

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended July 31, 2016
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 0-15451



PHOTRONICS, INC.

(Exact name of registrant as specified in its charter)

Connecticut
(State or other jurisdiction of incorporation or organization)

06-0854886
(IRS Employer Identification No.)

15 Secor Road, Brookfield, Connecticut
(Address of principal executive offices)

06804
(Zip Code)

Registrant's telephone number, including area code

(203) 775-9000

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 periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class
Common Stock, \$0.01 par value

Outstanding at August 26, 2016
68,186,790 Shares

Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” for forward-looking statements made by or on behalf of Photronics, Inc. (“Photronics” or the “Company” or “we”). These statements are based on management’s beliefs, as well as assumptions made by, and information currently available to, management. Forward-looking statements may be identified by words like “expect,” “anticipate,” “believe,” “plan,” “project,” “could,” “estimate,” “intend,” “may,” “will” and similar expressions, or the negative of such terms, or other comparable terminology. All forward-looking statements involve risks and uncertainties that are difficult to predict. In particular, any statement contained in this quarterly report on Form 10-Q or in other documents filed with the Securities and Exchange Commission, in press releases or in the Company’s communications and discussions with investors and analysts in the normal course of business through meetings, phone calls, or conference calls regarding, among other things, the consummation and benefits of transactions and acquisitions, expectations with respect to future sales, financial performance, operating efficiencies, or product expansion, are subject to known and unknown risks, uncertainties, and contingencies, many of which are beyond the control of the Company. Various factors may cause actual results, performance, or achievements to differ materially from anticipated results, performance, or achievements expressed or implied by forward-looking statements. Factors that might affect forward-looking statements include, but are not limited to, overall economic and business conditions; economic and political conditions in international markets; the demand for the Company’s products; competitive factors in the industries and geographic markets in which the Company competes; federal, state and international tax requirements (including tax rate changes, new tax laws and revised tax law interpretations); interest rate and other capital market conditions, including changes in the market price of the Company’s securities; foreign currency exchange rate fluctuations; changes in technology; the timing, impact, and other uncertainties relating to transactions and acquisitions, divestitures and joint ventures as well as decisions the Company may make in the future regarding the Company’s business, capital and organizational structure and other matters; the seasonal and cyclical nature of the semiconductor and flat panel display industries; management changes; damage or destruction to the Company’s facilities, or the facilities of its customers or suppliers, by natural disasters, labor strikes, political unrest, or terrorist activity; the ability of the Company to (i) place new equipment in service on a timely basis; (ii) obtain additional financing; (iii) achieve anticipated synergies and cost savings; (iv) fully utilize its tools; (v) achieve desired yields, pricing, product mix, and market acceptance of its products and (vi) obtain necessary export licenses. Any forward-looking statements should be considered in light of these factors. Accordingly, there is no assurance that the Company’s expectations will be realized. The Company does not assume responsibility for the accuracy and completeness of the forward-looking statements and does not assume an obligation to provide revisions to any forward-looking statements, except as otherwise required by securities and other applicable laws.

PHOTRONICS, INC.
AND SUBSIDIARIES

INDEX

PART I.	FINANCIAL INFORMATION	Page
Item 1.	Condensed Consolidated Financial Statements	
	Condensed Consolidated Balance Sheets at July 31, 2016 and November 1, 2015	4
	Condensed Consolidated Statements of Income for the Three and Nine Months Ended July 31, 2016 and August 2, 2015	5
	Condensed Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended July 31, 2016 and August 2, 2015	6
	Condensed Consolidated Statements of Cash Flows for the Nine Months Ended July 31, 2016 and August 2, 2015	7
	Notes to Condensed Consolidated Financial Statements	8
Item 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations	19
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	25
Item 4.	Controls and Procedures	25
PART II.	OTHER INFORMATION	
Item 1A.	Risk Factors	26
Item 6.	Exhibits	27

PART I. FINANCIAL INFORMATION**Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****PHOTRONICS, INC. AND SUBSIDIARIES**

Condensed Consolidated Balance Sheets
(in thousands, except per share amounts)
(unaudited)

	<u>July 31, 2016</u>	<u>November 1, 2015</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 291,669	\$ 205,867
Accounts receivable, net of allowance of \$3,281 in 2016 and \$3,301 in 2015	107,494	110,056
Inventories	24,615	24,157
Other current assets	<u>17,643</u>	<u>24,034</u>
Total current assets	441,421	364,114
Property, plant and equipment, net	522,192	547,284
Investment in joint venture	-	93,021
Intangible assets, net	20,950	24,616
Deferred income taxes	11,961	11,908
Other assets	<u>3,919</u>	<u>4,612</u>
Total assets	<u>\$ 1,000,443</u>	<u>\$ 1,045,555</u>
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term borrowings	\$ 5,846	\$ 65,495
Accounts payable	62,987	87,983
Accrued liabilities	<u>28,223</u>	<u>39,214</u>
Total current liabilities	97,056	192,692
Long-term borrowings	63,054	67,120
Other liabilities	<u>20,952</u>	<u>23,677</u>
Total liabilities	181,062	283,489
Commitments and contingencies		
Equity:		
Preferred stock, \$0.01 par value, 2,000 shares authorized, none issued and outstanding	-	-
Common stock, \$0.01 par value, 150,000 shares authorized, 67,968 shares issued and outstanding at July 31, 2016 and 66,602 shares issued and outstanding at November 1, 2015	680	666
Additional paid-in capital	539,562	526,402
Retained earnings	171,004	130,060
Accumulated other comprehensive loss	<u>(4,936)</u>	<u>(10,573)</u>
Total Photronics, Inc. shareholders' equity	706,310	646,555
Noncontrolling interests	<u>113,071</u>	<u>115,511</u>
Total equity	<u>819,381</u>	<u>762,066</u>
Total liabilities and equity	<u>\$ 1,000,443</u>	<u>\$ 1,045,555</u>

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended		Nine Months Ended	
	July 31, 2016	August 2, 2015	July 31, 2016	August 2, 2015
Net sales	\$ 123,209	\$ 131,699	\$ 376,088	\$ 382,513
Costs and expenses:				
Cost of sales	(91,759)	(94,456)	(277,915)	(283,991)
Selling, general and administrative	(11,163)	(12,430)	(34,386)	(36,795)
Research and development	(5,466)	(6,253)	(16,613)	(16,743)
Operating income	14,821	18,560	47,174	44,984
Other income (expense):				
Gains on sales of investments	157	-	8,940	-
Interest expense	(612)	(1,209)	(2,750)	(3,812)
Interest and other income (expense), net	1,849	1,449	1,878	1,312
Income before income tax provision	16,215	18,800	55,242	42,484
Income tax provision	(4,762)	(3,390)	(6,136)	(7,775)
Net income	11,453	15,410	49,106	34,709
Net income attributable to noncontrolling interests	(3,365)	(3,304)	(8,162)	(8,706)
Net income attributable to Photronics, Inc. shareholders	<u>\$ 8,088</u>	<u>\$ 12,106</u>	<u>\$ 40,944</u>	<u>\$ 26,003</u>
Earnings per share:				
Basic	<u>\$ 0.12</u>	<u>\$ 0.18</u>	<u>\$ 0.61</u>	<u>\$ 0.39</u>
Diluted	<u>\$ 0.12</u>	<u>\$ 0.17</u>	<u>\$ 0.56</u>	<u>\$ 0.37</u>
Weighted-average number of common shares outstanding:				
Basic	<u>67,953</u>	<u>66,454</u>	<u>67,377</u>	<u>66,250</u>
Diluted	<u>74,317</u>	<u>78,569</u>	<u>76,990</u>	<u>78,300</u>

See accompanying notes to condensed consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income
(in thousands)
(unaudited)

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>July 31, 2016</u>	<u>August 2, 2015</u>	<u>July 31, 2016</u>	<u>August 2, 2015</u>
Net income	\$ 11,453	\$ 15,410	\$ 49,106	\$ 34,709
Other comprehensive income (loss), net of tax of \$0:				
Foreign currency translation adjustments	5,051	(25,326)	7,787	(32,894)
Amortization of cash flow hedge	<u>32</u>	<u>32</u>	<u>96</u>	<u>96</u>
Total other comprehensive income (loss)	<u>5,083</u>	<u>(25,294)</u>	<u>7,883</u>	<u>(32,798)</u>
Comprehensive income (loss)	16,536	(9,884)	56,989	1,911
Less: comprehensive income attributable to noncontrolling interests	<u>4,538</u>	<u>1,105</u>	<u>10,408</u>	<u>5,939</u>
Comprehensive income (loss) attributable to Photronics, Inc. shareholders	<u>\$ 11,998</u>	<u>\$ (10,989)</u>	<u>\$ 46,581</u>	<u>\$ (4,028)</u>

See accompanying notes to condensed consolidated financial statements.

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

	Nine Months Ended	
	July 31, 2016	August 2, 2015
Cash flows from operating activities:		
Net income	\$ 49,106	\$ 34,709
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	60,471	61,465
Gains on sales of investments	(8,940)	-
Changes in assets and liabilities:		
Accounts receivable	3,936	(13,744)
Inventories	(204)	(1,814)
Other current assets	9,177	1,496
Accounts payable, accrued liabilities and other	(22,159)	9,715
Net cash provided by operating activities	91,387	91,827
Cash flows from investing activities:		
Purchases of property, plant and equipment	(44,828)	(80,107)
Proceeds from sales of investments	101,853	-
Other	584	(283)
Net cash provided by (used in) investing activities	57,609	(80,390)
Cash flows from financing activities:		
Repayments of long-term borrowings	(56,276)	(7,152)
Proceeds from share-based arrangements	3,172	2,375
Dividends paid to noncontrolling interests	(11,890)	-
Other	(19)	(171)
Net cash used in financing activities	(65,013)	(4,948)
Effect of exchange rate changes on cash and cash equivalents	1,819	(7,856)
Net increase (decrease) in cash and cash equivalents	85,802	(1,367)
Cash and cash equivalents at beginning of period	205,867	192,929
Cash and cash equivalents at end of period	\$ 291,669	\$ 191,562
Supplemental disclosure of noncash information:		
Accrual for property, plant and equipment purchased during the period	\$ 7,169	\$ 40,632

See accompanying notes to condensed consolidated financial statements.

PHOTRONICS, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
Three Months and Nine Months Ended July 31, 2016 and August 2, 2015
(unaudited)
(in thousands, except share amounts)

NOTE 1 - BASIS OF FINANCIAL STATEMENT PRESENTATION

Photronics, Inc. and its subsidiaries (“Photronics” or “the Company”) is one of the world’s leading manufacturers of photomasks, which are high precision photographic quartz plates containing microscopic images of electronic circuits. Photomasks are a key element in the manufacture of semiconductors and flat panel displays (“FPDs”), and are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates during the fabrication of integrated circuits (“ICs”) and a variety of FPDs and, to a lesser extent, other types of electrical and optical components. The Company currently operates principally from nine manufacturing facilities, two of which are located in Europe, three in Taiwan, one in Korea, and three in the United States. In August 2016 the Company announced its plans to build a research and development and manufacturing facility in Xiamen, China, with construction commencing in 2017 and production estimated to start in late 2018. See Note 14 for additional information.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to 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 annual financial statements. In the opinion of management, adjustments, all of which are of a normal recurring nature, considered necessary for a fair presentation have been included. The Company is typically impacted during its first fiscal quarter by the North American and European holiday periods, as some customers reduce their effective workdays and orders during these periods. Additionally, the Company can be impacted during its first or second quarter by the Asian New Year holiday period, which may also reduce customer orders. Operating results for the interim period are not necessarily indicative of the results that may be expected for the fiscal year ending October 30, 2016. For further information, refer to the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended November 1, 2015.

NOTE 2 - CHANGES IN EQUITY

The following tables set forth the Company’s consolidated changes in equity for the three and nine month periods ended July 31, 2016 and August 2, 2015:

	Three Months Ended July 31, 2016							
	Photronics, Inc. Shareholders						Non- controlling Interests	Total Equity
	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss			
Shares	Amount							
Balance at May 1, 2016	67,943	\$ 679	\$ 538,535	\$ 162,916	\$ (8,846)	\$ 109,488	\$ 802,772	
Net income	-	-	-	8,088	-	3,365	11,453	
Other comprehensive income	-	-	-	-	3,910	1,173	5,083	
Sale of common stock through employee stock option and purchase plans	7	-	53	-	-	-	53	
Restricted stock awards vesting and expense	18	1	313	-	-	-	314	
Share-based compensation expense	-	-	661	-	-	-	661	
Return of capital to noncontrolling interests	-	-	-	-	-	(955)	(955)	
Balance at July 31, 2016	<u>67,968</u>	<u>\$ 680</u>	<u>\$ 539,562</u>	<u>\$ 171,004</u>	<u>\$ (4,936)</u>	<u>\$ 113,071</u>	<u>\$ 819,381</u>	

Three Months Ended August 2, 2015
Photronics, Inc. Shareholders

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Non- controlling Interests</u>	<u>Total Equity</u>
	<u>Shares</u>	<u>Amount</u>					
Balance at May 3, 2015	66,298	\$ 663	\$ 522,873	\$ 99,332	\$ 14,838	\$ 116,277	\$ 753,983
Net income	-	-	-	12,106	-	3,304	15,410
Other comprehensive loss	-	-	-	-	(23,094)	(2,200)	(25,294)
Sale of common stock through employee stock option and purchase plans	194	2	1,076	-	-	-	1,078
Restricted stock awards vesting and expense	15	-	268	-	-	-	268
Share-based compensation expense	-	-	680	-	-	-	680
Purchase of common stock of subsidiary	-	-	27	-	-	(105)	(78)
Balance at August 2, 2015	<u>66,507</u>	<u>\$ 665</u>	<u>\$ 524,924</u>	<u>\$ 111,438</u>	<u>\$ (8,256)</u>	<u>\$ 117,276</u>	<u>\$ 746,047</u>

Nine Months Ended July 31, 2016
Photronics, Inc. Shareholders

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Loss</u>	<u>Non- controlling Interests</u>	<u>Total Equity</u>
	<u>Shares</u>	<u>Amount</u>					
Balance at November 1, 2015	66,602	\$ 666	\$ 526,402	\$ 130,060	\$ (10,573)	\$ 115,511	\$ 762,066
Net income	-	-	-	40,944	-	8,162	49,106
Other comprehensive income	-	-	-	-	5,637	2,246	7,883
Sale of common stock through employee stock option and purchase plans	521	5	2,890	-	-	-	2,895
Restricted stock awards vesting and expense	128	2	876	-	-	-	878
Share-based compensation expense	-	-	1,971	-	-	-	1,971
Conversion of debt to common stock	717	7	7,431	-	-	-	7,438
Repurchase of common stock of subsidiary	-	-	(8)	-	-	8	-
Subsidiary dividend	-	-	-	-	-	(11,901)	(11,901)
Return of capital to noncontrolling interests	-	-	-	-	-	(955)	(955)
Balance at July 31, 2016	<u>67,968</u>	<u>\$ 680</u>	<u>\$ 539,562</u>	<u>\$ 171,004</u>	<u>\$ (4,936)</u>	<u>\$ 113,071</u>	<u>\$ 819,381</u>

Nine Months Ended August 2, 2015
Photronics, Inc. Shareholders

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non- controlling Interests	Total Equity
	Shares	Amount					
Balance at November 2, 2014	65,930	\$ 659	\$ 520,183	\$ 85,435	\$ 21,774	\$ 111,443	\$ 739,494
Net income	-	-	-	26,003	-	8,706	34,709
Other comprehensive loss	-	-	-	-	(30,030)	(2,768)	(32,798)
Sale of common stock through employee stock option and purchase plans	433	4	1,932	-	-	-	1,936
Restricted stock awards vesting and expense	144	2	800	-	-	-	802
Share-based compensation expense	-	-	1,982	-	-	-	1,982
Purchase of common stock of subsidiary	-	-	27	-	-	(105)	(78)
Balance at August 2, 2015	<u>66,507</u>	<u>\$ 665</u>	<u>\$ 524,924</u>	<u>\$ 111,438</u>	<u>\$ (8,256)</u>	<u>\$ 117,276</u>	<u>\$ 746,047</u>

NOTE 3 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following:

	July 31, 2016	November 1, 2015
Land	\$ 8,096	\$ 8,172
Buildings and improvements	122,077	121,472
Machinery and equipment	1,481,252	1,458,623
Leasehold improvements	19,079	18,856
Furniture, fixtures and office equipment	12,879	12,700
Construction in progress	18,903	6,657
	<u>1,662,286</u>	<u>1,626,480</u>
Less accumulated depreciation and amortization	<u>1,140,094</u>	<u>1,079,196</u>
	<u>\$ 522,192</u>	<u>\$ 547,284</u>

Equipment under capital leases are included in above property, plant and equipment as follows:

	July 31, 2016	November 1, 2015
Machinery and equipment	\$ 34,917	\$ 56,245
Less accumulated amortization	<u>9,479</u>	<u>16,054</u>
	<u>\$ 25,438</u>	<u>\$ 40,191</u>

Depreciation and amortization expense for property, plant and equipment was \$ 18.4 million and \$56.4 million for the three and nine month periods ended July 31, 2016, respectively, and \$19.4 million and \$56.4 million for the three and nine month periods ended August 2, 2015, respectively.

NOTE 4 - JOINT VENTURE, TECHNOLOGY LICENSE AND OTHER AGREEMENTS WITH MICRON TECHNOLOGY, INC.

In May 2006, Photronics and Micron Technology, Inc. (“Micron”) entered into the MP Mask joint venture (“MP Mask”), which developed and produced photomasks for leading-edge and advanced next generation semiconductors. At the time of the formation of the joint venture, the Company also entered into both an agreement to license photomask technology developed by Micron and certain supply agreements.

This joint venture was a variable interest entity (“VIE”) (as that term is defined in the ASC) because all costs of the joint venture were passed on to the Company and Micron through purchase agreements they had entered into with the joint venture, and it was dependent upon the Company and Micron for any additional cash requirements. On a quarterly basis the Company reassessed whether its interest in MP Mask gave it a controlling financial interest in this VIE. The purpose of this quarterly reassessment was to identify the primary beneficiary (which is defined in the ASC as the entity that consolidates a VIE) of the VIE. As a result of the reassessment in the current quarter, the Company determined that Micron was still the primary beneficiary of the VIE, by virtue of its tie-breaking voting rights within MP Mask’s Board of Managers, thereby having given it the power to direct the activities of MP Mask that most significantly impacted its economic performance, including its decision making authority in the ordinary course of business and its purchasing the majority of products produced by the VIE.

The Company utilized MP Mask for both high-end IC photomask production and research and development purposes. MP Mask charged its variable interest holders based on their actual usage of its facility. MP Mask separately charged for any research and development activities it engaged in at the requests of its owners. The Company incurred cost of sales from MP Mask of \$0.8 and \$5.7 million in the three month and nine month periods ended July 31, 2016, respectively, and \$1.5 million and \$4.9 million during the respective prior year periods. The Company incurred research and development costs from MP Mask of \$0.2 million during the three month period ended August 2, 2015, and \$0.5 million and \$0.7 million during the nine month periods ended July 31, 2016 and August 2, 2015, respectively. At November 1, 2015, the Company owed MP Mask \$4.3 million and had a receivable from Micron of \$6.4 million, both primarily related to the aforementioned supply agreements.

MP Mask was governed by a Board of Managers, appointed by Micron and the Company. Since MP Mask’s inception, Micron, as a result of its majority ownership, had held majority voting power on its Board of Managers. The voting power held by each party was subject to change as ownership interests changed. Under the MP Mask joint venture operating agreement, the Company may have been required to make additional capital contributions to MP Mask up to the maximum amount defined in the operating agreement. However, had the Board of Managers determined that further additional funding was required, MP Mask would have pursued its own financing. If MP Mask was unable to obtain its own financing, it may have requested additional capital contributions from the Company. Had the Company chosen not to make a requested contribution to MP Mask, its ownership percentage may have been reduced.

The Company’s investment in the VIE, which represented its maximum exposure to loss, was \$93.0 million at November 1, 2015. This amount is reported in the Company’s condensed consolidated balance sheets as “Investment in joint venture.” The Company recorded losses from its investment in the VIE of \$0.1 million in the nine month periods ended July 31, 2016 and August 2, 2015.

On May 5, 2016, the Company sold its investment in MP Mask to Micron for \$93.1 million and recorded a gain on the sale of \$0.2 million, which is included in the Company’s 2016 condensed consolidated statement of income in Interest and other income (expense) net. On that same date a supply agreement commenced between the Company and Micron, which provides that the Company will be the majority outsourced supplier of Micron’s photomasks and related services. The supply agreement has a one year term, subject to mutually agreeable renewals. In addition, the Company forevermore has the rights to use technology under the prior technology license agreement.

NOTE 5 - LONG-TERM BORROWINGS

Long-term borrowings consist of the following:

	<u>July 31, 2016</u>	<u>November 1, 2015</u>
3.25% convertible senior notes due in April 2019	\$ 57,500	\$ 57,500
3.25% convertible senior notes due in April 2016	-	57,500
2.77% capital lease obligation payable through July 2018	11,400	15,346
3.09% capital lease obligation payable through March 2016	-	2,269
	<u>68,900</u>	<u>132,615</u>
Less current portion	<u>5,846</u>	<u>65,495</u>
	<u>\$ 63,054</u>	<u>\$ 67,120</u>

In April 2016 \$57.5 million of the Company's senior convertible notes matured. The Company repaid \$50.1 million to noteholders and issued approximately 0.7 million shares to noteholders that elected to convert their notes to common stock. The notes were exchanged at the rate of approximately 96 shares per \$1,000 note principal, equivalent to a conversion rate of \$10.37 per share.

In January 2015 the Company privately exchanged \$57.5 million in aggregate principal amount of its 3.25% convertible senior notes with a maturity date of April 1, 2016, for new 3.25% convertible senior notes with an aggregate principal amount of \$57.5 million with a maturity date of April 1, 2019. The conversion rate of the new notes is the same as that of the exchanged notes, which were issued in March 2011 with a conversion rate of approximately 96 shares of common stock per \$1,000 note principal, equivalent to a conversion price of \$10.37 per share of common stock, and is subject to adjustment upon the occurrence of certain events, which are described in the indenture dated January 22, 2015. Noteholders may convert each \$1,000 principal amount of notes at any time prior to the close of business on the second scheduled trading day immediately preceding April 1, 2019, and the Company is not required to redeem the notes prior to their maturity date. Interest on the notes accrues in arrears, and is paid semiannually through the notes' maturity date.

The Company's credit facility, which expires in December 2018, has a \$50 million limit with an expansion capacity to \$75 million, and is secured by substantially all of the Company's assets located in the United States and common stock the Company owns in certain of its foreign subsidiaries. The credit facility precludes the Company from paying cash dividends, and is subject to a minimum interest coverage ratio, total leverage ratio and minimum unrestricted cash balance financial covenants, all of which the Company was in compliance with at July 31, 2016. The Company had no outstanding borrowings against the credit facility at July 31, 2016, and \$50 million was available for borrowing. The interest rate on the credit facility (1.73% at July 31, 2016) is based on the Company's total leverage ratio at LIBOR plus a spread, as defined in the credit facility.

In August 2013 a \$26.4 million principal amount, five year capital lease commenced to fund the purchase of a high-end lithography tool. Payments under the capital lease, which bears interest at 2.77%, are \$0.5 million per month through July 2018. Under the terms of the lease agreement, the Company must maintain the equipment in good working order, and is subject to a cross default with cross acceleration provision related to certain nonfinancial covenants incorporated in its credit facility. As of July 31, 2016, the total amount payable through the end of the lease term was \$11.7 million, of which \$11.4 million represented principal and \$0.3 million represented interest.

In April 2011 the Company entered into a five year, \$21.2 million capital lease for manufacturing equipment. Payments under the lease, which bore interest at 3.09%, were \$0.4 million per month through March 2016. The lease agreement provided that the Company must maintain the equipment in good working order, and included a cross default with cross acceleration provision related to certain non-financial covenants incorporated in the Company's credit facility agreement. In March 2016 the Company paid the final installment on this lease and assumed ownership of the related equipment.

NOTE 6 - SHARE-BASED COMPENSATION

In March 2016 shareholders approved a new equity incentive compensation plan (“the Plan”), under which incentive stock options, non-qualified stock options, stock grants, stock-based awards, restricted stock, restricted stock units, stock appreciation rights, performance units, performance stock and other stock or cash awards may be granted. Shares to be issued under the Plan may be authorized and unissued shares, issued shares that have been reacquired by the Company (in the open-market or in private transactions) and that are being held in treasury, or a combination thereof. The maximum number of shares of common stock approved that may be issued under the Plan is four million shares. Awards may be granted to officers, employees, directors, consultants, advisors, and independent contractors of the Company or its subsidiaries. In the event of a change in control (as defined in the Plan), the vesting of awards may be accelerated. The Plan, aspects of which are more fully described below, prohibits further awards from being issued under prior plans. Total share-based compensation costs for the three and nine month periods ended July 31, 2016, were \$1.0 million and \$2.8 million, respectively, and \$0.9 million and \$2.8 million for the three and nine month periods ended August 2, 2015, respectively. The Company received cash from option exercises of \$0.1 million and \$2.9 million for the three and nine month periods ended July 31, 2016, respectively, and \$1.1 million and \$2.1 million for the three and nine month periods ended August 2, 2015, respectively. No share-based compensation cost was capitalized as part of an asset and no related income tax benefits were recorded during the periods presented.

Stock Options

Option awards generally vest in one to four years, and have a ten-year contractual term. All incentive and non-qualified stock option grants have an exercise price equal to the market value of the underlying common stock on the date of grant. The grant date fair values of options are based on closing prices of the Company’s common stock on the dates of grant using the Black-Scholes option pricing model. Expected volatility is based on the historical volatility of the Company’s stock. The Company uses historical option exercise behavior and employee termination data to estimate expected term, which represents the period of time that the options granted are expected to remain outstanding. The risk-free rate of return for the estimated term of the option is based on the U.S. Treasury yield curve in effect at the date of grant.

The weighted-average inputs and risk-free rate of return ranges used to calculate the grant date fair value of options issued during the three and nine month periods ended July 31, 2016 and August 2, 2015, are presented in the following table.

	Three Months Ended		Nine Months Ended	
	July 31, 2016	August 2, 2015	July 31, 2016	August 2, 2015
Volatility	38.9%	42.9%	48.8%	53.9%
Risk free rate of return	1.2%	1.4% – 1.6%	1.2%-1.7%	1.3% - 1.6%
Dividend yield	0.0%	0.0%	0.0%	0.0%
Expected term	5.1 years	4.7 years	5.1 years	4.7 years

Information on outstanding and exercisable option awards as of July 31, 2016, is presented below.

Options	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding at July 31, 2016	3,575,610	\$ 7.52	6.5 years	\$ 9,210
Exercisable at July 31, 2016	2,027,160	\$ 5.87	5.0 years	\$ 7,807

There were 45,000 share options granted during the three month period ended July 31, 2016, with a weighted-average grant date fair value of \$3.44 per share and 63,000 share options granted during the three month period ended August 2, 2015, with a weighted-average grant date fair value of \$3.46 per share. There were 647,250 share options granted during the nine month period ended July 31, 2016, with a weighted-average grant date fair value of \$4.55 per share and 667,800 share options granted during the nine month period ended August 2, 2015, with a weighted-average grant date fair value of \$3.82 per share. As of July 31, 2016, the total unrecognized compensation cost related to unvested option awards was approximately \$4.8 million. That cost is expected to be recognized over a weighted-average amortization period of 2.6 years.

Restricted Stock

The Company periodically grants restricted stock awards. The restrictions on these awards lapse over a service period that has ranged from less-than-one to four years. No restricted stock awards were granted during the three month period ended July 31, 2016, and 115,225 restricted stock awards were issued during the nine month period ended July 31, 2016, with a weighted average grant date fair value of \$12.13 per share. Awards totaling 10,000 shares of restricted stock were granted during the three month period ended August 2, 2015, with a weighted-average grant date fair value of \$8.84 per share, and 121,334 restricted stock awards were issued during the nine month period ended August 2, 2015, with a weighted-average grant date fair value of \$8.28 per share. As of July 31, 2016, the total compensation cost not yet recognized related to unvested restricted stock awards was approximately \$1.3 million. That cost is expected to be recognized over a weighted-average amortization period of 2.1 years. As of July 31, 2016, there were 177,375 shares of restricted stock outstanding.

NOTE 7 - INCOME TAXES

The effective tax rate differs from the U.S. statutory rate of 35% in the three and nine month periods ended July 31, 2016 and August 2, 2015, primarily due to earnings being taxed at lower statutory rates in foreign jurisdictions, combined with the realization of certain tax benefits (as further noted below) in a foreign jurisdiction and the benefit of various investment credits in a foreign jurisdiction. Valuation allowances in jurisdictions with historic losses eliminated the effective rate impact of these jurisdictions.

As of July 31, 2016 and August 2, 2015, the Company determined that deferred tax assets of \$2.5 million and \$1.7 million, respectively, including \$0.2 million within the three month period ended August 2, 2015, whose realization was previously not considered to be more likely than not, are realizable and, therefore, reduced their related valuation allowances. During the nine month period ended July 31, 2016, the Company realized a \$2.4 million benefit, which resulted from the reversal of a previously recorded undistributed earnings tax liability in a foreign jurisdiction. As a result of a shareholder action to approve a dividend in this jurisdiction, the Company determined that it is no longer liable for this tax. In addition, during the nine month period ended July 31, 2016, \$0.7 million of withholding tax was incurred upon the completion of a foreign subsidiary share redemption which commenced in fiscal year 2015.

Unrecognized tax benefits related to uncertain tax positions were \$4.8 million at July 31, 2016, and \$4.1 million at November 1, 2015, all of which would favorably impact the Company's effective tax rate if recognized. Accrued interest and penalties related to unrecognized tax benefits was \$0.1 million at July 31, 2016 and November 1, 2015. As of July 31, 2016, the total amount of unrecognized tax benefits is not expected to significantly increase or decrease in the next twelve months.

PKLT, the Company's FPD manufacturing facility in Taiwan, has been accorded a tax holiday, which started in 2012 and expires in 2017. This tax holiday had no dollar or per share effect in the three and nine month periods ended July 31, 2016 and August 2, 2015. PDMC, the Company's IC manufacturing facility in Taiwan was accorded a tax holiday that commenced in 2015 and expires in 2019. The Company realized tax benefits from this tax holiday of \$0.1 million in the three month periods ended July 31, 2016 and August 2, 2015, and \$0.3 million and \$0.2 million in the respective nine month periods. The tax holiday had no per share effect in the three and nine month periods ended July 31, 2016 and August 2, 2015.

NOTE 8 - EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is presented below.

	Three Months Ended		Nine Months Ended	
	July 31, 2016	August 2, 2015	July 31, 2016	August 2, 2015
Net income attributable to Photonics, Inc. shareholders	\$ 8,088	\$ 12,106	\$ 40,944	\$ 26,003
Effect of dilutive securities:				
Interest expense on convertible notes, net of related tax effects	496	1,071	2,442	3,292
Earnings for diluted earnings per share	\$ 8,584	\$ 13,177	\$ 43,386	\$ 29,295
Weighted-average common shares computations:				
Weighted-average common shares used for basic earnings per share	67,953	66,454	67,377	66,250
Effect of dilutive securities:				
Convertible notes	5,542	11,085	8,607	11,085
Share-based payment awards	822	1,030	1,006	965
Potentially dilutive common shares	6,364	12,115	9,613	12,050
Weighted-average common shares used for diluted earnings per share	74,317	78,569	76,990	78,300
Basic earnings per share	\$ 0.12	\$ 0.18	\$ 0.61	\$ 0.39
Diluted earnings per share	\$ 0.12	\$ 0.17	\$ 0.56	\$ 0.37

The table below shows the outstanding weighted-average share-based payment awards that were excluded from the calculation of diluted earnings per share because their exercise price exceeded the average market value of the common shares for the period.

	Three Months Ended		Nine Months Ended	
	July 31, 2016	August 2, 2015	July 31, 2016	August 2, 2015
Share-based payment awards	2,016	1,667	1,615	1,636
Total potentially dilutive shares excluded	2,016	1,667	1,615	1,636

NOTE 9 - CHANGES IN ACCUMULATED OTHER COMPREHENSIVE INCOME BY COMPONENT

The following tables set forth the changes in the Company's accumulated other comprehensive income by component (net of tax of \$0) for the three and nine month periods ended July 31, 2016 and August 2, 2015:

	Three Months Ended July 31, 2016			
	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at May 1, 2016	\$ (7,966)	\$ (242)	\$ (638)	\$ (8,846)
Other comprehensive income (loss) before reclassifications	5,064	-	(13)	5,051
Amounts reclassified from other comprehensive income	-	32	-	32
Net current period other comprehensive income (loss)	5,064	32	(13)	5,083
Less: other comprehensive (income) loss attributable to noncontrolling interests	(1,180)	-	7	(1,173)
Balance at July 31, 2016	<u>\$ (4,082)</u>	<u>\$ (210)</u>	<u>\$ (644)</u>	<u>\$ (4,936)</u>

	Three Months Ended August 2, 2015			
	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at May 3, 2015	\$ 15,648	\$ (370)	\$ (440)	\$ 14,838
Other comprehensive income (loss) before reclassifications	(25,342)	-	16	(25,326)
Amounts reclassified from other comprehensive income	-	32	-	32
Net current period other comprehensive income (loss)	(25,342)	32	16	(25,294)
Less: other comprehensive income (loss) attributable to noncontrolling interests	2,208	-	(8)	2,200
Balance at August 2, 2015	<u>\$ (7,486)</u>	<u>\$ (338)</u>	<u>\$ (432)</u>	<u>\$ (8,256)</u>

Nine Months Ended July 31, 2016

	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at November 1, 2015	\$ (9,634)	\$ (306)	\$ (633)	\$ (10,573)
Other comprehensive income (loss) before reclassifications	7,810	-	(23)	7,787
Amounts reclassified from other comprehensive income	-	96	-	96
Net current period other comprehensive income (loss)	7,810	96	(23)	7,883
Less: other comprehensive (income) loss attributable to noncontrolling interests	(2,258)	-	12	(2,246)
Balance at July 31, 2016	<u>\$ (4,082)</u>	<u>\$ (210)</u>	<u>\$ (644)</u>	<u>\$ (4,936)</u>

Nine Months Ended August 2, 2015

	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at November 2, 2014	\$ 22,651	\$ (434)	\$ (443)	\$ 21,774
Other comprehensive income (loss) before reclassifications	(32,915)	-	21	(32,894)
Amounts reclassified from other comprehensive income	-	96	-	96
Net current period other comprehensive income (loss)	(32,915)	96	21	(32,798)
Less: other comprehensive income (loss) attributable to noncontrolling interests	2,778	-	(10)	2,768
Balance at August 2, 2015	<u>\$ (7,486)</u>	<u>\$ (338)</u>	<u>\$ (432)</u>	<u>\$ (8,256)</u>

The amortization of the cash flow hedge is included in cost of sales in the condensed consolidated statements of income for all periods presented.

NOTE 10 - FAIR VALUE MEASUREMENTS

The accounting framework for determining fair value includes a hierarchy for ranking the quality and reliability of the information used to measure fair value, which enables the reader of the financial statements to assess the inputs used to develop those measurements. The fair value hierarchy consists of three tiers as follows: Level 1, defined as quoted prices (unadjusted) in active markets for identical securities; Level 2, defined as inputs other than Level 1 that are observable, either directly or indirectly; and Level 3, defined as unobservable inputs that are not corroborated by market data.

The Company did not have any assets or liabilities measured at fair value on a recurring or a nonrecurring basis at July 31, 2016 or November 1, 2015.

Fair Value of Other Financial Instruments

The fair values of the Company's cash and cash equivalents (Level 1 measurements), accounts receivable, accounts payable, and certain other current assets and current liabilities (Level 2 measurements) approximate their carrying value due to their short-term maturities. The fair value of the Company's convertible senior notes is a Level 2 measurement that is determined using recent bid prices.

The table below presents the fair and carrying values of the Company's convertible senior notes at July 31, 2016 and November 1, 2015.

	July 31, 2016		November 1, 2015	
	Fair Value	Carrying Value	Fair Value	Carrying Value
3.25% convertible senior notes due 2019	\$ 67,701	\$ 57,500	\$ 64,550	\$ 57,500
3.25% convertible senior notes due 2016	\$ -	\$ -	\$ 60,375	\$ 57,500

NOTE 11 - COMMITMENTS AND CONTINGENCIES

As of July 31, 2016, the Company had commitments outstanding for capital expenditures of approximately \$51 million.

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

Please see Note 14 for a discussion of the Company's announced expansion into China.

NOTE 12 – GAINS ON SALES OF INVESTMENTS

In the first quarter of fiscal 2016 the Company sold a minority interest it held in a foreign entity, which resulted in it recognizing a gain of \$8.8 million. As discussed in Note 4, in the third quarter of fiscal year 2016 we sold our investment in the MP Mask joint venture.

NOTE 13 – SUBSIDIARY DIVIDEND

In June 2016 PDMC, the Company's majority owned IC facility in Taiwan, paid a dividend of which 49.99%, or approximately \$11.9 million, was paid to its noncontrolling interest.

NOTE 14 – EXPANSION INTO CHINA

In August 2016 the Company announced that it had signed an investment agreement with the Xiamen Torch Hi-Tech Industrial Development Zone (Xiamen Torch) to establish an IC manufacturing facility in Xiamen, China. Under the terms of the agreement the Company will build and operate a state-of-the-art IC manufacturing and research and development facility, in return for which Xiamen Torch will provide certain investment incentives and support.

The Company plans to invest \$160 million over the next five years, with construction commencing in 2017 and production estimated to start in late 2018. The investment will be in the form of cash, transferred capital equipment and, possibly, local financing. Support for the project has been obtained from an existing customer.

NOTE 15 - RECENT ACCOUNTING PRONOUNCEMENTS

In March 2016 the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016 – 09 "Improvements to Employee Share-Based Payment Accounting", which simplifies the accounting for share-based payment transactions including their income tax consequences, classification as either equity or liability awards, classification on the statement of cash flows, and other areas. The method of adoption varies with the different aspects of the Update. The Update is effective for the Company in its first quarter of fiscal year 2018, with early application permitted. The Company is currently evaluating the effect this ASU will have on its consolidated financial statements.

In February 2016 the FASB issued ASU 2016 – 02 "Leases (Topic 842)", which requires lessees to recognize right-of-use assets and corresponding liabilities for all leases with an initial term in excess of twelve months. The Update is to be adopted using a modified retrospective approach, which includes a number of practical expedients, that require leases to be measured and recognized under the new guidance at the beginning of the earliest period presented. The ASU is effective for the Company in its first quarter of fiscal year 2020, with early application permitted, and the Company is currently evaluating the effect this ASU will have on its consolidated financial statements.

In January 2016 the FASB issued ASU 2016-01 “Recognition and Measurement of Financial Assets and Financial Liabilities”, which provides targeted improvements to the recognition, measurement, presentation and disclosure of financial assets and financial liabilities. Specific accounting areas addressed include, equity investments, financial liabilities reported under the fair value option and valuation allowance assessment resulting from unrealized losses on available-for-sale securities. The ASU also changes certain presentation and disclosure requirements for financial instruments. The Update is to be applied by means of a cumulative effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. This ASU is effective for the Company in its first quarter of fiscal year 2019. Early adoption, with certain exceptions, is not permitted. The Company is currently evaluating the effect this ASU will have on its consolidated financial statements.

In November 2015 the FASB issued ASU 2015-17 “Balance Sheet Classification of Deferred Taxes”, which requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. This ASU is effective for the Company in its first quarter of fiscal year 2018, with early application permitted and, upon adoption, may be applied either prospectively or retrospectively. The Company is currently evaluating the effect this ASU will have on its consolidated financial statements.

In April 2015 the FASB issued ASU 2015-03 “Simplifying the Presentation of Debt Issuance Costs”, which requires debt issuance costs related to recognized debt liability to be presented in the balance sheet as a direct deduction from that debt liability, consistent with the presentation of a debt discount. This ASU is effective for the Company in its first quarter of fiscal year 2017 and, upon adoption, should be applied retrospectively. Early adoption is permitted. The Company is currently evaluating the effect this ASU will have on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09 “Revenue from Contracts with Customers”, which will supersede nearly all existing revenue recognition guidance under accounting principles generally accepted in the United States. The core principle of this ASU is that revenue should be recognized for the amount of consideration expected to be received for promised goods or services transferred to customers. This ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments, and assets recognized for costs incurred to obtain or fulfill a contract. In August 2015 the FASB issued ASU 2015-14 which defers the effective date of ASU 2014-09 by one year and allows entities to early adopt, but no earlier than the original effective date. ASU 2014-09 will now be effective for the Company in its first quarter of fiscal year 2019. ASU 2014-09 allows for either full retrospective or modified retrospective adoption. In April 2016 the FASB issued ASU 2016-10 “Identifying Performance Obligations and Licensing” which amends guidance previously issued on these matters in ASU 2014-09. The effective date and transition requirements of ASU 2016-10 are the same as those for ASU 2014-09. The Company is evaluating the transition method that will be elected and the potential effects of the adoption of these Updates on its consolidated financial statements.

Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Management’s discussion and analysis (“MD&A”) of the Company’s financial condition, results of operations and outlook should be read in conjunction with its condensed consolidated financial statements and related notes. Various segments of this MD&A contain forward-looking statements, all of which are presented based on current expectations and may be adversely affected by uncertainties and risk factors (presented throughout this filing and in the Company’s Annual Report on Form 10-K for the fiscal 2015 year), that may cause actual results to materially differ from these expectations.

In August 2016 the Company announced that it had signed an investment agreement with the Xiamen Torch Hi-Tech Industrial Development Zone (Xiamen Torch) to establish an IC manufacturing facility in Xiamen, China. Under the terms of the agreement the Company will build and operate a state-of-the-art IC manufacturing and research and development facility, in return for which Xiamen Torch will provide certain investment incentives and support.

The Company plans to invest \$160 million over the next five years, with construction commencing in 2017 and production estimated to start in late 2018. The investment will be in the form of cash, transferred capital equipment and, possibly, local financing. Support for the project has been obtained from an existing customer.

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

The global semiconductor industry, including mobile displays, is driven by end markets which have been closely tied to consumer driven applications of high performance semiconductor devices including, but not limited to, mobile communications and computing solutions. The Company is typically required to fulfill its customer orders within a short period of time, sometimes within 24 hours. This results in the Company having a minimal level of backlog orders, typically one to two weeks for IC photomasks and two to three weeks for FPD photomasks. The Company cannot predict the timing of the industry's transition to volume production of next generation technology nodes or the timing of up and down cycles with precise accuracy, but believes that such transitions and cycles will continue into the future, beneficially and adversely affecting its business, financial condition and operating results in the near term. The Company believes its ability to remain successful in these environments is dependent upon achieving its goals of being a service and technology leader and efficient solutions supplier, which it believes should enable it to continually reinvest in its global infrastructure.

Material Changes in Results of Operations Three and Nine Months ended July 31, 2016 and August 2, 2015

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

	Three Months Ended		Nine Months Ended	
	July 31, 2016	August 2, 2015	July 31, 2016	August 2, 2015
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	(74.5)	(71.7)	(73.9)	(74.2)
Gross margin	25.5	28.3	26.1	25.8
Selling, general and administrative expenses	(9.1)	(9.4)	(9.1)	(9.6)
Research and development expenses	(4.4)	(4.8)	(4.5)	(4.4)
Operating income	12.0	14.1	12.5	11.8
Gains on sales of investments	0.2	-	2.4	-
Other income (expense), net	1.0	0.2	(0.2)	(0.7)
Income before income tax provision	13.2	14.3	14.7	11.1
Income tax provision	(3.9)	(2.6)	(1.6)	(2.0)
Net income	9.3	11.7	13.1	9.1
Net income attributable to noncontrolling interests	(2.7)	(2.5)	(2.2)	(2.3)
Net income attributable to Photronics, Inc. shareholders	6.6%	9.2%	10.9%	6.8%

Note: All of the following tabular comparisons, unless otherwise indicated, are for the three months ended July 31, 2016 (Q3-16) and August 2, 2015 (Q3-15) and for the nine months ended July 31, 2016 (YTD-16) and August 2, 2015 (YTD-15), in millions of dollars.

Net Sales

	Three Months Ended			Nine Months Ended		
	Q3-16	Q3-15	Percent Change	YTD-16	YTD-15	Percent Change
IC	\$ 91.7	\$ 104.0	(11.9)%	\$ 282.3	\$ 309.3	(8.7)%
FPD	31.5	27.7	13.9%	93.8	73.2	28.1%
Total net sales	\$ 123.2	\$ 131.7	(6.4)%	\$ 376.1	\$ 382.5	(1.7)%

Net sales for Q3-16 decreased 6.4% to \$123.2 million as compared to \$131.7 million for Q3-15. The decrease was primarily a result of reduced demand for both high-end and mainstream IC photomasks, which was partially offset by increased demand for FPD photomasks, including high-end. Revenues attributable to high-end products decreased by \$3.7 million to \$53.3 million in Q3-16 as compared to \$57.0 million in Q3-15. High-end photomask applications include mask sets for 45 nanometer and below for IC products, and G8 and above and active matrix organic light-emitting diode (AMOLED) display screen technologies for FPD products. By geographic area, net sales in Q3-16, as compared to Q3-15, increased (decreased) by \$1.4 million or 2.8% to \$52.0 million in Taiwan, \$(9.1) million or (26.9)%, to \$24.7 million in the United States, and \$(0.8) million or (8.3)% to \$8.4 million in Europe. Net sales in Korea in Q3-16 were \$37.6 million, unchanged from Q3-15.

Net sales for YTD-16 decreased to \$376.1 million as compared with \$382.5 million for YTD-15, as a result of lower high-end and mainstream IC revenues, partially offset by strong high-end FPD revenues. Revenues attributable to high-end products increased by \$11.1 million to \$176.5 million in YTD-16 as compared to \$165.4 million in YTD-15 primarily due to increased advanced display FPD revenues offset by decreased demand for high-end IC photomasks.

The Company's quarterly revenues can be affected by the seasonal purchasing of its customers. Demand for the Company's products is typically negatively impacted during the first six months of its fiscal year by the North American, European and Asian holiday periods, as some customers reduce their effective workdays and orders during this period.

Gross Margin

	Three Months Ended			Nine Months Ended		
	Q3-16	Q3-15	Percent Change	YTD-16	YTD-15	Percent Change
Gross margin	\$ 31.5	\$ 37.2	(15.6)%	\$ 98.2	\$ 98.5	(0.4)%
Percentage of net sales	25.5%	28.3%		26.1%	25.8%	

Gross margin percentage decreased to 25.5% in Q3-16 from 28.3% in Q3-15, primarily due to lower demand for IC products. YTD-16 gross margin percentage increased to 26.1% from 25.8% in YTD-15, primarily due to improved manufacturing efficiencies and cost reductions. The Company operates in a high fixed cost environment and, to the extent that the Company's revenues and utilization increase or decrease, gross margin will generally be positively or negatively impacted.

Selling, General and Administrative Expenses

	Three Months Ended			Nine Months Ended		
	Q3-16	Q3-15	Percent Change	YTD-16	YTD-15	Percent Change
Selling, general and administrative expenses	\$ 11.2	\$ 12.4	(10.2)%	\$ 34.4	\$ 36.8	(6.5)%
Percentage of net sales	9.1%	9.4%		9.1%	9.6%	

Selling, general and administrative expenses were \$11.2 million in Q3-16 and \$12.4 million in Q3-15, and were \$34.4 million in YTD-16 and \$36.8 million in YTD-15. These decreases were primarily the result of reduced costs, including freight and other items.

Research and Development

	Three Months Ended			Nine Months Ended		
	Q3-16	Q3-15	Percent Change	YTD-16	YTD-15	Percent Change
Research and development	\$ 5.5	\$ 6.3	(12.6)%	\$ 16.6	\$ 16.7	(0.8)%
Percentage of net sales	4.4%	4.8%		4.5%	4.4%	

Research and development expenses consist primarily of global development efforts related to high-end process technologies for advanced sub-wavelength reticle solutions for IC technologies. Research and development expenses decreased by \$0.8 million to \$5.5 million in Q3-16, as compared to \$6.3 million in Q3-15 due to decreased advanced nanometer technology development activities in the Asian region. YTD-16 research and development expenses did not significantly change from YTD-15.

Other Income (Expense), net

	Three Months Ended		Nine Months Ended	
	Q3-16	Q3-15	YTD-16	YTD-15
Gains on sales of investments	\$ 0.2	\$ -	\$ 8.9	\$ -
Interest expense	(0.6)	(1.2)	(2.7)	(3.8)
Interest and other income (expense), net	1.8	1.4	1.9	1.3
Other income (expense), net	\$ 1.4	\$ 0.2	\$ 8.1	\$ (2.5)

In January 2016 the Company sold a minority interest investment in a foreign entity and recognized a gain of \$8.8 million. In May the Company sold its 49.99% interest in the MP Mask joint venture and recognized a gain of \$0.2 million.

Interest expense decreased by \$0.6 million in Q3-16, as compared to Q3-15, and by \$1.1 million in YTD-16, as compared to YTD-15, primarily as a result of the impact of the 3.25% convertible debt that matured on April 1, 2016.

Interest and other income (expense), net increased in Q3-16 as compared to Q3-15 by \$0.4 million primarily due to the favorable settlement of a liability related to a prior year's acquisition, which was partially offset by less favorable foreign currency exchange gains. Interest and other income (expense), net increased in FY-16 from FY-15, primarily as the result of the aforementioned settlement of the liability related to a prior year's acquisition.

Income Tax (Benefit) Provision

	Three Months Ended		Nine Months Ended	
	Q3-16	Q3-15	YTD-16	YTD-15
Income tax provision	\$ 4.8	\$ 3.4	\$ 6.1	\$ 7.8
Effective income tax rate	29.4%	18.0%	11.1%	18.3%

The Company's effective income tax rate is sensitive to the jurisdictional mix of earnings, due in part to the non-recognition of tax benefits on losses in jurisdictions with valuation allowances.

The effective income tax rate increase in Q3-16, as compared with Q3-15, was primarily attributable to a greater percentage of income before income taxes being earned in jurisdictions where the Company does not maintain valuation allowances and, therefore recognizes a tax expense. The effective income tax rate decrease in YTD-16, as compared with YTD-15, is primarily a result of the following factors: the recognition in FY-16 of \$2.5 million, compared with \$1.5 million in FY-15, of previously unrecognized deferred tax assets which resulted from the improved performance of the Company's FPD operations; the reversal of previously recognized tax expense of \$2.4 million that was eliminated by a distribution of the FY-15 earnings of a foreign subsidiary to its foreign parent; and a higher percentage of income before income taxes, including the \$8.8 million gain on the sale of investment in Q1-16 that was generated in jurisdictions where the Company previously incurred losses which, due to valuation allowances, did not result in the Company recognizing tax benefits. These positive factors were offset in part by the accrual of \$0.7 million of withholding taxes related to a foreign subsidiary share redemption in a foreign jurisdiction. As of each reporting date, the Company considers new evidence, both positive and negative, that could impact management's view with regards to the future realizations of deferred tax assets.

Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests increased \$0.1 million to \$3.4 million in Q3-16, as compared to \$3.3 million in Q3-15, and decreased by \$0.5 million to \$8.2 million in YTD-16, as compared to \$8.7 million in YTD-15, as a result of fluctuations in net income of the Company's IC manufacturing facility in Taiwan.

Liquidity and Capital Resources

The Company's working capital increased to \$344.4 million at July 31, 2016 as compared to \$171.4 million at November 1, 2015, primarily as a result of the following: increased cash and cash equivalents due to the sale of the Company's 49.99% interest in the MP Mask joint venture for \$93.1 million in May 2016; the conversion of \$7.4 million of debt to common stock in April 2016; proceeds from the sale of an investment in a foreign entity of \$8.8 million in January 2016; and cash generated from operating activities. Net cash provided by operating activities was \$91.4 million for the nine month period ended July 31, 2016, essentially unchanged from \$91.8 million for the nine month period ended August 2, 2015. Net cash provided by investing activities for the nine month period ended July 31, 2016, was \$57.6 million, which was comprised primarily of proceeds of \$101.9 million received from the sale of investments, partially offset by capital expenditure payments. Net cash used in financing activities of \$65.0 million for the nine month period ended July 31, 2016, was comprised of repayments of long-term borrowings of \$56.3 million and the payment by a subsidiary of a dividend to noncontrolling interests of \$11.9 million in June 2016, which were partially offset by proceeds of \$3.2 million received from exercises of employee stock options. The Company may use its cash available on hand for operations, capital expenditures, debt repayments, strategic opportunities, stock repurchases or other corporate uses, any of which may be material.

As of July 31, 2016 and November 1, 2015, the Company's total cash and cash equivalents include \$115.9 million and \$102.9 million, respectively, held by its foreign subsidiaries. The majority of earnings of the Company's foreign subsidiaries are considered to be indefinitely reinvested. However, in the event that the Company was to repatriate these earnings, such action may result in increased U.S. federal income taxes and local country withholding tax in certain jurisdictions. The Company's foreign subsidiaries continue to grow through the reinvestment of earnings in additional manufacturing capacity and capability, particularly in the high-end IC and FPD areas.

In August 2016 the Company announced that it had signed an investment agreement with the Xiamen Torch Hi-Tech Industrial Development Zone (Xiamen Torch) to establish an IC manufacturing facility in Xiamen, China. Under the terms of the agreement the Company will build and operate a state-of-the-art IC manufacturing and research and development facility, in return for which Xiamen Torch will provide certain investment incentives and support.

The Company plans to invest \$160 million over the next five years, with construction commencing in 2017 and production estimated to start in late 2018. The investment will be in the form of cash, transferred capital equipment and, possibly, local financing. Support for the project has been obtained from an existing customer.

In June 2016 PDMC, the Company's majority owned IC facility in Taiwan, paid a dividend of \$11.9 million to its noncontrolling interests.

In May 2016, the Company sold its investment in MP Mask to Micron for \$93.1 million. On that same date a supply agreement commenced between the Company and Micron, which provides that the Company will be the majority outsourced supplier of Micron's photomasks and related services. The supply agreement has a one year term, subject to mutually agreeable renewals. In addition, the Company forevermore has the rights to use technology under the prior technology license agreement.

In April 2016 \$57.5 million of the Company's senior convertible notes matured. The Company repaid \$50.1 million to noteholders and issued approximately 0.7 million shares to noteholders that elected to convert their notes to common stock. The notes were exchanged at the rate of approximately 96 shares per \$1,000 note principle, equivalent to a conversion rate of \$10.37 per share.

In January 2015 the Company privately exchanged \$57.5 million in aggregate principal amount of its 3.25% convertible senior notes with a maturity date of April 1, 2016, for new 3.25% convertible senior notes with an aggregate principal amount of \$57.5 million with a maturity date of April 1, 2019. The conversion rate of the new notes is the same as that of the exchanged notes, which were issued in March 2011 with a conversion rate of approximately 96 shares of common stock per \$1,000 note principal, equivalent to a conversion price of \$10.37 per share of common stock, and is subject to adjustment upon the occurrence of certain events, which are described in the indenture dated January 22, 2015. Noteholders may convert each \$1,000 principal amount of notes at any time prior to the close of business on the second scheduled trading day immediately preceding April 1, 2019, and the Company is not required to redeem the notes prior to their maturity date. Interest on the notes accrues in arrears, and is paid semiannually through the notes' maturity date.

The Company's credit facility, which expires in December 2018, has a \$50 million limit with an expansion capacity to \$75 million, and is secured by substantially all of the Company's assets located in the United States and common stock the Company owns in certain of its foreign subsidiaries. The credit facility precludes the Company from paying cash dividends and is subject to a minimum interest coverage ratio, total leverage ratio and minimum unrestricted cash balance financial covenants, all of which the Company was in compliance with at July 31, 2016. The Company had no outstanding borrowings against the credit facility at July 31, 2016, and \$50 million was available for borrowing. The interest rate on the credit facility (1.73% at July 31, 2016) is based on the Company's total leverage ratio at LIBOR plus a spread, as defined in the credit facility.

As of July 31, 2016, the Company had capital equipment commitments outstanding of approximately \$51 million. The Company believes that its currently available resources, together with its capacity for growth, and its access to equity and other financing sources, will be sufficient to satisfy its currently planned capital expenditures, as well as its anticipated working capital requirements for the next twelve months. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

The Company's liquidity is highly dependent on its sales volume, cash conversion cycle, and the timing of its capital expenditures (which can vary significantly from period to period), as it operates in a high fixed cost environment. Depending on conditions in the semiconductor and FPD markets, the Company's cash flows from operations and current holdings of cash may not be adequate to meet its current and long-term needs for capital expenditures, operations and debt repayments. However, the Company believes its cash on hand, cash generated from its operations and cash committed under its credit facility will allow it to fund its operations through at least the next twelve months. Historically, in certain years, the Company has used external financing to fund these needs. Due to conditions in the credit markets, some financing instruments used by the Company in the past may not be currently available to it. The Company continues to evaluate further cost reduction initiatives. However, the Company cannot assure that additional sources of financing would be available to it on commercially favorable terms, should its cash requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

Off-Balance Sheet Arrangements

In April 2014 the Company acquired 50.01% (a controlling interest) of PDMC, its IC manufacturing facility located in Taiwan. Under the PDMC operating agreement the shareholders of PDMC may be requested to make additional contributions to PDMC. In the event that PDMC requests additional capital from its shareholders, the Company may be required to make additional capital contributions to PDMC in order to maintain its 50.01% ownership. The PDMC operating agreement limits the amount of contributions that may be requested during both the first four years of PDMC and during any individual year within those first four years. As of July 31, 2016, the Company had not been requested to make any capital contribution to PDMC.

The Company leases certain office facilities and equipment under operating leases that may require it to pay taxes, insurance and maintenance expenses related to the properties. Certain of these leases contain renewal or purchase options exercisable at the end of the lease terms.

Business Outlook

A majority of the Company's revenue growth is expected to continue to come from the Asian region, as customers increase their use of manufacturing foundries located outside of North America and Europe. Additional revenue growth is also anticipated in North America, as the Company expects to continue to benefit from advanced technology it may utilize under its technology license with Micron.

The Company continues to assess its global manufacturing strategy and monitor its market capitalization, sales volume and related cash flows from operations. This ongoing assessment could result in future facility closures, asset redeployments, additional impairments of intangible or long-lived assets, workforce reductions, or the addition of increased manufacturing facilities, all of which would be based on market conditions and customer requirements.

Effect of Recent Accounting Pronouncements

See "Note 15 – Recent Accounting Pronouncements" to the condensed consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Rate Risk

The Company conducts business in several major international currencies through its worldwide operations and its financial performance may be affected by fluctuations in the exchange rates of these currencies. Changes in exchange rates can positively or negatively affect the Company's sales, operating margins, assets, liabilities, and equity. The functional currencies of the Company's Asian subsidiaries are the South Korean won, the New Taiwan dollar, and the Singapore dollar. The functional currencies of the Company's European subsidiaries are the British pound and the euro. The Company also engages in transactions and holds balances in Japanese yen.

The Company attempts to minimize its risk of foreign currency transaction losses by producing its products in the same country in which the products are sold (thereby generating revenues and incurring expenses in the same currency), and by managing its working capital. There can be no assurance that this approach will continue to be successful, especially in the event of a significant adverse movement in the value of any foreign currency against the U.S. dollar, the New Taiwan dollar or the South Korean won. However, in some instances, the Company sells products in a currency other than the functional currency of the country where it was produced or purchases products in a currency that differs from the functional currency of the purchasing manufacturing facility.

The Company's primary net foreign currency exposures as of July 31, 2016, included the South Korean won, the Japanese yen, the New Taiwan dollar, the Singapore dollar, the British pound, and the euro. As of July 31, 2016, a 10% adverse movement in the value of these currencies against the functional currencies of our subsidiaries would have resulted in a net unrealized pre-tax loss of \$7.5 million. The Company does not believe that a 10% change in the exchange rates of other non-US dollar currencies would have a material effect on its results of operations or cash flows.

Interest Rate Risk

At July 31, 2016, the Company did not have any variable rate borrowings. A 10% change in interest rates would not have had a material effect on the Company's consolidated financial position, results of operations, or cash flows in the three or nine month periods ended July 31, 2016.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company has established and currently maintains disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), designed to provide reasonable assurance that information required to be disclosed in its reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including the Company's chief executive officer and chief financial officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating disclosure controls and procedures, management recognized 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 necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

The Company's management, under the supervision and with the participation of the Company's chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation the Company's chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures were effective at a reasonable assurance level as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting during the Company's third quarter of fiscal 2016 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1A. RISK FACTORS

The Company's announced expansion into China entails substantial risks.

In August 2016 the Company announced that it would invest \$160 million over the next five years to construct an IC manufacturing facility in Xiamen, China. This investment is subject to substantial risks which may include, but are not limited to: delays in or the inability to obtain necessary permits that are needed to enable us to construct our facility or conduct our ongoing business; the inability to protect our intellectual property rights under Chinese law, which may not offer as high of a level of protection as U.S. law; unexpectedly long negotiation periods with Chinese suppliers and customers; quality issues related to materials sourced from local vendors; unexpectedly high labor costs due to a tight labor supply; and difficulty in repatriating funds and selling or transferring assets. Our investment in China also exposes us to a significant additional foreign currency exchange risk, which we have not been subject to in recent years. These and other risks may result in our not realizing a return on, or losing some of or all of our planned investment in China, which would have a material adverse effect on our financial condition and financial performance.

Please refer to Part 1, Item 1A of the Company's Form 10-K for the year ended November 1, 2015, for additional risks related to the Company's business.

Item 6. EXHIBITS

(a) Exhibits

Exhibit Number	Description
10.35	Investment Agreement between Xiamen Torch Hi-Tech Industrial Development Zone Management Committee and Photronics Singapore Pte, Ltd dated August 18, 2016.*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Confidential information has been omitted and filed separately with the Commission.

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.

Photronics, Inc.
(Registrant)

By: /s/ SEAN T. SMITH
 Sean T. Smith
 Senior Vice President
 Chief Financial Officer
 (Duly Authorized Officer and
 Principal Financial Officer)

Date: September 2, 2016

* Confidential information has been omitted and filed separately with the Commission.

INVESTMENT AGREEMENT

Agreement Number: XM20160810-01

Parties:

Party A: Xiamen Torch Hi-Tech Industrial Development Zone Management Committee (hereinafter **"Party A"**);

Party B: Photronics Singapore Pte, Ltd. (hereinafter **"Party B"**)

Whereas:

Party A is an agency of Xiamen municipality, jointly established by the National Scientific and Technological Commission and the People's Municipal Government of Xiamen, one of the three national-level hi-tech zones named with "Torch" in China.

Xiamen municipality is *, Xiamen municipality and Party A acknowledges that the Photronics, Inc. and its subsidiaries, Photronics Singapore Pte, Ltd are major commercial photomask producers in the world, and recognizes its important position in the industry. Xiamen municipality and Party A welcomes and supports Party's B's proposed investment project of IC photomask in Xiamen.

Party A and Party B have agreed to the following with respect to Party B's proposed investment:

I. Party B's Investment Project, Construction Plan and Covenants

a. Investment Project

i. Party B intends to establish a manufacturing company within the jurisdiction of Xiamen Torch Hi-Tech Industrial Development (hereinafter **"Project Company"**) to operate the investment project. The Project Company shall be registered and established within * of the execution of this Agreement.

ii. Scope of Business: the Project Company shall engage in the research and development, manufacture and sale of photomasks.

* Investment Amount: The Project Company shall make * of investments. The total amount of the * will be USD\$ 160 million, which includes a * registration capital. Party B will assess the demand from * and subject to Board approval of Photronics, Inc. will * Subject to Board approval of Photronics, Inc. The registration capital will be *.

iv. Revenues: Party B hereby covenants that the Project Company shall generate all its revenues and pay all its taxes within Party A's jurisdiction, that the Project Company shall take steps to obtain permits required for the commencement of construction immediately after the Project Company is established, that the Project Company shall complete the construction and commence with production within Three (3) years, and the Project Company will use reasonable efforts to reach annual production capacity should reach yearly capacity of * within five (5) years of Party B's obtaining the industrial land.

b. Construction Plan

- i. Party B covenants that the Project Company shall commence and complete the construction of the plants strictly in accordance with the timeframe stipulated in the Land Sale Contract.
- ii. Party B agrees that Party B shall implement the project in accordance with Party A's requirements and the relevant regulations of the Municipal Government of Xiamen, that the project shall meet with the requirements of the overall planning of the Municipal Government of Xiamen and Party A, and that Party B shall fulfill Party A's investment requirements with respect to investment intensity, revenues and taxation.

II. Construction to be Conducted by Party A

- a. Party A agrees to provide industrial land with an area of approximately * in Xiamen Torch Hi-Tech Development Zone (Xiang An) the land price of which shall be determined through fair market appraisal based on the base price of industrial land in the Development Zone, and the provision of which land shall be in accordance with the Municipal Government of Xiamen's laws and regulations in relation to land sale and provision. The Project Company shall pay fees and taxes due in accordance with relevant regulations. In the unlikely event that Party A cannot provide Party B with the land referenced above then Party B can terminate this Agreement without any penalty or further obligation.
- b. The land that Party A provides to the Project Company shall comply with the Municipal Government of Xiamen's requirements on urban planning and environmental protection. The land condition shall meet with the requirements of the construction needs of the Project Company. The land use right shall be valid for * years. The floor area ratio, building density, greening, boundary line of building and the ratio of fixed investment amount to land area shall comply with the requirements of the Land and Resources Department, the Urban Planning Department and the Economic and Information Department of the Municipal Government of Xiamen.
- c. Delivery of Land: In accordance with the land use and construction schedule as agreed between the parties, and upon the lawful approval of the provision of the construction land, Party A shall deliver the land in accordance agreed timeframe without delay.
- d. Land Conditions upon Delivery: Party A covenants that, upon the delivery of the construction land, there shall be available major roads, storm water channel, sewage, water supply, power supply, telecommunications, and the internet. Party A shall be responsible for all the power supply and other infrastructure outside of the redlines defining the construction land used by the Project Company. The land surface shall be leveled and cleared in accordance with the leveling and clearance standard of the municipal urban planning.

III. Policy Support

In view of the significant scale of Party B's proposed investment and the leading technologies that Party B will utilize and in view of the fact that * and which will contribute to the development of the integrated circuit industry that the Municipal Government of Xiamen seeks to build, Party A shall provide the following support to the Project Company:

a. Subsidies for Purchase of Equipment

- i. Party A agrees to provide * for the * that the Project Company will purchase for the plants in Xiamen *. Such * shall be * of the purchase price of the equipment, provided that such * shall not exceed an amount in RMB equivalent to *.
- ii. Upon application for the above-mentioned equipment *, the Project Company shall provide the required and appropriate documentation, such as equipment purchase contracts, purchase orders, invoices, lists of equipment, list of customs clearance, etc. Upon review and approval, Party A shall provide the * in three installments as follows:
 1. Upon the payment of no less than * by the Project Company, and upon the application by the Project Company and the verification by Party A, Party A shall provide * of the *;
 2. Upon the * that the Project Company purchases and installs in its plants in Xiamen, and upon the application by the Project Company and the verification by Party A, Party A shall provide * of the *;
 3. No later than the commencement of production using the equipment purchased by the Project Company in Xiamen, and upon the application by the Project Company and the verification by Party A, Party A shall provide * of the *. The project company shall provide the equipment inspection report when fill the application.

Upon each * application by the Project Company and upon verification by Party A, Party A shall pay the relevant * within One (1) month. Party B's applications shall not be delayed without a reasonable cause.

* The above subsidies applications shall be effective if made between *.

b. Loan Interest Subsidies

- i. Party A shall assist the Project Company in its application for project financing from banks. The Project Company shall covenant that such bank loans shall be used exclusively for the *. Party A agrees to provide * for * that the Project Company incurs with respect to such financing. Such loan interest * shall not exceed an amount in RMB equivalent to *, and shall be valid for * years from the date when the financing is obtained.
- ii. Party A shall assist the Project Company in its application for *. The Project Company shall covenant that such * shall be used exclusively for the * incurred in the course of the * of the project. Party A agrees to provide * for the interests that the Project Company incurs with respect to such *. Such * shall not exceed an amount in RMB equivalent to *, and shall be valid for * from the date when the loan is obtained.

iii. Party A shall assist the Project Company in its application for * from *. The Project Company shall covenant that such * shall be used exclusively for *. Party A agrees to provide * that the Project Company incurs with respect to such *. Such * shall not exceed an amount in RMB equivalent to *, and shall be valid for * from the date when the * is obtained.

* After the payment of interests incurred with respect to the above project * for the current year, the Project Company shall make one application to Party A for the relevant *. Upon review and verification, Party A shall make one lump sum payment for the * to the Project Company *. The above * applications shall be effective if made between *.

c. The total * (including * for * and *) that Party A shall provide to the Project Company shall not exceed the lower of i) * and ii) * of the total investment the Project Company will make in the production and equipment in the Hi-Tech Development Zone within * years of the establishment of the Project Company.

d. Policy regarding Hi-Tech Companies

To the extent that the Project Company meets the conditions required for the classification of *, Party covenants that it shall use its best efforts to assist the Project Company to obtain such classification.

e. Policy regarding Talent Retention

Party A shall facilitate the Project Company's enjoyment of various * in accordance with the prevailing *.

f. Miscellaneous

Party A shall use its best efforts to assist the Project Company in obtaining and implementing various applicable and prevailing * made available by *.

....

IV. Party A's Assistance and Services

Party A shall establish a * to * the establishment and operation of the Project Company, and to assist the Project Company in obtaining *, including, without limitation, business registration, taxation registration, construction, etc.

V. Application of Policies and Amendment of Provisions

a. This Agreement is entered into and enforced in accordance with the relevant laws and regulations of the central government, the provincial government, the municipal government and the Hi-Tech Development Zone. To the extent that relevant policies governing this Agreement are amended due to the changes of the laws and/or regulations, Party A and Party B agree to enforce this Agreement as amended accordingly. In the event that any amendment or change to the law causes a *, then Party B shall be authorized to * the Project Company, which * shall not be treated as a * of this Agreement; in such incidence, Party A shall provide reasonable support to Party B, provided that the above shall be in compliance with the relevant PRC laws and regulations.

- b. Party B agrees that if Party B fails to or only partially fulfill its covenants under Article I of this Agreement due to its own reasons and without Party A's prior written consent, then Party A has the right to * the relevant provisions in this Agreement with respect to facilitating policies, including, without limitation, reducing or eliminating the various facilitating policies that are agreed upon in this Agreement but have yet to be enforced.
- c. Upon its establishment, the Project Company shall operate for no less than *, shall not * during its existence, and shall not * to * in any way, otherwise Party A has the right to reduce, eliminate to retrieve various *. For the avoidance of doubt, in the event that the Project Company sustains *, then Party B shall be authorized to * the Project Company, which * shall not be treated as a breach of this Agreement in accordance with PRC law, provided that the above shall be in compliance with the relevant PRC laws and regulations.

VI. Confidentiality

- a. To the extent that one party obtains knowledge or exposure to the other party's trade secret or other confidential information or documents by virtue of executing or enforcing this Agreement (together with the existence of this Agreement and any provision in this Agreement, **"Confidential Information"**), the party obtaining such Confidential Information shall have the obligations to maintain such information confidential. Unless otherwise agreed upon in writing, neither party may, directly or indirectly, disclose or allow any person to disclose or use any Confidential Information to any person (including, without limitation, the media, any corporation, partnership, group companies, individual or any other entity), unless otherwise provided for in this agreement and except the use of the Confidential Information for purposes of enforcing this Agreement, and except the disclosure made by one party (hereinafter the **"Recipient"**) to its affiliates, executives, directors, consultants, employees, agents or intermediaries (hereinafter, collectively, the **"Representatives"**) to the extent that such disclosure is necessary for the Recipient to evaluate this Agreement. The Recipient agrees to inform the Representatives of the confidential nature of the Confidential Information, and to require the Representatives to strictly maintain the confidentiality of such Confidential Information in accordance with the requirements in this Agreement. The Recipient agrees to be responsible and liable for any breach of confidentiality committed by its Representatives.
- b. Notwithstanding the foregoing, Confidential Information shall not include the following information:
 - i. the information publicly available at the time of the disclosure;
 - ii. the information that becomes publicly available without either party violating the confidentiality provisions in this Agreement;
 - iii. the information that either party is required to disclose in accordance with the relevant laws, regulations, regulatory requirements or public listing requirements; and
 - iv. the information that either party obtains from any third party that does not violate laws, regulations of the confidentiality provisions in this Agreement with respect to the Confidential Information.

- c. To the extent that one party is mandated by the law to disclose Confidential Information, such party shall immediately notify the other party of such lawful mandate and use its best efforts, permissible under applicable laws, to assist the other party in undertaking protective measures with respect to the disclosure of the Confidential Information. Party A acknowledges that Party A understands Party B's obligations and that Party A agrees that Party B may disclose certain provisions in accordance with certain requirements under securities laws, provided that Party B shall notify Party A of the specific information that shall be disclosed prior to any disclosure .
- d. The confidentiality provisions in this Agreement shall not cease to be effective upon the expiration or termination of this Agreement. The confidentiality provisions under this Article shall continue to bind both parties within One (1) year of the expiration or termination of this Agreement.

VII. Miscellaneous

- a. Any disputes arising from this Agreement shall be resolved through consultation between the parties or, should such consultation fail to resolve the disputes, shall be submitted to the Shanghai International Economic and Trade Arbitration Commission for adjudication .
- b. The exchange computations shall be as follows: On the day when Party B submits subsidiary application, if the US-RMB exchange rate fluctuation is 10% of less of the middle rate (or specified rate) published by the People's Bank of China on the same day, then such middle rate shall apply; if the exchange rate fluctuation exceeds 10% of such middle rate, then the applicable exchange rate shall be the average of i) the middle rate published by the People's Bank of China on the date when this Agreement is executed and ii) the middle rate published by the People's Bank of China on the date when the subsidy application is made by Party B.
- c. During the course of the resolution of the disputes, the parties shall continue to enforce the provisions and to fulfill their covenants under this Agreement except the provisions or covenants under dispute.
- d. Any matter not provided for in this Agreement may be determined through consultation between the parties and the parties may enter into supplementary agreements accordingly . Supplementary agreements and this Agreement shall be equally binding.
- e. Party A and Party B both agree that this Agreement will be fully assigned by Party B to the project company it is forming in Xiamen. With respect total investment and registered capital, If the project company is lack of capacity to perform this agreement, the Party B shall perform this agreement.
- f. This Agreement has been entered into in counterparts, including two identical copies in the language of Chinese and two identical copies in the language of English. All four counterparts shall be equally binding. The parties shall each maintain One (1) counterpart in the language of Chinese and One (1) counterpart in the language of English. All four counterparts shall take effect upon execution and stamping of seals. To the extent that there shall be conflicts between the Chinese version and the English version, the Chinese version shall control. This Agreement shall take effect when the parties' representatives sign or stamp their seals.

{THE REMAINDER OF THIS PAGE IS INTENTIONALLY BLANK}

EXHIBIT 31.1

I, Peter S. Kirlin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Photonics, 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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.

/s/ PETER S. KIRLIN

Peter S. Kirlin
Chief Executive Officer
September 2, 2016

EXHIBIT 31.2

I, Sean T. Smith, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Photonics, 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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.

/s/ SEAN T. SMITH

Sean T. Smith
Chief Financial Officer
September 2, 2016

Section 1350 Certification of the Chief Executive Officer

I, Peter S. Kirlin, Chief Executive Officer of Photonics, Inc. (the "Company"), certify, to my knowledge, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

- (1) The Quarterly Report on Form 10-Q of the Company for the quarter ended July 31, 2016, (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

The foregoing certification is being furnished pursuant to 18 U.S.C. § 1350 and will not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

/s/ PETER S. KIRLIN

Peter S. Kirlin
Chief Executive Officer
September 2, 2016

Section 1350 Certification of the Chief Financial Officer

I, Sean T. Smith, Chief Financial Officer of Photonics, Inc. (the "Company"), certify, to my knowledge, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

- (1) The Quarterly Report on Form 10-Q of the Company for the quarter ended July 31, 2016, (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

The foregoing certification is being furnished pursuant to 18 U.S.C. § 1350 and will not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

/s/ SEAN T. SMITH

Sean T. Smith
Chief Financial Officer
September 2, 2016
