

PINNACLE DATA SYSTEMS, INC.
CONDENSED BALANCE SHEETS
(Dollars in thousands)

| | <u>September 30,</u> <u>2006</u> | <u>December 31,</u> <u>2005</u> |
|---|-------------------------------------|------------------------------------|
| <u>ASSETS</u> | <u>(Unaudited)</u> | |
| CURRENT ASSETS | | |
| Cash | \$ 82 | \$ 486 |
| Accounts receivable, net of allowance for doubtful accounts of \$327 and \$70, respectively | 11,410 | 12,556 |
| Inventory, net | 13,442 | 9,233 |
| Prepaid expenses | 624 | 421 |
| Refundable income taxes | 1,668 | - |
| Deferred income taxes | 833 | 833 |
| Total current assets | <u>28,059</u> | <u>23,529</u> |
| PROPERTY AND EQUIPMENT | | |
| Leasehold improvements | 470 | 329 |
| Furniture and fixtures | 390 | 389 |
| Computer equipment and related software | 3,112 | 2,715 |
| Shop equipment | 628 | 599 |
| Total property and equipment, cost | <u>4,600</u> | <u>4,032</u> |
| Less accumulated depreciation and amortization | <u>(3,550)</u> | <u>(3,250)</u> |
| Total property and equipment, net | <u>1,050</u> | <u>782</u> |
| OTHER ASSETS | 112 | 108 |
| TOTAL ASSETS | <u>\$ 29,221</u> | <u>\$ 24,419</u> |
| <u>LIABILITIES AND STOCKHOLDERS' EQUITY</u> | | |
| CURRENT LIABILITIES | | |
| Line of credit | \$ 6,256 | \$ 9,336 |
| Short-term note | 4,000 | - |
| Accounts payable | 9,817 | 6,122 |
| Accrued expenses: | | |
| Wages, payroll taxes and benefits | 1,026 | 979 |
| Other | 1,129 | 652 |
| Income taxes | - | 366 |
| Unearned revenue | 748 | 209 |
| Total current liabilities | <u>22,976</u> | <u>17,664</u> |
| LONG-TERM LIABILITIES | | |
| Deferred income taxes | 63 | 63 |
| Long-term accrual | 667 | - |
| Total long-term liabilities | <u>730</u> | <u>63</u> |
| TOTAL LIABILITIES | <u>23,706</u> | <u>17,727</u> |
| COMMITMENTS AND CONTINGENCIES | | |
| | <u>-</u> | <u>-</u> |
| STOCKHOLDERS' EQUITY | | |
| Preferred stock; no par value; 4,000,000 shares authorized; no shares issued or outstanding | - | - |
| Common stock; no par value; 25,000,000 shares authorized; 6,306,948 and 5,985,356 shares issued and outstanding, respectively | 3,320 | 2,755 |
| Additional paid-in capital | 876 | 754 |
| Retained earnings | 1,319 | 3,183 |
| Total stockholders' equity | <u>5,515</u> | <u>6,692</u> |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | <u>\$ 29,221</u> | <u>\$ 24,419</u> |

PINNACLE DATA SYSTEMS, INC.
CONDENSED STATEMENTS OF OPERATIONS
(Dollars in thousands, except for per share totals)

| | <u>For Three Month Period Ended</u> | | <u>For Nine Month Period Ended</u> | |
|---|-------------------------------------|-----------------------|------------------------------------|-----------------------|
| | <u>Sept. 30, 2006</u> | <u>Sept. 30, 2005</u> | <u>Sept. 30, 2006</u> | <u>Sept. 30, 2005</u> |
| | (Unaudited) | | (Unaudited) | |
| SALES | | | | |
| Product sales | \$ 12,520 | \$ 11,736 | \$ 41,769 | \$ 22,040 |
| Service sales | <u>2,874</u> | <u>2,534</u> | <u>7,878</u> | <u>6,668</u> |
| Total sales | <u>15,394</u> | <u>14,270</u> | <u>49,647</u> | <u>28,708</u> |
| COST OF SALES | | | | |
| Product sales | 11,517 | 10,208 | 36,403 | 19,077 |
| Service sales | <u>1,477</u> | <u>970</u> | <u>3,588</u> | <u>2,872</u> |
| Total cost of sales | <u>12,994</u> | <u>11,178</u> | <u>39,991</u> | <u>21,949</u> |
| GROSS PROFIT | 2,400 | 3,092 | 9,656 | 6,759 |
| OPERATING EXPENSES | <u>4,801</u> | <u>2,464</u> | <u>12,504</u> | <u>5,735</u> |
| (LOSS) INCOME FROM OPERATIONS | <u>(2,401)</u> | <u>628</u> | <u>(2,848)</u> | <u>1,024</u> |
| OTHER EXPENSE | | | | |
| Interest expense | <u>222</u> | <u>87</u> | <u>551</u> | <u>148</u> |
| (LOSS) INCOME BEFORE INCOME TAXES | (2,623) | 541 | (3,399) | 876 |
| INCOME TAX (BENEFIT) EXPENSE | <u>(1,224)</u> | <u>202</u> | <u>(1,535)</u> | <u>328</u> |
| NET (LOSS) INCOME | <u>\$ (1,399)</u> | <u>\$ 339</u> | <u>\$ (1,864)</u> | <u>\$ 548</u> |
| BASIC (LOSS) EARNINGS PER COMMON SHARE | | | | |
| | <u>\$ (0.22)</u> | <u>\$ 0.06</u> | <u>\$ (0.30)</u> | <u>\$ 0.09</u> |
| DILUTED (LOSS) EARNINGS PER COMMON SHARE | | | | |
| | <u>\$ (0.22)</u> | <u>\$ 0.05</u> | <u>\$ (0.30)</u> | <u>\$ 0.09</u> |
| WEIGHTED AVERAGE COMMON SHARES OUTSTANDING | | | | |
| Basic | <u>6,297,108</u> | <u>5,940,957</u> | <u>6,199,777</u> | <u>5,834,297</u> |
| Diluted | <u>6,297,108</u> | <u>6,319,549</u> | <u>6,199,777</u> | <u>6,266,897</u> |

PINNACLE DATA SYSTEMS, INC.
CONDENSED STATEMENTS OF CASH FLOWS
(Dollars in thousands)

| | Nine Month Period Ended | |
|--|--------------------------------|----------------------|
| | September 30, | September 30, |
| | (Unaudited) | (Unaudited) |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net (loss) income | \$ (1,864) | \$ 548 |
| Adjustments to reconcile net (loss) income to net cash used in operating activities: | | |
| Depreciation | 300 | 369 |
| Stock-based compensation expense | 122 | - |
| Provision for doubtful accounts | 248 | 10 |
| Inventory reserves | - | 284 |
| (Increase)/decrease in assets: | | |
| Accounts receivable | 898 | (2,927) |
| Inventory | (4,210) | (1,085) |
| Prepaid expenses and other assets | (206) | 29 |
| Refundable income taxes | (1,668) | 215 |
| Increase (decrease) in liabilities: | | |
| Accounts payable | 2,927 | (1,730) |
| Accrued expenses and taxes | 825 | (70) |
| Unearned revenues | 539 | 58 |
| Total adjustments | (225) | (4,847) |
| Net cash used in operating activities | (2,089) | (4,299) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchases of property and equipment | (568) | (214) |
| Proceeds from acquisition | - | 125 |
| Net cash used in investing activities | (568) | (89) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Net (payments on) proceeds from line of credit | (3,080) | 5,478 |
| Proceeds from short-term note | 4,000 | - |
| Outstanding checks in excess of funds on deposit | 768 | 863 |
| Proceeds from stock options exercised | 565 | 472 |
| Payment of debt assumed in acquisition | - | (2,281) |
| Principal payments on capital lease obligation | - | (6) |
| Net cash provided by financing activities | 2,253 | 4,526 |
| (DECREASE) INCREASE IN CASH | (404) | 138 |
| Cash at beginning of period | 486 | 15 |
| Cash at end of period | \$ 82 | \$ 153 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION | | |
| Interest paid | \$ 204 | \$ 119 |
| Income taxes paid, net of refunds | \$ 457 | \$ 110 |
| SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING TRANSACTIONS | | |
| Inventory capitalized as computer equipment | \$ - | \$ 2 |
| Income tax benefit from stock option plans credited to additional paid-in-capital | \$ - | \$ 194 |

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