

CASTELLE \CA\  
Form 10-Q  
May 14, 2007

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

FORM 10-Q

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

For the quarterly period ended March 31, 2007

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
Commission File Number: 0-220-20

CASTELLE

(Exact name of Registrant as specified in its charter)

**California**  
(State or other jurisdiction of  
incorporation or organization)

**77-0164056**  
(IRS Employer Identification No.)

**855 Jarvis Drive, Suite 100, Morgan Hill, California 95037**  
(Address of principal executive offices, including zip code)

**(408) 852-8000**

(Registrant's telephone number, including area code)

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

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

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

The number of shares of Common Stock outstanding as of April 30, 2007 was 4,093,670.

**CASTELLE**  
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**PART I - FINANCIAL INFORMATION****ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**CASTELLE**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(in thousands)  
(unaudited)

	<u>March 31, 2007</u>	<u>December 31, 2006</u>
<b>Assets:</b>		
Current assets:		
Cash and cash equivalents	\$ 8,187	\$ 8,259
Accounts receivable, net of allowance for doubtful accounts of \$36 and \$44, respectively	1,321	932
Inventories	866	1,016
Prepaid expenses and other current assets	303	238
Deferred taxes	185	185
Total current assets	<u>10,862</u>	<u>10,630</u>
Property and equipment, net	272	280
Other non-current assets	119	125
Deferred taxes, non-current	944	944
Total assets	<u>\$ 12,197</u>	<u>\$ 11,979</u>
<b>Liabilities and Shareholders Equity:</b>		
Current liabilities:		
Accounts payable	\$ 257	\$ 349
Accrued liabilities	907	825
Deferred revenue	1,726	1,710
Total current liabilities	<u>2,890</u>	<u>2,884</u>
Shareholders equity:		
Common stock, no par value:		
Authorized: 25,000 shares		
Issued and outstanding: 4,042 and 4,019, respectively	28,253	28,234
Accumulated deficit:	(18,946)	(19,139)
Total shareholders equity	<u>9,307</u>	<u>9,095</u>
Total liabilities and shareholders equity	<u>\$ 12,197</u>	<u>\$ 11,979</u>

*See accompanying notes to condensed consolidated financial statements.*

**CASTELLE**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
(in thousands, except per share amounts)  
(unaudited)

	Three months ended	
	March 31, 2007	March 31, 2006
<b>Sales:</b>		
Products	\$ 2,004	\$ 2,187
Services	893	802
	2,897	2,989
<b>Cost of sales:</b>		
Products	876	791
Services	222	276
	1,098	1,067
	1,799	1,922
<b>Operating expenses:</b>		
Research and development	416	485
Sales and marketing	596	674
General and administrative	681	616
	1,693	1,775
Income from operations:	106	147
Interest income, net	99	69
Other expense, net	(12)	(10)
	193	206
Provision for income taxes		
Net income	\$ 193	\$ 206
<b>Income per share:</b>		
Net income per common share basic	\$ 0.05	\$ 0.05
Net income per common share diluted	\$ 0.04	\$ 0.05
Shares used in per share calculation basic	4,042	4,001
Shares used in per share calculation diluted	4,500	4,485

*See accompanying notes to condensed consolidated financial statements.*

**CASTELLE**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)  
(unaudited)

	Three months ended	
	March 31, 2007	March 31, 2006
Cash flows from operating activities:		
Net income	\$ 193	\$ 206
Adjustment to reconcile net income to net cash provided by operating activities:		
Share-based compensation	43	88
Depreciation and amortization	44	30
Provision for doubtful accounts	10	15
Provision for excess and obsolete inventory	6	16
Allowance for sales returns and stock rotation	(17)	(19)
Changes in assets and liabilities:		
Accounts receivable	(382)	228
Inventories	144	(160)
Prepaid expenses and other current assets	(64)	(96)
Accounts payable	(92)	34
Accrued liabilities	82	3
Deferred revenue	16	41
	(17)	386
Cash flows from investing activities:		
Acquisition of equipment	(31)	(37)
	(31)	(37)
Cash flows from financing activities:		
Repayment of long-term debt		