

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

FORM 10-K

(MARK ONE)

ANNUAL REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED JUNE 30, 1998; OR

TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.

FOR THE TRANSITION PERIOD FROM TO .

COMMISSION FILE NUMBER 0-23125

OSI SYSTEMS, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

CALIFORNIA
(STATE OR OTHER JURISDICTION
OF INCORPORATION OR ORGANIZATION)

33-0238801
(I.R.S. EMPLOYER
IDENTIFICATION NO.)

12525 CHADRON AVENUE HAWTHORNE, CALIFORNIA
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

90250
(ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (310) 978-0516

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
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Common Stock, No Par Value

Nasdaq

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the voting stock of the registrant held by non-affiliates of the registrant, based upon the closing sales price of the Common Stock on the Nasdaq National Market on September 18, 1998, was \$40,554,480.

The number of shares of the registrant's Common Stock outstanding as of September 18, 1998 was 9,694,165.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement relating to the 1998 Annual Meeting of Stockholders (to be filed subsequently) are incorporated by reference into Part III.

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PART I

ITEM 1. BUSINESS

GENERAL

The Company is a vertically integrated worldwide provider of devices, subsystems and end-products based on optoelectronic technology. The Company designs and manufactures optoelectronic devices and value-added subsystems for original equipment manufacturers ("OEMs") for use in a broad range of applications, including security, medical diagnostics, telecommunications, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products that it markets worldwide to end users under the "Rapiscan" and "SECURE" brand names. These products are used to inspect baggage, cargo, people and other objects for weapons, explosives, drugs and other contraband. In fiscal 1998, revenues from the sale of optoelectronic devices and subsystems amounted to \$50.1 million, or approximately 53.4%, of the Company's revenues, while revenues from sales of security and inspection products amounted to \$43.8 million, or approximately 46.6% of the Company's revenues. Unless the context otherwise requires, the term the "Company" as used herein includes OSI Systems, Inc., a California corporation, and its subsidiaries.

INDUSTRY OVERVIEW

The Company's products currently address two principal markets. The Company's optoelectronic devices and subsystems are designed and manufactured primarily for sale to OEMs, while the Company's security products are sold to end-users.

Optoelectronic Devices and Subsystems. Optoelectronic devices consist of both active components, such as silicon photodiodes that sense light of varying wavelengths and convert the light detected into electronic signals, and passive components, such as lenses, prisms, filters and mirrors. An optoelectronic subsystem typically consists of one or more optoelectronic devices that are combined with other electronic components for integration into an end-product. Optoelectronic devices and subsystems are used for a wide variety of applications ranging from simple functions, such as the detection of paper in the print path of a laser printer, to complex monitoring, measurement or positioning functions, such as in industrial robotics where the subsystem is used to detect the exact position, motion or size of another object. Because optoelectronic devices and subsystems can be used in a wide variety of measurement, control and monitoring applications, optoelectronics may be used in a broad array of industrial applications.

The Company believes that in recent years advances in technology and reductions in the cost of key components of optoelectronic systems, including computer processing power and memory, have broadened the market by enabling the use of optoelectronic devices in a greater number of applications. In addition, the Company believes that there is a trend among OEMs to increasingly outsource the design and manufacture of optoelectronic subsystems to fully integrated, independent manufacturers who may have greater specialization, broader expertise, and the ability and flexibility to respond in shorter time periods than the OEM could accomplish in-house. The Company believes that its high level of vertical integration, substantial engineering resources, expertise in the use and application of optoelectronic technology, and low-cost international manufacturing operations enable it to compete in the market for optoelectronic devices and subsystems.

Security and Inspection Products. A variety of products are currently used worldwide in security and inspection applications. These products include single energy x-ray equipment, dual energy x-ray equipment, trace detection systems that detect particulate and chemical traces of explosive materials, computer tomography ("CT"), scanners and x-ray machines employing backscatter detection technology. To date, most of these products have been deployed primarily at commercial airports worldwide. The Company believes that the growth in the market for security and inspection products will continue to be driven by the increased perception of threat fueled by recent terrorist incidents, increased government mandates and appropriations, and the emergence of a growing market for the non-security applications of its products.

In the 1970s, principally in response to civilian airline hijackings, the U.S. Federal Aviation Administration ("FAA") established security standards by setting guidelines for the screening of carry-on baggage for weapons such as guns and knives. These standards were later mandated by the United Nations for adoption by all of its member states. The Company believes that to date the imposition of these standards has resulted in the installation of over 10,000 x-ray inspection systems installed in airports worldwide. Additionally, the United Kingdom Department of Transport has required the United Kingdom's commercial airports to deploy systems for 100% screening of international checked baggage by the end of 1998, and the European Civil Aviation Conference, an organization of 33 member states, has agreed to implement 100% screening of international checked baggage by the year 2000. In the United States, largely in response to the explosion of Pan Am Flight 103 in December 1988, Congress enacted the Aviation Security Improvement Act of 1990 which, among other initiatives, directed the FAA to establish and implement strict security measures and to deploy advanced technology for the detection of various contraband, including explosives, drugs, and currency. In July 1996, President Clinton formed the White House Commission on Aviation Safety and Security (the "Gore Commission"), to review airline and airport security and to oversee aviation safety. In response to the initial report released by the Gore Commission, the United States enacted legislation that includes \$144 million in appropriations for the initial deployment of advanced security and inspection technology at major U.S. airports. The Clinton Administration is proposing budgeting \$100 million in fiscal 1999 for the purchase of state-of-the-art detection equipment for rapid deployment in every major U.S. airport.

X-ray inspection equipment, such as that sold by the Company, is also increasingly being used for a number of purposes not related to security. Newer versions of x-ray inspection equipment combine x-ray inspection with computer image enhancement capabilities and can be applied to various non-security purposes such as the detection of narcotics, gold and currency, the inspection of agricultural products, and the inspection of cargo by customs officers and international shippers.

GROWTH STRATEGY

The Company's objectives are to be a leading provider of specialized optoelectronic products, to enhance its position in the international inspection and detection marketplace and to leverage its expertise in the optoelectronic technology industry by entering into new end-product markets on a selective basis. Key elements of this strategy include:

Leverage its Optoelectronic Design and Manufacturing Expertise to Address New Applications. The Company believes that one of its primary competitive strengths is its expertise in designing and manufacturing specialized optoelectronic subsystems for its OEM customers in a cost-effective manner. The Company currently designs and manufactures devices and subsystems for over 200 customers serving over 100 applications. The Company has developed this expertise in the past through internal research and development efforts and through selective acquisitions. In 1990, the Company acquired UDT Sensors, Inc. ("UDT Sensors") to broaden its expertise and capabilities in developing and manufacturing optoelectronic devices and subsystems. In 1993, the Company acquired Rapiscan Security Products Limited ("Rapiscan U.K.") and, through Rapiscan Security Products (U.S.A.), Inc. ("Rapiscan U.S.A."), commenced its operations as a provider of security and inspection products in the United States. Thereafter, in 1993, the Company acquired Ferson Optics, Inc. ("Ferson") for its passive optic technologies. In 1994, the Company commenced operations of Opto Sensors (Malaysia) Sdn. Bhd. ("OSI Malaysia") to take advantage of low cost manufacturing. In 1997, the Company acquired Advanced Micro Electronics AS ("AME") for AME's hybrid optoelectronic capabilities.

In 1998, the Company expanded its operations in the field of optoelectronic devices used for medical diagnostic applications. The Company acquired Osteometer MediTech A/S ("Osteometer"), a Danish manufacturer of diagnostic scanners used to detect osteoporosis. The Company also made investments in other companies. See "Recent Developments" below.

The Company intends to continue to build this expertise in order to address a greater number of applications. By expanding the number of potential applications its products may serve, the Company intends to increase its business with existing customers and attract new customers.

Further Penetrate Existing Security and Inspection Markets and Expand into Other Markets. For the year ended June 30, 1998, approximately 22.0% of the Company's security and inspection products were sold to airports or airlines for security purposes, with the remainder of these products being sold to other facilities for both security and non-security related purposes. The Company intends to continue to expand its sales and marketing efforts both domestically and internationally to capitalize on opportunities in its existing markets for new installations as well as opportunities to replace, service and upgrade existing security installations. In addition, through research and development and selective acquisitions, the Company intends to enhance and expand its current product offering to better address new applications including automatic bomb detection and cargo scanning. In January 1998, the Company's subsidiary, Rapiscan U.S.A., acquired the "SECURE" product line from Nicolet Imaging Systems, a division of ThermoSpectra Corporation ("ThermoSpectra"), relating to x-ray machines employing backscatter detection technology, which are used to inspect people. See "Recent Developments" below.

The Company believes that this strategy will enable it to take advantage of the growth its existing markets are experiencing and to benefit from additional growth that these new and enhanced products will provide. The Company believes that sales of its security and inspection products at locations other than airports will constitute an increasingly larger portion of its sales in the future.

Capitalize on Vertical Integration. The Company believes that it offers significant added value to its OEM customers by providing a full range of vertically integrated services including component design and customization, subsystem concept design and application engineering, product prototyping and development, and efficient pre-production, short-run and high volume manufacturing. The Company believes that its vertical integration differentiates it from many of its competitors and provides value to its OEM customers, who can rely on the Company to be an integrated supplier of an optoelectronic subsystem. In addition, the Company's vertical integration provides several other advantages in both its optoelectronic devices and subsystems and security and detection product lines. These advantages include reduced manufacturing and delivery times, lower costs due to its access to competitive international labor markets and direct sourcing of raw materials, and quality control. The Company intends to continue to leverage its vertically integrated services to create greater value for its customers in the design and manufacturing of its products. The Company believes that this strategy better positions the Company for penetration into other end markets.

Capitalize on Global Presence. The Company operates in three locations in the United States, three in Europe and two in Asia. The Company views its international operations as providing an important strategic advantage over competitors in both the optoelectronic device and subsystem market and the security and inspection market for three primary reasons. First, international manufacturing facilities allow the Company to take advantage of competitive labor rates in order to be a low cost producer. Second, its international offices strengthen its sales and marketing efforts and its ability to maintain and repair its systems by providing direct access to growing foreign markets and to its existing international customer base. Third, multiple manufacturing locations allow the Company to reduce delivery times to its global customer base. In the future, the Company intends to develop new sources of manufacturing and sales capabilities to maintain and enhance the benefits of its international presence.

Selectively Enter New End Markets. The Company intends to selectively enter new end markets that complement its existing capabilities in designing, developing and manufacturing optoelectronic devices and subsystems, such as the expansion during fiscal 1998 into optoelectronic products for medical diagnostic applications. The Company believes that by manufacturing other end products which rely on the technological capabilities of the Company, it can leverage its existing integrated design and manufacturing infrastructure to capture greater margins and build a significant presence in new end markets which present attractive competitive market dynamics. The Company intends to achieve this strategy through internal growth and through selective acquisitions of end-product manufacturers.

RECENT DEVELOPMENTS

In furtherance of the Company's growth strategy, in January 1998 Rapiscan U.S.A. acquired the "SECURE" product line from ThermoSpectra. The purchased assets include, among other things, equipment, inventory, intellectual property rights relating to x-ray machines and x-ray backscatter detection technology (including patents and patent applications), business contracts and purchase orders, for use in the manufacture and sale of security screening products under the names "SECURE", "SECURE 1000", "SECURE 2000" and "Hands-Off Security Screening".

Subsequent to the end of the fiscal year ended June 30, 1998, the Company acquired one additional business and made investments in the aggregate amount of approximately \$800,000 in two other businesses. In September 1998, the Company acquired Osteometer, a Danish manufacturer of densitometers for scanning osteoporosis. Osteometer concentrates on the development of small, cost optimized scanners making it possible for small clinics to offer their patients a cost effective diagnosis of osteoporosis and is committed to the development of scientifically and clinically validated devices that result in accurate, precise, reliable and cost effective diagnosis. The acquisition is the Company's largest to date.

PRODUCTS AND TECHNOLOGY

The Company designs, develops, manufactures and sells products based on its core optoelectronic technology. These products range from discrete devices to value-added subsystems to complete x-ray security and inspection products.

Discrete Devices and Subsystems. Optoelectronic devices generally consist of both active and passive components. Active components sense light of varying wavelengths and convert the light detected into electronic signals, whereas passive components amplify, separate or reflect light. Active components manufactured by the Company consist of silicon photodiodes and hybrid photodetectors. Passive components include lenses, prisms, filters, mirrors and other precision optical products that are used by the Company in the manufacture of its optoelectronic products or are sold to others for use in telescopes, laser printers, copiers, microscopes and other detection and vision equipment. The devices manufactured by the Company are both standard products and products customized for specific applications. Most of the devices manufactured by the Company are incorporated by it into the subsystems that it manufactures. The Company does, however, also sell its discrete devices separately to OEMs. Direct sales of devices to third parties constituted less than 10% of the Company's revenues in fiscal 1998.

In addition to the manufacture of discrete devices, the Company also specializes in designing and manufacturing customized optoelectronic subsystems for use in a wide range of products and equipment. An optoelectronic subsystem typically consists of one or more optoelectronic devices that are combined with other electronic components and packaging for use in an end-product. The composition of a subsystem can range from a simple assembly of various optoelectronic devices that are incorporated into other subsystems (for example, a printed circuit board containing the Company's optoelectronic devices), to complete end-products (for example, medical pulse oximeter probes that are manufactured and packaged by the Company on behalf of the OEM customer and then shipped directly to the customer or the customer's distributors). Since the end of fiscal 1996, the Company has manufactured subsystems for a variety of applications, including the following: imaging electronics for medical CT scanners, disposable and reusable medical probes for use with medical pulse oximetry equipment, components and subsystems for laser gyroscopes used in military and commercial aviation, optoelectronic subsystems for slot machines, laser subsystems in military helicopter gun sighting equipment, positioning subassemblies for computer peripheral equipment, alignment subsystems for laser heads in optical disc players, and ultra-violet fire detection subsystems for submarines and surface ships.

Security and Inspection Equipment. The Company manufactures and sells a range of security and inspection equipment that it markets under the "Rapiscan" and "SECURE" brand names. To date, the security and inspection equipment has principally been used at airports to inspect carry-on and checked baggage for guns

and knives. However, inspection products are increasingly being used for both security purposes at a wide range of facilities other than airports and for other non-security purposes. For fiscal years 1996, 1997 and 1998, approximately 33.1%, 27.3% and 22.0% respectively, of the Company's security and inspection revenues were derived from the sale of inspection products to airlines and airports, and the balance of such revenues were derived from all other sales. The Company believes that sales of its inspection products for use at non-airport locations will constitute an increasingly larger portion of future revenues.

The Company's inspection and detection products combine the use of x-ray technology with the Company's core optoelectronic capabilities. The base models of its product line use single energy x-ray technology and are used for identifying weapons with distinct shapes, such as guns and knives. The Company's enhanced models combine dual- or multi-energy x-ray technology with computer enhanced imaging technology to facilitate the detection of materials such as explosives, narcotics, currency or other contraband. While all x-ray systems produce a two-dimensional image of the contents of the inspected material, the dual-energy x-ray systems also measure the x-ray absorption of the inspected materials' contents at two x-ray energies to determine the atomic number, mass and other characteristics of the object's contents. The different organic and non-organic substances in the inspected material are displayed in various colors. This information is then displayed to an operator of the inspection equipment who can identify and differentiate the objects in the inspected materials. These systems range in size from compact tabletop systems to large cargo pallet inspection systems weighing over 1,000 lbs.

Currently, all of the Company's inspection products require an operator to monitor the images produced by the inspection equipment. Depending on the model, the Company's products permit the operator to inspect the contents of packages at varying image modes and magnifications. The images range from the monochrome and pseudo-color images produced by single x-ray imaging systems, to high resolution, multi-color images in the Company's computer enhanced dual-energy models. The Company believes that its Rapiscan 500 Series provides one of the highest quality images currently available in the x-ray security and inspection industry.

The Company has also moved into the field of inspection of people with the recent acquisition of the "SECURE" brand product line that uses x-ray systems employing backscatter detection technology. SECURE 1000 is an electronic screening system for hands off people screening. The system is based on an extremely low dose of backscatter x-ray imaging to detect contraband and weapons concealed underneath clothing and hair. The system provides better screening than metal detectors as it detects very small amounts of metal as well as non-metallic contraband.

In order to monitor the performance of operators of the x-ray baggage screening systems that are used in the United States airports, the FAA has implemented a computer-based training and evaluation program known as the Screener Proficiency Evaluation And Reporting System ("SPEARS"). To continuously monitor the effectiveness of the screening system and its operator, test threat images, such as weapons, are projected into the images of actual parcels being inspected. The results of these tests are available to government agencies.

The following table sets forth certain information related to the standard security and inspection products currently offered by the Company. The Company does, however, also customize its standard products to suit specific applications and customer requirements:

MODEL (TECHNOLOGY)	APPLICATIONS	SELECTED INSTALLATIONS
Rapiscan 19 (single energy)	Inspection of incoming package	Embassies
Rapiscan 119 (single energy)		Post offices Courthouses High risk office buildings Manufacturing companies
Rapiscan 300 Series (160 kV x-ray source, single energy and dual energy)	Inspection of hand carried baggage	Airports Prisons Government buildings Nuclear facilities
Rapiscan 500 Series- Standard Tunnel (single view and dual view 160 kV x-ray source, single energy and dual energy)	Airport hand carried and checked baggage Pallet inspection Customs inspections Agriculture inspection	Airports Cruise ships Freight shippers Border crossings
Rapiscan 500 Series- Large Tunnel (single view and dual view 320-450 kV x-ray source)	Large pallet inspection Customs inspections	Airports Freight shippers Border crossings High risk seaport locations
Rapiscan 500 Series- Mobile Systems (x-ray van or trailer)	Mobile x-ray inspection	Conventions and special events Airports Customs inspections Border crossing
SECURE 1000 (non-intrusive personal screening system)	High Security Personnel Inspection	Prisons Military Facilities
SPEAR (Threat Image Projection ("TIP") Software)	Performance Monitoring	Any Rapiscan 500 Series System

In addition to its x-ray security and inspection products, the Company also markets three models of an archway walk-through metal detector and two models of a hand-held metal detector. These products are used to detect metal weapons such as guns and knives and are installed at airports and other locations, including prisons and schools.

Rapiscan U.S.A. has entered into a non-exclusive patent license agreement with EG&G, Inc. ("EG&G"). Under the license, Rapiscan U.S.A. is permitted to make, use and sell or otherwise dispose of security and inspection products that use an x-ray line scan system for baggage inspection purposes covered by EG&G's patent. The patent, which expires in 2000, does not affect sales of the Company's security and inspection products manufactured and sold outside of the United States.

Medical Imaging Equipment. The Company has also moved into the field of manufacturing and selling the DTX 200 (DEXACARE) and U.S. Food & Drug Administration ("FDA")-approved forearm DEXA (Dual Energy X-Ray) densitometer, which is used to diagnose osteoporosis as well as to provide follow-up bone density measurements. The Company also produces the ultra-sound DTU-one, the first commercially available scanner using imaging capability for the diagnosis of osteoporosis. The DTU-one is currently not available for sale in the United States, although the Company filed for pre-market approval from the FDA in Spring 1998.

MARKETS, CUSTOMERS AND APPLICATIONS

Optoelectronic Devices and Subsystems. The Company's optoelectronic devices and subsystems are used in a broad range of products by a variety of customers. The following chart illustrates, for the year ended June 30, 1998: (i) the major product categories for which the Company provided optoelectronic products; and (ii) certain representative customers in each such category. The Company expects that the list of product categories, the amount of business derived from each such product category, and the composition of its major customers will vary from period to period.

PRODUCT CATEGORY -----	REPRESENTATIVE MAJOR CUSTOMERS -----
Computed Tomography and X-Ray Imaging	Picker International Hologic InVision Technologies
Aerospace and Avionics	Adcole Allied Signal Honeywell Avionics Litton Systems
Medical Monitoring	Datascope BioChem International Criticare Systems
Analytical, Medical Diagnostics and Particle Analyzers	Abaxis Leica Coulter Corporation
Office Automation and Computer Peripherals	Xerox Eastman Kodak Dr. Johannes Heidenhain
Construction, Industrial Automation and Exploration	Schlumberger Spectra Physics Baumer Electric
Military/Defense and Weapons Simulations	Lockheed Martin (Loral) Hughes (HDOS) Norsk Forsvarstekmol
Bar Code Scanners	Symbol Technologies OCLI
Gaming Industry	Bally Gaming Ardac

During fiscal 1998, the Company entered into a number of significant agreements for the sale of the Company's optoelectronic devices and subsystems. Some of the principal agreements are the following.

The Company entered into a Master Purchase Agreement with a long-term customer, for \$31.1 million of optical subsystems to be used in medical products. Of this amount, \$8.1 million represents a firm order and the rest is cancellable based on convenience and other terms of the agreement. The subsystems will be delivered over a four-year period and have begun to be shipped.

The Company received a \$2.3 million purchase commitment from a U.S. defense systems manufacturer, for optoelectronic subsystems. These subsystems will be shipped during fiscal years 1999 and 2000.

Subsequent to the end of the fiscal year, the Company received an order of approximately \$10.0 million from the seismic services division of the world's largest oil services company. The contract is for hybrid optoelectronic subsystems that will be incorporated into sea-floor scanning devices. These systems will be shipped during fiscal years 1999 and 2000.

Security and Inspection Products. Since entering the security and inspection products market in 1993, the Company has shipped approximately 2,500 units to approximately 50 countries. The following is a list of certain customers and/or installations that have purchased the Company's security and inspection products since January 1993:

OVERSEAS

DOMESTIC

Nanjing Airport; People's Republic of China
 Prague Airport; Czech Republic
 Gatwick Airport; England
 Heathrow Airport; England
 TNT Freight; England
 Finnish Customs; Finland
 Indian Customs; India
 Japanese Embassies; worldwide
 Malaysian Airport Board; Malaysia
 New Zealand Customs; New Zealand
 Pakistan Airports; Pakistan
 Doha International Airport; Qatar
 HAJ Terminal; Saudi Arabia
 Spanish Radio/Television; Spain
 Sri Lanka Government; Sri Lanka
 Dubai Airport; U.A.E.
 Ukraine Airport; Ukraine
 United Kingdom Prison System; United Kingdom

American Airlines
 Bush Intercontinental Airport
 Continental Airlines
 Delta Airlines
 Federal Courthouses
 Federal Reserve Bank
 JFK International Airport
 Los Angeles County Courthouse
 Los Angeles International Airport
 Miami Airport
 Orlando Airport
 Ronald Reagan National Airport
 USAir
 U.S. Department of Corrections

Because the market for most security and inspection products developed in response to civilian airline hijackings, historically a large portion of the Company's security and inspection products were sold and continue to be sold for use at airports. Recently, however, the Company's security and inspection products have been used for security purposes at locations in addition to airports, such as courthouses, government buildings, mail rooms, schools, prisons and at unique locations such as Buckingham Palace in London, England. In addition, the Company's security and inspection products are increasingly being used for non-security purposes, such as for cargo inspection to detect narcotics and contraband, prevention of pilferage at semiconductor manufacturing facilities, quality assurance for agricultural products, and the detection of gold and currency.

During fiscal 1998, the Company entered into a number of significant agreements for the development and sale of the Company's security and inspection products. Some of the principal agreements are the following.

In December 1997, the Company's Indian joint venture, ECIL-Rapiscan Security Products Limited ("ECIL Rapiscan"), in which the Company owns a 36.0% interest, received a \$2.9 million order for 63 x-ray machines to be used by Indian Customs throughout India. This order was fully shipped during fiscal 1998.

In January 1998, the Company announced an order received for 21 x-ray machines from a customer in the People's Republic of China. Also in April 1998, the Company received an order for six x-ray machines at Tom Bradley International Terminal at Los Angeles International Airport, Los Angeles, California; and the installation of the Company's FAA-approved Threat Image Projection (TIP) software on existing x-ray machines at Ronald Reagan National Airport in Washington, D.C., JFK International Airport in New York, New York and Bush Intercontinental Airport in Houston, Texas.

In November 1996, the Company entered into a \$14 million contract with a foreign customer to deliver 16 large cargo scanners. Eight of these cargo scanners were shipped during fiscal 1998, with the remainder to be shipped during fiscal 1999 and beyond.

In May 1998, Rapiscan U.S.A. and the FAA entered into a Cooperative Research and Development Agreement (the "CRDA"). Under the CRDA, the Company and the FAA's Technical Center will jointly attempt to develop, over a three-year period, effective enhanced automated baggage screening systems at airports, using

Rapiscan's proprietary scanner technology and image processing ability. Rapiscan U.S.A. will retain title in all inventions made solely by employees of Rapiscan U.S.A. and the U.S. Government will have the option to retain title to all inventions made solely by the employees of the U.S. Government or jointly by employees of Rapiscan U.S.A. and the U.S. Government. If the U.S. Government retains title to any inventions under the CRDA, the U.S. Government will grant Rapiscan U.S.A. an exclusive license for any invention for use in automated detection of explosives in baggage, and a non-exclusive license for all other inventions developed under the CRDA, in exchange for a royalty based on gross revenues from the licensed invention. If Rapiscan U.S.A. retains title to any inventions under the CRDA, Rapiscan U.S.A. will grant the U.S. Government a non-exclusive license with respect to such inventions. The party retaining title to inventions developed under the CRDA has the option to file a patent application with respect thereto. Rapiscan U.S.A. has the option to own the copyright in all software, documentation and other works created in whole or in part by employees of Rapiscan U.S.A. under the CRDA.

MARKETING, SALES AND SERVICE

The Company markets and sells its optoelectronic devices and subsystems worldwide through both a direct sales and marketing staff of 25 employees and indirectly through a network of approximately 20 independent sales representatives and distributors, as of June 30, 1998. Most of the in-house sales staff is based in the United States while most of the independent sales representatives and distributors are located abroad. Since the acquisition of AME in March 1997, the Company's marketing efforts in Europe have been conducted through AME's sales and marketing staff and through a network of approximately six independent sales representatives. The Company markets and sells its security and inspection products worldwide through a direct sales and marketing staff of approximately 19 employees located in the United States, the United Kingdom, Dubai, and Malaysia and through a network of over 75 independent sales representatives, as of June 30, 1998.

The Company's optoelectronic products sales staff, located in the United States and Norway, is supported by an applications engineering group whose members are available to provide technical support. This support includes designing applications, providing custom tooling and process integration, defining solutions for customers and developing products that meet customer defined specifications. The security and inspection products sales staff is supported by a service organization of approximately 27 persons, as of June 30, 1998, located primarily in the United States, the United Kingdom and Malaysia. The Company also supports these sales and customer relations efforts by providing operator training, computerized training and testing equipment, in-country service, software upgrades, service training for customer technicians and a newsletter on security issues.

The Company considers its maintenance service operations to be an important element of its business. After the expiration of the standard product warranty period, the Company is often engaged by its customers to provide maintenance services for its security and inspection products through annual maintenance contracts. The Company believes that its international maintenance service capabilities allow it to be competitive in selling its security and inspection products. Furthermore, the Company believes that as its installed base of security and inspection products increases, revenues generated from such annual maintenance service contracts and from the sale of replacement parts will increase. In fiscal 1997 and 1998, maintenance service revenues and replacement part sales collectively represented 3.6% and 3.5%, respectively, of the Company's revenues.

RESEARCH AND DEVELOPMENT

The Company's components and optoelectronic subsystems are designed and engineered at the Company's offices in either Hawthorne, California, or Horten, Norway. The subsystems that the Company manufactures are engineered by the Company to solve specific application needs of its OEM customers. The Company's customers typically request that the Company design custom optoelectronic solutions for their specific needs when standard components or subsystems are not available from other manufacturers of optoelectronic devices. After an end-product has been conceptualized by the OEM, the Company normally will involve its engineers to design the application, establish the mechanical specifications for the application, create the appropriate subsystem architecture for the application, and design the development, production and assembly process for the manufacture of the ultimate subsystem. However, because the Company has the engineering, tooling and manufacturing capabilities to design and manufacture entire subsystems, and not just a specific component, the

Company typically also designs, manufactures and assembles the entire subsystem for the customer. Because the Company's engineers are able to provide additional value and services to its customers through the entire production process from concept to completion, the Company considers its engineering personnel to be an important extension of its core sales and marketing effort.

In addition to close collaboration with the Company's customers in the design and development of optoelectronics-based products, the Company maintains an active program for the development and introduction of new products and enhancements and improvements to its existing products, including the implementation of new applications of its technology. The Company seeks to further develop its research and development program and considers such program to be an important element of its business and operations. As of June 30, 1998, in addition to the engineers that the Company employed in manufacturing, process design and applications development, the Company engaged approximately 44 full-time engineers and technicians in research and development. During fiscal 1997 and 1998, the Company's research and development expenses were approximately \$2.5 million and \$3.8 million, respectively. In order to fulfill its strategy of increasing its security and inspection product lines and of enhancing the capabilities of its existing products, the Company intends to continue to increase its research and development efforts in the future.

The Company's security screening products are designed at Rapiscan U.S.A.'s facilities in Hawthorne, California and Rapiscan U.K.'s facilities in Crawley, England. These products include mechanical, electrical, electronic, digital electronic and software subsystems, which are all designed by the Company. In addition to product design, the Company provides system integration services to integrate its products into turnkey systems at the customer site. The Company supports cooperative research projects with government agencies and, on occasion, provides contract research for its customers and government agencies.

MANUFACTURING AND MATERIALS MANAGEMENT

The Company currently has manufacturing facilities in the United Kingdom, Malaysia, Norway and Denmark, in addition to its manufacturing facilities in Hawthorne, California and Ocean Springs, Mississippi. The Company's principal manufacturing facility is in Hawthorne, California. However, most of the Company's high volume, labor intensive manufacturing and assembly is generally performed at its facilities in Malaysia. Since most of the Company's customers currently are located in Europe and the United States, the Company's ability to assemble its products in these markets and provide follow-on service from offices located in these regions is an important component of the Company's global strategy.

The Company seeks to focus its subsystem manufacturing resources on its core competencies that enable it to provide value-added enhancements and distinctive value. The Company believes that its manufacturing organization has expertise in optoelectronic, electrical and mechanical manufacturing and assembly of products for commercial applications and for high reliability applications. High reliability devices and subsystems are those which are designed, manufactured, screened and qualified to function under exceptionally severe levels of environmental stress. The manufacturing techniques include silicon wafer processing and fabrication, manufacture and assembly of photodiodes, surface mounting (SMT) and manual thru-hole assembly, thick-film ceramic processing, wire bonding, molding, assembly of components, testing, and packaging. The Company also has the ability to manufacture plastic parts and certain other parts that are either not available from third party suppliers or that can be more efficiently or cost-effectively manufactured in-house. The Company outsources certain manufacturing operations including its sheet metal fabrication. The manufacturing process for components and subsystems consists of manual tasks performed by skilled and semi-skilled workers as well as automated tasks. The number of subsystems that the Company manufactures depends on the customers' needs and may range from a few subsystems (such as an optoelectronic sun sensor for use in a satellite) to many thousands (sensors used in laser printers and bar code readers).

The principal raw materials and subcomponents used in producing the Company's optoelectronic devices and subsystems consist of silicon wafers, ceramics, electronic subcomponents, light emitting diodes, phototransistors, printed circuit boards, headers and caps, housings, cables, filters and packaging materials. For cost, quality control and efficiency reasons, the Company generally purchases raw materials and subcomponents

only from single vendors with whom the Company has ongoing relationships. The Company does, however, qualify second sources for all of its raw materials and subcomponents, or has identified alternate sources of supply. The Company purchases the materials pursuant to purchase orders placed from time to time in the ordinary course of business. The silicon-based optoelectronic devices manufactured by the Company are critical components in most of its subsystems. Since 1987, the Company has purchased substantially all of the silicon wafers it uses to manufacture its optoelectronic devices from Wacker Siltronic Corp. Although to date the Company has not experienced any significant shortages or material delays in obtaining any of its raw materials or subcomponents, there can be no assurance that the Company will not face such shortages or delays in one or more of these materials in the future.

Substantially all of the optoelectronic, subsystems, circuit boards and x-ray generators used in the Company's inspection and detection systems are manufactured in-house. The metal shells of the x-ray inspection systems, and certain standard mechanical parts are purchased from various third-party unaffiliated providers.

ENVIRONMENTAL REGULATIONS

The Company is subject to various federal, state and local environmental laws, ordinances and regulations relating to the use, storage, handling, and disposal of certain hazardous substances and wastes used or generated in the manufacturing and assembly of the Company's products. Under such laws, the Company may become liable for the costs of removal or remediation of certain hazardous substances that have been or are being released on or in its facilities or that have been or are being disposed of off site as wastes. Such laws may impose liability without regard to whether the Company knew of, or caused, the release of such hazardous substances. In the past, the Company has conducted a Phase I environmental assessment report for each of the properties in the United States at which it currently manufactures products. The purpose of each such report was to identify, as of the date of that report, potential sources of contamination of the property. In certain cases, the Company has received a Phase II environmental assessment report consisting of further soil testing and other investigations deemed appropriate by an independent environmental consultant. The Company believes that it is currently in compliance with all material environmental regulations in connection with its manufacturing operations, and that it has obtained all environmental permits necessary to conduct its business. The amount of hazardous substances and wastes produced and generated by the Company may increase in the future depending on changes in the Company's operations. Any failure by the Company to comply with present or future regulations could subject the Company to the imposition of substantial fines, suspension of production, alteration of manufacturing process or cessation of operations, any of which could have a material adverse effect on the Company's business, financial condition and results of operations.

COMPETITION

The markets in which the Company operates are highly competitive and characterized by evolving customer needs and rapid technological change. The Company competes with a number of other manufacturers, many of which have significantly greater financial, technical and marketing resources than the Company. In addition, these competitors may have the ability to respond more quickly to new or emerging technologies, adapt more quickly to changes in customer requirements, have stronger customer relationships, have greater name recognition, and devote greater resources to the development, promotion and sale of their products than does the Company. There can be no assurance that the Company will be able to compete successfully against any current or future competitors in either the optoelectronic devices and subsystem markets or the security and inspection markets or that future competitive pressures will not materially and adversely affect its business, financial conditions and results of operations.

In the optoelectronic device and subsystem market, competition is based primarily on such factors as expertise in the design and development of optoelectronic devices, product quality, timeliness of delivery, price, customer technical support, and on the ability to provide fully integrated services from application development and design through volume subsystem production. The Company believes that its major competitors in the optoelectronic device and subsystem market are EG&G Electro-Optics, a division of EG&G, Inc., Optek

Technology Inc., Hamamatsu Corporation, and Honeywell Optoelectronics, a division of Honeywell, Inc. Because the Company specializes in custom subsystems requiring a high degree of engineering expertise, the Company believes that it generally does not compete to any significant degree with any other large United States, European or Asian manufacturers of standard optoelectronic components. Competition for the Company's medical imaging products comes principally from Lunar Corporation, Hologic, Inc. and Norland Medical Systems, Inc.

In the security and inspection market, competition is based primarily on such factors as product performance, functionality and quality, the over-all cost effectiveness of the system, prior customer relationships, technological capabilities of the products, price, local market presence, and breadth of sales and service organization. The Company believes that its principal competitors in the market for security and inspection products are EG&G Astrophysics, a division of EG&G, Inc., Heimann Systems GmbH, InVision Technologies, Inc., Vivid Technologies, American Science and Engineering, Inc., Barringer Technologies Inc., Control Screening L.L.C., and Thermedics Detection, Inc. Competition could result in price reductions, reduced margins, and loss of market share by the Company. The Company believes that the principal competitor for its products using x-ray backscatter detection technology is American Science & Engineering, Inc. In the airline and airport security and inspection market, particularly in the upgrade and replacement market, the Company also competes for potential customers based on existing relationships between its competitors and the customers. Certain of the Company's competitors have been manufacturing inspection systems since the 1980s and have established strong relationships with airlines and airport authorities. The Company believes that the image quality and resolution of certain of its security and inspection products is superior to the image quality offered by most of its competitors' x-ray based inspection products. Although the Company also has established relationships with a number of airport and airline customers, no assurance can be given that the Company will be able to successfully compete in the future with existing competitors or with new entrants.

BACKLOG

The Company measures its backlog as orders for which purchase orders or contracts have been signed, but which have not yet been shipped and for which revenues have not yet been recognized. The Company typically ships its optoelectronics devices and subsystems as well as its security and inspection products within one to three months after receiving an order. However, such shipments may be delayed for a variety of reasons including any special design or engineering requirements of the customer. In addition, large orders (more than ten machines) of security and inspection products typically require more lead time. Large cargo scanning machines require six to twelve months lead time.

At June 30, 1998, the Company's backlog products totalled approximately \$46.9 million, compared to approximately \$52.7 million at June 30, 1997. Most of the Company's backlog as of June 30, 1998 is expected to be shipped during the fiscal year ending June 30, 1999. Any failure of the Company to meet an agreed upon schedule could lead to the cancellation of the related order. Variations in the size of the order, the product mix, and delivery requirements of the customer order may result in substantial fluctuations in backlog from period to period. Backlog as of any particular date should not be relied upon as indicative of the Company's revenues for any future period and cannot be considered a meaningful indicator of the Company's performance on an annual or quarterly basis.

EMPLOYEES

As of June 30, 1998, the Company employed approximately 753 people, of whom 571 were employed in manufacturing, 44 were employed in research and development, 67 were employed in finance and administration, 44 were employed in sales and marketing, and 27 were employed in its service organization. Of the total employees, approximately 451 were employed in the United States, 131 were employed in Europe, 170 were employed in Asia, and one was employed in the Middle East. Thirty employees at AME are members of a union and have collective bargaining rights. Other than the employees of AME, none of the Company's other employees are unionized. There has never been a work stoppage or strike at the Company, and management believes that its relations with its employees are good.

ITEM 2. PROPERTIES

In June 1998, the Company exercised an option and purchased two buildings comprising its principal Hawthorne, California, facility for approximately \$2.95 million. The Company had previously leased these facilities. The Company also purchased one additional building and a parking lot in Hawthorne, California, adjacent to its executive offices, to house the operations of UDT Sensors. The purchase price for this building and the parking lot was approximately \$1.26 million. The Company paid the aggregate purchase price for both purchases with cash on hand.

As of June 30, 1998, the Company leased all of its other facilities, as reflected in the following table:

LOCATION	DESCRIPTION OF FACILITY	APPROXIMATE SQUARE FOOTAGE	LEASE EXPIRATION
Hawthorne, California	Manufacturing, engineering, sales and marketing and service	41,600	2006
Ocean Springs, Mississippi	Manufacturing, engineering and sales and marketing	41,800	2001
Johor Bahru, Malaysia	Manufacturing and sales	13,500	1999
Johor Bahru, Malaysia	Manufacturing	10,500	1999
Horten, Norway	Manufacturing, engineering, marketing and sales	19,800	2008
Singapore, Republic of Singapore	Administrative and materials procurement	3,000	2000
Crawley, United Kingdom	Manufacturing, engineering, sales and marketing	18,700	2011
Hayes, United Kingdom	Service	3,900	2003

Previously, the operations of Rapiscan U.S.A. were located in leased premises in Long Beach, California. Beginning April 1998, the Company consolidated these operations into newly leased space in Hawthorne, California. The Long Beach lease expired in September 1998.

AME terminated the lease on its previously-leased facility without significant cost, and relocated its operations to a new facility in Horten, Norway, in July 1998, which is included in the above table.

The Company believes that its facilities are in good condition and are adequate to support its operations for the foreseeable future. The Company currently anticipates that it will be able to renew the leases that are scheduled to expire in the next few years on terms that are substantially the same as those currently in effect. However, even if the Company were not able to renew one or more of the leases, the Company believes that suitable substitute space is available to relocate any of the facilities. Accordingly, the Company does not believe that its failure to renew any of the leases that are scheduled to expire in the next few years will have a material adverse effect on the Company's operations.

ITEM 3. LEGAL PROCEEDINGS

On January 21, 1997, Rapiscan U.S.A. filed a complaint in the U.S. District Court for the Central District of California against Lunar Corporation ("Lunar") in response to claims by Lunar that certain security inspection products produced by Rapiscan U.S.A. infringe U.S. Patent No. 4,626,688 (the "'688 patent"), which patent is owned by the University of Alabama Research Foundation ("UAB") and licensed exclusively to Lunar. The complaint seeks a declaratory judgment that the products produced by Rapiscan U.S.A. do not infringe the '688 patent, that the '688 patent is invalid, and that the patent may not be enforced against Rapiscan U.S.A. for a number of equitable and legal reasons. The complaint also asserts related non-patent claims including fraud and the breach of an oral agreement whereby Lunar would compensate Rapiscan U.S.A. for assisting Lunar in its enforcement of the '688 patent and seeks compensatory and punitive damages for these claims.

On January 23, 1997, Lunar and UAB filed suit against the Company, Rapiscan U.S.A. and UDT Sensors in the U.S. District Court for the Western District of Wisconsin. Lunar and UAB asserted patent infringement,

contributory infringement and inducement thereof. Lunar and UAB seek damages in an unspecified amount and an injunction preventing the Company, Rapiscan U.S.A. and UDT Sensors from further making, using, selling and offering for sale products including the dual energy detector allegedly covered by the '688 patent. The Wisconsin lawsuit has been transferred to the U.S. District Court for the Central District of California and has been consolidated with the lawsuit brought by Rapiscan U.S.A.

On August 31, 1998, the parties participated in a mandatory settlement conference and are now finalizing the language of the settlement.

In October 1994, UDT Sensors entered into a Consent Judgment and a Criminal Plea and Sentencing Agreement (collectively, the "Consent Agreements") with the United States of America. The charges contained in the Consent Agreements relate to high-reliability optoelectronic subsystems that UDT Sensors manufactured for use in military aircraft, attack helicopters and submarines. In the Consent Agreements, UDT Sensors agreed that it had not tested 100% of these products as required by the applicable military specifications. Under the terms of the Consent Agreements, UDT Sensors agreed to pay a total of \$1.5 million, plus interest, in five annual installments ending on March 31, 1999. UDT Sensors was placed on probation for the five-year period ending March 31, 2000 with respect to sales of optoelectronic subsystems for use by the U.S. Department of Defense. Probation does not, however, prohibit UDT Sensors from selling optoelectronic products to the United States, and UDT Sensors has, since the date of the Consent Agreements, continued to manufacture and sell the same optoelectronic products for use in military aircraft, attack helicopters and submarines. In addition, in order to ensure that UDT Sensors complies with all Federal procurement laws, UDT Sensors agreed to implement programs and practices to establish and monitor complying contracting procedures, and agreed to file periodic reports evidencing such practices and programs.

On January 18, 1996, Robert Praski and Sonia Praski filed a lawsuit against the Company, Ferson and others in the United States District Court for the Southern District of Mississippi, alleging wrongful termination of the Praskis' employment by Ferson. The Complaint was served on February 9, 1998. An Amended Complaint For Damages and Other Relief was filed on April 14, 1998. The plaintiffs alleged that irregularities occurred at Ferson, including the falsification of test data, quality control reports and shipping records, resulting in approximately \$560,000 in overpayments in the aggregate by the U.S. Government to Ferson and/or the Company.

The plaintiffs alleged that approximately 32,000 individual instances of such overcharges and false claims occurred. The plaintiffs sought, based upon the statutory civil penalty of \$10,000 for each false claim under Title 31 USC 3729 et seq., more popularly known as the False Claims Act, approximately \$320 million in civil damages on behalf of the U.S. Government. In addition, the plaintiffs sought for themselves actual damages of \$100,000 and punitive damages of \$2 million for their wrongful termination, together with litigation costs and reasonable attorney fees.

The Company has filed a motion to dismiss the suit, which is pending. Even though the court has not yet ruled on the Company's motion to dismiss, Sonia Praski voluntarily has filed a Notice of Dismissal of her claims against all of the defendants, thereby leaving Robert Praski as the sole plaintiff. The Company believes that the case is frivolous and without merit. If the motion to dismiss is not granted by the court, the Company will vigorously defend the lawsuit. Both the Company and its counsel believe that the Company will prevail. The U.S. Government investigated the allegations and declined to intervene in the case or bring any charges against any of the defendants.

Except for the foregoing, the Company is not a party to any material pending legal proceedings other than routine litigation incidental to its business.

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

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

Stock Market and Other Information

The Company's common stock has been traded on the Nasdaq National Market under the symbol "OSIS" since October 2, 1997. Prior to such date, there was no public trading market for the Company's equity securities.

The following table sets forth the high and low sale prices of a share of the Company's Common Stock as reported by the Nasdaq National Market on a quarterly basis for the Company's fiscal year ended June 30, 1998.

1998:	HIGH	LOW
-----	-----	-----
Quarter ended December 31, 1997.....	\$16.00	\$10.88
Quarter ended March 31, 1998.....	\$16.00	\$11.13
Quarter ended June 30, 1998.....	\$12.50	\$ 9.25

As of September 18, 1998, there were approximately 85 holders of record of the Company's Common Stock. This number does not include beneficial owners holding shares through nominee or "street" name.

Dividend Policy

The Company has not paid any dividends since the consummation of its initial public offering in 1997 and anticipates that it will retain any available funds for use in the operation of its business, and does not currently intend to pay any cash dividends in the foreseeable future. Future cash dividends, if any, will be determined by the Board of Directors. The payment of cash dividends by the Company is restricted by certain of the Company's current bank credit facilities, and future borrowing may contain similar restrictions.

Transfer Agent and Registrar

U.S. Stock Transfer Corp. of Glendale, California, serves as transfer agent and registrar of the Company's Common Stock.

Use of Proceeds

The Company's Registration Statement for its initial public offering of securities (File No. 333-29179) became effective on October 1, 1997. Of the total net proceeds to the Company from the offering in the amount of approximately \$41,000,000, the following amounts were used from the date of the offering through June 30, 1998.

CATEGORY OF USE	AMOUNT
-----	-----
Construction of plant, building and facilities.....	\$ --
Purchase and installation of machinery and equipment.....	--
Purchase of real estate.....	4,211,000
Acquisition of other businesses.....	750,000
Repayment of indebtedness.....	14,100,000
Working capital.....	3,490,000
Temporary investments.....	18,449,000
Other purposes.....	--

Total.....	\$41,000,000
	=====

ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth selected consolidated financial data of the Company as of and for each of the five fiscal years ended June 30, 1998 and is derived from the Consolidated Financial Statements of the Company. The consolidated financial statements as of June 30, 1997 and June 30, 1998, and for each of the years in the three-year period ended June 30, 1998, and the auditor's report thereon, are included elsewhere herein. The following data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and notes thereto included elsewhere in this Report.

	YEAR ENDED JUNE 30,				
	1994	1995	1996	1997	1998
(In thousands, except share and per share data)					
CONSOLIDATED STATEMENTS OF OPERATIONS DATA:					
Revenues.....	\$ 47,735	\$ 49,815	\$ 61,518	\$ 77,628	\$ 93,918
Cost of goods sold.....	36,037	37,818	45,486	56,174	66,952
Gross profit.....	11,698	11,997	16,032	21,454	26,966
Operating expenses:					
Selling, general and administrative(1)....	7,974	7,601	9,757	11,304	12,776
Research and development.....	1,451	1,591	1,663	2,504	3,790
Stock option compensation(2).....	--	--	--	856	--
Total operating expenses.....	9,425	9,192	11,420	14,664	16,566
Income from operations..	2,273	2,805	4,612	6,790	10,400
Interest expense/(income).....	710	1,251	1,359	1,197	(600)
Income before income taxes and minority interest.....	1,563	1,554	3,253	5,593	11,000
Provision for income taxes.....	814	413	1,111	1,416	2,752
Income before minority interest.....	749	1,141	2,142	4,177	8,248
Minority interest.....	38	17	117	--	--
Net income.....	\$ 787	\$ 1,158	\$ 2,259	\$ 4,177	\$ 8,248
Net income available to common shareholders(3).	\$ 995	\$ 1,357	\$ 2,308	\$ 4,269	\$ 8,248
Net income per share(3)(4).....	\$ 0.16	\$ 0.22	\$ 0.38	\$ 0.68	\$ 0.92
Weighted average shares outstanding(4).....	6,249,674	6,172,901	6,134,669	6,263,963	8,955,919
CONSOLIDATED BALANCE SHEET DATA:					
Cash and cash equivalents.....	\$ 625	\$ 1,405	\$ 581	\$ 553	\$ 22,447
Working capital.....	2,280	12,117	6,044	10,800	52,417
Total assets.....	25,807	30,780	35,309	47,333	86,822
Total debt.....	11,140	14,113	15,462	13,180	1,243
Total shareholders' equity.....	\$ 3,128	\$ 4,951	\$ 7,194	\$ 16,809	\$ 65,915

- (1) Fiscal 1994 includes a one time charge of \$1.5 million incurred in connection with the settlement of a governmental proceeding.
- (2) Represents a charge resulting from the acceleration of the vesting periods of outstanding stock options having exercise prices below the fair market value on the date of grant. The charge had the effect of decreasing income from operations, net income and net income available to common shareholders by \$856,000, \$514,000 and \$514,000, respectively.
- (3) Gives effect to the conversion of certain subordinated debt into preferred stock and Common Stock in October and November 1996, and the issuance of Common Stock for the purchase of the remaining minority interests in certain subsidiaries in October and December 1996 as if such transactions occurred on July 1, 1992. Adjustments in each of the five years ended June 30, 1998 consist of: (i) the elimination of interest expense related to converted subordinated debt of \$246,000, \$216,000, \$166,000, \$92,000 and

\$0, net of income taxes, respectively; and (ii) the elimination of the minority interest in the net loss of subsidiaries of \$38,000, \$17,000, \$117,000, \$0 and \$0, respectively.

- (4) Assumes the conversion of 2,568,750 shares of preferred stock into 3,853,125 shares of Common Stock as of July 1, 1992. The preferred stock had a liquidation preference of \$1.00 per share, and was otherwise entitled to the same voting, dividend and all other rights as the Common Stock.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the Company's consolidated financial statements and the notes thereto appearing elsewhere in this Annual Report on Form 10-K. Certain statements contained herein that are not related to historical results, including, without limitation, statements regarding the Company's business strategy and objectives, future financial position and estimated cost savings, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and involve risks and uncertainties. Although the Company believes that the assumptions upon which these forward-looking statements are based are reasonable, there can be no assurance that such assumptions will prove to be accurate and actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, regulatory policies in the United States and other countries, foreign currency fluctuations, market and general economic factors, competitive factors including other companies' pricing and marketing efforts, availability of third-party products at reasonable prices risks of obsolescence due to shifts in market demand, litigation outcomes and such other risks and uncertainties as are described in this Annual Report on Form 10-K and other documents previously filed or hereafter filed by the Company from time to time with the Securities and Exchange Commission. All forward-looking statements contained in this Annual Report on Form 10-K are qualified in their entirety by this statement.

OVERVIEW

The Company is a vertically integrated worldwide provider of devices, subsystems and end-products based on optoelectronic technology. The Company designs and manufactures optoelectronic devices and value added subsystems for OEMs for use in a broad range of applications, including security, medical diagnostics, telecommunications, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products that it markets worldwide to end users under the "Rapiscan" and "SECURE" brand names. These products are used to inspect baggage, cargo, people and other objects for weapons, explosives, drugs and other contraband. In fiscal 1998, revenues from the sale of optoelectronic devices subsystems amounted to \$50.1 million, or approximately 53.4% of the Company's revenues, while revenues from sales of security and inspection products amounted to \$43.8 million, or approximately 46.6% of the Company's revenues.

The Company was organized in May 1987. The Company's initial products were optoelectronic devices and subsystems sold to customers for use in the manufacture of x-ray scanners for carry-on airline baggage. In December 1987, the Company formed Opto Sensors (Singapore) Pte Ltd. ("OSI Singapore") to manufacture optoelectronic devices and subsystems. In April 1990, the Company acquired UDT Sensors' subsystem business. In February 1993, the Company acquired the security and inspection operations of Rapiscan U.K. and, through Rapiscan U.S.A., commenced its operations as a provider of security and inspection products in the United States. In April 1993, the Company acquired Ferson, a U.S. manufacturer of passive optic components. In July 1994, the Company established OSI Malaysia to manufacture optoelectronic subsystems as well as security and inspection products. In March 1997, the Company acquired AME for the purpose of broadening its optoelectronic subsystem business in Europe. The Company currently owns all of the outstanding shares of each of these companies. In January 1998, the Company acquired the "SECURE" product line from ThermoSpectra for the purpose of expanding into the area of inspection of people. Subsequent to the end of the 1998 fiscal year, the Company acquired Osteometer for the purpose of expanding further into the field of optoelectronic medical devices used for medical diagnostic purposes.

In January 1994, the Company entered into a joint venture agreement with Electronics Corporation of India, Limited ("ECIL"), an unaffiliated Indian corporation, pursuant to which the Company and ECIL formed ECIL Rapiscan. The joint venture was established for the purpose of manufacturing security and inspection products in India from kits sold to ECIL by the Company. The Company currently owns a 36.0% interest in ECIL Rapiscan. Subsequent to the end of the 1998 fiscal year, the Company made investments in an aggregate amount of approximately \$800,000 in two other businesses.

The Company engages in significant international operations. The Company currently manufactures its optoelectronic devices and subsystems at its facilities in Hawthorne, California, Ocean Springs, Mississippi, Johor Bahru, Malaysia, and Horten, Norway. Its security and inspection products are manufactured at its facilities in Crawley, England, Hawthorne, California, and Johor Bahru, Malaysia. As of June 30, 1998, the Company markets its products worldwide through approximately 44 sales and marketing employees located in five countries, and through approximately 102 independent sales representatives. Revenues from shipments made outside of the United States accounted for 38.0%, 42.2% and 49.4% of revenues for the fiscal years 1996, 1997 and 1998, respectively. Information regarding the Company's operating income or loss and identifiable assets attributable to each of the Company's geographic areas is set forth in Note 15 in the Company's Consolidated Financial Statements.

The effective income tax rate for the Company for fiscal 1996, 1997 and 1998 was 34.2%, 25.3% and 25.0%, respectively. Certain products manufactured in the United States and sold overseas are sold through a Foreign Sales Corporation ("FSC") organized by the Company in 1990. Export sales made through the FSC are subject to federal tax advantages. If the tax advantages derived from sales made through the FSC and certain existing state and federal tax credits remain in effect, and if certain future foreign tax benefits are received as anticipated, the Company believes that its effective income tax rate will be below 32.0% during the next fiscal year.

The Company's products currently address two principal markets. The Company's optoelectronic devices and subsystems are designed and manufactured primarily for sale to OEMs, while the Company's security and inspection products are sold to end-users. Two principal customers of the Company's optoelectronic devices and subsystems are the Company's Rapiscan U.K. and Rapiscan U.S.A. subsidiaries. Revenues from the sale of the Company's optoelectronic devices and subsystems to these two subsidiaries are eliminated from the Company's reported revenues. Revenues from the Company's principal markets and intercompany eliminations are presented in the table below.

	YEAR ENDED JUNE 30,		
	1996	1997	1998
	(IN THOUSANDS)		
Optoelectronic devices and subsystems.....	\$45,007	\$51,554	\$56,336
(Inter-company eliminations).....	(6,392)	(8,675)	(6,216)
Unaffiliated optoelectronic devices and subsys- tems.....	38,615	42,879	50,120
Security and inspection products.....	22,903	34,749	43,798
Total revenues.....	\$61,518	\$77,628	\$93,918

In recent years, the Company has experienced increased revenues from its security and inspection products, both in absolute dollars and as a percentage of total Company revenues. The Company has recently initiated a program to produce larger security and inspection products, including those for use in inspecting cargo, which products are likely to have significantly higher selling prices than most of the Company's products sold to date. Sales of products with higher average selling prices may increase fluctuations in the Company's quarterly revenues and earnings.

The Company recognizes revenues upon shipment. As the Company's product offerings change to include sales of significantly larger systems, such as cargo inspection products, the Company may adopt the percentage of completion method of revenue recognition for certain products.

RESULTS OF OPERATIONS

The following table sets forth certain income and expenditure items as a percentage of total revenues for the periods indicated.

	YEAR ENDED JUNE		
	30,		
	1996	1997	1998
Revenues.....	100.0%	100.0%	100.0%
Cost of goods sold.....	73.9	72.4	71.3
Gross profit.....	26.1	27.6	28.7
Operating expenses:			
Selling, general and administrative.....	15.9	14.6	13.6
Research and development.....	2.7	3.2	4.0
Stock option compensation.....	--	1.1	--
Total operating expenses.....	18.6	18.9	17.6
Income from operations.....	7.5	8.7	11.1
Interest expense (income).....	2.2	1.5	(0.6)
Income before income taxes and minority interest.....	5.3	7.2	11.7
Provision for income taxes.....	1.8	1.8	2.9
Income before minority interest.....	3.5	5.4	8.8
Minority interest.....	0.2	--	--
Net income.....	3.7%	5.4%	8.8%

COMPARISON OF THE FISCAL YEAR ENDED JUNE 30, 1998 TO THE FISCAL YEAR ENDED JUNE 30, 1997

Revenues. Revenues consist of sales of optoelectronics devices and subsystems as well as security and inspection products. Revenues are recorded net of inter-company eliminations. Revenues for the fiscal year ended June 30, 1998 increased by \$16.3 million, or 21.0% to \$93.9 million from \$77.6 million for the fiscal year ended June 30, 1997. Revenues for the sale of optoelectronics devices and subsystems, net of intercompany eliminations, increased by \$7.2 million, or 16.9% to \$50.1 million from \$42.9 million for fiscal 1997. The increase was the result of increase in sales to medical diagnostic and gaming industry and introduction of products that are sold for use in the oil exploration field. Revenues from the sale of security and inspection products increased by \$9.0 million, or 26.0% to \$43.8 million from \$34.7 million for fiscal 1997. The increase was due to an increase in sales of the Company's Rapiscan Series 500 systems and large cargo inspection machines, and continuing penetration in the security and inspection products market.

Gross Profit. Cost of goods sold consists of material, labor and manufacturing overhead. Gross profit increased by \$5.5 million, or 25.7% to \$27.0 million from \$21.5 million for fiscal 1997. As a percentage of revenues, gross profit increased to 28.7% in fiscal 1998 from 27.6% in fiscal 1997. The increase in gross profit was due to increased sales and increased efficiencies in manufacturing.

Selling, General and Administrative. Selling general and administrative expenses consist primarily of compensation paid to sales, marketing, and administrative personnel, professional service fees, and marketing expenses. For the year ended June 30, 1998 such expenses increased by \$1.5 million, or 13.0%, to \$12.8 million from \$11.3 million in fiscal 1997. This increase was due primarily to an increase in payroll expenses and marketing expenses to support revenue growth as well as an increase in legal expenses related primarily to ongoing litigation matters. As a percentage of revenues, selling, general and administrative expenses decreased to 13.6% in fiscal 1998 from 14.6% in fiscal 1997.

Research and Development. Research and development expenses include research related to new product development and product enhancement expenditures. For the year ended June 30, 1998, such expenses increased by \$1.3 million, or 51.4%, to \$3.8 million from \$2.5 million in fiscal 1997. As a percentage of revenues, research

and development expenses increased to 4.0% in fiscal 1998 from 3.2% in fiscal 1997. The increase was due primarily to acceleration of certain research and development projects, continued enhancement of Rapiscan x-ray systems, and increased efforts to develop product for cargo scanning and optoelectronic devices and subsystems products.

Income from Operations. Income from operations for the year ended June 30, 1998 increased by \$3.6 million, or 53.2%, to \$10.4 million from \$6.8 million in fiscal 1997. Excluding the non-recurring, non-cash incentive compensation expense of \$856,000 incurred in connection with the acceleration of the vesting period of stock options granted to certain employees and officers during the year ended June 30, 1997, income from operations increased by \$2.8 million or 36.0%, from \$7.6 million last year. As a percentage of revenues, income from operations increased to 11.1% from 8.7% last year and excluding the non-cash compensation expense referenced above, it would have increased to 11.1% from 9.8%.

Interest Expense. For the year ended June 30, 1998, the Company earned net interest income of \$600,000 compared to net interest expense of \$1.2 million in fiscal 1997. The interest income was due to proceeds from the initial public offering of the Company's common stock, in October 1997. A portion of the proceeds was used to repay a majority of the Company's debt and the remaining proceeds are invested in short-term investments.

Provision for Income Taxes. Provision for income taxes for fiscal 1998 increased by \$1.3 million, or 94.4% to \$2.8 million, from \$1.4 million for fiscal 1997. As a percentage of income before provision for income taxes, provision for income taxes decreased to 25.0% from 25.3% for fiscal 1997.

Net Income. For the reasons outlined above, net income for the year ended June 30, 1998 increased by \$4.1 million, or 97.5%, to \$8.2 million from \$4.2 million in fiscal 1997. The non-cash compensation charge described above, decreased net income by \$514,000 in fiscal 1997.

COMPARISON OF THE FISCAL YEAR ENDED JUNE 30, 1997 TO THE FISCAL YEAR ENDED JUNE 30, 1996

Revenues. Revenues consist of sales of optoelectronic devices and subsystems as well as of security and inspection products. Revenues are recorded net of all inter-company eliminations. Revenues for the fiscal year ended June 30, 1997 increased by \$16.1 million, or 26.2%, to \$77.6 million from \$61.5 million for the fiscal year ended June 30, 1996. Revenues from the sale of optoelectronic devices and subsystems, net of intercompany eliminations, increased by \$4.3 million, or 11.0%, to \$42.9 million from \$38.6 million for fiscal 1996. The increase was the result of increased orders from existing customers, particularly in the medical diagnostics industry, and the expansion of the Company's product base. Revenues from the sale of security and inspection products increased by \$11.8 million, or 51.7%, to \$34.7 million from \$22.9 million for fiscal 1996. The increase was due mainly to the continued acceptance of the Rapiscan Series 500 EPX System, which was introduced in 1995, the growth in sales of the Rapiscan 119 tabletop model and the introduction of large cargo inspection machines.

Gross Profit. Cost of goods sold consists of material, labor and manufacturing overhead. Gross profit increased by \$5.4 million, or 33.8%, to \$21.5 million from \$16.0 million for fiscal 1996. As a percentage of revenues, gross profit increased to 27.6% in fiscal 1997 from 26.1% in fiscal 1996. Gross margin increased as a result of the fact that fixed costs did not increase proportionally with the increase in revenues. In addition, gross profit improved as a result of the Company continuing to increase the production of product manufactured at its offshore facilities, thereby capitalizing on lower labor and other manufacturing costs.

Selling, General and Administrative. Selling, general and administrative expenses consist primarily of compensation paid to sales, marketing, and administrative personnel, professional service fees, and marketing expenses. For fiscal 1997, such expenses increased by \$1.5 million, or 15.9%, to \$11.3 million from \$9.8 million in fiscal 1996. As a percentage of revenues, selling, general and administrative expenses decreased to 14.6% from 15.9%. The increase in expenses was due to increases in payroll expenses to support revenue growth as well as to increases in legal expenses.

Research and Development. Research and development expenses include research related to new product development and product enhancement expenditures. For fiscal 1997, such expenses increased by \$841,000, or 50.6%, to \$2.5 million from \$1.7 million in fiscal 1996. As a percentage of revenues, research and development expenses increased to 3.2% from 2.7%. The increase was due primarily to continued enhancement of the Rapiscan Series 500 EPX System and efforts to develop products for cargo scanning. In addition, the Company expended all research and development expenses in the 1997 period as incurred, whereas certain of such expenses related to software products, the technological feasibility of which had been established, were capitalized in the 1996 period.

Income from Operations. Income from operations for fiscal 1997 increased by \$2.2 million, or 47.2%, to \$6.8 million from \$4.6 million for fiscal 1996. Excluding the non-recurring non-cash incentive compensation expense of \$856,000 incurred in connection with the acceleration of the vesting period of stock options granted to certain employees during fiscal 1997, income from operations increased by \$3.0 million, or 65.8%, to \$7.6 million from \$4.6 million. As a percent of revenues, income from operations increased to 8.7% from 7.5%, and excluding the non-cash compensation expense referenced above, it would have increased to 9.8% from 7.5%.

Interest Expense. Interest expense for fiscal 1997 decreased by \$162,000, or 11.9%, to \$1.2 million from \$1.4 million for fiscal 1996. As a percentage of revenues, interest expense decreased to 1.5% from 2.2%. The decrease was due to the conversion of the Company's subordinated debt to preferred and common stock during fiscal 1997, and to a decrease in the Company's borrowing outstanding under its lines of credit.

Provision for Income Taxes. Provision for income taxes for fiscal 1997 increased by \$305,000, or 27.5%, to \$1.4 million from \$1.1 million for fiscal 1996. As a percentage of income before provision for income taxes and minority interest, provision for income taxes decreased to 25.3% from 34.2% in fiscal 1996. The decrease was a result of increases in the Company's export sales through its FSC, which has the effect of reducing the tax rate on revenues from foreign sales made from the United States, and the increased utilization of research and development and certain state tax credits. In addition, the Company has made the California Waters Edge election under California tax law, which has the effect of exempting its foreign subsidiaries from California taxes through fiscal 2003.

Net Income. For the reasons outlined above, net income for fiscal 1997, increased \$1.9 million, or 84.9%, to \$4.2 million from \$2.3 million in fiscal 1996. The compensation charge described above, decreased net income by \$514,000 in fiscal 1997.

LIQUIDITY AND CAPITAL RESOURCES

The Company has financed its operations primarily through cash provided by operations, through various term loans, discounting facilities, and credit lines extended to its different subsidiaries worldwide and from its public offering. As of June 30, 1998, the Company's principal sources of liquidity consisted of \$22.4 million in cash and several credit agreements described below.

The Company's operations used net cash of \$436,000 during fiscal 1998. The amount of net cash used by operations reflects increases in accounts receivable, inventory, prepaid expenses, reduction in advances from customers and other accrued expenses and liabilities. Net cash used in operations was offset in part by a reduction of other receivables and increases in accounts payable, accrued payroll and related expenses, income taxes payable and warranty accrual. The increase in accounts receivable is due to an increase in sales as well as the timing of shipments made upon completion of certain contracts during fiscal 1998.

Net cash used by investing activities was \$8.0 and \$3.0 million for fiscal 1998 and 1997, respectively, in each case due primarily to purchase of property and equipment in the amount of \$7.5 million and \$2.2 million, respectively. In fiscal 1998, of the total property and equipment purchases, approximately \$708,000 was for the purchase of equipment to manufacture products used in the oil exploration field and approximately \$4.2 million was for the purchase of three buildings in Hawthorne, California. The Company paid \$750,000 for the acquisition of the "SECURE" product line. The Company expects to purchase property and equipment in fiscal 1999 as required. The Company has no significant capital spending or purchase commitments other than in the normal course of business and commitments under leases.

Net cash provided by financing activities was \$30.6 million for fiscal 1998 compared to net cash used by financing activities of \$526,000 for fiscal 1997. In fiscal 1998, net cash provided by financing activities resulted primarily from Company's initial public offering and was offset in part by repayment of the majority of the Company's debt.

The Company anticipates that current cash balances, anticipated cash flows from operations and current borrowing arrangements will be sufficient to meet its working capital and capital expenditure needs for the foreseeable future.

In January 1997, the Company and its three U.S. subsidiaries entered into a credit agreement with Sanwa Bank California. The agreement, as amended in May 1998, provides for a \$10.0 million line of credit, which includes revolving, letter of credit, acceptance and foreign exchange facilities. In addition, the Company has a \$3.0 million equipment line of credit for capital purchases and a \$15.0 million line of credit for acquisitions with certain restrictions. Advances under the lines of credit bear interest at a rate equal to a variable bank reference rate (8.5% at June 30, 1998) or, at the Company's option, at a fixed rate as quoted by the bank upon request. As of June 30, 1998, there were no amounts outstanding under the line of credit, equipment line of credit or the acquisition line of credit. As of June 30, 1998, \$124,000 was outstanding under letters of credit. The lines expire in November 1999. Borrowings under the agreement are secured by liens on substantially all of the Company's assets. The agreement restricts the four borrowers from incurring certain additional indebtedness and from making capital expenditures greater than \$3.5 million in the U.S. in any fiscal year, except for the purchase of real property to be occupied by the borrowers. In addition, the credit agreement currently requires that the Company at all times maintain (on a consolidated basis) a tangible net worth of at least \$40.0 million, a ratio of debt to tangible net worth of not more than 3.0 to 1, and a ratio of cash, cash equivalents and accounts receivable to current liabilities of not less than 0.8 to 1. The Company is currently in compliance with all of these financial conditions.

In November 1996, the Company and its three U.S. subsidiaries entered into an agreement with Wells Fargo HSBC Trade Bank, N.A. The agreement was renewed in January 1998 and, in August 1998, was extended until November 1999. As currently in effect, the agreement provides for revolving lines of credit up to a maximum of \$2.1 million to be used to pay obligations incurred in connection with export orders. Of this total amount, there is a sublimit of \$1.0 million for the purchase of foreign currency and a sublimit of \$1.9 million for letters of credit. The revolving credit lines bear interest at the bank's prime rate (8.5% at June 30, 1998) plus 5.0% per annum. As of June 30, 1998, there was outstanding approximately \$1.9 million for standby letters of credit. Borrowings under the agreement are secured by liens on certain of the Company's assets. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, profitability, payments of dividends and capital expenditures.

Rapiscan U.K. has a loan agreement with Midland Bank plc, which provides for an overdraft facility up to a maximum amount of 2.0 million Pounds Sterling (approximately \$3.3 million at June 30, 1998) outstanding at any one time, which amounts are secured by certain assets of Rapiscan U.K. At June 30, 1998, no amounts were outstanding under the overdraft facility. Outstanding borrowings bear interest at a base rate (7.5% at June 30, 1998) plus 1.5% per annum. The agreement also provides for a 1.0 million Pounds Sterling (approximately \$1.7 million at June 30, 1998) facility for tender and performance bonds and a 1.0 million Pounds Sterling (approximately \$1.7 million at June 30, 1998) facility for the purchase of forward exchange contracts. These facilities are secured by certain assets of Rapiscan U.K. and the Company has guaranteed Rapiscan U.K.'s obligations under the performance bond facility. As of June 30, 1998, \$588,000 was outstanding under the performance bond facility and Rapiscan U.K. had purchased forward exchange contracts in the amount of \$973,000. The above facilities expire in January 1999 and the Company believes that they will be renewed on the same or similar terms.

OSI Singapore has a loan agreement with Indian Bank (Singapore), which provides for an accounts receivable discounting facility for borrowing of up to 2.6 million Singapore dollars (approximately \$1.6 million

at June 30, 1998). Borrowings under the line of credit bear interest at the bank's prime rate (8.5% at June 30, 1998) plus 1.50%. The line of credit is terminable at any time. As of June 30, 1998 there were no amounts outstanding under the line of credit. Borrowings under the line of credit are collateralized by certain assets of OSI Singapore and are guaranteed by Messrs. Deepak Chopra, Ajay Mehra and Thomas Hickman, officers of the Company. Borrowings secured by intercompany receivables are guaranteed by the Company.

AME has a loan agreement with Christiania Bank OG Kreditkasse which provides for a revolving line of credit for borrowings of up to 5.0 million Norwegian kroner (approximately \$666,000 at June 30, 1998), of which \$198,000 was outstanding as of June 30, 1998. Borrowings under the line of credit bear interest at a variable rate, which was 5.9% at June 30, 1998. The agreement also provides for a term loan which matures in June 2001 and bears interest at an annual rate of 7.0%. At June 30, 1998 outstanding term loan borrowings totalled approximately 2.4 million Norwegian kroner (approximately \$312,000 at June 30, 1998). Subsequent to the end of the fiscal year, the outstanding amount of the term loan was paid in full.

OSI Malaysia has a loan agreement with the Hong Kong Bank Malaysia Berhad, which provides for a bank guarantee line of credit for 2.5 million Malaysia ringgits (approximately \$604,000 at June 30, 1998) for performance bonds and standby letters of credit, and a 1.0 million Malaysian ringgits overdraft facility (approximately \$242,000 at June 30, 1998). Borrowings under the overdraft facility bear interest at the bank's base lending rate (12.3% at June 30, 1998) plus 1.75%. At June 30, 1998, the amount outstanding under the performance bond facility was \$232,000 and there were no amounts outstanding under the overdraft facility. Borrowings under this agreement are secured by certain assets of OSI Malaysia. These lines expire in October 1998 and the Company believes that they will be renewed on the same or similar terms.

In August 1997, Bank Utama agreed to provide a revolving line of credit to OSI Malaysia up to an amount of 1.5 million Malaysian ringgits (approximately \$362,000 as of June 30, 1998). Borrowings under the line of credit bear interest at the bank's base lending rate (12.2% at June 30, 1998) plus 2.5%. As of June 30, 1998, no amounts were outstanding under this line of credit. Borrowings under this agreement are secured by certain assets of OSI Malaysia and are guaranteed by the Company. The line of credit was renewed for one year and will expire in August 1999.

The Company believes that cash from operations, existing cash and lines of credit will be sufficient to meet its cash requirements for the foreseeable future.

FOREIGN CURRENCY TRANSLATION

The accounts of the Company's operations in Singapore, Malaysia, England and Norway are maintained in Singapore dollars, Malaysian ringgits, Pounds Sterling and Norwegian kroner, respectively. Foreign currency financial statements are translated into U.S. dollars at current rates, with the exception of revenues, costs and expenses, which are translated at average rates during the reporting period. Gains and losses resulting from foreign currency transactions are included in income, while those resulting from translation of financial statements are excluded from income and accumulated as a component of shareholder's equity. Transaction gains/(losses) of approximately \$68,000 and \$(39,000) were included in income for fiscal 1997 and 1998, respectively.

IMPORTANCE OF INTERNATIONAL MARKETS

International markets provide the Company with significant growth opportunities. However, the following events, among others, could adversely affect the Company's financial results in subsequent periods: periodic economic downturns in different regions of the world, changes in trade policies or tariffs, and political instability. For the year ended June 30, 1998, overall foreign currency fluctuations relative to the U.S. dollar had an immaterial effect on the Company's consolidated revenues and results of operations. As a result of recent changes in monetary policy in Malaysia, including the pegging of the Malaysian ringgit to the U.S. dollar, the

Company believes that its foreign currency exposure in Malaysia will be immaterial in the foreseeable future. The Company continues to perform ongoing credit evaluations of its customers' financial condition and, if deemed necessary, the Company requires advance payments for sales. The Company is monitoring economic and currency conditions around the world to evaluate whether there may be any significant effect on its international sales in the future.

INFLATION

The Company does not believe that inflation has had a material impact on its results of operations.

YEAR 2000 COMPLIANCE

The Company has a comprehensive Year 2000 project designed to identify and assess the risks associated with its information systems, products, operations and infrastructure, suppliers, and customers that are not Year 2000 compliant, and to develop, implement, and test remediation and contingency plans to mitigate these risks. The project comprises four phases: (1) identification of risks, (2) assessment of risks, (3) development of remediation and contingency plans, and (4) implementation and testing. The Company's Year 2000 project is currently in the assessment phase and, with respect to certain information systems and products, is in the remediation phase. The Company believes that its greatest potential risks are associated with its information systems and systems embedded in its operations and infrastructure. The Company is at the beginning stage of assessments for its operations and infrastructure, and cannot predict whether significant problems will be identified. The Company has not yet determined the extent of contingency planning that may be required. Based on the status of the assessments made and remediation plans developed to date, the Company is not in a position to state the total cost of remediation of all Year 2000 issues. Costs identified to date have not been material. The Company does not currently expect the total costs to be material, and it expects to be able to fund the total costs through operating cash flows. However, the Company has not yet completed its assessments, developed remediation for all problems, developed any contingency plans, or completely implemented or tested any of its remediation plans. As the Year 2000 project continues, the Company may discover additional Year 2000 problems, may not be able to develop, implement, or test remediation or contingency plans, or may find that the costs of these activities exceed current expectations and become material. In many cases, the Company is relying on assurances from suppliers that new and upgraded information systems and other products will be Year 2000 compliant. The Company plans to test such third-party products, but cannot be sure that its tests will be adequate or that, if problems are identified, they will be addressed in a timely and satisfactory way. Because the Company uses a variety of information systems and has additional systems embedded in its operations and infrastructure, the Company cannot be sure that all of its systems will work together in a Year 2000 compliant fashion. Furthermore, the Company cannot be sure that it will not suffer business interruptions, either because of its own Year 2000 problems or those of its customers or suppliers whose Year 2000 problems may make it difficult or impossible for them to fulfill their commitments to the Company. If the Company fails to satisfactorily resolve Year 2000 issues related to its products in a timely manner, it could be exposed to liability to third parties. The Company is continuing to evaluate Year 2000-related risks and will take such further corrective actions as may be required.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Financial Statements of the Company are submitted as a separate section of this Annual Report on Form 10-K on pages F-1 through F-21.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1998 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 16, 1998.

ITEM 11. EXECUTIVE COMPENSATION

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1998 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 16, 1998.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1998 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 16, 1998.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1998 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 16, 1998.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) List of documents filed as part of Report

(1) FINANCIAL STATEMENTS INCLUDED IN ITEM 8:

Report of Independent Accountants.....	F-1
Consolidated Balance Sheets at June 30, 1997 and 1998.....	F-2
Consolidated Statements of Operations for the years ended June 30, 1996, 1997 and 1998.....	F-3
Consolidated Statements of Shareholders' Equity for the years ended June 30, 1996, 1997 and 1998.....	F-4
Consolidated Statements of Cash Flows for the years ended June 30, 1996, 1997 and 1998.....	F-5
Notes to Consolidated Financial Statements.....	F-7

(2) FINANCIAL STATEMENT SCHEDULES INCLUDED IN ITEM 8:

Schedule II - Valuation and Qualifying Accounts

No other financial statement schedules are presented as the required information is either not applicable or included in the Consolidated Financial Statements or notes thereto.

(3) EXHIBITS

The exhibits listed on the accompanying Exhibit Index are filed as part of this Annual Report.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the quarter ended June 30, 1998.

SIGNATURES

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

OSI SYSTEMS, INC.
(Registrant)

Date: September 28, 1998

By: /s/Ajay Mehra

Ajay Mehra
Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

SIGNATURE -----	TITLE -----	DATE -----
<p>/s/ Deepak Chopra</p> <hr/> <p>Deepak Chopra</p>	<p>Chairman of the Board, President and Chief Executive Officer (Principal Executive Officer)</p>	<p>September 28, 1998</p>
<p>/s/ Ajay Mehra</p> <hr/> <p>Ajay Mehra</p>	<p>Vice President, Chief Financial Officer (Principal Financial and Accounting Officer), Secretary and Director</p>	<p>September 28, 1998</p>
<p>/s/ Steven C. Good</p> <hr/> <p>Steven C. Good</p>	<p>Director</p>	<p>September 28, 1998</p>
<p>/s/ Meyer Luskin</p> <hr/> <p>Meyer Luskin</p>	<p>Director</p>	<p>September 28, 1998</p>
<p>/s/ Madan G. Syal</p> <hr/> <p>Madan G. Syal</p>	<p>Director</p>	<p>September 28, 1998</p>

INDEX TO EXHIBITS

NUMBER	EXHIBIT DESCRIPTION
3.1	Articles of Incorporation of the Company (1)
3.2	Amended and Restated Bylaws of the Company (1)
4.1	Specimen Common Stock Certificate (3)
10.1	1987 Incentive Stock Option Plan, as amended, and form of Stock Option Agreement (1)
10.2	1997 Stock Option Plan and forms of Stock Option Agreements (2)
10.3	Employment Agreement dated April 1, 1997 between the Company and Deepak Chopra (1)
10.4	Employment Agreement dated April 1, 1997 between the Company and Ajay Mehra (1)
10.5	Employment Agreement dated March 1, 1993 between the Company and Andreas F. Kotowski (3)
10.6	Employment Agreement dated April 1, 1997 between the Company and Manoocher Mansouri Aliabadi (1)
10.7	Employment Agreement dated October 5, 1994 between the Company and Anthony S. Crane (3)
10.8	Expatriate Employment Agreement dated July 11, 1995 between the Company and Thomas K. Hickman (2)
10.9	Incentive Compensation Agreement dated December 18, 1996 between the Company and Andreas F. Kotowski (1)
10.10	Form of Indemnity Agreement for directors and executive officers of the Company (3)
10.11	Joint Venture Agreement dated January 4, 1994 among the Company, Electronics Corporation of India, Limited and ECIL-Rapiscan Security Products Limited, as amended (2)
10.12	Amendment Number Two to Lease, dated October 24, 1995 to lease dated January 1, 1989 by and between KB Management Company, and UDT Sensors, Inc.(1)
10.13	Lease Agreement dated July 4, 1986 by and between Electricity Supply Nominees Limited and Rapiscan Security Products Limited (as assignee of International Aeradio Limited) (3)
10.14	Lease Agreement dated January 17, 1997 by and between Artloon Supplies Sdn. Bhd. and Opto Sensors (M) Sdn. Bhd.(1)
10.15	Credit Agreement entered into on November 1, 1996 by and between Opto Sensors, Inc., UDT Sensors, Inc., Rapiscan Security Products (U.S.A.), Inc. and Ferson Optics, Inc., and Wells Fargo HSBC Trade Bank (1)
10.16	License Agreement made and entered into as of December 19, 1994, by and between EG&G, Inc. and Rapiscan Security Products, Inc.(1)
10.17	Stock Purchase Agreement dated March 5, 1997 between Industriinvestor ASA and Opto Sensors, Inc.(1)
10.18	Lease dated September 24, 1997 between the Company and D.S.A. Properties (4)
10.19	Credit Agreement entered into on May 22, 1998, by and between Sanwa Bank California and Opto Sensors, Inc., UDT Sensors, Inc., Rapiscan Security Products (U.S.A.), Inc. and Ferson Optics, Inc.(5)
10.20	Agreement of Purchase and Sale and Joint Escrow Instructions dated as of June 23, 1998 by and between KB Chadron Building, LLC and UDT Sensors, Inc. (5)
10.21	Agreement of Purchase and Sale and Joint Escrow Instructions dated as of June 23, 1998 by and between Chadron II, LLC and UDT Sensors, Inc. (5)
21.1	Subsidiaries of the Company (5)
23.1	Independent Auditors' Consent (5)
27.1	Financial Data Schedule (5)
99.1	Criminal Plea and Sentencing Agreement between UDT Sensors, Inc. and U.S. Attorney's Office (2)
99.2	Agreement between UDT Sensors, Inc. and Department of Navy (2)

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- (1) Previously filed with the Company's Registration Statement filed June 13, 1997.
 - (2) Previously filed with the Company's Amendment No. 1 to the Registration Statement filed August 1, 1997.
 - (3) Previously filed with the Company's Amendment No. 2 to the Registration Statement filed August 15, 1997.
 - (4) Previously filed with the Company's Quarterly Report on Form 10-Q for the quarterly period ended December 31, 1997.
 - (5) Filed herewith.

INDEPENDENT AUDITORS' REPORT

OSI Systems, Inc.:

We have audited the accompanying consolidated balance sheets of OSI Systems, Inc. (the "Company") and its subsidiaries as of June 30, 1998 and 1997, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 1998. Our audits also included the financial statement schedule listed at Item 14. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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, such consolidated financial statements present fairly, in all material respects, the financial position of OSI Systems, Inc. and its subsidiaries as of June 30, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 1998 in conformity with generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

DELOITTE & TOUCHE LLP

Los Angeles, California
September 11, 1998

OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

JUNE 30, 1997 AND 1998
(DOLLARS IN THOUSANDS, EXCEPT SHARE AMOUNTS)

	1997	1998
	-----	-----
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents (Note 1).....	\$ 553	\$22,447
Accounts receivable, net of allowance for doubtful accounts of \$586 and \$551 at June 30, 1997 and 1998, respectively (Note 1).....	15,556	24,254
Other receivables (Note 2).....	2,346	1,990
Inventory (Note 1).....	18,517	21,705
Prepaid expenses.....	537	841
Deferred income taxes (Notes 1 and 6).....	874	1,381
	-----	-----
Total current assets.....	38,383	72,618
PROPERTY AND EQUIPMENT, Net (Notes 1 and 4).....	5,841	11,466
INTANGIBLE AND OTHER ASSETS, Net (Notes 1, 2 and 3).....	3,109	2,738
	-----	-----
TOTAL.....	\$47,333	\$86,822
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Bank lines of credit (Note 4).....	\$ 9,100	\$ 198
Current portion of long-term debt (Notes 1, 5 and 12).....	1,240	633
Accounts payable (Note 1).....	7,712	8,560
Accrued payroll and related expenses.....	1,607	2,400
Income taxes payable (Notes 1 and 6).....	1,804	2,517
Advances from customers.....	2,410	1,808
Accrued warranties.....	965	1,948
Other accrued expenses and current liabilities.....	2,745	2,137
	-----	-----
Total current liabilities.....	27,583	20,201
LONG-TERM DEBT (Notes 1, 5 and 12).....	2,840	412
DEFERRED INCOME TAXES (Notes 1 and 6).....	101	294
	-----	-----
Total liabilities.....	30,524	20,907
	-----	-----
COMMITMENTS AND CONTINGENCIES (Notes 7 and 12)		
SHAREHOLDERS' EQUITY (Notes 4, 8 and 9):		
Preferred stock, no par value; authorized, 10,000,000 shares, no shares issued or outstanding at June 30, 1997 and 1998, respectively.....		
Common stock, no par value; authorized, 40,000,000 shares, issued and outstanding 6,156,528 and 9,691,915 shares at June 30, 1997 and 1998, respectively.....	7,367	49,131
Retained earnings.....	9,171	17,419
Cumulative foreign currency translation adjustment (Note 1).	271	(635)
	-----	-----
Total shareholders' equity.....	16,809	65,915
	-----	-----
TOTAL.....	\$47,333	\$86,822
	=====	=====

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

YEARS ENDED JUNE 30, 1996, 1997 AND 1998
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

	1996	1997	1998
REVENUES (Note 1).....	\$61,518	\$77,628	\$93,918
COST OF GOODS SOLD.....	45,486	56,174	66,952
GROSS PROFIT.....	16,032	21,454	26,966
OPERATING EXPENSES:			
Selling, general and administrative expenses (Notes 10 and 11).....	9,757	11,304	12,776
Research and development (Note 1).....	1,663	2,504	3,790
Stock option compensation (Note 8).....		856	
Total operating expenses.....	11,420	14,664	16,566
INCOME FROM OPERATIONS.....	4,612	6,790	10,400
INTEREST EXPENSE (INCOME) (Notes 4, 5 and 10).....	1,359	1,197	(600)
INCOME BEFORE PROVISION FOR INCOME TAXES AND MINORITY INTEREST.....	3,253	5,593	11,000
PROVISION FOR INCOME TAXES (Notes 1 and 6).....	1,111	1,416	2,752
INCOME BEFORE MINORITY INTEREST IN NET LOSS OF SUBSIDIARIES.....	2,142	4,177	8,248
MINORITY INTEREST IN NET LOSS OF SUBSIDIARIES (Note 1).....	117		
NET INCOME.....	\$ 2,259	\$ 4,177	\$ 8,248
EARNINGS PER COMMON SHARE (Note 1).....	\$ 1.04	\$ 1.72	\$ 0.94
EARNINGS PER COMMON SHARE--ASSUMING DILUTION (Note 1).	\$ 0.38	\$ 0.68	\$ 0.92

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

YEARS ENDED JUNE 30, 1996, 1997 AND 1998
(DOLLARS IN THOUSANDS, EXCEPT SHARE AMOUNTS)

	PREFERRED		COMMON		RETAINED EARNINGS	CUMULATIVE FOREIGN CURRENCY TRANSLATION ADJUSTMENT	TOTAL
	NUMBER OF SHARES	AMOUNT	NUMBER OF SHARES	AMOUNT			
BALANCE, JUNE 30, 1995..	1,318,750	\$ 1,514	1,842,007	\$ 543	\$ 2,735	\$ 159	\$ 4,951
Exercise of stock options.....			16,125	17			17
Translation adjustment.....						(33)	(33)
Net income.....					2,259		2,259
BALANCE, JUNE 30, 1996..	1,318,750	1,514	1,858,132	560	4,994	126	7,194
Exercise of stock options.....			118,125	146			146
Conversion of debt....	1,250,000	2,500	120,536	225			2,725
Minority interest acquisitions.....			206,610	1,566			1,566
Conversion of preferred stock.....	(2,568,750)	(4,014)	3,853,125	4,014			
Stock option compensation.....				856			856
Translation adjustment.....						145	145
Net income.....					4,177		4,177
BALANCE, JUNE 30, 1997..			6,156,528	7,367	9,171	271	16,809
Initial public offering (Note 9)....			3,330,000	40,938			40,938
Exercise of stock options.....			205,387	508			508
Translation adjustment.....						(906)	(906)
Tax benefit of stock options exercised....				318			318
Net income.....					8,248		8,248
BALANCE, JUNE 30, 1998..		\$	9,691,915	\$49,131	\$17,419	\$(635)	\$65,915

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 1996, 1997 AND 1998
(DOLLARS IN THOUSANDS)

	1996	1997	1998
	-----	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income.....	\$2,259	\$4,177	\$ 8,248
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Minority interest in net loss of subsidiaries.....	(117)		
Provision for losses on accounts receivable.....	404	389	122
Depreciation and amortization.....	2,014	2,302	2,330
Stock option compensation.....		856	
Deferred income taxes.....	(12)	(900)	(314)
Gain on sale of property and equipment.....	(13)		(13)
Changes in operating assets and liabilities, net of business acquisition:			
Accounts receivable.....	(858)	(1,980)	(9,481)
Other receivables.....	(194)	(1,530)	462
Inventory.....	(4,068)	(4,573)	(3,995)
Prepaid expenses.....	(245)	96	(325)
Accounts payable.....	120	1,026	1,352
Accrued payroll and related expenses.....	707	(60)	840
Income taxes payable.....	652	1,005	884
Advances from customers.....	183	1,448	(603)
Accrued warranty.....	324	574	989
Other accrued expenses and current liabilities.....	(1,151)	527	(932)
	-----	-----	-----
Net cash provided by (used in) operating activities.....	5	3,357	(436)
	-----	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of property and equipment.....	120		46
Additions to property and equipment.....	(1,612)	(2,182)	(7,487)
Cash paid for business acquisition, net of cash acquired.....		(848)	(750)
Other assets.....	(688)	23	194
	-----	-----	-----
Net cash used in investing activities.....	(2,180)	(3,007)	(7,997)
	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net proceeds from (repayment of) bank lines of credit.....	1,502	1,014	(8,797)
Payments on senior subordinated debt.....		(350)	
Payments on long-term debt.....	(1,250)	(3,983)	(2,411)
Proceeds from issuance of long-term debt.....	1,097	2,647	
Proceeds from initial public offering and exercise of stock options and warrants.....	17	146	41,764
Proceeds from issuance of minority interest.....	21		
	-----	-----	-----
Net cash provided by (used in) financing activities.....	1,387	(526)	30,556
	-----	-----	-----
EFFECT OF EXCHANGE RATE CHANGES ON CASH.....	(36)	148	(229)
	-----	-----	-----
NET (DECREASE) INCREASE IN CASH EQUIVALENTS.....	(824)	(28)	21,894
CASH EQUIVALENTS, BEGINNING OF PERIOD.....	1,405	581	553
	-----	-----	-----
CASH EQUIVALENTS, END OF PERIOD.....	\$ 581	\$ 553	\$22,447
	=====	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION -			
Cash paid during the period for:			
Interest.....	\$1,346	\$1,197	\$ 452
Income taxes.....	\$ 377	\$1,511	\$ 1,869

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 1996, 1997 AND 1998
(DOLLARS IN THOUSANDS)

SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING
ACTIVITIES:

During 1997, certain related parties converted \$225 and \$2,500 of senior subordinated debt into 120,536 and 1,250,000 shares of common and preferred stock, respectively.

During October and December 1996, the Company acquired the minority interest of its two majority-owned subsidiaries through the issuance of 178,956 shares of common stock, at an estimated fair value of \$6.67 per share. An additional 27,654 shares, at an estimated fair value of \$13.50 per share, are issuable at June 30, 1997. The excess of the fair value of the common stock of \$1,566 over the book value of the minority interests of \$12 has been recorded as goodwill.

In 1997, the Company acquired all of the capital stock of Advanced Micro Electronics AS.

In conjunction with the acquisition, liabilities were assumed as follows:

Fair value of assets acquired.....	\$2,350
Goodwill.....	588
Cash paid for the capital stock.....	(916)

Liabilities assumed.....	\$2,022
	=====

In 1998, the Company acquired the "SECURE" product line from ThermoSpectra.

In conjunction with the acquisition, assets were acquired as follows:

Equipment.....	\$ 80
Patents.....	20
Inventory.....	650

Cash paid.....	\$ 750
	=====

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 YEARS ENDED JUNE 30, 1996, 1997 AND 1998

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

GENERAL--OSI Systems, Inc. (formerly Opto Sensors, Inc.) and its subsidiaries (collectively, the "Company") is a vertically integrated, worldwide provider of devices, subsystems and end-products based on optoelectronic technology. The Company designs and manufactures optoelectronic devices and value-added subsystems for original equipment manufacturers ("OEMs") in a broad range of applications, including security, medical diagnostics, telecommunications, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products that it markets worldwide to end users under the "Rapiscan" and "SECURE" brand names. These products are used to inspect baggage, cargo, people and other objects for weapons, explosives, drugs and other contraband.

CONSOLIDATION-- The consolidated financial statements include the accounts of OSI Systems, Inc. and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. In October and December 1996, the Company purchased the minority interests of its two majority-owned subsidiaries by exchanging 178,956 shares of common stock for the minority shares of the subsidiaries. The Company also issued additional shares of the Company's common stock to the selling shareholders of one of the subsidiaries. The number of shares issued were based upon the pre-tax net income of the subsidiary for the year ended June 30, 1997, and amounted to 27,654 shares. These shares have been included in the number of shares issued for minority interest acquisitions in the accompanying consolidated statement of shareholders equity. The excess of the fair value of the common stock issued of \$1,554,000 over the carrying value of the minority interest of \$12,000 has been recorded as goodwill and is being amortized over a period of 20 years.

For the purpose of the consolidated statements of cash flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

CONCENTRATIONS OF CREDIT RISK--Financial instruments that potentially subject the Company to credit notes consist primarily of cash, cash equivalents and accounts receivable. At June 30, 1998 approximately 75% of the Company's cash and cash equivalents were held at one financial institution. The Company performs ongoing credit valuations of its customers' financial condition and provides an allowance for potential credit losses.

INVENTORY--Inventory is stated at the lower of cost or market; cost is determined on the first-in, first-out method.

Inventory at June 30, 1997 and 1998 consisted of the following (in thousands):

	1997	1998
	-----	-----
Raw materials.....	\$11,408	\$12,200
Work-in-process.....	4,224	6,030
Finished goods.....	2,885	3,475
	-----	-----
Total.....	\$18,517	\$21,705
	=====	=====

PROPERTY AND EQUIPMENT--Property and equipment are stated at cost. Depreciation and amortization are computed using the straight-line and accelerated methods over lives ranging from three to ten years. Amortization of leasehold improvements is calculated on the straight-line basis over the shorter of the useful life of the asset or the lease term.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

Property and equipment at June 30, 1997 and 1998 consisted of the following (in thousands):

	1997	1998
	-----	-----
Land and buildings.....		\$ 4,211
Equipment.....	\$ 7,545	9,046
Leasehold improvements.....	2,093	2,768
Tooling.....	1,967	1,953
Furniture and fixtures.....	666	824
Computer.....	1,699	2,202
Vehicles.....	176	142
	-----	-----
Total.....	14,146	21,146
Less accumulated depreciation and amortization.....	8,305	9,680
	-----	-----
Property and equipment, net.....	\$ 5,841	\$11,466
	=====	=====

INTANGIBLES AND OTHER ASSETS--Intangible and other assets at June 30, 1997 and 1998 consisted of the following (in thousands):

	1997	1998
	-----	-----
Software development costs.....	\$ 588	\$ 588
Goodwill.....	2,142	2,142
Deposits.....	320	168
Other.....	444	530
	-----	-----
Total.....	3,494	3,428
Less accumulated amortization.....	385	690
	-----	-----
Intangible and other assets, net.....	\$ 3,109	\$ 2,738
	=====	=====

Goodwill in the amount of \$1,554,000 resulting from the acquisition of minority interests and \$588,000 resulting from the acquisition of Advanced Micro Electronics AS (see Note 3) is being amortized, on a straight-line basis, over a period of 20 years.

Software development costs incurred in the research and development of software products are expensed as incurred until the technological feasibility of the product has been established. After technological feasibility is established, certain software development costs are capitalized. The software, once developed, is a component which is included in x-ray security machines when they are sold to customers. The Company amortizes these costs on a straight-line basis over a two-year period. No software development costs were capitalized during the two years ended June 30, 1998.

IMPAIRMENT OF LONG-LIVED ASSETS--The Company reviews long-lived assets, including goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. If the sum of the expected future cash flows, undiscounted and without interest charges, is less than the carrying amount of the asset, the Company recognizes an impairment loss based on the estimated fair value of the asset.

INCOME TAXES--Deferred income taxes are provided for temporary differences between the financial statement and income tax bases of the Company's assets and liabilities, based on enacted tax rates. A valuation

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

allowance is provided when it is more likely than not that some portion or all of the deferred income tax assets will not be realized.

FAIR VALUE OF FINANCIAL INSTRUMENTS--The Company's financial instruments consist primarily of cash, accounts receivable, accounts payable, and debt instruments. The carrying values of financial instruments other than debt instruments, are representative of their fair values due to their short-term maturities. The carrying values of the Company's long-term debt instruments are considered to approximate their fair values because the interest rates of these instruments are variable or comparable to current rates offered to the Company. The fair value of the Company's senior subordinated debt cannot be determined due to the related-party nature of the obligations.

FOREIGN EXCHANGE INSTRUMENTS--The Company's use of derivatives is limited to the purchase of foreign exchange contracts in order to minimize foreign exchange transaction gains and losses. The Company purchases forward contracts to hedge commitments to acquire inventory for sale and does not use the contracts for trading purposes. As of June 30, 1998 there were approximately \$973,000 in outstanding foreign exchange contracts. The estimated fair value of these contracts closely approximated their carrying value as of June 30, 1998.

REVENUE RECOGNITION--The Company recognizes revenue upon shipment of its product.

FOREIGN CURRENCY TRANSLATION--The accounts of the Company's operations in Singapore, Malaysia, Norway and the United Kingdom are maintained in Singapore dollars, Malaysian ringgits, Norwegian kroner and U.K. pounds sterling, respectively. Foreign currency financial statements are translated into U.S. dollars at current rates, with the exception of revenues, costs and expenses, which are translated at average rates during the reporting period. Gains and losses resulting from foreign currency transactions are included in income, while those resulting from translation of financial statements are excluded from income and accumulated as a component of shareholders' equity. Transaction (losses) gains of approximately \$(123,000), \$68,000 and \$(39,000) were included in income for the years ended June 30, 1996, 1997 and 1998, respectively.

EARNINGS PER SHARE--The Company has adopted Statement of Financial Accounting Standards ("SFAS") No. 128 "Earnings Per Share." The Company has reflected the provisions of SFAS 128 in the accompanying financial statements for all periods presented. Earnings per common share is computed using the weighted average number of shares outstanding during the period. Earnings per common share--assuming dilution, is computed using the weighted average number of shares outstanding during the period and dilutive common stock equivalents from the Company's stock option plans, and in the 1996 period common equivalent shares from convertible debt and preferred stock, calculated using the treasury stock and if converted methods.

For the years ending June 30, 1996 and 1997, pursuant to Securities and Exchange Commission Staff Accounting Bulletin Topic 4D, common stock and stock options issued or granted during the twelve month period prior to the date of the initial filing of the Company's Form S-1 Registration Statement have been included in the calculation of the weighted average number of shares (denominator), using the treasury stock method as if they were outstanding for each period.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

The following table reconciles the numerator and denominator used in calculating earnings per share and earnings per common share--assuming dilution.

	YEAR ENDED JUNE 30, 1996		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Earnings per common share			
Income available to common stockholders.	\$2,259,000	2,163,548	\$1.04 =====
Effect of dilutive securities			
Convertible subordinated debt.....	166,000	1,729,815	
Convertible preferred stock.....		1,938,125	
Options, treasury stock method.....		96,571	
Convertible minority shareholding.....	(117,000)	206,610	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversions.....	\$2,308,000 =====	6,134,669 =====	\$0.38 =====
	YEAR ENDED JUNE 30, 1997		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Earnings per common share			
Income available to common stockholders.	\$4,177,000	2,430,347	\$1.72 =====
Effect of dilutive securities			
Convertible subordinated debt.....	92,000	2,098,125	
Convertible preferred stock.....		1,689,815	
Options, treasury stock method.....		45,676	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversions.....	\$4,269,000 =====	6,263,963 =====	\$0.68 =====
	YEAR ENDED JUNE 30, 1998		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Earnings per common share			
Income available to common stockholders.	\$8,248,000	8,753,702	\$0.94 =====
Effect of dilutive securities			
Options, treasury stock method.....		202,217	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversions.....	\$8,248,000 =====	8,955,919 =====	\$0.92 =====

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS--In June 1997, the Financial Accounting Standards Board issued SFAS No. 130, "Reporting for Comprehensive Income" and No. 131, "Disclosure About Segments of an Enterprise and Related Information." These statements are effective for financial statements issued for periods

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

beginning after December 15, 1997. In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." This statement is effective for financial statements issued for periods beginning June 15, 1999. The Company has not yet analyzed the impact of adopting these statements.

USE OF ESTIMATES--The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. INVESTMENT IN JOINT VENTURE

In January 1995, the Company, together with an unrelated company, formed ECIL-Rapiscan Security Products Limited, a joint venture organized under the laws of India. The Company, the Company's chairman and the Company's chief financial officer have a 36%, 10.5% and 4.5% ownership interest, respectively, in the joint venture. The Company's investment of approximately \$108,000 at June 30, 1998 is included in other assets in the accompanying financial statements and the Company's equity in the earnings of the joint venture, since its inception, have been insignificant.

The joint venture was formed for the purpose of the manufacture, assembly, service and testing of x-ray security and other products. One of the Company's subsidiaries is a supplier to the joint venture partner, who in turn manufactures and sells the resulting products to the joint venture utilizing technology received from the subsidiary. The agreement provides for technology transfer between the Company and the joint venture, subject to certain restrictions.

During the years ended June 30, 1997 and 1998, the Company earned a technical fee and dividend income from the joint venture in the amount of \$115,000 and \$144,000, respectively. At June 30, 1998, \$225,000 was unpaid and included in other receivables in the accompanying consolidated financial statements.

3. ACQUISITIONS

On March 3, 1997, the Company acquired the capital stock of Advanced Micro Electronics AS ("AME") headquartered in Horten, Norway, from Industriinvestor ASA. The cash purchase price amounted to \$916,000. The acquisition has been accounted for by the purchase method of accounting, and accordingly, the purchase price has been allocated to the assets acquired of \$2,350,000 and liabilities assumed of \$2,022,000, based on the estimated fair values of the assets and liabilities at the date of acquisition. The excess of the purchase price over the fair value of net assets acquired is being amortized over a period of 20 years.

The results of operations of AME are included in the Company's consolidated financial statements from the date of acquisition. Had the acquisition occurred as of July 1, 1995, pro forma consolidated sales for the years ended June 30, 1996 and 1997 would have been \$65,371,000 and \$79,871,000, respectively. Consolidated pro forma net income and net income per share would not have been materially different than the amounts reported for the respective periods.

During fiscal 1998, the Company acquired the "SECURE" product line from ThermoSpectra Corporation. The cash purchase price amounted to \$750,000. The purchased assets include, among other things, equipment, inventory, and intellectual property rights relating to x-ray machines and x-ray backscatter detection technology (including patents and patent applications).

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

4. BANK AGREEMENTS

At June 30, 1997 and 1998, line of credit borrowings consisted of the following:

	1997	1998
	-----	-----
Line of credit--U.S.....	\$6,577	
Line of credit--Singapore.....	974	
Line of credit--Norway.....	586	\$198
Line of credit--Rapiscaan U.K.....	963	
	-----	-----
Total bank lines of credit.....	\$9,100	\$198
	=====	=====

The Company maintains a senior loan agreement with a U.S. bank, which provides for a \$10,000,000 revolving line of credit, a \$3,000,000 equipment line of credit and a \$15,000,000 line of credit for acquisitions with certain restrictions. Borrowings under the line of credit bear interest at the bank's prime rate (8.5% at June 30, 1998) or, at the Company's option, at a fixed rate as quoted by the bank upon request for specific advances and terms. Interest is payable monthly, and the lines expire in November 1999. Borrowings under the senior loan agreement are collateralized by substantially all of the assets of the Company. At June 30, 1998, there were no amounts outstanding under the revolving, equipment or acquisition lines of credit. The agreement also provides a commitment for letters of credit up to \$10,000,000 not to exceed the available balance under the line of credit. At June 30, 1998, approximately \$124,000 was issued and outstanding under letters of credit. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, rental expense and capital expenditures.

The Company has a credit agreement with a U.S. bank that provides for borrowings up to an amount of \$2,084,903. Included in total borrowings is a facility for the purchase of foreign currencies of \$1,000,000. Borrowings under the facility bear interest at the banks prime rate (8.5% at June 30, 1998) plus 5%. Interest is payable on demand, and the line expires in November 1999. Borrowings under the current agreement are secured by certain of the Company's assets. At June 30, 1998, there were no amounts outstanding under the revolving line of credit. The agreement also provides a commitment for letters of credit up to \$1,885,000. At June 30, 1998, approximately \$1,885,000 was issued and outstanding under letters of credit. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, profitability, payments of dividends and capital expenditures.

Opto Sensors Pte. Ltd. ("OSP") has a loan agreement with a Singapore bank that provides for revolving line of credit borrowings up to 2,600,000 Singapore dollars (approximately US\$1,625,000 at June 30, 1998). Borrowings under the line of credit bear interest at the banks prime rate (8.5% at June 30, 1998) plus 1.5%. Interest is payable monthly, and borrowings are due on demand. Borrowings under the line of credit are collateralized by certain assets of OSP and are guaranteed by certain officers of the Company. Borrowings secured by intercompany receivables are guaranteed by the Company. At June 30, 1998, there were no amounts outstanding under the revolving line of credit.

AME has a loan agreement with a Norwegian bank that provides for revolving line of credit borrowings up to 5,000,000 Norwegian kroner (approximately US\$666,000 at June 30, 1998). Borrowings under the line of credit bear interest at a variable rate, which was 5.9% at June 30, 1998. Interest is payable quarterly. Borrowings under the line of credit are collateralized by certain AME assets. At June 30, 1998, approximately \$198,000 was issued and outstanding under the line of credit.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

Rapiscan U.K. has a loan agreement with a U.K. bank, which provides for an overdraft facility up to a maximum amount of 2,000,000 Pounds Sterling (approximately \$3,300,000 at June 30, 1998) outstanding at any one time, which amounts are secured by certain assets of Rapiscan U.K. At June 30, 1998, no amounts were outstanding under the overdraft facility. Outstanding borrowings bear interest at a base rate (7.5% at June 30, 1998) plus 1.5% per annum. The agreement also provides for a 1,000,000 Pounds Sterling (approximately \$1,700,000 at June 30, 1998) facility for tender and performance bonds and a 1,000,000 Pounds Sterling (approximately \$1,700,000 at June 30, 1998) facility for the purchase of forward exchange contracts. These facilities are secured by certain assets of Rapiscan U.K. and the Company has guaranteed Rapiscan U.K.'s obligations under the performance bond facility. As of June 30, 1998, \$588,000 was outstanding under the performance bond facility and Rapiscan U.K. had purchased forward exchange contracts in the amount of \$973,000. The above facilities expire in January 1999 and the Company believes that they will be renewed on the same or similar terms.

A subsidiary has a loan agreement with a Malaysian bank that provides for a revolving line of credit up to 1,500,000 Malaysian ringgits (approximately US\$362,000 at June 30, 1998). Borrowings under the line of credit bear interest at the bank's base lending rate (12.2% at June 30, 1998), plus 2.5%. Interest is payable on demand. No amounts were outstanding under this agreement at June 30, 1998. Borrowings under this agreement are secured by certain assets of the subsidiary and are guaranteed by the Company. The line of credit was renewed for one year and will expire in August 1999.

A subsidiary has a loan agreement with a Malaysian bank that provides for performance bonds and standby letters of credit of 2,500,000 Malaysian ringgits (approximately US \$604,000 at June 30, 1998). The agreement also provides for overdraft borrowings up to 1,000,000 Malaysian ringgits (approximately US\$242,000 at June 30, 1998). Borrowings under the overdraft facility bear interest at the bank's base lending rate (12.3% at June 30, 1998) plus 1.75%. At June 30, 1998, approximately \$232,000 was issued and outstanding under the performance bond facility and there were no amounts outstanding under the overdraft facility. Borrowings under this agreement are secured by certain assets of the subsidiary. These facilities expire on October 1998 and the Company believes that they will be renewed on the same or similar terms.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

5. LONG-TERM DEBT

At June 30, 1997 and 1998, long-term debt consisted of the following (in thousands):

	1997	1998
	-----	-----
Term loan payable to a bank, interest due monthly at the bank's prime rate (8.5% at June 30, 1997) plus 0.50%, principal due in monthly installments of \$52,083 until paid in full on March 31, 2001. Outstanding balances are collateralized by substantially all of the assets of the Company. The outstanding balance was paid in full in October 1997.....	\$2,344	
Term loan payable to a Norwegian bank, interest due quarterly at a rate of 7%, principal due in monthly installments of \$8,680 until paid in full on June 1, 2001. Outstanding balances are collateralized by certain assets of the subsidiary.....	437	\$ 312
Term loan payable to a bank, interest due monthly at the bank's prime rate (8.5% at June 30, 1997) plus 2.25%, principal due in monthly installments of \$8,333 until paid in full on November 30, 1997. The outstanding balance was paid in full in November 1997.....	41	
Liability under settlement agreements, interest computed at the 52 week treasury bill rate (5.055% at June 30, 1998), principal due \$400,000 in 1999.....	700	400
Other.....	558	333
	-----	-----
	4,080	1,045
Less current portion of long-term debt.....	1,240	633
	-----	-----
Long-term portion of debt.....	\$2,840	\$ 412
	=====	=====

Fiscal year principal payments of long-term debt as of June 30, 1998 are as follows (in thousands):

1999.....	\$ 633
2000.....	254
2001.....	138
2002.....	20

Total.....	\$1,045
	=====

6. INCOME TAXES

For financial reporting purposes, income before provision for income taxes and minority interest includes the following components (in thousands):

	1996	1997	1998
	-----	-----	-----
Pretax income:			
United States.....	\$1,965	\$2,655	\$ 4,505
Foreign.....	1,288	2,938	6,495
	-----	-----	-----
Total pretax income.....	\$3,253	\$5,593	\$11,000
	=====	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

The Company's provision for income taxes is composed of the following (in thousands):

	1996	1997	1998
	-----	-----	-----
Current:			
Federal.....	\$ 510	\$1,256	\$1,729
State.....	21	24	246
Foreign.....	592	1,036	1,091
	-----	-----	-----
	1,123	2,316	3,066
Deferred.....	(12)	(900)	(314)
	-----	-----	-----
Total provision.....	\$1,111	\$1,416	\$2,752
	=====	=====	=====

Deferred income tax assets (liabilities) At June 30, 1997 and 1998 consisted of the following (in thousands):

	1997	1998
	-----	-----
State income taxes.....	\$ 1,455	\$ 1,585
Depreciation.....		67
Other.....	301	644
	-----	-----
Total deferred income tax assets.....	1,756	2,296
	-----	-----
Depreciation.....	(43)	
Capitalized software development costs.....	(219)	(217)
State income taxes.....	(329)	(462)
Revitalization zone deductions.....	(392)	(530)
	-----	-----
Total deferred income tax liabilities.....	(983)	(1,209)
	-----	-----
Net deferred income taxes.....	\$ 773	\$ 1,087
	=====	=====

The consolidated effective income tax rate differs from the federal statutory income tax rate due primarily to the following:

	1996	1997	1998
	----	----	-----
Provision for income taxes at federal statutory rate...	35.0%	35.0%	35.0%
State income taxes (credits), net of federal benefit...	0.2	(4.7)	(1.1)
Nontaxable earnings of FSC.....	(5.7)	(4.9)	(1.3)
Research and development tax credits.....		(1.7)	(1.7)
Foreign income subject to tax at other than federal statutory rate.....	1.1	(1.0)	(10.9)
Other.....	3.6	2.6	5.0
	----	----	-----
Effective income tax rate.....	34.2%	25.3%	25.0%
	=====	=====	=====

The Company does not provide for U.S. income taxes on the undistributed earnings of the foreign subsidiaries, as it is the Company's intention to utilize those earnings in the foreign operations for an indefinite period of time. At June 30, 1998, undistributed earnings of the foreign subsidiaries amounted to approximately \$8,667,000. It is not practicable to determine the amount of income or withholding tax that would be payable upon the remittance of those earnings.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

7. COMMITMENTS AND CONTINGENCIES

The Company leases some of its production and office facilities and certain equipment under various operating leases. Most of these leases provide for increases in rents based on the Consumer Price Index and include renewal options ranging from two to ten years. Future minimum lease payments under such leases as of June 30, 1998 are as follows:

1999.....	\$ 833,000
2000.....	745,000
2001.....	711,000
2002.....	630,000
2003.....	622,000
2004 and thereafter.....	3,145,000

Total.....	\$6,686,000
	=====

Total rent expense included in the accompanying consolidated financial statements was \$901,000, \$921,000 and \$1,013,000 for the years ended June 30, 1996, 1997 and 1998, respectively.

The Company is involved in various claims and legal proceedings arising out of the conduct of its business, including those relating to patent rights and related licensing issues. The principal litigation involves claims that certain technology used in the Company's scanners infringes on certain existing patents and seeks damages in an unspecified amount and an injunction barring the Company from making, using, selling or offering for sale certain of its security and inspection products in the United States. The Company has alleged that its security products do not infringe the patents, and that the plaintiffs in the suit had previously granted the Company the right to market its security and inspection products. In the event it is determined that the Company's products infringe upon the rights of the plaintiffs and that the Company does not have the right to use the technology in its products, the Company could be prevented from marketing most of its security and inspection products in the United States and could be required to pay a significant amount of damages. On August 31, 1998, the parties participated in a mandatory settlement conference and are now finalizing the language of the settlement.

On January 18, 1996 a former employee filed a lawsuit against the Company, alleging wrongful termination of employment by the Company. The plaintiff alleged that irregularities occurred at the Company resulting in over payments by the U.S. Government to the Company. The Company has filed a motion to dismiss which is currently pending. If the motion to dismiss is not granted, the Company will vigorously defend the lawsuit. Both the Company and its counsel believe that the Company will prevail.

8. STOCK OPTIONS

The Company has two stock option plans. Under the 1987 plan, 1,050,000 shares of common stock have been reserved for the issuance of incentive stock options to key employees, directors and officers of the Company. The price, terms and conditions of each issuance are determined by the Board of Directors, with the advice of and input from the Compensation Committee.

The 1997 plan was established in May 1997 and authorizes the grant of up to 850,000 shares of the Company's common stock in the form of incentive and nonqualified options. Employees, officers and Directors are eligible under this plan, which is administered by the Board of Directors, which determines the terms and conditions of each grant with the advice of and input from the Compensation Committee. The exercise price of

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

nonqualified options may not be less than 85% of the fair market value of the Company's common stock at the date of grant. The exercise price of incentive stock options may not be less than the fair market value of the Company's common stock at the date of grant. The exercise price of incentive stock options granted to individuals that own greater than 10% of the Company's voting stock may not be less than 110% of the fair market value of the Company's common stock at the date of grant.

Exercise periods for incentive and nonqualified options granted under this plan may not exceed ten years from the grant date.

In November and December 1996, the Company granted stock options for the purchase of 235,125 shares of the Company's common stock to certain employees at prices below the \$6.67 estimated fair market value at the date of grant. The options were accelerated to vest immediately, and accordingly, the Company has recorded compensation expense for the year ended June 30, 1997, representing the excess of the fair value of the Company's common stock at the date of grant over the option exercise prices.

The following summarizes stock option activity for the years ended June 30, 1996, 1997 and 1998:

	NUMBER OF OPTIONS	OPTION PRICE	
		WEIGHTED AVERAGE	TOTAL
Outstanding, June 30, 1995.....	297,375	1.57	\$ 469,000
Granted.....	51,000	2.17	111,000
Exercised.....	(16,125)	1.06	(17,000)
Canceled.....	(13,500)	1.60	(22,000)
Outstanding, June 30, 1996.....	318,750	1.70	541,000
Granted.....	669,611	8.88	5,947,000
Exercised.....	(118,125)	1.24	(146,000)
Canceled.....	(9,750)	2.38	(23,000)
Outstanding, June 30, 1997.....	860,486	7.34	6,319,000
Granted.....	168,000	10.10	1,696,000
Exercised.....	(205,387)	2.47	(508,000)
Canceled.....	(10,187)	9.34	(95,000)
Outstanding, June 30, 1998.....	812,912	9.12	7,412,000

The following summarizes pricing and term information for options outstanding as of June 30, 1998:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	NUMBER OUTSTANDING AT JUNE 30, 1998	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	EXERCISABLE AT JUNE 30, 1998	WEIGHTED AVERAGE EXERCISE PRICE
\$ 2.00.....	45,000	1.6 years	\$2.00	45,000	\$2.00
2.33 to 3.33.....	173,175	3.2	2.70	160,988	2.75
10.00 to 11.01.....	168,000	5	10.10		
11.50 to 13.50.....	426,737	4	12.09	106,684	11.50
\$ 2.00 to 13.50.....	812,912	3.9	\$9.12	312,672	\$5.63

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

The Company has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." The estimated fair value of options granted during 1997 and 1998 pursuant to SFAS No. 123 was approximately \$1,054,000 and \$768,000, respectively. Had the Company adopted SFAS No. 123, pro forma net income would have been \$4,058,000 and \$7,787,000, and pro forma net income per share would have been \$0.64 and \$0.87 for 1997 and 1998, respectively. The fair value of each option grant was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: dividend yield of zero and volatility of 44% (1997 0%), a risk free interest rate of 5.47% (1997 6.33%) and expected option lives of five years.

9. STOCKHOLDERS' EQUITY

In May 1997, the Company's Board of Directors authorized a 1.5-for-1 stock split of the outstanding common stock. All share and per share numbers have been adjusted to retroactively reflect the common stock split.

The preferred stock had a liquidation preference of \$1.00 per share and was otherwise entitled to the same voting, dividend and all other rights as the common stock.

In June 1997, in order to simplify the capital structure of the Company, holders of the preferred stock converted each preferred share into 1.5 shares (post-split) of common stock.

In June 1997, the Company amended its articles of incorporation, which articles authorize 10,000,000 shares of new preferred stock. Such preferred stock has no par value, and no preferred shares are issued and outstanding at June 30, 1997 and June 30, 1998, respectively.

In connection with the acquisition of the minority interest of a subsidiary in November 1996 (see Note 1), the Company granted the selling shareholders/employees options to purchase 45,486 shares of the Company's common stock at \$11.50 per share. The options vest over four years from the date of grant.

The Company's Registration Statement for its initial public offering of securities (File No. 333-29179) became effective on October 1, 1997, when the Company issued 3,330,000 shares of its common stock for net proceeds of \$41,000,000.

10. RELATED-PARTY TRANSACTIONS

The Company contracts with entities affiliated by common ownership to provide messenger service and auto rental and printing services. The Company also contracts for professional services from a firm that has a partner serving as a member of the Company's Board of Directors. Included in cost of sales, selling, general and administrative expenses for the years ended June 30, 1996, 1997 and 1998 are approximately \$83,000, \$111,000 and \$99,000 for messenger service and auto rental; \$63,000, \$82,000 and \$186,000 for printing services; and \$7,000, \$11,000 and \$13,000 for professional services, respectively. For the year ended June 30, 1997, the Company paid an one time consulting fee amounting to \$100,000 to an entity that is a shareholder of the Company.

Shareholders and other parties related to the Company have made loans to the Company under agreements subordinating such loans to the Company's bank borrowings (see Notes 4 and 5). Interest expense related to such borrowings was approximately \$263,000 and \$146,000 for the years ended June 30, 1996 and 1997, respectively.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

11. GOVERNMENT SETTLEMENT

During 1994, a subsidiary of the Company was notified that the U.S. Department of Justice was conducting an investigation regarding the testing of certain products that were sold by a subsidiary under government contracts. A settlement of \$1,500,000 was agreed to, and was accrued and charged to operations in the year ended June 30, 1994. The settlement is being paid in five increasing installments, with the unpaid principal balance bearing interest at the 52-week Treasury bill rate. At June 30, 1998, the unpaid balance of this settlement was \$400,000 (see Note 5).

12. EMPLOYEE BENEFIT PLANS

OSI Systems, Inc. has a qualified employee retirement savings plan. The plan provides for a contribution by the Company, which is determined annually by the Board of Directors. In addition, the plan permits voluntary salary reduction contributions by employees. The Company made no contributions to the plan for the years ended June 30, 1998, 1997 and 1996. During 1995, a subsidiary in the U.K. ("Rapiscan U.K.") transferred its existing employees from their former owner's plan to a new plan, the Rapiscan U.K. Defined Benefit Plan, which covers certain Rapiscan U.K. employees. The benefits under this plan are based on years of service and the employees' highest 12 months' compensation during the last five years of employment. Rapiscan U.K.'s funding policy is to make the minimum annual contributions required by applicable regulations based on an independent actuarial valuation sufficient to provide for benefits accruing after that date. Pension expense for the years ended June 30, 1996, 1997 and 1998 was approximately \$91,000, \$89,000 and \$138,000, respectively.

13. SUBSEQUENT EVENTS

On September 2, 1998, the Company acquired all the shares of Osteometer MediTech A/S, a Danish manufacturer of diagnostic scanners to detect osteoporosis, for \$7,750,000 cash. The Company also made investments in the aggregate amount of \$800,000 in two other companies.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

14. UNAUDITED QUARTERLY RESULTS

The following table presents unaudited quarterly financial information for the four quarters ended June 30, 1998:

	QUARTER ENDED IN THOUSANDS			
	SEPTEMBER 30, 1997	DECEMBER 31, 1997	MARCH 31, 1998	JUNE 30, 1998
	(UNAUDITED)			
Revenues.....	\$22,961	\$24,285	\$21,893	\$24,779
Costs of goods sold.....	16,649	17,183	15,366	17,754
Gross profit.....	6,312	7,102	6,527	7,025
Operating expenses:				
Selling, general and administrative.....	3,099	3,293	3,106	3,278
Research and development.....	827	973	995	995
Total operating expenses.....	3,926	4,266	4,101	4,273
Income from operations.....	2,386	2,836	2,426	2,752
Interest expense (income), net...	411	(369)	(303)	(339)
Income before provision for in- come taxes.....	1,975	3,205	2,729	3,091
Provision for income taxes.....	534	835	667	716
Net income.....	\$ 1,441	\$ 2,370	\$ 2,062	\$ 2,375
Earnings per common share.....	\$ 0.23	\$ 0.25	\$ 0.21	\$ 0.25
Earnings per common share--Assum- ing dilution.....	\$ 0.22	\$ 0.24	\$ 0.21	\$ 0.24

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

YEARS ENDED JUNE 30, 1996, 1997 AND 1998

15. SEGMENT INFORMATION

The Company's operating locations include the United States, Europe (United Kingdom and Norway) and Asia (Singapore and Malaysia). The Company's operations and identifiable assets by geographical area are as follows (in thousands):

	YEAR ENDED JUNE 30, 1996				
	UNITED STATES	EUROPE	ASIA	ELIMINATIONS	CONSOLIDATED
Revenues.....	\$ 42,403	\$15,346	\$ 3,769		\$61,518
Transfer between geographical areas.....	6,304	3,092	10,974	\$(20,370)	
Net revenues.....	\$ 48,707	\$18,438	\$14,743	\$(20,370)	\$61,518
Operating income.....	\$ 2,641	\$ 1,278	\$ 890	\$ (197)	\$ 4,612
Identifiable assets.....	\$ 42,932	\$10,179	\$ 5,986	\$(23,788)	\$35,309

	YEAR ENDED JUNE 30, 1997				
	UNITED STATES	EUROPE	ASIA	ELIMINATIONS	CONSOLIDATED
Revenues.....	\$ 54,310	\$18,915	\$ 4,403		\$77,628
Transfer between geographical areas.....	8,655	5,156	12,191	\$(26,002)	
Net revenues.....	\$ 62,965	\$24,071	\$16,594	\$(26,002)	\$77,628
Operating income.....	\$ 3,814	\$ 1,849	\$ 1,390	\$ (263)	\$ 6,790
Identifiable assets.....	\$ 52,367	\$15,066	\$ 8,395	\$(28,495)	\$47,333

	YEAR ENDED JUNE 30, 1998				
	UNITED STATES	EUROPE	ASIA	ELIMINATIONS	CONSOLIDATED
Revenues.....	\$ 56,710	\$27,537	\$ 9,671		\$93,918
Transfer between geographical areas.....	6,786	3,329	12,672	\$(22,787)	
Net revenues.....	\$ 63,496	\$30,866	\$22,343	\$(22,787)	\$93,918
Operating income.....	\$ 4,151	\$ 2,686	\$ 4,329	\$ (766)	\$10,400
Identifiable assets.....	\$143,080	\$16,254	\$ 9,591	\$(82,103)	\$86,822

SCHEDULE II--VALUATION AND QUALIFYING ACCOUNTS

DESCRIPTION	ADDITIONS			DEDUCTIONS-- WRITE-OFFS (RECOVERIES)	BALANCE AT END OF PERIOD
	BALANCE AT BEGINNING OF PERIOD	(1) CHARGED TO COSTS AND EXPENSES	(2) CHARGED TO OTHER ACCOUNTS		
Balance for doubtful accounts:					
Year Ended June 30, 1996.	\$ 53	\$404	--	\$181	\$276
	====	====	===	====	====
Year Ended June 30, 1997.	\$276	\$389	--	\$ 79	\$586
	====	====	===	====	====
Year Ended June 30, 1998.	\$586	\$122	--	\$157	\$551
	====	====	===	====	====

[LOGO OF SANWA BANK CALIFORNIA]

CREDIT AGREEMENT

(\$10,000,000 Revolving Line of Credit)

[\$10,000,000 Letter of Credit Sub-Facility, \$5,000,000 Acceptance Sub-Facility
and \$4,500,000 Foreign Exchange Sub-Facility]

(\$3,000,000 Equipment Term Loan)

(\$15,000,000 Acquisition Non-revolving Line Converting to Term)

This Credit Agreement (the "Agreement"), which supersedes the prior agreement dated January 24, 1997, is made and entered into this 22nd day of May, 1998, by and between SANWA BANK CALIFORNIA (the "Bank") and OSI SYSTEMS, INC., UDT SENSORS, INC. RAPISCAN SECURITY PRODUCTS (U.S.A.), INC. AND FERSON OPTICS, INC. (each a "Borrower" and together, the "Borrowers"), on the terms and conditions that follow:

SECTION 1
DEFINITIONS

1.01 CERTAIN DEFINED TERMS: Unless elsewhere defined in this Agreement, the following terms shall have the following meanings (such meanings to be generally applicable to the singular and plural forms of the terms defined):

- (a) "ACCOUNT DEBTOR": shall mean the person or entity obligated to the Borrower upon an account.
- (b) "ACQUISITION ADVANCE": shall mean an advance to any Borrower under the Acquisition Line of Credit, Section 4.01.
- (c) "ALTERNATE CURRENCY": shall mean any lawful currency other than Dollars which is freely transferable and convertible into Dollars.
- (d) "BUSINESS DAY": shall mean a day other than a Saturday or Sunday on which commercial banks are open for business in California, USA, and, with respect to Eurocurrency Advances, on which dealings are carried on in the London interbank market and banks are open for business in London and in the country of issue of the currency of such Advance.
- (e) "COLLATERAL": shall mean the property described in Section 3.01, together with any other personal or real property in which the Bank may be granted a lien or security interest to secure payment of the Obligations.
- (f) "DEBT": shall mean all liabilities of each Borrower less Subordinated Debt.
- (g) "DOLLARS" AND THE SIGN "\$": shall mean lawful money of the United States.

(h) "EBITDA": shall mean earnings exclusive of extraordinary gains and before deductions for interest expense, taxes, depreciation and amortization expense.

(i) "EFFECTIVE TANGIBLE NET WORTH": shall mean each Borrower's stated net worth plus Subordinated Debt but less the book value of all intangible assets of such Borrower (i.e., goodwill, trademarks, patents, copyrights, organization expense and similar intangible items including, but not limited to investments in and all amounts due from affiliates, officers or employees).

(j) "EQUIPMENT ADVANCE": shall mean an advance to any Borrower under the Equipment Line under Section 3.01.

(k) "ERISA": shall mean the Employee Retirement Income Security Act of 1974, as amended from time to time, including (unless the context otherwise requires) any rules or regulations promulgated thereunder.

(l) "EVENT OF DEFAULT": shall have the meaning set forth in Section 9.

(m) "EXPIRATION DATE": shall mean November 30, 1999 or the date of termination of the Bank's commitment to lend under this Agreement pursuant to Section 10.03, whichever shall occur first.

(n) "INDEBTEDNESS": shall mean, with respect to each Borrower, (i) all indebtedness for borrowed money or for the deferred purchase price of property or services in respect of which any Borrower is liable, contingently or otherwise, as obligor, guarantor or otherwise, or in respect of which Borrower otherwise assures a creditor against loss and (ii) obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, reported as capital leases in respect of which any Borrower is liable, contingently or otherwise, or in respect of which any Borrower otherwise assures a creditor against loss.

(o) "OBLIGATIONS": shall mean all amounts owing by each Borrower to the Bank pursuant to this Agreement including, but not limited to, the unpaid principal amount of Acquisition, Revolving, and Equipment Advances.

(p) "PERMITTED LIENS": shall mean: (i) liens and security interests securing indebtedness owed by each Borrower to the Bank; (ii) liens for taxes, assessments or similar charges either not yet due or being contested in good faith; (iii) liens of materialmen, landlords, mechanics, warehousemen, or carriers or other like liens arising in the ordinary course of business and securing obligations which are not yet delinquent; (iv) purchase money liens or purchase money security interests upon or in any property acquired or held by each Borrower in the ordinary course of business to secure Indebtedness outstanding on the date hereof or permitted to be incurred under Section 8.09 hereof; (v) liens and security interests which, as of the date hereof, have been disclosed to and approved by the Bank in writing; and (vi) those liens and security interests which in the aggregate constitute an immaterial and insignificant monetary amount with respect to the net value of each Borrower's assets; (vii) liens against UDT Sensors, Inc. ("UDT") which may hereafter be granted in favor of the United States of America as set forth in that certain Stipulation for Consent Judgment referred to in and executed pursuant to that certain Criminal Plea and Sentencing Agreement between UDT and the United States Attorney's Office for the Central District of California, provided that such liens, if granted to the United States of America, shall be subordinated to those of the Bank pursuant

to a subordination agreement in form and substance satisfactory to the Bank and (Viii) real estate loans from other lenders which are obtained to finance real property of Borrowers not to exceed \$4,000,000.

(q) "REDENOMINATE", "REDENOMINATION" AND "REDENOMINATED": each refers to redenomination of each Revolving Advance from Dollars into an Alternate Currency or from an Alternate Currency into Dollars or another Alternate Currency pursuant to Section 2.01.

(r) "REFERENCE RATE": shall mean an index for a variable interest rate which is quoted, published or announced from time to time by the Bank as its reference rate and as to which loans may be made by the Bank at, below or above such reference rate.

(s) "REVOLVING LINE OF CREDIT": shall mean the credit facility described in Section 2.01

(t) "REVOLVING ADVANCES". Shall mean any advance under the Revolving Line of Credit, Section 2.01.

(u) "SPREAD". Shall mean the following interest rate percentage based upon the debt Coverage Ratio then in effect:

Debt Coverage Ratio	Spread
Less than 2 to 1	1.25%
Between 2.25 and 2 to 1	1.50%
Between 2.75 and 2.25 to 1	1.75%
2.75 to 1 or greater	2.00%

(v) "SUBORDINATED DEBT": shall mean such liabilities of each Borrower which have been subordinated to those owed to the Bank in a manner acceptable to the Bank.

(w) "VALUE". Shall mean the lesser of: the invoice cost of the equipment (including taxes, license fees, transportation costs, insurance premiums, and installation and connection expenses, fees and costs); or the book value of the equipment; or the liquidation value of the equipment as reasonably determined by the Bank.

1.02 ACCOUNTING TERMS: All references to financial statements, assets, liabilities, and similar accounting items not specifically defined herein shall mean such financial statements or such items prepared or determined in accordance with generally accepted accounting principles consistently applied and, except where otherwise specified, all financial data submitted pursuant to this Agreement shall be prepared in accordance with such principles.

1.03 OTHER TERMS: Other terms not otherwise defined shall have the meanings attributed to such terms in the California Uniform Commercial Code.

1.04 CURRENCY EQUIVALENTS GENERALLY: For all purposes of this Agreement other than Section 2, the equivalent in any Alternate Currency of an amount in Dollars shall be determined at the rate of exchange quoted by the Bank in Los Angeles, at 9:00 A.M. two days before the date of determination, for the spot purchase in the relevant foreign exchange market of such amount of Dollars with such Alternate Currency.

SECTION 2
REVOLVING LINE OF CREDIT

2.01 THE REVOLVING LINE OF CREDIT. On terms and conditions as set forth herein, the Bank agrees to make Revolving Advances in Dollars or in Alternate Currency to each Borrower from time to time from the date hereof to the Expiration Date, provided the aggregate amount of such Revolving Advances outstanding at any time does not exceed \$10,000,000 or the Dollar equivalent in Alternate Currency (the "Revolving Line of Credit"). Within the foregoing limits, each Borrower may borrow, partially or wholly prepay, and reborrow under this Section 2.01.

(a) MAKING REVOLVING LINE ADVANCES. Each Revolving Advance shall be conclusively deemed to have been made at the request of and for the benefit of each Borrower (i) when credited to any deposit account of any Borrower maintained with the Bank or (ii) when paid in accordance with such Borrower's written instructions. Subject to the requirements of Section 6, Revolving Advances shall be made by the Bank upon telephonic or facsimile request received from the Borrower, and confirmed in writing within two Business Days, which request shall be received not later than 12:00 p.m. (Pacific Time) on the date specified for a Variable Rate Revolving Advance and 7:00 a.m. (Pacific Time) two business days prior to the date specified for a Eurocurrency Revolving Advance or a Cost of Funds Revolving Advance, each of which dates shall be a Business Day. The rates for a Eurocurrency Revolving Advance or a Cost of Funds Revolving Advance shall be set two Business Days prior to the Advance.

(b) REVOLVING LINE ACCOUNT. The Bank shall maintain on its books a record of account in which the Bank shall make entries for each Revolving Advance and such other debits and credits as shall be appropriate in connection with the Revolving Line of Credit (the "Revolving Line Account"). The Bank shall provide the Borrowers with a monthly statement of the Borrowers' Account, which statement shall be considered to be correct and conclusively binding on the Borrowers unless any Borrower notifies the Bank to the contrary within 18 months after such Borrower's receipt of any such statement which it deems to be incorrect. Each Borrower hereby authorizes the Bank, if and to the extent payment owed to the Bank under the Revolving Line of Credit is not made when due, to charge, from time to time, against any or all of any Borrower's deposit accounts with the Bank any amount so due.

(c) MANDATORY REPAYMENTS. On the Expiration Date, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Revolving Advances then outstanding, together with all accrued and unpaid interest thereon, provided, however, that any Revolving Advance denominated in Dollars must be repaid in Dollars and any Revolving Advance denominated in an Alternate Currency must be repaid in the same Alternate Currency.

(d) INTEREST ON REVOLVING ADVANCES. Interest shall accrue from the date of each Revolving Advance under the Revolving Line of Credit at one of the following rates, as quoted by the Bank and as elected by any Borrower below:

(i) VARIABLE RATE REVOLVING ADVANCES. For Revolving Advances denominated in Dollars, a variable rate per annum equivalent to an index for a variable interest rate which is quoted, published or announced from time to time by the Bank as its reference rate (the "Reference Rate") and as to which loans may be made by the Bank at, below or above such Reference Rate (the "Variable Rate"). Interest shall be adjusted concurrently with any change in the Reference Rate. A Revolving Advance which bears interest at the Variable Rate is hereinafter referred to as a "Variable Rate Revolving Advance".

(ii) EUROCURRENCY REVOLVING ADVANCES. For Revolving Advances denominated in Dollars or in Alternate Currency, a fixed rate quoted by the Bank for one, three, six, nine or twelve months or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) [the "Eurocurrency Interest Period"] for Revolving Advances in the minimum amount of \$500,000 and in \$100,000 increments thereafter. Such interest rate shall be a percentage, rounded upward to the nearest one-hundredth of one percent, equivalent to the relevant Spread then in effect plus the Bank's Eurocurrency Rate for Dollars or such Alternate Currency which is that rate determined by the Bank's Treasury Desk as being the approximate rate at which the Bank could purchase Dollars or Alternate Currency deposits in an amount approximately equal to the amount of the relevant Revolving Advance and for a period of time approximately equal to the relevant Eurocurrency Interest Period (adjusted for any and all assessments, surcharges and reserve requirements pertaining to the purchase by the Bank of such Alternate Currency deposits [the "Eurocurrency Rate"]). A Revolving Advance which bears interest at the Eurocurrency Rate is hereinafter referred to as the "Eurocurrency Revolving Advance".

(iii) COST OF FUNDS REVOLVING ADVANCES. For Revolving Advances denominated in Dollars, the Bank hereby agrees to make Revolving Advances to the Borrower, at Borrower's election, at a fixed rate quoted by Bank in its sole discretion for each Revolving Advance (the "Cost of Funds Rate") plus the applicable Spread and for such period of time that the Bank may quote and offer, provided that any such period of time shall be for at least 7 days and provided further that any such period of time does not extend beyond the Expiration Date (the "Cost of Funds Interest Period") for Revolving Advances in the minimum amount \$500,000 and in \$100,000 increments thereafter. Revolving Advances based upon the Cost of Funds Rate are hereinafter referred to as "Cost of Funds Revolving Advances".

Eurocurrency Revolving Advances and Cost of Funds Revolving Advances are sometimes hereinafter referred to as a "Fixed Rate Revolving Advance".

Interest on Variable Rate Revolving Advances and Cost of Funds Revolving Advances shall be paid in Dollars in monthly installments commencing on the first day of the month following the date of the first such Revolving Advance and continuing on the first day of each month thereafter.

Interest on any Eurocurrency Revolving Advance shall be paid on the last day of the Eurocurrency Interest Period pertaining to such Eurocurrency Revolving Advance and shall be paid in Dollars or in the relevant Alternate Currency as the case may be. Each Borrower further jointly and severally promises and agrees to pay the Bank interest on any Eurocurrency Revolving Advance with an Eurocurrency Interest Period in excess of 90 days on a quarterly basis (i.e., on the last day of each 90-day period occurring in such Eurocurrency Interest Period) and on the last day of the relevant Eurocurrency Interest Period.

Interest on any Revolving Advances shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed.

If interest is not paid as and when it is due, it shall be added to the principal, become and be treated as a part thereof, and shall thereafter bear like interest.

(e) NOTICE OF ELECTION TO ADJUST INTEREST RATE. Each Borrower may elect that interest on a Fixed Rate Revolving Advance shall continue to accrue at a newly quoted Eurocurrency Rate or Cost of Funds Rate; provided, however, that such notice shall be received by the Bank no later than 7:00 a.m. two business days prior to the last day of the Eurocurrency Interest Period for a Eurocurrency Revolving Advance and 1:00 p.m. one business day prior to the last day of a Cost of Funds Interest Period for a Cost of Funds Revolving

Advance. Such notice may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with an air courier on the same day. The Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of such Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, the Borrowers shall have effected the borrowing, redenomination or continuation of Revolving Advances hereunder. Any Borrower may elect that interest on a Fixed Rate Revolving Advance shall accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than one business day prior to the last day of the Interest Period pertaining to such Fixed Rate Revolving Advance, and provided further, however, that such Fixed Rate Revolving Advance shall be in Dollars or Redenominated in Dollars pursuant to the terms of Section 2.01 (f). If the Bank shall not have received notice (as prescribed herein) of such Borrower's election that interest on any Fixed Rate Revolving Advance shall continue to accrue at the newly quoted Eurocurrency Rate or Cost of Funds Rate or Variable Rate as the case may be, the Borrower shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate then in effect and any Alternate Currency shall be Redenominated in Dollars.

(f) REDENOMINATION OF REVOLVING ADVANCES. Any Borrower may, upon notice given to the Bank at least four Business Days prior to the date of the proposed Redenomination, request that a Eurocurrency Revolving Advance be Redenominated from Dollars into an Alternate Currency or from an Alternate Currency into Dollars or another Alternate Currency; provided, however, that any Redenomination shall be made on, and only on, the last day of an Interest Period for such Revolving Advances. Each such notice of request of a Redenomination ("Notice of Redenomination") shall be by telecopier, telex or cable, confirmed immediately in writing, or may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with an air courier on the same day, and the Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of such Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, the Borrowers shall have effected the borrowing, redenomination or continuation of Revolving Advances hereunder, specifying (i) the Eurocurrency Revolving Advance(s) to be Redenominated, (ii) the date of the proposed Redenomination, (iii) the Alternate Currency into which such Revolving Advances are to be Redenominated, and (iv) the duration of the Interest Period for such Revolving Advances upon being so Redenominated. In the case of a Notice of Redenomination which requests a Redenomination of Revolving Advances into an Alternate Currency, such Redenomination is subject to confirmation by Bank not later than the third Business Day before the requested date of such Redenomination that such Bank agrees to such Redenomination. which confirmation shall be notified to the relevant Borrower. If no confirmation is provided the Redenomination will not occur. Each Revolving Advance so requested to be Redenominated will be Redenominated, on the date specified therefor in such Notice of Redenomination, into an equivalent amount thereof in the currency requested in such Notice of Redenomination, such equivalent amount to be determined on such date in accordance with Section 2.01 (l), and, upon being so Redenominated, will have an initial Interest Period as requested in such Notice of Redenomination.

(g) PREPAYMENT:

(i) The Borrowers may prepay any Revolving Advance in whole or in part, at any time and without penalty, provided, however, that: (a) any partial prepayment shall first be applied, at the Bank's option, to accrued and unpaid interest and next to the outstanding principal balance; and (b) during any period of time in which interest is accruing on any Revolving Advance on the basis of the Eurocurrency Rate or the Cost of Funds Rate, no prepayment shall be made except on a day which is the last day of the Interest Period pertaining thereto provided, however, if the whole or any part of any

Fixed Rate Revolving Advance is prepaid by reason of acceleration or otherwise, each Borrower shall jointly and severally, upon the Bank's request, promptly pay to and indemnify the Bank for all costs and any loss actually incurred by the Bank, excluding loss of profit on any margin, but including any loss resulting from the re-employment of funds, sustained by the Bank as a consequence of such prepayment, and provided further, that any prepayment hereunder shall not be deemed to be an event of default.

(ii) If, on the last day of any Interest Period, the equivalent in Dollars of the aggregate principal amount of all Eurocurrency Revolving Advances then outstanding when combined with the aggregate principal amount of all Variable Rate Revolving Advances and Cost of Funds Revolving Advances then outstanding exceeds the Revolving Line of Credit, each Borrower shall on such last day jointly and severally prepay an aggregate principal amount of such Revolving Advances to the Bank in an amount at least equal to such excess, with accrued interest to the date of such prepayment on the principal amount prepaid.

(h) INDEMNIFICATION FOR EUROCURRENCY RATE AND COST OF FUNDS RATE COSTS. During any period of time in which interest on any Revolving Advance is accruing on the basis of the Eurocurrency Rate or the Cost of Funds Rate, each Borrower shall jointly and severally, upon the Bank's 15-days written request, which request shall explain in reasonable detail the reason for such costs or payments, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to the Alternate Currency or Dollars or cost of funds used by the Bank in quoting and determining the Eurocurrency Rate or the Cost of Funds Rate under this Agreement, provided that Bank notifies Borrower within 15 days of Bank having knowledge that such assessment, reserve, deposit or similar requirement or any surcharge, tax or fee shall be imposed.

(i) EUROCURRENCY RATE OR COST OF FUNDS RATE INFEASIBLE. In the event that the Bank shall at any time determine that the accrual of interest on the basis of the Eurocurrency Rate or the Cost of Funds Rate (i) is infeasible at the time of any borrowing, continuation or Redenomination because the Bank is unable to determine the Eurocurrency Rate or Cost of Funds Rate due to the unavailability of Dollars or Alternate Currency deposits, contracts or time deposits in an amount approximately equal to the amount of the relevant Revolving Advance and for a period of time approximately equal to relevant Interest Period or (ii) is or has become unlawful or infeasible by reason of the Bank's compliance with any new law, rule, regulation, guideline or order, or any new interpretation of any present law, rule, regulation, guideline or order, then the Bank shall give telephonic notice thereof (confirmed in writing) to the Borrowers, in which event such Fixed Rate Revolving Advance shall be immediately converted or Redenominated into a Variable Rate Revolving Advance.

(j) FAILURE TO BORROW. In the case of any Fixed Rate Revolving Advance, each Borrower shall jointly and severally indemnify Bank against any loss, cost or expense incurred by Bank as a result of any failure to borrow on the date specified for such Fixed Rate Revolving Advance (other than as a result of Bank's failure to make funds available for such Revolving Advance), including, without limitation, any loss (excluding loss of anticipated profits), cost or expense incurred by reason of the liquidation or reemployment of deposits or other funds acquired by Bank to fund such Fixed Rate Revolving Advance to be made by Bank when such Fixed Rate Revolving Advance is not made on such date.

(k) COMPUTATIONS AND PAYMENTS. Interest on any Revolving Advance shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed. Whenever any payment hereunder shall be stated to be due on a day other than a Business Day, such payment shall be made on the

next succeeding Business Day, and such extension of time shall in such case be included in the computation of payment of interest; provided, however, if such extension would cause payment of interest on or principal of Eurocurrency Revolving Advances to be made in the next following calendar month, such payment shall be made on the immediately preceding Business Day.

(1) CURRENCY EQUIVALENTS. For purposes of the provisions of this Section 2, (i) the equivalent in Dollars of any Alternate Currency shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange Dollars for such Alternate Currency at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined, (ii) the equivalent in any Alternate Currency of any other Alternate Currency shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange such Alternate Currency for the equivalent in Dollars of such other Alternate Currency at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined, and (iii) the equivalent in any Alternate Currency of Dollars shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange such Alternate Currency for Dollars at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined. Except as specified in Section 1.04, the equivalent in Dollars of each Eurocurrency Rate Revolving Advance made in an Alternate Currency shall be recalculated hereunder on each date that it shall be necessary to determine the unused portion of Bank's Revolving Line of Credit or any or all Revolving Advance or Revolving Advances outstanding on such date.

(m) COMMITMENT FEE. The Borrowers agree to pay to Bank, jointly and severally, a commitment fee on the unused portion of the Revolving Line of Credit, beginning from the date of this Agreement, of .125% per annum, payable quarterly in arrears on the last day of each March, June, September and December of each year.

2.02 LETTERS OF CREDIT SUBLIMIT. The Bank agrees to issue commercial and stand-by letters of credit (each a "Letter of Credit") on behalf of the Borrower, provided, however, at no time shall the total face amount of all Letters of Credit outstanding (including all existing Letters of Credit outstanding at the time of execution of this Agreement issued by Bank under prior Credit Agreements) less any partial draws paid by the Bank and not reimbursed by the Borrower exceed the sum of \$10,000,000.00, and provided further, at no time shall the total undrawn amount of all Letters of Credit outstanding plus any partial draws paid by the Bank and not reimbursed by the Borrowers, together with the total principal amount of all Revolving Advances outstanding exceed the Revolving Line of Credit.

(a) Upon the Bank's request, each Borrower shall, jointly and severally, promptly pay to the Bank issuance fees and such other fees, commissions, costs and any out-of-pocket expenses charged or incurred by the Bank with respect to any Letter of Credit.

(b) The commitment by the Bank to issue Letters of Credit shall, unless earlier terminated in accordance with the terms of the Agreement, automatically terminate on the Expiration Date and no Letter of Credit shall expire on a date which is more than 90 days after the Expiration Date.

(c) Each Letter of Credit shall be in form and substance and in favor of beneficiaries satisfactory to the Bank, provided that the Bank may refuse to issue a Letter of Credit due to the nature of the transaction or its terms or in connection with any transaction where the Bank, due to the beneficiary or the nationality or residence of the beneficiary, would be prohibited by any applicable law, regulation or order from issuing such Letter of Credit.

(d) Prior to the issuance of each Letter of Credit but in no event later than 9:00 a.m. (California time) on the day such Letter of Credit is to be issued (which shall be a Business Day), the relevant Borrower

shall deliver to the Bank International Department a duly executed form of the Bank's standard form of application for issuance of letter of credit with proper insertions.

(e) The Borrowers shall, jointly and severally, upon the Bank's request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any future directive or requirement of any regulatory authority pertaining or relating to any Letter of Credit.

(f) Upon receipt from any beneficiary under a Letter of Credit of a demand for payment under such Letter of Credit (each a "Drawing"), the Bank

shall promptly notify the Borrower. Borrower promises and agrees to immediately reimburse the Bank, in cash or by a Revolving Advance, for any amounts paid the Bank pursuant to a Drawing. In the event the Borrower shall fail to reimburse the Bank in cash for a Drawing Bank shall make a Revolving Advance and the Borrower promises and agrees to pay interest on the amount of such Advance at a rate equal to the Reference Rate calculated on the basis of 360 day per year but charged on the actual number of days elapsed, said rate of interest to be adjusted concurrently with any change in the Reference Rate.

2.03 ACCEPTANCE FACILITY SUBLIMIT. Any Borrower may from time to time request the Bank to accept one or more drafts drawn on the Bank for the account of the Borrowers (each an "Acceptance"). At no time, however, shall the total principal balance of all Acceptances outstanding exceed \$5,000,000, and together with the total face amount of all outstanding Letters of Credit less any partial draws paid by the Bank and the total principal balance of all Revolving Advances outstanding, exceed the Revolving Line of Credit.

(a) REQUESTS FOR ACCEPTANCES. Each request for an Acceptance shall be made in writing or by telephone confirmed in writing (each a "Request"), shall be irrevocable, and shall involve one or more drafts as described below. Each Request shall be delivered or communicated to the Bank no later than 12:00 p.m. (California time) on the day (which shall be a business day) on which the creation of an Acceptance is requested. By making any such Request, the Borrower agrees that all matters relating to each such Acceptance shall be governed by the terms hereof and the Borrower restates all warranties and representations made by the Borrower herein as if made on the date of the Request and on the date that the Acceptance is created.

(b) ACCEPTANCES. Each Acceptance shall be created upon a Request by the Bank's acceptance of a draft in form and substance satisfactory to the Bank (each a "Draft"). Each Draft shall: (i) be drawn on the Bank by or on behalf or for the account of the Borrowers in accordance with the provisions hereof; (ii) have a minimum face amount of \$100,000 ; (iii) be for the purpose of financing only those transactions permitted by paragraph 7 of Section 13 of the Federal Reserve Act, as amended from time to time; and (iv) mature not more than 180 days after the date thereof (provided that, if such date is not a Business Day, the maturity shall be extended to the next succeeding Business Day). However, no Draft shall mature more than 90 days after the Expiration Date. Each Borrower hereby warrants that any Acceptances relating to the importation or exportation of goods or relating to the domestic shipment of goods shall: (i) not have a term in excess of the period of time which is usual and reasonably necessary to finance transactions of the character of the underlying import or export transaction or the underlying domestic shipment; (ii) not, together with all other Acceptances relating to any such shipment, have an aggregate face amount exceeding the CIF value of such shipment; and (iii) not be created more than 30 days after the date of shipment of goods to which such Acceptance relates. Acceptances relating to the storage of goods shall be subject to the further conditions that: (i) at the time such Acceptance is created, the goods being stored are covered by a warehouse receipt issued by a bonded warehouse independent of the Borrower and acceptable to the Bank; (ii) the goods covered by the warehouse receipt are readily marketable staples (as such term is defined in

Section 13 of the Federal Reserve Act by the Board of Governors of the Federal Reserve System or by Federal Reserve Bulletins) held pending a reasonably immediate sale, distribution or shipment; and (iii) the face amount of the Acceptance relating to such goods does not exceed the fair market value of the goods.

(c) ACCEPTANCE LIABILITY: Each Borrower is obligated, and hereby jointly and severally promises and agrees, to pay the Bank, on the maturity date of each Acceptance or on such earlier date as may be required pursuant hereto, the face amount of each such Acceptance.

(d) ACCEPTANCE COMMISSIONS. Each Borrower agrees, jointly and severally, upon acceptance by the Bank of each Draft and as a condition precedent to such Acceptance, to pay to the Bank a fee (the "Commission") in an amount equal to 1.5% per annum of the face amount of each Acceptance calculated on the basis of 360 days per year for the actual number of days (including the first day but excluding the last day) during the period which is for the term of the Draft.

(e) DISCOUNT OF ACCEPTANCES. The Bank agrees to discount any Acceptance that is created and presented to it for discount at a rate quoted by the Bank at the time the Acceptance is presented to the Bank for discount and for a similar dollar amount and a similar maturity as the Draft being presented to the Bank by the Borrower for acceptance (the "Acceptance Discount Rate"). On the date any such Acceptance is presented for discount, the Bank shall: (i) cause the aggregate discounted amount (less any Commission then payable by the Borrowers to the Bank hereunder) to be made available to the Borrowers by crediting such amount to any Borrower's demand deposit account maintained with the Bank, unless the Acceptance is created by a beneficiary under a Letter of Credit, in which event the Bank will cause the amount to be paid to such beneficiary and will notify the Borrowers as to the creation of the Acceptance; and (ii) advise the Borrowers of the Acceptance Discount Rate at which the Bank discounted such Acceptance. The Bank shall have the right, in its sole discretion, to sell, rediscount, hold or otherwise deal with or dispose of any such Acceptance discounted by it.

(f) ACCEPTANCE COLLATERAL. Each Draft accepted by the Bank in accordance with the above shall be secured by a security interest in the goods (as defined in the California Uniform Commercial Code) involved in the transaction out of which the Acceptance arose to the extent that such a security interest is either required by the Bank or in order that the relevant Acceptance conform to the requirements of Section 13 of the Federal Reserve Act.

(g) RESERVES. Each Borrower shall, jointly and severally, upon the Bank's 15-day written notice, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any future directive or requirement of any regulatory authority pertaining or relating to any Acceptance, provided that Bank notifies Borrower within 15 days of Bank having knowledge that such assessment, reserve, deposit or similar requirement or any surcharge, tax or fee shall be imposed.

2.04 FOREIGN EXCHANGE SUB-FACILITY. The Borrowers may from time to time request Bank to purchase or sell foreign currency in a specified amount, at a fixed price, and for delivery at a future date no greater than 364 days from the date of purchase (each a "Foreign Exchange Contract"). At no time, however, shall 15% of the aggregate of the settlement price of all Foreign Exchange Contracts outstanding exceed \$4,500,000 as determined by Bank at the time of entering into each Foreign Exchange Contract, and provided further, that all outstanding Revolving Advances, Letters of Credit and Acceptances and 15% of the aggregate of the settlement price of the Foreign Exchange Contracts outstanding may not exceed the Revolving Line of Credit.

(a) REQUESTS FOR FOREIGN EXCHANGE CONTRACTS. Each request for a Foreign Exchange Contract shall be made by telephone or fax, confirmed in writing (each a "Request"). Each Request shall be delivered or communicated to the Bank no later than 3:00 p.m. (California time) on the day (which shall be a business day) on which the Foreign Exchange Contract is requested. By making any such Request, each Borrower agrees that all matters relating to each such Foreign Exchange Contract shall be governed hereby and each Borrower restates all warranties and representations made by Borrower herein as if made on the date the Foreign Exchange Contract is entered into.

(b) EXPIRATION DATE. The commitment by the Bank to enter into Foreign Exchange Contracts shall, unless earlier terminated in accordance with this Agreement, automatically terminate on the Expiration Date and no Foreign Exchange Contract shall expire on a date which is after the Expiration Date.

(c) AVAILABILITY. Bank may refuse to enter into a Foreign Exchange Contract with the Borrower where the Bank, in its sole discretion, determines that such foreign currency is unavailable, or where Bank would be prohibited by any applicable law, regulation or order from purchasing such foreign currency.

(d) PURPOSE. The Foreign Exchange Contract shall be used to hedge foreign exchange exposure and/or risk.

(e) PAYMENT. Payment is due on the settlement date of any Foreign Exchange Contract (the "Payment Date"). Bank is hereby authorized by each Borrower to charge the full settlement price of any Foreign Exchange Contract against the depository account or accounts maintained by each Borrower with Bank on the Payment Date.

(f) RESERVES. The Borrowers shall, jointly and severally, upon the Bank's 15-day written notice request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit, capital maintenance or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any future directive or requirement of any regulatory authority pertaining or relating to any Foreign Exchange Contract, provided that Bank notifies Borrower within 15 days of Bank having knowledge that such assessment, reserve, deposit or similar requirement or any surcharge, tax or fee shall be imposed.

SECTION 3 EQUIPMENT LINE

3.01 EQUIPMENT PURCHASE FACILITY: The Bank hereby agrees to make loans and Equipment Advances to assist each Borrower in purchasing items of Equipment, upon a written request therefor made by any Borrower to the Bank prior to November 30, 1998 (the "Equipment Purchase Facility"). Each Equipment Advances made hereunder shall be in an amount not to exceed 80% of the Value of the item(s) of equipment being purchased; provided, however, that at no time shall the total aggregate outstanding principal amount of Equipment Advances made hereunder exceed the sum of \$3,000,000; and provided further that the amount of any Equipment Advances made hereunder which is repaid, in whole or in part, may not be reborrowed.

(a) EQUIPMENT ACCOUNT. The Bank shall maintain on its books a record of account in which the Bank shall make entries for each Equipment Advances and such other debits and credits as shall be appropriate in connection with the Equipment Purchase Facility (the "Equipment Account"). The Bank shall provide the Borrowers with a monthly statement of the Borrowers' Equipment Account, which statement shall be considered to be correct and conclusively binding on the Borrower unless any Borrower notifies the Bank to

the contrary within 18 months after such Borrower's receipt of any such statement which it deems to be incorrect.

(b) INTEREST ON EQUIPMENT ADVANCES. Borrowers shall have the option to select an interest rate under this facility at one of the interest rate options available for the Revolving Advances in Section 2.01 (d) and subject to the same terms as 2.01 (e) through (l).

(c) MATURITY. On November 30, 1998, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Equipment Advances then outstanding under the Equipment Purchase Facility, together with all accrued and unpaid interest thereon.

(d) CONVERSION TO TERM LOAN. It is hereby agreed that the Borrowers may not less than two (2) days prior to November 30, 1998, convert the principal balance of all Equipment Advances outstanding hereunder as of November 30, 1998 to be payable on a term loan basis. Accrued and unpaid interest hereunder shall be paid to the Bank concurrently with the Borrower's election to convert. Interest shall accrue and principal and interest shall be paid in accordance with the terms and provisions of the Equipment Line, provided however that principal shall be payable in 60 equal monthly payments beginning on December 31, 1998 and continuing on the last day of each month through November 30, 2003 at which time all principal and interest will be due.

3.03 LATE PAYMENT. If any payment of principal (other than a principal payment due on the Expiration Date) or interest, or any portion thereof, under this Agreement is not paid within ten (10) calendar days after it is due, a late payment charge equal to five percent (5%) of such past due payment may be assessed and shall be immediately payable.

3.04 JOINT LIABILITY. Notwithstanding that Equipment Advances may be made to a particular Borrower, each Borrower is jointly and severally liable for the repayment to Bank of any and all monies, together with interest thereon, disbursed under this Agreement. By each Borrower's respective execution of this Agreement, each such Borrower, jointly and severally, unconditionally and irrevocably promises to pay and guarantees the obligation for repayment of all indebtedness incurred hereunder.

SECTION 4 THE ACQUISITION LINE OF CREDIT

4.01 THE ACQUISITION LINE OF CREDIT. On terms and conditions as set forth herein, the Bank agrees to make Acquisition Advances in Dollars or in Alternate Currency to each Borrower from time to time from the date hereof to the Expiration Date, provided the aggregate amount of such Advances outstanding at any time does not exceed \$15,000,000 or the Dollar equivalent in Alternate Currency (the "Acquisition Line of Credit"). Acquisition Advances that are repaid may not be reborrowed. Acquisition Advances under the Acquisition Line of Credit shall be used only to fund acquisitions of companies in substantially the same line(s) of business as the Borrowers are presently engaged in and shall be in an amount not greater than \$5,000,000 per acquisition and only if a proforma financial covenant compliance certificate, after giving effect to the acquisition, shows the Borrower to be in compliance.

(a) MAKING ACQUISITION LINE ADVANCES. Each Acquisition Advance shall be conclusively deemed to have been made at the request of and for the benefit of each Borrower (i) when credited to any deposit account of any Borrower maintained with the Bank or (ii) when paid in accordance with such Borrower's written instructions. Subject to the requirements of Section 5, Acquisition Advances shall be made by the Bank upon telephonic or facsimile request received from the Borrower, and confirmed in writing within

two Business Days, which request shall be received not later than 12:00 p.m. (Pacific Time) on the date specified for a Variable Rate Acquisition Advance and 7:00 a.m. (Pacific Time) two business days prior to the date specified for a Eurocurrency Acquisition Advance or a Cost of Funds Acquisition Advance, each of which dates shall be a Business Day. The rates for a Eurocurrency Acquisition Advance or a Cost of Funds Acquisition Advance shall be set on the same Business Day as the request is received if received by 7:00 a.m. and on the next Business Day if received after 7:00 a.m.. Revolving Acquisition Advances shall be made by the Bank upon telephonic or facsimile request received from the Borrower, and confirmed in writing within two Business Days, which request shall be received not later than 12:00 p.m. (Pacific Time) on the date specified for a Variable Rate Revolving Advance and 7:00 a.m. (Pacific Time) two business days prior to the date specified for a Eurocurrency Revolving Advance or a Cost of Funds Revolving Advance, each of which dates shall be a Business Day.

(b) ACQUISITION ACCOUNT. The Bank shall maintain on its books a record of account in which the Bank shall make entries for each Acquisition Advance and such other debits and credits as shall be appropriate in connection with the Acquisition of Credit (the "Acquisition Account"). The Bank shall provide the Borrowers with a monthly statement of the Borrowers' Acquisition Account, which statement shall be considered to be correct and conclusively binding on the Borrowers unless any Borrower notifies the Bank to the contrary within 18 months after such Borrower's receipt of any such statement which it deems to be incorrect. Each Borrower hereby authorizes the Bank, if and to the extent payment owed to the Bank under the Acquisition Line of Credit is not made when due, to charge, from time to time, against any or all of any Borrower's deposit accounts with the Bank any amount so due.

(c) MANDATORY REPAYMENTS. On the Expiration Date, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Acquisition Advances then outstanding, together with all accrued and unpaid interest thereon, provided, however, that any Acquisition Advance denominated in Dollars must be repaid in Dollars and any Acquisition Advance denominated in an Alternate Currency must be repaid in the same Alternate Currency.

(d) INTEREST ON ACQUISITION ADVANCES. Borrowers shall have the option to select an interest rate under this facility from one of the interest rate options available to Borrowers for the Revolving Advances in Section 2.01 (d) and subject to the same terms as 2.01 (e) through (l).

(e) FEE. The Borrowers agree to pay to Bank, jointly and severally, a fee of .25% of the amount of each Acquisition Advance under the Acquisition Line of Credit, payable at the time each Acquisition Advance is made.

(f) CONVERSION TO TERM LOAN. It is hereby agreed that the Borrowers may, not less than 2 days prior to November 30, 1999, convert the principal balance of all Acquisition Advances outstanding hereunder as of November 30, 1999 to be payable on a term loan basis. Accrued and unpaid interest hereunder shall be paid to the Bank concurrently with the Borrower's election to convert. Interest shall accrue and principal and interest shall be paid in accordance with the terms and provisions of the Acquisition Line, provided however that principal shall be payable in 48 equal monthly payments beginning on December 31, 1999 and continuing on the last day of each month through November 30, 2003 at which time all principal and interest will be due.

4.02 LATE PAYMENT. If any payment of principal (other than a principal payment due on the Expiration Date) or interest, or any portion thereof, under this Agreement is not paid within ten (10) calendar days after it is due, a late payment charge equal to five percent (5%) of such past due payment may be assessed and shall be immediately payable.

4.03 JOINT LIABILITY. Notwithstanding that Acquisition Advances may be made to a particular Borrower, each Borrower is jointly and severally liable for the repayment to Bank of any and all monies, together with interest thereon, disbursed under this Agreement. By each Borrower's respective execution of this Agreement, each such Borrower, jointly and severally, unconditionally and irrevocably promises to pay and guarantees the obligation for repayment of all indebtedness incurred hereunder.

SECTION 5 COLLATERAL

5.01 THE COLLATERAL. To secure payment and performance of all of each Borrower's Obligations under this Agreement and all other liabilities, loans, guarantees, covenants and duties owed by the Borrower to the Bank, whether or not evidenced by this or by any other agreement, absolute or contingent, due or to become due, now existing or hereafter and howsoever created, each Borrower hereby grants the Bank a security interest in and to all of the following property (the "Collateral"):

(a) All goods now owned or hereafter acquired by each Borrower or in which any Borrower now has or may hereafter acquire any ownership interest, including, but not limited to, all machinery, equipment, furniture, furnishings, fixtures, tools, supplies and motor vehicles of every kind and description, and all additions, accessions, improvements, replacements and substitutions thereto and thereof.

(b) All inventory now owned or hereafter acquired by either Borrower, including, but not limited to, all raw materials, work in process, finished goods, merchandise, parts and supplies of every kind and description, including inventory temporarily out of either Borrower's custody or possession, together with all returns on accounts.

(c) All accounts, contract rights and general intangibles now owned or hereafter created or acquired by either Borrower, including, but not limited to, all receivables, goodwill, trademarks, trade styles, trade names, patents, patent applications, software, customer lists and business records, but excluding any equity interest in any of Borrower's foreign affiliates or subsidiaries.

(d) All documents, instruments and chattel paper now owned or hereafter acquired by either Borrower.

(e) All monies, deposit accounts, certificates of deposit and securities of each Borrower now or hereafter in the Bank's or its agents' possession, excluding the securities and stock of any Borrower's foreign affiliates or subsidiaries.

The Bank's security interest in the Collateral shall be a continuing lien and shall include the proceeds and products of the Collateral including, but not limited to, the proceeds of any insurance thereon.

SECTION 6 CONDITIONS OF LENDING

6.01 CONDITIONS PRECEDENT TO THE INITIAL ADVANCE. The obligation of the Bank to make the initial Acquisition Advance and the first extension of credit to or on account of any Borrower hereunder is subject to the conditions precedent that the Bank shall have received before the date of such initial Advance and such first extension of credit all of the following, in form and substance satisfactory to the Bank:

(a) Evidence that the execution, delivery and performance by each Borrower of this Agreement and any document, instrument or agreement required hereunder have been duly authorized.

(b) Executed UCC-1 financing statement(s) describing the Collateral, together with evidence of the recordation of such statement(s).

(c) Such other evidence as the Bank may request to establish the consummation of the transaction contemplated hereunder and compliance with the conditions of this Agreement.

6.02 CONDITIONS PRECEDENT TO ALL ADVANCES. The obligation of the Bank to make each Advance and each other extension of credit to or on account of either Borrower (including the initial Advance and the first extension of credit) shall be subject to the further conditions precedent that, on the date of each Advance or each extension of credit and after the making of such Advance or extension of credit:

(a) The Bank shall have received such supplemental approvals, opinions or documents as the Bank may reasonably request.

(b) The representations contained in Section 7 and in any other document, instrument or certificate delivered to the Bank hereunder are correct.

(c) No event has occurred and is continuing which constitutes, or, with the lapse of time or giving of notice or both, would constitute an Event of Default.

(d) The security interest in the Collateral has been duly authorized, created and perfected and is in full force and effect.

Each Borrower's acceptance of the proceeds of any Advance or the Borrower's execution of any document or instrument evidencing or creating any Obligation hereunder shall be deemed to constitute such Borrower's representation and warranty that all of the above statements are true and correct.

SECTION 7 REPRESENTATIONS AND WARRANTIES

Each Borrower hereby makes the following representations and warranties to the Bank, which representations and warranties are continuing:

7.01 STATUS. Each Borrower is a corporation, duly organized and validly existing under the laws of the State of California and is properly licensed and is qualified to do business and in good standing in, and, where necessary to maintain each Borrower's rights and privileges, has complied with the fictitious name statute of every jurisdiction in which the Borrower is doing business.

7.02 AUTHORITY. The execution, delivery and performance by each Borrower of this Agreement and any instrument, document or agreement required hereunder have been duly authorized and do not and will not: (i) violate any provision of any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award presently in effect having application to either Borrower; (ii) result in a breach of or constitute a default under any material indenture or loan or credit agreement or other material agreement, lease or instrument to which either Borrower is a party or by which it or its properties may be bound or affected; or (iii) require any consent or approval of its stockholders or violate any provision of its articles of incorporation or by-laws.

7.03 LEGAL EFFECT. This Agreement constitutes, and any instrument, document or agreement required hereunder when delivered hereunder will constitute, legal, valid and binding obligations of each Borrower enforceable against such Borrower in accordance with their respective terms.

7.04 FICTITIOUS TRADE STYLES. There are no fictitious trade styles used by any Borrower in connection with its business operations. Each Borrower shall notify the Bank not less than 30 days prior to effecting any change in the matters described herein or prior to using any other fictitious trade style at any future date, indicating the trade style and state(s) of its use.

7.05 FINANCIAL STATEMENTS: All financial statements, information and other data which may have been or which may hereafter be submitted by the Borrowers to the Bank are true, accurate and correct and have been or will be prepared in accordance with generally accepted accounting principles consistently applied and accurately represent the financial condition or, as applicable, the other information disclosed therein. Since the most recent submission of such financial information or data to the Bank, each Borrower represents and warrants that no material adverse change in such Borrower's financial condition or operations has occurred which has not been fully disclosed to the Bank in writing.

7.06 LITIGATION. Except as have been disclosed to the Bank in writing, there are no actions, suits or proceedings pending or, to the knowledge of each Borrower, threatened against or affecting any Borrower or any Borrower's properties before any court or administrative agency which, if determined adversely to such Borrower, would have a material adverse effect on such Borrower's financial condition or operations or on the Collateral.

7.07 TITLE TO ASSETS. Each Borrower has good and marketable title to all of its assets (including, but not limited to, the Collateral) and the same are not subject to any security interest, encumbrance, lien or claim of any third person except for Permitted Liens.

7.08 ERISA. If any Borrower has a pension, profit sharing or retirement plan subject to ERISA, such plan has been and will continue to be funded in accordance with its terms and otherwise complies with and continues to comply with the requirements of ERISA.

7.09 TAXES. Each Borrower has filed all tax returns required to be filed and paid all taxes shown thereon to be due, including interest and penalties, other than such taxes which are currently payable without penalty or interest or those which are being duly contested in good faith.

7.10 MARGIN STOCK. The proceeds of any Advance will not be used to purchase or carry margin stock as such term is defined under Regulation U of the Board of Governors of the Federal Reserve System.

7.11 ENVIRONMENTAL COMPLIANCE. Each Borrower has implemented and complied in all material respects with all applicable federal, state and local laws, ordinances, statutes and regulations with respect to hazardous or toxic wastes, substances or related materials, industrial hygiene or environmental conditions. There are no suits, proceedings, claims or disputes pending or, to the knowledge of any Borrower, threatened against or affecting any Borrower or its property claiming violations of any federal, state or local law, ordinance, statute or regulation relating to hazardous or toxic wastes, substances or related materials.

SECTION 8 COVENANTS

Each Borrower covenants and agrees that, during the term of this Agreement, and so long thereafter as any Borrower is indebted to the Bank under this Agreement, each Borrower will, unless the Bank shall otherwise consent in writing:

8.01 PRESERVATION OF EXISTENCE; COMPLIANCE WITH APPLICABLE LAWS. Maintain and preserve its existence and all rights and privileges now enjoyed; and conduct its business and operations in accordance with all applicable laws, rules and regulations.

8.02 MAINTENANCE OF INSURANCE. Maintain insurance in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which each Borrower operates and maintain such other insurance and coverages as may be required by the Bank. All such insurance shall be in form and amount and with companies satisfactory to the Bank. With respect to insurance covering properties in which the Bank maintains a security interest or lien, such insurance shall name the Bank as loss payee pursuant to a loss payable endorsement satisfactory to the Bank and shall not be altered or canceled except upon 10 days' prior written notice to the Bank. Upon the Bank's request, each Borrower shall furnish the Bank with the original policy or binder of all such insurance.

8.03 MAINTENANCE OF COLLATERAL AND OTHER PROPERTIES. Except for Permitted Liens, keep and maintain the Collateral free and clear of all levies, liens, encumbrances and security interests (including, but not limited to, any lien of attachment, judgment or execution) and defend the Collateral against any such levy, lien, encumbrance or security interest; comply with all laws, statutes and regulations pertaining to the Collateral and its use and operation; execute, file and record such statements, notices and agreements, take such actions and obtain such certificates and other documents as necessary to perfect, evidence and continue the Bank's security interest in the Collateral and the priority thereof; maintain accurate and complete records of the Collateral which show all sales, claims and allowances; and properly care for, house, store and maintain the Collateral in good condition, free of misuse, abuse and deterioration, other than normal wear and tear. Each Borrower shall also maintain and preserve all its properties in good working order and condition in accordance with the general practice of other businesses of similar character and size, ordinary wear and tear excepted.

8.04 PAYMENT OF OBLIGATIONS AND TAXES. Make timely payment of all assessments and taxes and all of its liabilities and obligations including, but not limited to, trade payables, unless the same are being contested in good faith by appropriate proceedings with the appropriate court or regulatory agency. For purposes hereof, any Borrower's issuance of a check, draft or similar instrument without delivery to the intended payee shall not constitute payment.

8.05 INSPECTION RIGHTS. At any reasonable time and from time to time, permit the Bank or any representative thereof to examine and make copies of the records and visit the properties of any Borrower and discuss the business and operations of such Borrower with any employee or representative thereof. If any Borrower shall maintain any records (including, but not limited to, computer generated records or computer programs for the generation of such records) in the possession of a third party, each Borrower hereby agrees to notify such third party to permit the Bank free access to such records at all reasonable times and to provide the Bank with copies of any records which it may request, all at the Borrowers' expense, the amount of which shall be payable immediately upon demand. In addition, the Bank may, at any reasonable time and from time to time, conduct inspections and audits of the Collateral and each Borrower's accounts payable, the cost and expenses of which shall be paid by the Borrowers to the Bank upon demand.

8.06 REPORTING AND CERTIFICATION REQUIREMENTS. Deliver or cause to be delivered to the Bank in form and detail satisfactory to the Bank:

(a) Not later than 125 days after the end of each Borrower's fiscal year, a copy of the annual audited consolidated financial report of the Borrowers for such year, prepared by a firm of certified public accountants acceptable to Bank and a copy of OSI System Inc.'s Form 10K filed with the Securities and Exchange Commission.

(b) Not later than 50 days after the end of the first three fiscal quarters of each year, the Borrowers' consolidated and consolidating financial statement for such quarter and a copy of OSI System Inc.'s Form 10Q filed with the Securities and Exchange Commission.

(c) Upon the Bank's request, such other information pertaining to the Borrower, the Collateral or any guarantor hereunder as the Bank may reasonably request.

8.07 REDEMPTION OR REPURCHASE OF STOCK. Not redeem or repurchase any class of each Borrower's stock now or hereafter outstanding other than up to \$5,000,000 of the Borrower's common stock.

8.08 PAYMENT OF DIVIDENDS. Not declare or pay any dividends on any class of stock now or hereafter outstanding except dividends payable solely in the Borrower's capital stock.

8.09 ADDITIONAL INDEBTEDNESS. Except as otherwise provided herein, not, after the date hereof, create, incur or assume, directly or indirectly, any additional Indebtedness other than (i) indebtedness owed or to be owed to the Bank or (ii) indebtedness to trade creditors incurred in the ordinary course of any Borrower's business or (iii) indebtedness owed or to be owed to Wells Fargo HSBC Trade Bank, or (iv) indebtedness to other real estate lenders for Borrowers' finance of its properties up to \$4,000,000.

8.10 LOANS. Not make any loans or advances or extend credit totalling more than \$350,000 in the aggregate to any third person, including, but not limited to, directors, officers, partners, or employees of any Borrower, except for credit extended in the ordinary course of each Borrower's business as presently conducted and except credit extended to any Borrower's affiliated entities and subsidiaries.

8.11 LIENS AND ENCUMBRANCES. Not create, assume or permit to exist any security interest, encumbrance, mortgage, deed of trust, or other lien (including, but not limited to, a lien of attachment, judgment or execution) affecting any of each Borrower's properties, or execute or allow to be filed any financing statement or continuation thereof affecting any of such properties, except for Permitted Liens or as otherwise provided in this Agreement.

8.12 TRANSFER ASSETS. Not, after the date hereof, sell, contract for sale, convey, transfer, assign, lease or sublet, any of its assets (including, but not limited to, the Collateral) except in the ordinary course of business as presently conducted by each Borrower and, then, only for full, fair and reasonable consideration.

8.13 CHANGE IN NATURE OF BUSINESS. Not make any material change in the nature of its business as existing or conducted as of the date hereof.

8.14 FINANCIAL CONDITION. Maintain at all times on a consolidated basis:

(a) NET WORTH. A minimum Effective Tangible Net Worth of at least \$40,000,000.

(b) LIQUID ASSETS. A ratio of the sum of cash, cash equivalents and accounts receivable to current liabilities of not less than .80 to 1.00.

(c) CASH FLOW. A ratio of EBITDA to the sum of interest expense and the current portion of long term Debt of not less than 2 to 1 at the end of each fiscal quarter with EBITDA based upon the immediately preceding three fiscal quarters and the current quarter just ended.

(d) LOSSES. Not allow any quarterly operating losses.

(e) DEBT COVERAGE. A ratio of Indebtedness to EBITDA for the immediately preceding three fiscal quarters and the current quarter just ended of not more than 3 to 1 at the end of each fiscal quarter.

8.15 COMPENSATION OF EMPLOYEES. Compensate its employees for services rendered at an hourly rate at least equal to the minimum hourly rate prescribed by any applicable federal or state law or regulation.

8.16 CAPITAL EXPENSE. Not make any fixed capital expenditure or any commitment therefor, including, but not limited to, incurring liability for leases which would be, in accordance with generally accepted accounting principles, reported as capital leases, or purchase any real or personal property in an amount greater than \$3,500,000 in any one fiscal year, except for the purchase of real property to be occupied by Borrowers.

8.17 MERGE OR CONSOLIDATE. Not liquidate or dissolve, merge or consolidate with or into, or acquire any other business organization, provided however, that Borrowers may make business acquisitions on a consolidated basis of up to \$15,000,000 in cash and \$25,000,000 in the aggregate.

8.18 NOTICE. Give the Bank prompt written notice of any and all (i) Events of Default; (ii) litigation, arbitration or administrative proceedings to which either Borrower is a party and in which the claim or liability exceeds \$500,000 or which affects the Collateral; and (iii) other matters which have resulted in, or might result in a material adverse change in the Collateral or the financial condition or business operations of any Borrower.

8.19 ENVIRONMENTAL COMPLIANCE. Each Borrower shall:

(a) Implement and comply in all material respects with all applicable federal, state and local laws, ordinances, statutes and regulations with respect to hazardous or toxic wastes, substances or related materials, industrial hygiene or to environmental conditions.

(b) Not own, use, generate, manufacture, store, handle, treat, release or dispose of any hazardous or toxic wastes, substances or related materials except in the ordinary course of the Borrower's business.

(c) Give prompt written notice of any discovery of or suit, proceeding, claim, dispute, threat, inquiry or filing respecting hazardous or toxic wastes, substances or related materials.

(d) At all times indemnify and hold harmless Bank from and against any and all liability arising out of the use, generation, manufacture, storage, handling, treatment, disposal or presence of hazardous or toxic wastes, substances or related materials.

SECTION 9 EVENTS OF DEFAULT

Any one or more of the following described events shall constitute an event of default (an "Event of Default") under this Agreement:

9.01 NON-PAYMENT. Any Borrower shall fail to pay any Obligations within 2 days of when due.

9.02 PERFORMANCE UNDER THIS AGREEMENT. Any Borrower shall fail in any material respect to perform or observe any term, covenant or agreement contained in this Agreement or in any document, instrument or agreement relating to this Agreement and any such failure shall continue unremedied for more than 30 days after the occurrence thereof.

9.03 OTHER AGREEMENTS. If there is a default under any agreement to which any Borrower is a party with a third party or parties resulting in a right by such third party or parties, whether or not exercised, to accelerate the maturity of any Indebtedness in excess of \$250,000.

9.04 REPRESENTATIONS AND WARRANTIES; FINANCIAL STATEMENTS. Any representation or warranty made by each Borrower under or in connection with this Agreement or any financial statement given by such Borrower or any guarantor shall prove to have been incorrect in any material respect when made or given or when deemed to have been made or given.

9.05 INSOLVENCY. Any Borrower shall: (i) become insolvent or be unable to pay its debts as they mature; (ii) make an assignment for the benefit of creditors or to an agent authorized to liquidate any substantial amount of its properties and assets; (iii) file a voluntary petition in bankruptcy or seeking reorganization or to effect a plan or other arrangement with creditors; (iv) file an answer admitting the material allegations of an involuntary petition relating to bankruptcy or reorganization or join in any such petition; (v) become or be adjudicated a bankrupt; (vi) apply for or consent to the appointment of, or consent that an order be made, appointing any receiver, custodian or trustee, for itself or any of its properties, assets or businesses; or (vii) any receiver, custodian or trustee shall have been appointed for all or substantially all of its properties, assets or businesses and shall not be discharged within 60 days after the date of such appointment.

9.06 EXECUTION. Any writ of execution or attachment or any judgment lien shall be issued against any property of any Borrower and shall not be discharged or bonded against or released within 30 days after the issuance or attachment of such writ or lien in excess of \$250,000.

9.07 SUSPENSION. Any Borrower shall voluntarily suspend the transaction of business or allow to be suspended, terminated, revoked or expired any permit, license or approval of any governmental body necessary to conduct such Borrower's business as now conducted.

9.08 CHANGE IN OWNERSHIP. There shall occur a sale, transfer, disposition or encumbrance (whether voluntary or involuntary), or an agreement shall be entered into to do so, with respect to more than 25% of the issued and outstanding capital stock of any Borrower owned by Deepak Chopra without the prior written consent of the Bank.

SECTION 10 REMEDIES ON DEFAULT

Upon the occurrence of any Event of Default, the Bank may, at its sole and absolute election, without demand and only upon such notice as may be required by law:

10.01 ACCELERATION. Declare any or all of the Borrowers' indebtedness owing to the Bank, whether under this Agreement or any other document, instrument or agreement, immediately due and payable, whether or not otherwise due and payable.

10.02 CEASE EXTENDING CREDIT. Cease making Advances or otherwise extending credit to or for the account of each Borrower under this Agreement or under any other agreement now existing or hereafter entered into between any Borrower and the Bank.

10.03 TERMINATION. Terminate this Agreement as to any future obligation of the Bank without affecting the Borrowers' obligations to the Bank or the Bank's rights and remedies under this Agreement or under any other document, instrument or agreement.

10.04 NOTIFICATION OF ACCOUNT DEBTORS:

(a) Notify any Account Debtor, any buyers or transferee of the Collateral or any other persons of the Bank's interest in the Collateral and the proceeds thereof.

(b) Sign any Borrower's name (which authority each Borrower hereby irrevocably and unconditionally grants to the Bank) on any invoice or bill of lading relating to accounts or other drafts against the Account Debtors, notify post office authorities to change the address for delivery of mail addressed to such Borrower to such address as the Bank may designate and take possession of and open mail addressed to any Borrower and remove therefrom, proceeds of and payments on the Collateral, and demand, receive and endorse payment and give receipts, releases and satisfactions for and sue for all money payable to any Borrower.

(c) Require each Borrower to indicate on the face of all invoices (or such other documentation as may be specified by the Bank relating to the services giving rise to the Account) that the Account has been assigned to the Bank and that all payments are to be made directly to the Bank at such address as the Bank may designate.

10.05 PROTECTION OF SECURITY INTEREST. Make such payments and do such acts as the Bank, in its sole judgment, considers necessary and reasonable to protect its security interest or lien in the Collateral. Each Borrower hereby irrevocably authorizes the Bank to pay, purchase, contest or compromise any encumbrance, lien or claim which the Bank, in its sole judgment, deems to be prior or superior to its security interest. Further, each Borrower hereby agrees to pay to the Bank, upon demand therefor, all expenses and expenditures (including attorneys' fees) incurred in connection with the foregoing.

10.06 FORECLOSURE. Enforce any security interest or lien given or provided for under this Agreement or under any security agreement, mortgage, deed of trust or other document, in such manner and such order, as to all or any part of the properties subject to such security interest or lien, as the Bank, in its sole judgment, deems to be necessary or appropriate and each Borrower hereby waives any and all rights, obligations or defenses now or hereafter established by law relating to the foregoing. In the enforcement of its security interest or lien, the Bank is authorized to enter upon the premises where any Collateral is located and take possession of the Collateral or any part thereof, together with each Borrower's records pertaining thereto, or the Bank may require each Borrower to assemble the Collateral and records pertaining thereto and make such Collateral and records available to the Bank at a place designated by the Bank. The Bank may sell the Collateral or any portions thereof, together with all additions, accessions and accessories thereto, giving only such notices and following only such procedures as are required by law, at either a public or private sale, or both, with or without having the Collateral present at the time of the sale, which sale shall be on such terms and conditions and conducted in such manner as the Bank determines in its sole judgment to be commercially reasonable. Any deficiency which exists after the disposition or liquidation of the Collateral shall be a continuing liability of each Borrowers to the Bank and shall be immediately paid by each Borrower, jointly and severally, to the Bank.

10.07 NON-EXCLUSIVITY OF REMEDIES. Exercise one or more of the Bank's rights set forth herein or seek such other rights or pursue such other remedies as may be provided by law, in equity or in any other agreement now existing or hereafter entered into between each Borrower and the Bank, or otherwise.

10.08 APPLICATION OF PROCEEDS. All amounts received by the Bank as proceeds from the disposition or liquidation of the Collateral shall be applied to the Borrowers' indebtedness to the Bank as follows: first, to the costs and expenses of collection, enforcement, protection and preservation of the Bank's lien in the Collateral, including court costs and reasonable attorneys' fees, whether or not suit is commenced by the Bank; next, to those costs and expenses incurred by the Bank in protecting, preserving, enforcing, collecting, liquidating, selling or disposing of the Collateral; next, to the payment of accrued and unpaid interest on all of the Obligations; next, to the payment of the outstanding principal balance of the Obligations; and last, to the payment of any other indebtedness owed by any Borrower to the Bank. Any excess Collateral or excess proceeds existing after the disposition or liquidation of the Collateral will be returned or paid by the Bank to the Borrowers.

SECTION 11
MISCELLANEOUS

11.01 AMOUNTS PAYABLE ON DEMAND. If any Borrower shall fail to pay on demand any amount so payable under this Agreement, the Bank may, at its option and without any obligation to do so and without waiving any default occasioned by the Borrower having so failed to pay such amount, create an Advance under the Revolving Line of Credit in an amount equal to the amount so payable, which Advance shall thereafter bear interest as provided under the Revolving Line of Credit.

11.02 DEFAULT INTEREST RATE. If an Event of Default, or an event which, with notice or passage of time could become an Event of Default, has occurred and is continuing, each Borrower, jointly and severally, shall pay to the Bank interest on any Indebtedness or amount payable under this Agreement at a rate which is 3% in excess of the rate or rates then in effect under this Agreement.

11.03 DISPOSAL OF INVOICES. All documents, schedules, invoices or other papers received by the Bank from the Borrowers may be destroyed or disposed of 6 months after receipt by the Bank, unless any Borrower requests in writing the return thereof, which shall be done at the Borrowers' expense.

11.04 RELIANCE. Each warranty, representation, covenant, obligation and agreement contained in this Agreement shall be conclusively presumed to have been relied upon by the Bank regardless of any investigation made or information possessed by the Bank and shall be cumulative and in addition to any other warranties, representations, covenants and agreements which each Borrower now or hereafter shall give, or cause to be given, to the Bank in writing.

11.05 ATTORNEYS' FEES. Each Borrower, jointly and severally, shall pay to the Bank all costs and expenses, including but not limited to reasonable attorneys fees, incurred by Bank in connection with the enforcement, or any refinancing or restructuring in the nature of a "work-out", of this Agreement or any document, instrument or agreement executed with respect to, evidencing or securing the indebtedness hereunder.

11.06 NOTICES. All notices, payments, requests, information and demands which either party hereto may desire, or may be required to give or make to the other party hereto, shall be given or made to such party by hand delivery or through deposit in the United States mail, postage prepaid, or by Western Union telegram, addressed as set forth below or to such other address as may be specified from time to time in writing by either party to the other.

To the Borrowers:

OSI SYSTEMS, INC.
12525 Chadron Ave.
Hawthorne, CA 90250

UDT SENSORS, INC.
12525 Chadron Ave.
Hawthorne, CA 90250

RAPISCAN SECURITY PRODUCTS
(U.S.A.), INC.
12525 Chadron Ave.
Hawthorne, CA 90250

FERSON OPTICS, INC.
12525 Chadron Ave.
Hawthorne, CA 90250

To the Bank:

SANWA BANK CALIFORNIA
Rosemead CBC #261-7
9000 East Valley Boulevard
Rosemead, CA 91770

Attn: David Carr, Vice President

With copy to:

Allan Duboff, Esq.
Richman, Lawrence, Mann, Chizever & Phillips
9601 Wilshire Blvd., Penthouse
Beverly Hills, CA 90210

11.07 WAIVER. Neither the failure nor delay by the Bank in exercising any right hereunder or under any document, instrument or agreement mentioned herein shall operate as a waiver thereof, nor shall any single or partial exercise of any right hereunder or under any other document, instrument or agreement mentioned herein preclude other or further exercise thereof or the exercise of any other right; nor shall any waiver of any right or default hereunder, or under any other document, instrument or agreement mentioned herein, constitute a waiver of any other right or default or constitute a waiver of any other default of the same or any other term or provision.

11.08 CONFLICTING PROVISIONS. To the extent the provisions contained in this Agreement are inconsistent with those contained in any other document, instrument or agreement executed pursuant hereto, the terms and provisions contained herein shall control. Otherwise, such provisions shall be considered cumulative.

11.09 BINDING EFFECT; ASSIGNMENT. This Agreement shall be binding upon and inure to the benefit of each Borrower and the Bank and their respective successors and assigns, except that no Borrower shall not have the right to assign its rights hereunder or any interest herein without the prior written consent of the Bank. The Bank may sell, assign or grant participation in all or any portion of its rights and benefits hereunder. Each Borrower agrees that, in connection with any such sale, grant or assignment, the Bank may deliver to the prospective buyer, participant or assignee financial statements and other relevant information relating to any Borrower and any guarantor.

11.10 JURISDICTION. This Agreement, any notes issued hereunder, the rights of the parties hereunder to and concerning the Collateral, and any documents, instruments or agreements mentioned or referred to herein shall be governed by and construed according to the laws of the State of California, to the jurisdiction of whose courts the parties hereby submit.

11.11 JUDGMENT CURRENCY. If for the purposes of obtaining judgment in any court it is necessary to convert a sum due hereunder in any currency (the "Original Currency") into another currency (the "Other Currency") the parties hereto agree, to the fullest extent that they may effectively do so, that the rate of exchange used shall be that at which in accordance with normal banking procedures the Bank could purchase the Original Currency with the Other Currency at Los Angeles on the second Business Day preceding that on which final judgment is given.

The obligation of any Borrower in respect of any sum due in the Original Currency from it to Bank shall, notwithstanding any judgment in any Other Currency, be discharged only to the extent that on the Business Day following receipt by Bank of any sum adjudged to be so due in such Other Currency Bank may in accordance with normal banking procedures purchase Dollars with such Other Currency; if the amount of the Original Currency so purchased is less than the sum originally due to the Bank, each Borrower jointly and severally agrees, as a separate obligation and notwithstanding any such judgment, to indemnify Bank against such loss, and if the amount of the Original Currency so purchased exceeds the sum originally due to Bank in the Original Currency, Bank agrees to remit to Borrowers such excess.

11.12 WAIVER OF JURY TRIAL. EACH BORROWER AND THE BANK EACH WAIVE THEIR RESPECTIVE RIGHTS TO A TRIAL BY JURY OF ANY CLAIM OR CAUSE OF ACTION BASED UPON OR ARISING OUT OF OR RELATED TO THIS AGREEMENT, THE OTHER LOAN DOCUMENTS, OR THE TRANSACTIONS CONTEMPLATED HEREBY OR THEREBY, IN ANY ACTION, PROCEEDING OR OTHER LITIGATION OF ANY TYPE BROUGHT BY ANY OF THE PARTIES AGAINST ANY OTHER PARTY OR PARTIES, WHETHER WITH RESPECT TO CONTRACT CLAIMS, TORT CLAIMS, OR OTHERWISE. EACH BORROWER AND THE BANK EACH AGREE THAT ANY SUCH CLAIM OR CAUSE OF ACTION SHALL BE TRIED BY A COURT TRIAL WITHOUT A JURY. WITHOUT LIMITING THE FOREGOING, THE PARTIES FURTHER AGREE THAT THEIR RESPECTIVE RIGHT TO A TRIAL BY JURY IS WAIVED BY OPERATION OF THIS SECTION AS TO ANY ACTION, COUNTERCLAIM OR OTHER PROCEEDING WHICH SEEKS, IN WHOLE OR IN PART, TO CHALLENGE THE VALIDITY OR ENFORCEABILITY OF THIS AGREEMENT OR THE OTHER LOAN DOCUMENTS OR ANY PROVISION HEREOF OR THEREOF. THIS WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS, SUPPLEMENTS OR MODIFICATIONS TO THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS.

11.13 NO GUARANTY OR SURETY. If any Borrower hereunder is deemed to be a surety or guarantor due to its joint and several liability hereunder such Borrower hereby unconditionally and irrevocably acknowledges and agrees to the matters set forth below:

(a) Each Borrower waives its rights of subrogation, reimbursement, indemnification and contribution and any other rights and defenses that are or may become available to such Borrower by reason of Sections 2787 to 2855, inclusive, of the California Civil Code and as they may be amended or superseded in the future. Without limiting the generality of the foregoing, each Borrower waives any defense based upon any Borrower's loss of a right against any other Borrower(s) arising from the Bank's election of a remedy on any indebtedness under bankruptcy or other debtor relief laws or under any other laws, including, but not limited to, those purporting to reduce the Bank's rights against any Borrower in proportion to the principal obligation of any indebtedness (as presently contained in Section 2809 of the California Civil Code and as it may be amended or superseded in the future).

(b) Each Borrower waives any defense arising by reason of:

(i) The cessation from any cause whatsoever, other than payment in full, of the Borrowers' indebtedness;

(ii) The application by the Borrowers of the proceeds of any Advance for purposes other than purposes represented by the Borrowers to the Bank or intended or understood by the Bank or such Borrower;

(iii) Any act or omission by the Bank which directly or indirectly results in or aids the discharge of the Borrowers or any Borrowers' indebtedness by operation of law or otherwise; or

(iv) Any modification of the Borrowers' indebtedness, in any form whatsoever, including, but not limited to, any renewal, extension, acceleration or other change in the time for payment of such indebtedness or other change in the terms of such indebtedness or any part thereof including, but not limited to, increase or decrease of the rate of interest thereon.

(c) Each Borrower waives all right to required the Bank to: (i) proceed against any other Borrower(s), any endorser, cosigner, other guarantor or other person liable on any indebtedness; (ii) join any endorser, cosigner, other guarantor on any indebtedness in any action or actions that may be brought and prosecuted by the Bank solely and separately against any Borrower(s) on any indebtedness; (iii) proceed against any item or items of collateral securing any indebtedness or any guaranty thereof; or (iv) pursue or refrain from pursuing any other remedy whatsoever in the Bank's power.

(d) Each Borrower waives any defense arising by reason of any disability or other defense of any other Borrower(s), successors or any endorser, cosigner, other guarantor or other person liable on any indebtedness. Until all indebtedness has been paid in full, each Borrower shall not have any right of subrogation and each Borrower waives any benefit of and right to participate in any collateral now or hereafter held by the Bank. Each Borrower waives all presentments, demands for performance, notices of nonperformance, protests, notices of protest, notices of dishonor, notices of sale of any collateral securing any indebtedness or any guaranty thereof, and notice of the existence, creation or incurring of new or additional indebtedness.

11.14 HEADINGS. The headings herein set forth are solely for the purpose of identification and have no legal significance.

11.15 ENTIRE AGREEMENT. This Agreement and all documents, instruments and agreements mentioned herein constitute the entire and complete understanding of the parties with respect to the transactions contemplated hereunder. All previous conversations, memoranda and writings between the parties pertaining to the transactions contemplated hereunder not incorporated or referenced in this Agreement or in such documents, instruments and agreements are superseded hereby.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first hereinabove written.

<p>BANK:</p> <p>SANWA BANK CALIFORNIA</p> <p>By: /s/ David B. Carr</p> <p>-----</p> <p>David B. Carr, Vice President</p> <p>-----</p> <p style="text-align: center;">Name/Title</p>	<p>BORROWERS:</p> <p>OSI SYSTEMS, INC.</p> <p>By: /s/ Ajay Mehra</p> <p>-----</p> <p>Ajay Mehra, Chief Financial Officer</p> <p>UDT SENSORS, INC.</p> <p>By: /s/ Ajay Mehra</p> <p>-----</p> <p>Ajay Mehra, Chief Financial Officer</p> <p>RAPISCAN SECURITY PRODUCTS (U.S.A.), INC.</p> <p>By: /s/ Ajay Mehra</p> <p>-----</p> <p>Ajay Mehra, Chief Financial Officer</p> <p>FERSON OPTICS, INC.</p> <p>By: /s/ Ajay Mehra</p> <p>-----</p> <p>Ajay Mehra, Chief Financial Officer</p>
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AGREEMENT OF PURCHASE AND SALE
AND JOINT ESCROW INSTRUCTIONS

This AGREEMENT OF PURCHASE AND SALE AND JOINT ESCROW INSTRUCTIONS ("Agreement") is made as of June 23, 1998 (the "Effective Date"), by and between KB CHADRON, BUILDING, LLC, a California limited liability company, ("Seller"), and UDT SENSORS, INC., a California corporation or its permitted assignee (pursuant to Paragraph 14(a) below) ("Buyer").

RECITALS:

A. Seller is the owner of that certain improved real property located at 12515 Chadron Avenue and 12525 Chadron Avenue ("Property-A") and 12533 Chadron Avenue ("Property-B") (collectively the "Property") in the City of Hawthorne, County of Los Angeles, State of California, as more particularly described on Exhibit "A" attached hereto and incorporated herein by this reference. Under

the terms of this Agreement, the "Property" shall also be defined to include, without limitation, transferable mineral rights, assignable development rights, air rights, sewer rights, fixtures, Seller's interest in signs and signage rights, heating, ventilation and air-conditioning systems, and all electrical, mechanical, elevator, plumbing, fire sprinkler and life safety systems, operating records, easements, rights-of-way, appurtenances and assignable permits, authorizations, licenses, warranties, and Service Contracts (as defined below) pertaining thereto, and all personal property (including, without limitation, all intangible property) and fixtures actually owned by Seller thereon.

B. Seller and Buyer acknowledge that Buyer is currently in possession of Property-A under that certain Standard Industrial Lease - NET, dated for reference purposes only January 1, 1989 by and between KB Management Company as Lessor and United Detector Technology, a division of ILC Technology as Lessee as amended by that certain First Amendment to Lease dated for reference purposes only July 7, 1992 and that certain Amendment Number Two to Lease dated for reference purposes only October 24, 1995 (the "Lease").

C. Buyer now desires to purchase from Seller, and Seller now desires to sell to Buyer, the Property.

D. Contemporaneously with the execution of this Agreement, Buyer has also executed a separate Agreement of Purchase and Sale and Joint Escrow Instructions for the purchase of 12605 Chadron Avenue ("12605 Property") from Chadron 11, LLC, a California limited liability company ("12605 Agreement"). It is the intent of the parties to this Agreement and the parties to the 12605 Agreement that both sales close simultaneously and that each sale is contingent upon successful simultaneous closing of the other sale.

NOW, THEREFORE, In consideration of the mutual covenants contained herein, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Buyer and Seller hereby agree as follows:

1. Purchase and Sale. Seller hereby agrees to sell, and Buyer hereby

agrees to purchase, the Property upon the terms and conditions set forth herein. Subject to the provisions hereof, the "Closing Date" means Wednesday, June 24, 1998 or sooner as mutually agreed upon, in writing, between Seller and Buyer.

2. Purchase Price. Pursuant to Paragraph 10 of Amendment Number Two to

Lease of the Lease, Buyer exercised its right on September 5, 1997 to purchase Property-A. The "Purchase Price-A" for Property-A will equal Two Million Eight Hundred Thousand Dollars (US\$2,800,000.00) plus the unamortized balance of the Tenant Improvements and Cabinet Work, as defined in Paragraph 10 of Amendment Number Two to Lease of the Lease. Said balance as of June 15, 1998 is one hundred and fifty-seven thousand dollars and thirteen cents (US\$157,000.00). The "Purchase Price-B" for Property-B will equal One Million One Hundred Thousand Dollars (US\$1,100,000.00). The combined "Purchase Price" for the Property, as of June 15, 1998, is Four Million Fifty-Seven Thousand Dollars (US\$4,057,000.00). At least one (1) business day prior to the Closing Date, Buyer will deposit with Escrow Holder the Purchase Price, plus Buyer's share of prorations and closing costs described below, by means of cash, cashier's check, federal wire transfer of funds or other method satisfactory to Escrow Holder in order that immediately available funds shall be available to Escrow Holder, for the benefit of Seller, at the opening of business on the Closing Date.

3. Escrow.

(a) Immediately following the parties' execution of this Agreement, the parties shall proceed to open an escrow (the "Escrow") with Commerce Escrow Company located at 1545 Wilshire Boulevard, Suite 600, Los Angeles, California 90017 (Attention: Mark Minsky -- Telephone No. (213) 484-0855 and Facsimile No. (213) 484-0417) (the "Escrow Holder"), by depositing therein a fully-executed, original of this Agreement. Buyer and Seller shall execute any further standard escrow instructions reasonably required by Escrow Holder, provided that this Agreement shall control in the event of any inconsistency between this Agreement and such additional escrow instructions.

(b) Buyer and Seller hereby agree that Chicago Title Company at 700 South Flower Street, Suite #900, Los Angeles, California, 90017 (Attention: Nate Glover -- Telephone No. (213) 488-4300 and Facsimile No. (213) 488-4385) will be the "Title Company," but if necessary, the Escrow Holder will remain the "real estate reporting person" for purposes of this Agreement, pursuant to Internal Revenue Code ("IRC") Section 6045(e).

4. Delivery of Title. Prior to the Closing Date, Seller shall deposit

with Escrow Holder a duly executed and acknowledged Grant Deed in the form of Exhibit "B" attached hereto and incorporated herein by this reference, conveying

the Property to Buyer, subject only to: (a) a lien to secure payment of real estate taxes and assessments, not delinquent, affecting the Property; (b) all matters of record not disapproved by Buyer, as described in Paragraph 5 below, affecting the Property; and (c) and all matters discoverable by means of a current ALTA survey or a physical inspection of the Property (collectively, the "Survey"), including, without limitation, Buyer's review of the Lease. Notwithstanding the foregoing,

any monetary liens encumbering the Property, other than non-delinquent real estate taxes and assessments, shall be removed from title or bonded against by Seller on or before the Closing, at Seller's sole cost and expense, unless otherwise agreed to or waived by Buyer in writing. Title shall be evidenced by the issuance, as of the Closing by the Title Company, of a standard CLTA owner's policy of title insurance (the "Title Policy") in the amount of the Purchase Price showing title to the Property vested in Buyer; provided, and if available, Buyer shall have the option of obtaining additional ALTA title insurance coverage and any endorsements thereto (collectively, the "ALTA Policy"), so long as Buyer pays for the ALTA Policy and satisfies the Title Company's requirements in connection therewith, if any.

5. Approvals by Buyer.

(a) Title. Buyer hereby approves the legal description of the

Property attached hereto as Exhibit "A", and any matters of title as disclosed by a current standard preliminary title report issued by the Title Company and legible copies of the recorded documents referred to in such preliminary title report, all of which have been delivered to Buyer.

(b) Documents. Buyer hereby approves the following documents with

respect to the Property:

(i) The ALTA Survey of the Property by Bone, Wright and Associates, dated May 18, 1998; and

(ii) All environmental reports (including reports regarding Hazardous Materials (as defined below)), certificates of occupancy, if any, and any other governmental or quasi-governmental reports, permits and/or entitlements in Seller's possession relating to the Property, if any, which Buyer has received from Seller.

(c) Inspections and Studies. Buyer hereby approves the results of

any and all inspections, economic feasibility analyses, investigations, tests and studies (including, without limitation, investigations with regard to zoning, building codes and other governmental regulations, architectural inspections, Hazardous Materials, engineering tests, surveys, and soils, and seismic and geological reports) with respect to the Property (including all structural and mechanical systems, and leased areas), as Buyer has received from Seller and/or Buyer may elect to make or obtain on its own. All such inspections, tests and studies shall be at Seller's sole cost and expense. Buyer and its consultants shall have the right to enter upon the Property, following the opening of Escrow and until the Contingency Date, to conduct such inspections, tests and studies; provided, that such entry onto the Property shall not interfere with the tenant's/lessee's quiet enjoyment of the Property under the Lease, and shall be conducted only following prior reasonable notice to Seller's local property manager to permit such property manager to accompany any such entry. Buyer hereby assumes all risk and expense relating to such entry, and hereby agrees to indemnify, defend (with counsel reasonably acceptable to Seller), protect and hold Seller, as well as Seller's principals, members, officers, directors, partners (either general or limited), employees, agents and representatives (collectively, "Seller's Agents"), and the Property harmless from

and against any and all claims, liabilities, damages, costs or expenses to the Property, Seller and/or Seller's Agents resulting from said inspections, including, without limitation, reasonable attorneys' fees and costs, and court costs. The indemnification obligations of Buyer set forth in this Paragraph 5(c) shall survive the Closing or any expiration or earlier termination of this Agreement.

6. Costs and Prorations. All rents, taxes, utilities and other payments

actually paid by or to Seller relating to the Property shall be prorated as of the Closing on either a 365-day year or a 30-day month, whichever is most convenient for Escrow Holder. Any security deposit, cleaning deposit and/or prepaid rent under the Lease as of the Closing, actually received by Seller and not already applied, shall be credited to Buyer. Seller shall be responsible for paying the premium for the Title Policy, except that Buyer may request an Extended Term Policy and pay for the increase, if any, in the amount of the premium due. Buyer and Seller shall each pay one-half (1/2) of any escrow fees charged by Escrow Holder. All other costs and expenses not specifically allocated herein shall be paid in accordance with the custom of the county in which the Property is located.

7. Closing Documents and Conditions; and Closing.

(a) Following the opening of Escrow, Seller shall operate and maintain the Property in the ordinary course of business (consistent with Seller's prior practice), reasonable wear and tear excepted (subject to obtaining reimbursement therefor pursuant to the terms of the Lease, if available), through and until the Closing.

(b) As conditions precedent to the Closing and Seller's obligations under this Agreement (unless otherwise waived in writing by Seller), and on or before the Closing Date, Buyer shall deliver to Escrow Holder: an executed closing statement prepared by Escrow Holder and reasonably agreed to by Buyer; the Purchase Price, in accordance with Paragraph 2 above; and such other documents as may be reasonably required by Escrow Holder and/or the Title Company in order to consummate the transaction set forth in this Agreement.

(c) As conditions precedent to the Closing and Buyer's obligations under this Agreement (unless otherwise waived in writing by Buyer), and on the Closing Date, Seller shall deliver to Buyer: the keys to and possession of the Property, subject to the Lease; and to Escrow Holder, on or before the Closing Date: the executed and acknowledged, original Grant Deed, in the form attached hereto as Exhibit "B"; an executed closing statement prepared by Escrow Holder;

an FIRPTA Certificate (as defined below), which shall be substantially in the form of Exhibit "C" attached hereto and incorporated herein by this reference;

and such other documents as may be reasonably required by Escrow Holder and/or the Title Company in order to consummate the transaction set forth in this Agreement.

(d) Unless otherwise mutually agreed to by Seller and Buyer in writing, and notwithstanding the Closing Date defined in Paragraph 1 above, the "Closing" of this transaction shall mean, and shall be conclusively deemed to occur on, the date the Title

Company records the Grant Deed in the County Recorder's Office of the county in which the Property is located and Escrow Holder concurrently releases the

Purchase Price to Seller.

(e) The simultaneous closing of the purchase and sale of the 12605 Property pursuant to the terms and conditions of the 12605 Agreement is a condition concurrent to the Closing and to each party's respective obligation under this Agreement.

8. Damage or Destruction and Condemnation. If all or any portion of the

Property is damaged or destroyed prior to the Closing, or if any condemnation or eminent domain proceedings (the "Proceedings") are instituted or threatened by written notice against the Property after the Contingency Date but prior to the Closing, and the costs of repair or reconstruction, or the extent of the Proceedings, are reasonably estimated to be in excess of One Million Dollars (US\$1,000,000), then Buyer shall have the right to terminate this Agreement by giving written notice thereof to Seller within five (5) business days after Seller notifies Buyer of the event of any damage or destruction or the Proceedings, whereupon neither Buyer nor Seller shall have any further rights or obligations hereunder (except as otherwise provided herein) following the return of the Deposit by Escrow Holder to Buyer. If Buyer does not terminate this Agreement, as aforesaid, this Agreement shall continue in full force and effect without modification or reduction in the Purchase Price, and Seller shall assign to Buyer, as of the Closing, all insurance proceeds or other funds, and Buyer shall assume all obligations of Seller, as a result of such damage or destruction or the Proceedings, whether or not such insurance proceeds or other funds are adequate or sufficient, and Seller shall not be obligated to repair any damage to the Property.

9. Representations and Warranties.

(a) Seller hereby represents and warrants to Buyer that Seller is a California limited liability company, whose principal office is at 9350 Wilshire Boulevard, Suite 302, Beverly Hills, California 90212, and that Michael Kaplan and Stanley Black are its Managers.

(b) Buyer hereby represents and warrants to Seller that Buyer is a duly formed and validly existing corporation in the State of California.

(c) Buyer and Seller, each for itself only, hereby represent and warrant to each other that: each has the requisite power and authority to execute, deliver and perform this Agreement and to consummate the transactions contemplated hereby; the execution and delivery of this Agreement by Buyer and Seller, the performance and compliance with all of the terms and conditions hereof to be performed and complied with by Buyer and Seller, and the consummation by Buyer and Seller of the transactions contemplated hereby have been duly authorized by all requisite action on the part of Buyer and Seller; this Agreement and all documents and agreements ancillary hereto and all documents required hereby have been, or when executed and delivered by Buyer and Seller will be, duly and validly executed and delivered by Buyer and Seller, and shall constitute the legal, valid and binding obligations of Buyer and Seller, enforceable in accordance with their respective terms.

(d) Buyer and Seller, each for itself only, hereby represent and warrant to each other that the execution, delivery and performance of this Agreement by Buyer and Seller, and the consummation by Buyer and Seller of the transactions contemplated hereby, do not require the consent, waiver, approval, license or authorization of any foreign, federal, state or local public authority or any other person or entity. Seller hereby further represents and warrants to Buyer that Seller's execution of this Agreement and the consummation of the transaction contemplated hereunder will not constitute a violation or breach by Seller of any agreement or other instrument to which Seller is a party or to which the Property is subject.

10. AS-IS. As a material inducement to the execution and delivery of this

Agreement by Seller and the performance by Seller of its duties and obligations hereunder, Buyer, and any and all of Buyer's successors and assigns, do hereby acknowledge, represent, warrant and agree to and with Seller as follows:

(a) Buyer is purchasing the Property in its current "AS-IS/WHERE-IS" condition "WITH ALL FAULTS" as of the Closing, and neither Seller nor any agent, employee or broker of Seller has made any representation or warranty regarding the Property (except as expressly set forth in Paragraph 9 of this Agreement). Buyer further acknowledges that an underground storage tank ("UST") formerly located on Property-B serviced Property-A for the benefit of the Buyer. Said UST was removed by the Buyer and Buyer has satisfied itself that a satisfactory closure report has been issued. Buyer hereby agrees to indemnify, defend (with counsel reasonably acceptable to Seller), protect and hold Seller and Seller's officers, directors, partners, employees, agents and representative harmless from and against any and all claims, liabilities, costs or damages resulting from the UST, its use or its removal;

(b) Buyer acknowledges receipt of the Phase I Environmental Assessment Report 12533 and 12605 Chadron Avenue prepared by Environmental Support Technologies, Inc. ("EST") and dated February 17, 1998, the Phase II Site Assessment Report 12533 and 12605 Chadron Avenue prepared by EST and dated March 4, 1998, and a Phase II Site Assessment Report for 12533 and 12605 Chadron Avenue prepared by EST and dated June 1, 1998 (collectively the "EST Reports"). Buyer has reviewed and accepted the EST Reports, its findings concerning the UST and other areas of potential environmental concern and accepts the responsibility for the recommendations, if any, of the EST Reports;

(c) Buyer acknowledges having ordered and received an Environmental Assessment Report for 12525 Chadron Avenue prepared by ERM-West, Inc. and dated March 30, 1990 ("ERM Report"). Buyer has received the ERM Report, its findings concerning the UST and other areas of potential environmental concern and accepts the responsibility for the recommendations, if any, of the EST Reports;

(d) Seller has no obligation to repair or correct any facts, circumstances, conditions or defects regarding the Property or to compensate Buyer for same;

(e) Seller is currently repairing certain toilet facilities in the building at 12533 Chadron. Since the repair will not be completed before closing, Seller hereby obligates itself to complete the repair in a timely and workmanlike fashion; and

11. Default and Legal Fees. Upon the bringing of any action or suit by a

party hereto against another party hereto by reason of any alleged default hereunder or to interpret or enforce any terms hereof, the prevailing party shall be entitled to recover as an element of its costs of suit, and not as damages, reasonable attorneys' fees and costs, and court costs, whether or not suit proceeds to final judgment, is settled or otherwise resolved.

12. WAIVER OF RIGHT TO RECORD LIS PENDENS. AS PARTIAL CONSIDERATION FOR

SELLER ENTERING INTO THIS AGREEMENT, BUYER EXPRESSLY WAIVES ANY RIGHT UNDER CALIFORNIA CODE OF CIVIL PROCEDURE, PART II, TITLE 4.5 (INCLUDING SECTIONS 405-405.39), AS MAY BE AMENDED OR SUPPLEMENTED FROM TIME TO TIME, OR AT COMMON LAW OR OTHERWISE, TO RECORD OR FILE A LIS PENDENS OR A NOTICE OF PENDENCY OF ACTION OR SIMILAR NOTICE AGAINST 12533 CHADRON AVENUE IN CONNECTION WITH ANY ALLEGED DEFAULT BY SELLER HEREUNDER. THIS WAIVER DOES NOT APPLY TO ANY OPTION RIGHTS OF BUYER FOR PROPERTY A UNDER ITS LEASE WITH SELLER. BUYER AND SELLER HEREBY EVIDENCE THEIR SPECIFIC AGREEMENT TO THE TERMS OF THIS WAIVER BY PLACING THEIR INITIALS IN THE PLACE PROVIDED HEREINBELOW.

BUYER'S INITIALS

SELLER'S INITIALS

13. Notices. All notices or other communications required or permitted

hereunder must be in writing, and shall be personally delivered or sent by registered or certified mail, return receipt requested, or delivered via overnight mail (via Federal Express or similar courier), or delivered via facsimile, and shall be deemed received upon the earlier of: (a) the date of delivery, if personally delivered or delivered via overnight mail, (b) three (3) business days after the date of posting by the U.S. postal service, if mailed, or (c) the date when sent, if faxed. Any notice or other communication sent by facsimile shall be confirmed within two (2) business days by letter mailed or delivered to the receiving party according to the foregoing. All such notices or communications shall be addressed as follows:

To Seller: KB Chadron Building, LLC, a California limited liability company
c/o ARKA Properties Group
9350 Wilshire Boulevard, Suite 302
Beverly Hills, California 90212
Attn: Michael B. Kaplan, Esq.
Facsimile No. (310) 274-1798

To Buyer: UDT Sensors, Inc.
12515 Chadron Avenue
Hawthorne, California
Attn: Ajay Mehra
Facsimile No. (310) 978-3898

To Escrow Holder:
Commerce Escrow Company
1545 Wilshire Boulevard, Suite 600
Los Angeles, California 90017
Attn: Mark Minsky
Facsimile No. (213) 484-0417

14. Assignment; Successors and Assigns; and 1031 Exchange.

(a) Notwithstanding anything to the contrary set forth in this Agreement, Buyer shall have the right to assign Buyer's interest in this Agreement to a third-party entity or individual; provided, such assignment must be completed within three (3) business days prior to the Closing Date, as reflected in a written assignment of, and amendment to, this Agreement, reasonably prepared and executed by Seller; and provided further, the original Buyer shall remain obligated for, and shall not be released from, the primary performance of Buyer's obligations hereunder.

(b) This Agreement shall be binding upon, and shall inure to the benefit of, the permitted successors and assigns of the parties hereto.

(c) Seller and Buyer hereby agree that Seller may assign this Agreement to any third-party entity or individual, including a nominee to act in place of Seller in accordance with an IRC Section 1031 Exchange, without Buyer's consent (but upon written notice to Buyer and Escrow Holder) and at no cost or expense to Buyer and with no delay or extension to the Closing. Such assignment shall be made, in writing, by Seller, and upon such assignment of this Agreement to a nominee and that nominee's assumption of Seller's obligations, Seller's nominee shall be substituted for Seller in the Escrow regarding the Property. Buyer hereby further agrees to accept all required performance under this Agreement from Seller's nominee and to render Buyer's performance of all of Buyer's obligations under this Agreement to Seller's nominee, if requested, in accordance with this Paragraph 14(c). Performance by Seller's nominee will be treated as Seller's performance by Buyer, and Buyer's performance to Seller's nominee will be treated as performance to Seller. Buyer hereby further agrees to reasonably cooperate with Seller and Escrow Holder, if necessary, to execute such reasonable, additional documents or provide such reasonable, additional information necessary to assist Seller in consummating the IRC Section 1031 Exchange contemplated under this Paragraph 14(c).

15. Entire Agreement and Exhibits. This Agreement, together with the

Recitals and all Exhibits attached hereto, contain the entire agreement between the parties hereto

with respect to the subject matter hereof, and no addition or modification of any term or provision shall be effective unless set forth in writing and executed by both Buyer and Seller.

16. Time of Essence. Time is of the essence of each and every term,

condition, obligation and provision hereof.

17. California Law. This Agreement shall be construed and enforced in

accordance with the laws of the State of California. Buyer and Seller hereby consent and agree to the jurisdiction of the state or federal courts sitting in the County of Los Angeles, State of California, and waive any objection based on venue or forum non conveniens with respect to any action instituted therein, and

further agree that any dispute concerning the relationship between the parties or this Agreement, or otherwise, shall be heard only in the courts described above.

18. Broker. Buyer and Seller hereby agree that neither are represented by

a broker and agree to hold one another harmless from any claims brought against the other for any and all commissions or fees related to the connection with this Agreement and its negotiation. Buyer hereby agrees to indemnify, defend (with reasonably acceptable counsel), protect and hold harmless Seller, Seller's Agents and the Property from and against any claims (including reasonable attorneys' fees and costs, and court costs) by any real estate broker or agent claiming through or under Buyer. Seller hereby agrees to indemnify, defend (with reasonably acceptable counsel), protect and hold harmless Buyer from and against any claims (including reasonable attorneys' fees and costs, and court costs) by any real estate broker or agent claiming through or under Seller. The indemnification obligations of both Seller and Buyer, as set forth in this Paragraph 18, shall survive the Closing or any expiration or earlier termination of this Agreement.

19. FIRPTA Compliance. Seller is not a foreign person within the meaning

of Section 1445 of the IRC, as amended. Based upon the foregoing, and on or prior to the Closing, Seller shall deliver to Escrow Holder a "FIRPTA Certificate" certifying Seller's non-foreign status, which FIRPTA Certificate is attached hereto as Exhibit "C."

20. Interpretation of Agreement. Terms, captions, headings and titles of

this Agreement are solely for convenience of reference and shall not affect its interpretation. This Agreement shall be construed without regard to any presumption or other rule requiring construction against the party drafting a document, and shall be construed neither for nor against Seller or Buyer, but shall be given a reasonable interpretation in accordance with the plain meaning of its terms and the intent of the parties hereto. All terms and words used in this Agreement, regardless of the number or gender in which they are used, shall be deemed to include any other number and any other gender as the context may require. This Agreement shall have no binding force or effect until its execution and delivery by both Seller and Buyer.

21. Counterparts. This Agreement may be executed in several counterparts

and all counterparts so executed constitute one agreement that is binding on all of the parties,

notwithstanding that all of the parties are not signatories to the original or the same counterpart.

IN WITNESS WHEREOF, Seller and Buyer have executed this Agreement as of the date first above written.

"SELLER": KB CHADRON BUILDING, LLC, a California Limited Liability Company

By: /s/ Michael Kaplan

Michael Kaplan, Manager

By: /s/ Stanley Black

Stanley Black, Manager

"BUYER": UDT Sensors, Inc.,
a California corporation

By: /s/ Ajay Mehra

Name: Ajay Mehra

Title: Chief Financial Officer

1 DESCRIPTION

EXHIBIT "A"

PARCEL 1:

THE NORTHERLY 180 FEET OF THAT PORTION OF THE EAST HALF OF THE SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 3 SOUTH, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, IN THE CITY OF HAWTHORNE, COUNTY OF LOS ANGELES, STATE OF CALIFORNIA, ACCORDING TO THE OFFICIAL PLAT OF SAID LAND FILED IN THE DISTRICT LAND OFFICE ON APRIL 22, 1868, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTH LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT WESTERLY THEREON 858.39 FEET FROM THE WEST LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED IN THE NOTICE OF ACTION, RECORDED ON APRIL 19, 1943 IN BOOK 19942 PAGE 242, OFFICIAL RECORDS OF SAID COUNTY; THENCE NORTHERLY PARALLEL WITH SAID WESTERLY LINE OF 1027 FEET, MORE OR LESS, TO A POINT IN THE SOUTH LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY; THENCE WESTERLY ALONG SAID SOUTH LINE 408.39 FEET, MORE OR LESS, TO THE WEST LINE OF THE EAST HALF OF SAID SOUTHEAST QUARTER; THENCE SOUTHERLY ALONG THE WEST LINE OF SAID EAST HALF, A DISTANCE OF 1027 FEET, MORE OR LESS, TO SAID NORTHERLY LINE OF EL SEGUNDO BOULEVARD; THENCE EASTERLY ALONG SAID NORTH LINE TO THE POINT OF BEGINNING.

PARCEL 2:

THE SOUTHERLY 136.75 FEET OF THE NORTHERLY 316.75 FEET OF THAT PORTION OF THE EAST HALF OF THE SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 3 SOUTH, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, IN THE CITY OF HAWTHORNE, COUNTY OF LOS ANGELES, STATE OF CALIFORNIA, ACCORDING TO THE OFFICIAL PLAT OF SAID LAND FILED IN THE DISTRICT LAND OFFICE ON APRIL 22, 1868, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTH LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT WESTERLY THEREON 858.39 FEET FROM THE WEST LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED IN THE NOTICE OF ACTION, RECORDED ON APRIL 19, 1943 IN BOOK 19942 PAGE 242, OFFICIAL RECORDS OF SAID COUNTY; THENCE NORTHERLY PARALLEL WITH SAID WESTERLY LINE 1027 FEET, MORE OR LESS, TO A POINT IN THE SOUTH LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY; THENCE WESTERLY

ALONG SAID SOUTH LINE 408.39 FEET, MORE OR LESS, TO THE WEST LINE OF THE EAST HALF OF SAID SOUTHEAST QUARTER; THENCE SOUTHERLY ALONG THE WEST LINE OF SAID EAST HALF, A DISTANCE OF 1027 FEET, MORE OR LESS, TO SAID NORTHERLY LINE OF EL SEGUNDO BOULEVARD; THENCE EASTERLY ALONG SAID NORTH LINE TO THE POINT OF BEGINNING.

PARCEL 3:

THE SOUTHERLY 133.25 FEET OF THE NORTHERLY 450 FEET OF THAT PORTION OF THE EAST HALF OF THE SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 3 SOUTH, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, IN THE CITY OF HAWTHORNE, COUNTY OF LOS ANGELES, STATE OF CALIFORNIA, ACCORDING TO THE OFFICIAL PLAT OF SAID LAND FILED IN THE DISTRICT LAND OFFICE ON APRIL 22, 1868, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTH LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT WESTERLY THEREON 858.39 FEET FROM THE WEST LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED IN THE NOTICE OF ACTION, RECORDED ON APRIL 19, 1943 IN BOOK 19942 PAGE 242, OFFICIAL RECORDS OF SAID COUNTY; THENCE NORTHERLY PARALLEL WITH SAID WESTERLY LINE 1027 FEET, MORE OR LESS, TO A POINT IN THE SOUTH LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY; THENCE WESTERLY ALONG SAID SOUTH LINE 408.39 FEET, MORE OR LESS, TO THE WEST LINE OF THE EAST HALF OF SAID SOUTHEAST QUARTER; THENCE SOUTHERLY ALONG THE WEST LINE OF SAID EAST HALF, A DISTANCE OF 1027 FEET, MORE OR LESS, TO SAID NORTHERLY LINE OF EL SEGUNDO BOULEVARD; THENCE EASTERLY ALONG SAID NORTH LINE TO THE POINT OF BEGINNING.

PARCEL 4:

A NON-EXCLUSIVE EASEMENT FOR STREET PURPOSES TO BE USED IN COMMON WITH OTHERS OVER THAT PORTION OF THE EAST HALF OF THE SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 3 SOUTH, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, IN THE CITY OF HAWTHORNE, COUNTY OF LOS ANGELES, STATE OF CALIFORNIA, ACCORDING TO THE OFFICIAL PLAT OF SAID LAND FILED IN THE DISTRICT LAND OFFICE ON APRIL 22, 1868, INCLUDED WITHIN A STRIP OF LAND, 60 FEET WIDE, THE CENTER LINE OF SAID 60 FOOT STRIP BEING DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTHERLY LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT SOUTH 89 DEGREES 51 MINUTES 30 SECONDS WEST THEREON 858.39 FEET FROM THE WESTERLY LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED IN THE NOTICE OF ACTION, RECORDED IN BOOK 19942 PAGE 242, OFFICIAL RECORDS OF SAID COUNTY; THENCE NORTH 0 DEGREES 01 MINUTES 50 SECONDS EAST, PARALLEL WITH THE WESTERLY LINE OF SAID 20 FOOT STRIP OF 1027 FEET, MORE OR LESS, TO THE

SOUTHERLY LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY.

EXCEPT THEREFROM ANY PORTION THEREOF LYING WITHIN THE CONFINES OF PARCELS 1, 2
AND 3 ABOVE DESCRIBED.

RECORDING REQUESTED BY AND
WHEN RECORDED MAIL TO:

Attention:

MAIL TAX STATEMENTS TO:

Same as Above

(Above Space for Recorder's Use Only)

GRANT DEED

The undersigned Grantor declares:

Documentary Transfer Tax is \$_____ computed on full value of property conveyed.

City and County of Los Angeles, State of California.

FOR VALUABLE CONSIDERATION, receipt of which is hereby acknowledged,
a _____ ("Grantor"),
hereby sells, grants, conveys and transfers to _____,
a _____ ("Grantee"), all of Grantor's right, title and
interest in and to the following property located in the City of _____,
County of _____, State of California, described on Schedule "1"
attached hereto and incorporated herein by this reference (collectively, the
"Property").

DATED: _____, 1998.

"GRANTOR":

a

By: DO NOT SIGN - EXHIBIT ONLY

Name: _____
Title: _____

By: DO NOT SIGN - EXHIBIT ONLY

Name: _____
Title: _____

DESCRIPTION OF PROPERTY

[To Be Attached]

SCHEDULE "1" TO EXHIBIT "B"

Page 2 of 3

STATE OF CALIFORNIA)
) ss.
COUNTY OF _____)

On _____ before me, _____
personally appeared _____, personally known to me (or proved to
me on the basis of satisfactory evidence) to be the person(s) whose name(s)
is/are subscribed to the within instrument and acknowledged to me that
he/she/they executed the same in his/her/their authorized capacity(ies), and
that by his/her/their signature(s) on the instrument the person(s), or the
entity upon behalf of which the person(s) acted, executed the instrument.

WITNESS my hand and official seal.

Signature:

STATE OF CALIFORNIA)
) ss.
COUNTY OF _____)

On _____ before me, _____
personally appeared _____, personally known to me (or proved to
me on the basis of satisfactory evidence) to be the person(s) whose name(s)
is/are subscribed to the within instrument and acknowledged to me that
he/she/they executed the same in his/her/their authorized capacity(ies), and
that by his/her/their signature(s) on the instrument the person(s), or the
entity upon behalf of which the person(s) acted, executed the instrument.

WITNESS my hand and official seal.

Signature:

STATE OF CALIFORNIA)
) ss.
COUNTY OF _____)

On _____ before me, _____
personally appeared _____, personally known to me (or proved to
me on the basis of satisfactory evidence) to be the person(s) whose name(s)
is/are subscribed to the within instrument and acknowledged to me that
he/she/they executed the same in his/her/their authorized capacity(ies), and
that by his/her/their signature(s) on the instrument the person(s), or the
entity upon behalf of which the person(s) acted, executed the instrument.

WITNESS my hand and official seal.

Signature:

EXHIBIT "B"

Page 3 of 3

AGREEMENT OF PURCHASE AND SALE
AND JOINT ESCROW INSTRUCTIONS

This AGREEMENT OF PURCHASE AND SALE AND JOINT ESCROW INSTRUCTIONS ("Agreement") is made as of June 23, 1998 (the "Effective Date"), by and between CHADRON II, LLC, a California limited liability company, ("Seller"), and UDT SENSORS, INC., a California corporation or its permitted assignee (pursuant to Paragraph 14(a) below) ("Buyer").

RECITALS:

A. Seller is the owner of that certain improved real property located at 12605 Chadron Avenue (the "Property") in the City of Hawthorne, County of Los Angeles, State of California, as more particularly described on Exhibit "A" attached hereto and incorporated herein by this reference. Under the terms of this Agreement, the "Property" shall also be defined to include, without limitation, transferable mineral rights, assignable development rights, air rights, sewer rights, fixtures, Seller's interest in signs and signage rights, heating, ventilation and air-conditioning systems, and all electrical, mechanical, elevator, plumbing, fire sprinkler and life safety systems, operating records, easements, rights-of-way, appurtenances and assignable permits, authorizations, licenses, warranties, and Service Contracts (as defined below) pertaining thereto, and all personal property (including, without limitation, all intangible property) and fixtures actually owned by Seller thereon.

B. Seller and Buyer acknowledge that Buyer is currently in possession of the Property under that certain Standard Industrial/Commercial Single-Tenant Lease-NET, dated for reference purposes only April 15, 1992 by and between Stanley Black, Jack Black, A & R Management and K Associates as Lessor and UDT Sensors, Inc., a California corporation as Lessee as amended by that certain Amendment Number One to Lease dated for reference purposes only October 20, 1995 (the "Lease").

C. Buyer now desires to purchase from Seller, and Seller now desires to sell to Buyer, the Property.

D. Contemporaneously with the execution of this Agreement, Buyer has also executed a separate Agreement of Purchase and Sale and Joint Escrow Instructions for the purchase of 12515, 12525 and 12533 Chadron Avenue (collectively "12515-33 Property") from KB Chadron Building, LLC, a California limited liability company ("12515-33 Agreement"). It is the intent of the parties to this Agreement and the parties to the 12515-33 Agreement that both sales close simultaneously and that each sale is contingent upon successful simultaneous closing of the other sale.

NOW, THEREFORE, in consideration of the mutual covenants contained herein, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Buyer and Seller hereby agree as follows:

1. Purchase and Sale. Seller hereby agrees to sell, and Buyer hereby

agrees to purchase, the Property upon the terms and conditions set forth herein. Subject to the provisions hereof, the "Closing Date" means Wednesday, June 24, 1998 or sooner as mutually agreed upon, in writing, between Seller and Buyer.

2. Purchase Price. The "Purchase Price" for the Property will equal One

Hundred Fifty Thousand Dollars (US\$150,000.00). At least one (1) business day prior to the Closing Date, Buyer will deposit with Escrow Holder the Purchase Price, plus Buyer's share of prorations and closing costs described below, by means of cash, cashier's check, federal wire transfer of funds or other method satisfactory to Escrow Holder in order that immediately available funds shall be available to Escrow Holder, for the benefit of Seller, at the opening of business on the Closing Date.

3. Escrow.

(a) Immediately following the parties' execution of this Agreement, the parties shall proceed to open an escrow (the "Escrow") with Commerce Escrow Company located at 1545 Wilshire Boulevard, Suite 600, Los Angeles, California 90017 (Attention: Mark Minsky -- Telephone No. (213) 484-0855 and Facsimile No. (213) 484-0417) (the "Escrow Holder"), by depositing therein a fully-executed, original of this Agreement. Buyer and Seller shall execute any further standard escrow instructions reasonably required by Escrow Holder, provided that this Agreement shall control in the event of any inconsistency between this Agreement and such additional escrow instructions.

(b) Buyer and Seller hereby agree that Chicago Title Company, at 700 South Flower Street, Suite #900, Los Angeles, California, 90017 (Attention: Nate Glover -- Telephone No. (213) 488-4300 and Facsimile No. (213) 488-4385) will be the "Title Company," but if necessary, the Escrow Holder will remain the "real estate reporting person" for purposes of this Agreement, pursuant to Internal Revenue Code ("IRC") Section 6045(e).

4. Delivery of Title. Prior to the Closing Date, Seller shall deposit

with Escrow Holder a duly executed and acknowledged Grant Deed in the form of Exhibit "B" attached hereto and incorporated herein by this reference, conveying

the Property to Buyer, subject only to: (a) a lien to secure payment of real estate taxes and assessments, not delinquent, affecting the Property; (b) all matters of record not disapproved by Buyer, as described in Paragraph 5 below, affecting the Property; and (c) and all matters discoverable by means of a current ALTA survey or a physical inspection of the Property (collectively, the "Survey"), including, without limitation, Buyer's review of the Lease. Notwithstanding the foregoing, any monetary liens encumbering the Property, other than non-delinquent real estate taxes and assessments, shall be removed from title or bonded against by Seller on or before the Closing, at Seller's sole cost and expense, unless otherwise agreed to or waived by Buyer in writing. Title shall be evidenced by the issuance, as of the Closing by the Title Company, of a standard CLTA owner's policy of title insurance (the "Title Policy") in the amount of the Purchase Price showing title to the Property vested in Buyer; provided, and if available, Buyer shall have the option of obtaining additional ALTA title insurance coverage and any

endorsements thereto (collectively, the "ALTA Policy"), so long as Buyer pays for the ALTA Policy and satisfies the Title Company's requirements in connection therewith, if any.

5. Approvals by Buyer.

(a) Title. Buyer hereby approves the legal description of the

Property attached hereto as Exhibit "A", and any matters of title as disclosed

by a current standard preliminary title report issued by the Title Company and legible copies of the recorded documents referred to in such preliminary title report, all of which have been delivered to Buyer.

(b) Documents. Buyer hereby approves the following documents with

respect to the Property:

(i) The ALTA Survey of the Property by Bone, Wright and Associates, dated May 18, 1998; and

(ii) All environmental reports (including reports regarding Hazardous Materials (as defined below)), certificates of occupancy, if any, and any other governmental or quasi-governmental reports, permits and/or entitlements in Seller's possession relating to the Property, if any which Buyer has received from Seller.

(c) Inspections and Studies. Buyer hereby approves the results of any

and all inspections, economic feasibility analyses, investigations, tests and studies (including, without limitation, investigations with regard to zoning, building codes and other governmental regulations, architectural inspections, Hazardous Materials, engineering tests, surveys, and soils, and seismic and geological reports) with respect to the Property (including all structural and mechanical systems, and leased areas), as Buyer has received from Seller and/or Buyer may elect to make or obtain on its own. All such inspections, tests and studies shall be at Seller's sole cost and expense. Buyer and its consultants shall have the right to enter upon the Property, following the opening of Escrow and until the Contingency Date, to conduct such inspections, tests and studies; provided, that such entry onto the Property shall not interfere with the tenant's/lessee's quiet enjoyment of the Property under the Lease, and shall be conducted only following prior reasonable notice to Seller's local property manager to permit such property manager to accompany any such entry. Buyer hereby assumes all risk and expense relating to such entry, and hereby agrees to indemnify, defend (with counsel reasonably acceptable to Seller), protect and hold Seller, as well as Seller's principals, members, officers, directors, partners (either general or limited), employees, agents and representatives (collectively, "Seller's Agents"), and the Property harmless from and against any and all claims, liabilities, damages, costs or expenses to the Property, Seller and/or Seller's Agents resulting from said inspections, including, without limitation, reasonable attorneys' fees and costs, and court costs. The indemnification obligations of Buyer set forth in this Paragraph 5(c) shall survive the Closing or any expiration or earlier termination of this Agreement.

6. Costs and Prorations. All rents, taxes, utilities and other payments

actually paid by or to Seller relating to the Property shall be prorated as of the Closing on either a 365-day year or a 30-day month, whichever is most convenient for Escrow Holder. Any security deposit, cleaning deposit and/or prepaid rent under the Lease as of the Closing, actually received by Seller and not already applied, shall be credited to Buyer. Seller shall be responsible for paying the premium for the Title Policy. Buyer and Seller shall each pay one-half (1/2) of any escrow fees charged by Escrow Holder. All other costs and expenses not specifically allocated herein shall be paid in accordance with the custom of the county in which the Property is located.

7. Closing Documents and Conditions; and Closing.

(a) Following the opening of Escrow, Seller shall operate and maintain the Property in the ordinary course of business (consistent with Seller's prior practice), reasonable wear and tear excepted (subject to obtaining reimbursement therefor pursuant to the terms of the Lease, if available), through and until the Closing.

(b) As conditions precedent to the Closing and Seller's obligations under this Agreement (unless otherwise waived in writing by Seller), and on or before the Closing Date, Buyer shall deliver to Escrow Holder: an executed closing statement prepared by Escrow Holder and reasonably agreed to by Buyer; the Purchase Price, in accordance with Paragraph 2 above; and such other documents as may be reasonably required by Escrow Holder and/or the Title Company in order to consummate the transaction set forth in this Agreement.

(c) As conditions precedent to the Closing and Buyer's obligations under this Agreement (unless otherwise waived in writing by Buyer), and on the Closing Date, Seller shall deliver to Buyer: the keys to and possession of the Property, subject to the Lease; and to Escrow Holder, on or before the Closing Date: the executed and acknowledged, original Grant Deed, in the form attached hereto as Exhibit "B"; an executed closing statement prepared by Escrow Holder;

an FIRPTA Certificate (as defined below), which shall be substantially in the form of Exhibit "C" attached hereto and incorporated herein by this reference;

and such other documents as may be reasonably required by Escrow Holder and/or the Title Company in order to consummate the transaction set forth in this Agreement.

(d) Unless otherwise mutually agreed to by Seller and Buyer in writing, and notwithstanding the Closing Date defined in Paragraph 1 above, the "Closing" of this transaction shall mean, and shall be conclusively deemed to occur on, the date the Title Company records the Grant Deed in the County Recorder's Office of the county in which the Property is located and Escrow

Holder concurrently releases the Purchase Price to Seller.

(e) The simultaneous closing of the purchase and sale of the 12515-33 Property pursuant to the terms and conditions of the 12515-33 Agreement is a condition concurrent to the Closing and to each party's respective obligation under this Agreement.

8. Damage or Destruction and Condemnation. If all or any portion of the

Property is damaged or destroyed prior to the Closing, or if any condemnation or eminent domain proceedings (the "Proceedings") are instituted or threatened by written notice against the Property after the Contingency Date but prior to the Closing, and the costs of repair or reconstruction, or the extent of the Proceedings, are reasonably estimated to be in excess of Thirty-Eight Thousand Dollars (US\$38,000.00), then Buyer shall have the right to terminate this Agreement by giving written notice thereof to Seller within five (5) business days after Seller notifies Buyer of the event of any damage or destruction or the Proceedings, whereupon neither Buyer nor Seller shall have any further rights or obligations hereunder (except as otherwise provided herein) following the return of the Deposit by Escrow Holder to Buyer. If Buyer does not terminate this Agreement, as aforesaid, this Agreement shall continue in full force and effect without modification or reduction in the Purchase Price, and Seller shall assign to Buyer, as of the Closing, all insurance proceeds or other funds, and Buyer shall assume all obligations of Seller, as a result of such damage or destruction or the Proceedings, whether or not such insurance proceeds or other funds are adequate or sufficient, and Seller shall not be obligated to repair any damage to the Property.

9. Representations and Warranties.

(a) Seller hereby represents and warrants to Buyer that Seller is a California limited liability company, whose principal office is at 9350 Wilshire Boulevard, Suite 302, Beverly Hills, California 90212, and that Michael Kaplan and Stanley Black are its Managers.

(b) Buyer hereby represents and warrants to Seller that Buyer is a duly formed and validly existing corporation in the State of California.

(c) Buyer and Seller, each for itself only, hereby represent and warrant to each other that: each has the requisite power and authority to execute, deliver and perform this Agreement and to consummate the transactions contemplated hereby; the execution and delivery of this Agreement by Buyer and Seller, the performance and compliance with all of the terms and conditions hereof to be performed and complied with by Buyer and Seller, and the consummation by Buyer and Seller of the transactions contemplated hereby have been duly authorized by all requisite action on the part of Buyer and Seller; this Agreement and all documents and agreements ancillary hereto and all documents required hereby have been, or when executed and delivered by Buyer and Seller will be, duly and validly executed and delivered by Buyer and Seller, and shall constitute the legal, valid and binding obligations of Buyer and Seller, enforceable in accordance with their respective terms.

(d) Buyer and Seller, each for itself only, hereby represent and warrant to each other that the execution, delivery and performance of this Agreement by Buyer and Seller, and the consummation by Buyer and Seller of the transactions contemplated hereby, do not require the consent, waiver, approval, license or authorization of any foreign, federal, state or local public authority or any other person or entity. Seller hereby further represents and warrants to Buyer that Seller's execution of this Agreement and the consummation of

the transaction contemplated hereunder will not constitute a violation or breach by Seller of any agreement or other instrument to which Seller is a party or to which the Property is subject.

10. AS-IS. As a material inducement to the execution and delivery of this

Agreement by Seller and the performance by Seller of its duties and obligations hereunder, Buyer, and any and all of Buyer's successors and assigns, do hereby acknowledge, represent, warrant and agree to and with Seller as follows:

(a) Buyer is purchasing the Property in its current "AS-IS/WHERE-IS" condition "WITH ALL FAULTS" as of the Closing, and neither Seller nor any agent, employee or broker of Seller has made any representation or warranty regarding the Property (except as expressly set forth in Paragraph 9 of this Agreement);

(b) Buyer acknowledges receipt of the Phase I Environmental Assessment Report 12533 and 12605 Chadron Avenue prepared by Environmental Support Technologies, Inc. ("EST") and dated February 17, 1998, the Phase II Site Assessment Report 12533 and 12605 Chadron Avenue prepared by EST and dated March 4, 1998, and a Phase II Site Assessment Report for 12533 and 12605 Chadron Avenue prepared by EST and dated June 1, 1998 (collectively the "EST Reports"). Buyer has reviewed and accepted the EST Reports, its findings of potential environmental concern and accepts the responsibility for the recommendations, if any, of the EST Reports;

(c) Buyer acknowledges having ordered and received an Environmental Assessment Report for 12525 Chadron Avenue prepared by ERM-West, Inc. and dated March 30, 1990 ("ERM Report"). Buyer has received the ERM Report, its findings concerning the UST and other areas of potential environmental concern and accepts the responsibility for the recommendations, if any, of the EST Reports;

(d) Seller has no obligation to repair or correct any facts, circumstances, conditions or defects regarding the Property or to compensate Buyer for same; and

11. Default and Legal Fees. Upon the bringing of any action or suit by a

party hereto against another party hereto by reason of any alleged default hereunder or to interpret or enforce any terms hereof, the prevailing party shall be entitled to recover as an element of its costs of suit, and not as damages, reasonable attorneys' fees and costs, and court costs, whether or not suit proceeds to final judgment, is settled or otherwise resolved.

12. WAIVER OF RIGHT TO RECORD LIS PENDENS. AS PARTIAL CONSIDERATION FOR

SELLER ENTERING INTO THIS AGREEMENT, BUYER EXPRESSLY WAIVES ANY RIGHT UNDER CALIFORNIA CODE OF CIVIL PROCEDURE, PART II, TITLE 4.5 (INCLUDING SECTIONS 405-405.39), AS MAY BE AMENDED OR SUPPLEMENTED FROM TIME TO TIME, OR AT COMMON LAW OR OTHERWISE, TO RECORD OR FILE A LIS PENDENS OR A NOTICE OF PENDENCY OF ACTION OR SIMILAR NOTICE AGAINST ALL OR ANY PORTION OF THE PROPERTY IN CONNECTION WITH ANY ALLEGED DEFAULT BY SELLER

HEREUNDER. THIS WAIVER DOES NOT APPLY TO ANY OPTION RIGHTS OF BUYER FOR PROPERTY A UNDER ITS LEASE WITH SELLER. BUYER AND SELLER HEREBY EVIDENCE THEIR SPECIFIC AGREEMENT TO THE TERMS OF THIS WAIVER BY PLACING THEIR INITIALS IN THE PLACE PROVIDED HEREINBELOW.

BUYER'S INITIALS

SELLER'S INITIALS

13. Notices. All notices or other communications required or permitted

hereunder must be in writing, and shall be personally delivered or sent by registered or certified mail, return receipt requested, or delivered via overnight mail (via Federal Express or similar courier), or delivered via facsimile, and shall be deemed received upon the earlier of: (a) the date of delivery, if personally delivered or delivered via overnight mail, (b) three (3) business days after the date of posting by the U.S. postal service, if mailed, or (c) the date when sent, if faxed. Any notice or other communication sent by facsimile shall be confirmed within two (2) business days by letter mailed or delivered to the receiving party according to the foregoing. All such notices or communications shall be addressed as follows:

To Seller: Chadron II, LLC, a California limited liability company
c/o ARKA Properties Group
9350 Wilshire Boulevard, Suite 302
Beverly Hills, California 90212
Attn: Michael B. Kaplan, Esq.
Facsimile No. (310) 274-1798

To Buyer: UDT Sensors, Inc.
12515 Chadron Avenue
Hawthorne, California
Attn: Ajay Mehra
Facsimile No. (310) 978-3898

To Escrow Holder: Commerce Escrow Company
1545 Wilshire Boulevard, Suite 600
Los Angeles, California 90017
Attn: Mark Minsky
Facsimile No. (213) 484-0417

14. Assignment; Successors and Assigns; and 1031 Exchange.

(a) Notwithstanding anything to the contrary set forth in this Agreement, Buyer shall have the right to assign Buyer's interest in this Agreement to a third-party entity or individual; provided, such assignment must be completed within three (3) business days prior to the Closing Date, as reflected in a written assignment of, and amendment to, this Agreement, reasonably prepared and executed by Seller; and provided further, the original

Buyer shall remain obligated for, and shall not be released from, the primary performance of Buyer's obligations hereunder.

(b) This Agreement shall be binding upon, and shall inure to the benefit of, the permitted successors and assigns of the parties hereto.

(c) Seller and Buyer hereby agree that Seller may assign this Agreement to any third-party entity or individual, including a nominee to act in place of Seller in accordance with an IRC Section 1031 Exchange, without Buyer's consent (but upon written notice to Buyer and Escrow Holder) and at no cost or expense to Buyer and with no delay or extension to the Closing. Such assignment shall be made, in writing, by Seller, and upon such assignment of this Agreement to a nominee and that nominee's assumption of Seller's obligations, Seller's nominee shall be substituted for Seller in the Escrow regarding the Property. Buyer hereby further agrees to accept all required performance under this Agreement from Seller's nominee and to render Buyer's performance of all of Buyer's obligations under this Agreement to Seller's nominee, if requested, in accordance with this Paragraph 14(c). Performance by Seller's nominee will be treated as Seller's performance by Buyer, and Buyer's performance to Seller's nominee will be treated as performance to Seller. Buyer hereby further agrees to reasonably cooperate with Seller and Escrow Holder, if necessary, to execute such reasonable, additional documents or provide such reasonable, additional information necessary to assist Seller in consummating the IRC Section 1031 Exchange contemplated under this Paragraph 14(c).

15. Entire Agreement and Exhibits. This Agreement, together with the -----
Recitals and all Exhibits attached hereto, contain the entire agreement between the parties hereto with respect to the subject matter hereof, and no addition or modification of any term or provision shall be effective unless set forth in writing and executed by both Buyer and Seller.

16. Time of Essence. Time is of the essence of each and every term, -----
condition, obligation and provision hereof.

17. California Law. This Agreement shall be construed and enforced in -----
accordance with the laws of the State of California. Buyer and Seller hereby consent and agree to the jurisdiction of the state or federal courts sitting in the County of Los Angeles, State of California, and waive any objection based on venue or forum non conveniens with respect to any action instituted therein, and -----
further agree that any dispute concerning the relationship between the parties or this Agreement, or otherwise, shall be heard only in the courts described above.

18. Broker. Buyer and Seller hereby agree that neither are represented by -----
a broker and agree to hold one another harmless from any claims brought against the other for any and all commissions or fees related to the connection with this Agreement and its negotiation. Buyer hereby agrees to indemnify, defend (with reasonably acceptable counsel), protect and hold harmless Seller, Seller's Agents and the Property from and against any claims (including reasonable attorneys' fees and costs, and court costs) by any real estate broker or agent claiming through or under Buyer. Seller hereby agrees to indemnify, defend

(with reasonably acceptable counsel), protect and hold harmless Buyer from and against any claims (including reasonable attorneys' fees and costs, and court costs) by any real estate broker or agent claiming through or under Seller. The indemnification obligations of both Seller and Buyer, as set forth in this Paragraph 18, shall survive the Closing or any expiration or earlier termination of this Agreement.

19. FIRPTA Compliance. Seller is not a foreign person within the meaning

of Section 1445 of the IRC, as amended. Based upon the foregoing, and on or prior to the Closing, Seller shall deliver to Escrow Holder a "FIRPTA Certificate" certifying Seller's non-foreign status, which FIRPTA Certificate is attached hereto as Exhibit "C."

20. Interpretation of Agreement. Terms, captions, headings and titles of

this Agreement are solely for convenience of reference and shall not affect its interpretation. This Agreement shall be construed without regard to any presumption or other rule requiring construction against the party drafting a document, and shall be construed neither for nor against Seller or Buyer, but shall be given a reasonable interpretation in accordance with the plain meaning of its terms and the intent of the parties hereto. All terms and words used in this Agreement, regardless of the number or gender in which they are used, shall be deemed to include any other number and any other gender as the context may require. This Agreement shall have no binding force or effect until its execution and delivery by both Seller and Buyer.

21. Counterparts. This Agreement may be executed in several counterparts

and all counterparts so executed constitute one agreement that is binding on all of the parties, notwithstanding that all of the parties are not signatories to the original or the same counterpart.

IN WITNESS WHEREOF, Seller and Buyer have executed this Agreement as of the date first above written.

"SELLER": CHADRON II, LLC, a California limited liability company

By: /s/ Michael Kaplan

Michael Kaplan, Manager

By: /s/ Stanley Black

Stanley Black, Manager

"BUYER":

UDT Sensors, Inc.,
a California corporation

By: /s/ Ajay Mehra

Name: Ajay Mehra

Title: Chief Financial Officer

DESCRIPTION

EXHIBIT "A"

PARCEL 1:

THE SOUTH 59 FEET OF THE NORTH 509 FEET OF THAT PORTION OF THE EAST HALF OF SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 35, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, IN THE CITY OF HAWTHORNE, COUNTY OF LOS ANGELES, STATE OF CALIFORNIA, ACCORDING TO THE OFFICIAL PLAT THEREOF, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTH LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT WESTERLY THEREON 858.39 FEET FROM THE WEST LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED AS PARCEL 4-5. IN THE NOTICE OF ACTION, RECORDED ON APRIL 19, 1943 AS INSTRUMENT NO. 1166 IN BOOK 19942 PAGE 242, OFFICIAL RECORDS, IN THE OFFICE OF THE COUNTY RECORDER OF SAID COUNTY; THENCE NORTHERLY PARALLEL WITH SAID WEST LINE 1027 FEET, MORE OR LESS, TO A POINT IN THE SOUTH LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY; THENCE WESTERLY ALONG SAID SOUTH LINE 408.39 FEET TO THE WEST LINE OF THE EAST HALF OF SAID SOUTHEAST QUARTER; THENCE SOUTHERLY ALONG SAID LAST MENTIONED WEST LINE, A DISTANCE OF 1027 FEET, MORE OR LESS, TO SAID NORTHERLY LINE OF EL SEGUNDO BOULEVARD; THENCE EASTERLY ALONG SAID NORTH LINE TO THE POINT OF BEGINNING.

PARCEL 2:

AN EASEMENT FOR STREET PURPOSES TO BE USED IN COMMON WITH OTHERS OVER THAT PORTION OF EAST HALF OF THE SOUTHEAST QUARTER OF SECTION 10, TOWNSHIP 3 SOUTH, RANGE 14 WEST, SAN BERNARDINO MERIDIAN, ACCORDING TO THE OFFICIAL PLAT THEREOF, INCLUDED WITHIN A STRIP OF LAND 60 FEET WIDE, THE CENTER LINE OF SAID 60 FOOT STRIP BEING DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE NORTHERLY LINE OF EL SEGUNDO BOULEVARD, 60 FEET WIDE, DISTANT SOUTH 89 DEGREES 51 MINUTES 30 SECONDS WEST THEREON 858.39 FEET FROM THE WESTERLY LINE OF THE 20 FOOT STRIP OF LAND DESCRIBED IN THE NOTICE OF ACTION, RECORDED IN BOOK 19942 PAGE 242, OFFICIAL RECORDS OF SAID COUNTY; THENCE NORTH 0 DEGREES 01 MINUTES 50 SECONDS EAST, PARALLEL WITH THE WESTERLY LINE OF SAID 20 FOOT STRIP 1027.90 FEET, MORE OR LESS, TO THE SOUTHERLY LINE OF THE RIGHT OF WAY OF THE PACIFIC ELECTRIC RAILWAY COMPANY.

EXCEPT THE SOUTH 20 FEET OF SAID LAND.

ALSO EXCEPT THEREFROM THAT PORTION THEREOF INCLUDED WITHIN THE LINES OF PARCEL 1
HEREINABOVE DESCRIBED.

SUBSIDIARIES OF THE COMPANY

UDT Sensors, Inc.	California
Rapiscan Security Products (U.S.A.), Inc.	California
Ferson Optics, Inc.	California
Rapiscan Security Products Limited	United Kingdom
Opto Sensors (Singapore) Pte Ltd.	Singapore
Opto Sensors (Malaysia) Sdn. Bhd.	Malaysia
Rapiscan Consortium (M) Sdn. Bhd.	Malaysia
Advanced Micro Electronics AS	Norway

INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in Registration Statement No. 333-45049 of OSI Systems Inc. and Subsidiaries on Form S-8 of our report dated September 11, 1998, appearing in this Annual Report on Form 10-K of OSI Systems Inc. and Subsidiaries for the year ended June 30, 1998.

DELOITTE & TOUCHE LLP
Los Angeles, California

September 11, 1998.

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YEAR
JUN-30-1998
JUL-01-1997
JUN-30-1998
22,447
0
24,254
0
21,705
72,618
11,466
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