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GREATBATCH, INC.
Form 10-Q
November 06, 2007

U.S. 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 Quarter ended September 28, 2007

Commission File Number 1-16137

GREATBATCH, INC.
(Exact name of Registrant as specified in its charter)

Delaware
(State of incorporation)

16-1531026
(I.R.S. employer identification no.)

9645 Wehrle Drive
Clarence, New York
14031
(Address of principal executive offices)

(716) 759-5600
(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 [X] 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 Exchange Act Rule 12b-2 (check one):

Large accelerated filer [] Accelerated filer [X] Non-accelerated filer []

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

The number of shares outstanding of the Company's common stock, \$0.001 par value per share, as of November 6, 2007 was: 22,477,340 shares.

GREATBATCH, INC.
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AS OF AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 28, 2007

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

GREATBATCH, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS - Unaudited
 (in thousands except share and per share data)

| | As of | |
|---|-----------------------|------------------|
| | September 28, 2007 | December 2006 |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 95,979 | \$ 7 |
| Short-term investments available for sale | 19,774 | 7 |

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| | | |
|---|------------|-------|
| Accounts receivable, net of allowance of \$743 in 2007 and \$532 in 2006 | 44,108 | 3 |
| Inventories | 68,565 | 5 |
| Refundable income taxes | - | |
| Deferred income taxes | 6,597 | |
| Prepaid expenses and other current assets | 3,063 | |
| | ----- | ----- |
| Total current assets | 238,086 | 24 |
| Property, plant and equipment, net | 103,208 | 9 |
| Amortizing intangible assets, net | 48,595 | 2 |
| Trademarks and tradenames | 32,582 | 2 |
| Goodwill | 208,786 | 15 |
| Other assets | 13,605 | |
| | ----- | ----- |
| Total assets | \$ 644,862 | \$ 54 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 24,009 | \$ 1 |
| Accrued expenses and other current liabilities | 29,417 | 2 |
| | ----- | ----- |
| Total current liabilities | 53,426 | 4 |
| Convertible subordinated notes | 240,902 | 17 |
| Deferred income taxes | 31,740 | 3 |
| Other long-term liabilities | 127 | |
| | ----- | ----- |
| Total liabilities | 326,195 | 24 |
| | ----- | ----- |
| Stockholders' equity: | | |
| Preferred stock, \$0.001 par value, authorized 100,000,000 shares; no shares issued or outstanding in 2007 or 2006 | - | |
| Common stock, \$0.001 par value, authorized 100,000,000 shares; 22,468,840 shares issued and outstanding in 2007 and 22,119,142 shares issued and 22,111,516 shares outstanding in 2006 | 22 | |
| Additional paid-in capital | 237,210 | 22 |
| Treasury stock, at cost, no shares in 2007 and 7,626 shares in 2006 | - | |
| Retained earnings | 81,435 | 6 |
| Accumulated other comprehensive income | - | |
| | ----- | ----- |
| Total stockholders' equity | 318,667 | 29 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 644,862 | \$ 54 |
| | ===== | ===== |

The accompanying notes are an integral part of these condensed consolidated financial statements

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GREATBATCH, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME - Unaudited
(in thousands except per share data)

Three months ended

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| | September 28, 2007 | September 29, 2006 | Se |
|---|-----------------------|-----------------------|----|
| Sales | \$ 79,009 | \$ 69,294 | \$ |
| Costs and expenses: | | | |
| Cost of sales - excluding amortization of intangible assets | 48,647 | 42,709 | |
| Cost of sales - amortization of intangible assets | 1,222 | 948 | |
| Selling, general and administrative expenses | 11,362 | 9,311 | |
| Research, development and engineering costs, net | 8,423 | 6,022 | |
| Acquired in-process research and development | (2,260) | - | |
| Other operating expense, net | 1,275 | 6,239 | |
| Operating income | 10,340 | 4,065 | |
| Interest expense | 2,112 | 1,135 | |
| Interest income | (1,586) | (1,521) | |
| Gain on sale of investment security | - | - | |
| Gain on extinguishment of debt | - | - | |
| Other expense, net | 70 | 171 | |
| Income before provision for income taxes | 9,744 | 4,280 | |
| Provision for income taxes | 4,744 | 1,041 | |
| Net income | \$ 5,000 | \$ 3,239 | \$ |
| Earnings per share: | | | |
| Basic | \$ 0.23 | \$ 0.15 | \$ |
| Diluted | \$ 0.22 | \$ 0.15 | \$ |
| Weighted average shares outstanding: | | | |
| Basic | 22,214 | 21,816 | |
| Diluted | 23,872 | 21,983 | |
| Comprehensive income: | | | |
| Net income | \$ 5,000 | \$ 3,239 | \$ |
| Net unrealized gain (loss) on short-term investments available for sale, net of tax | - | (96) | |
| Less: reclassification adjustment for net realized gain on short-term investments available for sale, net of tax | - | - | |
| Comprehensive income | \$ 5,000 | \$ 3,143 | \$ |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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GREATBATCH, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - Unaudited
(in thousands)

Nine m
September 2

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2007

Cash flows from operating activities:

| | |
|---|--------|
| Net income | \$12,2 |
| Adjustments to reconcile net income to net cash provided by operating activities: | |
| Depreciation and amortization | 18,5 |
| Stock-based compensation | 7,0 |
| Gain on sale of investment security | (4,00) |
| Gain on extinguishment of debt | (4,47) |
| Acquired in-process research and development | 16,0 |
| (Gain) loss on disposal of assets | (12 |
| Deferred income taxes | (8,37) |
| Changes in operating assets and liabilities: | |
| Accounts receivable | (8,20) |
| Inventories | (4,93) |
| Prepaid expenses and other current assets | (61 |
| Accounts payable | 8,7 |
| Accrued expenses and other current liabilities | (4,09) |
| Income taxes refundable/payable | 2,9 |
| Net cash provided by operating activities | 30,8 |

Cash flows from investing activities:

| | |
|--|----------|
| Purchase of short-term investments | (59,20) |
| Proceeds from maturity/disposition of short-term investments | 109,9 |
| Acquisition of property, plant and equipment | (10,85) |
| Proceeds from sale of property, plant and equipment | |
| Purchase of cost method investment, net of distributions | (1,75) |
| Insurance proceeds for replacement of assets | 3 |
| Acquisitions, net of cash acquired | (109,73) |
| Increase in other assets | |
| Net cash used in investing activities | (71,16) |

Cash flows from financing activities:

| | |
|---|--------|
| Repayments under line of credit | (1,00) |
| Principal payments of long-term debt | (6,09) |
| Proceeds from issuance of long-term debt | 76,0 |
| Debt issuance costs | (6,61) |
| Issuance of common stock | 2,6 |
| Excess tax benefits from stock-based awards | 3 |
| Repurchase of treasury stock | (20 |
| Net cash provided by (used in) financing activities | 65,1 |

| | |
|--|--------|
| Net increase in cash and cash equivalents | 24,8 |
| Cash and cash equivalents, beginning of year | 71,1 |
| Cash and cash equivalents, end of period | \$95,9 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information (Accounting Principles Board Opinion ("APB") No. 28, Interim Financial Reporting) and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole. In the opinion of management, the condensed consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the results of Greatbatch, Inc. and its indirect wholly-owned subsidiary Greatbatch Ltd. (collectively "Greatbatch" or the "Company") for the periods presented. 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 the reported amounts of assets, liabilities, sales, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from these estimates. The December 29, 2006 condensed consolidated balance sheet data was derived from audited financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America. For further information, refer to the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 29, 2006. The Company utilizes a fifty-two, fifty-three week fiscal year ending on the Friday nearest December 31st. For 52-week years, each quarter contains 13 weeks. The third quarter of 2007 and 2006 each contained 13 weeks and ended on September 28, and September 29, respectively.

2. ACQUISITIONS

BIOMECH, Inc. - On April 3, 2007, the Company acquired substantially all of the assets of BIOMECH, Inc. ("BIOMECH"), a biomedical device company based in Cleveland, OH with the objective of accelerating technology from major medical and academic institutions, national laboratories, and from internally developed proprietary products. With the BIOMECH acquisition, we acquired an engineering team with diverse capabilities in medical device development, including mechanical design, software engineering, biocompatible coatings, and electronics. As a result, we can now offer our customers device engineering expertise along with full device assembly utilizing our proprietary components. This will also enable us to work in conjunction with our customers' design teams to build more sophisticated devices.

This transaction was accounted for under the purchase method of accounting in accordance with Statement of Financial Accounting Standards ("SFAS") No. 141 Business Combinations. Accordingly, the results of BIOMECH's operations were included in our condensed consolidated financial statements from the date of acquisition. The aggregate purchase price was \$11.4 million, which was paid in cash. This purchase price is preliminary and is subject to change based upon the Company incurring direct acquisition costs in connection with this transaction. Any adjustment to the purchase price is not expected to be material and will be allocated to goodwill, which totaled \$5.2 million. During the third quarter, the Company received a payment of \$0.25 million from the former BIOMECH representing its share of

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the purchase price resulting from its 2% ownership interest in the former BIOMECH. This payment was recorded as a reduction to the carrying amount of this investment.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

Various factors contributed to the establishment of goodwill, including: the value of BIOMECH's highly trained assembled work force; the expected revenue growth over time and the incremental value to the Company's Implantable Medical Components ("IMC") business from having device engineering capabilities; and the strategic partnership established with IntElect Medical, Inc. ("IntElect") an early stage neurostimulation device company that works in conjunction with the Cleveland Clinic. Goodwill resulting from the BIOMECH acquisition was allocated to the Company's IMC segment and is deductible for tax purposes.

Approximately \$2.3 million of the purchase price represents the estimated fair value of acquired in-process research and development ("IPR&D") projects that had not yet reached technological feasibility and had no alternative future use as of the acquisition date. Accordingly, the amount was immediately expensed after the acquisition date. The value assigned to IPR&D relates to projects that incorporate BIOMECH's novel-polymer coating (biomimetic) technology that mimics the surface of endothelial cells of blood vessels. The estimated fair value of these projects was determined using a discounted cash flow model. This model utilized discount rates that took into consideration the stage of completion and the risks surrounding the successful development and commercialization of each of the IPR&D projects of approximately 40%, which is consistent with the early development stage of these projects. The Company expects various products that utilize the biomimetic coatings technology to be commercially launched by original equipment manufacturers ("OEM") in 2009 once Food and Drug Administration ("FDA") approval is received. With BIOMECH, the Company acquired grants that will fund the remaining development costs for these products. The Company believes that the estimated acquired IPR&D amounts represent their fair value at the date of acquisition and do not exceed the amount an independent third party would pay for the projects. Pro forma amounts are not presented as, excluding the IPR&D charge, BIOMECH did not materially impact our results of operations.

Approximately \$3.7 million of the purchase price was allocated to BIOMECH's investment in IntElect. Subsequent to the acquisition, the Company made an additional \$2.0 million investment in IntElect, which increased its ownership percentage to approximately 19%. The IntElect investment is being accounted for under the cost method of accounting and is included in other assets.

Enpath Medical, Inc. - On June 15, 2007, the Company completed its acquisition of Enpath Medical, Inc. ("Enpath"). Enpath is a medical products company engaged in designing, developing, manufacturing and marketing single use medical device products for the cardiac rhythm management, neuromodulation and interventional radiology markets. We believe that the acquisition will further expand our product and service offerings to the cardiac rhythm management ("CRM") and neurostimulation marketplaces, broaden our market reach into the vascular segment through Enpath's introducer product lines, as well as add several new OEM customers.

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This transaction was accounted for under the purchase method of accounting in accordance with SFAS No. 141. Accordingly, the results of Enpath's operations were included in our condensed consolidated financial statements from the date of acquisition. The aggregate purchase price was \$98.4 million, consisting of the cash issued at closing to Enpath shareholders (\$91.7 million), the consideration paid to employees in exchange for the cancellation of their Enpath stock options and restricted stock (\$3.9 million) and other direct acquisition-related costs, including financial advisory, legal and accounting services (\$2.8 million). Subsequent to the acquisition date, the Company repaid the line of credit and term loans assumed from Enpath of approximately \$7.1 million.

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GREATBATCH, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

In accordance with SFAS No. 141, the cost of the acquisition was preliminarily allocated to the assets acquired and liabilities assumed from Enpath based on their fair values as of the close of the acquisition, with the amount exceeding the fair value recorded as goodwill. As the values of certain assets and liabilities are preliminary in nature, they are subject to adjustment as additional information is obtained, including, but not limited to, the finalization of our intangible asset valuation and the Company incurring direct acquisition costs in connection with this transaction. The valuations will be finalized within 12 months of the close of the acquisition. Any adjustment to the valuation is not expected to be material and will be allocated to goodwill.

The following table summarizes the preliminary allocation of the cost of the acquisition to the assets acquired and liabilities assumed as of the close of the acquisition (in thousands):

| (in thousands) | As of June 15, 2007 |
|-------------------------------|------------------------|
| <hr/> | |
| Assets acquired | |
| Current assets | \$ 10,942 |
| Property, plant and equipment | 11,623 |
| Acquired IPR&D | 13,840 |
| Amortizing intangible assets | 24,144 |
| Tradenames | 4,330 |
| Goodwill | 48,595 |
| | <hr/> |
| Total assets acquired | 113,474 |
| Liabilities assumed | |
| Current liabilities | 5,950 |
| Notes payable | 4,379 |
| Deferred income taxes | 4,625 |
| Other non-current liabilities | 145 |
| | <hr/> |
| Total liabilities assumed | 15,099 |
| | <hr/> |
| Purchase price | \$ 98,375 |
| | <hr/> <hr/> |

The fair values of the assets acquired and liabilities assumed were preliminarily determined using one or more of three valuation approaches: market, income and cost. The selection of a particular method for a given asset depended on the reliability of available data and the nature of the

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asset, among other considerations. The market approach, which indicates value for a subject asset based on available market pricing for comparable assets, was utilized for certain acquired personal property. The income approach, which indicates value for a subject asset based on the present value of risk adjusted cash flows projected to be generated by the asset, was used for certain intangible assets such as core and developed technology, acquired IPR&D, customer relationships, corporate tradenames and for noncompete agreements with employees. The risk adjusted projected cash flows were discounted at a required rate of return that reflects the relative risk of the Enpath transaction and the time value of money. The risk adjusted projected cash flows for each asset considered multiple factors, including current revenue from existing customers, distinct analysis of expected price, volume, and attrition trends, reasonable contract renewal assumptions from the perspective of a marketplace participant, and expected profit margins giving consideration to historical and expected margins. The cost approach, which estimates value by determining the current cost of replacing an asset with another of equivalent economic utility, was used for the majority of personal property. The cost to replace a

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

given asset reflects the estimated reproduction or replacement cost for the property, less an allowance for loss in value due to depreciation or obsolescence, with specific consideration given to economic obsolescence if indicated.

Inventory - The fair value of the inventory acquired was estimated by applying a version of the cost approach called the net realizable value method. This approach estimates the fair value of the asset by calculating the potential sales generated from selling the inventory and subtracting from it the costs related to the sale of that inventory and a reasonable profit allowance. Based upon this methodology, the Company recorded the inventory acquired at fair value resulting in an increase in inventory of \$1.3 million. For the three and nine months ended September 28, 2007, the Company expensed as cost of sales \$1.1 million and \$1.3 million, respectively, of the step-up value relating to the acquired Enpath inventory sold during the respective periods. As of September 28, 2007, there was no inventory step-up value remaining to be expensed.

Intangible assets - The purchase price was allocated to specific intangible assets on a preliminary basis as follows (dollars in thousands):

| | Amount assigned | Weighted average amortization period (years) | Probability assigned to revenues |
|-------------------------------|--------------------|--|--|
| | | | |
| Amortizable intangible assets | | | |
| Technology - core | \$ 6,927 | 11 | 100% |
| Technology - developed | 2,774 | 6 | 100% |
| Customer relationships | 14,133 | 11 | 100% |
| Noncompete agreements | 310 | 1 | 50% |
| | | | |

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| | | | |
|------------------------------|----------|------------|-----------|
| | \$24,144 | 10 | |
| Tradenames | \$ 4,330 | indefinite | 100% |
| Acquired IPR&D - Introducers | \$12,640 | - | 60% - 90% |
| Acquired IPR&D - Catheters | \$ 1,200 | - | 70% - 75% |

Core technology - Core technology consists of technical processes, patented and unpatented technology, manufacturing know-how and the understanding with respect to products or processes that have been developed by Enpath and that will be leveraged in future products or processes and will be carried forward from one product generation to the next. Approximately 85 percent of the preliminary value assigned to core technology is associated with Enpath's introducer products. The Company determined that the estimated useful life of the core technology is 11 years. This life is based upon management's estimate of the product life cycle associated with core technology before they will be replaced by new technologies. The expected cash flows associated with core technology were nominal after 11 years.

Developed technology - Developed technology acquired from Enpath represents the preliminary value associated with currently marketed products that have received FDA approval as of the acquisition date. Enpath's currently marketed products include:

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

- o Venous vessel introducers and valved introducers that enable physicians to create a conduit through which they can insert infusion catheters, implantable ports and pacemaker leads into a blood vessel;
- o Advanced delivery catheters that have a "fixed curve" or articulating distal tip section that can be manipulated to enable the health care professional to access parts of the patient's anatomy that cannot be reached by traditional introducers; and
- o Implantable stimulation leads, adaptors and delivery systems for the cardiac and neuromodulation markets.

The Company determined that the estimated useful life of the developed technology is 6 years. This life is based upon management's estimate of the life cycle associated with the above products before they will be replaced by new technologies or the next generation of products. The expected cash flows associated with developed technology were nominal after 6 years.

Customer relationships - Customer relationships represent the preliminary estimated fair value of both the contractual and non-contractual customer relationships Enpath has with OEMs as of the acquisition date. The primary customers of Enpath include C.R. Bard, Boston Scientific, Medtronic and St. Jude Medical, some of which are also customers of Greatbatch. These relationships were valued separately from goodwill at the amount which an independent third party would be willing to pay for these OEM relationships. The Company determined that the estimated useful life of the intangible assets associated with the existing customer relationships is 11 years. This life was based upon historical customer attrition and management's understanding of the industry. The customer relationships

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valuation was modified during the quarter due to the finalization of assumptions used in the excess earnings analysis and primarily related to the allocation of R&D costs between new and existing customers.

Acquired IPR&D - Approximately \$13.8 million of the purchase price represents the preliminary estimated fair value of acquired IPR&D projects that had not yet reached technological feasibility and had no alternative future use. Accordingly, the amount was immediately expensed on the acquisition date. The preliminary value assigned to IPR&D related to introducer projects (\$12.6 million) and catheter projects (\$1.2 million). These projects primarily represent the next generation of products already being sold by Enpath which incorporate new enhancements and customer modifications. The Company expects to commercially launch various introducer products in 2008 and 2009 and various catheter products in 2009 which will replace existing products. For purposes of valuing the acquired research and development, the Company estimated total costs to complete the introducer projects to be approximately \$0.3 million and approximately \$0.5 million to complete the catheter projects. If we are not successful in completing these projects on a timely basis, our future sales from introducers and catheters may be adversely affected resulting in erosion of our market share.

The preliminary fair value of these projects was determined based on the excess earnings method. This model utilized discount rates that took into consideration the internal rate of return expected from the Enpath transaction and applied that rate to risk adjusted revenues. The risk adjustment assigned to the revenues was based upon the stage of completion and the risks surrounding the successful development and commercialization of each of the IPR&D projects. The Company believes that the estimated acquired IPR&D amounts represent the fair value at the date of acquisition and do not exceed the amount an independent third party would pay for the projects. The IPR&D valuation was modified during the quarter due to the finalization of assumptions used in the excess earnings analysis and primarily related to the allocation of R&D costs between new and existing customers.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

Goodwill - The excess of the purchase price over the preliminary fair value of net tangible and intangible assets acquired of \$48.6 million was allocated to goodwill. Various factors contributed to the establishment of goodwill, including: the strategic benefit of entering the neurostimulation and interventional markets; the value of Enpath's highly trained assembled work force; the expected revenue growth over time that is attributable to increased market penetration from future products and customers; and the incremental value to the Company's IMC business from having a leads platform. The goodwill acquired in connection with the Enpath acquisition was allocated to the Company's IMC business segment and is not deductible for tax purposes.

Pro Forma Results - The following unaudited pro forma information presents the consolidated results of operations of the Company and Enpath as if the acquisition of Enpath had occurred as of the beginning of each of the fiscal periods presented (in thousands, except per share amounts):

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| (Unaudited) | Three months ended | | Nine months ended | |
|---------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2007 | September 29, 2006 | September 28, 2007 | September 29, 2006 |
| Sales | \$79,009 | \$78,404 | \$251,949 | \$235,307 |
| Net income | 3,469 | 2,628 | 22,868 | 13,163 |
| Earnings per share: | | | | |
| Basic | \$0.16 | \$0.12 | \$1.03 | \$0.60 |
| Diluted | \$0.15 | \$0.12 | \$0.97 | \$0.59 |

The unaudited pro forma information presents the combined operating results of Greatbatch and Enpath, with the results prior to the acquisition date adjusted to include the pro forma impact of the adjustment of amortization of acquired intangible assets and depreciation of fixed assets based on the preliminary purchase price allocation, the elimination of acquisition expenses incurred by Enpath (\$5.9 million), the elimination of the non-recurring IPR&D charge (\$13.8 million) and inventory step-up adjustment related to the Enpath acquisition recorded by Greatbatch in 2007 (\$1.1 million/\$1.3 million for the three and nine month periods), the adjustment to interest income reflecting the cash paid in connection with the acquisition, including acquisition-related expenses, at Greatbatch's weighted average interest income rate, and the impact of income taxes on the pro forma adjustments utilizing the federal statutory tax rate of 35%, except for IPR&D which is not deductible for tax purposes. The unaudited pro forma consolidated basic and diluted earnings per share are based on the consolidated basic and diluted weighted average shares of Greatbatch.

The unaudited pro forma results are presented for illustrative purposes only and do not reflect the realization of potential cost savings, and any related integration costs. Certain cost savings may result from the acquisition; however, there can be no assurance that these cost savings will be achieved. These pro forma results do not purport to be indicative of the results that would have actually been obtained if the acquisition occurred as of the beginning of each of the periods presented, nor does the pro forma data intend to be a projection of results that may be obtained in the future.

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GREATBATCH, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

3. SUPPLEMENTAL CASH FLOW INFORMATION

| | Nine months ended | |
|---|-----------------------|-----------------------|
| | September 28, 2007 | September 29, 2006 |
| Noncash investing and financing activities (in thousands): | | |
| Net unrealized gain (loss) on available-for-sale securities | \$ (869) | \$ 2,726 |
| Common stock contributed to 401(k) Plan | 2,956 | 2,780 |
| Property, plant and equipment purchases included in accounts payable | 1,958 | 619 |
| Exchange of convertible subordinated notes (Note 7) | 117,782 | - |

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Cash paid during the period for:

| | | | | |
|--|----|---------|----|-------|
| Interest | \$ | 2,429 | \$ | 1,960 |
| Income taxes | | 16,718 | | 2,769 |
| Acquisition of noncash assets and liabilities: | | | | |
| Assets acquired | \$ | 126,182 | \$ | - |
| Liabilities assumed | | 15,678 | | - |

4. SHORT-TERM INVESTMENTS

Short-term investments available for sale are comprised of the following (in thousands):

| | Cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value |
|-------------------------------------|-----------|------------------------|-------------------------|----------------------|
| September 28, 2007 | | | | |
| Auction rate securities and other | \$ 19,774 | \$ - | \$ - | \$ 19,774 |
| Total available for sale securities | \$ 19,774 | \$ - | \$ - | \$ 19,774 |
| December 29, 2006 | | | | |
| Equity securities | \$ 291 | \$ 4,588 | \$ - | \$ 4,879 |
| Auction rate securities and other | 66,537 | 4 | (4) | 66,537 |
| Total available for sale securities | \$ 66,828 | \$ 4,592 | \$ (4) | \$ 71,416 |

In the second quarter of 2007, the Company sold an equity security investment which resulted in a pre-tax gain of \$4.0 million (\$2.6 million net of tax) or \$0.11 per diluted share.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

5. INVENTORIES

Inventories are comprised of the following (in thousands):

| | September 28, 2007 | December 29, 2006 |
|-----------------|--------------------|-------------------|
| Raw materials | \$ 36,341 | \$ 28,568 |
| Work-in-process | 17,748 | 13,528 |
| Finished goods | 14,476 | 15,571 |
| Total | \$ 68,565 | \$ 57,667 |

6. INTANGIBLE ASSETS

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Amortizing intangible assets are comprised of the following (in thousands):

| | Gross carrying amount | Accumulated amortization | Net carrying amount |
|------------------------------------|-----------------------------|-----------------------------|------------------------|
| | ----- | ----- | ----- |
| September 28, 2007 | | | |
| ----- | | | |
| Customer lists | \$ 14,133 | \$ (374) | \$ 13,759 |
| Patented technology | 21,462 | (14,472) | 6,990 |
| Unpatented technology | 40,587 | (12,961) | 27,626 |
| Other | 1,650 | (1,430) | 220 |
| | ----- | ----- | ----- |
| Total amortizing intangible assets | \$ 77,832 | \$ (29,237) | \$ 48,595 |
| | ===== | ===== | ===== |
| December 29, 2006 | | | |
| ----- | | | |
| Patented technology | \$ 21,462 | \$ (13,320) | \$ 8,142 |
| Unpatented technology | 30,886 | (10,975) | 19,911 |
| Other | 1,340 | (1,315) | 25 |
| | ----- | ----- | ----- |
| Total amortizing intangible assets | \$ 53,688 | \$ (25,610) | \$ 28,078 |
| | ===== | ===== | ===== |

Aggregate amortization expense for the third quarter of 2007 and 2006 was \$1.6 million and \$0.9 million, respectively. Aggregate amortization expense for the nine months ended September 28, 2007 and September 29, 2006 was \$3.6 million and \$2.9 million, respectively. As of September 29, 2007, annual amortization expense is estimated to be \$1.6 million for the remainder of 2007, \$6.3 million for 2008, \$5.6 million for 2009, \$5.1 million for 2010, 2011 and 2012.

The change in the carrying amount of goodwill during 2007 is as follows (in thousands):

| | IMC | ECP | Total |
|--------------------------------------|------------|----------|------------|
| | ----- | ----- | ----- |
| Balance at December 29, 2006 | \$ 152,473 | \$ 2,566 | \$ 155,039 |
| Goodwill recorded for BIOMECH | 5,172 | - | 5,172 |
| Goodwill recorded for Enpath | 48,595 | - | 48,595 |
| Resolution of Enpath tax contingency | (20) | - | (20) |
| | ----- | ----- | ----- |
| Balance at September 28, 2007 | \$ 206,220 | \$ 2,566 | \$ 208,786 |
| | ===== | ===== | ===== |

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

7. DEBT

Long-term debt is comprised of the following (in thousands):

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| | September 28, 2007 | December 29, 2006 |
|---|-----------------------|----------------------|
| | ----- | ----- |
| 2.25% convertible subordinated notes I, due 2013 | \$ 52,218 | \$ 170,000 |
| 2.25% convertible subordinated notes II, due 2013 | 197,782 | - |
| Unamortized discount | (9,098) | - |
| | ----- | ----- |
| Total long-term debt | \$ 240,902 | \$ 170,000 |
| | ===== | ===== |

Convertible Subordinated Notes - In May 2003, the Company completed a private placement of \$170 million of 2.25% convertible subordinated notes, due 2013 ("CSN I"). In November 2003, the Company had a registration statement with the Securities and Exchange Commission ("SEC") declared effective with respect to these notes and the underlying common stock. In March 2007, the Company entered into separate, privately negotiated agreements to exchange \$117.8 million of CSN I for an equivalent principal amount of a new series of 2.25% convertible subordinated notes due 2013 ("CSN II") (collectively the "Exchange") at a 5% discount.

The primary purpose of the Exchange was to eliminate the June 15, 2010 call and put option that is included in the terms of CSN I. In connection with the Exchange, the Company issued an additional \$80 million aggregate principal amount of CSN II at a price of \$950 per \$1,000 of principal. In June 2007, the Company had a registration statement with the SEC declared effective with respect to these notes and the underlying common stock.

The Exchange was accounted for as an extinguishment of debt and resulted in a pre-tax gain of \$4.5 million (\$2.9 million net of tax) or \$0.12 per diluted share. As a result of the extinguishment, the Company had to recapture the tax interest expense that was previously deducted on the extinguished notes. This resulted in an additional current income tax liability of approximately \$11.3 million, of which approximately \$8.5 million has been paid as of September 28, 2007 and the remainder will be paid by the end of 2007. This amount was previously recorded as a non-current deferred tax liability on the balance sheet. The following is a summary of the significant terms of CSN I and CSN II:

CSN I - The notes bear interest at 2.25% per annum, payable semi-annually. Holders may convert the notes into shares of the Company's common stock at a conversion rate of 24.8219 shares per \$1,000 of principal, subject to adjustment, before the close of business on June 15, 2013 only under the following circumstances: (1) during any fiscal quarter commencing after July 4, 2003, if the closing sale price of the Company's common stock exceeds 120% of the \$40.29 conversion price for at least 20 trading days in the 30 consecutive trading day period ending on the last trading day of the preceding fiscal quarter; (2) subject to certain exceptions, during the five business days after any five consecutive trading day period in which the trading price per \$1,000 of principal for each day of such period was less than 98% of the product of the closing sale price of the Company's common stock and the number of shares issuable upon conversion of \$1,000 of principal; (3) if the notes have been called for redemption; or (4) upon the occurrence of certain corporate events.

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Beginning June 20, 2010, the Company may redeem any of the notes at a redemption price of 100% of their principal amount, plus accrued interest. Note holders may require the Company to repurchase their notes on June 15, 2010 or at any time prior to their maturity following a fundamental change, as defined in the indenture agreement, at a repurchase price of 100% of their principal amount, plus accrued interest. The notes are subordinated in right of payment to all of our senior indebtedness and effectively subordinated to all debts and other liabilities of the Company's subsidiaries.

Beginning with the six-month interest period commencing June 15, 2010, the Company will pay additional contingent interest during any six-month interest period if the trading price of the notes for each of the five trading days immediately preceding the first day of the interest period equals or exceeds 120% of the principal amount of the notes.

CSN II - The notes bear interest at 2.25% per annum, payable semi-annually. The holders may convert the notes into shares of the Company's common stock at a conversion price of \$34.70 per share, which is equivalent to a conversion ratio of 28.8219 shares per \$1,000 of principal. The conversion price and the conversion ratio will adjust automatically upon certain changes to the Company's capitalization.

The notes are convertible at the option of the holders at such time as: (i) the closing price of the Company's common stock exceeds 150% of the conversion price of the notes for 20 out of 30 consecutive trading days; (ii) the trading price per \$1,000 of principal is less than 98% of the product of the closing sale price of common stock for each day during any five consecutive trading day period and the conversion rate per \$1,000 of principal; (iii) the notes have been called for redemption; (iv) the Company distributes to all holders of common stock rights or warrants entitling them to purchase additional shares of common stock at less than the average closing price of common stock for the ten trading days immediately preceding the announcement of the distribution; (v) the Company distributes to all holders of common stock any form of dividend which has a per share value exceeding 5% of the price of the common stock on the day prior to such date of distribution; (vi) the Company affects a consolidation, merger, share exchange or sale of assets pursuant to which its common stock is converted to cash or other property; (vii) the period beginning 60 days prior to but excluding June 15, 2013; and (viii) certain fundamental changes, as defined in the indenture agreement, occur or are approved by the Board of Directors.

Conversions in connection with corporate transactions that constitute a fundamental change require the Company to pay a premium make-whole amount whereby the conversion ratio on the notes may be increased by up to 8.2 shares per \$1,000 of principal. The premium make-whole amount will be paid in shares of common stock upon any such conversion, subject to the net share settlement feature of the notes described below.

The notes contain a net share settlement feature that requires the Company to pay cash for each \$1,000 of principal. Any amounts in excess of \$1,000 will be settled in shares of the Company's common stock, or at the Company's option, cash. The Company has a one-time irrevocable election to pay the holders in shares of its common stock, which it currently does not plan to exercise.

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The notes are redeemable by the Company at any time on or after June 20, 2012, or at the option of a holder upon the occurrence of certain fundamental changes, as defined in the agreement, affecting the Company. The notes are subordinated in right of payment to all of our senior indebtedness and effectively subordinated to all debts and other liabilities of the Company's subsidiaries.

Revolving Line of Credit - In May 2007, the Company entered into a new senior credit facility (the "New Credit Facility") consisting of a \$235 million revolving credit facility, which can be increased to \$335 million upon the Company's request. The New Credit Facility also contains a \$15 million letter of credit subfacility and a \$15 million swingline subfacility. This New Credit Facility replaced the Company's previous \$50 million revolving credit facility. The New Credit Facility is secured by the Company's non-realty assets including cash, accounts and notes receivable, and inventories, and has an expiration date of May 22, 2012 with a one-time option to extend to April 1, 2013 if no default has occurred. Interest rates under the New Credit Facility are, at the Company's option, based upon the current prime rate or the LIBOR rate plus a margin that varies with the Company's leverage ratio. If interest is paid based upon the prime rate, the applicable margin is between minus 1.25% and 0.00%. If interest is paid based upon the LIBOR rate, the applicable margin is between 1.00% and 2.00%. The Company is required to pay a commitment fee between 0.125% and 0.250% per annum on the unused portion of the New Credit Facility based on the Company's leverage ratio.

The New Credit Facility contains limitations on the incurrence of indebtedness, limitations on the incurrence of liens and licensing of intellectual property, limitations on investments and restrictions on certain payments. Except to the extent paid for by common equity of Greatbatch or paid for out of cash on hand, the New Credit Facility limits the amount paid for acquisitions to \$100 million. The restrictions on payments, among other things, limit repurchases of Greatbatch's stock to \$60 million and limits the ability of the Company to make cash payments upon conversion of CSN II.

In addition, the New Credit Facility requires the Company to maintain a ratio of adjusted EBITDA, as defined in the credit agreement, to interest expense of at least 3.00 to 1.00, and a total leverage ratio, as defined in the credit agreement, of not greater than 5.00 to 1.00 from May 22, 2007 through September 29, 2009 and not greater than 4.50 to 1.00 from September 30, 2009 and thereafter.

The New Credit Facility contains customary events of default. Upon the occurrence and during the continuance of an event of default, a majority of the lenders may declare the outstanding advances and all other obligations under the New Credit Facility immediately due and payable.

There were no borrowings outstanding under the New Credit Facility as of September 28, 2007.

Deferred Financing Fees - The following is a reconciliation of deferred financing fees for the third quarter of 2007, which are included in other assets (in thousands):

| | | |
|--------------------------|----|-------|
| Balance at June 29, 2007 | \$ | 7,031 |
|--------------------------|----|-------|

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| | | |
|--------------------------------|----|-------|
| Financing costs deferred | | 11 |
| Write-off during the period | | - |
| Amortization during the period | | (339) |
| | | ----- |
| Balance at September 28, 2007 | \$ | 6,703 |
| | | ===== |

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

8. STOCK-BASED COMPENSATION

Beginning in fiscal year 2006, the Company adopted SFAS No. 123 (revised 2004), Share-Based Payment ("SFAS No. 123(R)"), and related SEC rules included in Staff Accounting Bulletin ("SAB") No. 107. Under SFAS No. 123(R) the Company records compensation costs related to all stock-based awards. Compensation costs related to share-based payments for the three and nine months ended September 28, 2007 totaled \$1.4 million, \$0.9 million net of tax, or \$0.4 per diluted share and \$4.3 million, \$2.8 million net of tax, or \$0.11 per diluted share, respectively. This compares to \$1.6 million, \$1.1 million net of tax, or \$0.05 per diluted share and \$4.2 million, \$2.8 million net of tax, or \$0.11 per diluted share for the three and nine months ended September 29, 2006, respectively.

The following table summarizes stock option activity related to the Company's stock-based incentive plans:

| | Number of stock options | Weighted average exercise price | Weighted average remaining contractual life (in years) | Aggregate intrinsic value(1) (in millions) |
|-----------------------------------|----------------------------|--|---|---|
| Outstanding at January 1, 2006 | 1,397,160 | \$ 23.16 | | |
| Granted(2) | 483,265 | 23.92 | | |
| Exercised | (160,605) | 12.97 | | |
| Forfeited or Expired | (93,291) | 24.94 | | |
| | ----- | | | |
| Outstanding at December 29, 2006 | 1,626,529 | \$ 24.27 | 7.4 | \$6.4 |
| Granted(3) | 334,613 | 27.63 | | |
| Exercised | (141,302) | 19.10 | | |
| Forfeited or Expired | (117,576) | 27.50 | | |
| | ----- | | | |
| Outstanding at September 28, 2007 | 1,702,264 | \$ 25.17 | 7.4 | \$5.0 |
| | ===== | | | |
| Exercisable at September 28, 2007 | 788,492 | \$ 26.04 | 5.8 | \$2.4 |
| | ===== | | | |

(1) Intrinsic value is calculated for in-the-money options (exercise price less than market price) outstanding and/or exercisable as the

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difference between the market price of our common shares as of September 28, 2007 (\$26.59) and the weighted average exercise price of the underlying options, multiplied by the number of options outstanding and/or exercisable.

- (2) Includes 183,648 performance based stock options which had a weighted average exercise price of \$22.38 per share.
- (3) Includes 146,231 performance based stock options which had a weighted average exercise price of \$29.65 per share.

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GREATBATCH, INC.

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The weighted-average fair value and assumptions used to value options granted are as follows:

| | Nine months ended | |
|-----------------------------|-----------------------|-----------------------|
| | September 28, 2007 | September 29, 2006 |
| Weighted-average fair value | \$12.33 | \$10.85 |
| Risk-free interest rate | 4.62% | 4.74% |
| Expected volatility | 41% | 43% |
| Expected life (in years) | 5.4 | 5.4 |
| Expected dividend yield | 0% | 0% |

The following table summarizes restricted stock and restricted stock unit activity related to the Company's plans:

| | Activity | Weighted average fair value |
|---------------------------------|----------|--------------------------------|
| Nonvested at January 1, 2006 | 93,956 | \$ 22.46 |
| Shares granted | 145,126 | 23.25 |
| Shares vested | (25,911) | 20.00 |
| Shares forfeited | (9,015) | 22.63 |
| | | |
| Nonvested at December 29, 2006 | 204,156 | \$ 23.32 |
| Shares granted | 113,531 | 27.33 |
| Shares vested | (9,436) | 25.50 |
| Shares forfeited | (7,618) | 23.30 |
| | | |
| Nonvested at September 28, 2007 | 300,633 | \$ 24.77 |

At the Company's 2007 Annual Meeting of Stockholders held on May 22, 2007, an amendment to the Company's 2005 Stock Incentive Plan was approved by stockholders which increased the number of shares available for grant by 1,450,000 shares.

9. OTHER OPERATING EXPENSE

The following were recorded in other operating expense, net in the Company's Consolidated Statements of Operations and Comprehensive Income (in thousands):

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| | Three months ended | | Nine m |
|---|-----------------------|-----------------------|----------------------|
| | September 28, 2007 | September 29, 2006 | September 28 2007 |
| (a) Alden facility consolidation | \$ - | \$ - | \$ |
| (b) Carson City facility shutdown and Tijuana facility consolidation No. 1 | 10 | 411 | 58 |
| (c) Columbia facility shutdown, Tijuana facility consolidation No. 2 and RD&E consolidation | 1,030 | 1,225 | 3,70 |
| (d) ECP expansion | 126 | - | 40 |
| (e) Asset dispositions and other | 109 | 4,603 | 9 |
| | <u>\$ 1,275</u> | <u>\$ 6,239</u> | <u>\$ 4,79</u> |

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GREATBATCH, INC.

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(a) Alden Facility consolidation - Beginning in the first quarter of 2005 and ending in the second quarter of 2006 the Company consolidated the medical capacitor manufacturing operations in Cheektowaga, NY, and the implantable medical battery manufacturing operations in Clarence, NY, into the advanced power source manufacturing facility in Alden, NY ("Alden Facility"). The Company also consolidated the capacitor research, development and engineering operations from the Cheektowaga, NY facility into the Technology Center in Clarence, NY.

The total cost for these consolidation efforts was \$3.4 million, which was below the Company's original estimate of \$3.5 to \$4.0 million. The expenses for the Alden Facility consolidation are included in the IMC business segment and included the following:

- o Production inefficiencies and revalidation - \$0.3 million;
- o Moving and facility closures - \$2.7 million; and
- o Other - \$0.4 million.

(b) Carson City Facility shutdown and Tijuana Facility consolidation No. 1. On March 7, 2005, the Company announced its intent to close the Carson City, NV facility ("Carson City Facility") and consolidate the work performed at that facility into the Tijuana, Mexico facility ("Tijuana Facility consolidation No. 1").

The Company ceased operating at the Carson City Facility on July 15, 2007. The total cost for this consolidation effort was \$7.8 million. The major categories of costs include the following:

- o Costs related to the shutdown of the Carson City Facility:
 - a. Severance and retention - \$3.9 million;
 - b. Accelerated depreciation - \$0.6 million; and
 - c. Other - \$0.3 million.
- o Costs related to the Tijuana Facility consolidation No. 1:

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- a. Production inefficiencies and revalidation - \$0.5 million;
- b. Relocation and moving - \$0.1 million;
- c. Personnel (including travel, training and duplicate wages) - \$1.7 million; and
- d. Other - \$0.7 million.

All categories of costs are considered to be cash expenditures, except accelerated depreciation. The Company anticipates annual cost savings in the range of \$2.5 million to \$3.1 million. The expenses for the Carson City Facility shutdown and the Tijuana Facility consolidation No. 1 are included in the IMC business segment.

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GREATBATCH, INC.

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Accrued liabilities related to the Carson City Facility shutdown are comprised of the following (in thousands):

| | Severance and retention | Accelerated depreciation | Other | |
|-----------------------------|----------------------------|-----------------------------|--------|----|
| Restructuring charges | \$ 3,551 | \$ 600 | \$ 278 | \$ |
| Cash payments | (2,394) | - | (278) | |
| Write-offs | - | (600) | - | |
| Balance, December 29, 2006 | \$ 1,157 | \$ - | \$ - | \$ |
| Restructuring charges | 338 | - | 26 | |
| Cash payments | (1,020) | - | (26) | |
| Balance, September 28, 2007 | \$ 475 | \$ - | \$ - | \$ |

Accrued liabilities related to the Tijuana Facility consolidation No. 1 are comprised of the following (in thousands):

| | Production inefficiencies and revalidation | Relocation and moving | Personnel | Ot |
|-----------------------------|--|--------------------------|-----------|----|
| Restructuring charges | \$ 293 | \$ 124 | \$ 1,701 | \$ |
| Cash payments | (293) | (124) | (1,701) | |
| Balance, December 29, 2006 | \$ - | \$ - | \$ - | \$ |
| Restructuring charges | 220 | - | - | |
| Cash payments | (220) | - | - | |
| Balance, September 28, 2007 | \$ - | \$ - | \$ - | \$ |

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(c) Columbia Facility shutdown, Tijuana Facility consolidation No. 2 and RD&E consolidation. On November 16, 2005, the Company announced its intent to close both the Columbia, MD facility ("Columbia Facility") and the Fremont, CA Advanced Research Laboratory ("ARL"). The Company also announced that the manufacturing operations at the Columbia Facility will be moved into the Tijuana Facility ("Tijuana Facility consolidation No. 2") and that the research, development and engineering ("RD&E") and product development functions at the Columbia Facility and at ARL will relocate to the Technology Center in Clarence, NY.

The total estimated cost for this facility consolidation plan is anticipated to be between \$11.1 million and \$11.6 million of which \$10.0 million has been incurred through September 28, 2007. The ARL move and closure portion of this consolidation project is complete. The Company expects to incur the remaining cost for the other portions of the consolidation project in 2007 and the first quarter of 2008, with cash payments being made through the second quarter of 2008.

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GREATBATCH, INC.

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The major categories of costs include the following:

- o Costs related to the shutdown of the Columbia Facility and ARL and the move and consolidation of the RD&E functions to Clarence, NY:
 - a. Severance and retention - \$3.7 to \$3.9 million;
 - b. Personnel (including travel, training and duplicate wages) - \$1.4 million ;
 - c. Accelerated depreciation/asset write-offs - \$0.5 million; and d. Other - \$0.4 to \$0.5 million.

- o Costs related to Tijuana Facility consolidation No. 2:
 - a. Production inefficiencies and revalidation - \$1.0 to \$1.1 million;
 - b. Relocation and moving - \$0.3 million;
 - c. Personnel (including travel, training and duplicate wages) - \$2.9 to \$3.0 million; and
 - d. Other (including asset write-offs) - \$0.9 million.

All categories of costs are considered to be cash expenditures, except for accelerated depreciation and asset write-offs. Once the moves are completed, the Company anticipates annual cost savings in the range of \$5.0 million to \$6.0 million. The expenses for the Columbia Facility and ARL shutdowns, the Tijuana Facility consolidation No. 2 and the RD&E consolidation are included in the IMC business segment.

Accrued liabilities related to the Columbia Facility and ARL shutdowns and the RD&E consolidation are comprised of the following (in thousands):

| | Severance and retention | | Personnel | | Accelerated depreciation / asset write-offs | | Other |
|-----------------------|-------------------------------|----|-----------|----|---|----|-------|
| | | | | | | | |
| Restructuring charges | \$ 2,297 | \$ | 701 | \$ | 509 | \$ | |
| Cash payments | (550) | | (701) | | - | | |

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| | | | |
|-----------------------------|----------|-------|-------|
| Write-offs | - | - | (509) |
| Balance, December 29, 2006 | \$ 1,747 | \$ - | \$ - |
| Restructuring charges | 1,127 | 363 | (54) |
| Cash payments | (990) | (363) | - |
| Write-offs | - | - | 54 |
| Balance, September 28, 2007 | \$ 1,884 | \$ - | \$ - |

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Accrued liabilities related to Tijuana Facility consolidation No. 2 are comprised of the following (in thousands):

| | Production inefficiencies and revalidation | Relocation and moving | Personnel | Other |
|-----------------------------|--|--------------------------|-----------|-------|
| Restructuring charges | \$ 264 | \$ 149 | \$ 1,594 | \$ - |
| Cash payments | (264) | (149) | (1,594) | - |
| Balance, December 29, 2006 | \$ - | \$ - | \$ - | \$ - |
| Restructuring charges | 770 | 109 | 880 | - |
| Cash payments | (770) | (109) | (880) | - |
| Balance, September 28, 2007 | \$ - | \$ - | \$ - | \$ - |

(d) Electrochem Commercial Power ("ECP") expansion. In February 2007, the Company announced that it will close its current manufacturing facility in Canton, MA and construct a new 80,000 square foot replacement facility in the Massachusetts area. The expected completion of this \$28 million expansion project is mid-2008. The total expense to be recognized for this relocation is estimated to be \$2.2 million to \$2.4 million, of which \$0.4 million has been incurred primarily related to accelerated depreciation. Costs related to this move are included in the ECP business segment and include the following:

- o Production inefficiencies and revalidation - \$0.6 million;
- o Moving and facility closure - \$0.9 million to \$1.0 million;
- o Accelerated depreciation - \$0.4 million; and
- o Other - \$0.3 million to \$0.4 million.

(e) Asset dispositions and other. During the third quarter of 2007, the Company had various asset dispositions. During the third quarter of 2006, the Company recorded a loss of \$4.4 million related to the write-off of a battery test system that was under development. Upon completion of the Company's engineering and technical evaluation, it was determined that the system could not meet the required specifications in a cost effective manner. This charge was included in the IMC business segment.

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In addition to the quarter disposals discussed above, the nine month period in 2007 includes \$0.3 million of insurance proceeds received related to equipment damaged during transportation to the Tijuana Facility. The nine month period of 2006 also includes the loss of \$0.5 million related to this equipment damaged (included in the IMC business segment) and an expense of \$0.8 million for professional fees related to a potential acquisition that we no longer considered probable.

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10. INCOME TAXES

Effective in the first quarter of 2007, the Company adopted the provisions of Financial Standards Accounting Board ("FASB") Interpretation ("FIN") No. 48 Accounting for Uncertainty in Income Taxes, an interpretation of SFAS No. 109. FIN No. 48, clarifies the accounting for uncertainty in income taxes recognized under SFAS No. 109. Additionally, in May 2007, the FASB published FASB Staff Position ("FSP") No. FIN No. 48-1, Definition of Settlement in FASB Interpretation No. 48, which clarifies how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. As of our adoption date of FIN No. 48, our accounting is consistent with the guidance in FSP FIN No. 48-1.

Upon adoption of FIN No. 48, the Company did not recognize any adjustment to its \$1.8 million of unrecognized tax benefits, all of which would favorably impact the effective tax rate (net of federal benefit on state issues), if recognized. The Company's unrecognized tax benefits consist of refund claims which did not meet the more likely than not threshold under FIN No. 48.

During the third quarter of 2007, the balance of unrecognized tax benefits increased approximately \$0.1 million as a result of filing positions taken on our 2006 tax returns. As of September 28, 2007, approximately \$0.3 million of unrecognized tax benefits would impact goodwill if recognized. Of the remaining approximately \$1.6 million of unrecognized tax benefits, approximately \$1.3 million would favorably impact the effective tax rate (net of federal benefit on state issues), if recognized. The Company anticipates that the total unrecognized tax benefits could significantly change within the next twelve months due to the settlement of audits/appeals currently in process, however, quantification of an estimated range cannot be made at this time.

The tax years 2004-2006 remain open to examination by the major taxing jurisdictions to which we are subject. The 2001 - 2003 tax years remain open in certain jurisdictions as a result of audits/appeals currently in process.

The effective tax rate for 2007 includes the impact of the \$16.1 million of acquired IPR&D written off, \$13.8 million of which is not deductible for tax purposes. Excluding this expense, the effective tax rate for the three and nine months ended September 28, 2007 would have been approximately 32% compared to 24.3% and 32.5% for the same periods of 2006, respectively. During the third quarter of 2006, we adjusted our tax accounts to reflect the filing of our 2005 tax returns as well as the completion of various tax

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savings initiatives which resulted in the lower effective tax rate for that period.

Subsequent to the end of the third quarter, Mexico enacted new tax legislation that will take effect on January 1, 2008. We are currently evaluating the impact of this tax law change on our financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

11. COMMITMENTS AND CONTINGENCIES

Litigation - The Company is a party to various legal actions arising in the normal course of business. While the Company does not believe that the ultimate resolution of any such pending activities will have a material adverse effect on its consolidated results of operations, financial position or cash flows, litigation is subject to inherent uncertainties. If an unfavorable ruling were to occur, there exists the possibility of a material adverse impact in the period in which the ruling occurs.

During 2002, a former non-medical customer commenced an action alleging that Greatbatch had used proprietary information of the customer to develop certain products. We have meritorious defenses and are vigorously defending the matter. The potential risk of loss is between \$0.0 and \$1.7 million.

In connection with our acquisition of Enpath Medical, Inc. ("Enpath"), we assumed liability in connection with the following proceeding:

On June 12, 2006, Enpath was named as defendant in a patent infringement action filed by Pressure Products Medical Supplies, Inc. and venued in the United States District Court in the Eastern District of Texas. On October 2, 2006, Enpath was officially served. Enpath has filed an answer denying liability and has filed counterclaims against the plaintiff alleging antitrust violations and patent misuse. The plaintiff has alleged that Enpath's FlowGuard(TM) valved introducer, which has been on the market for more than three years, infringes claims in the plaintiff's patents and is seeking damages and injunctive relief. Enpath believes that the plaintiff's claims are without merit and intends to pursue its defenses vigorously. Revenues from products sold that include the FlowGuard valved introducer were approximately 5% of Enpath's total revenue for 2007 (\$29.3 million), 2006 (\$36.8 million) and 2005 (\$29.4 million). The lawsuit is currently in the discovery stage. The District Court held a hearing to construe the claims of the plaintiff's patents in August 2007, but has not yet issued its decision. It is not possible to predict the timing or outcome of this litigation at this time, including whether it will affect the Company's ability to sell its FlowGuard products, or to estimate the amount or range of potential loss.

Product Warranties - The Company generally warrants that its products will meet customer specifications and will be free from defects in materials and workmanship. The Company accrues its estimated exposure to warranty claims based upon recent historical experience and other specific information as it becomes available.

The change in aggregate product warranty liability for the quarter ended September 28, 2007 is as follows (in thousands):

| | | |
|------------------------------------|----|-------|
| Beginning balance at June 29, 2007 | \$ | 1,817 |
|------------------------------------|----|-------|

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| | |
|--------------------------------------|----------|
| Reductions to warranty reserve | (251) |
| Warranty claims paid | (340) |
| | ----- |
| Ending balance at September 28, 2007 | \$ 1,226 |
| | ===== |

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

Purchase Commitments - Contractual obligations for purchase of goods or services are defined as agreements that are enforceable and legally binding on the Company and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Our purchase orders are normally based on our current manufacturing needs and are fulfilled by our vendors within short time horizons. We enter into blanket orders with vendors that have preferred pricing and terms, however these orders are normally cancelable by us without penalty. As of September 28, 2007, the total contractual obligation related to such expenditures is approximately \$32.9 million and primarily relate to the construction of our new ECP manufacturing facility and the expansion of our corporate headquarters. These commitments will be financed by existing cash, short-term investments or cash generated from operations. We also enter into contracts for outsourced services; however, the obligations under these contracts were not significant and the contracts generally contain clauses allowing for cancellation without significant penalty.

12. EARNINGS PER SHARE

The following table reflects the calculation of basic and diluted earnings per share (in thousands, except per share amounts):

| | Three months ended | | Ni |
|---|--------------------|--------------------|--------------|
| | September 28, 2007 | September 29, 2006 | September 20 |
| | ----- | ----- | ----- |
| Numerator for basic earnings per share: | | | |
| Net income | \$ 5,000 | \$ 3,239 | \$ |
| Effect of dilutive securities: | | | |
| Interest expense on convertible notes and related deferred financing fees, net of tax | 223 | - | |
| Numerator for diluted earnings per share | \$ 5,223 | \$ 3,239 | \$ |
| | ===== | ===== | ===== |
| Denominator for basic earnings per share: | | | |
| Weighted average shares outstanding | 22,214 | 21,816 | |
| Effect of dilutive securities: | | | |
| Convertible subordinated notes | 1,296 | - | |
| Stock options and unvested restricted stock | 362 | 167 | |
| Dilutive potential common shares | 1,658 | 167 | |
| | ----- | ----- | ----- |
| Denominator for diluted earnings per share | 23,872 | 21,983 | |
| | ===== | ===== | ===== |

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| | | | | | |
|----------------------------|-------|------|-------|------|-------|
| Basic earnings per share | \$ | 0.23 | \$ | 0.15 | \$ |
| | ===== | | ===== | | ===== |
| Diluted earnings per share | \$ | 0.22 | \$ | 0.15 | \$ |
| | ===== | | ===== | | ===== |

The 2007 diluted weighted average share calculations do not include stock options of 319,000 and 600,000 for the three and nine month periods, respectively, as they are not dilutive to the earnings per share calculations. The 2006 diluted weighted average share calculations do not include 1,193,000 stock options for the three and nine month periods and 4,219,000 shares related to the Company's convertible subordinated notes for the three month period as they are not dilutive to the earnings per share calculations. The diluted weighted average share calculations for both periods in 2007 and 2006 also do not include 338,000 shares and 235,000 shares, respectively, of performance based stock options and restricted stock units as the performance criteria for those awards had not been met.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

13. COMPREHENSIVE INCOME

The Company's comprehensive income includes net income and the net unrealized gain (loss) on its short-term investments available for sale adjusted for any realized gains/losses. The net unrealized gain (loss) on short-term investments available for sale reported on the Condensed Consolidated Statements of Operations and Comprehensive Income are shown net of a deferred income tax benefit of \$0.5 million for the nine month period of 2007 and deferred income tax benefit of \$0.06 million and deferred tax expense of \$0.6 million for the three and nine month periods of 2006, respectively.

14. BUSINESS SEGMENT INFORMATION

The Company operates its business in two reportable segments: Implantable Medical Components ("IMC") and Electrochem Commercial Power ("ECP"). The IMC segment designs and manufactures critical components used in implantable medical devices. The principal components are batteries, capacitors, filtered feedthroughs, enclosures and precision components. Additionally, the IMC business includes value-added assembly of products that incorporate these components. The principal medical devices are pacemakers, defibrillators and neurostimulators. The IMC business segment also includes the operations acquired from Enpath and BIOMEC in 2007 (see Note 2), from the date of acquisition. The Enpath operations include revenue from designing, developing, manufacturing and marketing single use medical device products for the CRM, neuromodulation and interventional radiology markets including venous vessel and valved introducers, advanced delivery catheters that have a "fixed curve" or articulating distal tip section and implantable stimulation leads, adaptors and delivery systems for the cardiac and neuromodulation markets.

The ECP segment designs and manufactures high performance batteries and battery packs; principal markets for these products are for oil and gas exploration, pipeline inspection, telematics, oceanography equipment, seismic, communication, military and aerospace applications.

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The Company defines segment income from operations as sales less cost of sales, including amortization, and expenses attributable to segment-specific selling, general, administrative, research, development, engineering and other operating expenses. Segment income also includes a portion of non-segment specific selling, general, administrative, research, development and engineering expenses based on allocations appropriate to the expense categories. The remaining unallocated operating expenses are primarily corporate headquarters and administrative function expenses. The unallocated operating expenses along with other income and expense are not allocated to reportable segments. Transactions between the two segments are not significant.

The 2007 results for the IMC segment includes a \$16.1 million IPR&D charge related to the BIOMECH and Enpath acquisitions.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

An analysis and reconciliation of the Company's business segment information to the respective information in the consolidated financial statements is as follows (in thousands):

| | Three months ended | | | Nine |
|--|-----------------------|-----------------------|----|--|
| | September 28, 2007 | September 29, 2006 | | Months ended September 28, 2007 |
| Sales: | | | | |
| IMC | | | | |
| ICD batteries | \$ 12,265 | \$ 11,456 | \$ | 37 |
| Pacemaker and other batteries | 4,701 | 4,439 | | 16 |
| ICD capacitors | 5,782 | 4,499 | | 22 |
| Feedthroughs | 14,448 | 17,355 | | 49 |
| Enclosures | 4,584 | 5,698 | | 16 |
| Introducers, catheters and leads | 10,047 | - | | 11 |
| Other medical | 15,176 | 13,560 | | 45 |
| Total IMC | 67,003 | 57,007 | | 199 |
| ECP | 12,006 | 12,287 | | 34 |
| Total sales | \$ 79,009 | \$ 69,294 | \$ | 234 |
| Segment income from operations: | | | | |
| IMC | \$ 10,930 | \$ 3,476 | \$ | 18 |
| ECP | 2,445 | 3,976 | | 7 |
| Total segment income from operations | 13,375 | 7,452 | | 25 |
| Unallocated operating expenses | (3,035) | (3,387) | | (11) |
| Operating income as reported | 10,340 | 4,065 | | 14 |
| Unallocated other income (expense) | (596) | 215 | | 9 |
| Income before provision for income taxes as reported | \$ 9,744 | \$ 4,280 | \$ | 23 |

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15. SUBSEQUENT EVENTS

On October 29, 2007, the Company announced that its wholly-owned subsidiary, Electrochem Commercial Power, acquired substantially all of the assets of IntelliSensing LLC ("IntelliSensing") for approximately \$3.9 million in cash plus/minus any working capital adjustment as defined in the purchase agreement. IntelliSensing designs and manufactures wireless sensor solutions that measure temperature, pressure, flow and other critical data.

On October 30, 2007, the Company announced that it has signed a definitive agreement to acquire substantially all of the assets of Quan Emerteq LLC ("Quan Emerteq") for approximately \$55 million in cash plus/minus any working capital adjustment as defined in the purchase agreement. The Company expects to close this transaction in November 2007. Quan Emerteq designs, develops and manufactures single use medical device products for the vascular, cardiac rhythm management and neurostimulation markets.

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GREATBATCH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (con't) - Unaudited

On November 5, 2007, the Company announced that its wholly-owned subsidiary, Electrochem Commercial Power, signed a definitive agreement to acquire substantially all of the assets of Engineered Assemblies Corporation ("EAC") for approximately \$12 million in cash plus/minus any working capital adjustment as defined in the purchase agreement. The Company expects to close this transaction in November 2007. EAC is a leading provider of custom battery solutions and electronics integration focused on rechargeable battery systems.

16. IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

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. This Statement provides entities with an option to choose to measure eligible items at fair value at specified election dates. If elected, an entity must report unrealized gains and losses on the item in earnings at each subsequent reporting date. The fair value option may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method, is irrevocable (unless a new election date occurs), and is applied only to entire instruments and not to portions of instruments. The Company is still evaluating the impact of SFAS No. 159 on its financial statements, which is effective beginning in fiscal year 2008.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value while applying generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions based on market data obtained from independent sources and (2) the reporting entity's own assumptions developed based on unobservable inputs. The Company is still evaluating the impact of SFAS No. 157 on its financial statements, which is effective beginning in fiscal year 2008.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our Business

We are a leading developer and manufacturer of batteries, capacitors, feedthroughs, enclosures, and other components used in implantable medical devices ("IMDs") through our Implantable Medical Components ("IMC") business. We offer technologically advanced, highly reliable and long lasting products that enable our customers to introduce IMDs that are progressively smaller, longer lasting, more efficient and more functional. Additionally, through our manufacturing facility in Tijuana Mexico, our IMC business includes value-added assembly of products that incorporates the components we manufacture. We also leverage our core competencies in technology and manufacturing through our Electrochem Commercial Power ("ECP") business to develop and produce cells and battery packs for commercial applications that demand high performance and reliability, including oil and gas exploration, pipeline inspection, telematics, oceanographic equipment, seismic, communication, military and aerospace applications.

Most of the IMC products that we sell are utilized by customers in cardiac rhythm management ("CRM") devices. The CRM market comprises devices utilizing high-rate batteries and capacitors such as implantable cardioverter defibrillators ("ICDs") and cardiac resynchronization therapy ("CRT") with backup defibrillation devices ("CRT-D") and devices utilizing low or medium rate batteries but no capacitors (pacemakers and CRTs). All CRM devices utilize other components such as enclosures and feedthroughs, and certain CRM devices utilize electromagnetic interference ("EMI") filtering technology. With the acquisition of Enpath Medical, Inc. ("Enpath") in 2007, we now develop and manufacture vascular access devices used primarily in the CRM market. These include venous vessel and valved introducers, advanced delivery catheters that have a "fixed curve" or articulating distal tip section, and implantable stimulation leads, adaptors and delivery systems for the cardiac and neuromodulation markets.

Our Customers

Our products are designed to provide reliable, long lasting solutions that meet the evolving requirements and needs of our customers and the end users of their products. Our medical customers include leading IMD manufacturers such as Boston Scientific, St. Jude Medical, Medtronic, Biotronik, Cyberonics and the Sorin Group. A substantial part of our business is conducted with a limited number of customers. For the first nine months of 2007, Boston Scientific, Medtronic and St. Jude Medical collectively accounted for approximately 67% of our total sales. With the acquisition of Enpath in 2007, we were able to deepen our relationships with many of our larger customers while at the same time broadening both our market and product reach. The nature and extent of our selling relationships with each CRM customer are different in terms of breadth of component products purchased, purchased product volumes, length of contractual commitment, ordering patterns, inventory management and selling prices.

Our ECP customers are primarily companies involved in oil and gas exploration, pipeline inspection, telematics, oceanographic equipment, seismic, communication, military and aerospace applications industries.

We have entered into long-term supply agreements with some of our customers. For each of our products, we recognize revenue when the products are shipped and

title passes.

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Business Highlights

Our CEO's View

This was our third consecutive quarter of record sales, which included the benefits of our acquisition growth strategy. After adjusting for the acquisition of Enpath, our organic growth rate for the year is 7%, which exceeds our market growth rate, and sales were consistent with the prior year quarter due to customer inventory adjustments. Additionally, our manufacturing initiatives have led to improvement in our cost of sales as a percentage of sales. Even though we have been impacted by our customer actions in the short-term, we are positioned to take advantage of our long-term growth opportunities as we further leverage our Company.

On a strategic front, the recently announced acquisitions (see Note 15 of the Condensed Consolidated Financial Statements), combined with the earlier acquisitions of Enpath and BIOMECH, are enhancing the overall capabilities of Greatbatch including 1) increasing our CRM, neurostimulation and commercial market presence, 2) enhancing our product offering by providing new competencies in the areas of rechargeable cells, wireless sensors, enhanced design and prototyping capabilities, regulatory expertise and established important clinical relationships and 3) giving us entree into the therapy delivery markets, which brings new growth opportunities and several new blue chip customers allowing for cross selling opportunities. The business model of the acquired companies is very synergistic with the strategic direction of Greatbatch - technology leadership through proprietary innovation - and supports our device field of view of becoming an even more important OEM supplier through added customer content and capabilities.

Product Development

Currently, the company is developing a series of new products for customer applications in the CRM, neurostimulation and commercial markets.

Some of the key development initiatives are as follows:

1. Continue the evolution of our Q series high rate ICD batteries.
2. Complete the development of a high voltage and high energy density capacitor system.
3. Develop Q series medium rate battery for neurostimulation and pacemaker applications.
4. Augment our existing rechargeable battery with a new rechargeable battery offering for use in neurostimulation applications.
5. Develop MRI compatible technology for our medical components.
6. Develop rechargeable battery packs for use in commercial applications.
7. Continue development of the batteries and capacitors used in intravascular ICD devices.

IMC. Our near term focus for growth in the medical battery market, a portion of our IMC business, is the introduction of our Q-Series batteries. Initially they will be available in two configurations - QHR (High Rate) and QMR (Medium Rate). These batteries hold the promise of unparalleled performance in a wide range of implantable device and neurostimulation applications and allow our customers to

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incorporate advanced power-hungry features into these devices. These batteries deliver advanced performance to an industry that historically embraces new products. We believe the Q-Series will represent a major breakthrough by combining a smaller size with greater energy density (more power). The first ICD device implant with our new QHR technology occurred in the third quarter of 2006. We also released a new, non-proprietary model of medium-rate implantable "Q" series battery. Our rechargeable battery program also continues to make progress in qualification and is receiving tremendous interest from neurostimulation customers.

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In addition to our battery programs, we continue to advance our ICD capacitor technology with the development of a higher energy capacitor expected for release in 2009. Furthermore, we continue to develop the technology for a next generation higher voltage capacitor.

Finally, enabling safe MRI device interaction continues to remain a key focus and represents a potential growth opportunity for the company. We anticipate unveiling a series of new technologies in this area in the near future.

With the acquisition of BIOMECH, we now offer our customers device engineering expertise along with full device assembly utilizing our proprietary components. This enables us to work in conjunction with our customer's design teams to build more sophisticated devices. Approximately \$2.3 million of the BIOMECH purchase price was allocated to the estimated fair value of acquired in-process research and development ("IPR&D") projects that had not yet reached technological feasibility and had no alternative future use as of the acquisition date. The value assigned to IPR&D relates to projects that incorporate BIOMECH's novel-polymer coating (biomimetic) technology that mimics the surface of endothelial cells of blood vessels. The estimated fair value of these projects was determined using a discounted cash flow model. This model utilized discount rates that took into consideration the stage of completion and the risks surrounding the successful development and commercialization of each of the IPR&D projects of approximately 40% which is consistent with these projects being in the early development stage. The Company expects various products that utilize the biomimetic coatings technology to be commercially launched by original equipment manufacturers ("OEM") in 2009 once Food and Drug Administration ("FDA") approval is received. With BIOMECH, the Company acquired grants that will fund the remaining development costs for these products. There were no significant changes from our original estimates with regards to these projects during the third quarter of 2007.

With the acquisition of Enpath, we added a complementary business that further expands our product and service offerings to the CRM and neurostimulation marketplaces. This acquisition also broadened our market reach into the vascular segment as well as added several new customers. These factors support our long-term objective of customer and market diversification. Enpath's currently marketed products include:

- o Venous vessel introducers and valved introducers that enable physicians to create a conduit through which they can insert infusion catheters, implantable ports and pacemaker leads into a blood vessel;
- o Advanced delivery catheters that have a "fixed curve" or articulating distal tip section that can be manipulated to enable the health care professional to access parts of the patient's anatomy that cannot be reached by traditional introducers; and
- o Implantable stimulation leads, adaptors and delivery systems for the cardiac and neuromodulation markets.

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Approximately \$13.8 million of the Enpath purchase price was allocated to the preliminary estimated fair value of acquired IPR&D projects that had not yet reached technological feasibility and had no alternative future use. These projects primarily represent the next generation of products already being sold by Enpath which incorporate new enhancements and customer modifications. The Company expects to commercially launch various introducer products in 2008 and 2009 and various catheter products in 2009 which will replace existing products. For purposes of valuing the acquired purchased research and development, the Company estimated total costs to complete the introducer projects to be approximately \$0.3 million and \$0.5 million to complete the catheter projects. If we are not successful in completing these projects on a timely basis, our future sales from introducers and catheters may be adversely affected resulting in erosion of our market share. There were no significant changes from our original estimates with regards to these projects during the third quarter of 2007.

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ECP. ECP continues to develop new and innovative power solutions for the world's most demanding commercial applications. ECP has developed a new high energy lithium cell for a customer in the telematics market. Due to their exceptional high energy, two of these new cells are capable of providing power for the entire 10-year life of the telematics device. ECP also has developed a battery pack capable of withstanding harsh operating conditions such as high vibration, high shock, salt spray, high temperature, low temperature, and high humidity.

Finally, ECP has developed a modular battery pack for a customer's fleet of underwater sonabuys which measure water characteristics. The long life of ECP cells, coupled with their ability to withstand harsh conditions, make them ideally suited for buoys. The customer's expense of commissioning a ship to replace the batteries in each buoy is reduced when using ECP batteries due to their long life.

Cost Savings and Consolidation Efforts

During 2005, we initiated several significant cost savings and consolidation efforts, the implementation of which continued during 2006 and the first nine months of 2007.

Alden Facility Consolidation. Beginning in the first quarter of 2005 and ending in the second quarter of 2006 we consolidated our medical capacitor manufacturing operations in Cheektowaga, NY, and our implantable medical battery manufacturing operations in Clarence, NY, into our advanced power source manufacturing facility in Alden, NY ("Alden Facility"). We also consolidated our capacitor research, development and engineering operations from our Cheektowaga, NY facility into our Technology Center in Clarence, NY.

The total cost for these consolidation efforts was \$3.4 million, which was below the Company's original estimate of \$3.5 to \$4.0 million. Expenses of \$0.6 million were incurred during the first two quarters of 2006. In total, \$0.8 million was paid in cash during 2006. The expenses for the Alden Facility consolidation were included in the IMC business segment.

Carson City Facility shutdown and Tijuana Facility consolidation No. 1. On March 7, 2005, we announced our intent to close the Carson City, NV facility ("Carson City Facility") and consolidate the work performed at our Carson City Facility into our Tijuana, Mexico facility ("Tijuana Facility consolidation No. 1").

The Company ceased operating at the Carson City Facility on July 15, 2007. The

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total cost for this consolidation effort was \$7.8 million. The Company anticipates that the \$0.5 million of severance accrued as of September 28, 2007 related to this consolidation project will be paid out over the next two quarters.

The major categories of costs include the following:

- o Costs related to the shutdown of the Carson City Facility:
 - Severance and retention - \$3.9 million;
 - Accelerated depreciation - \$0.6 million; and
 - Other - \$0.3 million.

- o Costs related to the Tijuana Facility consolidation No. 1:
 - Production inefficiencies and revalidation - \$0.5 million;
 - Relocation and moving - \$0.1 million;
 - Personnel (including travel, training and duplicate wages) - \$1.7 million; and
 - Other - \$0.7 million.

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All categories of costs are considered to be cash expenditures, except accelerated depreciation. The Company anticipates annual cost savings in the range of \$2.5 million to \$3.1 million. The expenses for the Carson City Facility shutdown and the Tijuana Facility consolidation No. 1 are included in the IMC business segment.

Columbia Facility & ARL shutdown, Tijuana Facility consolidation No. 2, and RD&E Consolidation. On November 16, 2005, we announced our intent to close both our Columbia, MD facility ("Columbia Facility") and our Fremont, CA Advanced Research Laboratory ("ARL"). The manufacturing operations at our Columbia Facility will be moved into our Tijuana Facility ("Tijuana Facility consolidation No. 2"). The research, development and engineering ("RD&E") and product development functions at our Columbia Facility have begun to relocate to the Technology Center in Clarence, NY. The ARL relocation to the Technology Center in Clarence, NY is complete.

The total revised estimated cost for this facility consolidation plan is anticipated to be between \$11.1 million and \$11.6 million. To date, we have expensed \$10.0 million related to these projects and expect to incur the remaining costs in 2007 and the first quarter of 2008, with cash payments being made through the second quarter of 2008. All categories of costs are considered to be future cash expenditures, except for accelerated depreciation and asset write-offs.

Approximately \$3.9 million of the Columbia Facility and ARL shutdown costs were incurred in 2005 and 2006 (\$0.5 million for assets written-off), and \$1.5 million were incurred in the first three quarters of 2007. Approximately \$1.4 million was paid in cash during the first nine months of 2007. Tijuana Facility consolidation plan No. 2 expenses of \$2.3 million were incurred and paid in cash in 2006 and \$2.3 million in the first three quarters of 2007.

Once the moves are completed, the Company anticipates annual cost savings in the range of \$5.0 million to \$6.0 million. The expenses for the Columbia Facility and ARL shutdowns, the Tijuana Facility consolidation No. 2 and the RD&E consolidation are included in the IMC business segment.

ECP Expansion. In February 2007, the Company announced that it will close its current manufacturing facility in Canton, MA and construct a new 80,000 square foot replacement facility in the Massachusetts area. The expected completion of this \$28 million expansion project is mid-2008. The total expense to be

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recognized for this relocation is estimated to be \$2.2 million to \$2.4 million. During the first nine months of 2007, \$0.4 million of costs were incurred related to this project, which were primarily non-cash items. Costs related to this move are included in the ECP business segment.

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Our Financial Results

We utilize a fifty-two, fifty-three week fiscal year ending on the Friday nearest December 31st. For 52-week years, each quarter contains 13 weeks. The third quarter of 2007 and 2006 each contained 13 weeks and ended on September 28, and September 29, respectively. The commentary that follows should be read in conjunction with our condensed consolidated financial statements and related notes and with the Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Form 10-K for the fiscal year ended December 29, 2006.

| In thousands, except per share data | Three months ended | | | | Nine mon |
|---|-----------------------|-----------------------|--------------|-------------|-----------------------|
| | September 28, 2007 | September 29, 2006 | \$ Change | % Change | September 28, 2007 |
| IMC | | | | | |
| ICD batteries | \$ 12,265 | \$ 11,456 | 809 | 7% | \$ 37,657 |
| Pacemaker and other batteries | 4,701 | 4,439 | 262 | 6% | 16,449 |
| ICD capacitors | 5,782 | 4,499 | 1,283 | 29% | 22,188 |
| Feedthroughs | 14,448 | 17,355 | (2,907) | -17% | 49,851 |
| Enclosures | 4,584 | 5,698 | (1,114) | -20% | 16,284 |
| Introducers, catheters and leads | 10,047 | - | 10,047 | N/A | 11,632 |
| Other medical | 15,176 | 13,560 | 1,616 | 12% | 45,730 |
| Total IMC | 67,003 | 57,007 | 9,996 | 18% | 199,791 |
| ECP | 12,006 | 12,287 | (281) | -2% | 34,540 |
| Total sales | 79,009 | 69,294 | 9,715 | 14% | 234,331 |
| Cost of sales - excluding amortization of intangible assets | 48,647 | 42,709 | 5,938 | 14% | 141,697 |
| Cost of sales - amortization of intangible assets | 1,222 | 948 | 274 | 29% | 3,164 |
| Total Cost of sales | 49,869 | 43,657 | 6,212 | 14% | 144,861 |
| Cost of sales as a % of sales | 63.1% | 63.0% | | 0.1% | 61.8% |
| Selling, general, and administrative expenses (SG&A) | 11,362 | 9,311 | 2,051 | 22% | 32,130 |
| SG&A as a % of sales | 14.4% | 13.4% | | 1.0% | 13.7% |
| Research, development and engineering costs, net (RD&E) | 8,423 | 6,022 | 2,401 | 40% | 21,856 |
| RD&E as a % of sales | 10.7% | 8.7% | | 2.0% | 9.3% |
| Other operating expense, net | (985) | 6,239 | (7,224) | -116% | 20,889 |
| Operating income | 10,340 | 4,065 | 6,275 | 154% | 14,595 |

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| | | | | |
|-----------------------------|----------|----------|----------|---------------|
| Operating margin | 13.1% | 5.9% | 7.2% | 6.2% |
| Interest expense | 2,112 | 1,135 | 977 | 5,345 |
| Interest income | (1,586) | (1,521) | (65) | (6,028) |
| Other (income) expense, net | 70 | 171 | (101) | (8,318) |
| Provision for income taxes | 4,744 | 1,041 | 3,703 | 11,326 |
| Effective tax rate | 48.7% | 24.3% | 24.4% | 48.0% |
| ----- | | | | |
| Net income | \$ 5,000 | \$ 3,239 | \$ 1,761 | 54% \$ 12,270 |
| ===== | | | | |
| Net margin | 6.3% | 4.7% | 1.6% | 5.2% |
| Diluted earnings per share | \$ 0.22 | \$ 0.15 | \$ 0.07 | 47% \$ 0.54 |

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Sales

IMC. The nature and extent of our selling relationship with each CRM customer is different in terms of component products purchased, selling prices, product volumes, ordering patterns and inventory management. We have pricing arrangements with our customers that at times do not specify minimum order quantities. Our visibility to customer ordering patterns is over a relatively short period of time. Our customers may have inventory management programs and alternate supply arrangements of which we are unaware. Additionally, the relative market share among the CRM device manufacturers changes periodically. Consequently, these and other factors can significantly impact our sales in any given period.

Our customers may initiate field actions with respect to market-released products. These actions may include product recalls or communications with a significant number of physicians about a product or labeling issue. The scope of such actions can range from very minor issues affecting a small number of units to more significant actions. There are a number of factors, both short-term and long-term related to these field actions that may impact our results. In the short-term, if product has to be replaced, or customer inventory levels have to be restored, this will result in increased component demand. Also, changing customer order patterns due to market share shifts or accelerated device replacements may also have a positive impact on our sales results in the near-term. These same factors may have longer-term implications as well. Customer inventory levels may ultimately have to be rebalanced to match demand.

IMC sales increased 18% and 15% for the three and nine month periods of 2007, respectively, and includes sales from the former Enpath of \$10.0 million and \$11.6 million, respectively. Additionally, sales were driven by growth of ICD capacitors, ICD batteries and our assembly business offset by decreases in sales of feedthroughs (QTD) and enclosures.

The increase in ICD capacitor sales was primarily the result of a customer supply issue during the first half of 2007, which has subsequently been resolved. For the year, we experienced growth in our feedthrough business, which was primarily being driven by the continued acceptance of filtered feedthrough technology and domestic market share penetration. During the third quarter, the Company received lower demand forecasts from its larger customers. We believe that these revisions include the impact of inventory adjustments as well as our customers' revised outlook for the balance of the year. ICD battery sales increased by 7% over both prior year periods. ICD battery sales softened through the balance of 2006 reflecting the general slowdown in the ICD market but began to rebound in the first three quarters of 2007. Based upon the updated demand

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forecasts from our larger customers', we expect our lower sales volume to continue in the fourth quarter. The variances in our enclosure and assembly revenues are due to both product mix and prices.

ECP. Similar to IMC customers, we have pricing arrangements with our customers that many times do not specify minimum quantities. Our visibility to customer ordering patterns is over a relatively short period of time.

ECP sales were consistent with the prior year third quarter and increased 3% for the nine month period. ECP revenue for the 2006 quarter included approximately \$2 million of customer inventory stocking. The core growth in ECP sales primarily came from oil and gas, pipeline inspection and military markets. Oil and gas drilling and pipeline inspection activity remains strong. Additionally, we continue to gain market share across our markets.

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Cost of sales

Changes from the prior year to cost of sales as a percentage of sales were primarily due to the following:

| | September 28, 2007 | |
|--|-----------------------|----------------------|
| | Three months ended | Nine months ended |
| Excess capacity at Tijuana Facility (a) | -1.2% | -1.1% |
| Mix change (b) | 0.5% | 0.8% |
| Enpath inventory step-up amortization(c) | 1.4% | 0.6% |
| Enpath amortization of intangible assets (d) | 0.3% | 0.1% |
| Inventory warranty reserves (e) | -1.1% | -0.1% |
| Other | 0.2% | 0.0% |
| | ----- | ----- |
| Total percentage point change to cost of sales as a percentage of sales | 0.1% | 0.3% |
| | ===== | ===== |

- (a) The Tijuana Facility was fully operational in 2006 but was not being fully utilized as it was only producing sub-assemblies. In 2007, primarily in the second quarter, the facility is producing increased volumes of sub-assemblies and the majority of our filtered feedthroughs, thus reducing excess capacity. In accordance with the Company's inventory accounting policy, excess capacity costs are expensed.
- (b) The revenue increase from 2006 was primarily in lower margin products, which included our assembly business as well as the addition of the lower margin introducer, catheter and leads operations acquired with Enpath.
- (c) The Company completed its acquisition of Enpath on June 15, 2007. The 2007 quarter and year-to-date periods include \$1.1 million and \$1.3 million, respectively, of inventory step-up amortization related to the Enpath acquisition. As of September 28, 2007, there was no additional inventory step-up adjustment remaining to be amortized.
- (d) The Company completed its acquisition of Enpath on June 15, 2007. The 2007 quarter and year-to-date periods include \$0.3 million of amortization related to intangible assets recorded as a result of that acquisition.
- (e) Variances relate to a decrease in inventory warranty reserves. The Company allows customers to return defective or damaged products for credit, replacement, or exchange. The Company generally warrants that its products will meet customer specifications and will be free from defects in materials and workmanship. The Company accrues its estimated exposure to

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warranty claims as cost of sales based upon recent historical experience and other specific information as it becomes available.

We expect our cost of sales as a percentage of sales to decrease over the next several years as a result of our consolidation efforts, the elimination of excess capacity and the elimination of inventory step-up amortization related to the Enpath acquisition. Excess capacity for the Tijuana Facility is not expected to be fully eliminated until the beginning of 2008 when the last announced consolidation effort is anticipated to be completed (see "Cost Savings and Consolidation Efforts" section of this Management Discussion and Analysis).

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SG&A expenses

Changes from the prior year to SG&A expenses were due to the following (in thousands):

| | September 28, 2007 | |
|--|-----------------------|----------------------|
| | Three months ended | Nine months ended |
| SG&A related to Enpath (a) | \$ 1,935 | \$ 2,232 |
| Stock-based and incentive compensation (b) | (829) | (504) |
| Increased workforce (c) | 180 | 930 |
| Director fees (d) | 18 | 183 |
| Professional and consulting fees (e) | 170 | 442 |
| Other (f) | 577 | 656 |
| | ----- | ----- |
| Net increase in SG&A | \$ 2,051 | \$ 3,939 |
| | ===== | ===== |

- (a) The Company completed its acquisition of Enpath on June 15, 2007. Accordingly, year over year comparisons will continue to be impacted by this acquisition through the second quarter of 2008.
- (b) The decrease in stock-based compensation is related to leadership transition costs incurred in 2006. Stock-based compensation is expected to increase in the future which is consistent with the growth in the Company's workforce. Incentive compensation is accrued based upon the achievement of performance goals relative to planned results.
- (c) The increase in workforce is a result of our planned increase in marketing and sales personnel.
- (d) The increase in director fees is consistent with our amended director compensation plan as discussed in our 2006 proxy statement.
- (e) The increase in professional and consulting fees is consistent with the increase in corporate development initiatives of the Company as well as increased contract negotiations.
- (f) The increase in other SG&A costs is primarily due to overall growth of the Company as well as an increase in various corporate development initiatives.

RD&E expenses

Net research, development and engineering costs are as follows (in thousands):

Three months ended

Nine months e

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| | September 28, 2007 | September 29, 2006 | September 28, 2007 | September 29, 2006 |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| Research and development costs | \$ 4,493 | \$ 3,852 | \$ 12,035 | \$ 12,035 |
| Engineering costs | 5,389 | 2,521 | 12,511 | 12,511 |
| Less cost reimbursements | (1,459) | (351) | (2,690) | (2,690) |
| Engineering costs, net | 3,930 | 2,170 | 9,821 | 9,821 |
| Total research and development and engineering costs, net | \$ 8,423 | \$ 6,022 | \$ 21,856 | \$ 21,856 |

The increase in RD&E expenses for the three and nine month periods ended September 28, 2007 is primarily due to the planned increase in engineering personnel costs (headcount), as we continue to invest substantial resources to develop new products. In terms of the development costs billed, reimbursements were higher due to the timing of reimbursable development projects as well as higher design engineering services activity which includes operations of the former BIOMECH. Reimbursements for achieving certain development milestones are netted against gross spending.

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Acquired in-process research and development

Approximately \$2.3 million and \$13.8 million of the BIOMECH and Enpath purchase price, respectively, represents the estimated fair value of IPR&D projects acquired from those companies. These projects had not yet reached technological feasibility and had no alternative future use as of the acquisition date, thus were immediately expensed on the date of acquisition. The Enpath IPR&D valuation was lowered by \$2.3 million during the third quarter of 2007 due to the finalization of assumptions used in the excess earnings analysis. These assumptions primarily related to the allocation of R&D costs between new and existing customers.

Other operating expense

Other operating expense for 2007 and 2006 are comprised of the following costs (in thousands):

| | Three months ended | | Nine months | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2007 | September 29, 2006 | September 28, 2007 | September 29, 2006 |
| (a) Alden facility consolidation | \$ - | \$ - | \$ - | \$ - |
| (a) Carson City facility shutdown and Tijuana facility consolidation No. 1 | 10 | 411 | 584 | 584 |
| (a) Columbia facility shutdown, Tijuana facility consolidation No. 2 and RD&E consolidation | 1,030 | 1,225 | 3,705 | 3,705 |
| (a) ECP expansion | 126 | - | 408 | 408 |
| (b) Asset dispositions and other | 109 | 4,603 | 99 | 99 |

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\$ 1,275 \$ 6,239 \$ 4,796 \$
 =====

- (a) Refer to the "Cost Savings and Consolidation Efforts" discussion for disclosure related to the timing and level of remaining expenditures for these items as of September 28, 2007.
- (b) During the third quarter of 2007, the Company had various asset dispositions. During the third quarter of 2006, the Company recorded a loss of \$4.4 million related to the write-off of a battery test system that was under development. Upon completion of the Company's engineering and technical evaluation, it was determined that the system could not meet the required specifications in a cost effective manner. This charge was included in the IMC business segment.

In addition to the quarter variances discussed above, the nine month period in 2007 includes \$0.3 million of insurance proceeds received related to equipment damaged during transportation to the Tijuana Facility. The nine month period in 2006 includes the loss of \$0.5 million related to this damaged equipment (included in the IMC business segment) and an expense of \$0.8 million for professional fees related to a potential acquisition that we no longer considered probable.

Interest expense and interest income

Interest expense for the three and nine month periods ended September 28, 2007 is higher than the prior year periods primarily due to the additional \$80 million of 2.25% convertible notes issued at the end of the first quarter of 2007 and additional amortization of deferred fees and discounts associated with these notes and the notes exchanged during the first quarter (See "Gain on extinguishment of debt").

Interest income for the nine months ended September 28, 2007 increased in comparison to the same period of 2006 primarily due to increased cash, cash equivalents and short-term investment balances. Interest income for the third quarter of 2007 was consistent with the same period of 2006. In the future, interest income is expected to be lower as a result of the cash deployed in connection with the BIOMEK and Enpath acquisitions near the end of the second quarter of 2007, as well as the cash that will be deployed in connection with the acquisitions announced subsequent to September 28, 2007. See note 15 of the condensed consolidated financial statements.

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Gain on sale of investment security

In the second quarter of 2007, the Company sold an equity security investment which resulted in a pre-tax gain of \$4.0 million (\$2.6 million net of tax) or \$0.11 per diluted share.

Gain on extinguishment of debt

In March 2007, the Company entered into separate, privately negotiated agreements to exchange \$117.8 million of the original \$170.0 million of 2.25% convertible subordinated notes due 2013 ("CSN I") for an equivalent principal amount of a new series of 2.25% convertible subordinated notes due 2013. The primary purpose of this transaction was to eliminate the June 15, 2010 call and put option that is included in the terms of CSN I. This exchange was accounted for as an extinguishment of debt and resulted in a net pre-tax gain of \$4.5 million (\$2.9 million net of tax) or \$0.12 per diluted share.

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Provision for income taxes

The effective tax rate for 2007 includes the impact of the \$16.1 million of acquired IPR&D written off, \$13.8 million of which is not deductible for tax purposes. Excluding the impact of this expense, the effective tax rate for the three and nine months ended September 28, 2007 would have been approximately 32% compared to 24.3% and 32.5% for the same periods of 2006. During the third quarter of 2006, we adjusted our tax accounts to reflect the filing of our 2005 tax returns as well as the completion of various tax savings initiatives which resulted in the lower effective tax rate for that period. We expect our effective tax rate to be approximately 48% for the remainder of 2007.

Subsequent to the end of the third quarter, Mexico enacted new tax legislation that will take effect on January 1, 2008. We are currently evaluating the impact of this tax law change on our financial statements.

Liquidity and Capital Resources

| (Dollars in millions) | September 28, 2007 | December 29, 2006 |
|--|-----------------------|----------------------|
| | ----- | ----- |
| Cash and cash equivalents and short-term investments (a) (b) | \$ 115.8 | \$ 142.6 |
| Working capital (b) | \$ 184.7 | \$ 199.1 |
| Current ratio (b) | 4.5:1.0 | 5.7:1.0 |

- (a) Short-term investments consist of investments acquired with maturities that exceed three months and are less than one year at the time of acquisition, equity securities classified as available-for-sale and auction rate securities.
- (b) Cash and cash equivalents and short-term investments, working capital and our current ratio decreased primarily due to the \$109.7 million of cash used to acquire BIOMEC and Enpath partially offset by \$69.4 million of net cash received from the issuance of additional 2.25% convertible subordinated notes due 2013 in March 2007 and cash provided by operating activities of \$30.8 million.

Revolving line of credit

In May 2007, the Company entered into a new senior credit facility (the "New Credit Facility") consisting of a \$235 million revolving credit facility, which can be increased to \$335 million upon the Company's request. The New Credit Facility also contains a \$15 million letter of credit subfacility and a \$15 million swingline subfacility. This New Credit Facility replaced the Company's prior \$50 million revolving credit facility. The New Credit Facility is secured

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by the Company's non-realty assets including cash, accounts and notes receivable, and inventories and has an expiration date of May 22, 2012 with a one-time option to extend to April 1, 2013 if no default has occurred. Interest rates under the New Credit Facility are, at the Company's option, based upon the current prime rate or the LIBOR rate plus a margin that varies with the Company's leverage ratio. If interest is paid based upon the prime rate, the applicable margin is between minus 1.25% and 0.00%. If interest is paid based

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upon the LIBOR rate, the applicable margin is between 1.00% and 2.00%. The Company is required to pay a commitment fee between 0.125% and 0.250% per annum on the unused portion of the New Credit Facility based on the Company's leverage ratio.

The New Credit Facility contains limitations on the incurrence of indebtedness, limitations on the incurrence of liens and licensing of intellectual property, limitations on investments and restrictions on certain payments. Except to the extent paid for by common equity of Greatbatch or paid for out of cash on hand, the New Credit Facility limits the amount paid for acquisitions to \$100 million. The restrictions on payments, among other things, limit repurchases of Greatbatch's stock to \$60 million and limits the ability of the Company to make cash payments upon conversion of our convertible subordinated notes. In addition, the New Credit Facility requires the Company to maintain a ratio of adjusted EBITDA, as defined in the agreement, to interest expense of at least 3.00 to 1.00, and a total leverage ratio, as defined in the credit agreement, of not greater than 5.00 to 1.00 from May 22, 2007 through September 29, 2009 and not greater than 4.50 to 1.00 from September 30, 2009 and thereafter. The New Credit Facility contains customary events of default. Upon the occurrence of an event of default, a majority of the lenders may declare all obligations under the New Credit Facility immediately due and payable.

There were no borrowings outstanding under the New Credit Facility as of September 28, 2007. The Company expects to fund the acquisitions announced subsequent to September 28, 2007 with cash, short-term investments and borrowings under the New Credit Facility. See note 15 of the condensed consolidated financial statements.

Operating activities

Net cash flows from operating activities for the nine months ended September 28, 2007 increased \$6.1 million over the comparable period in 2006. This increase was primarily the result of a \$4.3 million increase in net income excluding non-cash items (i.e. depreciation, amortization, stock-based compensation, gains/loss on investments, disposal of PP&E, and debt extinguishment, and IPR&D charges). The extinguishment of debt in 2007 resulted in a reclassification of approximately \$11.3 million of current income tax liability, of which approximately \$8.5 million has been paid as of September 28, 2007 and the remainder will be paid by the end of 2007. This amount was previously recorded as a non-current deferred tax liability on the balance sheet.

Investing activities

Net cash used in investing activities of \$71.2 million for the nine months ended September 28, 2007 increased over the comparable period in 2006. This was primarily the result of the acquisitions of BIOMEK and Enpath in 2007 (\$109.7 million) which were funded with both short-term investments and cash on hand. Approximately, \$3.5 million of the property, plant and equipment acquired during the first nine months of 2007 relate to construction of our new ECP manufacturing facility in the Massachusetts area and the expansion of our corporate headquarters. Total cash expenditures under these projects is expected to be approximately \$36 million which will be paid throughout the remainder of 2007 and 2008. The remainder of the property, plant and equipment purchases relate to routine investment in order to support our internal growth and to maintain our technology leadership. In addition to the above, in 2007 we made an additional \$2.0 million investment in IntElect Medical, Inc., an early stage neurostimulation device company that works in conjunction with the Cleveland Clinic.

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Financing activities

Cash flow provided by financing activities for the first nine months of 2007 was primarily related to net proceeds of \$76.0 million received in connection with the issuance of 2.25% convertible subordinated notes due 2013 during the first quarter. The Company has paid approximately \$6.6 million of financing fees related to this transaction as well as the new revolving credit agreement discussed above. In connection with the Enpath acquisition, the Company acquired \$7.1 million of debt which it subsequently paid down with short-term investments and cash on hand. Cash flows from financing activities also include cash received from stock option exercises for both 2007 and 2006.

Capital structure

At September 28, 2007, our capital structure consisted of \$240.9 million of convertible subordinated notes and our 22.5 million shares of common stock outstanding. We have \$115.8 million in cash, cash equivalents and short-term investments and are in a position to finance our future acquisitions. We are also authorized to issue 100 million shares of common stock and 100 million shares of preferred stock. The market value of our outstanding common stock since our IPO has exceeded our book value; accordingly, we believe that if needed we can access public markets to sell additional common or preferred stock assuming conditions are appropriate.

Our capital structure allows us to support our internal growth and provides liquidity for corporate development initiatives. Our current expectation for 2007 is that capital spending will be in the range of \$20.0 million to \$35.0 million.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements within the meaning of Item 303(a)(4) of Regulation S-K.

Contractual Obligations

In the normal course of business, the Company makes routine purchase commitments (primarily equipment and raw material purchases) in order to maintain the technological leadership of its manufacturing facilities and meet the needs of its customers. As of September 28, 2007, total contractual obligations related to such expenditures are approximately \$32.9 million and primarily relate to the construction of our new ECP manufacturing facility and the expansion of our corporate headquarters. These commitments will be financed by existing cash, short-term investments, or cash generated from operations.

Inflation

We do not believe that inflation has had a significant effect on our operations.

Impact of Recently Issued Accounting Standards

In February 2007, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 159, The Fair Value Option for Financial Assets and Financial Liabilities--Including an amendment of FASB Statement No. 115. This Statement provides entities with an option to choose to measure eligible items at fair value at specified election dates. If elected, an entity must report unrealized gains and losses on the item in

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earnings at each subsequent reporting date. The fair value option: may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method; is irrevocable (unless a new election date occurs); and is applied only to entire instruments and not to portions of instruments. The Company is still evaluating the impact of SFAS No. 159 on its financial statements, which is effective beginning in fiscal year 2008.

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In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value while applying generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions based on market data obtained from independent sources and (2) the reporting entity's own assumptions developed based on unobservable inputs. The Company is still evaluating the impact of SFAS No. 157 on its financial statements, which is effective beginning in fiscal year 2008.

Application of Critical Accounting Estimates

Our unaudited condensed consolidated financial statements are based on the selection of accounting policies and the application of significant accounting estimates, some of which require management to make significant assumptions. We believe that some of the more critical estimates and related assumptions that affect our financial condition and results of operations are in the areas of inventories, goodwill and other indefinite lived intangible assets, long-lived assets, share-based compensation and income taxes. For further information, refer to Item 7 "Managements Discussion and Analysis of Financial Condition and Results of Operations" and Item 8 "Financial Statements and Supplementary Data" in the Company's Annual Report on Form 10-K for the year ended December 29, 2006. During the three months ended September 28, 2007, we did not change or adopt new accounting policies that had a material effect on our consolidated financial condition and results of operations.

Effective in the first quarter of 2007, the Company adopted the provisions of FASB Interpretation ("FIN") No. 48 Accounting for Uncertainty in Income Taxes, an interpretation of FASB SFAS No. 109. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized under SFAS No. 109. FIN No. 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on various related matters such as derecognition, interest and penalties, and disclosure.

Additionally, in May 2007, the FASB published FASB Staff Position ("FSP") No. FIN 48-1, Definition of Settlement in FASB Interpretation No. 48. FSP FIN No. 48-1 is an amendment to FIN No. 48. It clarifies how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. As of our adoption date of FIN No. 48, our accounting is consistent with the guidance in FSP FIN No. 48-1.

Forward-Looking Statements

Some of the statements contained in this Quarterly Report on Form 10-Q and other written and oral statements made from time to time by us and our representatives are not statements of historical or current fact. As such, they are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934,

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as amended. We have based these forward-looking statements on our current expectations, which are subject to known and unknown risks, uncertainties and assumptions. They include statements relating to:

- o future sales, expenses and profitability;
- o the future development and expected growth of our business and the industries we operate in;
- o our ability to successfully execute our business model and our business strategy;
- o our ability to identify trends within the implantable medical devices, medical components, and commercial power sources industries and to offer products and services that meet the changing needs of those markets;

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- o projected capital expenditures; and
- o trends in government regulation.

You can identify forward-looking statements by terminology such as "may," "will," "should," "could," "expects," "intends," "plans," "anticipates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of these terms or other comparable terminology. These statements are only predictions. Actual events or results may differ materially from those suggested by these forward-looking statements. In evaluating these statements and our prospects generally, you should carefully consider the factors set forth below. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary factors and to others contained throughout this report. We are under no duty to update any of the forward-looking statements after the date of this report or to conform these statements to actual results.

Although it is not possible to create a comprehensive list of all factors that may cause actual results to differ from the results expressed or implied by our forward-looking statements or that may affect our future results, some of these factors include the following: dependence upon a limited number of customers, product obsolescence, inability to market current or future products, pricing pressure from customers, reliance on third party suppliers for raw materials, products and subcomponents, fluctuating operating results, inability to maintain high quality standards for our products, challenges to our intellectual property rights, product liability claims, inability to successfully consummate and integrate acquisitions, unsuccessful expansion into new markets, competition, inability to obtain licenses to key technology, regulatory changes or consolidation in the healthcare industry, and other risks and uncertainties that arise from time to time as described in the Company's Annual Report on Form 10-K and other periodic filings with the Securities and Exchange Commission.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Under our line of credit any borrowings bear interest at fluctuating market rates. At September 28, 2007, we did not have any borrowings outstanding under our line of credit and thus no interest rate sensitive financial instruments other than short-term investments. We do not believe that the impact of fluctuations in interest rates on our short-term investments will have a material effect on our condensed consolidated financial statements.

The company incurs certain expenses related to its Tijuana, Mexico operations that are denominated in a foreign currency. We do not believe that the impact of foreign currency fluctuations will have a material effect on our condensed consolidated financial statements.

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ITEM 4. CONTROLS AND PROCEDURES.

a. Evaluation of Disclosure Controls and Procedures.

Our management, including the principal executive officer and principal financial officer, evaluated our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) related to the recording, processing, summarization and reporting of information in our reports that we file with the SEC as of September 28, 2007. These disclosure controls and procedures have been designed to provide reasonable assurance that material information relating to us, including our subsidiaries, is made known to our management, including these officers, by other of our employees, and that this information is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the SEC's rules and forms.

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Based on their evaluation, as of September 28, 2007, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures are effective.

b. Changes in Internal Control Over Financial Reporting.

There have been no changes in our internal control over financial reporting that occurred during our last fiscal quarter to which this Quarterly Report on Form 10-Q relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

We completed the acquisition of Enpath on June 15, 2007, at which time Enpath became a subsidiary of Greatbatch. We believe that the internal controls and procedures of Enpath are reasonably likely to materially affect our internal control over financial reporting. We are currently in the process of incorporating the internal controls and procedures of the former Enpath into our internal controls over financial reporting. The Company has extended its Section 404 compliance program under the Sarbanes-Oxley Act of 2002 (the "Act") and the applicable rules and regulations under such Act to include the former Enpath. The Company will report on its assessment of the internal controls of its combined operations within the time period provided by the Act and the applicable SEC rules and regulations concerning business combinations.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

In connection with our acquisition of Enpath Medical, Inc. ("Enpath"), we assumed liability in connection with the following proceeding:

On June 12, 2006, Enpath was named as defendant in a patent infringement action filed by Pressure Products Medical Supplies, Inc. and venued in the United States District Court in the Eastern District of Texas. On October 2, 2006, Enpath was officially served. Enpath has filed an answer denying liability and has filed counterclaims against the plaintiff alleging antitrust violations and patent misuse. The plaintiff has alleged that Enpath's FlowGuard(TM) valved introducer, which has been on the market for more than three years, infringes claims in the plaintiff's patents and is seeking damages and injunctive relief. Enpath believes that the plaintiff's claims are without merit and intends to

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pursue its defenses vigorously. Revenues from products sold that include the FlowGuard valved introducer were approximately 5% of Enpath's total revenue for 2007 (\$29.3 million), 2006 (\$36.8 million) and 2005 (\$29.4 million). The lawsuit is currently in the discovery stage. The District Court held a hearing to construe the claims of the plaintiff's patents in August 2007, but has not yet issued its decision. It is not possible to predict the timing or outcome of this litigation at this time, including whether it will affect the Company's ability to sell its FlowGuard products, or to estimate the amount or range of potential loss.

There have been no other material changes to those legal proceedings as previously disclosed in the Company's Form 10-K for the year ended December 29, 2006.

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ITEM 1A. RISK FACTORS.

There have been no material changes in risk factors as previously disclosed in the Company's Form 10-K for the year ended December 29, 2006, except as follows:

We face risks associated with our acquisitions

Our acquisition of BIOMECH, Inc. Enpath Medical, Inc., IntelliSensing LLC, Quan Emerteq LLC and Engineered Assemblies Corporation presents several risks and uncertainties, including the following:

- o The allocation of the purchase price to the assets acquired, the amortization of intangible assets resulting from that allocation and the impact of fair value purchase accounting adjustments may adversely affect our earnings;
- o We may be unsuccessful in integrating these businesses;
- o Integrating these businesses may be distracting to our management and disruptive to our business and the costs of integration may be significant; and
- o We may assume liabilities in the acquisitions that we did not anticipate that could have a material adverse effect on our operating results.

Enpath's products are subject to regulatory oversight.

The medical products that Enpath sells and proposes to sell are subject to regulation by the Food and Drug Administration ("FDA") and by comparable agencies in certain states and foreign countries. The process of complying with requirements of the FDA and other agencies can be costly and time consuming. Enpath has received clearance from the FDA to market its vessel introducer products, safety needle, steerable catheter, and epicardial lead and implant tool. There is no assurance that any future additional clearance can be obtained. In addition, once obtained, these clearances are subject to review and later discovery of problems may result in restrictions on the marketing of a product or withdrawal of the product from the market. Enpath's products are also subject to certain FDA regulations governing manufacturing practices, packaging and labeling. Non-compliance with these regulations can result in product recalls or other sanctions which could have a material adverse effect on Enpath's business and our financial condition.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

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None.

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

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

See the Exhibit Index for a list of those exhibits filed herewith.

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SIGNATURES

Pursuant to the requirements of Sections 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: November 6, 2007 GREATBATCH, INC.

By /s/ Thomas J. Hook

Thomas J. Hook
President and Chief Executive Officer
(Principal Executive Officer)

By /s/ Thomas J. Mazza

Thomas J. Mazza
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

By /s/ Marco F. Benedetti

Marco F. Benedetti
Corporate Controller
(Principal Accounting Officer)

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EXHIBIT INDEX

| Exhibit No. ----- | Description ----- |
|----------------------|---|
| 3.1 | Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to our quarterly report on Form 10-Q ended July 1, 2005). |

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- 3.2 Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to our quarterly report on Form 10-Q ended March 29, 2002).
- 31.1* Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.
- 31.2* Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.
- 32* Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* - Filed herewith.