

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

FORM 10-Q

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

For the quarterly period ended July 28, 2007

OR

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

For the transition period from _____ to _____

Commission file number: 001-33261

AEROVIRONMENT, INC.

Delaware

(State or other jurisdiction of incorporation or organization)

95-2705790

(I.R.S. Employer Identification No.)

**181 W. Huntington Drive, Suite 202
Monrovia, California**

(Address of principal executive offices)

91016

(Zip Code)

(626) 357-9983

(Registrant's telephone number, including area code)

N/A

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

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

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

Large accelerated filer £

Accelerated filer £

Non-accelerated filer R

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

As of August 30, 2007, the number of shares outstanding of the registrant's common stock, \$0.0001 par value, was 19,401,058.

AeroVironment, Inc.

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements:

<u>Consolidated Balance Sheets as of July 28, 2007 (Unaudited) and April 30, 2007</u>	1
<u>Consolidated Statements of Income for the three months ended July 28, 2007 (Unaudited) and July 29, 2006 (Unaudited)</u>	2
<u>Consolidated Statements of Cash Flows for the three months ended July 28, 2007 (Unaudited) and July 29, 2006 (Unaudited)</u>	3
<u>Notes to Consolidated Financial Statements (Unaudited)</u>	4
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	9
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	13
<u>Item 4T. Controls and Procedures</u>	13

PART II. OTHER INFORMATION

<u>Item 1. Legal Proceedings</u>	15
<u>Item 1A. Risk Factors</u>	15
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	15
<u>Item 3. Defaults Upon Senior Securities</u>	15
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	15
<u>Item 5. Other Information</u>	15
<u>Item 6. Exhibits</u>	16
<u>Signatures</u>	17
Exhibit Index	
Exhibit 10.1	
Exhibit 31.1	
Exhibit 31.2	
Exhibit 32	

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

AeroVironment, Inc.
Consolidated Balance Sheets
(In thousands except share data)

	July 28, 2007	April 30, 2007
	<u>(Unaudited)</u>	
Assets		
Current assets:		
Cash and cash equivalents	\$ 29,622	\$ 20,920
Restricted cash	406	389
Short-term investments	71,400	88,325
Accounts receivable, net of allowance for doubtful accounts of \$184 at July 28, 2007 and \$149 at April 30, 2007	23,855	7,691
Unbilled receivables and retentions	14,789	26,494
Inventories, net	16,415	14,015
Deferred income taxes	1,738	1,730
Prepaid expenses and other current assets	<u>1,355</u>	<u>1,504</u>
Total current assets	159,580	161,068
Property and equipment, net	7,594	6,229
Deferred income taxes	761	761
Other assets	<u>119</u>	<u>119</u>
Total assets	<u>\$ 168,054</u>	<u>\$ 168,177</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 11,517	\$ 16,024
Wages and related accruals	9,157	8,942
Customer advances	257	139
Income taxes payable	1,640	4,564
Other current liabilities	<u>1,580</u>	<u>1,544</u>
Total current liabilities	24,151	31,213
Deferred rent	640	541
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.0001 par value:		
Authorized shares — 10,000,000		
None issued or outstanding		
Common stock, \$0.0001 par value:		
Authorized shares — 100,000,000		
Issued and outstanding shares — 19,279,809 at July 28, 2007 and 18,875,957 at April 30, 2007	2	2
Additional paid-in capital	87,188	83,611
Retained earnings	<u>56,073</u>	<u>52,810</u>
Total stockholders' equity	<u>143,263</u>	<u>136,423</u>
Total liabilities and stockholders' equity	<u>\$ 168,054</u>	<u>\$ 168,177</u>

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Consolidated Statements of Income (Unaudited)
(In thousands except share and per share data)

	Three months ended	
	July 28, 2007	July 29, 2006
Revenue:		
Product sales	\$ 29,684	\$ 23,844
Contract services	19,520	7,713
	<u>49,204</u>	<u>31,557</u>
Cost of sales:		
Product sales	18,291	14,301
Contract services	14,076	5,270
	<u>32,367</u>	<u>19,571</u>
Gross margin	16,837	11,986
Research and development	4,300	3,841
Selling, general and administrative	7,726	6,132
Income from operations	4,811	2,013
Other income		
Interest income	979	206
Income before income taxes	5,790	2,219
Provision for income taxes	1,946	854
Net income	<u>\$ 3,844</u>	<u>\$ 1,365</u>
Earnings per share data (a):		
Basic	\$ 0.20	\$ 0.10
Diluted	\$ 0.18	\$ 0.09
Weighted average shares outstanding (a):		
Basic	18,897,711	13,508,079
Diluted	21,077,055	15,165,685

(a) All share information has been adjusted to reflect a 7.0378-for-one stock split which was effective January 18, 2007.

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Consolidated Statements of Cash Flows (Unaudited)
(In thousands)

	Three months ended	
	July 28, 2007	July 29, 2006
Operating activities		
Net income	\$ 3,844	\$ 1,365
Adjustments to reconcile net income to net cash and cash equivalents used in operating activities:		
Depreciation and amortization	805	667
Provision for doubtful accounts	35	—
Deferred income taxes	(8)	—
Stock-based compensation	68	—
Tax benefit from exercise of stock options	3,252	213
Changes in operating assets and liabilities:		
Accounts receivable	(16,199)	7,269
Unbilled receivables and retentions	11,705	(468)
Inventories	(2,400)	416
Other assets	149	(88)
Accounts payable	(4,507)	(3,209)
Customer advances	118	(4,719)
Other liabilities	(3,155)	(2,869)
Net cash and cash equivalents used in operating activities	(6,293)	(1,423)
Investing activities		
Acquisitions of property and equipment	(2,170)	(681)
Purchases of short-term investments	(242,360)	—
Sales of short-term investments	259,285	—
Net cash and cash equivalents provided by (used in) investing activities	14,755	(681)
Financing activities		
Transfers to restricted cash	(17)	(23)
Repayments of long-term debt	—	(6,232)
Proceeds from long-term debt	—	6,232
Exercise of stock options	257	217
Net cash and cash equivalents provided by financing activities	240	194
Net increase (decrease) in cash and cash equivalents	8,702	(1,910)
Cash and cash equivalents at beginning of period	20,920	15,388
Cash and cash equivalents at end of period	<u>\$ 29,622</u>	<u>\$ 13,478</u>

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

1. Organization and Significant Accounting Policies

Organization

AeroVironment, Inc., a Delaware corporation, is engaged in the design, development and production of unmanned aircraft systems and energy technologies for various industries and governmental agencies.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation with respect to the interim financial statements have been included. The results of operations for the three months ended July 28, 2007 are not necessarily indicative of the results for the full year ending April 30, 2008. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended April 30, 2007, included in AeroVironment, Inc.'s Annual Report on Form 10-K.

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, including estimates of anticipated contract costs and revenue utilized in the revenue recognition process, that affect the reported amounts in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Certain prior year amounts have been reclassified to conform to the current year presentation.

The Company's consolidated financial statements include the assets, liabilities and operating results of wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Segments

The Company's products are sold and divided among three reportable segments, as defined by Statement of Financial Accounting Standards ("SFAS") No. 131, *Disclosures about Segments of an Enterprise and Related Information*, to reflect the Company's strategic goals. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the Chief Operating Decision Maker ("CODM") in deciding how to allocate resources and in assessing performance. The Company's CODM is the Chief Executive Officer, who reviews the revenue and gross margin results for each of these segments in order to make resource allocation decisions, including the focus of research and development, or R&D, activities, and assessing performance. The Company's reportable segments are business units that offer different products and services and are managed separately.

Earnings Per Share

Basic earnings per share is computed using the weighted-average number of common shares outstanding. The dilutive effect of potential common shares outstanding is included in diluted earnings per share and excludes any anti-dilutive effects of options.

The reconciliation of diluted to basic shares is as follows:

	Three Months Ended	
	July 28, 2007	July 29, 2006
Denominator for basic earnings per share:		
Weighted average common shares outstanding	18,897,711	13,508,079
Dilutive effect of employee stock options	<u>2,179,344</u>	<u>1,657,606</u>
Denominator for diluted earnings per share	<u>21,077,055</u>	<u>15,165,685</u>

All share information has been adjusted to reflect a 7.0378-for-one stock split which was effective January 18, 2007.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

During the three months ended July 28, 2007 certain options were not included in the computation of diluted earnings per share because their inclusion would have been anti-dilutive. The number of options which met this anti-dilutive criterion was approximately 108,000. During the three months ended July 29, 2006 there were no stock options that were anti-dilutive to earnings per share.

Recently Issued Accounting Standards

In July 2006, the Financial Accounting Standards Board (“FASB”) issued Interpretation No. 48 (“FIN No. 48”), *Accounting for Uncertainty in Income Taxes: an interpretation of FASB Statement No. 109*. This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity’s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. FIN No. 48 prescribes a recognition threshold and measurement principles for financial statement disclosure of tax positions taken or expected to be taken on a tax return. The Company adopted the provisions of this interpretation effective May 1, 2007. The adoption of FIN No. 48 did not have a material impact on the Company’s consolidated financial position, results of operations or cash flows. See Note 8, Income Taxes, for further discussion.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, which is the year beginning May 1, 2008 for the Company. The adoption of SFAS No. 157 is not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115*. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. SFAS No. 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007, which is the year beginning May 1, 2008 for the Company. The adoption of SFAS No. 159 is not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

2. Inventories, net

Inventories consist of the following:

	July 28, 2007	April 30, 2007
(In thousands)		
Raw materials	\$ 11,600	\$ 5,418
Work in process	3,064	3,514
Finished goods	2,862	6,221
Inventories, gross	17,526	15,153
Reserve for inventory obsolescence	(1,111)	(1,138)
Inventories, net	\$ 16,415	\$ 14,015

3. Warranty Reserves

The warranty reserve is included in other current liabilities. The related expense is included in cost of sales. Warranty reserve activity is summarized as follows for the three months ended July 28, 2007 and July 29, 2006:

	July 28, 2007	July 29, 2006
(In thousands)		
Beginning balance	\$ 263	\$ 344
Warranty expense	208	152
Warranty costs incurred	(228)	(141)
Ending balance	\$ 243	\$ 355

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

4. Bank Borrowings

The Company has a working capital line of credit with a bank with a borrowing limit of \$16,500,000. Borrowings bear interest at the bank's prime commercial lending rate, which was 8.25% as of July 28, 2007 and April 30, 2007. The line of credit is secured by substantially all of the Company's assets. Payment of amounts outstanding is made at the Company's discretion. All principal plus accrued interest is due August 31, 2007. The Company had no outstanding balance on the line of credit as of July 28, 2007 and April 30, 2007.

There was no interest expense for the three months ended July 28, 2007 and July 29, 2006.

The credit agreement contains certain financial covenants and conditions which require, among other things, that the Company maintain certain tangible net worth and cash flow ratios. The credit agreement also restricts the Company from paying any dividends to stockholders. The Company was in compliance with these covenants as of July 28, 2007 and April 30, 2007.

Effective August 31, 2007, the Company amended and restated its Business Loan Agreement with its bank, California Bank & Trust, to increase the borrowing limit from \$16,500,000 to \$25,000,000 and to extend the maturity date. Borrowings bear interest at the bank's prime commercial lending rate minus 0.25%. The line of credit is secured by substantially all of the Company's assets.

The credit facility contains several financial covenants, including that the Company not exceed maximum liquidity and leverage ratios, and limitations on additional indebtedness. In addition, the facility contains certain other restrictive loan covenants, including covenants limiting the Company's ability to dispose of assets, make acquisitions, be acquired, incur indebtedness, grant liens, make investments, pay dividends, and repurchase stock. The facility also includes customary default provisions, and all outstanding obligations may become immediately due and payable in the event of the Company's default.

Interest on amounts outstanding under the line of credit are due monthly. All principal plus accrued but unpaid interest on the line of credit is due August 31, 2009. The Company had no outstanding balance on the line of credit as of August 31, 2007.

The Company has entered into standby letter-of-credit agreements and bank guarantee agreements with financial institutions and customers primarily relating to the guarantee of the Company's future performance on certain contracts to provide products and services and to secure advance payments the Company has received from certain international customers. As of July 28, 2007 and April 30, 2007, the Company had standby letters of credit totaling \$0.4 million and had received no claims against such letters of credit. These letters of credit expire upon release by the customer.

5. Stockholders' Equity

In connection with its initial public offering completed on January 26, 2007, the Company reincorporated in Delaware, effective on December 6, 2006, and effected a 7.0378-to-one stock split on January 18, 2007. All share and per share data, including prior period data as appropriate, have been adjusted to reflect this split.

6. Stock-Based Compensation

For the three months ended July 28, 2007 and July 29, 2006, the Company recorded stock-based compensation expense for options that vested of approximately \$68,000 and \$0, respectively.

The fair value of stock options granted was estimated at the grant date using the Black-Scholes option pricing model with the following weighted average assumptions for the three months ended July 28, 2007:

	Three Months Ended July 28, 2007
Expected term (in years)	6.5
Expected volatility	19.49%
Risk-free interest rate	5.12%
Expected dividend	—
Weighted average fair value at grant date	\$ 7.93

The expected term of stock options represents the weighted average period the Company expects the stock options to remain outstanding, using a midpoint model based on the Company's historical exercise and post-vesting cancellation experience and the remaining contractual life of its outstanding options.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The expected volatility is based on peer group volatility in the absence of historical market data for the Company's stock, as permitted under FAS 123R. The peer group volatility was derived based on historical volatility of a comparable peer group index consisting of companies operating in a similar industry.

The risk free interest rate is based on the implied yield on a U.S. Treasury zero-coupon bond with a remaining term that approximates the expected term of the option.

The expected dividend yield of zero reflects that the Company has not paid any cash dividends since inception and does not anticipate paying cash dividends in the foreseeable future.

Information related to the Company's stock option plans at July 28, 2007 and for the three months then ended is as follows:

	2006 Plan		2002 Plan		1994 Directors' Plan		1992 Plan	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at April 30, 2007	—	—	1,532,423	1.95	35,189	.59	1,941,706	.55
Options granted	243,310	21.48	—	—	—	—	—	—
Options exercised	—	—	(102,325)	.76	—	—	(301,527)	.59
Options canceled	—	—	(5,630)	.64	—	—	—	—
Outstanding at July 28, 2007	<u>243,310</u>	<u>21.48</u>	<u>1,424,468</u>	<u>2.04</u>	<u>35,189</u>	<u>.59</u>	<u>1,640,179</u>	<u>.55</u>
Options exercisable at July 28, 2007	—	—	633,068	.91	35,189	.59	1,640,179	.55

7. Customer Funded Research & Development

Customer-funded R&D costs are incurred pursuant to contracts (revenue arrangements) to perform R&D activities according to customer specifications. These costs are direct contract costs and are expensed to cost of sales when the corresponding revenue is recognized, which is generally as the R&D services are performed. Revenues from customer-funded R&D were approximately \$4,286,000 and \$1,939,000 for the three months ended July 28, 2007 and July 29, 2006, respectively.

8. Income Taxes

On May 1, 2007, the Company adopted the provisions of FIN No. 48. The Company recorded a reduction to retained earnings of approximately \$581,000 as a result of the implementation of FIN No. 48. At the adoption date of May 1, 2007, the Company had approximately \$4,107,000 of unrecognized tax benefits. At July 28, 2007, the Company had approximately \$4,107,000 of unrecognized tax benefits all of which would impact the Company's effective tax rate if recognized. The Company estimates that no unrecognized tax benefits will decrease in the next twelve months.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The Company records interest and penalties on uncertain tax positions to income tax expense. As of April 30, 2007 and July 28, 2007, the Company had accrued approximately \$208,000 of interest and penalties related to uncertain tax positions. The Company is currently under audit by various state jurisdictions but does not anticipate any material adjustments from these examinations. The tax years 2004 to 2007 remain open to examination by the IRS for federal income taxes. The tax years 2003 to 2007 remain open for major state taxing jurisdictions.

9. Segment Data

The Company's product segments are as follows:

- Unmanned Aircraft Systems ("UAS") — engages primarily in the design, manufacture, sale and support of small unmanned aircraft systems.
- PosiCharge Systems ("PosiCharge") — engages primarily in the design, manufacture, sale and support of fast charge systems and related services for users of electrical industrial vehicles.
- Energy Technology Center — provides contract engineering for electric energy-related projects, and engages in the design, manufacture, sale and support of power processing test systems.

The accounting policies of the segments are the same as those described in Note 1, "Organization and Significant Accounting Policies." The operating segments do not make sales to each other. Depreciation and amortization related to the manufacturing of goods is included in gross margin for the segments. The Company does not discretely allocate assets to its operating segments, nor does the CODM evaluate operating segments using discrete asset information. Consequently, the Company operates its financial systems as a single segment for accounting and control purposes, maintains a single indirect rate structure across all segments, has no inter-segment sales or corporate elimination transactions, and maintains only limited financial statement information by segment.

The segment results are as follows (in thousands):

	Three Months Ended	
	July 28, 2007	July 29, 2006
Revenue:		
UAS	\$ 41,873	\$ 24,983
PosiCharge	5,358	4,943
Energy Technology Center	1,973	1,631
Total	<u>49,204</u>	<u>\$ 31,557</u>
Gross margin:		
UAS	14,091	\$ 9,271
PosiCharge	1,945	1,940
Energy Technology Center	801	775
Total	<u>16,837</u>	<u>\$ 11,986</u>
Research and development	4,300	3,841
Selling, general and administrative	7,726	6,132
Income from operations	4,811	2,013
Interest income	979	206
Income before income taxes	<u>\$ 5,790</u>	<u>\$ 2,219</u>

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

This section and other parts of this Quarterly Report on Form 10-Q contain forward-looking statements that involve risks and uncertainties. In some cases, forward-looking statements can be identified by words such as "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would" or similar expressions. Such forward-looking statements are based on current expectations, estimates and projections about our industry, our management's beliefs and assumptions made by our management. Forward-looking statements are not guarantees of future performance and our actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in Part II, Item 1A, "Risk Factors."

Unless required by law, we expressly disclaim any obligation to update publicly any forward-looking statements, whether as result of new information, future events or otherwise.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. When we prepare these consolidated financial statements, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Some of our accounting policies require that we make subjective judgments, including estimates that involve matters that are inherently uncertain. Our most critical estimates include those related to revenue recognition, inventories and reserves for excess and obsolescence, self-insured liabilities, accounting for stock-based awards, and income taxes. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for our judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Our actual results may differ from these estimates under different assumptions or conditions.

There have been no material changes made to the critical accounting estimates during the periods presented in the consolidated financial statements from those disclosed in the Form 10-K for the fiscal year ended April 30, 2007.

Fiscal Periods

Our fiscal year ends on April 30 and our fiscal quarters end on the last Saturday of July, October and January.

Results of Operations

Our operating segments are UAS, PosiCharge and our Energy Technology Center. The accounting policies for each of these segments are the same. In addition, a significant portion of our research and development, selling, general and administrative, and general overhead resources are shared across our segments.

The following table sets forth our revenue and gross margin generated by each operating segment for the periods indicated (in thousands):

	Three Months Ended	
	July 28, 2007	July 29, 2006
	(Unaudited)	
Revenue:		
UAS	\$ 41,873	\$ 24,983
PosiCharge	5,358	4,943
Energy Technology Center	1,973	1,631
Total	<u>49,204</u>	<u>\$ 31,557</u>
Gross margin:		
UAS	\$ 14,091	\$ 9,271
PosiCharge	1,945	1,940
Energy Technology Center	801	775
Total	<u>\$ 16,837</u>	<u>\$ 11,986</u>

Three Months Ended July 28, 2007 Compared to Three Months Ended July 29, 2006

Revenue. Revenue for the three months ended July 28, 2007 was \$49.2 million, as compared to \$31.6 million for the three months ended July 29, 2006, representing an increase of \$17.6 million, or 56%. UAS revenue increased \$16.9 million to \$41.9 million for the three months ended July 28, 2007, largely due to increased UAS product sales, services and customer-funded R&D. The increase in product sales resulted primarily from higher Raven B manufacturing volume. The completion of Raven B customer testing and evaluation led to the initiation of full-rate production during fiscal 2007, in turn resulting in an increase in procurement. The increase in UAS services revenue was primarily due to increased Raven spares and training services. These contract logistics services, or CLS, are cost reimburseable arrangements, which typically result in lower gross margin than fixed price contracts. PosiCharge revenue increased by \$0.5 million to \$5.4 million for the three months ended July 28, 2007, primarily due to increased installations of our fast charge systems. Energy Technology Center revenue increased by \$0.4 million to \$2.0 million in the three months ended July 28, 2007, primarily due to higher sales of power processing test equipment and customer-funded R&D.

Cost of Sales. Cost of sales for the three months ended July 28, 2007 was \$32.4 million, as compared to \$19.6 million for the three months ended July 29, 2006, representing an increase of \$12.8 million, or 65%. The increase in cost of sales was caused primarily by higher UAS cost of sales of \$12.1 million, PosiCharge cost of sales of \$0.4 million, and Energy Technology Center cost of sales of \$0.3 million.

Gross Margin. Gross margin for the three months ended July 28, 2007 was \$16.8 million, as compared to \$12.0 million for the three months ended July 29, 2006, representing an increase of \$4.8 million, or 40%. UAS gross margin increased \$4.8 million to \$14.1 million for the three months ended July 28, 2007. As a percentage of revenue, gross margin for UAS decreased from 37% to 34%. The decrease in UAS gross margin percent was primarily due to lower fixed price revenue relative to cost reimbursable revenue compared to the same period in the prior year. PosiCharge gross margin was unchanged at \$1.9 million for the three months ended July 28, 2007. As a percentage of revenue, PosiCharge gross margin decreased from 39% to 36% primarily due to increased manufacturing and engineering infrastructure support costs. Energy Technology Center gross margin was unchanged at \$0.8 million for the three months ended July 28, 2007. As a percentage of revenue, Energy Technology Center gross margin decreased from 48% to 41% for the three months ended July 28, 2007, primarily due to higher sustaining engineering costs for power processing test equipment deliveries.

Research and Development. R&D expense for the three months ended July 28, 2007 was \$4.3 million, or 9% of revenue, which was higher than R&D expense of \$3.8 million or 12% of revenue for the three months ended July 29, 2006. R&D expense increased \$0.5 million primarily due to higher investment in development initiatives including Global Observer.

Backlog. We define funded backlog as unfilled firm orders for products and services for which funding currently is appropriated to us under the contract by the customer. Because of possible future changes in delivery schedules and/or cancellations of orders, funded backlog at any particular date is not necessarily representative of actual sales to be expected for any succeeding period, and actual sales for the year may not meet or exceed the funded backlog represented. As of July 28, 2007 and April 30, 2007, our funded backlog was \$61.7 million and \$60.9 million, respectively.

In addition to funded backlog, we define unfunded backlog as the total remaining potential order amounts under cost reimbursable and fixed price contracts with multiple one-year options, or indefinite delivery indefinite quantity (“IDIQ”) contracts. Unfunded backlog does not obligate the U.S. government to purchase goods or services. There can be no assurance that unfunded backlog will result in any orders in any particular period, if at all. As of July 28, 2007 and April 30, 2007, our unfunded backlog was \$454.1 million and \$477.5 million, respectively.

Selling, General and Administrative. SG&A expense for the three months ended July 28, 2007 was \$7.7 million, or 16% of revenue, compared to SG&A expense of \$6.1 million, or 19% of revenue, in the three months ended July 29, 2006. The increase in SG&A expense of \$1.6 million was caused primarily by increased marketing and bid and proposal expense.

Income Tax Expense. Our effective income tax rate was 33.6% for the three months ended July 28, 2007, as compared to 38.5% for the three months ended July 29, 2006. This decrease was largely due to tax-exempt interest income received from our short-term investments. During the three months ended July 29, 2006, the Company did not receive any tax-exempt interest.

Liquidity and Capital Resources

We currently have no material cash commitments, except for normal recurring trade payables, accrued expenses and ongoing R&D costs, all of which we anticipate funding through our existing working capital, funds provided by operating activities and our working capital line of credit. The majority of our purchase obligations are pursuant to funded contractual arrangements with our customers. We believe that our existing cash, cash equivalents, cash provided by operating activities, funds available through our working capital line of credit and other financing sources will be sufficient to meet our anticipated working capital, capital expenditure and debt service requirements, if any, during the next twelve months. There can be no assurance, however, that our business will continue to generate cash flow at current levels. If we are unable to generate sufficient cash flow from operations, then we may be required to sell assets, reduce capital expenditures or obtain additional financing.

Our primary liquidity needs are for financing working capital, investing in capital expenditures, supporting product development efforts, introducing new products and enhancing existing products, and marketing acceptance and adoption of our products and services. Our future capital requirements, to a certain extent, are also subject to general conditions in or affecting the defense industry and are subject to general economic, political, financial, competitive, legislative and regulatory factors that are beyond our control. Moreover, to the extent that existing cash, cash equivalents, cash from operations, and cash from short-term borrowing are insufficient to fund our future activities, we may need to raise additional funds through public or private equity or debt financing. Although we are currently not a party to any agreement or letter of intent with respect to potential investment in, or acquisitions of, businesses, services or technologies, we may enter into these types of arrangements in the future, which could also require us to seek additional equity or debt financing.

Our working capital requirements vary by contract type. On cost reimburseable programs, we typically bill our incurred costs and fees monthly as work progresses, and therefore working capital investment is minimal. On fixed-price contracts, we typically are paid as we deliver products, and working capital is needed to fund labor and expenses incurred during the lead time from contract award until contract deliveries begin.

Cash Flows

The following table provides our cash flow data for the three months ended July 28, 2007 and July 29, 2006 (in thousands):

	Three Months Ended	
	July 28, 2007	July 29, 2006
	(Unaudited)	
Net cash used in operating activities	\$ (6,293)	\$ (1,423)
Net cash provided by (used in) investing activities	\$ 14,755	\$ (681)
Net cash provided by financing activities	\$ 240	\$ 194

Cash Used in Operating Activities. Net cash used in operating activities for the three months ended July 28, 2007 increased by \$4.9 million to \$6.3 million, compared to net cash used in operating activities of \$1.4 million for the three months ended July 29, 2006. This increase in net cash used in operating activities was primarily due to continued sales growth that resulted in higher working capital needs of \$10.6 million partially offset by higher net income of \$2.5 million, and a higher tax benefit from stock option exercises of \$3.1 million.

Cash Provided by Investing Activities. Net cash provided by investing activities increased by \$15.5 million to \$14.8 million for the three months ended July 28, 2007, compared to net cash used in investing activities of \$0.7 million for the three months ended July 29, 2006. The increase in net cash provided by investing activities was primarily due to sales of short-term investments to fund working capital needs. During the three months ended July 28, 2007 and July 29, 2006, we used cash to purchase property and equipment totaling \$2.2 million and \$0.7 million, respectively.

Cash Provided by Financing Activities. Net cash provided by financing activities was unchanged at \$0.2 million for the three months ended July 28, 2007, compared to the three months ended July 29, 2006. During the three months ended July 28, 2007 and July 29, 2006, we received proceeds from stock option exercises of \$0.3 million and \$0.2 million, respectively.

Line of Credit and Term Loan Facilities

We have a revolving line of credit with a bank, under which we may borrow up to \$16.5 million. Borrowings bear interest at the bank's prime commercial lending rate, which was 8.25% as of July 28, 2007 and April 30, 2007. The line of credit is secured by substantially all of our assets. Payment of amounts outstanding is made at our discretion. All principal plus accrued interest is due August 31, 2007. We had no outstanding balance on the line of credit as of July 28, 2007 and April 30, 2007.

Effective August 31, 2007, we amended and restated our Business Loan Agreement with our bank, California Bank & Trust, to increase our borrowing limit from \$16,500,000 to \$25,000,000 and to extend the maturity date. Borrowings bear interest at the bank's prime commercial lending rate minus 0.25%. The line of credit is secured by substantially all of our assets.

The credit facility contains several financial covenants, including that we not exceed maximum liquidity and leverage ratios, and limitations on additional indebtedness. In addition, the facility contains certain other restrictive loan covenants, including covenants limiting our ability to dispose of assets, make acquisitions, be acquired, incur indebtedness, grant liens, make investments, pay dividends, and repurchase stock. The facility also includes customary default provisions, and all outstanding obligations may become immediately due and payable in the event of our default.

Interest on amounts outstanding under the line of credit are due monthly. All principal plus accrued but unpaid interest on the line of credit is due August 31, 2009. We had no outstanding balance on the line of credit as of August 30, 2007.

We have entered into standby letter-of-credit agreements and bank guarantee agreements with financial institutions and customers primarily relating to the guarantee of our future performance on certain contracts to provide products and services and to secure advance payments we have received from certain international customers. As of July 28, 2007, we had standby letters of credit totaling \$0.4 million and had received no claims against such letters of credit. These letters of credit expire upon release by the customer.

Off-Balance Sheet Arrangements

During the first quarter, there were no material changes in our off balance sheet arrangements or contractual obligations and commercial commitments from those disclosed in the Form 10-K for the fiscal year ended April 30, 2007.

Inflation

Our operations have not been, and we do not expect them to be, materially affected by inflation. Historically, we have been successful in adjusting prices to our customers to reflect changes in our material and labor costs.

New Accounting Standards

See Notes to Consolidated Financial Statements (Unaudited) included elsewhere herein for disclosure on new accounting pronouncements.

Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

It is our policy not to enter into interest rate derivative financial instruments. We do not currently have any significant interest rate exposure.

Foreign Currency Exchange Rate Risk

Since a significant part of our sales and expenses are denominated in U.S. dollars, we have not experienced significant foreign exchange gains or losses to date, and do not expect to incur significant foreign exchange gains or losses in the future. We occasionally engage in forward contracts in foreign currencies to limit our exposure on non-U.S. dollar transactions.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the ordinary course of business, we are exposed to various market risk factors, including fluctuations in interest rates, changes in general economic conditions, domestic and foreign competition, and foreign currency exchange rates. Please refer to Item 7A — Quantitative and Qualitative Disclosures About Market Risk, contained in our Annual Report on Form 10-K for the fiscal year ended April 30, 2007, for further discussion on quantitative and qualitative disclosures about market risk.

ITEM 4T. CONTROLS AND PROCEDURES

Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure.

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by Rule 13a-15(b) under the Exchange Act, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures.

Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective and were operating at a reasonable assurance level.

Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting or in other factors identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during the quarter ended July 28, 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are not currently a party to any material legal proceedings. We are, however, subject to lawsuits from time to time in the ordinary course of business.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors disclosed under Part I, Item 1A, "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended April 30, 2007. Please refer to that section for disclosures regarding the risks and uncertainties related to our business.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit Number	Description
10.1	Amended and Restated Business Loan Agreement, dated August 31, 2007, between AeroVironment, Inc. and California Bank & Trust.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
32	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: September 6, 2007

AEROVIRONMENT, INC.

By: /s/ Timothy E. Conver
Timothy E. Conver
Chief Executive Officer and President
(Principal Executive Officer)

/s/ Stephen C. Wright
Stephen C. Wright
Chief Financial Officer (Principal
Financial and Accounting Officer)

Exhibit 10.1

BUSINESS LOAN AGREEMENT

Principal	Loan Date	Maturity	Loan No	Call/Coll	Account	Officer	Initials
\$25,000,000.00	08-31-2007	08/31/2009	9329000055-1		9329000055-1	22163	JL

References in the shaded area are for the Lender's use only and do not limit the applicability of this document to any particular loan or item. Any item above containing "****" has been omitted due to text length limitations

Borrower:	AeroVironment Inc. 181 W. Huntington Drive, Suite 202 Monrovia, CA 91016	Lender:	California Bank & Trust Los Angeles Commercial Banking 550 South Hope Street, Suite 300 Los Angeles, CA 90071
------------------	---	----------------	---

THIS BUSINESS LOAN AGREEMENT dated August 31, 2007, is made and executed between AeroVironment, Inc. ("Borrower") and California Bank & Trust ("Lender") on the following terms and conditions. Borrower has received prior commercial loans from Lender or has applied to Lender for a commercial loan or loans or other financial accommodations, including those which may be described on any exhibit or schedule attached to this Agreement ("Loan"). Borrower understands and agrees that: (A) in granting, renewing, or extending any Loan, Lender is relying upon Borrower's representations, warranties, and agreements as set forth in this Agreement; (B) the granting, renewing, or extending of any Loan by Lender at all times shall be subject to Lenders sole judgment and discretion; and (C) all such Loans shall be and remain subject to the terms and conditions of this Agreement.

TERM. This Agreement shall be effective as of August 31, 2007, and shall continue in full force and effect until such time as all of Borrower's Loans in favor of Lender have been paid in full, including principal, interest, costs, expenses, attorneys' fees, and other fees and charges, or until such time as the parties may agree in writing to terminate this Agreement.

ADVANCE AUTHORITY. The following persons currently are authorized to request advances and authorize payments under the line of credit until Lender receives from Borrower, at Lender's address shown above, written notice of revocation of their authority: **Timothy Conver, President/CEO of AeroVironment, Inc.; Stephen C. Wright, CFO/VP of Finance/Sec. of AeroVironment, Inc.; and Suzanne Gilman, Controller.**

CONDITIONS PRECEDENT TO EACH ADVANCE . Lender's obligation to make the initial Advance and each subsequent Advance under this Agreement shall be subject to the fulfillment to Lender's satisfaction of all of the conditions set forth in this Agreement and in the Related Documents.

Loan Documents. Borrower shall provide to Lender the following documents for the Loan: (1) the Note; (2) Security Agreements granting to Lender security interests in the Collateral; (3) financing statements and all other documents perfecting Lender's Security Interests; (4) evidence of insurance as required below; (5) together with all such Related Documents as Lender may require for the Loan; all in form and substance satisfactory to Lender and Lender's counsel.

Borrower's Authorization. Borrower shall have provided in form and substance satisfactory to Lender properly certified resolutions, duly authorizing the execution and delivery of this Agreement, the Note and the Related Documents. In addition, Borrower shall have provided such other resolutions, authorizations, documents and instruments as Lender or its counsel, may require.

Payment of Fees and Expenses. Borrower shall have paid to Lender all fees, charges, and other expenses which are then due and payable as specified in this Agreement or any Related Document.

Representations and Warranties. The representations and warranties set forth in this Agreement, in the Related Documents, and in any document or certificate delivered to Lender under this Agreement are true and correct.

No Event of Default. There shall not exist at the time of any Advance a condition which would constitute an Event of Default under this Agreement or under any Related Document.

REPRESENTATIONS AND WARRANTIES. Borrower represents and warrants to Lender, as of the date of this Agreement, as of the date of each disbursement of loan proceeds, as of the date of any renewal, extension or modification of any Loan, and at all times any indebtedness exists:

Organization. Borrower is a corporation for profit which is, and at all times shall be, duly organized, validly existing, and in good standing under and by virtue of the laws of the State of Delaware. Borrower is duly authorized to transact business in all other states in which Borrower is doing business, having obtained all necessary filings, governmental licenses and approvals for each state in which Borrower is doing business. Specifically, Borrower is, and at all times shall be, duly qualified as a foreign corporation in all states in which the failure to so qualify would have a material adverse effect on its business or financial condition. Borrower has the full power and authority to own its properties and to transact the business in which it is presently engaged or presently proposes to engage. Borrower maintains an office at 2711 Centerville Road, Suite 400, Wilmington, DE 19808. Unless Borrower has designated otherwise in writing, the principal office is the office at which Borrower keeps its books and records including its records concerning the Collateral. Borrower will notify Lender prior to any change in the location of Borrower's state of organization or any change in Borrower's name. Borrower shall do all things necessary to preserve and to keep in full force and effect its existence, rights and privileges, and shall comply with all regulations, rules, ordinances, statutes, orders and decrees of any governmental or quasi-governmental authority or court applicable to Borrower and Borrower's business activities.

Assumed Business Names. Borrower has filed or recorded all documents or filings required by law relating to all assumed business names used by Borrower. Excluding the name of Borrower, the following is a complete list of all assumed business names under which Borrower does business: **None.**

Authorization. Borrower's execution, delivery, and performance of this Agreement and all the Related Documents have been duly authorized by all necessary action by Borrower and do not conflict with, result in a violation of, or constitute a default under (1) any provision of (a) Borrower's articles of incorporation or organization, or bylaws, or (b) any agreement or other instrument binding upon Borrower or (2) any law, governmental regulation, court decree, or order applicable to Borrower or to Borrower's properties.

Financial Information. Each of Borrower's financial statements supplied to Lender truly and completely disclosed Borrower's financial condition as of the date of the statement, and there has been no material adverse change in Borrowers financial condition subsequent to the date of the most recent financial

statement supplied to Lender. Borrower has no material contingent obligations except as disclosed in such financial statements.

Legal Effect. This Agreement constitutes, and any instrument or agreement Borrower is required to give under this Agreement when delivered will constitute legal, valid, and binding obligations of Borrower enforceable against Borrower in accordance with their respective terms.

Properties. Except as contemplated by this Agreement or as previously disclosed in Borrower's financial statements or in writing to Lender and as accepted by Lender, and except for property tax liens for taxes not presently due and payable, Borrower owns and has good title to all of Borrowers properties free and clear of all Security Interests, and has not executed any security documents or financing statements relating to such properties. All of Borrower's properties are titled in Borrower's legal name, and Borrower has not used or filed a financing statement under any other name for at least the last five (5) years.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 2

Hazardous Substances. Except as disclosed to and acknowledged by Lender in writing, Borrower represents and warrants that: (1) During the period of Borrower's ownership of the Collateral, there has been no use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance by any person on, under, about or from any of the Collateral. (2) Borrower has no knowledge of, or reason to believe that there has been (a) any breach or violation of any Environmental Laws; (b) any use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance on, under, about or from the Collateral by any prior owners or occupants of any of the Collateral; or (c) any actual or threatened litigation or claims of any kind by any person relating to such matters. (3) Neither Borrower nor any tenant, contractor, agent or other authorized user of any of the Collateral shall use, generate, manufacture, store, treat, dispose of or release any Hazardous Substance on, under, about or from any of the Collateral; and any such activity shall be conducted in compliance with all applicable federal, state, and local laws, regulations, and ordinances, including without limitation all Environmental Laws. Borrower authorizes Lender and its agents to enter upon the Collateral to make such inspections and tests as Lender may deem appropriate to determine compliance of the Collateral with this section of the Agreement. Any inspections or tests made by Lender shall be at Borrower's expense and for Lender's purposes only and shall not be construed to create any responsibility or liability on the part of Lender to Borrower or to any other person. The representations and warranties contained herein are based on Borrower's due diligence in investigating the Collateral for hazardous waste and Hazardous Substances. Borrower hereby (1) releases and waives any future claims against Lender for indemnity or contribution in the event Borrower becomes liable for cleanup or other costs under any such laws, and (2) agrees to indemnify, defend, and hold harmless Lender against any and all claims, losses, liabilities, damages, penalties, and expenses which Lender may directly or indirectly sustain or suffer resulting from a breach of this section of the Agreement or as a consequence of any use, generation, manufacture, storage, disposal, release or threatened release of a hazardous waste or substance on the Collateral. The provisions of this section of the Agreement, including the obligation to indemnify and defend, shall survive the payment of the Indebtedness and the termination, expiration or satisfaction of this Agreement and shall not be affected by Lender's acquisition of any interest in any of the Collateral, whether by foreclosure or otherwise.

Litigation and Claims. No litigation, claim, investigation, administrative proceeding or similar action (including those for unpaid taxes) against Borrower is pending or threatened, and no other event has occurred which may materially adversely affect Borrower's financial condition or properties, other than litigation, claims, or other events, if any, that have been disclosed to and acknowledged by Lender in writing.

Taxes. To the best of Borrower's knowledge, all of Borrower's tax returns and reports that are or were required to be filed, have been filed, and all taxes, assessments and other governmental charges have been paid in full, except those presently being or to be contested by Borrower in good faith in the ordinary course of business and for which adequate reserves have been provided.

Lien Priority. Unless otherwise previously disclosed to Lender in writing, Borrower has not entered into or granted any Security Agreements, or permitted the filing or attachment of any Security Interests on or affecting any of the Collateral directly or indirectly securing repayment of Borrower's Loan and Note, that would be prior or that may in any way be superior to Lender's Security Interests and rights in and to such Collateral.

Binding Effect. This Agreement, the Note, all Security Agreements (if any), and all Related Documents are binding upon the signers thereof, as well as upon their successors, representatives and assigns, and are legally enforceable in accordance with their respective terms.

AFFIRMATIVE COVENANTS. Borrower covenants and agrees with Lender that, so long as this Agreement remains in effect, Borrower will:

Notices of Claims and Litigation. Promptly inform Lender in writing of (1) all material adverse changes in Borrower's financial condition, and (2) all existing and all threatened litigation, claims, investigations, administrative proceedings or similar actions affecting Borrower or any Guarantor which could materially affect the financial condition of Borrower or the financial condition of any Guarantor.

Financial Records. Maintain its books and records in accordance with GAAP, applied on a consistent basis, and permit Lender to examine and audit Borrower's books and records at all reasonable times.

Financial Statements. Furnish Lender with the following:

Annual Statements. As soon as available, but in no event later than ninety (90) days after the end of each fiscal year. Borrower's balance sheet and income statement for the year ended, audited by a certified public accountant satisfactory to Lender.

Interim Statements. As soon as available, but in no event later than forty-five (45) days after the end of each fiscal quarter, Borrower's balance sheet and profit and loss statement for the period ended, prepared by Borrower.

All financial reports required to be provided under this Agreement shall be prepared in accordance with GAAP, applied on a consistent basis, and certified by Borrower as being true and correct.

Additional Information. Furnish such additional information and statements, as Lender may request from time to time. Financial Covenants and Ratios. Comply with the following covenants and ratios:

Working Capital Requirements. Borrower shall comply with the following working capital ratio requirements:

Quick Ratio. Maintain a Quick Ratio in excess of **1.000 to 1.000**. The term "Quick Ratio" means Borrower's Cash & Equivalent plus Borrower's net Trade Receivables divided by Borrower's total Current Liabilities. This liquidity ratio will be evaluated as of quarter-end.

Tangible Net Worth Requirements. Borrower shall comply with the following net worth ratio requirements:

Debt / Worth Ratio. Maintain a ratio of Debt / Worth not in excess of **2.250 to 1.000**. The ratio "Debt / Worth" means Borrower's Total Liabilities divided by Borrower's Tangible Net Worth. This leverage ratio will be evaluated as of quarter-end.

Other Requirements.

Debt Service Coverage Ratio. Maintain a minimum Debt Service Coverage ratio of 2.50 to 1.00, to be measured quarterly on a rolling 4-quarter basis. Debt Service Coverage Ratio is defined as “Earning Before Interest Expenses, Taxes, Depreciation and Amortization Expenses divided by Current Portion of Long-Term Debt plus Interest Expense.

Additional Provision. Borrower covenants and agrees with Lender that, notwithstanding anything herein to the contrary, while this Agreement is in effect, (a) Borrower shall be allowed to issue dividends of up to 50% of net annual earnings provided that such dividends does not result in the violation of any covenant (other than the conveanant against eh payment of dividend set forth in subsection (3) under “NEGATIVE COVENANCTS – Continuity of Operations”); and (b) Borrower shall be allowed to acquire or invest in other entities in an amount not to exceed \$15,000,000 provided that such acquisition/Investment does not result in the violation of any covenant (other than the covenants against acquisitions and investments set forth in subsection (2) under “NEGATIVE COVENANCES – continuity of Operations” and subsection (1) and (2) under “NEGATIVE COVENANTS – Loans, Acquisitions and Guaranties”).

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 3

Except as provided above, all computations made to determine compliance with the requirements contained in this paragraph shall be made in accordance with generally accepted accounting principles, applied on a consistent basis, and certified by Borrower as being true and correct.

Insurance. Maintain fire and other risk insurance, public liability insurance, and such other insurance as Lender may require with respect to Borrower's properties and operations, in form, amounts, coverages and with insurance companies acceptable to Lender. Borrower, upon request of Lender, will deliver to Lender from time to time the policies or certificates of insurance in form satisfactory to Lender, including stipulations that coverages will not be cancelled or diminished without at least ten (10) days prior written notice to Lender. Each insurance policy also shall include an endorsement providing that coverage in favor of Lender will not be impaired in any way by any act, omission or default of Borrower or any other person. In connection with all policies, covering assets in which Lender holds or is offered a security interest for the Loans, Borrower will provide Lender with such lender's loss payable or other endorsements as Lender may require.

Insurance Reports. Furnish to Lender, upon request of Lender, reports on each existing insurance policy showing such information as Lender may reasonably request, including without limitation the following: (1) the name of the insurer; (2) the risks insured; (3) the amount of the policy; (4) the properties insured; (5) the then current property values on the basis of which insurance has been obtained, and the manner of determining those values; and (6) the expiration date of the policy. In addition, upon request of Lender (however not more often than annually), Borrower will have an independent appraiser satisfactory to Lender determine, as applicable, the actual cash value or replacement cost of any Collateral. The cost of such appraisal shall be paid by Borrower.

Other Agreements. Comply with all terms and conditions of all other agreements, whether now or hereafter existing, between Borrower and any other party and notify Lender immediately in writing of any default in connection with any other such agreements.

Loan Proceeds. Use all Loan proceeds solely for Borrower's business operations, unless specifically consented to the contrary by Lender in writing.

Taxes, Charges and Liens. Pay and discharge when due all of its indebtedness and obligations, including without limitation all assessments, taxes, governmental charges, levies and liens, of every kind and nature, imposed upon Borrower or its properties, income, or profits, prior to the date on which penalties would attach, and all lawful claims that, if unpaid, might become a lien or charge upon any of Borrower's properties, income, or profits.

Performance. Perform and comply, in a timely manner, with all terms, conditions, and provisions set forth in this Agreement, in the Related Documents, and in all other instruments and agreements between Borrower and Lender. Borrower shall notify Lender immediately in writing of any default in connection with any agreement.

Operations. Maintain executive and management personnel with substantially the same qualifications and experience as the present executive and management personnel; provide written notice to Lender of any change in executive and management personnel; conduct its business affairs in a reasonable and prudent manner.

Environmental Studies. Promptly conduct and complete, at Borrower's expense, all such investigations, studies, samplings and testings as may be requested by Lender or any governmental authority relative to any substance, or any waste or by-product of any substance defined as toxic or a hazardous substance under applicable federal, state, or local law, rule, regulation, order or directive, at or affecting any property or any facility owned, leased or used by Borrower.

Compliance with Governmental Requirements. Comply with all laws, ordinances, and regulations, now or hereafter in effect, of all governmental authorities applicable to the conduct of Borrower's properties, businesses and operations, and to the use or occupancy of the Collateral, including without limitation, the Americans With Disabilities Act. Borrower may contest in good faith any such law, ordinance, or regulation and withhold compliance during any proceeding, including appropriate appeals, so long as Borrower has notified Lender in writing prior to doing so and so long as, in Lender's sole opinion, Lender's interests in the Collateral are not jeopardized. Lender may require Borrower to post adequate security or a surety bond, reasonably satisfactory to Lender, to protect Lenders interest.

Inspection. Permit employees or agents of Lender at any reasonable time to inspect any and all Collateral for the Loan or Loans and Borrower's other properties and to examine or audit Borrower's books, accounts, and records and to make copies and memoranda of Borrower's books, accounts, and records. If Borrower now or at any time hereafter maintains any records (including without limitation computer generated records and computer software programs for the generation of such records) in the possession of a third party. Borrower, upon request of Lender, shall notify such party to permit Lender free access to such records at all reasonable times and to provide Lender with copies of any records it may request, all at Borrower's expense.

Environmental Compliance and Reports. Borrower shall comply in all respects with any and all Environmental Laws; not cause or permit to exist, as a result of an intentional or unintentional action or omission on Borrower's part or on the part of any third party, on property owned and/or occupied by Borrower, any environmental activity where damage may result to the environment, unless such environmental activity is pursuant to and in compliance with the conditions of a permit issued by the appropriate federal, state or local governmental authorities; shall furnish to Lender promptly and in any event within thirty (30) days after receipt thereof a copy of any notice, summons, lien, citation, directive, letter or other communication from any governmental agency or instrumentality concerning any intentional or unintentional action or omission on Borrower's part in connection with any environmental activity whether or not there is damage to the environment and/or other natural resources.

Additional Assurances. Make, execute and deliver to Lender such promissory notes, mortgages, deeds of trust, security agreements, assignments, financing statements, instruments, documents and other agreements as Lender or its attorneys may reasonably request to evidence and secure the Loans and to perfect all Security Interests.

LENDER'S EXPENDITURES. If any action or proceeding is commenced that would materially affect Lenders interest in the Collateral or if Borrower fails to comply with any provision of this Agreement or any Related Documents, including but not limited to Borrower's failure to discharge or pay when due any amounts Borrower is required to discharge or pay under this Agreement or any Related Documents, Lender on Borrower's behalf may (but shall not be

obligated to) take any action that Lender deems appropriate, including but not limited to discharging or paying all taxes, liens, security interests, encumbrances and other claims, at any time levied or placed on any Collateral and paying all costs for insuring, maintaining and preserving any Collateral. All such expenditures incurred or paid by Lender for such purposes will then bear interest at the rate charged under the Note from the date incurred or paid by Lender to the date of repayment by Borrower. All such expenses will become a part of the Indebtedness and, at Lender's option, will (A) be payable on demand; (B) be added to the balance of the Note and be apportioned among and be payable with any installment payments to become due during either (1) the term of any applicable insurance policy; or (2) the remaining term of the Note; or (C) be treated as a balloon payment which will be due and payable at the Note's maturity.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 4

NEGATIVE COVENANTS. Borrower covenants and agrees with Lender that while this Agreement is in effect, Borrower shall not, without the prior written consent of Lender:

Indebtedness and Liens. (1) Except for trade debt incurred in the normal course of business and indebtedness to Lender contemplated by this Agreement, create, incur or assume indebtedness for borrowed money, including capital leases, (2) sell, transfer, mortgage, assign, pledge, lease, grant a security interest in, or encumber any of Borrower's assets (except as allowed as Permitted Liens), or (3) sell with recourse any of Borrower's accounts, except to Lender.

Continuity of Operations. (1) Engage in any business activities substantially different than those in which Borrower is presently engaged, (2) cease operations, liquidate, merge, transfer, acquire or consolidate with any other entity, change its name, dissolve or transfer or sell Collateral out of the ordinary course of business, or (3) pay any dividends on Borrower's stock (other than dividends payable in its stock), provided, however that notwithstanding the foregoing, but only so long as no Event of Default has occurred and is continuing or would result from the payment of dividends, if Borrower is a "Subchapter S Corporation" (as defined in the Internal Revenue Code of 1986, as amended), Borrower may pay cash dividends on its stock to its shareholders from time to time in amounts necessary to enable the shareholders to pay income taxes and make estimated income tax payments to satisfy their liabilities under federal and state law which arise solely from their status as Shareholders of a Subchapter S Corporation because of their ownership of shares of Borrower's stock, or purchase or retire any of Borrower's outstanding shares or alter or amend Borrower's capital structure,

Loans, Acquisitions and Guaranties. (1) Loan, invest in or advance money or assets to any other person, enterprise or entity, (2) purchase, create or acquire any interest in any other enterprise or entity, or (3) incur any obligation as surety or guarantor other than in the ordinary course of business.

Agreements. Borrower will not enter into any agreement containing any provisions which would be violated or breached by the performance of Borrower's obligations under this Agreement or in connection herewith.

CESSATION OF ADVANCES. If Lender has made any commitment to make any Loan to Borrower, whether under this Agreement or under any other agreement, Lender shall have no obligation to make Loan Advances or to disburse Loan proceeds if: (A) Borrower or any Guarantor is in default under the terms of this Agreement or any of the Related Documents or any other agreement that Borrower or any Guarantor has with Lender; (B) Borrower or any Guarantor dies, becomes incompetent or becomes insolvent, files a petition in bankruptcy or similar proceedings, or is adjudged a bankrupt; (C) there occurs a material adverse change in Borrower's financial condition, in the financial condition of any Guarantor, or in the value of any Collateral securing any Loan; or (D) any Guarantor seeks, claims or otherwise attempts to limit, modify or revoke such Guarantor's guaranty of the Loan or any other loan with Lender; or (E) Lender in good faith deems itself insecure, even though no Event of Default shall have occurred.

DEFAULT. Each of the following shall constitute an Event of Default under this Agreement:

Payment Default. Borrower fails to make any payment when due under the Loan.

Other Defaults. Borrower fails to comply with or to perform any other term, obligation, covenant or condition contained in this Agreement or in any of the Related Documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Borrower.

Default in Favor of Third Parties. Borrower or any Grantor defaults under any loan, extension of credit, security agreement, purchase or sales agreement, or any other agreement, in favor of any other creditor or person that may materially affect any of Borrower's or any Grantor's property or Borrower's or any Grantor's ability to repay the Loans or perform their respective obligations under this Agreement or any of the Related Documents.

False Statements. Any warranty, representation or statement made or furnished to Lender by Borrower or on Borrower's behalf under this Agreement or the Related Documents is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Insolvency. The dissolution or termination of Borrower's existence as a going business, the insolvency of Borrower, the appointment of a receiver for any part of Borrower's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Borrower.

Defective Collateralization. This Agreement or any of the Related Documents ceases to be in full force and effect (including failure of any collateral document to create a valid and perfected security interest or lien) at any time and for any reason.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Borrower or by any governmental agency against any collateral securing the Loan. This includes a garnishment of any of Borrower's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Borrower as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Borrower gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any Guarantor of any of the Indebtedness or any Guarantor dies or becomes incompetent, or revokes or disputes the validity of, or liability under, any Guaranty of the Indebtedness. In the event of a death, Lender, at its option, may, but shall not be required to, permit the Guarantor's estate to assume unconditionally the obligations arising under the guaranty in a manner satisfactory to Lender, and, in doing so, cure any Event of Default.

Change in Ownership. Any change in ownership of twenty-five percent (25%) or more of the common stock of Borrower.

Adverse Change. A material adverse change occurs in Borrower's financial condition, or Lender believes the prospect of payment or performance of the

Loan is impaired.

Insecurity. Lender in good faith believes itself insecure.

Right to Cure. If any default, other than a default on Indebtedness, is curable and if Borrower or Grantor, as the case may be, has not been given a notice of a similar default within the preceding twelve (12) months, it may be cured if Borrower or Grantor, as the case may be, after receiving written notice from Lender demanding cure of such default: (1) cure the default within fifteen (15) days; or (2) if the cure requires more than fifteen (15) days, immediately initiate steps which Lender deems in Lender's sole discretion to be sufficient to cure the default and thereafter continue and complete all reasonable and necessary steps sufficient to produce compliance as soon as reasonably practical.

EFFECT OF AN EVENT OF DEFAULT. If any Event of Default shall occur, except where otherwise provided in this Agreement or the Related Documents, all commitments and obligations of Lender under this Agreement or the Related Documents or any other agreement immediately will terminate (including any obligation to make further Loan Advances or disbursements), and, at Lender's option, all Indebtedness immediately will become due and payable, all without notice of any kind to Borrower, except that in the case of an Event of Default of the type described in the 'Insolvency' subsection above, such acceleration shall be automatic and not optional. In addition, Lender shall have all the rights and remedies provided in the Related Documents or available at law, in equity, or otherwise. Except as may be prohibited by applicable law, all of Lender's rights and remedies shall be cumulative and may be exercised singularly or concurrently. Election by Lender to pursue any remedy shall not exclude pursuit of any other remedy, and an election to make expenditures or to take action to perform an obligation of Borrower or of any Grantor shall not affect Lender's right to declare a default and to exercise its rights and remedies.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 5

DEPOSIT AGREEMENT SECURITY. Borrower hereby grants a security interest to Lender in any and all deposit accounts (checking, savings, money market or time) of Borrower at Lender, now existing or hereinafter opened, to secure the Indebtedness. This includes all deposit accounts Borrower holds jointly with someone else.

JURY WAIVER; JUDICIAL REFERENCE. Borrower and Lender each waive their respective rights to a trial before a jury in connection with any disputes related to this Agreement, any of the Related Documents and the transactions contemplated hereby and thereby. Such disputes include without limitation any claim by Borrower or Lender, claims brought by Borrower as a class representative on behalf of others, and claims by a class representative on Borrower's behalf as a class member (so-called "class action" suits). This provision shall not apply if, at the time an action is brought, Borrower's loan is funded or maintained in a state where this jury trial waiver is not permitted by law.

If a jury trial waiver is not permitted by applicable law and a dispute arises between Borrower and Lender with respect to this Agreement, any of the Related Documents, the enforcement hereof or thereof or the transactions contemplated hereby or thereby, either of Borrower or Lender may require that it be resolved by judicial reference in accordance with California Code of Civil Procedure, Sections 638, et seq., including without limitation whether the dispute is subject to a judicial reference proceeding. The referee shall be a retired judge, agreed upon by the parties, from either the American Arbitration Association (AAA) or Judicial Arbitration and Mediation Service, Inc. (JAMS). If the parties cannot agree on the referee, the party who initially selected the reference procedure shall request a panel of ten retired judges from either AAA or JAMS, and the court shall select the referee from that panel. The referee shall be appointed to sit with all of the powers provided by law. The parties agree that time is of the essence in conducting the judicial reference proceeding set forth herein. The costs of the judicial reference proceeding, including the fee for the court reporter, shall be borne equally by the parties as the costs are incurred, unless otherwise awarded by the referee. The referee shall hear all pre-trial and post-trial matters (including without limitation requests for equitable relief), prepare an award with written findings of fact and conclusions of law and apportion costs as appropriate. The referee shall be empowered to enter equitable relief as well as legal relief, provide all temporary or provisional remedies, enter equitable orders that are binding on the parties and rule on any motion that would be authorized in a trial, including without limitation motions for summary judgment or summary adjudication. Judgment upon the award shall be entered in the court in which such proceeding was commenced and all parties shall have full rights of appeal. This provision will not be deemed to limit or constrain Lender's right of offset, to obtain provisional or ancillary remedies, to interplead funds in the event of a dispute, to exercise any security interest or lien Lender may hold in property or to comply with legal process involving Borrower's accounts or other property.

INCREASED COSTS. If any change in a law, rule or regulation, or the interpretation or application thereof, or Lender's compliance with any request, guideline or directive (whether or not having the force of law) of any governmental authority (collectively, a "Change in Law") shall (i) impose, modify or deem applicable any reserve, special deposit or similar requirement against or with respect to the assets of, deposits with or for the account of or credit extended by Lender or (ii) impose on Lender any other condition affecting this Agreement or the loans hereunder or any letter of credit or participation therein and the result of any of the foregoing shall be to increase the cost to Lender of making or maintaining any loan (or its commitment to make any such loan) or to increase the cost to Lender of issuing or maintaining any letter of credit or to reduce the amount of any sum received or receivable by Lender hereunder, then Borrower will pay to Lender such additional amount as will compensate Lender for such additional costs or reduction. If Lender determines that any Change in Law regarding capital requirements has or would have the effect of reducing the rate of return on the capital of Lender or Lender's holding company from this Agreement or the loans or letters of credit made or issued by Lender to a level below that which Lender or Lender's holding company could have achieved but for such Change in Law (taking into consideration Lender's policies and the policies of Lender's holding company with respect to capital adequacy), then from time to time Borrower will pay to Lender such additional amount as will compensate Lender or Lender's holding company for any such reduction, as set forth in a certificate of Lender describing in reasonable detail the amount or amounts necessary to compensate Lender or its holding company. The amounts and description in such certificate shall be conclusive absent manifest error, and Borrower agrees to pay to Lender the amount shown in such certificate within ten (10) business days after receipt thereof. Failure or delay on the part of Lender to demand compensation pursuant to this section shall not constitute a waiver of Lender's right to demand such compensation.

AMENDED AND RESTATED BUSINESS LOAN AGREEMENT . THIS AGREEMENT AMENDS AND RESTATES THE BUSINESS LOAN AGREEMENT DATED JUNE 16, 2005, BETWEEN BORROWER AND LENDER, AS AMENDED PRIOR TO THE DATE HEREOF (the "Original Loan Agreement"). Upon the execution and delivery of this Agreement, the Indebtedness, obligations and other liabilities, including without limitation interest and fees accrued to the date hereof under the Original Loan Agreement (collectively, the "Prior Obligations"), shall continue to exist and be in full force and effect but shall be governed by the terms and conditions set forth in this Agreement. The Prior Obligations, together with any and all additional Indebtedness and other obligations incurred by Borrower hereunder or the Related Documents shall continue to be secured by all of the pledges and security interests pursuant to the Commercial Security Agreement dated June 16, 2005, between Borrower and Lender (the "Original Security Agreement") and from and after the date hereof shall be secured by all of the pledges and security interests provided in connection with this Agreement, all as more specifically set forth in the Commercial Security Agreement dated August 31, 2007, which shall amend and restate the Original Security Agreement. Borrower hereby reaffirms the Indebtedness and its other obligations under the Original Loan Agreement and the Related Documents as defined in the Original Loan Agreement (collectively, the "Original Loan Documents"), as amended, supplemented or otherwise modified by this Agreement and Related Documents. Borrower further agrees that each such Original Loan Document shall remain in full force and effect following the execution and delivery of this Agreement and that all references to the Business Loan Agreement or the Loan Agreement in the Original Loan Documents shall be deemed to refer to this Agreement. The execution and delivery of this Agreement shall constitute an amendment, replacement and restatement, but not novation or repayment, of the Prior Obligations.

ADDITIONAL PROVISION. Borrower's waiver of its right to privacy in the section entitled "MISCELLANEOUS PROVISIONS - Consent to Loan Participation" shall be subject to the condition precedent that Lender and the purchaser of any participation interest (the "Participant") enter into a confidentiality agreement that provides for the Participant to maintain the confidentiality and not disclose any confidential or proprietary information of Borrower to the same extent that Lender is required to maintain the confidentiality or privacy of such information disclosed by Borrower to Lender.

MISCELLANEOUS PROVISIONS. The following miscellaneous provisions are a part of this Agreement:

Amendments. This Agreement, together with any Related Documents, constitutes the entire understanding and agreement of the parties as to the matters set forth in this Agreement. No alteration of or amendment to this Agreement shall be effective unless given in writing and signed by the party or parties sought to be charged or bound by the alteration or amendment.

Attorneys' Fees; Expenses. Borrower agrees to pay upon demand all of Lenders costs and expenses, including Lenders attorneys' fees and Lenders legal expenses, incurred in connection with the enforcement of this Agreement. Lender may hire or pay someone else to help enforce this Agreement, and Borrower shall pay the costs and expenses of such enforcement. Costs and expenses include Lender's attorneys' fees and legal expenses whether or not there is a lawsuit, including attorneys' fees and legal expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Borrower also shall pay all court costs and such additional fees as may be directed by the court.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 6

Caption Headings. Caption headings in this Agreement are for convenience purposes only and are not to be used to interpret or define the provisions of this Agreement.

Consent to Loan Participation. Borrower agrees and consents to Lenders sale or transfer, whether now or later, of one or more participation interests in the Loan to one or more purchasers, whether related or unrelated to Lender. Lender may provide, without any limitation whatsoever, to any one or more purchasers, or potential purchasers, any information or knowledge Lender may have about Borrower or about any other matter relating to the Loan, and Borrower hereby waives any rights to privacy Borrower may have with respect to such matters. Borrower additionally waives any and all notices of sale of participation interests, as well as all notices of any repurchase of such participation interests. Borrower also agrees that the purchasers of any such participation interests will be considered as the absolute owners of such interests in the Loan and will have all the rights granted under the participation agreement or agreements governing the sale of such participation interests. Borrower further waives all rights of offset or counterclaim that it may have now or later against Lender or against any purchaser of such a participation interest and unconditionally agrees that either Lender or such purchaser may enforce Borrower's obligation under the Loan irrespective of the failure or insolvency of any holder of any interest in the Loan. Borrower further agrees that the purchaser of any such participation interests may enforce its interests irrespective of any personal claims or defenses that Borrower may have against Lender.

Governing Law. This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of California without regard to its conflicts of law provisions. This Agreement has been accepted by Lender in the State of California.

Choice of Venue. If there is a lawsuit, Borrower agrees upon Lender's request to submit to the jurisdiction of the courts of Los Angeles County, State of California.

No Waiver by Lender. Lender shall not be deemed to have waived any rights under this Agreement unless such waiver is given in writing and signed by Lender. No delay or omission on the part of Lender in exercising any right shall operate as a waiver of such right or any other right. A waiver by Lender of a provision of this Agreement shall not prejudice or constitute a waiver of Lenders right otherwise to demand strict compliance with that provision or any other provision of this Agreement. No prior waiver by Lender, nor any course of dealing between Lender and Borrower, or between Lender and any Grantor, shall constitute a waiver of any of Lenders rights or of any of Borrower's or any Grantor's obligations as to any future transactions. Whenever the consent of Lender is required under this Agreement, the granting of such consent by Lender in any instance shall not constitute continuing consent to subsequent instances where such consent is required and in all cases such consent may be granted or withheld in the sole discretion of Lender.

Notices. Any notice required to be given under this Agreement shall be given in writing, and shall be effective when actually delivered, when actually received by telefacsimile (unless otherwise required by law), when deposited with a nationally recognized overnight courier, or, if mailed, when deposited in the United States mail, as first class, certified or registered mail postage prepaid, directed to the addresses shown near the beginning of this Agreement. Any party may change its address for notices under this Agreement by giving formal written notice to the other parties, specifying that the purpose of the notice is to change the party's address. For notice purposes, Borrower agrees to keep Lender informed at all times of Borrowers current address. Unless otherwise provided or required by law, if there is more than one Borrower, any notice given by Lender to any Borrower is deemed to be notice given to all Borrowers.

Severability. If a court of competent jurisdiction finds any provision of this Agreement to be illegal, invalid, or unenforceable as to any circumstance, that finding shall not make the offending provision illegal, invalid, or unenforceable as to any other circumstance. If feasible, the offending provision shall be considered modified so that it becomes legal, valid and enforceable. If the offending provision cannot be so modified, it shall be considered deleted from this Agreement. Unless otherwise required by law, the illegality, invalidity, or unenforceability of any provision of this Agreement shall not affect the legality, validity or enforceability of any other provision of this Agreement.

Subsidiaries and Affiliates of Borrower. To the extent the context of any provisions of this Agreement makes it appropriate, including without limitation any representation, warranty or covenant, the word "Borrower" as used in this Agreement shall include all of Borrower's subsidiaries and affiliates. Notwithstanding the foregoing however, under no circumstances shall this Agreement be construed to require Lender to make any Loan or other financial accommodation to any of Borrower's subsidiaries or affiliates.

Successors and Assigns. All covenants and agreements by or on behalf of Borrower contained in this Agreement or any Related Documents shall bind Borrower's successors and assigns and shall inure to the benefit of Lender and its successors and assigns. Borrower shall not, however, have the right to assign Borrower's rights under this Agreement or any interest therein, without the prior written consent of Lender.

Survival of Representations and Warranties. Borrower understands and agrees that in extending Loan Advances, Lender is relying on all representations, warranties, and covenants made by Borrower in this Agreement or in any certificate or other instrument delivered by Borrower to Lender under this Agreement or the Related Documents. Borrower further agrees that regardless of any investigation made by Lender, all such representations, warranties and covenants will survive the extension of Loan Advances and delivery to Lender of the Related Documents, shall be continuing in nature, shall be deemed made and redated by Borrower at the time each Loan Advance is made, and shall remain in full force and effect until such time as Borrower's Indebtedness shall be paid in full, or until this Agreement shall be terminated in the manner provided above, whichever is the last to occur.

Time is of the Essence. Time is of the essence in the performance of this Agreement.

DEFINITIONS. The following capitalized words and terms shall have the following meanings when used in this Agreement. Unless specifically stated to the contrary, all references to dollar amounts shall mean amounts in lawful money of the United States of America. Words and terms used in the singular shall include the plural, and the plural shall include the singular, as the context may require. Words and terms not otherwise defined in this Agreement shall have the meanings attributed to such terms in the Uniform Commercial Code. Accounting words and terms not otherwise defined in this Agreement shall have the meanings assigned to them in accordance with generally accepted accounting principles as in effect on the date of this Agreement:

Advance. The word "Advance" means a disbursement of Loan funds made, or to be made, to Borrower or on Borrower's behalf on a line of credit or

multiple advance basis under the terms and conditions of this Agreement.

Agreement. The word "Agreement" means this Business Loan Agreement, as this Business Loan Agreement may be amended or modified from time to time, together with all exhibits and schedules attached to this Business Loan Agreement from time to time.

Borrower. The word "Borrower" means AeroVironment, Inc. and includes all co-signers and co-makers signing the Note and all their successors and assigns.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 7

Cash & Equivalent. The words ‘Cash & Equivalent’ mean all of Borrower’s cash, marketable securities, and other near-cash items, excluding sinking funds.

Collateral. The word “Collateral” means all property and assets granted as collateral security for a Loan, whether real or personal property, whether granted directly or indirectly, whether granted now or in the future, and whether granted in the form of a security interest, mortgage, collateral mortgage, deed of trust, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factor’s lien, equipment trust, conditional sale, trust receipt, lien, charge, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever, whether created by law, contract, or otherwise.

Environmental Laws. The words “Environmental Laws” mean any and all state, federal and local statutes, regulations and ordinances relating to the protection of human health or the environment, including without limitation the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, 42 U.S.C. Section 9601, et seq. (“CERCLA”), the Superfund Amendments and Reauthorization Act of 1985, Pub. L. No. 99-499 (“SARA”), the Hazardous Materials Transportation Act, 49 U.S.C. Section 1801, et seq., the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901, et seq., Chapters 6.5 through 7.7 of Division 20 of the California Health and Safety Code, Section 25100, et seq., or other applicable state or federal laws, rules, or regulations adopted pursuant thereto.

Event of Default. The words “Event of Default” mean any of the events of default set forth in this Agreement in the default section of this Agreement.

GAAP. The word “GAAP” means generally accepted accounting principles.

Grantor. The word “Grantor” means each and all of the persons or entities granting a Security Interest in any Collateral for the Loan, including without limitation all Borrowers granting such a Security Interest.

Guarantor. The word “Guarantor” means any guarantor, surety, or accommodation party of any or all of the Loan.

Guaranty. The word “Guaranty” means the guaranty from Guarantor to Lender, including without limitation a guaranty of all or part of the Note.

Hazardous Substances. The words “Hazardous Substances” mean materials that, because of their quantity, concentration or physical, chemical or infectious characteristics, may cause or pose a present or potential hazard to human health or the environment when improperly used, treated, stored, disposed of, generated, manufactured, transported or otherwise handled. The words “Hazardous Substances” are used in their very broadest sense and include without limitation any and all hazardous or toxic substances, materials or waste as defined by or listed under the Environmental Laws. The term “Hazardous Substances” also includes, without limitation, petroleum and petroleum by-products or any fraction thereof and asbestos.

Indebtedness. The word “Indebtedness” means the indebtedness evidenced by the Note or Related Documents, including all principal and interest together with all other indebtedness and costs and expenses for which Borrower is responsible under this Agreement or under any of the Related Documents.

Lender. The word “Lender” means California Bank & Trust, its successors and assigns.

Loan. The word “Loan” means any and all loans and financial accommodations from Lender to Borrower whether now or hereafter existing, and however evidenced, including without limitation those loans and financial accommodations described herein or described on any exhibit or schedule attached to this Agreement from time to time.

Note. The word “Note” means the Note executed by AeroVironment Inc. in the original principal amount of \$10,000,000.00 dated March 31, 2004, together with all renewals of, extensions of, modifications of, refinancings of, consolidations of, and substitutions for the Note or Credit Agreement or any other subsequent Notes evidencing further Indebtedness.

Permitted Liens. The words “Permitted Liens” mean (1) liens and security interests securing Indebtedness owed by Borrower to Lender; (2) liens for taxes, assessments, or similar charges either not yet due or being contested in good faith; (3) liens of materialmen, mechanics, warehousemen, or carriers, or other like liens arising in the ordinary course of business and securing obligations which are not yet delinquent; (4) purchase money liens or purchase money security interests upon or in any property acquired or held by Borrower in the ordinary course of business to secure indebtedness outstanding on the date of this Agreement or permitted to be incurred under the paragraph of this Agreement titled “indebtedness and Liens”; (5) liens and security interests which, as of the date of this Agreement, have been disclosed to and approved by the Lender in writing; and (6) those liens and security interests which in the aggregate constitute an immaterial and insignificant monetary amount with respect to the net value of Borrower’s assets.

Related Documents. The words “Related Documents” mean all promissory notes, credit agreements, loan agreements, environmental agreements, guaranties, security agreements, mortgages, deeds of trust, security deeds, collateral mortgages, and all other instruments, agreements and documents, whether now or hereafter existing, executed in connection with the Loan.

Security Agreement. The words “Security Agreement” mean and include without limitation any agreements, promises, covenants, arrangements, understandings or other agreements, whether created by law, contract, or otherwise, evidencing, governing, representing, or creating a Security Interest.

Security Interest. The words “Security Interest” mean, without limitation, any and all types of collateral security, present and future, whether in the form of a lien, charge, encumbrance, mortgage, deed of trust, security deed, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factor’s lien, equipment trust, conditional sale, trust receipt, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever whether created by law, contract, or otherwise.

Tangible Net Worth. The words “Tangible Net Worth” mean Borrower’s total assets excluding all intangible assets (i.e., goodwill, trademarks, patents, copyrights, organizational expenses, and similar intangible items, but including leaseholds and leasehold improvements) less total debt.

Trade Receivables. The words “Trade Receivables” mean all of Borrower’s accounts from trade, net of allowance for doubtful accounts.

BUSINESS LOAN AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 8

BORROWER ACKNOWLEDGES HAVING READ ALL THE PROVISIONS OF THIS BUSINESS LOAN AGREEMENT AND BORROWER AGREES TO ITS TERMS. THIS BUSINESS LOAN AGREEMENT IS DATED AUGUST 31, 2007.

BORROWER:

AEROVIRONMENT. INC.

By: /s/ Timothy Conver

Timothy Conver,
President/CEO

By: /s/ Stephen Wright

Stephen Wright,
CFO /VP of Finance/Secretary

LENDER:

CALIFORNIA BANK & TRUST

By: /s/ Joe Lim

Authorized Signer

CHANGE OF TERMS

Principal	Loan Date	Maturity	Loan No	Call/Coll	Account	Officer	Initials
\$25,000,000.00	08-31-2007	08/31/2009	9329000055-1		9329000055-1	22163	JL

References in the shaded area are for the Lender's use only and do not limit the applicability of this document to any particular loan or item. Any item above containing "****" has been omitted due to text length limitations

Borrower:	AeroVironment Inc. 181 W. Huntington Drive, Suite 202 Monrovia, CA 91016	Lender:	California Bank & Trust Los Angeles Commercial Banking 550 South Hope Street, Suite 300 Los Angeles, CA 90071
------------------	---	----------------	--

Principal Amount: \$25,000,000.00

Initial Rate: 8.000%

Date of Agreement: August 31, 2007

DESCRIPTION OF EXISTING INDEBTEDNESS.

The Business Loan Agreement dated June 16, 2005 and Promissory Note dated March 31, 2004, in the original amount of \$10,000,000.00, as amended by those certain Change In Terms Agreements dated May 11, 2004 and June 16, 2005 from AeroVironment, Inc. to Lender.

DESCRIPTION OF COLLATERAL.

All inventory, equipment, accounts (including but not limited to all health-care-insurance receivables), chattel paper, instruments (including but not limited to all promissory notes), letter-of-credit rights, letters of credit, documents, deposit accounts, investment property, money, other rights to payment and performance, and general intangibles (including but not limited to all software and all payment intangibles); all fixtures; all attachments, accessions, accessories, fittings, increases, tools, parts, repairs, supplies, and commingled goods relating to the foregoing property, and all additions, replacements of and substitutions for all or any part of the foregoing property; all insurance refunds relating to the foregoing property; all good will relating to the foregoing property; all records and data and embedded software relating to the foregoing property, and all equipment, inventory and software to utilize, create, maintain and process any such records and data on electronic media; and all supporting obligations relating to the foregoing property; all whether now existing or hereafter arising, whether now owned or hereafter acquired or whether now or hereafter subject to any rights in the foregoing property; and all products and proceeds (including but not limited to all insurance payments) of or relating to the foregoing property.

Without limiting the generality of the foregoing, the Collateral shall include the following government contracts:

Government Contract Number W58RGZ-04 for US Army Raven

Government Contract Number DAAHO1-03-C0134 for US Army Raven

Government Contract Number DAAD16-03-C-0074 for SOCOM/NATICK Repair

Government Contract Number W91 IQY-04-C-0046

Government Contract Number FA8620 for AFOSOC Pointer

Government Contract Number M67854-04-D-101 1-0001 for Dragon Eye BOA

Government Contract Number N41756-04-D-4726 for Swift IDQ

Government Contract Number NCA4-3 for Pathfinder/Systems Analysis/Refurbish/Flight Testing.

DESCRIPTION OF CHANGE IN TERMS.

- 1) The Maturity Date is hereby extended from August 31, 2007 to August 31, 2009.
- 2) The Revolving Line of Credit is hereby increased from \$16,500,000.00 to \$25,000,000.00.
- 3) The interest rate is hereby amended from the California Bank & Trust Prime Rate, variable or the option of the One Month, Two Months, Three Months or Four Months, LIBOR plus 2.50% to California Bank & Trust Prime Rate minus 0.25%, variable or the option of the One Month, Two Months, Three Months or Four Months, LIBOR plus 2.00%.
- 4) The Stand-By Letter of Credit Subline is hereby amended and restated as set forth in the attached exhibit.
- 5) The Letter of Credit Subline is hereby amended and restated as set forth in the attached exhibit.
- 6) The Note is subject to the terms and conditions of that Business Loan Agreement executed by Borrower in favor of Lender, as amended and restated as of August 31 2007.

The Note is hereby amended and restated as follows:

PROMISE TO PAY. AeroVironment, Inc. ("Borrower") promises to pay to California Bank & Trust ("Lender"), or order, in lawful money of the United States of America, the principal amount of Twenty Five Million and 00/100 Dollars (\$25,000,000.00) or so much as may be outstanding, together with interest on the unpaid outstanding principal balance of each advance. Interest shall be calculated from the date of each advance until repayment of each advance.

PAYMENT. Borrower will pay this loan in one payment of all outstanding principal plus all accrued unpaid interest on August 31, 2009. In addition, Borrower will pay regular monthly payments of all accrued unpaid interest due as of each payment date, beginning September 30, 2007, with all subsequent interest payments to be due on the last day of each month after that. Unless otherwise agreed or required by applicable law, payments will be applied first to any accrued unpaid interest; then to principal; then to any unpaid collection costs; and then to any late charges. Interest on this loan is computed on a 365/360 simple interest basis; that is, by applying the ratio of the annual interest rate over a year of 360 days, multiplied by the outstanding principal balance, multiplied by the actual number of days the principal balance is outstanding. Borrower will pay Lender at Lender's address shown above or at such other place as Lender may designate in writing.

VARIABLE INTEREST RATE. Subject to designation of a different interest rate index by Borrower as provided below, the interest rate on this loan is subject to change from time to time based on changes in an index which is the rate of interest set from time to time by Bank as its Prime Rate- California Bank & Trust Prime Rate is determined by Bank as a means of pricing credit extensions to some customers and is neither tied to any external rate of interest or index nor is it necessarily the lowest rate of interest charged by Bank at any given time for any particular class of customers or credit extensions (the "Index"). The Index is not necessarily the lowest rate charged by Lender on its loans and is set by Lender in its sole discretion. If the Index becomes unavailable during the term of this loan, Lender may designate a substitute index after notifying Borrower. Lender will tell Borrower the current Index rate upon Borrower's request. The interest rate change will not occur more often than each Day. Borrower understands that Lender may make loans based on other rates as well. **The Index currently is 8.250% per annum.** The interest rate to be applied to the unpaid principal balance during this loan will be at a rate of 0.250 percentage points under the Index, resulting in an initial rate of 8.000% per annum. NOTICE: Under no circumstances will the interest rate on this loan be more than the maximum rate allowed by applicable law.

INTEREST RATE OPTIONS. On the terms and subject to the conditions set forth herein, Borrower will be able to select, from one of the following Rate Options, an interest rate which will be applicable to a particular dollar increment of amounts outstanding, or to be disbursed, under this Agreement. Principal shall be payable as specified herein in the "Payment" section, and interest shall be payable as specified for each Rate Option. The following Rate Options are available to Borrower:

CHANGE IN TERMS AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 2

(A) Default Option. The interest rate margin and index described in the "VARIABLE INTEREST RATE paragraph herein (the "Default Option").

(B) LIBOR. A margin of 2.000 percentage points over LIBOR. For purposes of this Agreement, LIBOR shall mean Lender's LIBOR rate for the relevant Interest Period determined as of the start of each Interest Period. The length of the Interest Period selected shall be designated One Month, Two Months, Three Months or Four Months, though the actual length of such periods shall be calculated as set forth below. The initial Interest Period, unless commenced on the first business day of a month, shall, notwithstanding the length of the Interest Period selected by Borrower, (i) for Interest Periods beginning before the 25th of each calendar month, end on the first business day of the month following commencement of the initial Interest Period; and (ii) for Interest Periods beginning on or after the 25th of each calendar month, end on the first business day of the second month following commencement of the initial Interest Period. All subsequent Interest Periods shall commence on the first business day of the relevant month and end on the first business day of the month determined by the length of the Interest Period selected by Borrower. The Bank's calculation pursuant to the provision of the length of the Interest Periods shall be in its sole and absolute discretion and shall conclusively bind the Borrower absent manifest error. Lender's LIBOR rate shall mean the rate per annum quoted by Lender as Lender's LIBOR rate based upon quotes from the London Interbank Offered Rate from the British Bankers Association Interest Settlement Rates, as quoted for U.S. Dollars by Bloomberg, or other comparable services selected by the Lender. This definition of Lender's LIBOR rate is to be strictly interpreted and is not intended to serve any purpose other than providing an index to determine the interest rate used herein. Lender's LIBOR rate may not necessarily be the same as the quoted offered side in the Eurodollar time deposit market by any particular institution or service applicable to any interest period. Interest based on this Rate Option is a floating rate and will change on and as of the date of a change in LIBOR (the "Interest Period"). Adjustments in the interest rate due to changes in the maximum nonusurious interest rate allowed (the "Highest Lawful Rate") shall be made on the effective day of any change in the Highest Lawful Rate. Under this Rate Option, Borrower shall make monthly interest payments on the same day of the month, with a final payment of all accrued and unpaid interest on the last day of such Interest Period and, in the case of an Interest Period greater than three (3) months, at three month (3 month) intervals after the first day of such Interest Period.

The following provisions concerning Rate Options are a part of this Agreement:

Selection of Rate Options. Provided Borrower is not in default under this Agreement, Borrower may request (a "Rate Request") that a \$100,000.00 increment or any amount in excess thereof (an "Increment") of the outstanding principal of, or amounts to be disbursed under, this Agreement bear interest at the selected rate. Borrower may make this Rate Request by telephonic notice, however no later than 10:00 AM PDT three (3) business days prior to the effective date of the Rate Request to permit Lender to quote the rate requested.

Applicable Interest Rate. Borrower's Rate Request will become effective, and interest on the increment designated will be calculated at the rate (the "Effective Rate"), which Borrower requested, for the applicable Interest Period, subject to the following:

(1) Notwithstanding any Rate Request, interest shall be calculated on the basis of the Default Option if (a) Lender, in good faith, is unable to ascertain the requested Rate Option by reason of circumstances then affecting the applicable money market or otherwise, (b) it becomes unlawful or impracticable for Lender to maintain loans based upon the requested Rate Option, or (c) Lender, in good faith, determines that it is impracticable to maintain loans based on the requested Rate Option because of increased taxes, regulatory costs, reserve requirements, expenses or any other costs or charges that affect such Rate Options. Upon the occurrence of any of the events described in this "Interest Rate Options" section, any increment to which a requested Rate Option applies shall be immediately (or at the option of Lender, at the end the current Interest Period), without further action of Lender or Borrower, converted to an increment to which the Default Option applies.

(2) Borrower may have no more than a total of 2 Effective Rates applicable to amounts outstanding under this Agreement at any given time.

(3) A Rate Request shall be effective as to amounts to be disbursed under this Agreement only if, on the effective date of the Rate Requests, such amounts are in fact disbursed to or for Borrower's account in accordance with the provisions of this Agreement and any related loan documents.

(4) Any amounts of outstanding principal for which a Rate Request has not been made, or is otherwise not effective, shall bear interest until paid in full at the Default Option.

(5) Any amounts of outstanding principal bearing interest based upon a Rate Option shall bear interest at such rate until the end of the Interest Period therefor, and thereafter shall bear interest based upon the Default Option unless a new Rate Request for a Rate Option complying with the terms hereof has been made and has become effective.

(6) If Borrower is in default under this Agreement ("Default"), then Lender shall no longer be obligated to honor any Rate Requests.

(7) No Interest Period shall extend beyond the maturity date of this Agreement.

Notices: Authority to Act. Borrower acknowledges and agrees that the agreement of Lender herein to receive certain notices by telephone is solely for Borrower's convenience. Lender shall be entitled to rely on the authority of the person purporting to be a person authorized by Borrower to give such notice, and Lender shall have no liability to Borrower on account of any action taken by Lender in reliance upon such telephonic notice. Borrower's obligation to repay all sums owing under the Note shall not be affected in any way or to any extent by any failure by Lender to receive written confirmation of any telephonic notice or the receipt by Lender of a confirmation which is at variance with the terms understood by Lender to be contained in the telephonic notice.

PREPAYMENT; MINIMUM INTEREST CHARGE. In any event, even upon full prepayment of this Agreement, Borrower understands that Lender is entitled to a **minimum interest charge of \$200.00**. Other than Borrower's obligation to pay any minimum interest charge, Borrower may pay without penalty all or a portion of the amount owed earlier than it is due. Early payments will not, unless agreed to by Lender in writing, relieve Borrower of Borrower's obligation to continue to make payments of accrued unpaid interest. Rather, early payments will reduce the principal balance due. Borrower agrees not to send Lender payments marked "paid in full", "without recourse", or similar language. If Borrower sends such a payment, Lender may accept it without losing any of Lender's rights under this Agreement, and Borrower will remain obligated to pay any further amount owed to Lender. All written communications

concerning disputed amounts, including any check or other payment instrument that indicates that the payment constitutes 'payment in full' of the amount owed or that is tendered with other conditions or limitations or as full satisfaction of a disputed amount must be mailed or delivered to: California Bank & Trust, Los Angeles Commercial Banking, 550 South Hope Street, Suite 300, Los Angeles, CA 9D071.

LATE CHARGE. If a payment is 15 days or more late, Borrower will be charged **6.000% of the regularly scheduled payment or \$500.00, whichever is less.**

CHANGE IN TERMS AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 3

INTEREST AFTER DEFAULT. Upon default, the interest rate on this loan shall, if permitted under applicable law, immediately increase by adding a 5.00 percentage point margin ("Default Rate Margin"). The Default Rate Margin shall also apply to each succeeding interest rate change that would have applied had there been no default.

DEFAULT. Each of the following shall constitute an Event of Default under this Agreement:

Payment Default. Borrower fails to make any payment when due under the Indebtedness.

Other Defaults. Borrower fails to comply with or to perform any other term, obligation, covenant or condition contained in this Agreement or in any of the Related Documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Borrower.

Default in Favor of Third Parties. Borrower defaults under any loan, extension of credit, security agreement, purchase or sales agreement, or any other agreement, in favor of any other creditor or person that may materially affect any of Borrowers property or Borrower's ability to perform Borrower's obligations under this Agreement or any of the Related Documents.

False Statements. Any warranty, representation or statement made or furnished to Lender by Borrower or on Borrower's behalf under this Agreement or the Related Documents is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Insolvency. The dissolution or termination of Borrower's existence as a going business, the insolvency of Borrower, the appointment of a receiver for any part of Borrower's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Borrower.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Borrower or by any governmental agency against any collateral securing the Indebtedness. This includes a garnishment of any of Borrower's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Borrower as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Borrower gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any guarantor, endorser, surety, or accommodation party of any of the Indebtedness or any guarantor, endorser, surety, or accommodation party dies or becomes incompetent, or revokes or disputes the validity of, or liability under, any Guaranty of the Indebtedness evidenced by this Note. In the event of a death, Lender, at its option, may, but shall not be required to, permit the guarantor's estate to assume unconditionally the obligations arising under the guaranty in a manner satisfactory to Lender, and, in doing so, cure any Event of Default.

Change In Ownership. Any change in ownership of twenty-five percent (25%) or more of the common stock of Borrower.

Adverse Change. A material adverse change occurs in Borrower's financial condition, or Lender believes the prospect of payment or performance of the Indebtedness is impaired.

Insecurity. Lender in good faith believes itself insecure.

Cure Provisions. If any default, other than a default in payment is curable and if Borrower has not been given a notice of a breach of the same provision of this Agreement within the preceding twelve (12) months, it may be cured if Borrower, after receiving written notice from Lender demanding cure of such default: (1) cures the default within fifteen (15) days; or (2) if the cure requires more than fifteen (15) days, immediately initiates steps which Lender deems in Lender's sole discretion to be sufficient to cure the default and thereafter continues and completes all reasonable and necessary steps sufficient to produce compliance as soon as reasonably practical.

LENDER'S RIGHTS. Upon default, Lender may declare the entire unpaid principal balance under this Agreement and all accrued unpaid interest immediately due, and then Borrower will pay that amount.

ATTORNEYS' FEES; EXPENSES. Lender may hire or pay someone else to help collect this Agreement if Borrower does not pay. Borrower will pay Lender that amount. This includes, subject to any limits under applicable law, Lender's attorneys' fees and Lender's legal expenses, whether or not there is a lawsuit, including attorneys' fees, expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), and appeals. Borrower also will pay any court costs, in addition to all other sums provided by law.

GOVERNING LAW, This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of California without regard to its conflicts of law provisions. This Agreement has been accepted by Lender in the State of California.

CHOICE OF VENUE. If there is a lawsuit, Borrower agrees upon Lender's request to submit to the jurisdiction of the courts of Los Angeles County, State of California.

COLLATERAL. Borrower acknowledges this Agreement is secured by the following collateral described in the security instrument listed herein: inventory, chattel paper, accounts, equipment and general intangibles described in a Commercial Security Agreement dated August 31, 2007.

LINE OF CREDIT. This Agreement evidences a revolving line of credit. Advances under this Agreement may be requested either orally or in writing by

Borrower or as provided in this paragraph. Lender may, but need not, require that all oral requests be confirmed in writing. All communications, instructions, or directions by telephone or otherwise to Lender are to be directed to Lender's office shown above. The following persons currently are authorized to request advances and authorize payments under the line of credit until Lender receives from Borrower, at Lender's address shown above, written notice of revocation of their authority: **Timothy Conver, President/CEO of AeroVironment, Inc.; Stephen C. Wright, CFO/VP of Finance/Sec. of AeroVironment, Inc.; and Suzanne Gilman, Controller.** Borrower agrees to be liable for all sums either: (A) advanced in accordance with the instructions of an authorized person or (B) credited to any of Borrower's accounts with Lender. The unpaid principal balance owing on this Agreement at any time may be evidenced by endorsements on this Agreement or by Lender's internal records, including daily computer print-outs.

CONTINUING VALIDITY. Except as expressly changed by this Agreement, the terms of the original obligation or obligations, including all agreements evidenced or securing the obligation(s), remain unchanged and in full force and effect. Consent by Lender to this Agreement does not waive Lender's right to strict performance of the obligation(s) as changed, nor obligate Lender to make any future change in terms. Nothing in this Agreement will constitute a satisfaction of the obligation(s). It is the intention of Lender to retain as liable parties all makers and endorsers of the original obligation(s), including accommodation parties, unless a party is expressly released by Lender in writing. Any maker or endorser, including accommodation makers, will not be released by virtue of this Agreement. If any person who signed the original obligation does not sign this Agreement below, then all persons signing below acknowledge that this Agreement is given conditionally, based on the representation to Lender that the non-signing party consents to the changes and provisions of this Agreement or otherwise will not be released by it. This waiver applies not only to any initial extension, modification or release, but also to all such subsequent actions.

CHANGE IN TERMS AGREEMENT

(Continued)

Loan No. 0329000055-1

Page 4

FINANCIAL STATEMENT CERTIFICATIONS. The undersigned hereby certifies to California Bank & Trust ("Bank") that all financial information ("Information") submitted to Bank now and at all times during the terms of this loan does, and will, fairly and accurately represent the financial condition of the undersigned, all Borrowers and Guarantors. Financial Information includes, but is not limited to all Business Financial Statements (including Interim and Year-End financial statements that are company prepared and/or CPA-prepared), Business Income Tax Returns, Borrowing Base Certificates, Accounts Receivable and Accounts Payable Agings, Personal Financial Statements and Personal Income Tax Returns. The undersigned understands that the Bank will rely on all financial information, whenever provided, and that such information is a material inducement to Bank to make, to continue to make, or otherwise extend credit accommodations to the undersigned. The undersigned covenants and agrees to notify Bank of any adverse material changes in her/his/its financial condition in the future. The undersigned further understands and acknowledges that there are criminal penalties for giving false financial information to federally insured financial institutions.

DEPOSIT AGREEMENT SECURITY. Borrower hereby grants a security interest to Lender in any and all deposit accounts (checking, savings, money market or time) of Borrower at Lender, now existing or hereinafter opened, to secure its Indebtedness hereunder. This includes all deposit accounts Borrower holds jointly with someone else. -

JURY WAIVER; JUDICIAL REFERENCE. Borrower and Lender each waive their respective rights to a trial before a jury in connection with any disputes related to this Note, the loan evidenced hereby and any other loan documents in connection herewith and therewith. Such disputes include without limitation any claim by Borrower or Lender, claims brought by Borrower- as a class representative on behalf of others, and claims by a class representative on Borrower's behalf as a class member (so-called "class action" suits). This provision shall not apply if, at the time an action is brought, Borrower's loan is funded or maintained in a state where this jury trial waiver is not permitted by law.

If a jury trial waiver is not permitted by applicable law and a dispute arises between Borrower and Lender with respect to this Note, its enforcement or the transactions contemplated by the related loan documents, either of Borrower or Lender may require that it be resolved by judicial reference in accordance with California Code of Civil Procedure, Sections 638, et seq., including without limitation whether the dispute is subject to a judicial reference proceeding. The referee shall be a retired judge, agreed upon by the parties, from either the American Arbitration Association (AAA) or Judicial Arbitration and Mediation Service, Inc. (JAMS). If the parties cannot agree on the referee, the party who initially selected the reference procedure shall request a panel of ten retired judges from either AAA or JAMS, and the court shall select the referee from that panel. The referee shall be appointed to sit with all of the powers provided by law. The parties agree that time is of the essence in conducting the judicial reference proceeding set forth herein. The costs of the judicial reference proceeding, including the fee for the court reporter, shall be borne equally by the parties as the costs are incurred, unless otherwise awarded by the referee. The referee shall hear all pre-trial and post-trial matters (including without limitation requests for equitable relief), prepare an award with written findings of fact and conclusions of law and apportion costs as appropriate. The referee shall be empowered to enter equitable relief as well as legal relief, provide all temporary or provisional remedies, enter equitable orders that are binding on the parties and rule on any motion that would be authorized in a trial, including without limitation motions for summary judgment or summary adjudication. Judgment upon the award shall be entered in the court in which such proceeding was commenced and all parties shall have full rights of appeal. This provision will not be deemed to limit or constrain Lender's right of offset, to obtain provisional or ancillary remedies, to interplead funds in the event of a dispute, to exercise any security interest or lien Lender may hold in property or to comply with legal process involving Borrower's accounts or other property.

STAND-BY LETTER OF CREDIT SUBLINE EXHIBIT. An exhibit, titled "Stand-By Letter of Credit Subline, is attached to this Agreement and by this reference is made a part of this Agreement just as if all the provisions, terms and conditions of the Exhibit had been fully set forth in this Agreement.

LETTER OF CREDIT SUBLINE EXHIBIT. An exhibit, titled "Letter of Credit Subline Exhibit," is attached to this Agreement and by this reference is made a part of this Agreement just as if all the provisions, terms and conditions of the Exhibit had been fully set forth in this Agreement.

SUCCESSORS AND ASSIGNS. Subject to any limitations stated in this Agreement on transfer of Borrower's interest, this Agreement shall be binding upon and inure to the benefit of the parties, their successors and assigns. If ownership of the Collateral becomes vested in a person other than Borrower, Lender, without notice to Borrower, may deal with Borrower's successors with reference to this Agreement and the Indebtedness by way of forbearance or extension without releasing Borrower from the obligations of this Agreement or liability under the Indebtedness.

MISCELLANEOUS PROVISIONS. If any part of this Agreement cannot be enforced, this fact will not affect the rest of the Agreement. Lender may delay or forgo enforcing any of its rights or remedies under this Agreement without losing them. Borrower and any other person who signs, guarantees or endorses this Agreement, to the extent allowed by law, waive any applicable statute of limitations, presentment, demand for payment, and notice of dishonor. Upon any change in the terms of this Agreement, and unless otherwise expressly stated in writing, no party who signs this Agreement, whether as maker, guarantor, accommodation maker or endorser, shall be released from liability. All such parties agree that Lender may renew or extend (repeatedly and for any length of time) this loan or release any party or guarantor or collateral; or impair, fail to realize upon or perfect Lender's security interest in the collateral; and take any other action deemed necessary by Lender without the consent of or notice to anyone. All such parties also agree that Lender may modify this loan without the consent of or notice to anyone other than the party with whom the modification is made. The obligations under this Agreement are joint and several.

PRIOR TO SIGNING THIS AGREEMENT, BORROWER READ AND UNDERSTOOD ALL THE PROVISIONS OF THIS AGREEMENT, INCLUDING THE VARIABLE INTEREST RATE PROVISIONS. BORROWER AGREES TO THE TERMS OF THE AGREEMENT.

BORROWER:

AEROVIRONMENT, INC.

By: /s/ Timothy Conver
Timothy Conver, President/CEO of
AeroVironment Inc.

By: /s/ Stephen C. Wright
Stephen C. Wright, CFO/VP of
Finance/Sec. Of AeroVironment, Inc.



Exhibit 31.1

**Certification of Principal Executive Officer
Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934**

I, Timothy E. Conver, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AeroVironment, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 6, 2007

/s/ Timothy E. Conver

Timothy E. Conver

Chief Executive Officer and Director

Exhibit 31.2

**Certification of Principal Financial Officer
Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934**

I, Stephen C. Wright, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AeroVironment, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 6, 2007

/s/ Stephen C. Wright

Stephen C. Wright

Chief Financial Officer

Exhibit 32

Certification

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(Subsections (a) and (b) of Section 1350, Chapter 63 of title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) (the "Act"), each of the undersigned officers of AeroVironment, Inc., a Delaware corporation (the "Company"), does hereby certify, to each such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended July 28, 2007 (the "Periodic Report") of the Company fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 780(d)) and information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Timothy E. Conver

Timothy E. Conver

Chief Executive Officer and Director

/s/ Stephen C. Wright

Stephen C. Wright

Chief Financial Officer

Dated: September 6, 2007

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.
