, 2005	October 31, 2004	November 2, 2003
OPERATING DATA:					
Net sales	$421,479	$454,875	$440,770	$395,539	$348,884
Cost and expenses:					
Cost of sales	(321,958)	(307,851)	(295,649)	(260,232)	(250,687
Selling, general and administrative	(61,507)	(62,215)	(54,295)	(53,487)	(56,154
Research and development	(17,300)	(27,337)	(32,152)	(30,520)	(29,965
Consolidation, restructuring and related charges	-	(15,639) (a)	-	-	(42,000
Gain on sale of facility	2,254	-	-	-	-
Operating income (loss)	22,968	41,833	58,674	51,300	(29,922
Other income (expense):					
Interest expense	(5,928)	(11,916)	(10,885)	(14,723)	(17,089
Investment and other income, net	6,844	15,469	7,556 (b)	4,468 (c)	5,346
Income (loss) before income tax benefit (provision) and minority interest	23,884	45,386	55,345	41,045	(41,665
Income tax benefit (provision)	3,178	(10,462)	(10,058)	(5,761)	(924
Minority interest in income of consolidated subsidiaries	(2,539)	(5,592)	(6,634)	(10,818)	(5,573
Net income (loss)	$ 24,523	$ 29,332 (a)	$ 38,653 (b)	$ 24,466 (c)	$(48,162
Earnings (loss) per share:					
Basic	$0.59	$0.71 (a)	$1.09 (b)	$0.75 (c)	$(1.50
Diluted	$0.56	$0.66 (a)	$0.95 (b)	$0.68 (c)	$(1.50
Weighted average number of common shares outstanding:					
Basic	41,539	41,369	35,519	32,564	32,144
Diluted	51,282	51,072	45,256	42,339	32,144

BALANCE SHEET DATA:

	As of				
	October 28, 2007	October 29, 2006	October 30, 2005	October 31, 2004	November 2, 2003
Working capital	$96,606	$127,691	$300,557	$240,401	$256,872
Property, plant and equipment, net	531,578	443,637	412,429	396,461	387,977
Total assets	1,059,780	1,045,683	945,729	858,210	863,903
Long-term debt	191,253	170,288	238,949	315,888	368,307
Shareholders' equity	654,284	614,282	561,875	349,473	308,329

(a) Includes consolidation charges of $15.6 million after tax in connection with the closure of the Company's Austin, Texas manufacturing and research and development facility.

(b) Includes early extinguishment charge of $1.7 million in connection with the early redemption of $64.4 million of the Company's 4.75% convertible notes.

(c) Includes early extinguishment charge of $1.2 million in connection with the early redemption of $48.5 million of the Company's 4.75% convertible notes.

(d) Includes consolidation charge of $42.0 million in connection with the closure of the Company's Phoenix, Arizona manufacturing facility and the consolidation of the Company's North American operating infrastructure.

(e) Includes early extinguishment charge of $0.9 million in connection with the early redemption of $62.1 million of the Company's 6% convertible notes.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations for the Years Ended October 28, 2007, October 29, 2006 and October 30, 2005

Overview

The Company sells substantially all of its photomasks to semiconductor designers and manufacturers, and manufacturers of FPDs. Photomask technology is also being applied to the fabrication of other higher performance electronic products such as photonics, micro-electronic mechanical systems and certain nanotechnology applications. Thus, the Company's selling cycle is tightly interwoven with the development and release of new semiconductor designs and flat panel applications, particularly as it relates to the semiconductor industry's migration to more advanced design methodologies and fabrication processes. The Company believes that the demand for photomasks primarily depends on design activity rather than sales volumes from products produced using photomask technologies. Consequently, an increase in semiconductor or FPD sales does not necessarily result in a corresponding increase in photomask sales. In addition, the reduced use of customized ICs, reductions in design complexity or other changes in the technology or methods of manufacturing semiconductors or a slowdown in the introduction of new semiconductor or FPD designs could reduce demand for photomasks even if demand for semiconductors and FPDs increases. Advances in semiconductor and photomask design and semiconductor production methods could reduce the demand for photomasks. Historically, the semiconductor industry has been volatile, with sharp periodic downturns and slowdowns. These downturns have been characterized by, among other things, diminished product demand, excess production capacity and accelerated erosion of selling prices.

The global semiconductor industry is driven by end markets which have been closely tied to consumer driven applications for high performance semiconductor devices including, but not limited to communications and mobile computing solutions. The Company cannot predict the timing of the industry's transition to volume production of next generation technology nodes or the timing of up and down cycles with precise accuracy, but believes that such transitions and cycles will continue into the future, beneficially and adversely affecting its business, financial condition and operating results in the near term. The Company's ability to remain successful in these environments is based upon achieving its goals of being a service and technology leader, an efficient solutions supplier, and a company able to continually reinvest in its global infrastructure.

As of December 2007, state-of-the-art production for semiconductor masks is considered to be 45 nanometer for ICs, and Generation 7 to Generation 8 process technologies for FPDs, while 65 nanometer has moved into volume production. 130 and above nanometer and Generation 3 through Generation 6 process technologies for FPDs constitute the majority of high performance designs being fabricated in volume today. The Company expects there to be an increase in 65 nanometer designs moving to wafer fabrication throughout fiscal 2008 and believes it is well positioned to service an increasing volume of this business through investments in manufacturing processes and technology in the global regions where its customers are located. In 2005 and 2006, the Company experienced growth in demand for FPD photomasks, which it currently supplies from its facilities in Korea and Taiwan. In December 2006, the Company completed construction of its manufacturing facility in Shanghai, China, which began production in the second quarter of the Company's 2007 fiscal year.

The photomask industry has been, and is expected to continue to be, characterized by technological change and evolving industry standards. In order to remain competitive, the Company will be required to continually anticipate, respond to and utilize changing technologies. In particular, the Company believes that, as semiconductor geometries continue to become smaller, it will be required to manufacture even more complex optically-enhanced reticles, including optical proximity correction and phase-shift photomasks. Additionally, demand for photomasks has been, and could in the future be adversely affected by changes in methods of semiconductor manufacturing (which could affect the type or quantity of photomasks utilized), such as changes in semiconductor demand that favor field programmable gate arrays and other semiconductor designs that replace application-specific ICs. Through fiscal 2007, the Company has not experienced a significant loss of revenue as a result of alternative semiconductor design methodologies. Additionally, increased market acceptance of alternative methods of transferring circuit designs onto semiconductor wafers, such as direct-write lithography, could reduce or eliminate the need for photomasks. Through fiscal 2007, direct-write lithography has not been proven to be a commercially viable alternative to photomasks, as it is considered too slow for high volume semiconductor wafer production. However, should direct-write or any other alternative methods of transferring IC designs to semiconductor wafers be done without the use of photomasks, the Company's business and results of operations would be materially adversely affected. If the Company is unable to anticipate, respond to, or utilize these or other changing technologies, due to resource, technological or other constraints, its business and results of operations could be materially adversely affected.

Both revenues and costs have been affected by the increased demand for high-end technology photomasks that require more advanced manufacturing capabilities but generally command higher average selling prices ("ASP"). To meet the technological demands of its customers and position the Company for future growth, the Company continues to make substantial investments in high-end manufacturing capability both at existing and new facilities. The Company's cash payments for capital expenditures for new facilities and equipment to support its customers' requirements for high-end technology products aggregated approximately $310 million for the three fiscal years ended

October 28, 2007, resulting in significant increases in operating expenses. Based on the anticipated technological changes in the industry, the Company expects these trends to continue. In 2006, the Company invested $135 million in the MP Mask joint venture, and technology license and related agreements, and will continue to invest in advanced technologies.

The manufacture of photomasks for use in fabricating ICs and other related products built using comparable photomask-based process technologies has been, and continues to be, capital intensive due to the need to maintain a technology-based infrastructure. The Company's integrated global manufacturing network and employees, which consist of ten current manufacturing sites, plus commencement of a capital lease agreement in the first quarter of fiscal 2008 for the U.S. Nanofab, which is scheduled to begin production during the first quarter of calendar 2008, represent a significant portion of its fixed operating cost base. Should sales volumes decrease based upon the flow of design releases from the Company's customers, the Company may have excess or underutilized production capacity that could significantly impact operating margins, or result in write-offs from asset impairments.

The vast majority of photomasks produced for the semiconductor industry employ geometries of 130 nanometers or larger for ICs, and Generation 6 technologies or lower for FPDs. At these geometries, the Company can produce full lines of photomasks and there is no significant technology employed by the Company's competitors that is not available to the Company. Semiconductor fabrication also occurs below 90 nanometer for ICs, and Generation 7 and above for FPDs. The Company is currently capable of producing a selective range of photomasks at these smaller geometries, and has begun accelerating its efforts to support the development and production of photomasks for 65, 45 and 32 nanometer technology nodes in semiconductors and Generation 8 in FPD. However, as is typical of industries in the midst of technological change, some of the Company's competitors may be able to achieve higher manufacturing yields than the Company when

producing these smaller geometry photomasks, in part because these competitors may have completed more cycles of learning than the Company in this area and in part because of the Company's need to replicate production of these complex photomasks at its four advanced technology locations worldwide, and at its U.S. Nanofab.

On May 5, 2006, Photronics and Micron entered into the MP Mask joint venture, which develops and produces photomasks for leading-edge and advanced next generation semiconductors. As part of the formation of the joint venture, Micron contributed its existing photomask technology center located at its Boise, Idaho, headquarters to MP Mask and Photronics has paid Micron $127.5 million through October 28, 2007, and a final payment of $7.5 million is due to Micron on May 5, 2008, in exchange for a 49.99% interest in MP Mask and a license for photomask technology of Micron and certain supply agreements. In 2007, the Company invested an additional $3.5 million in MP Mask for capital expenditure and working capital purposes.

In the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab for a total cost of $61.7 million (total payments under the capital lease are $73.9 million of which $12.2 million represents interest). Photronics' total investment in the purchase and equipping of its U.S. Nanofab is expected to fall within a range of $190 million to $200 million and may include the redeployment of some existing Photronics assets. The U.S. Nanofab is expected to begin production during the first quarter of calendar 2008.

In March of 2006, the Company further streamlined its operating infrastructure in North America by closing the Austin, Texas manufacturing and research and development center and relocating certain development and manufacturing work to other facilities within the global network. The Company incurred total restructuring charges of $15.6 million in its fiscal year ended October 29, 2006. In January 2007, the Company sold its Austin, Texas manufacturing and research and development facility for proceeds of $5.0 million and realized a gain of $2.3 million.

Results of Operations

The following table represents selected operating information expressed as a percentage of net sales:

	Year Ended		
	October 28, 2007	**October 29, 2006**	**October 30, 2005**
Net sales	100.0%	100.0%	100.0%
Cost of sales	(76.4)	(67.7)	(67.1)
Gross margin	23.6	32.3	32.9
Selling, general and administrative expenses	(14.6)	(13.7)	(12.3)
Research and development expenses	(4.1)	(6.0)	(7.3)
Consolidation, restructuring and related charges	-	(3.4)	-
Gain on sale of facility	0.5	-	-
Operating income	5.4	9.2	13.3
Interest expense	(1.4)	(2.6)	(2.5)
Investment and other income, net	1.6	3.4	1.8
Income before income tax benefit (provision) and minority interest	5.6	10.0	12.6
Income tax benefit (provision)	0.8	(2.3)	(2.3)
Minority interest	(0.6)	(1.3)	(1.5)
Net income	5.8%	6.4%	8.8%

Note: All the following tabular comparisons, unless otherwise indicated, are for the fiscal years ended October 28, 2007 (2007), October 29, 2006 (2006) and October 30, 2005 (2005), in millions of dollars.

Net Sales

				Percent Change	
	2007	**2006**	**2005**	**2007 to 2006**	**2006 to 2005**
FPD	$ 82.1	$ 99.8	$ 79.3	(17.7)%	25.9%
IC	339.4	355.1	361.5	(4.4)	(1.8)

Total net sales	$421.5	$454.9	$440.8	(7.3)%	3.2%

Net sales for 2007 decreased 7.3% to $421.5 million as compared to $454.9 million for 2006. The decrease is related to reducedsales of FPD photomasks of $17.7 million associated with decreased ASPs primarily for high-end FPD photomasks; and reduced sales of IC photomasks of $15.7 million as a result of a decline in ASPs, primarily from mainstream products. High-end photomask applications, which typically have higher ASPs, include mask sets for FPD products using G6 and above technologies and IC products using 90 nanometer and below technologies. During 2007, sales of high-end photomasks totaled $92 million as compared to $91 million in 2006. Total sales of high-end FPD masks decreased by $18 million, while sales of high-end IC photomasks increased by $19 million. By geographic area, net sales in 2007 as compared to 2006 decreased by $9.8 million or 3.9% in Asia, by $15.2 million or 12.4% in North America, and by $8.4 million or 10.5% in Europe. As a percent of total sales in 2007, sales were 58% in Asia, 25% in North America, and 17% in Europe. By geographic area, 2007 compared to 2006, net sales in Asia decreased $9.8 million or 3.9%, North American sales decreased $15.2 million or 12.4%, and European sales decreased $8.4 million or 10.5%.

Net sales for 2006 increased 3.2% to $454.9 million as compared to fiscal year 2005, due principally to increased sales of FPD photomasks, as a result of increased consumer demand for FPD applications. This increase was somewhat mitigated by decreased sales of IC photomasks of 1.8% as a result of reduced demand for mainstream IC photomasks. Total sales of high-end photomasks, which include FPD and IC, increased to 35% in 2006 as compared to 21% in 2005. FPD revenue for 2006 increased to $99.8 million as compared to $79.3 million in 2005. High-end technology applications typically have higher ASPs, for both IC and FPD photomasks. High-end photomask applications include mask sets for semiconductor designs at and below 130 nanometer for ICs, and for FPD products using G6 and above technologies. By geographic area, 2006 compared to 2005, net sales in Asia increased $19.9 million or 8.6%, North American sales decreased $12.6 million or 9.3%, and European sales increased $6.8 million or 9.3%.

Gross Margin

				Percent Change	
	2007	**2006**	**2005**	**2007 to 2006**	**2006 to 2005**
Gross margin	$99.5	$147.0	$145.1	(32.3)%	1.3%
Gross margin %	23.6%	32.3%	32.9%	-	-

Gross margin decreased to 23.6% in 2007 from 32.3% in 2006 primarily due to decreased ASPs for both IC and FPD photomasks and the Company's increased manufacturing base in Asia. The Company operates in a high fixed cost environment and to the extent that the Company's revenues and utilization increase or decrease, gross margin will be positively or negatively impacted. The gross margin percentage for fiscal 2008 could be negatively impacted by increased depreciation expense associated with the Company's recent capital expenditures, principally for its U.S. Nanofab and for PKL, its subsidiary in Korea.

Gross margin decreased slightly to 32.3% of net sales for 2006 as compared to 32.9% in 2005 as a result of the Company's increased infrastructure and expanded manufacturing capability which includes increased high-end IC manufacturing capability and increased FPD capacity, principally with the opening of the Taiwan FPD facility.

Selling, General and Administrative Expenses

				Percent Change	
	2007	**2006**	**2005**	**2007 to 2006**	**2006 to 2005**
S,G&A expense	$61.5	$62.2	$54.3	(1.1)%	14.6%
% of net sales	14.6%	13.7%	12.3%	-	-

Selling, general and administrative expenses decreased by $0.7 million or 1.1% to $61.5 million in 2007 from $62.2 million in 2006. The decrease was primarily due to decreased compensation expense, which was partially offset by start-up expenses related to the U.S. Nanofab.

Selling, general and administrative expenses increased 14.6% in 2006 as compared to 2005, primarily due to the Company's expanded Asian infrastructure, which includes expansion in Shanghai, China and Taichung, Taiwan, and increased stock compensation expenses of $1.3 million related to the Company's 2006 adoption of Statement of Financial Accounting Standards ("SFAS") No. 123(R).

Research and Development

				Percent Change	
	2007	**2006**	**2005**	**2007 to 2006**	**2006 to 2005**
R&D expense	$17.3	$27.3	$32.2	(36.7)%	(15.0)%
% to net sales	4.1%	6.0%	7.3%	-	-

Research and development expenditures consist primarily of global development efforts of high-end process technologies for advanced sub-wavelength reticle solutions for IC and FPD technologies. Research and development expenses decreased in both 2007 and 2006 as compared to each prior year as a result of cost savings associated with the 2006 closure of the Company's Austin, Texas research and development operations, which were in part offset by amortization expenses of the fair value of the agreement to license technology from Micron.

Consolidation, Restructuring and Related Charges

In the second quarter of 2006, the Company continued to streamline its operating infrastructure in North America by ceasing the manufacture and research and development of photomasks at its Austin, Texas facility. The Company recorded total restructuring charges of $15.6 million in 2006, primarily comprised of $14.3 million related to the impairment of facilities and equipment and $1.3 million relating to workforce reductions of approximately 95 employees in the United States.

The Company continues to assess its global manufacturing strategy as its sales volume continues to grow in Asia.

This ongoing assessment could result, in the future, in facilities closures, asset redeployment, workforce reductions, and the addition of increased manufacturing facilities, all of which would be predicated by market conditions and customer requirements.

Gain on Sale of Facility

In January 2007, the Company sold its Austin, Texas manufacturing and research and development facility for proceeds of $5.0 million and realized a gain of $2.3 million.

Other Income (Expense)

	2007	2006	2005
Interest expense	$(5.9)	$(11.9)	$(10.9)
Investment and other income, net	6.8	15.5	7.6
Total other income (expense)	$ 0.9	$ 3.6	$ (3.3)

Interest expense decreased in 2007 as compared to 2006, primarily as a result of the Company's repaying the remaining outstanding balance of its $87.1 million, 4.75% convertible subordinated notes upon maturity on December 15, 2006. Investment and other income net, for 2007, decreased as compared to 2006, primarily due to reduced foreign currency gains and reduced investment income associated with reduced investment balances. Further, realized gains on the sales of investments and other assets were $0.9 million in 2007 as compared to $3.6 million in 2006.

Interest expense increased in 2006 as compared to 2005 due to increases in interest rates as the Company's interest rate swap contract effectively converted $100 million of its 4.75% fixed rate convertible subordinated notes to a variable rate. Investment and other income increased in 2006 as compared to 2005 primarily due to foreign currency transaction gains of $4.3 million in 2006 as compared to $1.6 million in 2005; net realized gains on the sales of certain investments of $3.6 million in 2006 as compared to $0.1 million in 2005; and interest income of $6.8 million in 2006 as compared to $4.2 million in 2005. Further, investment and other income, net, for 2005 includes early extinguishment charges of $1.7 million relating to the redemption of $64.4 million of the Company's 4.75% convertible subordinated notes.

Income Tax Benefit (Provision)

	2007	2006	2005
Income tax benefit (provision)	$3.2	$(10.5)	$(10.1)
Effective income tax rate	13.3%	(23.1)%	(18.2)%

The Company's operations have followed the recent migration of semiconductor industry fabrication to Asia, where the Company operates in countries where it is accorded favorable tax treatments. PKLT, the Company's FPD manufacturing facility in Taiwan, is accorded a tax holiday which expires in December 2012. In addition, the Company has been accorded a tax holiday in China which is expected to expire in 2011. In Korea, various investment tax credits have been utilized to reduce the Company's effective income tax rate. The Company's tax returns are subject to periodic examination by the tax authorities in the various jurisdictions in which it operates. The Company regularly assesses the potential outcomes of ongoing and future examinations and has provided accruals for tax contingencies in accordance with SFAS No. 5, "Accounting for Contingencies."

The income tax benefit for the fiscal year ended October 28, 2007 was $3.2 million or 13.3% of pretax income, which differs from the federal statutory income tax expense rate of 35%, primarily as a result of a recognized tax benefit of $7.4 million and to a lesser extent available tax credits in Korea. During the fiscal year ended October 28, 2007, the Company recorded a tax benefit in the amount of $7.4 million relating to the resolution and settlement of U.S. and foreign tax matters that were associated with certain tax positions in prior years.

The provision for income taxes for the fiscal year ended October 29, 2006 was $10.5 million on a pre-tax income of $45.4 million. The provision differs from the federal statutory rate of 35% as a result of Taiwan's tax holiday, available tax credits in Korea, and valuation reserves on losses generated in the United States.

The Company evaluates the recoverability of deferred tax assets from future taxable income and establishes valuation allowances if recovery is deemed not likely. The valuation allowance increased $2.4 million and $1.7 million in fiscal 2007 and 2006, respectively.

The availability of tax holidays in some Asian jurisdictions did not have a significant impact on the Company's decision to close some of its North American facilities nor in the Company's increased Asian presence which is in response to fundamental changes taking place in the semiconductor industry that the Company serves. As semiconductor fabrication has migrated to Asia, in large part from the United States, the Company has followed, in order to avoid a severe loss of business.

Minority Interest in Consolidated Subsidiaries

Minority interest in consolidated subsidiaries, which represents the minority interest in earnings of the Company's non-wholly owned subsidiaries in Taiwan and Korea, was $2.5 million in fiscal year 2007 as compared to $5.6 million in fiscal year 2006. The decrease in minority interest expense is due to decreased net income of the Company's non-wholly owned subsidiary in Taiwan. The Company's ownership in its subsidiary in Korea was 99.7% at October 28, 2007 and October 29, 2006, and 96.5% at October 30, 2005. The Company's ownership in its subsidiary in Taiwan was 58% at October 28, 2007, October 29, 2006 and October 30, 2005. The Company increased its ownership in its subsidiary in Korea from 75.0% to 96.5% during fiscal 2005 for cash of approximately $58.2 million, and further increased its ownership to 99.7% in 2006 for cash of approximately $8.5 million.

Liquidity and Capital Resources

	October 28, 2007	**October 29, 2006**	**October 30, 2005**
	(in millions)	*(in millions)*	*(in millions)*

Cash and cash equivalents	$146.0	$129.4	$196.0
Short-term investments	5.7	69.9	90.6
Total	$151.7	$199.3	$286.6
Net cash provided by operating activities	$134.7	$ 116.2	$ 142.6
Net cash used in investing activities	$(29.7)	$(201.2)	$(185.5)
Net cash (used in) provided by financing activities	$(89.8)	$ 13.5	$ 98.6

The Company's working capital decreased $31.1 million to $96.6 million as of the end of fiscal 2007, as compared to $127.7 million at the end of fiscal 2006. The decrease was partially related to reduced short-term investments and accounts receivables due to decreased sales in 2007. Additionally, in 2007 there was an increase in accounts payable, primarily related to $51.6 million of increased accrued capital expenditures compared to the prior year. During fiscal 2007 the Company paid off $87.1 million of the remaining outstanding balance of the Company's 4.75% convertible subordinated notes which matured on December 15, 2006.

Cash provided by operating activities was $134.7 million for fiscal 2007, as compared to $116.2 million for fiscal 2006. This increase was primarily due to lower accounts receivable balances associated with decreased 2007 sales as well as increases in accounts payable partially offset by decreased accrued liabilities.

Cash used in investing activities in fiscal 2007 decreased to $29.7 million, as compared to $201.2 million in 2006, primarily as a result of the initial payment of $120 million to Micron for the investment in MP Mask and related technology license and supply agreements having been made in fiscal 2006 and a decrease in the purchase of short-term investments from $82.6 million in 2006 to $4.2 million in 2007. Capital expenditures for the fiscal years ended 2007, 2006, and 2005 were $94.1 million, $94.6 million and $121.4 million, respectively. The Company expects capital expenditure payments for fiscal 2008 to be approximately $120 million to $150 million, primarily to continue the expansion of its high-end IC manufacturing capability.

In 2007, cash used in financing activities was $89.8 million, which is primarily related to the Company's redeeming its $87.1 million outstanding 4.75% convertible subordinated notes in December 2006. In 2006, cash provided by financing activities was $13.5 million, which was primarily a result of net proceeds from long-term debt of $11.7 million to support the start-up of the new facility in China.

On June 6, 2007, the Company entered into a credit agreement with a group of financial institutions that provides for a 5-year, credit facility with an aggregate commitment of $155 million at October 28, 2007. In connection therewith, the Company has classified its $150 million, 2.25% convertible subordinated notes due April 15, 2008 as long-term. The credit facility allows for borrowings in various currencies. The applicable interest rate spread and facility fee vary based upon the Company's senior leverage ratio. Under the terms of the credit facility, the Company is subject to compliance with certain financial and other covenants, as defined, including, but not limited to: Senior Leverage Ratio, Total Leverage Ratio and Minimum Unrestricted Cash Balances; and limits the amount of both secured and unsecured debt. The credit facility is secured by a pledge of the Company's stock in certain of its subsidiaries. Borrowings under the credit facility bear interest at a LIBOR rate, as defined, plus 87 basis points. As of October 28, 2007, $3.3 million of the credit facility was utilized for a standby letter of credit, and the remaining balance of $151.7 million was available to the Company.

The Company's commitments represent investments in the tooling of the U.S. Nanofab, additional manufacturing capacity, as well as advanced equipment for the production of high-end, more complex photomasks in Asia, principally Korea. At October 28, 2007, the Company had capital commitments outstanding of approximately $66 million, primarily related to equipment for its U.S. Nanofab facility and equipment in Korea, plus $61.7 million principal amount for a build-to-suit capital lease through 2012 for its U.S. Nanofab facility. The Company will use its working capital and its credit facility to finance its capital expenditures. Photronics believes that its currently available resources, together with its capacity for growth, and its access to other debt and equity financing sources, will be sufficient to satisfy its currently planned capital expenditures, as well as its anticipated working capital requirements for the 2008 fiscal year. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed cash available from operations and existing cash, short-term investments and its credit facility.

Cash Requirements

The Company's cash requirements in fiscal 2008 will be primarily to fund operations, including spending on capital expenditures, MP Mask commitments, and debt service, including its $150 million, 2.25% subordinated convertible notes due April 15, 2008, as well as any cash acquisitions that it may undertake. The Company expects that cash, cash equivalents and short-term investments and cash generated from operations, along with borrowings under its $155 million credit facility, along with access to other debt and equity financing sources, if needed, will be sufficient to meet its cash requirements for the next 12 months. The Company regularly reviews the availability and terms on which it might issue additional equity or debt securities in the public or private markets. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed cash available from operations, cash available under its credit facility, existing cash and short-term investments.

Contractual Cash Obligations

The following table quantifies the Company's future contractual obligations as of October 28, 2007 (in millions):

	Payments Due				
	Total	**Less Than 1 Year**	**1 - 3 Years**	**3 - 5 Years**	**More Than 5 Years**
Long-term borrowings	$175.8	$150.9	$24.9	$ -	$ -
Operating leases	8.2	2.5	2.9	1.8	1.0
Capital leases	81.6	15.0	30.9	35.7	-
Unconditional purchase obligations	78.0	71.1	6.9	-	-

Interest	21.8	7.7	11.1	3.0	-
Total	$365.4	$247.2	$76.7	$40.5	$1.0

Certain Transactions

The Company has a 49.99% ownership interest in the MP Mask joint venture that was established in 2006 with Micron. Since the Company does not control this venture, the Company does not consolidate the results. As part of the joint venture, various supply agreements exist between the Company, Micron, and MP Mask. As of October 28, 2007, the Company owed MP Mask $6.4 million and had a receivable from Micron of $6.1 million primarily related to the supply agreements. During 2007, the Company recognized net revenue of $2.1 million related to commissions earned under supply agreements between the Company, Micron and MP Mask; comprised of gross commission income of $3.9 million less $1.8 million of amortization of the value of the supply agreement intangible asset. The gross commission revenue includes $56.3 million in orders from Micron less the Company's cost of the corresponding orders placed with MP Mask in the amount of $52.4 million. In addition, in 2007 the Company incurred outsourcing expenses of $1.0 million from MP Mask for research and development activities purchased by the Company. Further, the Company recorded cost of sales in the amount of $3.7 million for photomasks produced by MP Mask for sales to the Company's customers in 2007. As of October 29, 2006, the Company owed MP Mask $8.7 million and had a receivable from Micron of $8.3 million. During 2006, the Company recognized net revenue of $1.0 million related to commissions earned under supply agreements between the Company, Micron and MP Mask; comprised of gross commission income of $1.7 million less $0.7 million of amortization of the value of the supply agreement intangible asset. The gross commission income results from $23.8 million in sales orders from Micron less the Company's cost of the corresponding orders placed with MP Mask in the amount of $22.1 million. In addition, in 2006 the Company incurred outsourcing expenses of $0.4 million from MP Mask for research and development activities purchased by the Company. In 2007, the Company invested an additional $3.5 million in MP Mask. Also, the Company purchased excess equipment from MP Mask for use in its U.S. Nanofab in the amount of $4.0 million in 2007. In addition, in the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab for total capital lease payments by the Company of $73.9 million, of which $12.2 million represents interest and $61.7 million represents both principal and the cost of the facility.

The Chairman of the Board of the Company is also the Chairman of the Board and majority shareholder of a company who is a supplier of secure managed information technology services. Another director of the Company is also a shareholder, CEO and Executive Vice Chairman of this company. Since 2002, the Company has entered into various service contracts with this company to provide services to all of the Company's worldwide facilities. The Company incurred expenses of $3.8 million in 2007, $4.3 million in 2006, and $3.7 million in 2005 related to services provided by the company, for which the amount owed to this company was $0.6 million at October 28, 2007 and $0.1 million at October 29, 2006. In 2006, the Company signed a new 3-year service contract with this company for $2.5 million per year.

An officer of the Company is also the CEO, president and director of one of the Company's majority held subsidiaries. The Company purchases photomask blanks from a company of which this officer of the Company is a significant shareholder. The Company purchased $21.6 million, $16.8 million, and $13.6 million of photomask blanks from this company in 2007, 2006, and 2005, respectively, for which the amount owed to this company was $5.0 million at October 28, 2007 and $2.2 million at October 29, 2006.

The Company believes that the terms of the transactions described above with affiliated persons were negotiated at arm's-length and were no less favorable to the Company than the Company could have obtained from non-affiliated parties.

During fiscal years 2005 and 2006, the Company acquired substantially all of the remaining outstanding shares of its non-wholly owned subsidiary in Korea, PKL. As part of the purchase of outstanding shares in 2005, the Company acquired 1,136,036 shares or 3.4% from employees, including officers, of PKL for 8,980 won per share or $8.70 U.S. dollars per share. Two of these employees were also officers of the Company. The total purchase price of $9.9 million from PKL employees represents a premium of approximately 15% per share above similar purchases of stock from other stockholders during the same time period.

Stock-based Compensation

Total stock-based compensation expense for the year ended October 28, 2007 was $2.9 million, as compared to $2.0 million for the year ended October 29, 2006, substantially all of which is in selling, general and administrative expenses. No compensation cost was capitalized as part of inventory, and no income tax benefit has been recorded. As of October 28, 2007 total unrecognized compensation cost of $7.1 million is expected to be recognized over a weighted average amortization period of 2.6 years.

Business Outlook

A majority of the Company's revenue growth has come from, and is expected to continue to come from, the Asian region as customers increase their use of manufacturing foundries located outside of North America and Europe. Additional revenue growth is also anticipated from North America and Europe as a result of utilizing technology licensed under the Company's technology license with Micron. The Company's Korean and Taiwanese operations are non-wholly owned subsidiaries; therefore a portion of earnings generated at each location is allocated to the minority shareholders.

The Company continues to assess its global manufacturing strategy as its sales volume continues to grow in Asia. In addition to the restructuring plan implemented in the second quarter of 2006 relating to closing the Austin facility, this ongoing assessment could result in the future, in facilities closures, asset redeployment, workforce reductions, and the addition of increased manufacturing facilities, all of which would be based on market conditions and customer requirements.

The Company's future results of operations and the other forward-looking statements contained in this filing involve a number of risks and uncertainties. Various factors that have been discussed and a number of other factors could cause actual results to differ materially from the Company's expectations.

Application of Critical Accounting Procedures

The Company's consolidated financial statements are based on the selection and application of significant accounting policies, which require management to make significant estimates and assumptions. The Company believes that the following are some of the more critical judgment areas in the application of the Company's accounting policies that affect its financial condition and results of operations.

Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in them. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Significant accounting estimates include management's review of long-lived assets

and goodwill for potential impairment, income tax provision, allowance for uncollectible accounts receivable, inventory valuation allowances and restructuring reserves. The Company's estimates are based on the facts and circumstances available at the time; different reasonable estimates could have been used in the current period, and changes in the accounting estimates used are likely to occur from period to period, which may have a material impact on the presentation of the Company's financial condition and results of operations. Actual results reported by the Company may differ from such estimates. The Company reviews these estimates periodically and reflects the effect of revisions in the period that they are determined.

Derivative Instruments and Hedging Activities

The Company records derivatives in the consolidated balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives are reported in the Company's consolidated statements of income or as accumulated other comprehensive income, a separate component of shareholders' equity, depending on the use of the derivatives and whether they qualify for hedge accounting. In order to qualify for hedge accounting, the derivative must be highly effective in achieving offsetting changes in fair value or cash flows of the hedged items during the term of the hedge. The Company uses judgment in assessing the fair value of derivatives and related financial instruments, including assumptions utilized in derivative fair value models in areas such as projected interest rates and changes in the Company's stock price during the contract term. The Company's derivatives primarily relate to cash flow hedges to manage foreign currency fluctuation risk.

Property, Plant and Equipment

Property, plant and equipment is stated at cost less accumulated depreciation and amortization. Repairs and maintenance as well as renewals and replacements of a routine nature are charged to operations as incurred, while those which improve or extend the lives of existing assets are capitalized. Upon sale or other disposition, the cost of the asset and accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in operations.

Depreciation and amortization are computed on the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 15 to 40 years, machinery and equipment over 3 to 10 years and furniture, fixtures and office equipment over 3 to 5 years. Leasehold improvements are amortized over the life of the lease or the estimated useful life of the improvement, whichever is less. Judgment and assumptions are used in establishing estimated useful lives and depreciation periods. The Company also uses judgment and assumptions as it periodically reviews property, plant and equipment for any potential impairment in carrying values whenever events such as a significant industry downturn, plant closures, technological obsolescence or other changes in circumstances indicate that their carrying amount may not be recoverable. Actual fair values may differ from estimated fair values.

Goodwill and Other Intangible Assets

Intangible assets consist primarily of goodwill and other acquisition-related intangibles, a technology license agreement and a supply agreement. These assets are stated at fair value as of the date acquired less accumulated amortization. Amortization is calculated on a straight-line basis or another method that more fairly represents the utilization of the assets. The future economic benefit of the carrying value of intangible assets is reviewed annually and the Company uses judgment whenever events or changes in circumstances indicate the carrying value of an intangible asset may not be recoverable based on discounted cash flows or market factors and an impairment loss would be recorded in the period so determined.

The Company recognizes the excess of the cost of acquired businesses over the fair value of the net assets purchased as goodwill. Goodwill is not amortized to earnings, but instead is reviewed for impairment at least annually. A review of goodwill completed in the second quarter and the fourth quarter found no impairment. In accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets," the Company tests goodwill and other intangible assets with indefinite lives for impairment on an annual basis (or on an interim basis if an event occurs that indicates an impairment might exist). The Company completed its required annual impairment tests in fiscal 2007, 2006 and 2005, and it was determined that the carrying value of goodwill and other intangible assets with indefinite lives was not impaired.

Impairment of Long-Lived Assets

Long-lived assets and certain identifiable assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on the Company's judgment and estimate of future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets and certain identifiable intangible assets to be disposed of are reported at the lower of carrying amount or fair value less costs of disposition.

Investment in Joint Venture

Investments in joint ventures over which the Company has the ability to exercise significant influence and that, in general, are at least 20 percent owned are stated at cost plus equity in undistributed net income (loss) of the joint venture. These investments are evaluated for impairment in accordance with the requirements of Accounting Principles Board ("APB") Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. In judging "other than temporary", the Company would consider the length of time and extent to which the fair value of the investment has been less than the carrying amount of the equity company, the near-term and longer-term operating and financial prospects of the equity company, and its longer-term intent of retaining the investment in the equity company.

Income Taxes

The income tax provision (benefit) is computed on the basis of consolidated financial statement income or loss before income taxes. Deferred income taxes reflect the tax effects of differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company uses judgment and assumptions to determine if valuation allowances for deferred income tax assets are required if realization is not likely by considering future market growth, forecasted operations, future taxable income, and the mix of earnings in the tax jurisdictions in which it operates in order to determine the need for a valuation allowance.

The Company considers income taxes in each of the tax jurisdictions in which it operates in order to determine its effective income tax rate. Current income tax exposure is identified along with assessing temporary differences resulting from differing treatment of items for tax and financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included in the Company's consolidated balance sheets. Additionally, the

Company evaluates the recoverability of deferred income tax assets from future taxable income and establishes valuation allowances if recovery is deemed not likely. Accordingly, the income tax provision in the consolidated statements of operations is impacted by changes in the valuation allowance. Significant management estimates and judgment are required in determining any valuation allowance recorded against net deferred tax assets.

Revenue Recognition

The Company recognizes revenue when both title and risk of loss transfer to the customer. The Company makes estimates and assumptions and uses judgment relating to discounts and estimates for product return and warranties, which are accrued and recognized at the time of sale.

Discounts - Sales discounts are negotiated with customers prior to billing and at the time of billing, sales invoices are prepared net of negotiated sales discounts.

Product Returns- Customer returns have historically been insignificant. However, the Company does record a liability for the immaterial amount of estimated sales returns based upon historical experience.

Warranties and Other Post Shipment Obligations - For a 30-day period, the Company warrants that items sold will conform to customer specifications. However, the Company's liability is limited to repair or replacement of the photomasks at its sole option. The Company inspects photomasks for conformity to customer specifications prior to shipment. Accordingly, customer returns of items under warranty have historically been insignificant. However, the

Company records a liability for the insignificant amount of estimated warranty returns based on historical experience. The Company's specific return policies include accepting returns for products with defects, or products that have not been produced to precise customer specifications. At the time of revenue recognition, a liability is established for these items.

Stock-based Compensation

The Company adopted SFAS No. 123(R) on October 31, 2005, using the modified prospective method. Subsequently, compensation expense is recognized in the Company's consolidated statements of income, over the service period that the awards are expected to vest. The Company recognizes expense for all stock-based compensation with graded vesting granted on or after October 31, 2005 on a straight-line basis over the vesting period of the entire award. For awards with graded vesting granted prior to October 31, 2005, the Company continues to recognize compensation cost over the vesting period following accelerated recognition as if each underlying vesting date represented a separate award. Stock-based compensation expense includes the estimated effects of forfeitures, which will be adjusted over the requisite service period to the extent actual forfeitures differ, or are expected to differ from such estimates. Changes in estimated forfeitures are recognized in the period of change and will also impact the amount of expense to be recognized in future periods. The Company adopted the alternative transition method provided in Financial Accounting Standards Board ("FASB") Staff Position No. 123(R)-3 for calculating the tax effects of share-based compensation. Determining the appropriate fair-value model and calculating the fair value of stock-based awards at the grant date requires considerable judgment, including estimating stock price volatility, expected option life and forfeiture rates.

The Company uses the Black-Scholes option valuation model to value employee stock awards. The Company estimates stock price volatility based on weekly averages of its historical volatility over a term approximately equal to the grant's estimated option life. Estimated option life and forfeiture rate assumptions are derived from historical data.

Effect of New Accounting Standards

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements - an amendment of Accounting Research Bulletin ("ARB") No. 51." SFAS No. 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary for the deconsolidation of a subsidiary. SFAS No. 160 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim statements within those fiscal years. The Company is currently evaluating the impact, if any, SFAS No. 160 will have on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, "Business Combinations." SFAS No. 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statement to evaluate the nature and financial effects of the business combination. SFAS No. 141R is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim statements within those fiscal years. The Company is currently evaluating the impact, if any, SFAS No. 141R will have on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities-Including an Amendment of FASB Statement No. 115." SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value, and is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company is currently evaluating the impact that the adoption of SFAS No. 159 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact, if any, that SFAS No. 157 may have on its consolidated financial statements.

In September 2006, the United States Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB No. 108"). This SAB provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. The Company early adopted SAB No. 108 during its quarter ended January 28, 2007, and its adoption did not have a material impact on its consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation Number 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109." The interpretation contains a two step approach to recognizing and measuring uncertain tax positions accounted for in accordance with SFAS No. 109. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement. The provisions are effective as of the beginning of the Company's 2008 fiscal year. The Company is analyzing the impact that the adoption of FIN 48 will have on its consolidated financial statements, but expects the adjustment to decrease shareholders' equity as of October 29, 2007 to be approximately $0.5 million to

$1.0 million.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company records derivatives on the balance sheet as assets or liabilities, measured at fair value. The Company does not engage in derivative instruments for speculative purposes. Gains or losses resulting from changes in the values of those derivatives are reported in the statement of operations or as accumulated other comprehensive income, a separate component of shareholders' equity, depending on the use of the derivatives and whether they qualify for hedge accounting. In order to qualify for hedge accounting, among other criteria the derivative must be highly effective in achieving offsetting changes in fair value or cash flows of the hedged items during the term of the hedge. In general, the types of risks hedged are those relating to the variability of future cash flows caused by movements in foreign currency exchange rates and interest rates. The Company documents its risk management strategy and hedge effectiveness at the inception of and during the term of each hedge.

In the fourth quarter of fiscal year 2002, the Company entered into an interest rate swap contract, which effectively converted $100 million of its 4.75% fixed rate convertible subordinated notes to a variable rate. Contract payments were made on a LIBOR based variable rate (6.69% at October 29, 2006) and are received at the 4.75% fixed rate. This swap expired in December 2006 when the Company repaid the remaining outstanding balance of its 4.75% convertible subordinated notes. At this time, the Company does not have plans to enter into additional interest rate swap contracts, however, at a future point the Company may decide to do so.

Foreign Currency Exchange Rate Risk

The Company conducts business in several major international currencies through its worldwide operations and is subject to changes in foreign exchange rates of such currencies. Changes in exchange rates can positively or negatively affect the Company's sales, operating margins and retained earnings. The principal functional currencies of the Company's Asian subsidiaries are the Korean won, New Taiwan dollar, Chinese renminbi and Singapore dollar. The principal functional currencies of the Company's European subsidiaries are the British pound and euro.

The Company attempts to minimize its risk to foreign currency transaction losses by producing its products in the same country in which the products are sold and thereby generating revenues and incurring expenses in the same currency and by managing its working capital. In some instances, the Company may sell products in a currency other than the functional currency of the country where it was produced. To date, the Company has not experienced a significant foreign exchange loss on these sales. However, there can be no assurance that this approach will be successful, especially in the event of a significant adverse movement in the value of any foreign currencies against the U.S. dollar. The Company does not engage in purchasing forward exchange contracts for speculative purposes.

The Company's primary net foreign currency exposures as of October 28, 2007 included the Korean won, the Singapore dollar, the New Taiwan dollar, the Chinese renminbi, the British pound and the euro. As of October 28, 2007, a 10% adverse movement in the value of these currencies against the U.S. dollar would have resulted in a net unrealized pre-tax loss of $4.7 million. The Company does not believe that a 10% change in the exchange rates of other non-U.S. dollar currencies would have a material effect on its consolidated financial position, results of operations or cash flows.

In April, 2006, the Company's Korean subsidiary entered into a foreign currency rate swap contract which was maintained throughout 2007. Under the terms of the contract, the Company has effectively converted a $50 million interest bearing intercompany loan denominated in U.S. dollars to Korean won. Subsequent to fiscal year-end 2007, the intercompany loan and the related swap were reduced to a balance of $30 million. This contract was initially scheduled to expire in December 2006, however, it has been extended to November 2008. The Company elected not to designate the foreign currency rate swap contract as a hedge which results in a mark-to-market adjustment in the income statement.

In September, 2006, the Company entered into forward contracts to convert the fixed yen purchase price of certain equipment into fixed U.S. dollar amounts. In accordance with SFAS No. 133, "Accounting for Derivatives and Hedging Activities," hedges related to anticipated transactions are designated and documented at the inception of the respective hedges as cash flow and are evaluated for effectiveness. The Company records these derivative instruments in either other current assets or non current assets or accrued liabilities, depending on their net position, at fair value regardless of the purpose or intent for holding the instrument. Changes in the fair value of the derivative financial instrument are recognized in earnings or in shareholders equity as a component of accumulated other comprehensive income depending on whether the derivative financial instrument qualifies for hedge accounting as defined by SFAS No. 133.

Interest Rate Risk

The majority of the Company's borrowings at October 28, 2007 was in the form of a convertible subordinated note with a fixed interest rate of 2.25% and certain unsecured international notes payable which bear interest at rates ranging from 6.57% to 6.93% at October 28, 2007, and ranging from 6.12% to 6.48% at October 29, 2006. The $86.9 million net carrying value of its 4.75% convertible subordinated note was repaid by the Company in December 2006. In addition, the interest rate swap contract discussed above subjects the Company to market risk as interest rates fluctuate on the $100 million notional amount of the contract. At October 28, 2007 and October 29, 2006, the Company had approximately $97 million and $56 million, respectively, in net variable rate financial instruments which were sensitive to interest rate risk. A 10% change in interest rates would not have a material effect on the Company's consolidated financial position, results of operations or cash flows in either 2007 or 2006.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Photronics, Inc.
Brookfield, Connecticut

We have audited the accompanying consolidated balance sheets of Photronics, Inc. and subsidiaries (the "Company") as of October 28, 2007 and October 29, 2006 and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three fiscal years ended October 28, 2007, October 29, 2006 and October 30, 2005. We also have audited the Company's internal control over financial reporting as of October 28, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting in Item 9A. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting 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 the company; (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 the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of October 28, 2007 and October 29, 2006, and the results of their operations and their cash flows for each of the fiscal years ended October 28, 2007, October 29, 2006 and October 30, 2005, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of October 28, 2007, based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ Deloitte & Touche LLP
Stamford, Connecticut
January 9, 2008

PHOTRONICS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(in thousands, except per share amounts)

	October 28, 2007	October 29, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 146,049	$ 129,425
Short-term investments	5,657	69,899
Accounts receivable, net of allowance of $3,721 in 2007 and $4,471 in 2006	68,248	84,299
Inventories	17,716	19,209
Deferred income taxes	3,071	2,623
Other current assets	6,244	13,432
Total current assets	246,985	318,887
Property, plant and equipment, net	531,578	443,637
Goodwill	138,534	138,534
Investment in joint venture	67,900	64,365
Other intangibles, net	68,835	71,763
Other assets	5,948	8,497
	$1,059,780	$1,045,683

LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term borrowings	$ 4,482	$ 86,903
Accounts payable	114,221	53,907
Accrued liabilities	31,676	50,386
Total current liabilities	150,379	191,196
Long-term borrowings	191,253	170,288
Deferred income taxes	8,143	9,700
Other liabilities	6,256	14,220
Total liabilities	356,031	385,404
Minority interest	49,465	45,997
Shareholders' equity:		
Preferred stock, $0.01 par value, 2,000 shares authorized, none issued and outstanding	-	-
Common stock, $0.01 par value, 150,000 shares authorized, 41,635 shares issued and outstanding at October 28, 2007 and 41,485 shares issued and outstanding at October 29, 2006	416	415
Additional paid-in capital	381,876	378,143
Retained earnings	227,175	202,652
Accumulated other comprehensive income	44,817	33,072
Total shareholders' equity	654,284	614,282
	$1,059,780	$1,045,683

See accompanying notes to consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES
Consolidated Statements of Income
(in thousands, except per share amounts)

Year Ended

	October 28, 2007	October 29, 2006	October 30, 2005
Net sales	$421,479	$454,875	$440,770
Cost and expenses:			
Cost of sales	(321,958)	(307,851)	(295,649)
Selling, general and administrative	(61,507)	(62,215)	(54,295)
Research and development	(17,300)	(27,337)	(32,152)
Consolidation, restructuring and related charges	-	(15,639)	-
Gain on sale of facility	2,254	-	-
Operating income	22,968	41,833	58,674
Other income (expense):			
Interest expense	(5,928)	(11,916)	(10,885)
Investment and other income, net	6,844	15,469	7,556
Income before income tax benefit (provision) and minority interest	23,884	45,386	55,345
Income tax benefit (provision)	3,178	(10,462)	(10,058)
Income before minority interest	27,062	34,924	45,287
Minority interest in income of consolidated subsidiaries	(2,539)	(5,592)	(6,634)
Net income	$ 24,523	$ 29,332	$ 38,653
Income per share:			
Basic	$0.59	$0.71	$1.09
Diluted	$0.56	$0.66	$0.95
Weighted average number of common shares outstanding:			
Basic	41,539	41,369	35,519
Diluted	51,282	51,072	45,256

See accompanying notes to consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES

Consolidated Statements of Shareholders' Equity
Years Ended October 28, 2007, October 29, 2006 and October 30, 2005
(in thousands)

	Common Stock		Add'l Paid-In Capital	Retained Earnings	Accumu-lated Other Compre-hensive Income	Deferred Compen-sation on Restricted Stock	Total Share-holders Equity
	Shares	Amount					
alance at November 1, 2004	32,690	$327	$202,313	$134,667	$12,166	$ -	$349,47
omprehensive income:							
Net income	-	-	-	38,653	-	-	38,65
Change in unrealized gains on investments	-	-	-	-	(16)	-	(1
Change in fair value of cash flow hedge	-	-	-	-	112	-	11
Foreign currency translation adjustment	-	-	-	-	1,588	-	1,58
otal comprehensive income	-	-	-	-	-	-	40,33
ale of common stock through employee stock option and purchase plans	546	5	8,942	-	-	-	8,94
estricted stock awards, net of amortization o compensation expense	18	-	300	-	-	(34)	26
ommon stock issued in public offering	8,050	81	162,771	-	-	-	162,85
alance at October 30, 2005	41,304	413	374,326	173,320	13,850	(34)	561,87
omprehensive income:							
Net income	-	-	-	29,332	-	-	29,33
Change in unrealized gains on investments	-	-	-	-	(1,109)	-	(1,10
Change in fair values of cash flow hedges	-	-	-	-	(35)	-	(3
Foreign currency translation adjustment	-	-	-	-	20,366	-	20,36
otal comprehensive income	-	-	-	-	-	-	48,55
ale of common stock through employee stock option and purchase plan	151	2	2,078	-	-	-	2,08

estricted stock awards, net of amortization o compensation expense	30	-	399	-	-	34	43
ock-based compensation expense	-	-	1,340	-	-	-	1,34
alance at October 29, 2006	41,485	415	378,143	202,652	33,072	-	614,28
omprehensive income:							
Net income	-	-	-	24,523	-	-	24,52
Change in unrealized gains on investments	-	-	-	-	(458)	-	(45
Change in fair values of cash flow hedges	-	-	-	-	(1,024)	-	(1,02
Foreign currency translation adjustment	-	-	-	-	13,496	-	13,49
otal comprehensive income	-	-	-	-	-	-	36,53
ale of common stock through employee stock option and purchase plan	80	1	972	-	-	-	97
estricted stock awards, net of amortization o compensation expense	70	-	730	-	-	-	73
ock-based compensation expense	-	-	2,031	-	-	-	2,03
ther	-	-	-	-	(269)	-	(26
alance at October 28, 2007	41,635	$416	$381,876	$227,175	$44,817	$ -	$654,28

ee accompanying notes to consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(in thousands)

	Year Ended		
	October 28, 2007	**October 29, 2006**	**October 30, 2005**
Cash flows from operating activities:			
Net income	$ 24,523	$ 29,332	$ 38,653
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization of property, plant and equipment	89,752	85,409	85,303
Amortization of deferred financing fees and intangible assets	8,266	5,269	2,545
Stock-based compensation	2,890	1,970	266
Minority interest in income of consolidated subsidiaries	2,539	5,592	6,634
Gain on sale of facility	(2,254)	-	-
Loss on repurchase of note	-	-	1,677

Deferred income taxes	(961)	965	4,636
Restructuring and related charges	-	15,639	-
Changes in assets and liabilities:			
Accounts receivable	18,370	(9,161)	3,553
Inventories	2,008	3,302	(1,672)
Other current assets	7,528	(7,272)	768
Accounts payable, accrued liabilities and other	(17,968)	(14,846)	204
Net cash provided by operating activities	134,693	116,199	142,567
Cash flows from investing activities:			
Purchases of property, plant and equipment	(94,132)	(94,646)	(121,354)
Purchases of short-term investments and other	(4,151)	(82,582)	(94,550)
Proceeds from sales of short-term investments and other	66,304	104,962	88,629
Investment in joint venture, technology and supply agreements	(3,499)	(120,505)	-
Proceeds from sale of facility and other	5,784	-	-
Acquisition of additional interest in PK, Ltd.	-	(8,432)	(58,248)
Net cash used in investing activities	(29,694)	(201,203)	(185,523)
Cash flows from financing activities:			
Proceeds from long-term borrowings	4,303	20,303	4,511
Repayments of long-term borrowings	(87,084)	(8,566)	(76,628)
Payment to Micron Technology, Inc.	(7,500)	-	-
Proceeds from exercised stock options and other	988	1,809	7,815
Net proceeds from issuance of common stock	-	-	162,852
Other	(527)	-	-
Net cash (used in) provided by financing activities	(89,820)	13,546	98,550
Effect of exchange rate changes on cash	1,445	4,834	(1,845)
Net increase (decrease) in cash and cash equivalents	16,624	(66,624)	53,749
Cash and cash equivalents at beginning of year	129,425	196,049	142,300
Cash and cash equivalents at end of year	$146,049	$129,425	$196,049
Supplemental disclosure of cash flow information:			
Change in accrual for purchases of property, plant and equipment	$51,582	$ 18,692	$(19,834)
Capital lease obligation for purchases of property, plant and equipment	$19,912	$ -	$ -

See accompanying notes to consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
Years Ended October 28, 2007, October 29, 2006 and October 30, 2005
(in thousands, except share amounts)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business

Photronics, Inc. and its subsidiaries ("Photronics" or the "Company") is one of the world's leading manufacturers of photomasks, which are high precision photographic quartz plates containing microscopic images of electronic circuits. Photomasks are a key element in the manufacture of semiconductors and flat panel displays ("FPD"), and are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates during the fabrication of integrated circuits ("IC") and a variety of FPD and, to a lesser extent, other types of electrical and optical components. The Company currently operates principally from ten manufacturing facilities, two of which are located in the United States, three in Europe, two in Taiwan, and one each in Korea, Singapore and China, which began production in the second quarter of the Company's fiscal 2007 year. Also, under a build-to-suit lease, in the first quarter of fiscal 2008, a capital lease agreement commenced with Micron Technology, Inc. ("Micron") for a state-of-the-art nanofab facility ("U.S. Nanofab") in Boise, Idaho.

Consolidation

The accompanying consolidated financial statements include the accounts of Photronics and its majority-owned subsidiaries, in which the Company exercises control. All significant intercompany balances and transactions have been eliminated in consolidation.

Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in them. Actual results may differ from such estimates.

Derivative Instruments and Hedging Activities

The Company records derivatives in the consolidated balance sheets at fair value. The Company does not engage in derivative instruments for speculative purposes. Gains or losses resulting from changes in the values of those derivatives are reported in the consolidated statements of operations or as accumulated other comprehensive income ("OCI"), depending on whether they meet certain criteria and qualify for hedge accounting. Among other criteria, in order to qualify for hedge accounting, the derivative must be highly effective in achieving offsetting changes in fair value or cash flows of the hedged items during the term of the hedge. The Company uses judgment in assessing the fair value of derivatives and related financial instruments including assumptions utilized in derivative fair value models in such areas as projected interest rates and bond prices which are affected by changes in the Company's stock price during the contract term.

Fiscal Year

The Company's fiscal year ends on the Sunday closest to October thirty-first, and, as a result, a 53-week year occurs every 5 to 6 years. Fiscal years 2005, 2006 and 2007 included 52 weeks; fiscal year 2008 will include 53 weeks.

Cash and Cash Equivalents

Cash and cash equivalents include cash and highly liquid investments purchased with an original maturity of 3 months or less. The carrying values approximate fair values based on the short maturity of these instruments.

Investments

The Company's investments, comprised of marketable equity securities, fixed income bonds, and auction rate securities, are classified as available-for-sale, and are carried at fair value. Investments available for current operations are classified in the consolidated balance sheets as current assets; investments held for long-term purposes are classified as non-current assets. Unrealized gains and losses, net of tax, are reported in OCI as a separate component of shareholders' equity. Gains and losses are reported in the consolidated statements of operations when realized, determined based on the disposition of specifically identified investments.

Investments identified by the Company as having potential impairment are subject to further analysis to determine if the impairment is other than temporary. Other than temporary declines in market value from original costs are charged to investment and other income, net, in the period in which the loss occurs. In determining whether investment holdings are other than temporarily impaired, the Company considers the nature, cause, severity and duration of the impairment. The Company and its investment advisors used analyst reports, credit ratings or other items as part of its review. None of the Company's investments were impaired as of October 28, 2007.

Inventories

Inventories, principally raw materials, are stated at the lower of cost, determined under the first-in, first-out ("FIFO") method, or market.

Property, Plant and Equipment

Property, plant and equipment is stated at cost less accumulated depreciation and amortization. Repairs and maintenance as well as renewals and replacements of a routine nature are charged to operations as incurred, while those which improve or extend the lives of existing assets are capitalized. Upon sale or other disposition, the cost of the asset and accumulated depreciation are eliminated from the accounts, and any resulting gain or loss is reflected in operations.

Depreciation and amortization are computed on the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 15 to 40 years, machinery and equipment over 3 to 10 years and furniture, fixtures and office equipment over 3 to 5 years. Leasehold improvements are amortized over the life of the lease or the estimated useful life of the improvement, whichever is less. The Company periodically reviews property, plant, and equipment for any potential impairment in carrying values. Judgment and assumptions are used in establishing estimated useful lives and depreciation periods.

Goodwill and Other Intangible Assets

Intangible assets consist primarily of goodwill and other acquisition-related intangibles, a technology license agreement and a supply agreement. These assets are stated at fair value as of the date acquired less accumulated amortization. Amortization is calculated on a straight-line basis or another method that more fairly represents the utilization of the assets. The future economic benefit of the carrying value of all intangible assets is reviewed annually and the Company uses judgment whenever events or changes in circumstances indicate the carrying value of an intangible asset may not be recoverable based on discounted cash flows or market factors and an impairment loss would be recorded in the period so determined (see Note 6).

The Company recognizes the excess cost of acquired businesses over the fair value of the net assets purchased as goodwill. Goodwill is not amortized to earnings, but instead is reviewed for impairment at least annually. In accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," the Company tests goodwill and other intangible assets with indefinite lives for impairment on an annual basis (or on an interim basis if an event occurs that indicates an impairment might exist). The Company completed its required annual impairment tests in fiscal 2007, 2006 and 2005, and it was determined that the carrying value of goodwill and other intangible assets with indefinite lives was not impaired.

Impairment of Long-Lived Assets

Long-lived assets and certain identifiable assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on the Company's judgment and estimate of future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets and certain identifiable intangible assets to be disposed of are reported at the lower of carrying amount or fair value less costs of disposition.

Investment in Joint Venture

Investments in joint ventures over which the Company has the ability to exercise significant influence and that, in general, are at least 20 percent owned are stated at cost plus equity in undistributed net income (loss) of the joint venture. These investments are evaluated for impairment in accordance with the requirements of Accounting Principles Board ("APB") Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. In judging "other than temporary," the Company would consider the length of time and extent to which the fair value of the investment has been less than the carrying amount of the equity company, the near-term and longer-term operating and financial prospects of the equity company, and its longer-term intent of retaining the investment in the equity company.

Income Taxes

The income tax provision (benefit) is computed on the basis of consolidated financial statement income or loss before income taxes. Deferred income taxes reflect the tax effects of differences between the carrying amounts of assets and liabilities for financial reporting and the amounts used for income tax purposes. The Company uses judgment and assumptions to determine if a valuation allowance for deferred income tax assets is required if realization is not likely.

The Company considers income taxes in each of the tax jurisdictions in which it operates in order to determine its effective income tax rate. Current tax exposure is identified along with assessing temporary differences resulting from differing treatment of items for tax and financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included in the Company's consolidated balance sheets. Additionally, the Company evaluates the recoverability of deferred tax assets from future taxable income and establishes valuation allowances if recovery is deemed not likely. Accordingly, the income tax provision in the consolidated statements of operations is impacted by changes in the valuation allowance. Significant management judgment is required in determining the Company's provision for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against net deferred tax assets.

Earnings Per Share

Basic earnings per share ("EPS") is based on the weighted average number of common shares outstanding for the period, excluding any dilutive common share equivalents. Diluted EPS reflects the potential dilution that could occur if certain securities or other contracts to issue common stock were exercised or converted.

Stock-Based Compensation

The Company adopted SFAS No. 123(R), "Share-Based Payments" on October 31, 2005, using the modified prospective method. Subsequently compensation expense is recognized in its consolidated statements of operations over the service period that the awards are expected to vest. The Company recognizes expense for all stock-based compensation with graded vesting granted on or after October 31, 2005 on a straight-line basis over the vesting period of the entire award. For awards with graded vesting granted prior to October 31, 2005, the Company continues to recognize compensation cost over the vesting period following accelerated recognition as if each underlying vesting date represented a separate award. Stock-based compensation expense includes the estimated effects of forfeitures, which will be adjusted over the requisite service period to the extent actual forfeitures differ, or are expected to differ from such estimates. Changes in estimated forfeitures will be recognized in the period of change and will also impact the amount of expense to be recognized in future periods.

Prior to October 31, 2005, the Company recorded stock-based compensation in accordance with the provisions of APB Opinion No. 25. The Company estimated the fair value of stock option awards in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation," and disclosed the resulting estimated effect on net income on a pro forma basis. Forfeitures of employee awards were provided in the pro forma effects as they occurred.

As a result of adopting SFAS No. 123(R) on October 31, 2005, the Company's income before income taxes and net income for the year ended October 29, 2006 was $1.3 million, or $0.03 per basic and diluted share less than if it had continued to account for share-based compensation under APB Opinion No. 25. There was no change in the statement of cash flows as a result of adoption of SFAS No. 123(R).

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123(R), "Accounting for Stock-Based Compensation," to stock-based employee compensation for the year ended October 30, 2005:

Year Ended October 30, 2005:

Net income	$38,653
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	266
Deduct: Total stock-based compensation expense determined under fair value-based method for all awards, net of related tax	

effects	(7,859)
Pro forma net income	$31,060
Basic earnings per share:	
As reported	$1.09
Pro forma	$0.87
Diluted earnings per share:	
As reported	$0.95
Pro forma	$0.78

Research and Development

Research and development costs are expensed as incurred, and consist primarily of global development efforts of high-end process technologies for advanced sub wavelength reticle solutions for IC and FPD photomask technologies.

Research and development expenses also include the amortization of the carrying value of a technology license agreement with Micron (see Note 2 and Note 6). Under this technology license agreement, the Company has access to certain photomask technology developed by Micron.

Foreign Currency Translation

The Company's international subsidiaries maintain their accounts in their respective local currencies. Assets and liabilities of such subsidiaries are translated to U.S. dollars at year-end exchange rates. Income and expenses are translated at average rates of exchange prevailing during the year. Foreign currency translation adjustments are accumulated and reported as OCI as a separate component of shareholders' equity. The effects of changes in exchange rates on foreign currency transactions, which are included in investment and other income, net, were $1.0 million, $4.3 million and $1.6 million in fiscal 2007, 2006 and 2005, respectively.

Minority Interest

Minority interest represents the minority shareholders' proportionate share in the equity of the Company's two majority-owned subsidiaries, PK, Ltd. ("PKL") in Korea, and Photronics Semiconductor Mask Corporation ("PSMC") in Taiwan, of which minority shareholders owned approximately 0.3% and 42%, respectively, as of October 28, 2007.

Revenue Recognition

The Company recognizes revenue when both title and risk of loss transfer to the customer. The Company makes estimates and assumptions and uses judgment relating to discounts and estimates for product return and warranties, which are accrued and recognized at the time of sale.

Discounts - Sales discounts are negotiated with customers prior to billing and at the time of billing, sales invoices are prepared net of negotiated sales discounts.

Product Returns - Customer returns have historically been insignificant. However, the Company does record a liability for the insignificant amount of estimated sales returns based upon historical experience.

Warranties and Other Post Shipment Obligations - For a 30-day period, the Company warrants that items sold will conform to customer specifications. However, the Company's liability is limited to repair or replacement of the photomasks at its sole option. The Company inspects photomasks for conformity to customer specifications prior to shipment. Accordingly, customer returns of items under warranty have historically been insignificant. However, the Company records a liability for the insignificant amount of estimated warranty returns based on historical experience. The Company's specific return policies include accepting returns for products with defects, or products that have not been produced to precise customer specifications. At the time of revenue recognition, a liability is established for these items.

Sales Taxes - The Company presents it revenues in the consolidated statements of income, net of sales taxes, if any (excluded from revenues).

NOTE 2 - JOINT VENTURE, TECHNOLOGY LICENSE AND OTHER AGREEMENTS WITH MICRON TECHNOLOGY, INC.

On May 5, 2006, Photronics and Micron entered into the MP Mask joint venture, which develops and produces photomasks for leading-edge and advanced next generation semiconductors. As part of the formation of the joint venture, Micron contributed its existing photomask technology center located at its Boise, Idaho, headquarters to MP Mask and Photronics has, as of October 28, 2007, paid Micron $127.5 million to date, and will pay Micron an additional $7.5 million (included in accrued liabilities at October 28, 2007) on May 5, 2008 in exchange for a 49.99% interest in MP Mask and a license for photomask technology of Micron and certain supply agreements. In 2007, the Company invested an additional $3.5 million in MP Mask for capital expenditure and working capital purposes.

In the first quarter of fiscal 2008, a capital lease agreement commenced with Micron for the U.S. Nanofab for a total of $61.7 million principal amount, payable by the Company to Micron over a 5-year period (see Note 8). Photronics' total investment in the purchase and equipping of its U.S. Nanofab is expected to fall within a range of $190 million to $200 million and may include redeployment of some existing Photronics assets. This U.S. Nanofab is expected to begin production in the first quarter of calendar 2008.

The Company has completed its analysis of fair value attributes of its total $135,505 investment through the use of independent appraisals and management estimates, and has reallocated values that were preliminarily allocated to the investment in MP Mask joint venture and related intangible assets. The Company has allocated $64,209 to the net fair value of tangible assets acquired, $59,616 to the technology agreement, which will be amortized over 15 years, $6,959 to the supply agreement which will be amortized over 10 years, and $4,721 to goodwill. The Company accounts for its interest in the joint venture using the equity method of accounting. The Company's proportionate share of income or losses from its investment in the joint venture is recorded in other income and expense. In fiscal 2007, the Company invested an additional $3.5 million in the MP Mask joint venture.

NOTE 3 - ACQUISITION OF ADDITIONAL SHARES OF PK, LTD. ("PKL")

During the first quarter of fiscal 2006, Photronics invested $8.5 million to purchase additional shares of PKL, its non-wholly owned subsidiary in Korea. This transaction increased the Company's ownership in PKL from 96.5% as of October 30, 2005 to 99.7% as of October 29, 2006. During 2005, the Company invested $58.3 million to purchase additional shares of PKL which increased the Company's ownership in PKL from 75% at October 31, 2004 to 96.5%

at October 30, 2005. The Company has completed its analysis of fair value attributes of the additional ownership through the use of independent appraisals and management estimates, and has reallocated values that were preliminarily allocated to goodwill to PKL's customer relationships and patents which are included in "Other Intangibles, net" in the consolidated balance sheets (see Note 6).

NOTE 4 - INVESTMENTS

Short-term investments at October 28, 2007 and October 29, 2006 consist of available-for-sale fixed income and marketable equity securities. Long-term investments of $0.1 million at October 28, 2007 and $0.7 million at October 29, 2006 included in "Other Assets" consist primarily of available-for-sale equity securities, where fair values were determined based upon quoted market prices.

Available-for-sale investments at October 28, 2007 were as follows:

	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Short-term investments:				
Term deposit	$3,260	$ -	$ -	$3,260
Foreign bond funds and other	2,289	108	-	2,397
Total short-term investments	5,549	108	-	5,657
Long-term equity investments	29	109	-	138
	$5,578	$217	$ -	$5,795

Available-for-sale investments at October 29, 2006 were as follows:

	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Short-term investments:				
Auction rate securities	$50,400	$ -	$ -	$50,400
Foreign bond funds and other	19,479	125	(105)	19,499
Total short-term investments	69,879	125	(105)	69,899
Long-term equity investments	51	655	-	706
	$69,930	$780	$(105)	$70,605

In determining whether investment holdings are other than temporarily impaired, the Company considers the nature, cause, severity and duration of the impairment. The Company and its investment advisors used analyst reports, credit ratings or other items as part of its review. No investments were impaired as of October 28, 2007.

The maturities of available-for-sale short-term investments as of October 28, 2007 were as follows:

	Cost Basis	Estimated Fair Value
Due in one year or less	$5,549	$5,657

Gross realized gains and losses related to the Company's investments are as follows:

	Year Ended		
	October 28, 2007	October 29, 2006	October 30, 2005
Gross realized gains	$851	$4,037	$353
Gross realized losses	(87)	(410)	(271)
Net realized gains	$764	$3,627	$ 82

NOTE 5 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following:

	October 28, 2007	October 29, 2006
Land	$ 8,429	$ 9,221
Buildings and improvements	103,010	111,818
Machinery and equipment	1,076,938	914,756
Leasehold improvements	6,085	5,535
Furniture, fixtures and office equipment	20,700	18,578
Construction in progress	119,277	95,011

	1,334,439	1,154,919
Less accumulated depreciation and amortization	802,861	711,282
	$ 531,578	$ 443,637

At October 28, 2007, machinery and equipment with a cost of $19.9 million was recorded under a capital lease with no accumulated amortization. There were no capital leases at October 29, 2006. The Company capitalized interest expense of $0.2 million during the fiscal year ended October 28, 2007.

NOTE 6 - GOODWILL AND OTHER INTANGIBLE ASSETS

The carrying value of goodwill was $138.5 million at October 28, 2007 and October 29, 2006. Intangible assets that do not have indefinite lives are amortized based on average lives, which range from 3 to 15 years. Intangible asset amortization is forecasted to range from $5.1 million to $7.4 million per year for the next 5 years.

Other intangible assets include assets related to the purchase of additional shares of PKL and the investment to form the MP Mask joint venture. The following table summarizes the type, value and amortization periods of other intangible assets as of October 28, 2007:

	Gross Value	Accumulated Amortization	Net Value	Weighted Average Amortization Period
Technology license agreement	$59,616	$ 5,630	$53,986	15 years
Customer lists	7,210	1,321	5,889	10 years
Supply agreement	6,959	2,461	4,498	10 years
Patents	156	28	128	10 years
Software and other	5,969	1,635	4,334	3 years
	$79,910	$11,075	$68,835	

NOTE 7 - ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	October 28, 2007	October 29, 2006
Income taxes	$ 4,977	$18,789

Salaries, wages and related benefits	7,466	9,997
Restructuring	1,687	2,654
Interest	309	818
Property taxes	919	1,609
Payable to Micron Technology, Inc.	7,500	7,500
Other	8,818	9,019
	$31,676	$50,386