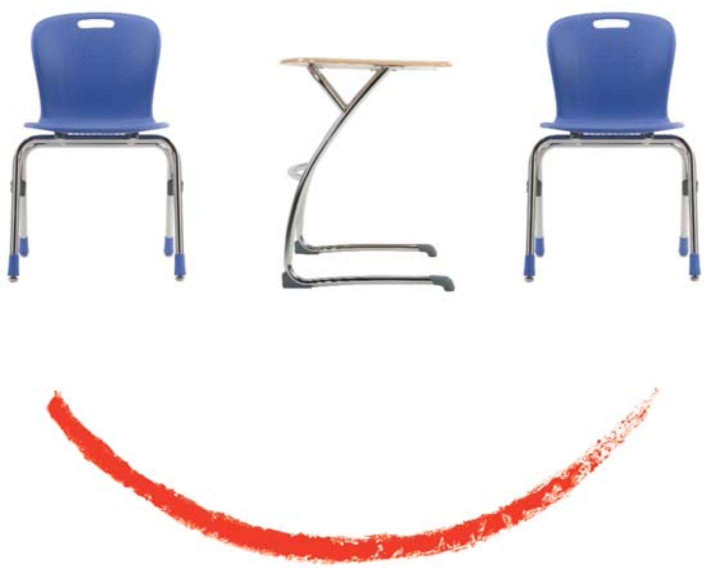
2006 Annual Report

VIRCO MFG. CORPORATION



equipment for educators™

Company Profile

Virco Mfg. Corporation, founded in 1950 and headquartered in Torrance, California, is the nation's leading supplier of equipment for educators.

2006 Annual Report

Virco's Sage™ Series was introduced in 2007.

Financial Highlights

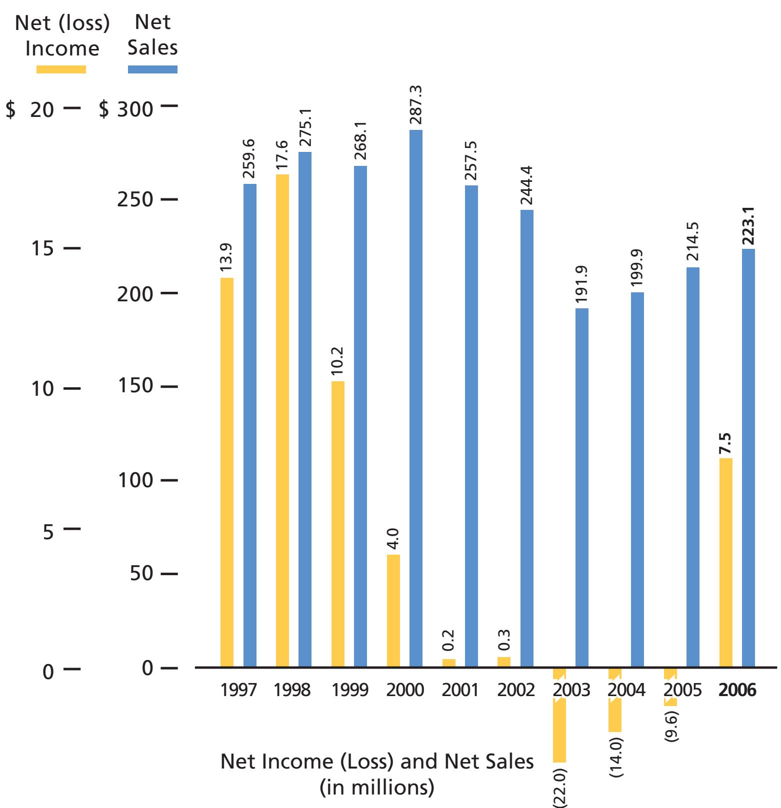
In thousands, except per share data	**2006**	2005	2004	2003	2002	2001	2000	1999	1998	1997
Summary of Operations										
Net sales *(3)(4)*	**$ 223,107**	$ 214,450	$ 199,854	$ 191,852	$ 244,355	$ 257,462	$ 287,342	$ 268,079	$ 275,096	$ 259,586
Net income (loss)										
Net income (loss) before change in accounting methods	**$ 7,545**	$ (9,574)	$ (13,995)	$ (21,961)	$ 282	$ 246	$ 4,313	$ 10,166	$ 17,630	$ 13,852
Change in accounting methods	**—**	—	—	—	—	—	(297)	—	—	—
	7,545	$ (9,574)	$ (13,995)	$ (21,961)	$ 282	$ 246	$ 4,016	$ 10,166	$ 17,630	$ 13,852
Net income (loss) per share *(1)*	**$ 0.55**	$ (0.73)	$ (1.07)	$ (1.68)	$ 0.02	$ 0.02	$ 0.29	$ 0.72	$ 1.20	$ 0.94
Stockholder's equity	**48,878**	39,100	49,265	62,352	82,774	90,223	94,141	93,834	88,923	77,077
Stockholder's equity per share *(2)*	**3.40**	2.98	3.76	4.76	6.31	6.71	6.90	6.82	6.30	5.39

(1) Based on average number of shares outstanding each year after giving retroactive effect for stock dividends and stock split.

(2) Based on number of shares outstanding at year-end giving effect for stock dividends and stock split.

(3) The prior period statements of operations contain certain reclassifications to conform to the presentation required by EITF No. 00-10, "Accounting for Shipping and Handling Fees and Costs," which the Company adopted during the fourth quarter of the year ended January 31, 2001.

(4) During the fourth quarter of 2000, the Company changed its method of accounting for revenue recognition in accordance with Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements." Pursuant to Financial Accounting Standards Board Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements," effective February 1, 2000, the Company recorded the cumulative effect of the accounting change.



Net Income (Loss) and Net Sales
(in millions)

In 2006 we accomplished a $17 million turnaround. Key financial metrics include:

- Sales increased 4.0% from $214.5 million to $223.1 million.
- Gross margin improved from 30.2% to 35.2%.
- Selling, general and administrative expenses as a percent of sales declined from 34.7% to 31.7%.
- Pre-tax operating margin of 3.6% generated $8.0 million in pre-tax earnings.
- Earnings per share improved from a loss of $0.73 per share to income of $0.55 per share.
- Shareholders' equity increased from $39.1 million to $48.9 million.

left: **Robert A. Virtue** - President and CEO
right: **Douglas A. Virtue** - Executive Vice President

May 7, 2007

The obvious question after a turnaround year like 2006 is: what's next? In terms of results, we certainly will not repeat the magnitude of last year's improvement in 2007. As the initiatives described in this report continue to mature, we hope to achieve incremental annual improvement toward the 8%-10% pre-tax earnings of the late 1990s.

Our present position reminds us of a similar period in 1994-95 as we emerged from recession and were just beginning to realize the operating advantages of a business model re-oriented toward domestic fabrication and distribution. A major decision preceded those years of success: we had recently closed our factory in Mexico, relocated to a larger facility in Torrance, California, and invested heavily in automation. We believed then that labor rates and logistical expenses in Mexico would rise faster than domestic costs. We believe now that the China pendulum is making a similar swing.

Although we've told the story before, a brief recap of how we arrived at our present strategic position may be helpful for new readers. We began by reassessing everything about our business: from infrastructure and capital structure, to customers, markets, a more broadly defined array of competitors, and the rapidly emerging threat of low-cost imports. We concluded that:

- A broader product and service assortment built around the "natural market" of K-12 furniture, fixtures and equipment (FF&E) was necessary to satisfy our customers' preference for a single-point-of-purchase and single-point-of-service supplier;

- Our domestic factories would shift from cost neutrality to cost advantage as the all-in costs of global sourcing began to be realized;

- The speed, flexibility, and coordination offered by our infrastructure were essential for providing reliable service during our customers' narrow summer delivery window; and
- A low-cost model of organic growth based on value-added design provided both our customers and shareholders the best return on their dollar going forward.

We emerged with a vertically integrated, multi-channel strategy called Equipment for Educators™, which we adopted as our corporate tagline. Since then we've methodically populated product categories, price points and support services to become the single-source supplier we envisioned. And we've learned one very important lesson: the products we develop ourselves are the most profitable. To that end, we continue to focus intently on organic growth through value-added design. That is the engine behind Equipment for Educators.

Equipment for Educators doubled the size of our addressable market from $400M to $800M and aligned it with the natural market of K-12 furniture, fixtures and equipment (FF&E).

In the late 1990s we defined the market we served by the products we were then making, which consisted primarily of moveable classroom furniture. We estimated the market at $400M and our share at about 50%. Our factories, warehouses and service offerings were organized around this historic definition of our addressable market. When we talked about competition, we focused on other manufacturers whose current product lines were similar to our own. When we talked about growth we imagined selling more units of what we were already making.

During this time a sea change was occurring among our traditional

VIRCO EQUIPMENT FOR EDUCATORS

- classroom chairs and desks
- science tables and lab stools
- technology support furniture
- cafeteria and foodservice furniture
- library and media center furniture
- audio-visual equipment
- early learning furniture and equipment
- performing arts equipment
- full project management & installation services

Equipment for Educators aligns our product assortment and services with the "natural market" of K-12 furniture, fixtures and equipment (FF&E). We estimate the market for these products and services at approximately $800M.

customer base of public school business officials. Confronted with shrinking budgets, rising costs, and pressure from parents and students to make individual schools more accountable for results, they found themselves managing increasingly decentralized organizations. "Site-based management" became the goal and brought a series of changes to the orderly market we were used to.

Rather suddenly, our narrow product range and wholesale-type distribution were deemed inconvenient by both business managers and site-based principals. What they needed was a convenient single-point-of-purchase and single-point-of-service supplier that could supplement the functions of their reduced purchasing and maintenance staffs.

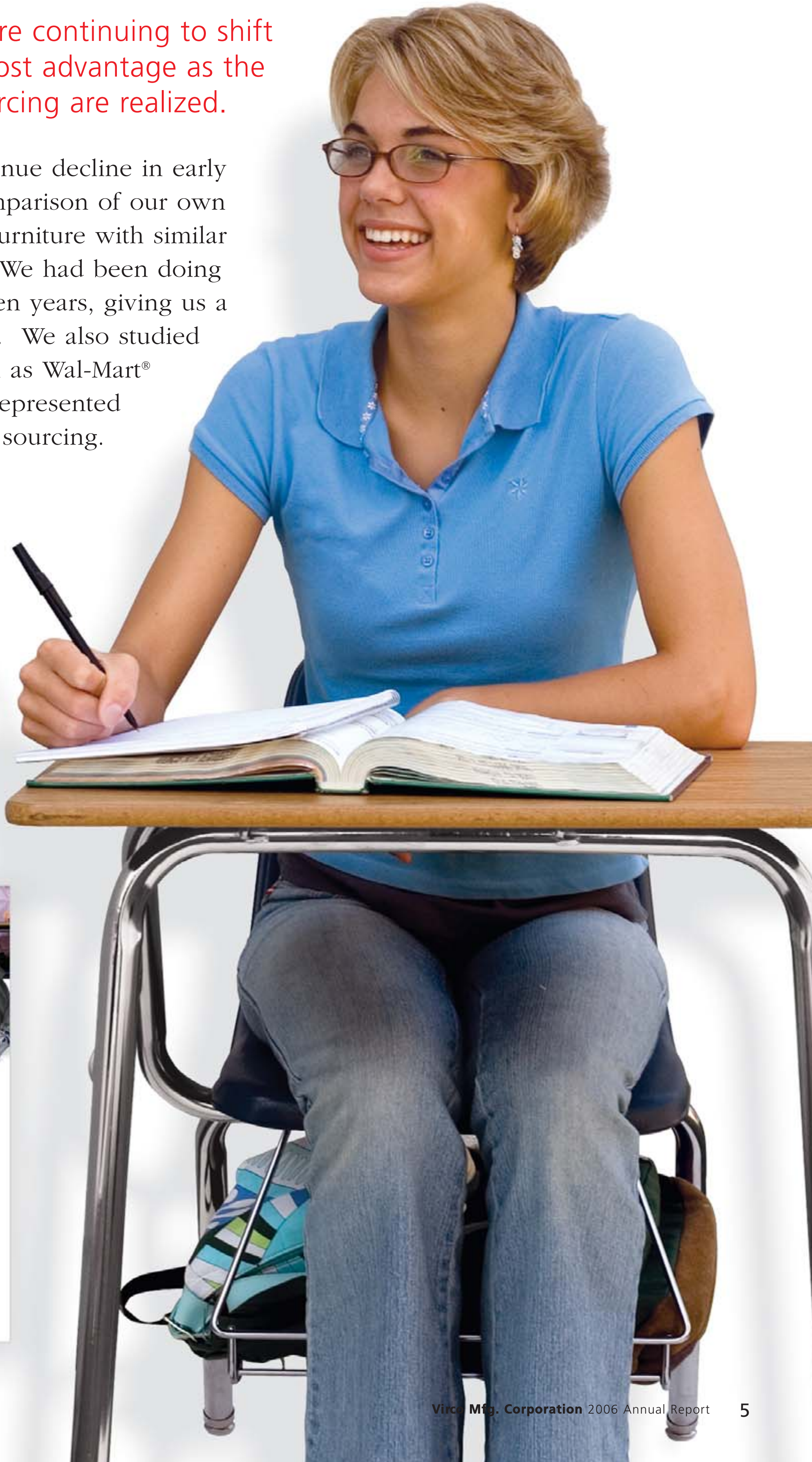
At the same time, a number of other factors combined to create what was, for us, a perfect storm:

- Collapse of the dot-com bubble reduced state tax receipts and related public school funding;
- Office furniture manufacturers and distributors began prospecting in the public schools following an earlier contraction in their own markets;
- Low-cost imports gave at least the appearance of value and further encouraged "bargain shopping";
- Volatile raw material costs and supply interruptions impacted both cost-of-goods-sold and service expense as we adjusted to maintain traditional levels of performance; and
- We incurred the burden of the largest capital investment in our history – $62M for our Conway, Arkansas facility – at precisely the moment these other factors were cutting revenue by 40%.

After another year of analysis, we determined that our infrastructure and know-how were well suited to serving the larger, more natural market of FF&E as defined by school business officials and principals. This market had a familiar economic and performance constraint – extreme seasonality – and this remained the pivot around which we built our new strategy. The full FF&E market was also approximately twice the size of the K-12 furniture market alone, giving us broad scope to develop new products and services that would utilize our newly expanded infrastructure.

Our domestic factories are continuing to shift from cost neutrality to cost advantage as the all-in costs of global sourcing are realized.

At the low point of our revenue decline in early 2003 we made a careful comparison of our own domestically manufactured furniture with similar products sourced offshore. We had been doing business in China for over ten years, giving us a factual basis for comparison. We also studied larger scale distributors such as Wal-Mart® and Lowes®, which we felt represented the state-of-the-art in global sourcing.



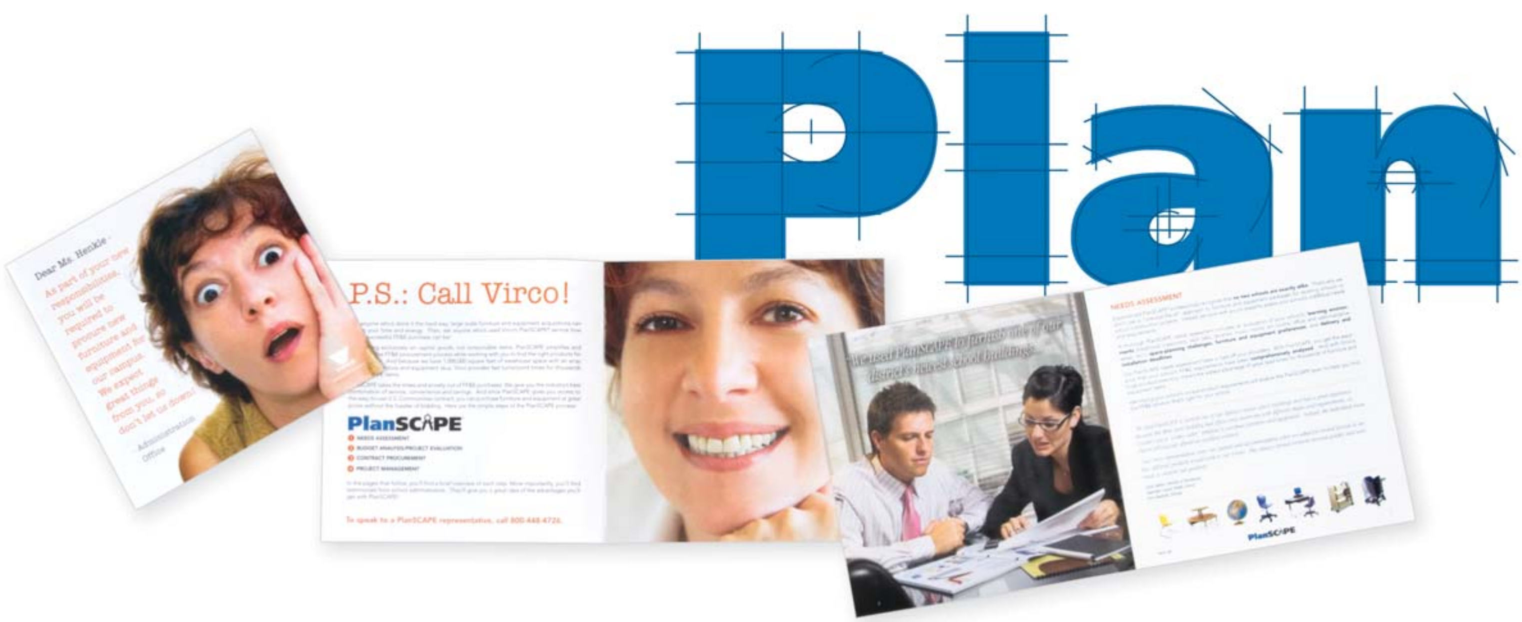
Our vertically integrated domestic factories and warehouses support the broadest, most reliable quick ship program in the seasonally compressed FF&E market. We aggressively promote this performance advantage to educators of all grade levels.

We concluded that a counter-intuitive economic boundary existed below which the benefits of cheap labor were offset by higher freight costs. We called this boundary the “price/cube threshold”. It became the basis of our long-term decision to keep our domestic factories open even as conventional wisdom argued for the closure of one or both of them.

The price/cube threshold was also the day-to-day dividing line between what we imported and what we made ourselves. Continuous monitoring of both absolute and relative costs over the intervening years confirmed that raw materials were escalating evenly in both markets, but offshore labor plus freight was climbing faster than domestic labor alone. For the following reasons, we believe this trend is likely to continue:

- Wage rates in coastal China increased approximately 20% in 2006.
- Labor shortages in China are now creating occasional supply chain disruptions.
- Deferred environmental clean-up costs estimated by the World Bank at 8-12% of China’s GDP are not factored into current pricing.
- Upward valuation of China’s currency may increase the cost of exports.
- Ocean freight and port costs are likely to rise.

With our own gross margins near historic highs and additional improvement possible as Equipment for Educators™ matures, we like our cost position relative to competitors who placed a bigger bet on outsourcing. Container-scale sourcing demands pinpoint forecasting, strong financing, and coordinated delivery, all of which are



exacerbated by the extreme seasonality of the FF&E market. Several years ago these hidden costs were easily rationalized in the face of what seemed miraculously low prices. The pendulum swings of selling prices in our market may have been an attempt on the part of all players to estimate these hidden costs. Now that there's sufficient history, we've seen an upward stabilization of prices that correlates with what we believe is more accurate all-in cost accounting.

Our vertically integrated infrastructure provides essential performance advantages for the seasonal FF&E market.

To further illustrate the seasonal challenge of the FF&E market, consider that our biggest month for incoming orders is June and our two heaviest shipping months are July and August. The compression between incoming orders and shipments is approximately equal to the lead-time for globally-sourced ocean freight plus final-destination delivery. Combined with the increasing sophistication of modern campuses and the breadth of furniture and equipment that goes inside, a traditional drop-ship and/or offshore sourcing model presents significant performance challenges. The greater the number of sources and the longer the lead time for each, the greater the risk of a failed installation. In addition to damaged reputation, failures have real economic costs: return trips for installers and burdensome growth in receivables.

Our vertical infrastructure, divided evenly between Assemble-to-Ship (ATS) manufacturing and distribution, allows us to pre-stage, ship and install these types of orders with much better control. Recognizing our strengths, we have aggressively promoted

SCOPE®

quick ship, color, custom options and coordinated delivery because these are precisely the benefits a non-integrated offshore model cannot offer. Finally, we've scripted all of these capabilities into proprietary PlanSCAPE® project management software, extending the know-how we gained from Furniture Focus® to our entire sales organization.

Value-added design in products and services is the key to low-cost organic growth.

Having assessed our market and our own position in the competitive landscape, we must now turn economic and performance advantage into profitable growth. While we're always open to fairly priced acquisitions with provable synergies, our preferred model is organic growth through value-added design.

As a manufacturer with substantial capacity and a strong culture of efficiency, we've worked hard over the past five years to create an equally strong culture of good design. Given our current physical

ZUMA*frd*™ Series

3 models
13 colors

ZUMA® Series

17 models
22 colors

3000 Series

12 models
10 colors

and financial structure, the leverage offered by internal product development is far greater than that of acquisitions.

In a field as commonplace as classroom furniture and equipment, the concept of value-added design may seem a bit inflated. But we've developed a quantitative measure that relates not only to the price a customer is willing to pay, but to our own efficiency of manufacture and distribution. That measure is price per pound.

In our market, where raw material and conversion costs are readily benchmarked against global standards, a product's price per pound provides unambiguous evidence of customer-defined value. True commodities sell for material and conversion cost plus a razor-thin, sometimes negative margin. Products with real value sell at various multiples of this baseline, and increasingly are the only source of sustainable profitability.

With the success of ZUMA®, IQ®, Plateau®, and other new lines, we've become the acknowledged design leader in classroom furniture. Leaders by definition are followed by others, and ZUMA has launched a flurry of imitative knock-offs. While our patents can prevent exact duplication, they can't stop generalized imitation. That's why no single product or product line can provide permanent competitive advantage.

A steady stream of new products is a different matter. Driven by a culture of good design and backed by a strong development process, we believe we can methodically populate the most important product categories and price points in the FF&E market with new designs or re-designs that add greater value.

Sage™ Series
9 models
22 colors

9000 Series
18 models
12 colors

I.Q.® Series
11 models
12 colors

2000 Series
15 models
12 colors

3300 Series
4 models
10 colors

A key opportunity provided by our vertical model is to design for total efficiency, from the use of common raw materials and processes to final assembly, delivery and installation. All of our new designs have been integrated into ATS, which uses modular components that can be quickly assembled in a variety of configurations. Ten years ago ATS was a simple program for color flexibility. It has now become a product and workforce flexibility program as well, reaching into all levels of operations beginning with initial design.

Our new designs are integrated operationally, visually and functionally. We focus not on designing one chair, but on developing whole families of complementary products that build together in the factory and work together in the classroom. We believe this integrated approach adds value by creating smarter, better, more efficient products instead of simply cutting corners and making (or buying) uninspired "me-too" products.

The continuity of our design effort extends to services as well. We understand that convenience for educators includes a choice of channels, contracts, and service levels in addition to products and price points. In 2006 we upgraded both our PlanSCAPE® project management software and our website, which now features full e-commerce capabilities. Our multi-channel resale partners are also growing in number and volume, providing important penetration into niche markets that are less efficient for us to serve.

We never lose sight of the fact that during their school careers, students have more physical contact with their chairs and desks than any other equipment on campus.

ZUMAfrd™ is 70% recycled, 98% recyclable, Greenguard® certified, flameproof, scratch resistant, surprisingly comfortable, available in 17 colors, and built from materials provided by the Virco Take-Back Program. It also has a very long service life, making it the most sustainable classroom furniture line available.

FORTIFIED RECYCLED WOOD zumafrd™

VIRCO TAKE-BACK PROGRAM

Comfort, safety, style, strength, and sustainability: all of these are expressions of care that we take seriously. Good design is a sign – a lasting signature – of our good intent.

This year there's a collective smile on our corporate face. It's fun to have good work rewarded by excitement in the market and a return to profitability. It's also good to have the support of so many friends, for whom we continue to be sincerely grateful.

Although it may be last on the list, behind a doll and pink shoes and skates and a pony, most students really do wish for comfortable furniture. We never lose sight of the fact that during their school careers, students have more physical contact with their chairs and desks than any other equipment on campus.

This Management's Discussion and Analysis of Financial Condition and Results of Operations includes a number of forward-looking statements that reflect the Company's current views with respect to future events and financial performance, including, but not limited to, statements regarding plans and objectives of management for future operations, including plans and objectives relating to products, pricing, marketing, expansion, manufacturing processes and potential or contemplated acquisitions; new business strategies; the Company's ability to continue to control costs and inventory levels; availability and cost of raw materials, especially steel and petroleum-based products; the availability and cost of labor: the potential impact of the Company's "Assemble-To-Ship" program on earnings; market demand; the Company's ability to position itself in the market; references to current and future investments in and utilization of infrastructure; statements relating to management's beliefs that cash flow from current operations, existing cash reserves, and available lines of credit will be sufficient to support the Company's working capital requirements to fund existing operations; references to expectations of future revenues; pricing; and seasonality.

Such statements involve known and unknown risks, uncertainties, assumptions and other factors, many of which are out of the Company's control and difficult to forecast, that may cause actual results to differ materially from those which are anticipated. Such factors include, but are not limited to, changes in, or the Company's ability to predict, general economic conditions, the markets for school and office furniture generally and specifically in areas and with customers with which the Company conducts its principal business activities, the rate of approval of school bonds for the construction of new schools, the extent to which existing schools order replacement furniture, customer confidence, and competition.

In this report, words such as "anticipates," "believes," "expects," "will continue," "future," "intends," "plans," "estimates," "projects," "potential," "budgets," "may," "could" and similar expressions identify forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof.

Executive Overview

Management's strategy is to position Virco as the overall value supplier of moveable furniture and equipment. The markets that Virco serves include the education market (the Company's primary market), which is made up of public and private schools (preschool through 12th grade), junior and community colleges, four-year colleges and universities, and trade, technical and vocational schools; convention centers and arenas; the hospitality industry, with respect to their banquet and meeting facilities requirements; government facilities at the federal, state, county and municipal levels; and places of worship. In addition, the Company sells to wholesalers, distributors, retailers and catalog retailers that serve these same markets. These institutions are frequently characterized by extreme seasonality and/or a bid-based purchasing function. The Company's business model, which is designed to support this strategy, includes the development of several competencies to enable superior service to the markets in which Virco competes. An important element of Virco's business model is the Company's emphasis on developing and maintaining key manufacturing, warehousing, distribution, and service capabilities. The Company has developed a comprehensive product offering for the furniture, fixtures, and equipment ("FF&E") needs for the K-12 education market, enabling a school to procure all of its FF&E requirements from one source. This product offering consists primarily of items manufactured by Virco, complemented with product sourced from other furniture manufacturers. The product offering is continually enhanced with an ongoing new product development program that incorporates internally developed product as well as product lines developed with accomplished designers. Finally, management continues to hone Virco's ability to forecast, finance, manufacture, warehouse, deliver, and install furniture within the relatively narrow delivery window associated with the highly seasonal demand for education sales. In fiscal year 2006, over 50% of the Company's total sales were delivered in June, July, August and September with an even higher portion of educational sales delivered in that period. Virco's substantial warehouse space allows the Company to build adequate inventories to service this narrow delivery window for the education market.

The market and operating environment for school furniture was turbulent during the period from 2001 through 2005. As a group, the members of BIFMA (the Business and Institutional Furniture Manufacturer's Association) recorded decreases in shipments of 3%, 19.1% and 17.4% in 2003, 2002 and 2001, respectively. The impact of the recession on the school market lagged the commercial market and did not hit with full intensity until 2003. During this time Virco incurred sales declines of 21.5%, 5.1%, and 10.4% in 2003, 2002, and 2001 respectively.

For two years following the recession in the furniture markets, the Company incurred supply chain disruptions and severe cost increases in certain raw materials. During 2005, the severe hurricanes in the Gulf Coast region of the United States impacted the availability of certain raw materials used in the production of steel. In addition to steel shortages, Virco obtains plastic used in the production of certain high-volume components from the Gulf Coast region. Both the cost and availability of plastic was severely affected. Finally, Virco incurs significant costs relating to energy. The most significant of the Company's energy costs are for diesel fuel, for both outbound freight and inbound materials, though the Company also incurs significant costs for both electricity and natural gas. In 2004 the cost of steel, which is the Company's largest raw material, doubled and was nearly three times higher than at the beginning of 2002. The Company incurred severe supply chain disruptions related to steel in 2004, and incurred unfavorable "yield variances" as the Company substituted more expensive or heavier gauge steel when the standard steel required was unavailable. The cost of plastic and fuel also increased.

Throughout this turbulent period, the Company took appropriate corrective measures to reduce the Company's cost structure to match the decreased sales volume and to raise prices to cover the increased cost of raw materials. Unfortunately, due to the nature of the Company's annual contracts with school districts, the price increases lagged to commodities cost increases resulting in reduced margins and losses during the 2003, 2004, and 2005. Restructuring costs, primarily related to severance payments to terminated employees, adversely impacted results. In addition to price increases and reductions in force, the Company used a variety of tactics to reduce spending, including its Assemble-to-Ship ("ATS") operating model, which permits: the Company to hold reduced inventory levels; strict disciplines over capital expenditures to reduce the investment in PP&E; and wage and hiring freezes. The cumulative impact of these cost-saving measures was realized during 2006 as the Company showed a significant improvement in operating results, recording an operating profit after three years of losses.

During 2006, Virco's sales increased by 4%. This followed a 7% increase in 2005 and a 4% increase in 2004. During this three year period, sales dollars have increased, but unit volume declined. The Company has been emphasizing newly developed products, the value of Virco's products, the value of Virco's project management, distribution and delivery capabilities, and the value of timely deliveries during the peak seasonal delivery period. Although this policy has had an adverse effect on unit volume for lower priced commodity items, it has enabled the Company to successfully raise prices and return margins to profitable levels.

The Company does not anticipate that demand for furniture in the education markets will change substantially in the coming year. Rather we anticipate a continued strong market in bond-funded projects, with project completions being slightly better than 2006. In addition, management anticipates relatively flat demand for replacement furniture due to the continued financial pressures placed on school operating budgets. It is our intent to raise prices modestly, in order to recover the anticipated increases of raw material, freight and service costs for those customers that require full-service installation and delivery. Actual volume shipped during 2007 will be impacted by the behavior of our competitors in response our modestly increased selling prices. We will maintain our core workforce at current levels for the near future, supplemented with temporary labor as considered necessary in order to produce, warehouse, deliver, and install furniture during the coming summer. Because the Company has not closed any manufacturing or distribution facilities, any increase in demand for our product can be met without any required investment in physical infrastructure.

Critical Accounting Policies and Estimates

This discussion and analysis of Virco's financial condition and results of operations is based upon the Company's financial statements which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires Virco management to make estimates and judgments that affect the Company's reported assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, management evaluates such estimates, including those related to revenue recognition, allowance for doubtful accounts, valuation of inventory including LIFO and obsolescence reserves, self-insured retention for products and general liability insurance, self-insured retention for workers compensation insurance, provision for warranty, liabilities under defined benefit and other compensation programs, and estimates related to deferred tax assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. This forms the basis of judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Factors that could cause or contribute to these differences include the factors discussed above under Item 1, Business, and elsewhere in Virco's report on Form 10-K. Virco's critical accounting policies are as follows:

Revenue Recognition: The Company recognizes revenue in accordance with Staff Accounting Bulletin (SAB) No. 101, "Revenue Recognition," as revised by SAB No. 104. Sales are recorded when title passes and collectability is reasonably assured under its various shipping terms. The Company reports sales as net of sales returns and allowances and sales taxes imposed by various government authorities.

Allowances for Doubtful Accounts: Considerable judgment is required when assessing the ultimate realization of receivables, including assessing the probability of collection, current economic trends, historical bad debts and the current creditworthiness of each customer. The Company maintains allowances for doubtful accounts that may result from the inability of our customers to make required payments. Over the past five years, the Company's allowance for doubtful accounts has ranged from approximately 0.7% to 1.4% of accounts receivable at year-end. The allowance is evaluated using historic experience combined with a detailed review of past due accounts. The Company does not typically obtain collateral to secure credit risk. The primary reason that Virco's allowance for doubtful accounts represents such a small percentage of accounts receivable is that a large portion of the accounts receivable are attributable to low-credit-risk governmental entities, giving Virco's receivables a historically high degree of collectability. Although many states are experiencing budgetary difficulties, it is not anticipated that Virco's credit risk will be significantly impacted by these events. Over the next year, no significant change is expected in the Company's sales to government entities as a percentage of total revenues.

Inventory Valuation: Inventory is valued at the lower of cost or market. The Company uses the LIFO (last-in, first-out) method of accounting for the material component of inventory. The Company maintains allowances for estimated obsolete inventory to reflect the difference between the cost of inventory and the estimated market value. Valuation allowances are determined through a physical inspection of the product in connection with a physical inventory, a review of slow-moving product, and consideration of active marketing programs. The market for education furniture is traditionally driven by value, not style, and the Company has not typically incurred significant obsolescence expense. If market conditions are less favorable than those anticipated by management, additional allowances may be required.

Due to reductions in sales volume in the past years, the manufacturing facilities are operating at reduced levels of capacity. The Company records the cost of excess capacity as a period expense, not as a component of capitalized inventory valuation.

Self-Insured Retention: For 2004, 2005, and 2006, the Company was self-insured for product liability losses up to $500,000 per occurrence, for workers' compensation losses up to $250,000 per occurrence, and for auto liability up to $50,000 per occurrence. The Company obtains annual actuarial valuations for the self-insured retentions. Product liability and auto reserves for known and unknown incurred but not reported (IBNR) losses are recorded at the net present value of the estimated losses using a 5.75% discount rate for 2006, and a 6.0% discount rate for 2005 and 2004. Given the relatively short term over which the IBNR losses are discounted, the sensitivity to the discount rate is not significant. Estimated workers' compensation losses are funded during the insurance year and subject to retroactive loss adjustments. The Company's exposure to self-insured retentions varies depending upon the market conditions in the insurance industry and the availability of cost-effective insurance coverage. It is anticipated that self-insured retentions for 2007 will be comparable to the retention levels for 2006.

Warranty Reserve: The Company provides a product warranty on most products. The standard warranty offered on products sold through January 31, 2005, is five years. Effective February 1, 2005, the standard warranty was increased to 10 years on products sold after February 1, 2005. It generally warranties that customers can return a defective product during the specified warranty period following purchase in exchange for a replacement product or that the Company can repair the product at no charge to the customer. The Company determines whether replacement or repair is appropriate in each circumstance. The Company uses historic data to estimate appropriate levels of warranty reserves. Because product mix, production methods, and raw material sources change over time, historic data may not always provide precise estimates for future warranty expense. Warranty expense for 2005 and 2004 was higher than normal due to a recurring cosmetic complaint relating to a high-volume component. In 2005, the Company made appropriate engineering modifications to correct this condition, but may still incur warranty related costs for components produced and sold in prior years.

Defined Benefit Obligations: The Company has three defined benefit plans, the Virco Employees Retirement Plan, the Virco Important Performers (VIP) Plan and the Non-Employee Directors Retirement Plan, which provide retirement benefits to employees and outside directors. Virco discounted the pension obligations under the plans using a 5.75% discount rate in 2006, and a 6.5% discount rate in 2005 and 2004. The Company utilized a 5.0% assumed rate of increase in compensation rates, and estimated a 6.5% return on plan assets. These rate assumptions can vary due to changes in interest rates, the employment market, and expected returns in the stock market. In prior years, the discount rate and the anticipated rate of return on plan assets have decreased by several percentage points, causing pension expense and pension obligations to increase. Although the Company does not anticipate any change in these rates in the coming year, any moderate change should not have a significant effect on the Company's financial position, results of operations or cash flows. Effective December 31, 2003, the Company froze new benefit accruals under all three plans. The effect of freezing future benefit accruals minimizes the impact of future raises in compensation, but introduces a new assumption related to the plan freeze. It is the Company's intent to resume some form of a retirement benefit when the profitability and the financial condition of the Company allow, and the actuarial valuations assume the plans will be frozen for one additional year. If the assumption is modified to a permanent freeze, the Company would be required to immediately recognize any prior service cost / benefit. If the Company had assumed a permanent freeze, pension expense for 2006 and 2005 would have increased by $75,000 and $9,000, respectively. The Company obtains annual actuarial valuations for all three plans.

Deferred Tax Assets and Liabilities: The Company recognizes deferred income taxes under the asset and liability method of accounting for income taxes in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 109, "Accounting for Income Taxes". Deferred income taxes are recognized for differences between the financial statement and tax basis of assets and liabilities at enacted statutory tax rates in effect for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income or reversal of deferred tax liabilities during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based on this consideration, the Company anticipates that it is more likely than not that the net deferred tax assets will not be realized, and a valuation allowance has been recorded against the net deferred tax assets at January 31, 2007 and January 31, 2006. At January 31, 2007, the Company had net operating losses carried forward for federal and state income tax purposes, expiring at various dates through 2027 if not utilized. Federal net operating losses that can potentially be carried forward total approximately $15,409,000 at January 31, 2007. State net operating losses that can potentially be carried forward total approximately $32,791,000 at January 31, 2007.

Industry Overview

As discussed above, the commercial furniture markets, including Virco's core school markets, suffered from the recent economic downturn. The financial difficulties experienced by our core education customers derive primarily from budgetary pressures and shortfalls at state and local government levels. The state and local budgets have improved in recent years, but still remain pressured by costs related to medical care and unfunded pension obligations.

Funding for school furniture comes from two primary sources. The first source is from bonds issued to fund new school construction, make major renovations of older schools, and fully equip new and renovated schools. Funding from bond financing has been relatively stable during the past years. The second source is the general operating fund, which is a primary source of replacement furniture. The decline in Virco's sales in recent years is primarily attributable to sharp reductions in replacement furniture purchased from the general fund. Approximately 80-85% of a school's budget is spent on salaries and benefits for teachers and administrators. In times of budget shortfalls, schools traditionally attempt to retain teachers and spend less on repairs, maintenance, and replacement furniture.

While the short-term economic conditions impacting our core customer base are not overwhelmingly positive, there are certain underlying demographics, customer responses, and changes in the competitive landscape that provide opportunities. First, the underlying demographics of the student population are very stable compared to the volatility of furniture purchases. The student population grows slowly. The volatility is attributable to the financial health of the school systems. Virco management believes that there is a pent-up demand for quality school furniture. Second, management believes that parents and voters will demand that we educate our children and make this an ongoing priority for future government spending. Third, many schools have responded to the budget strains by reducing their support infrastructure. School districts historically have operated central warehouses and professional purchasing departments in a central business office. In order to retain teaching staff, many school districts have shut down the warehouses and reduced their purchasing departments and janitorial staffs. This change provides opportunities to sell services to schools, such as project management for new or renovated schools, delivery to individual school sites rather than truckload deliveries to central warehouses, installation of furniture in classrooms, and opportunities to provide a complete product assortment allowing one-stop shopping as opposed to sourcing furniture needs from a variety of suppliers. Fourth, many suppliers have shut down or dramatically curtailed their domestic manufacturing capabilities, making it difficult for competitors to provide custom colors or finishes during a tight seasonal summer delivery window when they are reliant upon a supply chain extending to China. Finally, the financial health of the competition, both manufacturers and dealers, has been adversely impacted by the downturn in the school furniture business, creating opportunities for suppliers that can provide dependable delivery of quality product and services.

Virco Response to the Industry Environment

In response to robust industry growth during the mid-to-late 1990s, Virco built and equipped a large new furniture manufacturing and distribution facility in Conway, Arkansas, that initiated operations in 1999 and 2000. In addition to that significant capital expansion of physical capacity, the Company implemented an SAP ERP system in 1999 in response to Y2K concerns coupled with limitations to its legacy computer system. The timing of these large capital investments was unfortunate, as the economic downturn discussed above initiated approximately one year after this new capacity came on line.

In response to the volatile changes in what has traditionally been a relatively stable market, Virco has pursued a variety of programs to improve its competitive position in the market, to reduce its cost structure to be appropriate for reduced sales volume, and to position the Company for growth in volume and market share as the industry recovers.

In response to the sharp decline in sales, many furniture manufacturers responded by shutting down significant portions of their manufacturing capacity and laying off thousands of workers, incurring large restructuring charges in the process. Because the education market was not impacted as rapidly as the commercial markets, in the first two years of this recession, Virco responded with a different approach designed to preserve the Company's manufacturing and distribution infrastructure and save the jobs of Virco's trained workforce. The Company used a variety of tactics to reduce spending. Capital expenditures were severely curtailed. During 2006 capital expenditures were approximately 50% of depreciation and during 2005 capital expenditures were approximately 40% of depreciation These expenditures were reduced to approximately one-quarter of depreciation expense in 2004, 2003 and 2002, and one-third of depreciation expense in 2001. While expenditures on capital equipment have been curtailed, aggressive maintenance programs, complimented with opportunistic purchases of good quality used equipment have enhanced the Company's productive capabilities. The Company embraced its ATS operating model, which facilitated reductions in inventory levels and improved levels of customer service. To control and reduce the cost of Virco's workforce, the Company used traditional measures such as wage freezes and hiring freezes, as well as more creative measures that addressed the unique demands of a highly seasonal business, including programs to encourage workforce flexibility.

The tactics used by Virco to reduce capital investment were supplemented with reductions in its workforce. In 2003 Virco implemented a voluntary separation program, which was accepted by 485 employees (25% of the workforce) in the second quarter. In the third quarter, the Company laid off an additional 160 employees. During 2005, the Company completed what management is confident will be the final reduction in force by laying off approximately 100 employees. The cumulative result of these six years of cost reductions has been significant. Virco's headcount of permanent employees has declined from a peak of nearly 2,950 in August 2000 to a total of approximately 1,200 permanent employees at January 31, 2007. Factory overhead, which peaked at over $72 million in fiscal year ended January 31, 2001, was approximately

$47 million in fiscal year ended January 31, 2007. For the fiscal year ended January 31, 2007, factory overhead as a percentage of sales is less than it was prior to the significant capital expenditures in 1998, 1999, and 2000, despite the reduction in sales volume. Virco has accomplished this without closing factories and without closing any of the primary distribution facilities. Selling, general, and administrative expenses, which do not fluctuate significantly with volume have declined by approximately $15 million from their peak and currently represent a lower percentage of sales as in 2000, despite our reduced sales volume.

In addition to significant cost reductions, the Company has made several investments in both product and process to strengthen its competitive position. During the last five years, Virco has completed three modest acquisitions, all within the constrained capital expenditure budgets discussed above. The first acquisition was Furniture Focus™, a reseller of FF&E that was a former Virco customer. The acquisition of Furniture Focus included their proprietary PlanSCAPE® software, used to bid and manage projects to furnish all items in the FF&E budget category of a new school project. Over the past five years, Furniture Focus has been integrated into Virco, and at the February 2006 sales meeting, a new release of the PlanSCAPE software was rolled out to the entire Virco sales force. Virco has embraced the relationships Furniture Focus had developed with other furniture manufacturers that provide FF&E not manufactured by Virco. Virco has incorporated these items into our product offering, enabling Virco to provide one-stop shopping for FF&E needs.

In addition to Furniture Focus, Virco has acquired assets from two furniture component manufacturers. While the production of many furniture components has moved to low-cost locations such as China, many components are too bulky to import on a cost-effective basis. In 2003, Virco purchased assets and intellectual property of Corex Products, Inc., a component manufacturer of compression-molded parts. The acquired equipment was integrated into our existing compression-molding facility in Conway, Arkansas. In 2005, Virco purchased substantial injection-molding capacity from a former supplier, allowing Virco to bring the production of certain high-volume components in house. These machines have been integrated into our Conway, Arkansas facility.

Finally, during the past five years of cost reductions, Virco has continued to invest in new products, including our successful ZUMA® and ZUMAfrd™ lines of education furniture. Initiatives to improve product and service quality have been successful, and the Company has improved its track record for dependable on-time delivery of product during the tight summer delivery window.

The Company's significant improvement in operating results for 2006 reflected the cumulative effect of three years of price increases and several rounds of cost reductions. In 2006, the Company significantly raised prices and introduced tiered pricing under its most significant contracts to cover the costs of servicing small orders. This followed two years of increased prices in 2005 and 2004. The cumulative effect of three years of price increases was adequate to cover the increased cost of raw materials, and gross margins return to more typical levels compared to historic norms.

The Company's lack of financial performance during 2005 and 2004 was attributable to the consequences of annual fixed-price contracts, coupled with extraordinary volatility in our most significant commodity and energy costs. During the past five years, it has been difficult to raise prices in the midst of the most significant sales downturns we have ever experienced. In 2004, the Company did not charge high-enough prices to cover the variable cost of services, especially related to small orders delivered to customer locations. This was exacerbated with the extreme increase in steel and other commodity costs. For 2005, the Company raised prices, but not enough. Continued commodity cost increases, fueled by petroleum-related costs for plastics and fuel, accompanied by supply chain disruptions related to Gulf Coast hurricanes, adversely impacted operating margins.

For 2007, the Company has raised prices modestly, and retained tiered pricing under its most significant contracts to cover the costs of servicing small orders. The Company is hopeful that this more modest price increase, coupled with our comprehensive product assortment, newly developed product offerings, and dependable delivery and service will allow the Company to increase market share while retaining the margins achieved in 2006.

Results of Operations (2006 vs. 2005)

Financial Results and Cash Flow

For the year ended January 31, 2007, the Company earned net income of $7,545,000 on net sales of $223,107,000 compared to a net loss of $9,574,000 on net sales of $214,450,000 in the same period last year. The net income was $0.56 per share for the year ended January 31, 2007, compared to a net loss of $0.73 per share in the prior year. Cash flow from operations was $10,915,000 compared to $304,000 in the prior year.

Sales

Virco's sales increased by 4.0% in 2006 to $223,107,000 compared to $214,450,000 in 2005. The increased sales volume was attributable to increased prices, offset by a slight decline in unit volume. The Company benefited from increased project sales and increased sales through commercial channels. Sales of Virco's new ZUMA product line increased, but were offset by reductions in older product lines.

For 2007 the Company will raise selling prices moderately to cover the anticipated increased cost of raw materials and freight expenses. The Company continues to emphasize the value of Virco's products, the value of Virco's distribution and delivery capabilities, and the value of timely deliveries during the peak seasonal delivery period. The Company is hopeful that the moderate increase in prices, combined with superior product and service will allow the Company to increase unit volume and maintain the gross margin levels achieved in 2006.

Cost of Sales

Cost of sales was 65% of sales in 2006 and 70% of sales for 2005. This significant improvement was achieved by increased prices combined with moderate growth in material costs and controlled spending on manufacturing costs. At the beginning of 2006, the Company raised prices with the intent of covering the increased cost of raw materials experienced in 2005 and 2004. The Company was successful in raising prices, and achieved that goal while incurring a modest reduction in unit volume, primarily in older commodity items that sell for lower prices.

In 2007, the Company intends to maintain the improved overhead cost structure attained through the restructurings in 2005 and 2003. Because the Company has improved its financial strength, we are able to finance our production of inventory for summer delivery earlier in the year. This allows a larger portion of annual production by permanent employees, who tend to be more efficient and produce better quality than temporary labor.

The Company intends to more tightly integrate the ATS model with our marketing programs, product development programs, and product stocking plan. This anticipated improvement in execution of ATS should allow the Company to offer a wide variety of product while improving on-time delivery performance. Although the Company is beginning the year with more inventory, production levels, which will vary depending upon selling volumes, are anticipated to be comparable to 2006.

The Company anticipates continued uncertainty and upward pressure on costs, particularly in the areas of certain raw materials, transportation, energy, and employee benefits in the coming year. Raw material costs continue to be less volatile that 2005 and 2004, but remain high. For more information, please see the section below entitled "Inflation and Future Change in Prices".

Selling, General and Administrative and Others

Selling, general and administrative expenses for the year ended January 31, 2007, excluding severance costs, decreased by approximately $3 million, and were 29.9% as a percentage of sales as compared to 32.8% in 2005 (excluding severance costs). Freight costs decreased both in dollars and as a percentage of sales. Installation costs increased in both dollars and as a percentage of sales due to increased project orders, and selling expenses decreased in dollars and as a percentage of sales.

For 2007, the Company intends to raise selling prices moderately to cover anticipated increased raw material costs as well as maintaining tiered pricing to increase prices on smaller orders and orders requiring full service. If successful, this should cause freight and installation costs to decline as a percentage of sales in 2007, but there can be no assurance of attaining a reduction due to volatility in fuel and freight rates as well as fluctuations in the portion of business requiring full service.

Interest expense was nearly $534,000 more than the prior year. Borrowing levels were slightly higher than the prior year, and interest rates were higher. In 2007, the Company anticipates lower average borrowing levels and a decrease in the average interest rate paid.

Results of Operations (2005 vs. 2004)

Financial Results and Cash Flow

For the year ended January 31, 2006, the Company had a net loss of $9,574,000 on net sales of $214,450,000 compared to a net loss of $13,995,000 on net sales of $199,854,000 in the same period last year. The loss was $0.73 per share for the year ended January 31, 2006, compared to a net loss of $1.07 per share in the prior year. Cash flow from operations was $304,000 compared to $3,678,000 in the prior year. During 2005, the Company incurred a large operating loss, yet managed to finish the year with cash flow from operations being slightly positive. To accomplish this, the Company was able to substantially finance the increase in inventory with vendor credit. The Company limited capital expenditures to $3,470,000 compared to depreciation expense of $8,844,000.

Sales

Virco's sales increased by 7.3% in 2005 to $214,450,000 compared to $199,854,000 in 2004. As discussed above, the furniture industry stabilized in 2005 and 2004 after three consecutive years of decline. The increased sales volume was attributable to increased prices, offset by a slight decline in unit volume. The Company benefited from increased project sales and increased sales through commercial channels. Sales of Virco's new ZUMA® product line increased significantly, but were offset by reductions in older product lines.

For 2006 the Company significantly raised selling prices to cover the cumulative impact of the increased cost of raw materials and freight expenses that had adversely impacted the last two years' financial results. The Company continued to emphasize the value of Virco's products, the value of Virco's distribution and delivery capabilities, and the value of timely deliveries during the peak seasonal delivery period. Although this policy may have had an adverse effect on unit volume, the Company intended for the policy to restore its gross margins to levels that restored profitable operations.

Cost of Sales

Cost of sales was 70% of sales in 2005 and 72% of sales for 2004. The cost of sales in total was slightly improved, but the components of the cost varied in 2005 compared to 2004. At the beginning of 2005, the Company raised prices with the intent of covering the increased cost of raw materials experienced in 2004. The Company was successful in raising prices, but did not raise them enough to recover the cumulative impact of increased material costs compounded with the increases incurred in 2005. As a percentage of sales, material cost increased in 2005, but was offset by reduced direct labor and overhead costs, resulting in a net improvement in gross margin.

Selling, General and Administrative and Others

Selling, general and administrative expenses for the year ended January 31, 2006, excluding severance costs, increased by approximately $2 million, but were 32.8% as a percentage of sales as compared to 34.1% in 2004. Freight costs were flat and decreased slightly as a percentage of sales. Freight costs were adversely impacted by increased fuel rates, offset by a reduction in the numbers of smaller orders delivered to customers. Installation costs increased as a result of increased project orders, and selling expenses increased as a result of variable sales costs and rebates paid to customers.

Interest expense was nearly $1,200,000 more than the prior year. Borrowing levels were slightly higher than the prior year, and interest rates were higher.

Provision for Income Taxes

The Company recognizes deferred income taxes under the asset and liability method of accounting for income taxes in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 109, "Accounting for Income Taxes". Deferred income taxes are recognized for differences between the financial statement and tax basis of assets and liabilities at enacted statutory tax rates in effect for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income or reversal of deferred tax liabilities during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based on this consideration, the Company anticipates that it is more likely than not that the net deferred tax assets will not be realized, and a valuation allowance has been recorded against the net deferred tax assets at January 31, 2007 and January 31, 2006.

At January 31, 2007, the Company had net operating losses carried forward for federal and state income tax purposes, expiring at various dates through 2026 if not utilized. Federal net operating losses that can potentially be carried forward total approximately $15,409,000 at January 31, 2007. State net operating losses that can potentially be carried forward total approximately $32,791,000 at January 31, 2007.

For the fiscal year ended January 31, 2007, the Company benefited from net operating loss carryforwards for both federal and state income taxes, and recognized an income tax expense of $446,000. The income tax expense is primarily attributable to alternative minimum taxes combined with income and franchise taxes as required by various states. For the fiscal year ended January 31, 2006, the Company incurred an income tax benefit of $109,000 due to an adjustment of deferred tax reserves partially offset by income and franchise taxes as required by various states.

Liquidity and Capital Resources

Working Capital Requirements

Virco addresses liquidity and capital requirements in the context of short-term seasonal requirements and the long-term capital requirements of the business. The Company's core business of selling furniture to publicly funded educational institutions is extremely seasonal. The seasonal nature of this business permeates most of Virco's operational, capital, and financing decisions.

The Company's working capital requirements during and in anticipation of the peak summer season oblige management to make estimates and judgments that affect Virco's assets, liabilities, revenues and expenses. Management expends a significant amount of time during the year, and especially in the first quarter, developing a stocking plan and estimating the number of employees, the amount of raw materials, and the types of components and products that will be required during the peak season. If management underestimates any of these requirements, Virco's ability to fill customer orders on a timely basis or to provide adequate customer service may be diminished. If management overestimates any of these requirements, the Company may be required to absorb higher storage, labor and related costs, each of which may affect profitability. On an ongoing basis, management evaluates such estimates, including those related to market demand, labor costs, and inventory levels, and continually strives to improve Virco's ability to correctly forecast business requirements during the peak season each year.

As part of Virco's efforts to address seasonality, financial performance and quality without sacrificing service or market share, management has been refining the Company's ATS operating model. ATS is Virco's version of mass-customization, which assembles standard, stocked components into customized configurations before shipment. The Company's ATS program reduces the total amount of inventory and working capital needed to support a given level of sales. It does this by increasing the inventory's versatility, delaying assembly until the last moment, and reducing the amount of warehouse space needed to store finished goods.

In addition, Virco finances its largest balance of accounts receivable during the peak season. This occurs for two primary reasons. First, accounts receivable balances naturally increase during the peak season as shipments of products increase. Second, many customers during this period are government institutions, which tend to pay accounts receivable more slowly than commercial customers.

As the capital required for the summer season generally exceeds cash available from operations, Virco has historically relied on third-party bank financing to meet seasonal cash flow requirements. Virco has established a long-term relationship with its primary lender, Wells Fargo Bank. On an annual basis, the Company prepares a forecast of seasonal working capital requirements, and renews its revolving line of credit. For fiscal 2007, Virco has entered into a revolving credit facility with Wells Fargo Bank, amended and restated March 26, 2007, which provides a term loan of $20,000,000 and a secured revolving line of credit that varies with levels of inventory and receivables, up to a maximum of $40,000,000, with the maximum borrowing increasing to $50,000,000 during certain months of the year. The term loan is a two-year line amortizing at $10,000,000 per year with interest payable monthly at a fluctuating rate equal to the Bank's prime rate plus 1/2%. The revolving line has a 23-month maturity with interest payable monthly at a fluctuating rate equal to the Bank's prime rate plus a margin of 1/2%. The revolving line typically provides for advances of 80% on eligible accounts receivable and 20% – 60% on eligible inventory. The line of credit is secured by the Company's accounts receivable, inventories, and equipment and property. The credit facility with Wells Fargo Bank is subject to various financial covenants and places certain restrictions on capital expenditures, new operating leases, dividends and the repurchase of the Company's common stock. In addition, there is a "clean down" provision that requires the Company to reduce borrowings under the line to less than $30 million for a period of 90 days at year end. The Company believes that normal operating cash flow will allow us to meet the "clean down" requirement with no adverse impact on the Company's liquidity. Approximately $14,605,000 was available for borrowing as of January 31, 2007.

During 2006 the Company strengthened its balance sheet and increased liquidity through three primary methods. First, the Company raised approximately $4.7 million through a private placement of equity. Second, the Company earned an after tax profit of approximately $7.5 million. Third, our continued disciplines over capital expenditures resulted in depreciation expense in excess of capital expenditures by approximately $3.6 million. This improved financial strength allowed the Company to run the factories at increased levels of production during the fourth quarter. It is the Company's intent to run production at a more level rate while building for the summer of 2007. This will allow us to use our permanent work force to build component inventory early in the year, relying less on relatively inefficient temporary labor to increase production rates closer to the summer.

During fiscal years 2005 and 2004, the Company incurred operating losses, yet managed to have positive cash flow from operations. This was accomplished through the following actions. In 2005, the Company spent $3.5 million on capital expenditures compared to $8.8 million of depreciation expense. Increases in inventory were substantially financed by increases in vendor credit. In 2004, the Company spent $2.8 million on capital expenditures, compared to depreciation expense of $9.8 million. In addition, receivables were reduced by over $1 million and inventories were reduced by nearly $2.5 million. Some of these actions are one-time events, and will not be repeated in future years. The only anticipated recurring event is the excess of depreciation over capital expenditures. The Company is budgeting for capital expenditures to be less than depreciation for fiscal year 2007, and the amount of cash generated is expected to be approximately $3-4 million.

As a result of the increased material costs previously described, the Company violated debt covenants related to the line of credit with Wells Fargo at the end of the third quarter of 2005. The violation of covenants was waived at the end of the quarter, and the Company re-negotiated its line of credit with the bank effective December 6, 2005. As a result of the increased material costs previously described, the Company violated debt covenants related to the line of credit with Wells Fargo and at the end of the third quarter of 2004. The violation of covenants was waived at the end of the quarter, and the Company re-negotiated its line of credit with the bank effective January 21, 2005.

Management believes cash generated from operations and from the previously described sources will be adequate to meet its capital requirements in the next 12 months.

Long-Term Capital Requirements

In addition to short-term liquidity considerations, the Company continually evaluates long-term capital requirements. From 1997 through 2000, the Company completed two large capital projects, which have had significant effects on cash flow for the past six years. The first project was the implementation of the SAP enterprise resources planning system. The second project was the expansion and re-configuration of the Conway, Arkansas, manufacturing and distribution facility.

Upon completion of these projects, the Company dramatically reduced capital spending. During 2001, 2002, 2003, and 2004 capital expenditures ranged from one-quarter to one-third of depreciation expense. During 2006 capital expenditures were approximately 53% of depreciation and 2005 capital expenditures were approximately 40% of depreciation.

Management intends to limit future capital spending until growth in sales volume fully utilizes the new plant and distribution capacity. The Company has established a goal of limiting capital spending to less than $3,000,000 for 2007, which is slightly less than one-half of anticipated depreciation expense.

Asset Impairment

In 2002, Virco acquired certain assets of Furniture Focus™, including its proprietary PlanSCAPE® software. As part of this acquisition, the Company recorded goodwill of $2,200,000. During the period from 2003 to 2005, the Company rolled out the Furniture Focus package business nationwide and expended significant effort training the sales force in package selling. In 2006, Virco released the next generation of the PlanSCAPE software and for 2007 the Company anticipates several enhancements to PlanSCAPE. Virco evaluates the impairment of goodwill at least annually, or when indicators of impairment occur. As of January 31, 2007, there has been no impairment to the goodwill recorded.

In December 2003, Virco acquired certain assets of Corex Products, Inc., a manufacturer of compression-molded components, for approximately $1 million. The assets have been transferred to the Company's Conway, Arkansas, location where they have been integrated with Virco's existing compression-molding operation. In connection with this acquisition, Virco acquired certain patents and other intangible assets. As of January 31, 2007, there has been no impairment to the intangible assets recorded.

Virco made substantial investments in its infrastructure in 1998, 1999, and 2000. The investments included a new factory, new warehouse, and new production and distribution equipment. The factory, warehouse, and equipment acquired are used to produce, store, and ship a variety of product lines, and the use of any one piece of equipment is not dependent on the success or volume of any individual product. New products are designed to use as many common or existing components as practical. As a result, both our ATS inventory components and the machines used to produce them become more versatile. Virco evaluates the potential for impaired assets on a quarterly basis. As of January 31, 2007, there has been no impairment to the long-term assets of the Company.

Contractual Obligations

The Company leases manufacturing, transportation, and office equipment, as well as real estate under a variety of operating leases. The Company leases substantially all vehicles, including trucks and passenger cars under operating leases where the lessor provides fleet management services for the Company. The fleet management services provide Virco with operating efficiencies relating to the acquisition, administration, and operation of leased vehicles. The use of operating leases for manufacturing equipment has enabled the Company to qualify for and use Industrial Revenue Bond financing. Real estate leases have been used where the Company did not want to make a long-term commitment to a location, or when economic conditions favored leasing. The Torrance manufacturing and distribution facility is leased under an operating lease through 2010. The Company has one five-year option to extend the lease. The Company does not have any lease obligations or purchase commitments in excess of normal recurring obligations. Leasehold improvements and tenant improvement allowances are depreciated over the lesser of the expected life of the asset or the lease term.

Contractual Obligations Payments Due by Period

In thousands	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-term debt obligations	$ 15,083	$ 5,012	$ 10,024	$ 24	$ 23
Interest on long-term debt obligations	2,201	439	1,754	4	4
Capital lease obligations	181	62	119	—	—
Operating lease obligations	16,653	6,244	9,008	1,401	—
Purchase obligations	18,094	18,094	—	—	—
Other long-term obligations	—	—	—	—	—
	$ 52,212	$ 29,850	$ 20,906	$ 1,429	$ 27

Virco's largest market is publicly funded school districts. A significant portion of this business is awarded on a bid basis. Many school districts require that a bid bond be posted as part of the bid package. In addition to bid bonds, many districts require a performance bond when the bid is awarded. At January 31, 2007, the Company had bonds outstanding valued at approximately $1,900,000. To the best of management's knowledge, in over 57 years of selling to schools, Virco has never had a bid or performance bond called.

The Company provides a warranty against all substantial defects in material and workmanship. In 2005 the Company extended its standard warranty from five years to 10 years. The Company's warranty is not a guarantee of service life, which depends upon events outside the Company's control may be different from the warranty period. The Company accrues an estimate of its exposure to warranty claims based upon both product sales data, and an analysis of actual warranty claims incurred. At the current time, management cannot reasonably determine whether warranty claims for the upcoming fiscal year will be less than, equal to, or greater than warranty claims incurred in 2006. The following is a summary of the Company's warranty-claim activity during 2006 and 2005.

	January 31, 2007	January 31, 2006
Beginning balance	$ 1,500	$ 1,500
Provision	1,154	900
Costs incurred	(904)	(900)
Ending balance	$ 1,750	$ 1,500

Retirement Obligations

The Company provides retirement benefits to employees and non-employee directors under three defined benefit retirement plans; the Virco Employee's Retirement Plan, the Virco Important Performers (VIP) Retirement Plan, and the Retirement Plan for Non-Employee Directors. The Virco Employee Retirement Plan is a qualified retirement plan that is funded through a trust held at Wells Fargo Bank (Trustee). The other two plans are non-qualified retirement plans. The VIP Plan is secured by life insurance policies held in a rabbi trust and the Plan for Non-Employee Directors is not funded.

For 2006, the Company used a 5.75% discount rate. For 2005 and 2004, the Company used a 6.5% discount rate. For 2006, 2005 and 2004 the Company used a 6.5% expected return on plan assets and a 5.0% expected rate of increase in compensation.

Three significant events occurred during 2003 that affected the retirement plans. First, approximately 40% of Virco's employees severed their employment with Virco during the year. The majority of these employees accepted a voluntary severance package. This severance was treated as plan curtailment. Second, a significant number of employees that severed their employment elected a lump sum benefit. During 2003 the pension trust disbursed approximately $6.3 million to severed employees. These distributions were accounted for as a plan settlement. Finally, effective December 31, 2003, Virco froze all future benefit accruals under the plans. Employees can continue to vest under the benefits earned to date, but no covered participants will earn additional benefits under the plan freeze. As a result of these activities, Virco incurred additional pension expense of approximately $1,250,000 related to the plan curtailment, additional pension expense of approximately $1,540,000 related to the plan settlement, and additional pension expense of approximately $40,000 related to the plan freeze. As a result of the freeze, the projected benefit obligation decreased by approximately $7,500,000. The plan freeze is not intended to be permanent. It is management's intention to restore some form of a retirement benefit when the Company's profitability and cash flow allow.

During 2006, 2005, and 2004, the Company's results of operations and financial position did not allow for a retirement benefit to be restored. Benefit accruals under the plans have remained frozen. For 2006, 2005, and 2004, expenses related to the pensions decreased by more than $6 million compared to 2003.

It is the Company's intent to maintain the funded status of the qualified plan at a minimum of 90% of the current liability as determined by the plan's actuaries. The Company made no contributions to the pension trust during 2006 or 2005. Contributions during 2007 will depend upon actual investment results and benefit payments. During 2006, 2005, and 2004, the Company paid approximately $255,000 per year under the non-qualified plans. It is anticipated that contributions for 2007 will be comparable.

During 2006, the Company implemented SFAS No. 158 Employers Accounting for Defined Benefit Pension and Other Postretirement Plans. The implementation of this standard did not impact pension expense for the year. As a result of implementing SFAS No. 158, accrued pension liability increased by approximately $1.9 million, offset by an increase in other comprehensive loss. At January 31, 2007, accumulated other comprehensive loss of approximately $7.6 million is attributable to the pension plans.

The Company does not anticipate making any significant changes to the pension assumptions in the near future. If the Company were to have used different assumptions in the fiscal year ended January 31, 2007, a 1% reduction in investment return would have increased expense by approximately $100,000, a 1% change in the rate of compensation increase would had no impact, and a 1% reduction in the discount rate would have increased expense by $300,000. A 1% reduction in the discount rate would have increased the PBO by approximately $3.4 million. If Virco elected to make the plan freeze permanent, pension expense would decrease by approximately $75,000. Refer to Note 4 to the consolidated financial statements for additional information regarding the pension plans and related expenses.

Stockholders' Equity

From April 1998 to December 2002, the Board of Directors approved and expanded a stock buy-back program giving the Company authorization to buy back up to $22,000,000 of Company stock. As of the end of January 2004, the Company had repurchased approximately 1,454,000 shares at a cost of approximately $18,788,000. During 2004, the Company retired the shares of treasury stock. The Company's current line of credit with Wells Fargo Bank does not allow for repurchases of stock. When the results of operations and cash flow allow, the Company will re-evaluate the stock buy-back program if permitted under the Wells Fargo Bank line of credit. The Company did not repurchase any shares of stock during 2006, 2005 and 2004.

Prior to 2003, Virco had established a track record of paying cash dividends to its stockholders for more than 20 consecutive years. As a result of the recent operating losses, the Company discontinued paying dividends in the second quarter of 2003. The current line of credit with Wells Fargo Bank does not allow for cash dividends. When the results of operations, cash flow, and loan covenants allow, the Company intends to reinstate the cash dividend policy if permitted under the Wells Fargo Bank line of credit

Virco issued a 10% stock dividend or 3/2 stock split every year beginning in 1982 through 2002. Although the stock dividend has no cash consequences to the Company, the accounting methodology required for 10% dividends has affected the equity section of the balance sheet. When the Company records a 10% stock dividend, 10% of the market capitalization of the Company on the date of the declaration is reclassified from retained earnings to additional paid-in capital. During the period from 1982 through 2002, the cumulative effect of the stock dividends has been to reclassify over $122 million from retained earnings to additional paid-in capital. The equity section of the balance sheet on January 31, 2007, reflects additional paid-in capital of approximately $114 million and deficit retained earnings of approximately $57 million. Other than the losses incurred during 2003, 2004, and 2005, the retained deficit is a result of the accounting reclassification, and is not the result of accumulated losses.

On June 6, 2006, the Company sold 1,072,041 shares of its common stock (the "Shares"), and warrants to purchase 268,010 shares of its common stock, to WEDBUSH, Inc. and clients of Wedbush Morgan Securities, Inc. for an aggregate purchase price of $5 million, or $4.66 per Share (the "Per Share Purchase Price"). On June 26, 2006, the Company entered into a follow-on investment agreement with certain directors and members of management. The investment with directors and management was made under substantially the same terms but at a higher price, for the issuance of 57,455 shares of common stock and 14,363 warrants, yielding proceeds of approximately $288,000. The investment with directors and managers was completed subsequent to October 31, 2006. The Company incurred approximately $481,000 in closing costs which were netted against the proceeds received from the sale of shares. The cash received from the shares of stock was used to strengthen the balance sheet and finance seasonal business activities.

Environmental and Contingent Liabilities

The Company and other furniture manufacturers are subject to federal, state, and local laws and regulations relating to the discharge of materials into the environment and the generation, handling, storage, transportation, and disposal of waste and hazardous materials. In addition to policies and programs designed to comply with environmental laws and regulations, Virco has enacted programs for recycling and resource recovery that have earned repeated commendations, including the 2005 and 2004 California Waste Reduction Awards Program, designation in 2003 as a Charter Member of the WasteWise Hall of Fame, in 2002 as a WasteWise Partner of the Year, and in 2001 as a WasteWise Program Champion for Large Businesses by the United States Environmental Protection Agency. Despite these significant accomplishments, environmental laws have changed rapidly in recent years, and Virco may be subject to more stringent environmental laws in the future. The Company has expended, and expects to continue to spend, significant amounts in the future to comply with environmental laws. Normal recurring expenses relating to operating our factories in a manner that meets or exceeds environmental laws are matched to the cost of producing inventory. Despite our significant dedication to operating in compliance with applicable laws, there is a risk that the Company could fail to comply with a regulation or that applicable laws and regulations change. On these occasions, the Company records liabilities for remediation costs when remediation costs are probable and can be reasonably estimated.

In 2006 and 2005, the Company was self-insured for product liability losses up to $500,000 per occurrence, for workers compensation losses up to $250,000 per occurrence, and for auto liability up to $50,000 per occurrence. In prior years the Company has been self-insured for workers compensation, automobile, product, and general liability losses. The Company has purchased insurance to cover losses in excess of the self-insured retention or deductible up to a limit of $30,000,000. For the insurance year beginning April 1, 2007, the Company will be self-insured for product liability losses up to $250,000 per occurrence, for workers compensation losses up to $250,000 per occurrence, and for auto liability up to $50,000 per occurrence. In future years, the Company's exposure to self-insured retentions will vary depending upon the market conditions in the insurance industry and the availability of cost-effective insurance coverage.

During the past 10 years the Company has aggressively pursued a program to improve product quality, reduce product liability claims and losses, and to more aggressively litigate product liability cases. This program has continued through 2007 and has resulted in reductions in product liability claims and litigated product liability cases. In addition, the Company has active safety programs to improve plant safety and control workers compensation losses. Management does not anticipate that any related settlement, after consideration of the existing reserves for claims and potential insurance recovery, would have a material adverse effect on the Company's financial position, results of operations, or cash flows.

Off-Balance Sheet Arrangements

The Company did not enter into any material off-balance sheet arrangements during its 2006 fiscal year, nor did the Company have any material off-balance sheet arrangements outstanding at January 31, 2007.

New Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments" (SFAS 155). SFAS 155 establishes, among other things, the accounting for certain derivatives embedded in other financial instruments. This statement permits fair value remeasurement for any hybrid financial instrument containing an embedded derivative that would otherwise require bifurcation. It also requires that beneficial interests in securitized financial assets be accounted for in accordance with SFAS No. 133. SFAS 155 is effective for fiscal years beginning after September 15, 2006, and is not expected to have a material impact on the Company's financial operations or financial positions.

In July 2006, the Financial Accounting Standards Board issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109 ("FIN 48"), which clarifies what criteria must be met prior to recognition of the financial statement benefit of a position taken in a tax return. The Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Also, the Interpretation provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The adoption of FIN 48 will be effective for years beginning after December 15, 2006, and the Company will be required to adopt this Interpretation in the first quarter of 2007. Based on the Company's evaluation as of January 31, 2007, FIN 48 is not expected to have a material impact.

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements ("SFAS 157") which provides enhanced guidance for using fair value to measure assets and liabilities. The standard also expands the amount of disclosure regarding the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently reviewing the impact, if any, that SFAS 157 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158 Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R) ("SFAS 158"). This statement requires an employer that is a business entity to recognize in its balance sheet the over-funded or under-funded status of a defined benefit postretirement plan measured as the difference between the fair value of plan assets and the benefit obligation. The recognition of the net liability or asset will require an offsetting adjustment to accumulate other comprehensive income in shareholders' equity. SFAS 158 does not change how pensions and other postretirement benefits are accounted for and reported in the income statement. This statement is effective for fiscal years ending after December 15, 2006, and measurement elements to be effective for fiscal years ending after December 15, 2008. The Company adopted the recognition provisions of SFAS No. 158 and applied them to the funded status of the its defined benefit plans resulting in a decrease in Shareholders Equity of $1.9 million. The Company will be required to apply the new standard for its 2006 year-end financial statements and recognize on the 2006 balance sheet the funded status of pension and other postretirement benefit plans.

In October 2006, the FASB ratified EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. This statement is effective for years beginning after December 15, 2007. This statement clarifies FASB 106, Employers Accounting for Post-Retirement Benefits other than Pensions, applies to endorsement split-dollar life insurance arrangements. The Company estimates that adoption of this statement will increase the Company's recorded liabilities by approximately $2 million with no impact to the statement of operations or cash flows of the Company. The Company has purchased life insurance policies that are designed to pay a death benefit that is greater than the promised retirement benefit.

Quantitative and Qualitative Disclosures about Market Risk

Inflation and Future Change in Prices

Inflation rates had a modest impact on the Company in 2006, and a significant impact on the results of operations for 2005 and 2004. During 2006, raw material prices increased, but the rate of increase and volatility of pricing was substantially more moderate when compared to the prior two years. During 2005 and 2004 the Company faced substantial increases in the cost of raw materials and energy, particularly steel, plastic, and diesel fuel. During the beginning of 2004, Virco incurred significant disruption in the supply of steel in addition to markedly higher prices. Significant purchases of steel by China, including both finished product and raw materials to produce steel, impacted the market for steel. In addition, a fire in one of the largest coal mines in the United States disrupted the supply of domestic steel. During 2004 the cost of steel nearly doubled. In addition to higher steel prices, the Company incurred increases in the prices of raw materials and operating expenses that are impacted by the cost of oil, especially plastics and freight expense. During 2005, the Company again incurred increased commodity prices and supply disruptions, primarily related to petroleum-related fuel and plastics. Steel, which has experienced volatile price increases in recent years remained expensive. Furthermore, one of the Company's significant suppliers of steel obtained 100% of a key component of their steel processing from the Gulf Coast region. Steel deliveries were disrupted as a result of the hurricanes. The Company uses large quantities of plastic to manufacture certain high-volume components. The Company's suppliers of plastic are concentrated in the Gulf Coast region. For a period of time during and after the storms, price, availability, and rail car delivery of plastic was adversely impacted.

For 2007, the Company anticipates continued upward pressure on costs, particularly in the areas of certain raw materials, transportation, energy and employee benefits. The price and supply of steel have stabilized compared to 2004 and 2005, but continue to be high. There is continued uncertainty on raw material costs that are affected by the price of oil, especially plastics. Transportation costs are also expected to be adversely affected by increased oil prices, in the form of increased operation costs for our fleet, and surcharges on freight paid to third-party carriers. Virco expects to incur continued pressure on employee benefit costs. Virco has aggressively addressed these costs by reducing headcount, freezing pension benefits, passing on a portion of increased medical costs to employees, and hiring temporary workers who are not eligible for benefit programs.

To recover the cumulative impact of increased costs, the Company raised the list prices for Virco's products in 2005 and 2006. A more modest price increase is anticipated for 2007. As a significant portion of Virco's business is obtained through competitive bids, the Company is carefully considering increased material costs in addition to increased transportation costs as part of the bidding process. Total material costs for 2007, as a percentage of sales, could be higher than in 2006, but it is the Company's intention to raise selling prices enough so that material costs, as a percentage of sales, will be comparable to the prior year. However, no assurance can be given that the Company will experience stable, modest or substantial increases in prices in 2007. The Company is working to control and reduce costs by improving production and distribution methodologies, investigating new packaging and shipping materials, and searching for new sources of purchased components and raw materials.

The Company uses the LIFO method of accounting for the material component of inventory. Under this method, the cost of products sold as reported in the financial statements approximates current cost, and reduces the distortion in reported income due to increasing costs. Depreciation expense represents an allocation of historic acquisition costs and is less than if based on the current cost of productive capacity consumed. In 2006, 2005, 2004, 2003, 2002 and 2001, the Company significantly reduced its expenditures for capital assets, but in the previous three fiscal years (1998, 1999, and 2000) the Company made the significant fixed-asset acquisitions described above. The assets acquired result in higher depreciation charges, but due to technological advances should result in operating cost savings and improved product quality. In addition, some depreciation charges were offset by a reduction in lease expense. The Company is also subject to interest rate risk related to its $15,000,000 of borrowings as of January 31, 2007, and any seasonal borrowings used to finance additional inventory and receivables. Rising interest rates may adversely affect the Company's results of operations and cash flows related to its variable-rate bank borrowings. Accordingly, a 100 basis point upward fluctuation in the lender's base rate would have caused the Company to incur additional interest charges of approximately $324,000 for the 12 months ended January 31, 2007. The Company would have benefited from a similar interest savings if the base rate were to have fluctuated downward by a like amount.

The Company has used derivative financial instruments to reduce interest rate risks. The Company does not hold or issue derivative financial instruments for trading purposes. All derivatives are recognized as either assets or liabilities in the statement of financial condition and are measured at fair value. At January 31, 2007 and 2006, the Company had no derivative instruments.

FIVE YEAR SUMMARY OF SELECTED FINANCIAL DATA

The following table sets forth selected historical consolidated financial data for the periods indicated. The following data should be read in conjunction with Item 8, Financial Statements and Supplementary Data, and with Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations in Virco's report on Form 10K.

In thousands except per share data	**2006**	2005	2004	2003	2002
Summary of Operations					
Net sales	**$ 223,107**	$ 214,450	$ 199,854	$ 191,852	$ 244,355
Net income (loss)	**$ 7,545**	$ (9,574)	$ (13,995)	$ (21,961)	$ 282
Income (loss) per share data					
Net income(loss) *(1)*					
Basic	**$ 0.56**	$ (0.73)	$ (1.07)	$ (1.68)	$ 0.02
Assuming dilution	**$ 0.55**	$ (0.73)	$ (1.07)	$ (1.68)	$ 0.02
Dividends declared per share, adjusted for 10% stock dividend					
Cash dividends *(3)*	**$ —**	$ —	$ —	$ 0.04	$ 0.08
Other Financial Data					
Total assets	**$ 116,277**	$ 114,720	$ 114,041	$ 126,268	$ 154,796
Working capital	**$ 22,994**	$ 15,488	$ 15,334	$ 25,404	$ 38,748
Current ratio	**1.6/1**	1.4/1	1.5/1	2.0/1	2.4/1
Total long-term obligations	**$ 30,101**	$ 38,862	$ 34,090	$ 37,934	$ 44,702
Stockholders' equity	**$ 48,878**	$ 39,100	$ 49,265	$ 62,352	$ 82,774
Shares outstanding at year-end *(3)*	**14,380**	13,137	13,098	13,096	13,111
Stockholders' equity per share *(2)*	**$ 3.40**	$ 2.98	$ 3.76	$ 4.76	$ 6.31

(1) Based on average number of shares outstanding each year after giving retroactive effect for stock dividends and stock split.

(2) Based on number of shares outstanding at year-end after giving effect for stock dividends and stock split.

(3) Adjusted for stock dividends and stock split.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of Virco Mfg. Corporation (the "Company") is responsible for establishing and maintaining adequate internal control over financial reporting and for the assessment of the effectiveness of internal control over financial reporting. As defined by the Securities and Exchange Commission, internal control over financial reporting is a process designed by, or supervised by, the Company's principal executive and principal financial officers, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles.

The Company's internal control over financial reporting is supported by written policies and procedures, that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the Company's assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of the Company's management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In connection with the preparation of the Company's annual financial statements, management of the Company has undertaken an assessment of the effectiveness of the Company's internal control over financial reporting as of January 31, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of the Company's internal control over financial reporting and testing of the operational effectiveness of the Company's internal control over financial reporting.

Based on this assessment, management did not identify any material weakness in the Company's internal control, and management has concluded that the Company's internal control over financial reporting was effective as of January 31, 2007.

Ernst & Young LLP, the independent registered public accounting firm that audited the Company's financial statements, has issued an attestation report on management's assessment of internal control over financial reporting, a copy of which is included in this Annual Report.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Board of Directors and Stockholders of Virco Mfg. Corporation

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that Virco Mfg. Corporation maintained effective internal control over financial reporting as of January 31, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Virco Mfg. Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Virco Mfg. Corporation maintained effective internal control over financial reporting as of January 31, 2007, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Virco Mfg. Corporation maintained, in all material respects, effective internal control over financial reporting as of January 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of January 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended January 31, 2007 of Virco Mfg. Corporation and our report dated April 12, 2007 expressed an unqualified opinion thereon.

Ernst & Young LLP

Los Angeles, California

April 12, 2007

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of Virco Mfg. Corporation

We have audited the accompanying consolidated balance sheets of Virco Mfg. Corporation as of January 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended January 31, 2007. Our audits also included the financial statement schedule listed in the Index at Items 15. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Virco Mfg. Corporation at January 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended January 31, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set for the therein.

As discussed in Notes 1 and 5 to the consolidated financial statements, on February 1, 2006, the Company changed its method of accounting for share-based payments in accordance with Statement of Financial Accounting Standards No. 123(R).

Additionally, as discussed in Notes 1 and 4 to the consolidated financial statements, on January 31, 2007, the Company changed its method of accounting for defined benefit pension plans in accordance with Statement of Financial Accounting Standards No. 158.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Virco Mfg. Corporation's internal control over financial reporting as of January 31, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 12, 2007 expressed an unqualified opinion thereon.

Ernst & Young LLP

Los Angeles, California

April 12, 2007

Consolidated Balance Sheets

In thousands, except share data	January 31, 2007	2006
Assets		
Current assets		
Cash	**$ 1,892**	$ 1,489
Trade accounts receivable (net of allowance for doubtful accounts of $200 in 2006 and 2005)	**18,596**	17,270
Other receivables	**228**	377
Inventories:		
Finished goods, net	**11,651**	11,070
Work in process, net	**19,690**	13,796
Raw materials and supplies, net	**6,496**	6,751
	37,837	31,617
Prepaid expenses and other current assets	**1,479**	1,493
Total current assets	**60,032**	52,246
Property, plant and equipment:		
Land and land improvements	**3,596**	3,591
Buildings and building improvements	**49,555**	49,581
Machinery and equipment	**109,730**	106,475
Leasehold improvements	**1,323**	1,289
	164,204	160,936
Less accumulated depreciation and amortization	**116,116**	109,513
Net property, plant and equipment	**48,088**	51,423
Goodwill and other intangible assets	**2,350**	2,350
Less accumulated depreciation and amortization	**39**	26
Net goodwill and other intangible assets	**2,311**	2,324
Other assets	**5,846**	8,727
Total assets	$ **116,277**	$ 114,720

See accompanying notes.

Consolidated Balance Sheets

	January 31,	
In thousands, except share data	**2007**	2006
Liabilities		
Current liabilities		
Checks released but not yet cleared bank	**$ 2,563**	$ 2,030
Accounts payable	**14,463**	17,504
Accrued compensation and employee benefits	**8,094**	6,047
Income tax payable	**989**	847
Current portion of long-term debt	**5,074**	5,012
Other accrued liabilities	**5,855**	5,318
Total current liabilities	**37,038**	36,758
Non-current liabilities		
Accrued self-insurance retention and other	**3,962**	2,703
Accrued pension expenses	**15,949**	14,618
Long-term debt, less current portion	**10,190**	21,541
Total non-current liabilities	**30,101**	38,862
Deferred tax liabilities	**260**	—
Commitments and contingencies		
Stockholders' equity		
Preferred stock:		
Authorized 3,000,000 shares, $.01 par value; none issued or outstanding	**—**	—
Common stock:		
Authorized 25,000,000 shares, $.01 par value; issued 14,379,506 shares in 2006 and 13,137,288 shares in 2005	**143**	131
Additional paid-in capital	**113,737**	108,143
Accumulated deficit	**(57,436)**	(64,981)
Accumulated comprehensive loss	**(7,566)**	(4,193)
Total stockholders' equity	**48,878**	39,100
Total liabilities and stockholders' equity	**$ 116,277**	$ 114,720

See accompanying notes.

Consolidated Statements of Operations

In thousands, except share data	2007	2006	2005
	Year ended January 31,		
Net sales	**$ 223,107**	$ 214,450	$ 199,854
Costs of goods sold	**144,495**	149,785	143,415
Gross profit	**78,612**	64,665	56,439
Selling, general and administrative expenses	**66,828**	70,271	68,229
Separation costs	**—**	742	—
Interest expense, net	**3,792**	3,258	2,090
Loss on sale of assets, net	**1**	77	—
Income (loss) before income taxes	**7,991**	(9,683)	(13,880)
Income expense (tax benefit)	**446**	(109)	115
Net income (loss)	**$ 7,545**	$ (9,574)	$ (13,995)
Net income (loss) per common share (a)			
Basic	**$ 0.56**	$ (0.73)	$ (1.07)
Diluted	**$ 0.55**	$ (0.73)	$ (1.07)
Weighted average shares outstanding			
Basic	**13,590**	13,114	13,112
Diluted	**13,611**	13,114	13,112

(a) Net loss per share was calculated based on basic shares outstanding due to the anti-dilutive effect on the inclusion of common stock equivalent shares.

See accompanying notes.

Consolidated Statements of Stockholders' Equity

In thousands, except share data	Shares	Amount	Additional Paid-in Capital	Retained Earnings (Deficit)	Comprehensive Income (Loss)	Treasury Stock	Accumulated Comprehensive Loss	Total
Balance at January 31, 2004	13,095,801	$ 146	$ 127,133	$ (41,412)	$ —	$ (19,271)	$ (4,244)	$ 62,352
Net loss	—	—	—	(13,995)	$ (13,995)	—	—	(13,995)
Minimum pension liability	—	—	—	—	902	—	902	902
Comprehensive loss	—	—	—	—	$ (13,093)	—	—	—
Stock issued under option plans	2,563	—	6	—	—	—	—	6
Retirement of treasury stock	—	(15)	(19,256)	—	—	19,271	—	—
Balance at January 31, 2005	13,098,364	131	107,883	(55,407)	—	—	(3,342)	49,265
Net loss	—	—	—	(9,574)	$ (9,574)	—	—	(9,574)
Minimum pension liability	—	—	—	—	(851)	—	(851)	(851)
Comprehensive loss	—	—	—	—	$ (10,425)	—	—	—
Stock issued under option plans	38,924	—	260	—	—	—	—	260
Balance at January 31, 2006	13,137,288	131	108,143	(64,981)	—	—	(4,193)	39,100
Net income	**—**	**—**	**—**	**7,545**	**$ 7,545**	**—**	**—**	**7,545**
Minimum pension liability	**—**	**—**	**—**	**—**	**(3,373)**	**—**	**(3,373)**	**(3,373)**
Comprehensive income	**—**	**—**	**—**	**—**	**$ 4,172**	**—**	**—**	**—**
Stock based payments under stock compensation plans	**112,722**	**—**	**754**	**—**	**—**	**—**	**—**	**754**
Stock issued under private placement	**1,129,496**	**12**	**4,740**	**—**	**—**	**—**	**—**	**4,752**
Balance at January 31, 2007	**14,379,506**	**$ 143**	**$ 113,737**	**$ (57,436)**	**—**	**—**	**$ (7,566)**	**$ 48,878**

See accompanying notes.

Consolidated Statements of Cash Flows

In thousands, except share data	Year ended January 31, 2007	2006	2005
Operating activities			
Net income (loss)	**$ 7,545**	$ (9,574)	$ (13,995)
Adjustments to reconcile net income / (loss) to net cash provided by operating activities			
Depreciation and amortization	**7,199**	8,844	9,799
Provision for doubtful accounts	**72**	(2)	17
Loss on sale of property, plant and equipment	**1**	77	—
Deferred income taxes	**260**	—	—
Stock based compensation	**754**	408	230
Changes in operating assets and liabilities			
Trade accounts receivable	**(1,399)**	(1,271)	1,319
Other receivables	**149**	(212)	(27)
Inventories	**(6,220)**	(5,570)	2,424
Income taxes	**142**	2,126	144
Prepaid expenses and other current assets	**14**	(153)	622
Accounts payable and accrued liabilities	**2,398**	5,576	3,134
Other	**—**	55	11
Net cash provided by operating activities	**10,915**	304	3,678
Investing activities			
Capital expenditures	**(3,622)**	(3,470)	(2,799)
Proceeds from sale of property, plant and equipment	**—**	15	9
Net investment in life insurance	**(167)**	109	442
Net cash used in investing activities	**(3,789)**	(3,346)	(2,348)
Financing activities			
Proceeds from long-term debt	**—**	3,330	1,862
Repayment of long-term debt	**(11,475)**	—	(4,065)
Proceeds from issuance of common stock	**4,752**	9	6
Net cash (used in) provided by financing activities	**(6,723)**	3,339	(2,197)
Net increase (decrease) in cash	**403**	297	(867)
Cash at beginning of year	**1,489**	1,192	2,059
Cash at end of year	**$ 1,892**	$ 1,489	$ 1,192
Supplemental disclosures of cash flow information			
Cash paid (received) during the year for:			
Interest, net of amounts capitalized	**$ 3,792**	$ 3,258	$ 2,090
Income tax, net	**44**	(2,235)	(320)
Non-cash activities			
Accrued asset retirement obligations	**$ 626**	$ 583	$ 540
Assets acquired under capital leases	**$ 186**	$ —	$ —

See accompanying notes.

1. Summary of Business and Significant Accounting Policies

Business

Virco Mfg. Corporation (the "Company"), which operates in one business segment, is engaged in the design, production and distribution of quality furniture for the commercial and education markets. Over 57 years of manufacturing has resulted in a wide product assortment. Major products include mobile tables, mobile storage equipment, desks, computer furniture, chairs, activity tables, folding chairs and folding tables. The Company manufactures its products in Torrance, California, and Conway, Arkansas, for sale primarily in the United States.

The Company operates in a seasonal business, and requires significant amounts of working capital through the existing credit facility to fund acquisitions of inventory and finance receivables during the summer delivery season. Restrictions imposed by the terms of the existing credit facility may limit the Company's operating and financial flexibility. However, the Company believes that its existing cash and amounts available under the credit facility, and any cash generated from operations will be sufficient to fund its working capital requirements, capital expenditures and other obligations through the next 12 months.

Principles of Consolidation

The consolidated financial statements include the accounts of Virco Mfg. Corporation and its wholly owned subsidiaries. All material intercompany balances and transactions have been eliminated in consolidation.

Management Use of Estimates

Preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities – and disclosure of contingent assets and liabilities – at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Significant estimates made by management include, but are not limited to, valuation of: inventory; deferred tax assets and liabilities; useful lives of property, plant, and equipment; intangible assets; liabilities under pension, warranty, and environmental claims; and the ultimate collection of accounts receivable. Actual results could differ from these estimates.

Fiscal Year End

Fiscal years 2006, 2005 and 2004, refer to the years ended January 31, 2007, 2006 and 2005, respectively.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with maturities of three months or less at the date of purchase.

Concentration of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of accounts receivable. The Company performs ongoing credit evaluations of its customers and maintains allowances for potential credit losses. Sales to the Company's recurring customers are generally made on open account with terms consistent with the industry. Credit is extended based on an evaluation of the customer's financial condition and payment history. Past due accounts are determined based on how recently payments have been made in relation to the terms granted. Amounts are written off against the allowance in the period that the Company determines that the receivable is not collectable. The Company purchases insurance on receivables from certain commercial customers to minimize the Company's credit risk. The Company does not typically obtain collateral to secure credit risk, customers with inadequate credit are required to provide cash in advance or letters or credit. The Company does not assess interest on receivable balances. A substantial percentage of the Company's receivables come from low-risk government entities. No customers exceeded 10% of the Company's sales for each of the three years in the period ended January 31, 2007. Foreign sales were less than 5% for the period ended January 31, 2007, and each of the prior two fiscal years.

No single customer accounted for more than 10% of the Company's accounts receivable at January 31, 2007 or 2006. Because of the short time between shipment and collection, the net carrying value approximates the fair value for these assets.

Derivatives

The Company has used derivative financial instruments to reduce interest rate risks. The Company does not hold or issue derivative financial instruments for trading purposes. All derivatives are recognized as either assets or liabilities in the statement of financial condition and are measured at fair value. At January 31, 2007 and 2006, the Company had no derivative instruments.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the last-in, first-out (LIFO) method of valuation for the material content of inventories and the first-in, first-out (FIFO) method for labor and overhead. The Company uses LIFO as it results in a better matching of costs and revenues. The Company records the cost of excess capacity as a period expense, not as a component of capitalized inventory valuation.

Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation and amortization are computed on the straight-line method for financial reporting purposes based upon the following estimated useful lives:

Land improvements	5 to 25 years
Buildings and building improvements	5 to 40 years
Machinery and equipment	3 to 10 years
Leasehold improvements	shorter of lease or useful life

The Company did not capitalize interest costs as part of the acquisition cost of property, plant and equipment for the years ended January 31, 2007, 2006 and 2005. The Company capitalizes the cost of significant repairs that extend the life of an asset; repairs and maintenance that do not extend the life of an asset are expensed as incurred.

The Company capitalizes costs associated with software developed for its own use. Such costs are amortized over three to seven years from the date the software becomes operational. The net book value of capitalized software, included in machinery and equipment, was $0 and $414,000 at January 31, 2007 and 2006, respectively. Depreciation expense attributable to capitalized software was $414,000 for fiscal year 2006 and $1,352,000 for fiscal years 2005 and 2004.

The Company leases certain computer equipment under a capital lease. The cost, accumulated depreciation, and depreciation expense are included in the property, plant, and equipment accounts. Assets acquired under capital leases totaled approximately $180,000, $0, and $0 in 2006, 2005, and 2004 respectively. Future minimum lease payments under capital leases as of January 31, 2006 are $62,000, $62,000, $59,000 in 2007, 2008, and 2009 respectively.

The Company subleases space at one of our facilities on a month-to-month basis. Rental income for 2006, 2005, and 2004 was $330,000, $36,000, and $0 respectively.

The Company has established asset retirement obligations related to leased manufacturing facilities in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 143, “Accounting for Asset Retirement Obligations”. Accrued asset retirement obligations are recorded at net present value and discounted over the life of the lease. Asset retirement obligations, included in other non-current liabilities are $626,000 and $583,000 at January 31, 2007 and 2006, respectively.

	Asset	Accumulated Depreciation	Liability
Beginning balance at January 31, 2006	$ 540,000	$ (108,000)	$ (583,000)
Additional obligation	—	—	—
Depreciation expense	—	(108,000)	—
Accretion expense	—	—	(43,000)
Ending balance at January 31, 2007	$ 540,000	$ (216,000)	$ (626,000)

Impairment of Long-Lived Assets

An impairment loss is recognized in the event facts and circumstances indicate the carrying amount of an asset may not be recoverable, and an estimate of future undiscounted cash flows is less than the carrying amount of the asset. Impairment is recorded based on the excess of the carrying amount of the impaired asset over the fair value. Generally, fair value represents the Company’s expected future cash flows from the use of an asset or group of assets, discounted at a rate commensurate with the risks involved. The Company has not recorded an impairment of assets at January 31, 2007 or 2006.

Net Income (Loss) Per Share

Basic net loss per share is calculated by dividing net loss by the weighted-average number of common shares outstanding. Diluted net loss per share is calculated by dividing net loss by the weighted-average number of common shares outstanding plus the dilution effect of convertible securities. The following table sets forth the computation of basic and diluted loss per share:

In thousands, except per share data	**2006**	2005	2004
Numerator:			
Net income (loss)	**$ 7,545**	$ (9,574)	$ (13,995)
Denominator:			
Weighted-average shares – basic	**13,590**	13,114	13,112
Common equivalent shares from common stock options and warrants	**21**	—	—
Weighted-average shares – diluted	**13,611**	13,114	13,112
Net income (loss) per common share (a)			
Basic	**$ 0.56**	$ (0.73)	$ (1.07)
Diluted	**0.55**	$ (0.73)	$ (1.07)

(a) For the period ended January 31, 2006, approximately 253,000 shares of unvested stock awards and incentive stock options were excluded in the computation of diluted net income per share, as the effect would be anti-dilutive. For the period ended January 31, 2005, approximately 225,000 shares of incentive stock options were excluded in the computation of diluted net income per share, as the effect would be anti-dilutive.

Goodwill and Other Intangible Assets

The Company accounts for goodwill and other intangible assets in accordance with SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." Under SFAS No. 142, goodwill and intangible assets deemed to have an indefinite life are not amortized but are subject to annual impairment tests. Impairment tests are prepared in the fourth quarter of each fiscal year. Other intangible assets are amortized on a straight line basis over their useful lives (3-17 years).

Information regarding the Company's goodwill and other intangible assets is as follows (in thousands):

	2006			2005		
	Gross Amount	**Accumulated Amortization**	**Net Amount**	Gross Amount	Accumulated Amortization	Net Amount
Goodwill (not amortized)	**$ 2,200**	**$ —**	**$ 2,200**	$ 2,200	$ —	$ 2,200
Intangible assets	**150**	**39**	**111**	150	26	124
	$ 2,350	**$ 39**	**$ 2,311**	$ 2,350	$ 26	$ 2,324

The Company anticipates that amortization expense will be approximately $13,000 per year for the next five years. The Company does not have amortization expense other than related to intangible assets.

Environmental Costs

The Company is subject to numerous environmental laws and regulations in the various jurisdictions in which it operates that (a) govern operations that may have adverse environmental effects, such as the discharge of materials into the environment, as well as handling, storage, transportation and disposal practices for solid and hazardous wastes, and (b) impose liability for response costs and certain damages resulting from past and current spills, disposals or other releases of hazardous materials. Normal, recurring expenses related to operating the factories in a manner that meets or exceeds environmental laws and regulations are matched to the cost of producing inventory.

Despite our efforts to comply with existing laws and regulations, compliance with more stringent laws or regulations, or stricter interpretation of existing laws, may require additional expenditures by us, some of which may be material. We reserve amounts for such matters when expenditures are probable and reasonably estimable.

Costs incurred to investigate and remediate environmental waste are expensed, unless the remediation extends the useful life of the assets employed at the site. At January 31, 2007 and 2006, the Company has not capitalized any remediation costs and has not recorded any amortization expense in fiscal years 2006, 2005 and 2004.

Advertising Costs

Advertising costs are expensed in the period in which they occur. Selling, general and administrative expenses include advertising costs of $1,506,000 in 2006, $1,826,000 in 2005 and $2,843,000 in 2004. Prepaid advertising costs reported as an asset on the balance sheet at January 31, 2007 and 2006, were $352,000 and $357,000, respectively.

Product Warranty Expense

The Company provides a product warranty on most products. The standard warranty offered on products sold through January 31, 2005, is five years. Effective February 1, 2005, the standard warranty was increased to 10 years on products sold after February 1, 2005. It generally warranties that customers can return a defective product during the specified warranty period following purchase in exchange for a replacement product or that the Company can repair the product at no charge to the customer. The Company determines whether replacement or repair is appropriate in each circumstance. The Company uses historic data to estimate appropriate levels of warranty reserves. Because product mix, production methods, and raw material sources change over time, historic data may not always provide precise estimates for future warranty expense. The Company recorded reserves of $1,750,000 as of January 31, 2007 and $1,500,000 as of January 31, 2006, respectively.

Self-Insurance

In 2006 and 2005, the Company was self-insured for product liability losses up to $500,000 per occurrence, for workers compensation losses up to $250,000 per occurrence, and for auto liability up to $50,000 per occurrence. In prior years the Company has been self-insured for workers compensation, automobile, product, and general liability losses. Actuaries assist the Company in determining its liability for the self-insured component of claims, which have been discounted to their net present value utilizing a discount rate of 5.75%.

Stock-Based Compensation Plans

The Company has two stock-based compensation plans, which are described more fully in Note 5, "Stock-Based Compensation". Effective February 1, 2006, the Company adopted FASB Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment, ("FAS 123 (R)") using the modified prospective application method for transition for its two stock-based compensation plans. Accordingly, prior year amounts have not been restated.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the prior years' balance sheets to conform to the current year presentation.

Revenue Recognition

The Company recognizes all sales when title passes under its various shipping terms and when collectability is reasonably assured. The Company reports sales net of sales returns and allowances and sales tax imposed by various government authorities.

Shipping and Installation Fees

Revenues related to shipping and installation are included as revenue in net sales. Costs related to shipping and installation are included in operating expenses. For the years ended January 31, 2007, 2006 and 2005, shipping and installation costs of approximately $22,579,000, $23,745,000 and $22,777,000, respectively, were included in selling, general and administrative expenses.

Accounting for Income Taxes

The Company recognizes deferred income taxes under the asset and liability method of accounting for income taxes in accordance with the provisions of SFAS No. 109, "Accounting for Income Taxes". Deferred income taxes are recognized for differences between the financial statement and tax basis of assets and liabilities at enacted statutory tax rates in effect for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance against deferred tax assets is recorded when it is determined to be more likely than not that the asset will not be realized.

New Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments" (SFAS 155). SFAS 155 establishes, among other things, the accounting for certain derivatives embedded in other financial instruments. This statement permits fair value remeasurement for any hybrid financial instrument containing an embedded derivative that would otherwise require bifurcation. It also requires that beneficial interests in securitized financial assets be accounted for in accordance with SFAS No. 133. SFAS 155 is effective for fiscal years beginning after September 15, 2006, and is not expected to have a material impact on the Company's financial operations or financial positions.

In July 2006, the Financial Accounting Standards Board issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109 ("FIN 48"), which clarifies what criteria must be met prior to recognition of the financial statement benefit of a position taken in a tax return. The Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Also, the Interpretation provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The adoption of FIN 48 will be effective for years beginning after December 15, 2006, and the Company will be required to adopt this Interpretation in the first quarter of 2007. Based on the Company's evaluation as of January 31, 2007, FIN 48 is not expected to have a material impact on the Company's consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements ("SFAS 157") which provides enhanced guidance for using fair value to measure assets and liabilities. The standard also expands the amount of disclosure regarding the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently reviewing the impact, if any, that SFAS 157 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158 Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R). This standard requires recognition of the funded status of a benefit plan in the statement of financial position. The standard also requires recognition in other comprehensive income of certain gains and losses that arise during the period but are deferred under pension accounting rules, as well as modifies the timing of reporting and adds certain disclosures. SFAS No. 158 provides recognition and disclosure elements to be effective as of the end of the fiscal after December 15, 2006, and measurement elements to be effective for fiscal years ending after December 15, 2008. The Company adopted the recognition provisions of SFAS No. 158 and applied them to the funded status of the its defined benefit plans resulting in a decrease in Shareholders Equity of $1.9 million.

In October 2006, the FASB ratified EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. This statement is effective for years beginning after December 15, 2007. This statement clarifies FASB 106, Employers Accounting for Post-Retirement Benefits other than Pensions, applies to endorsement split-dollar life insurance arrangements. The Company estimates that adoption of this statement will increase the Company's recorded liabilities by approximately $2 million with no impact to the statement of operations or cash flows of the Company . The Company has purchased life insurance policies that are designed to pay a death benefit that is greater than the promised retirement benefit.

2. Inventories

The current material cost for inventories exceeded LIFO cost by $7,357,000 and $6,422,000 at January 31, 2007 and 2006, respectively. Liquidation of prior year LIFO layers due to a reduction in certain inventories increased income by $75,000, $60,000 and $410,000 in the years ended January 31, 2007, 2006 and 2005, respectively.

Details of inventory amounts, including the material portion of inventory which is valued at LIFO, at January 31, 2006 and 2005, are as follows (in thousands):

	January 31, 2007			
	Material Content at FIFO	**LIFO Reserve**	**Labor, Overhead and Other**	**Total**
Finished goods	$ 8,559	$ (1,616)	$ 4,708	$ 11,651
Work in process	13,974	(3,306)	9,022	19,690
Raw materials and supplies	8,931	(2,435)	—	6,496
Total	$ 31,464	$ (7,357)	$ 13,730	$ 37,837

	January 31, 2006			
	Material Content at FIFO	LIFO Reserve	Labor, Overhead and Other	Total
Finished goods	$ 8,581	$ (1,630)	$ 4,119	$ 11,070
Work in process	9,883	(2,594)	6,507	13,796
Raw materials and supplies	8,949	(2,198)	—	6,751
Total	$ 27,413	$ (6,422)	$ 10,626	$ 31,617

3. Debt

Outstanding balances (in thousands) for the Company's long-term debt were as follows:

	January 31,	
In thousands, except per share data	**2007**	2006
Revolving credit line with Wells Fargo Bank(a)	**$ —**	$ 6,448
Term note with Wells Fargo Bank(a)	**15,000**	20,000
Other	**264**	105
	15,264	26,553
Less current portion	**5,074**	5,012
	$ 10,190	$ 21,541
Outstanding stand-by letters of credit	**$ 329**	$ 329

(a) Virco has entered into a revolving credit facility with Wells Fargo Bank, which was amended and restated in March 2007, and which provides a term loan of $20,000,000 and a secured revolving line of credit that varies as a percentage of inventory and receivables, up to a maximum of $40,000,000, with the maximum increasing to $50,000,000 during certain months of the year. The amended agreement, which is effective March 2007, extended the maturing date from February 15, 2008 to February 15, 2009. The term note is a two-year loan, amortizing at $10,000,000 per year with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate (8.25% at January 31, 2007) plus a 0.5% margin.

The amendment extended the maturing date of the revolving line from February 15, 2008 to February 15, 2009 with interest payable monthly at a fluctuating rate equal to the Wells Fargo Bank's prime rate plus a fluctuating margin similar to the term note. The revolving line typically provides for advances of 80% on eligible accounts receivable and 20% – 60% on eligible inventory. The advance rates fluctuate depending on the time of the year and the types of assets. The agreement has an unused commitment fee of 0.375%. Approximately $14,604,000 was available for borrowing as of January 31, 2007.

The revolving credit facility with Wells Fargo Bank is subject to various financial covenants including a liquidity requirement, a leverage requirement, a cash flow coverage requirement and profitability requirements. The agreement also places certain restrictions on capital expenditures, new operating leases, dividends and the repurchase of the Company's common stock. The revolving credit facility is secured by the Company's accounts receivable, inventories, equipment and property. The Company is in compliance with its covenants at January 31, 2007.

Long-term debt repayments are approximately as follows (in thousands):

Year ending January 31,	
2008	$ 5,074
2009	10,074
2010	69
2011	12
2012	12
Thereafter	23

The Company believes that the carrying value of debt approximates fair value at January 31, 2007 and 2006, as all of the long-term debt bears interest at variable rates based on prevailing market conditions.

4. Retirement Plans

The Company maintains three defined benefit pension plans, the Virco Employees Retirement Plan, the VIP Retirement Plan, and the Non-Employee Directors Retirement Plan. Pension expense and cash contributions for the fiscal years ended January 31, 2007, 2006, and 2005, were substantially less than the prior years as a result of several major events during 2003. Three significant events occurred during the fiscal year ended January 31, 2004. First, approximately 40% of Virco's employees severed their employment with Virco during the year. The majority of these employees accepted a voluntary severance package. This severance was treated as a plan curtailment. Second, a significant number of employees that severed their employment elected a lump sum benefit. During 2003, the pension trust disbursed approximately $6.3 million to severed employees. These distributions were accounted for as a plan settlement. Finally, effective December 31, 2003, the Company froze all future benefit accruals under the plans. Employees can continue to vest under the benefits earned to date, but no covered participants will earn additional benefits under the plan freeze. The annual measurement dates for the plans is December 31. As a result of these activities, Virco incurred additional pension expense of approximately $1,250,000 related to the plan curtailment, additional pension expense of approximately $1,540,000 related to the plan settlement, and additional pension expense of approximately $40,000 related to the plan freeze. As a result of the plan freeze, the projected benefit obligation decreased by approximately $7,500,000. Accounting policy regarding pensions requires management to make complex and subjective estimates and assumptions relating to amounts which are inherently uncertain. Three primary economic assumptions influence the reported values of plan liabilities and pension costs. The Company takes the following factors into consideration.

The discount rate represents an estimate of the rate at which retirement plan benefits could effectively be settled. The Company obtains data on several reference points when setting the discount rate including current rates of return available on longer term high-grade bonds and changes in rates that have occurred over the past year. This assumption is sensitive to movements in market rates that have occurred since the preceding valuation date, and therefore, may change from year to year.

When setting its rate of compensation increase assumption, the Company takes into consideration its recent experience with respect to average rates of compensation increase, compensation survey data relative to average compensation increases that other large corporations have awarded, and compensation increases that other large corporations expect to award over the upcoming year. This assumption is somewhat sensitive to inflation and may change from year to year. Effective December 31, 2003, the Company froze future benefit accruals for all three defined benefit plans. As such, the compensation increase assumption had no impact on pension expense, accumulated benefit obligation or projected benefit obligation for the period ended January 31, 2007 or 2006.

The assumed rate of return on plan assets represents an estimate of long-term returns available to investors who hold a mixture of stocks, bonds, and cash equivalent securities. When setting its expected return on plan asset assumptions, the Company considers long-term rates of return on various asset classes (both historical and forecasted, using data collected from various sources generally regarded as authoritative) in the context of expected long-term average asset allocations for its defined benefit pension plan.

Two of the Company's defined benefit pension plans (the VIP Plan and the Non-Employee Directors Plan) are executive benefit plans that are not funded and are subject to the Company's creditors. Because these plans are not funded, the assumed rate of return has no impact on pension expense or the funded status of the plans.

The Company maintains a trust that funds the pension obligations for the Virco Mfg. Corporation Employees Pension. The Board of Directors appoints a Retirement Plan Committee that establishes policy for investment and funding strategies. Approximately 75% of the trust assets are managed by investment advisors and held in common trust funds with the balance managed by the Retirement Plan Committee. The Committee has established target asset allocations for its investment advisors, who invest the trust assets in a variety of institutional collective trust funds. The long-term asset allocation target provided to the investment advisors is 85% stock and 15% bond, with maximum allocations of 80% large cap stocks, 30% small cap stocks, and 30% international stock. The Company has established a custom benchmark derived from a variety of stock and bond indices that are weighted to approximate the asset allocation provided to the investment advisors. The investment advisors' performance is compared to the custom index as part of the evaluation of the investment advisors' performance. The Committee receives monthly reports from the investment advisors and meets periodically with them to discuss investment performance. At December 31, 2006 and 2005, the amount of the plan assets invested in bond or short-term investment funds were 1% and 2%, respectively, and the balance in equity funds or investments. The trust does not hold any Company stock. It is the Company's policy to contribute adequate funds to the trust accounts to cover benefit payments under the VIP and Non-Employee Director Plans and to maintain the funded status of the Virco Mfg. Corporation Employees Pension at a minimum of 90% of the current liability as determined by the plan actuaries. It is anticipated that the Company will be required to contribute approximately $263,000 to the non-qualified plan during the fiscal year ending January 31, 2008.

Estimated payments from the qualified plan pension trust to plan participants are estimated to be $557,000 during the fiscal year ending January 31, 2008. It is anticipated that the Company may have to contribute approximately $2.3 million to the trust if the Company elects to maintain the 90% funded status. Actual contributions will depend upon investment return on the plan assets.

Payments made under the qualified plan are made from the trust fund. Payments made under the VIP Plan and Non-Employee Directors Plan are made by the Company. Estimated payments (in thousands) under the plans are as follows:

Plan Year	Qualified Plan	VIP Plan	Directors Plan	Total
2007	$ 557	$ 263	$ 0	$ 820
2008	596	247	48	891
2009	664	232	46	942
2010	745	216	43	1,004
2011	855	200	40	1,095
Thereafter	5,796	852	226	6,874

Qualified Pension Plan

The Company and its subsidiaries cover all employees under a non-contributory defined benefit retirement plan, the Virco Employees' Retirement Plan (the Plan). Benefits under the Plan are based on years of service and career average earnings. The Company's general funding policy is to contribute enough to maintain a funded status of at least 90% of the current liability as determined by the Plan actuaries. Minimum pension liability adjustments for the years 2006, 2005 and 2004 were $(1,462,000) , $(851,000), and $902,000, respectively, and are included in comprehensive loss. As a result of implementing SFAS 158, the Company recorded an adjustment to comprehensive loss of $1,910,000. At January 31, 2006 and 2005, a full valuation allowance has been recorded against the net deferred tax assets. Accumulated comprehensive loss at January 31, 2007 and 2006 was primarily composed of minimum pension liability adjustments. Assets of the Plan are invested in common trust funds.

The following table sets forth (in thousands) the funded status of the Plan at December 31, 2006 and 2005:

	Pension Benefits	
	12/31/2006	12/31/2005
Change in Benefit Obligation		
Benefit obligation at beginning of year	**$ 22,284**	$ 21,675
Service cost	**165**	173
Interest cost	**1,382**	1,408
Plan participant's contributions	**—**	—
Amendments	**424**	416
FASB 88 events	**—**	—
Actuarial (gains) losses	**3,013**	509
Benefits paid	**(3,189)**	(1,897)
Benefit obligation at end of year	**$ 24,079**	$ 22,284
Change in Plan Assets		
Fair value at beginning of year	**$ 14,812**	$ 16,192
Actual return on plan assets	**2,288**	517
Acquisition	**—**	—
Company contributions	**—**	—
Plan participant's contributions	**—**	—
Benefits paid	**(3,189)**	(1,897)
Fair value at end of year	**$ 13,911**	$ 14,812

	Pension Benefits	
	12/31/2006	12/31/2005
Funded Status		
Funded status of plan	**$ (10,167)**	$ (7,472)
Unrecognized net transition amount	**—**	(52)
Unrecognized net actuarial loss	**—**	4,246
Unrecognized prior service cost	**—**	2,849
Accrual of minimum liability	**—**	—
Accrued benefit cost	**(10,167)**	(429)
Statements of Financial Position		
Prepaid benefit cost	**—**	—
Accrued benefit liability	**(10,167)**	(7,472)
Intangible asset	**—**	2,849
Accumulate other comprehensive loss	**8,459**	4,194
Net amount recognized	**$ (1,708)**	$ (429)
Items not yet recognized as a component of net periodic pension expense:		
Unrecognized net actuarial losses	**5,670**	N/A
Unamortized prior service costs	**2,804**	N/A
Net initial asset recognition	**(15)**	N/A
	8,459	N/A
Supplementary Data		
Projected benefit obligation	**$ 24,079**	$ 22,284
Accumulated benefit obligation	**24,079**	22,284
Fair value of plan assets	**13,911**	14,812
Components of net cost		
Service cost	**$ 165**	$ 173
Interest cost	**1,382**	1,408
Expected return on plan assets	**(896)**	(986)
Amortization of transition amount	**(37)**	(37)
Amortization of prior service cost	**469**	469
Recognized net actuarial loss	**196**	163
FASB 88	**—**	—
Benefit cost	**$ 1,279**	$ 1,190
Additional Information		
Increase in minimum liability included in other comprehensive income	**$ 4,266**	$ 851
Estimated Future Benefit Payments		
FYE 01-31-2007	**$ —**	$ 493
FYE 01-31-2008	**557**	521
FYE 01-31-2009	**596**	580
FYE 01-31-2010	**664**	653
FYE 01-31-2011	**745**	739
FYE 01-31-2012	**855**	—
FYE 01-31-2013 to 2016	**5,796**	5,211
Total	$ **9,213**	$ 8,197
Weighted Average Assumptions		
Discount rate	**5.75%**	6.50%
Expected return on plan assets	**6.50%**	6.50%
Rate of compensation increase	**5%**	5%
	5.00%	5.00%

VIP Retirement Plan

The Company also provides a supplementary retirement plan for certain key employees, the VIP Retirement Plan (VIP Plan). The VIP Plan provides a benefit up to 50% of average compensation for the last five years in the VIP Plan, offset by benefits earned under the Virco Employees' Retirement Plan. The VIP Plan benefits are secured by a life insurance program. The cash surrender values of the policies securing the VIP Plan were $2,488,000 and $2,592,000 at January 31, 2007 and 2006, respectively. These cash surrender values are included in other assets in the consolidated balance sheets.

The Company maintains a rabbi trust to hold assets related to the VIP Retirement Plan. Substantially all assets securing the VIP Plan are held in the rabbi trust.

The following table sets forth (in thousands) the funded status of the VIP Plan at December 31, 2006 and 2005:

	Non-Qualified VIP Pension	
	12/31/2006	12/31/2005
Change in Benefit Obligation		
Benefit obligation at beginning of year	**$ 5,675**	$ 5,592
Service cost	**202**	211
Interest cost	**360**	341
Plan participant's contributions	**—**	—
Amendments	**(424)**	(416)
FASB 88 events	**0**	0
Actuarial (gains) losses	**207**	203
Benefits paid	**(256)**	(256)
Benefit obligation at end of year	**$ 5,764**	$ 5,675
Change in Plan Assets		
Fair value at beginning of year	**$ —**	$ —
Actual return on plan assets	**—**	—
Acquisition	**—**	—
Company contributions	**256**	256
Plan participant's contributions	**—**	—
Benefits paid	**(256)**	(256)
Fair value at end of year	**$ —**	$ —
Funded Status		
Funded status of plan	**$ (5,764)**	$ (5,675)
Unrecognized net transition amount	**—**	—
Unrecognized net actuarial loss	**—**	1,946
Unrecognized prior service cost	**—**	(2,840)
Accrual of minimum liability	**—**	—
Accrued benefit cost	**$ (5,764)**	$ (6,569)
Statements of Financial Position		
Prepaid benefit cost	**$ —**	$ —
Accrued benefit liability	**(5,764)**	(6,569)
Intangible asset	**—**	—
Accumulate other comprehensive loss	**—**	—
Net amount recognized	**$ (5,764)**	$ (6,569)
Items not yet recognized as a component of net periodic pension expense:		
Unrecognized net actuarial losses	**2,034**	N/A
Unamortized prior service costs	**(2,729)**	N/A
Net initial asset recognition	**—**	N/A
	(695)	N/A
Supplementary Data		
Projected benefit obligation	**$ 5,764**	$ 5,675
Accumulated benefit obligation	**5,764**	5,675
Fair value of plan assets	**—**	—

	Non-Qualified VIP Pension	
	12/31/2006	12/31/2005
Components of net cost		
Service cost	**$ 202**	$ 211
Interest cost	**360**	341
Expected return on plan assets	**—**	—
Amortization of transition amount	**—**	—
Amortization of prior service cost	**(535)**	(535)
Recognized net actuarial loss	**119**	134
FASB 88	**—**	—
Benefit cost	**$ 146**	$ 151
Additional Information		
Increase in minimum liability included in other comprehensive income	**$ (695)**	$ —
Estimated Future Benefit Payments		
FYE 01-31-2007	**$ —**	$ 248
FYE 01-31-2008	**263**	243
FYE 01-31-2009	**247**	226
FYE 01-31-2010	**232**	211
FYE 01-31-2011	**216**	194
FYE 01-31-2012	**200**	—
FYE 01-31-2013 to 2016	**852**	781
Total	**$ 2,010**	$ 1,903
Weighted Average Assumptions		
Discount rate	**5.75%**	6.50%
Expected return on plan assets	**6.50%**	6.50%
Rate of compensation increase	**5.00%**	5.00%

Non-Employee Directors Retirement Plan

In April 2001, the Board of Directors established a non-qualified plan for non-employee directors of the Company. The plan provides a lifetime annual retirement benefit equal to the director's annual retainer fee for the fiscal year in which the director terminates his or her position with the Board, subject to the director providing 10 years of service to the Company. At January 31, 2007, the plan did not hold any assets.

The following table sets forth (in thousands) the funded status of the Non-Employee Directors Retirement Plan at December 31, 2006 and 2005:

	Non-Employee Directors Pension	
	12/31/2006	12/31/2005
Change in Benefit Obligation		
Benefit obligation at beginning of year	**$ 419**	$ 391
Service cost	**26**	23
Interest cost	**27**	25
Plan participant's contributions	**—**	—
Amendments	**—**	—
FASB 88 events	**—**	—
Actuarial (gains) losses	**(1)**	(20)
Benefits paid	**—**	—
Benefit obligation at end of year	**$ 471**	$ 419
Change in Plan Assets		
Fair value at beginning of year	**$ —**	$ —
Actual return on plan assets	**—**	—
Acquisition	**—**	—
Company contributions	**—**	—
Plan participant's contributions	**—**	—
Benefits paid	**—**	—
Fair value at end of year	**$ —**	$ —

	Non-Employee Directors Pension	
	12/31/2006	12/31/2005
Funded Status		
Funded status of plan	**$ (471)**	$ (419)
Unrecognized net transition amount	**—**	—
Unrecognized net actuarial loss	**—**	(225)
Unrecognized prior service cost	**—**	23
Accrual of minimum liability	**—**	–
Accrued benefit cost	**(471)**	(621)
Statements of Financial Position		
Prepaid benefit cost	**—**	—
Accrued benefit liability	**$ (471)**	$ (621)
Intangible asset	**—**	—
Accumulate other comprehensive loss	**—**	—
Net amount recognized	**$ (471)**	$ (621)
Items not yet recognized as a component of net periodic pension expense:		
Unrecognized net actuarial gain	**(198)**	N/A
Unamortized prior service costs	**—**	N/A
Net initial asset recognition	**—**	N/A
	(198)	N/A
Supplementary Data		
Projected benefit obligation	**471**	419
Accumulated benefit obligation	**471**	419
Fair value of plan assets	**—**	—
Components of net cost		
Service cost	**$ 26**	$ 23
Interest cost	**27**	26
Expected return on plan assets	**—**	—
Amortization of transition amount	**—**	—
Amortization of prior service cost	**23**	88
Recognized net actuarial loss	**(28)**	(27)
FASB 88	**—**	—
Benefit cost	**$ 48**	$ 110
Additional Information		
Increase in minimum liability included in other comprehensive income	**$ (198)**	$ —
Estimated Future Benefit Payments		
FYE 01-31-2007	**$ —**	$ —
FYE 01-31-2008	**—**	48
FYE 01-31-2009	**48**	45
FYE 01-31-2010	**46**	42
FYE 01-31-2011	**43**	39
FYE 01-31-2012	**40**	—
FYE 01-31-2013 to 2016	**225**	218
Total	**$ 402**	$ 392
Weighted Average Assumptions		
Discount rate	**5.75%**	6.50%
Expected return on plan assets	**6.50%**	6.50%
Rate of compensation increase	**5.00%**	5.00%

Implementation of SFAS No. 158

The Company adopted the recognition provisions of SFAS No. 158 and initially applied them to the funded status of its defined benefit plans as of December 31, 2006. The initial recognition of the funded status of its defined benefit plans resulted in a decrease in Shareholders' Equity of $1.9 million.

The amounts in accumulated other comprehensive income that are expected to be recognized as components of net periodic pension expense during 2007 are as follows:

In thousands	Qualified Plan	VIP Plan	Directors Plan
Actuarial (gain)/loss recognition	$ 313	$ 145	$ (25)
Prior service cost recognition	505	(499)	0
Net initial obligation/(asset) recognition	(15)	0	0

The incremental effect of applying SFAS on individual lines of the Consolidated Balance Sheet at January 31, 2007 was:

In thousands	Before SFAS No. 158	Effect of SFAS No. 158	After SFAS No. 158
Assets:			
Other non-current assets	$ 2,804	(2,804)	$ —
Liabilities:			
Accrued pension expenses	$ 16,842	893	$ 15,949
Shareholders' Equity:			
Accumulated comprehensive loss	$ 50,789	(1,911)	$ 48,878

401(k) Retirement Plan

The Company's retirement plan, which covers all U.S. employees, allows participants to defer from 1% to 15% of their eligible compensation through a 401(k) retirement program. Through December 31, 2001, the plan included an employee stock ownership component. The plan continues to include the Virco stock as one of the investment options. Shares owned by the plan are held by the plan trustee, Security Trust Company. At January 31, 2007 and 2006, the plan held 512,783 shares and 448,933 shares of Virco stock, respectively. For the fiscal years ended January 31, 2007, 2006 and 2005, there was no employer match and therefore no compensation cost to the Company.

Life Insurance

The Company provided current and post-retirement life insurance to certain salaried employees with split dollar life insurance policies under the Dual Option Life Insurance Plan. Effective January 2004, the Company terminated this plan for active employees. Cash surrender values of these policies, which are included in other assets in the consolidated balance sheets, were $2,946,000 and $2,842,000 at January 31, 2007 and 2006 respectively. The Company maintains a rabbi trust to hold assets related to the Dual Options Life Insurance Plan. Substantially all assets securing this plan are held in the rabbi trust.

5. Stock Based Compensation and Stockholders Rights

Stock Option Plans

The Company's two stock plans are the 1997 Employee Incentive Plan (the 1997 Plan) and the 1993 Employee Incentive Stock Plan (the 1993 Plan). Under the 1993 Plan, the Company may grant an aggregate of 707,384 shares (as adjusted for stock splits and stock dividends) to its employees in the form of stock options. The 1993 Plan expired in 2003 and had no unexercised options outstanding at January 31, 2007. Under the 1997 Plan, the Company may grant an aggregate of 724,729 shares (as adjusted for stock splits and stock dividends) to its employees in the form of stock options or awards. As of January 31, 2007, the 1997 Plan had 234,594 unexercised options outstanding and 109,262 shares remain available for future grant. Options granted under the plans have an exercise price equal to the market price at the date of grant, have a maximum term of 10 years and generally become exercisable ratably over a five-year period. There was no stock option grant for the fiscal year ended January 31, 2007.

The shares of common stock issued upon exercise of a previously granted stock option are considered new issuances from shares reserved for issuance upon adoption of the various plans. While the Company does not have a formal written policy detailing such issuance, it requires that the option holders provides a written notice of exercise to the stock plan administrator and payment for the shares prior to issuance of the shares.

Accounting for the Plans

Prior to February 1, 2006, the Company accounted for incentive stock plans in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), and related Interpretations, as permitted by FASB Statement No. 123, "Accounting for Stock Based Compensation". No stock based employee compensation was reflected in net income, as all options granted under those plans had an exercise price equal to the fair value of the underlying common stock on the date of grant. Effective February 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), "Share-Based Payment", using the modified prospective-transition. The modified prospective method was applied to those unvested options issued prior to the Company's adoption that have historically been accounted for under the Intrinsic Value Method. All outstanding options were 100% vested prior to the adoption and no options were granted during fiscal 2006. Accordingly, no compensation expense was recorded on the Company's options during the twelve months ended January 31, 2007. At January 31, 2007, the Company has no unrecognized compensation expense relating to options. The following table illustrates the impact on net earnings and earnings per common share if the fair value method had been applied for all periods presented.

in thousands except per share data	Year ended January 31, **2006**	2005
Net loss, as reported	**$ (9,574)**	$ (13,995)
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of tax effects	**(51)**	(54)
Net loss, pro forma	**$ (9,625)**	$ (14,049)
Basic earnings per share:		
Net income loss, as reported	**$ (0.73)**	$ (1.07)
Net income loss, pro forma	**(0.73)**	(1.07)
Diluted earnings per share:		
Net income loss, as reported	**$ (0.73)**	$ (1.07)
Net income loss, pro forma	**(0.73)**	(1.07)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

Expected life	5 years
Risk-free interest rate	3.6% to 6.26%
Expected volatility	0.26 to 0.42
Expected dividend yield	0.00% to 0.98%

The Company has estimated the fair value of all stock option awards as of the date of grant by applying the Black-Scholes pricing valuation model. The application of this valuation model involves assumptions that are judgmental and sensitive in the determination of compensation expense. Historical information was the primary basis for the selection of the expected volatility and life of the option. The risk-free interest rate was selected based upon the yield of the U.S. Treasury issue with a term equal to the expected life of the option being valued.

A summary of the Company's stock option activity, and related information for the years ended January 31, are as follows:

	2007		2006		2005	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price	Option	Weighted-Average Exercise Price
Outstanding at beginning of year	292,571	$ 11.56	367,888	$ 11.39	372,381	$ 11.30
Granted	—	—	14,000	7.20	12,000	6.89
Exercised	—	—	(2,922)	2.91	(2,563)	2.41
Forfeited	(57,977)	7.66	(86,395)	9.28	(13,930)	8.54
Outstanding at end of year	234,594	12.53	292,571	11.56	367,888	11.17
Exercisable at end of year	234,594	12.53	292,571	$ 11.56	336,352	$ 11.39
Weighted-average fair value of options granted during the year		—		$ 2.78		$ 2.86

The data included in the above table have been retroactively adjusted, if applicable, for stock dividends.

Information regarding stock options outstanding as of January 31, 2007, is as follows:

	Options Outstanding		Options Exercisable	
		Remaining		
Price	Number of Shares	Contractual Life	Number of Shares	Price
$ 8.82	12,100	4.55	12,100	$ 8.82
$ 11.06	92,965	2.47	92,965	$ 11.06
$ 11.65	1,098	2.70	1,098	$ 11.65
$ 12.53	58,564	1.70	58,564	$ 12.53
$ 12.64	69,867	0.67	69,867	$ 12.64
$ 12.53	234,594	1.85	234,594	$ 12.53

As all options had vested prior to February 1, 2006, there was no effect on the statement of operations or cash flows due to the adoption of FASB Statement No. 123(R).

Restricted Stock Unit Awards

On June 30, 2004, the Company granted a total of 270,000 restricted stock units, with an estimated fair value of $6.92 per unit and exercise price of $0.01 per unit, to eligible employees under the 1997 Plan. Interests in such restricted stock units vest ratably over five years, with such units vesting 20% at each anniversary date. At such time that the restricted stock units vest, they become exchangeable for shares of common stock. Compensation expense is recognized based on the estimated fair value of restricted stock units and vesting provisions. Compensation expense incurred in connection with this award was $353,000 for fiscal year ended January 31, 2007; $367,000 for fiscal year ended January 31, 2006; and $230,000 for fiscal year ended January 31, 2005. As of January 31, 2007, there was approximately $853,000 of unrecognized compensation cost related to non-vested restricted stock unit awards, which is expected to be recognized through June 30, 2009.

On January 13, 2006, the Company granted a total of 73,881 restricted stock units, with an estimated fair value of $5.21 per unit and exercise price of $0.01 per unit, to non-employee directors under the 1997 Plan. Interests in such restricted stock units vested 100% on July 5, 2006. Compensation expense is recognized based on the estimated fair value of restricted stock units and vesting provisions. For the twelve months ended January 31, 2007, compensation expense incurred in connection with this award was $343,000. As of January 31, 2007, there was no unrecognized compensation cost related to this award.

On June 20, 2006, the Company granted a total of 17,640 shares of restricted stock, with an estimated fair value of $4.96 per unit and exercise price of $0.01 per unit, to non-employee directors under the 1997 Plan. Interests in such restricted stock units vest 100% on June 19, 2007. Compensation expense is recognized based on the estimated fair value of restricted stock units and vesting provisions. For the twelve months ended January 31, 2007, compensation expense incurred in connection with this award was $58,000. As of January 31, 2007, there was approximately $29,000 of unrecognized compensation cost related to non-vested restricted stock unit awards. The cost is expected to be recognized through May 31, 2007. In connection with the grant of these restricted stock units all outstanding, unexercised stock options held by the non-employee directors were cancelled.

As the compensation cost for the restricted stock units was measured using the estimated fair value on the date of grant and recognized over the vesting period, there was no effect on the statements of operations due to the adoption of FASB Statement No. 123(R). At February 1, 2006, the Company recorded a reclassification of $247,000 from current liabilities to additional paid-in capital.

A summary of the Company's restricted stock unit awards activity, and related information for the years ended January 31, are as follows:

	2006		2005		2004	
	Restricted Stock Units	Weighted-Avg. Fair Value of Restricted Stock Units	Restricted Stock Units	Weighted-Avg. Fair Value of Restricted Stock Units	Restricted Stock Units	Weighted-Avg. Fair Value of Restricted Stock Units
Outstanding at beginning of year	277,881	$ 6.91	270,000	$ 6.92	—	$ —
Granted	17,640	4.96	73,881	5.21	285,000	6.92
Vested	(142,521)	4.99	(54,000)	6.80	—	—
Forfeited	—	—	(12,000)	6.92	(15,000)	6.92
Outstanding at end of year	153,000	6.91	277,881	6.91	270,000	6.92
Weighted-average fair value of restricted stock units granted during the year		$ 4.96		$ 5.21		$ 6.92

The data included in the above table have been retroactively adjusted, if applicable, for stock dividends.

Stockholders' Rights

On October 15, 1996, the Board of Directors declared a dividend of one preferred stock purchase right (a Right) for each outstanding share of the Company's common stock. Each Right entitles a stockholder to purchase for an exercise price of $50.00 ($20.70, as adjusted for stock splits and stock dividends), subject to adjustment, one one-hundredth of a share of Series A Junior Participating Cumulative Preferred Stock of the Company, or under certain circumstances, shares of common stock of the Company or a successor company with a market value equal to two times the exercise price. The Rights are not exercisable, and would only become exercisable for all other persons when any person has acquired or commences to acquire a beneficial interest of at least 20% of the Company's outstanding common stock. The Rights expired on October 25, 2006, have no voting privileges, and may be redeemed by the Board of Directors at a price of $.001 per Right at any time prior to the acquisition of a beneficial ownership of 20% of the outstanding common shares. There are 200,000 shares (483,153 shares as adjusted by stock splits and stock dividends) of Series A Junior Participating Cumulative Preferred Stock reserved for issuance upon exercise of the Rights.

6. Income Taxes

The provision / (benefit) for the last three years are reconciled to the statutory federal income tax rate using the liability method as follows:

		January 31,	
	2007	2006	2005
Statutory	**$ 2,717**	$ (3,292)	$ (4,719)
State taxes (net of federal tax)	**272**	(329)	(472)
Change in valuation allowance	**(2,432)**	3,721	5,219
Other	**(111)**	(209)	87
	$ 446	$ (109)	$ 115

Significant components of the (benefit) provision for income taxes (in thousands) attributed to continuing operations are as follows:

		January 31,	
	2007	2006	2005
Current			
Federal	**$ 220**	$ —	$ —
State	**(34)**	(109)	115
	186	(109)	115
Deferred			
Federal	**2,205**	(3,502)	(4,466)
State	**487**	(219)	(753)
	2,692	(3,721)	(5,219)
Valuation allowance	**(2,432)**	3,721	5,219
	260	—	—
	$ 446	$ (109)	$ 115

Deferred tax assets and liabilities (in thousands) are comprised of the following:

	January 31,	
	2007	2006
Deferred tax assets		
Accrued vacation and sick leave	**$ 979**	$ 926
Retirement plans	**6,517**	4,953
Insurance reserves	**1,060**	606
Inventory	**858**	804
Warranty	**655**	561
Net operating loss carry forwards	**6,872**	11,058
	16,941	18,908
Deferred tax liabilities		
Tax in excess of book depreciation	**(1,407)**	(2,062)
Capitalized software development costs	**—**	(53)
Other	**(204)**	(153)
	(1,611)	(2,268)
Valuation allowance	**(15,591)**	(16,640)
Net deferred tax liability	**$ (260)**	$ —

In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income or reversal of deferred tax liabilities during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based on this consideration, the Company anticipates that it is more likely than not that the net of certain deferred tax assets will not be realized, and a valuation allowance has been recorded against certain of the net deferred tax assets at January 31, 2007 and January 31, 2006.

At January 31, 2007, the Company has net operating losses carried forward for federal and state income tax purposes, expiring at various dates through 2026 if not utilized. Federal net operating losses that can potentially be carried forward total approximately $15,409,000 at January 31, 2007. State net operating losses that can potentially be carried forward total approximately $32,791,000 at January 31, 2007.

For the fiscal year ended January 31, 2007, the Company benefited from net operating loss carryforwards for both federal and state income taxes, and recognized an income tax expense of $446,000. The income tax expense is primarily attributable to alternative minimum taxes combined with income and franchise taxes as required by various states. For the fiscal year ended January 31, 2006, the Company incurred and income tax benefit of $109,000 due to an adjustment of deferred tax reserves partially offset by income and franchise taxes as required by various states.

7. Commitments

The Company has operating leases on real property and equipment, which expire at various dates. The Torrance manufacturing and distribution facility is leased under a 5-year operating lease that expires at the end of 2010. The Company leases machinery and equipment under a 10-year operating lease arrangement. The Company has the option of buying out the leases three to five years into the lease period. The Company leases trucks, automobiles, and forklifts under operating leases that include certain fleet management and maintenance services. Certain of the leases contain renewal, purchase options and require payment for property taxes and insurance.

Minimum future lease payments (in thousands) for operating leases in effect as of January 31, 2007, are as follows:

Year ending January 31,	
2008	$ 6,244
2009	4,825
2010	4,184
2011	792
2012	608
Thereafter	0

Rent expense relating to operating leases was as follows (in thousands):

Year ending January 31,	
2007	$ 8,019
2006	9,457
2005	9,050

The Company has issued purchase commitments for raw materials at January 31, 2007, of approximately $18.10 million. There were no commitments in excess of normal operating requirements. All purchase commitments will be settled in the fiscal year ending January 31, 2009.

8. Contingencies

The Company and other furniture manufacturers are subject to federal, state and local laws and regulations relating to the discharge of materials into the environment and the generation, handling, storage, transportation and disposal of waste and hazardous materials. The Company has expended, and expects to continue to spend, significant amounts in the future to comply with environmental laws. Normal recurring expenses relating to operating our factories in a manner that meets or exceeds environmental laws are matched to the cost of producing inventory. Despite our significant dedication to operating in compliance with applicable laws, there is a risk that the Company could fail to comply with a regulation or that applicable laws and regulations change. On these occasions, the Company records liabilities for remediation costs when remediation costs are probable and can be reasonably estimated.

The Company is subject to contingencies pursuant to environmental laws and regulations that in the future may require the Company to take action to correct the effects on the environment of prior disposal practices or releases of chemical or petroleum substances by the Company or other parties. We have been identified as a potentially responsible party pursuant to the Comprehensive Environmental Response Compensation and Liability Act, or CERCLA, for remediation costs associated with waste disposal sites previously used by us. In general, CERCLA can impose liability for costs to investigate and remediate contamination without regard to fault or the legality of disposal and, under certain circumstances, liability may be joint and several, resulting in one party being held responsible for the entire obligation. We reserve amounts for such matters when expenditures are probable and reasonably estimable. At January 31, 2007 and 2006, the Company had reserves of approximately $100,000 for such environmental contingencies. An estimate of liability in excess of this amount cannot be made.

The Company has a self-insured retention for product and general liability losses up to $500,000 per occurrence, workers' compensation liability losses up to $250,000 and automobile liability losses up to $50,000 per occurrence. The Company has purchased insurance to cover losses in excess of the retention up to a limit of $30,000,000. The Company has obtained an actuarial estimate of its total expected future losses for liability claims and recorded a liability equal to the net present value of $2,835,000 and $1,600,000 at January 31, 2007 and 2006, respectively, based upon the Company's estimated payout period of four years using a 5.75% discount rate.

Workers' compensation, automobile, general and product liability claims may be asserted in the future for events not currently known by management. Management does not anticipate that any related settlement, after consideration of the existing reserve for claims incurred and potential insurance recovery, would have a material adverse effect on the Company's financial position, results of operations or cash flows. Estimated payments under self-insurance programs are as follows:

Year ending January 31,	
2008	$ 620
2009	620
2010	620
2011	620
2012	610
Total	3,090
Discount to net present value	(255)
Thereafter	$ 2,835

The Company and its subsidiaries are defendants in various legal proceedings resulting from operations in the normal course of business. It is the opinion of management, in consultation with legal counsel, that the ultimate outcome of all such matters will not materially affect the Company's financial position, results of operations or cash flows.

9. Warranty

The Company accrues an estimate of its exposure to warranty claims based upon both current and historical product sales data and warranty costs incurred. The majority of the Company's products sold through January 31, 2005, carry a five-year warranty. Effective February 1, 2005, the Company extended its standard warranty period to 10 years. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. The warranty liability is in accrued liabilities in the accompanying consolidated balance sheet.

Changes in the Company's warranty liability were as follows (in thousands):

	January 31,	
	2007	2006
Beginning balance	**$ 1,500**	$ 1,500
Provision	**1,154**	900
Costs incurred	**(904)**	(900)
Ending balance	**$ 1,750**	$ 1,500

10. Other Financing Activities

On June 6, 2006, WEDBUSH, Inc. and Wedbush Morgan Securities, Inc. (together with WEDBUSH, Inc., the "Purchasers"), entered into a stock purchase agreement (the "Agreement") with the Company. Pursuant to the Agreement, (a) the Purchasers purchased from the Company shares (the "Shares") of the Company's common stock yielding gross proceeds to the Company of $5,000,000 at a purchase price per share of $4.66 (the "Per Share Purchase Price") and (b) the Company issued warrants to the Purchasers exercisable for 268,010 shares of common stock pursuant to which the Purchasers will have the right to acquire the 268,010 shares at an exercise price of 120% of the Per Share Purchase Price during the first three years following the closing of the transaction and at 130% of the Per Share Purchase Price during the fourth and fifth years following the closing of the transaction. The Company filed a Registration Statement on Form S-3 registering the resale of the Shares on July 6, 2006 and amended that registration statement on August 17, 2006. The Registration Statement became effective on September 18, 2006. Wedbush Morgan holds the securities purchased pursuant to the Agreement as nominee on behalf those of its clients which purchased the securities.

On June 26, 2006, certain members of management and certain Directors (the "Follow-on Purchasers") entered into a stock purchase agreement with the Company to purchase shares of common stock and warrants. On August 29, 2006, this agreement was rescinded and replaced with a similar agreement for the purchase of 57,455 shares at a purchase price per share of $5.02 (the "Follow-on Per Share Purchase Price") yielding gross proceeds to the Company of approximately $288,000. Additionally the Company issued warrants to the Follow-on Purchasers exercisable for 14,364 shares of common stock pursuant to which the Follow-on Purchasers will have the right to acquire the 14,364 shares at an exercise price of 120% of the Follow-on Per Share Purchase Price during the first three years following the closing of the transaction and at 130% of the Follow-on Per Share Purchase Price during the fourth and fifth years following the closing of the transaction. The transaction closed during the third quarter ended October 31, 2006.

The securities sold to the Purchasers and Follow-on Purchasers were issued pursuant to the exemption from the registration requirements of the Securities Act of 1933, as amended (the "Securities Act"), afforded by Section 4(2) of the Securities Act and Rule 506 of Regulation D thereunder, as a transaction to accredited and sophisticated investors not involving a public offering. The proceeds from the sale of the Shares were used for general corporate purposes, and the proceeds, if any, received from the exercise of the warrant agreements will be used to reduce outstanding indebtedness and for general corporate purposes. At January 31, 2007, the Company incurred $537,000 in closing costs, which were netted against the proceeds received.

11. Quarterly Results (Unaudited)

The Company's quarterly results for the years ended January 31, 2007 and 2006, are summarized as follows (in thousands, except per share data):

	Three months ended			
	Apr. 30	Jul. 31	Oct. 31	Jan. 31
Year ended January 31, 2007:				
Net sales	**$ 34,515**	**$ 78,595**	**$ 73,678**	**$ 36,319**
Gross profit	**11,494**	**28,383**	**27,092**	**11,643**
Net (loss) income	**(3,267)**	**7,832**	**5,833**	**(2,853)**
Per common share(1)				
Net (loss) income				
Basic	**(0.25)**	**0.58**	**0.41**	**(0.20)**
Assuming dilution	**(0.25)**	**0.58**	**0.41**	**(0.20)**
Year ended January 31, 2006:				
Net sales	$ 33,254	$ 75,906	$ 70,484	$ 34,806
Gross profit	9,407	26,504	20,084	8,670
Net (loss) income	(5,683)	6,085	(2,194)	(7,782)
Per common share(1)				
Net (loss) income				
Basic	(0.43)	0.46	(0.17)	(0.59)
Assuming dilution	(0.43)	0.46	(0.17)	(0.59)

(1) Per common share amounts for the quarters and full years have each been calculated separately. Accordingly, quarterly amounts may not add to the annual amounts because of differences in the average common shares outstanding during each period and with regard to diluted per common share amounts only, because of the effect of potentially dilutive securities only in the periods in which the effect would have been dilutive.

Annual Meeting

The Annual Meeting of Virco stockholders will be held on Tuesday, June 19, 2007, at 10:00 a.m., at 2027 Harpers Way, Torrance, California 90501. The record date for this meeting is April 27, 2007. The Proxy Statement and Proxy pertaining to this meeting will be mailed on or about May 21, 2007.

SEC Form 10-K

A copy of the annual report to the Securities and Exchange Commission on Form 10-K may be obtained without charge upon written request to:

Corporate Secretary
Virco Mfg. Corporation
2027 Harpers Way
Torrance, CA 90501
www.virco.com

Virco Common Stock

The American Stock Exchange is the principal market on which Virco Mfg. Corporation (VIR) stock is traded. As of April 27, 2007, there were approximately 358 registered stockholders according to the transfer agent records. There are approximately 1,150 beneficial stockholders.

Stockholder Records

Records pertaining to stockholdings and dividends are maintained by Mellon Investor Services. Inquiries with respect to these matters, as well as notices of address changes, should be directed to:

Mellon Investor Services, LLP
Stock Transfer Department
Newport Office Center VII
480 Washington Blvd.
Jersey City, NJ 07310
Phone: (800) 522-6645
Foreign: (201) 680-6578
TDD for Hearing Impaired: (800) 231-5469
TDD for Foreign Shareowners: (201) 680-6610
website address: www.melloninvestor.com

If a stock certificate is lost or mutilated, immediately communicate with Mellon Investor Services at the above addresses.

Additional Services for Stockholders

Information about the Company is now available to stockholders at the Company's website (www.virco.com). A brief description of Virco's product line is offered together with illustrations showing a sampling of our furniture.

Quarterly Dividend and Stock Market Information

	Cash Dividends Declared		Common Stock Range			
	2006	2005	**2006**		2005	
			High	**Low**	High	Low
1st Quarter	**$ _**	$ _	**$ 6.63**	**$ 4.40**	$ 7.94	$ 7.42
2nd Quarter	**_**	_	**5.11**	**4.50**	7.47	6.60
3rd Quarter	**_**	_	**6.00**	**4.36**	7.94	6.64
4th Quarter	**_**	_	**9.50**	**5.62**	7.15	5.13

The data included in the above table has been retroactively adjusted, if applicable, for the stock split and stock dividends.

Directors

Robert A. Virtue
President, Chairman of the Board
and Chief Executive Officer

Donald S. Friesz
Former Vice President - Sales
and Marketing

Evan M. Gruber
Chief Executive Officer
Class Leasing, Inc.

Robert K. Montgomery
Partner, Gibson Dunn & Crutcher

Albert J. Moyer
Board Member of California
Amplifier, Inc., Collectors Universe,
Inc., and LaserCard Corporation

Glen D. Parish
Former Vice President and General
Manager Conway Division

Donald A. Patrick
Management Consultant
Former Vice President Diversified
Business Resources, Inc.

Douglas A. Virtue
Executive Vice President

Dr. James R. Wilburn
Dean of the School of Public Policy
Pepperdine University

Officers

Robert A. Virtue
President, Chairman of the Board
and Chief Executive Officer

Douglas A. Virtue
Executive Vice President

J. Scott Bell
Vice President and General Manager
Conway Division

Robert E. Dose
Vice President - Finance
Secretary and Treasurer

Angelica Gamble
Vice President - Human Resources

Patricia Quinones
Vice President
Logistics and Marketing Services
and Information Technology

D. Randal Smith
Vice President - Marketing

Lori L. Swafford
Vice President - Legal Affairs

Nick Wilson
Vice President and General Manager
Torrance Division

Larry O. Wonder
Vice President - Sales

Bassey Yau
Corporate Controller,
Assistant Secretary and Treasurer

Independent Registered Public Accounting Firm

Ernst & Young LLP
725 South Figueroa Street,
Suite 500
Los Angeles, CA 90017

Legal Counsel

Gibson, Dunn & Crutcher
2029 Century Park East
Los Angeles, California 90067

Corporate Headquarters

2027 Harpers Way
Torrance, California 90501
(310) 533-0474

Major Facilities

Torrance Division
2027 Harpers Way
Torrance, California 90501

Conway Division
Highway 65, South
Conway, Arkansas 72032

"Upon the subject of education, not presuming to dictate any plan or system respecting it, I can only say that I view it as the most important subject which we as a people may be engaged in.

–Abraham Lincoln

2006 Annual Report

VIRCO MFG. CORPORATION

equipment for educators™

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